HOUSE OF COMMONS

ORAL EVIDENCE

TAKEN BEFORE THE

INTERNATIONAL DEVELOPMENT COMMITTEE

THE FUTURE OF UK DEVELOPMENT CO-OPERATION PHASE 1: DEVELOPMENT FINANCE

TUESDAY 18 JUNE 2013

JONATHAN GLENNIE, ELIZABETH STUART AND RICHARD MANNING

PETER CHOWLA, MATTHEW MARTIN AND PROFESSOR STEPHANY GRIFFITH-JONES

Evidence heard in Public Questions 1-40

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Oral Evidence

Taken before the International Development Committee

on Tuesday 18 June 2013

Members present:

Rt Hon Sir Malcolm Bruce (Chair)
Hugh Bayley
Fiona Bruce
Richard Burden
Fabian Hamilton
Pauline Latham
Jeremy Lefroy
Mr Michael McCann
Chris White

Examination of Witnesses

Witnesses: **Jonathan Glennie**, Research Fellow, Overseas Development Institute, **Elizabeth Stuart**, Director of Policy and Research, Save the Children, and **Richard Manning**, Chair of Board of Trustees, Institute of Development Studies, gave evidence.

Q1 Chair: Can I thank you all for coming in to help? This is the first evidence session we are taking on a fairly longish inquiry, looking at the future of development co-operation. For the record, could you introduce yourselves?

Richard Manning: I am Richard Manning. Is that what you want me to say?

Chair: Well—just your title, as it were.

Richard Manning: I am an independent consultant and chair of a couple of boards, and I am currently co-ordinating the replenishments of the African Development Fund and the Global Fund.

Elizabeth Stuart: I am Elizabeth Stuart, director of policy and research at Save the Children.

Jonathan Glennie: Good morning. Jonathan Glennie; I am a research fellow at the Overseas Development Institute, working on aid and development finance.

Q2 Chair: Thank you very much for coming in. Obviously, the whole development landscape is changing. DFID has acknowledged that in their evidence to us. I suppose the preface is that we have been very focused on delivering 0.7%, which hopefully we will achieve, and we are committed to achieving, this year. However, it is really quite important to say, "0.7% to do what, and how will it change over the next 10 to 15 years?"

DFID say the development finance landscape has changed rapidly over the last decade and is likely to continue to do so. I wondered if you could give us your views on what you think have been the key things that have been driving this change, and what the implications are for DFID, because obviously that is what is of concern to us.

Is DFID in its present structure and format fit for purpose? Is it appropriately deployed for the future, or does it need to reorganise itself in any way to meet these changes? That is essentially what we would like to set the course to hear. Who would like to kick off?

Elizabeth Stuart: I am happy to start. You are absolutely correct; I think everyone would agree that the landscape is changing. The main differences on this new global horizon would be the rise of Middle Income Countries and BRICs, and with that the new location of the poorest. Andy Sumner's work identified that 72% of poor people now live in Middle Income Countries, not because they have moved but because those countries have changed status. Twenty-eight countries have graduated from Low Income Country to Middle Income Country over the past decade, which is a huge change. Some of those countries have now become donors themselves, in some cases at the same time as being aid recipients.

There is also the introduction to the aid landscape of large-scale lending by philanthropic foundations, NGOs and the private sector. Some of that is not new, but the scale of it is new. We have not seen this kind of scale of lending before. It is difficult to quantify exactly the amount of aid coming from non-traditional, non-DAC donors, but it seems to be substantial. One calculation, by Homi Kharas at the Brookings Institution, has assessed that, if you take what is called country programme aid, which is aid that is delivered to the country for the country to spend in-country—so it is not being spent on domestic consultants or things like that—then aid from new donors is of the same size as aid from traditional donors, which is fairly extraordinary.

Briefly, the implications on this for DFID would first of all be the amount. We would argue very strongly that, in the short to medium term, the 0.7% figure is absolutely still necessary. It has been very carefully costed. Back in 2005, the UN estimated that to meet basic poverty needs—i.e. to reduce basic poverty and nothing but that—donors would need to be spending 0.54% of GNI. However, if you wanted to get to the wider sorts of poverties and the wider inequalities, which indeed DFID does and which we would very much welcome because it is not just about income, you would need to be spending approximately 0.7%.

It has been very carefully costed, and it also seems clear that, although poverty is actually reducing—we have seen the extraordinary poverty reduction figures in countries, primarily led by China but in other countries as well—counter-intuitively reducing poverty is going to get more expensive because the people who are left in poverty are the hardest to reach. You might like to term it "the highest hanging fruit".

The people who have been reached so far are those who are easiest to bring above an internationally agreed poverty line. The people who are left in poverty are going to be the hardest to reach; it is going to be more expensive. Also, if we are going to be more ambitious in what we are trying to achieve with our poverty reduction, which is very much the parameter that has been set out in the process that is being co-chaired by the Prime Minister around a successor to the MDGs, the post-2015 process, what is being targeted is something that is rightly a bit broad and ambitious. The 0.7% figure needs to stay in the short to medium term. Of course, we do not want to be aid-dependent forever, but in the long run, as John Maynard Keynes said, we are all dead, so I think in the short to medium term, it needs to be there.

There are other implications for DFID. It will not be a surprise to you that we are very supportive of UK aid; we think it is very high quality and effective. We like the emphasis on fragile states. Again, according to the work done by Andy Sumner, two-thirds of the poorest people are going to be living in fragile states, so that emphasis by DFID is very welcome.

There will need to be a greater emphasis on partnership, though, particularly with Middle Income Countries. Relating to Middle Income Countries will not be a traditional relationship of donor/donee; it needs to be more of a partnership. There needs to be a greater understanding of soft skills at DFID rather than the traditional managing big aid programmes. Finally, we do think that Middle Income Countries should still be receiving aid, but I can talk about that later.

Chair: We will explore some of those in a bit more detail.

Richard Manning: I agree with what everybody has said about the changing landscape. I do not have anything very new to say about that. I suppose the question is how we can achieve sustainable improvements in people's lives as the world population rises to about 9 billion people in 2050.

We are on a path to somewhere we have not been before. Admittedly, populations are growing more slowly, but this is a big challenge. Sustaining these people on a gradually improving level of income is a huge challenge for everybody. It seems likely that, given the very large disparity that still exists between incomes in different countries, some form of inter-country concessional flows from the official sector is going to be a very important part of achieving a sustainable future for all of us. There is still a case for a strong investment by countries in these cross-border official concessional flows.

Obviously, you have to position this in a world where we are dealing with the results of huge progress. I used to deal with Bangladesh when I was working for DFID's predecessor in the late 1970s. The figures show that, in those days, aid was more or less equivalent to total tax revenue in Bangladesh. Tax revenue in Bangladesh is now six times aid flows to Bangladesh, not because aid flows have fallen but because tax revenues have hugely increased.

Ghana, a country which was desperately marginalised in the 1980s, famously launched a Eurobond in 2008. Other poor African countries, many of them recipients of debt cancellation and HIPC, have been doing the same in the recent past, so we are definitely in a different world. To me, a crucial issue is the proper use of these funds and whether we have a good system internationally for encouraging debt-creating flows to be used in a sustainable manner. That is a very important issue.

Finally, on DFID, I obviously have a bias as I spent most of my life working for DFID and its various predecessors from 1965 to 2003. There are many models of how you deliver aid across countries. When I was also chair of the OECD Development Assistance Committee, we produced a publication, which I recommend to the Committee, about the characteristics of more or less effective official aid systems. It is not about one model being inherently better than another. The Dutch have a total different model from the British, but both have proved to be quite effective.

DFID does tick a lot of the boxes. It has got a strong legal basis and a budget that can be very flexibly used across different types of assistance. The multilateral and bilateral trade-offs can be done more easily in that kind of system than one where the Ministry of Finance does or the IFIs, and the Foreign Ministry does other forms of assistance and so on, which is the case in many other countries. Also, and this is a key strength of the British system that one would perceive internationally, DFID has over the years built a fairly high level of core expertise, and managed to combine professionals of various kinds into one entity with a single focus. That is quite a powerful model, in my opinion.

As far as 0.7% itself is concerned, everybody knows the history of this and it would be unlikely that there is a magic about this figure. It is curious to have a target for inputs, i.e. spending, rather than for outcomes such as the Millennium Development Goals or whatever framework we have after 2015. I think the argument that has been used, however, right from the start of creating the concept of official development assistance in the 1960s, is that there is some value in an international norm that incentivises countries to move in a particular direction, particularly for a category of spending that is not self-evidently in their very short-term interests. This is long term.

Chair: We are going to come back to that in a bit more detail later.

Jonathan Glennie: Of the changes that are taking place, for me there are two mega changes that are irreversible: the rise of the poorer countries, the emerging countries as now described, has transformed the global landscape in every way, and we are talking about development as a subset of that; and secondly, and this has been going on for decades but, again, is about to be part of the UN framework finally, the sustainable development aspect—the recognition that we are living within planetary boundaries. Those are the two new elements in this era of development. There is maybe a third, which may not be irreversible, which is the realisation that the experiment with exaggerated neo-liberalism over the last 30 years was a mistake. In other words, there is a recognition that too much focus on the private sector and neglect of the public sector was a mistake, and there is a rowing back from that.

I have a couple of comments on the changes in poverty. There is an opportunity for the Committee in looking at the next steps for DFID over the next two to five years, or however long your time horizon is, also to set out the beginnings of a transformation of our understanding of poverty and the role of aid. We and Andy Sumner's numbers think of poverty as $1 or $2 a day. It is an incredibly stingy analysis of poverty. There are even some analyses going round today that people living on $10 a day should be described as middle class.

Our traditional understanding of people living in poverty is an incredibly stingy one. We need to be thinking about bringing people up to something approaching the standard of living that we have in this country. If we start thinking that way, we are miles away, and years and decades away, from resolving some of the problems that exist in our world. We have to be careful of combining this idea that of course you want to end extreme poverty in the poorest of the poor with the idea that, at that point, our responsibility as wealthy countries begins to come to an end, which is often what one hears in the press and in some analyses, which I think is a big mistake.

Secondly, as we know, the definition of a Middle Income Country is when countries have an income per capita of $1,000 a year. That is totally arbitrary; we do not even know where that equation emerges from—somewhere in the 1960s or 1970s in the World Bank. There is a danger of focusing on Middle Income as a level. We need to start thinking about the role that aid plays. We have Andy Sumner's numbers. I know Andy, and he has done some really important work. Nevertheless, the supposed move of poor people to Middle Income Countries I think is quite misleading. It is basically talking about five countries. Yes, a lot of countries have moved to Middle Income status in the last 10 years. It is worth noting that, in the '80s and '90s, there was also a great movement towards Middle Income, and a lot of countries regressed again.

Let's not assume that this is uni-linear. Things can happen; shocks can happen. In the late '90s, shocks did happen. Countries that were Middle Income moved back to low income status. This movement of poor people to Middle Income Country is based on five countries: China in the late 1990s, while India, Pakistan, Indonesia and Nigeria all became Middle Income Countries in the last 10 years. Some 80% of the poorest people in the world live in 10 countries. When those countries shift over an arbitrary barrier, they have suddenly become Middle Income. That really does not mean anything, in my view, in terms of what the role of aid is in those countries.

If you look at countries like India, they have been receiving a very small amount of their GDP in aid for the last 20 or 30 years; I think it is 0.2%. That money has never been significant. The question becomes: what role does that money play? I worked in Latin America for a long time, and those countries are not aid-dependent and really never have been, certainly not for decades. Again, what is the role of aid? It is a very small amount of money in Middle Income Countries and those countries that do not depend on aid, compared with the role of aid in countries that are heavily dependent on aid, most of which are in Africa—and they are increasingly less dependent on aid as well.

The final thought I will share with you is on the rise, as Liz mentioned, of aid from other countries. It is quite an interesting position that we are in—that in traditionally wealthy countries, we are re-examining the purpose of aid. I know there is quite a strong pressure on MPs and others to look at why we still need aid in this world. When you look around the world, countries are setting up aid agencies, which is quite the reverse of what is happening here. They are just beginning on the process of engaging in aid. That is because, as we know, the term “aid” is a little bit unhelpful because it is has got history. Most countries setting up aid agencies do not call it aid.

Chair: Well, this is the International Development Committee, and we like to call ourselves that.

Jonathan Glennie: Sure, but it is International Development. I have no problem with using the word “aid”—it does not matter—but what I am saying is that most countries that are setting up international development agencies do not call it aid; they call it co-operation. There is a very strong recognition that this is about mutual benefit between countries. The idea that it is from rich to poor is happily beginning to be less important. It is still important, of course, in the transfer of wealth, but now it is much more about interchange of experience, ideas and, yes, money when it is necessary.

I can see a future in which rich countries no longer deliver money to poor countries but all countries in the world, including the very poorest countries, contribute a certain amount of their income to respond to the global challenges that exist. Those would be classically the Global Public Goods Agenda. That is the long-term vision that I would use to challenge the idea that aid is somehow on its way out.

Chair: I can see Fiona Bruce has a question.

Q3 Fiona Bruce: Yes. Elizabeth, you said we need to be more ambitious. For example in education, how practically could you make this happen? We have had a massive investment in primary education, but we now see, for example, in Africa, the growth of jobless young people under the age of 25. We have got to invest in science and technology and change our whole approach towards education and our focus. How do we broaden our approach to that investment? Isn’t it essential that we also do that with businesses and with industries as they invest in those nations? In other words, that is what Jonathan is talking about, which is co-operation.

Chair: That was focused at Jonathan, I think.

Fiona Bruce: Elizabeth first, I think, because it is how we have to think beyond the box now. All these young people are coming out of school at 12 or 14, but what do they do?

Elizabeth Stuart: Absolutely. That is right. Getting children into school is the first stage. Getting children out of primary school able to read, write, and do arithmetic—basic educational attainment—is the next stage. Getting them into secondary school is the next stage. Then thinking about tertiary education, skills and vocational education are all absolutely vital. I go back to the money question: there still is not enough money to do the first thing. That does not mean we should not be ambitious and trying to achieve two, three, four and five down the line, but we need to be realistic that number one has not yet been achieved. We have made huge strides, but it has not yet been attained.

We are getting better, in that we are looking at measuring impacts and not looking at inputs. I take the point about money being an input, of course, but our interest is in the outcomes. We need to get better at examining what developmental outcomes we want and being able to measure those. We need to get better data to be able to do that as well. Then I think we need to be very clear that the private sector does have a major role to play in terms of building skills, and not least in terms of creating jobs. That said, there is a slight caveat on that; it has got to be the right sorts of jobs.

Save the Children just signed a partnership agreement with GlaxoSmithKline, for instance. We are interested in innovative ways of working with the private sector, but we have to make sure that we are very clear on what the private sector is, because it is many different things in different countries. The private sector can be a kiosk in an unpaved street that is selling de-worming tablets as malaria pills, or it can be a multinational company.

What has been lacking in the past has been exactly that: the evidence. The impact that private-sector investment has had on poverty reduction has not been looked for. Analysing and measuring those impacts is very important. When polling is done of poor people in poor countries, and when the World Bank carried out the Voices of the Poor exercise, a key ask that poor people have is they want jobs.

Fiona Bruce: Yes, absolutely.

Elizabeth Stuart: I think Nancy Birdsall from the Centre for Global Development put it very nicely. I heard her speak the other day in London, and she said, "It is about pay stubs rather than about entrepreneurship." On the whole, it is about a regular pay check.

Q4 Fiona Bruce: I absolutely agree. A brief supplementary, if I may. We need to help countries, particularly for example those in Africa, to ensure that, if other countries are coming in and starting to build factories and develop and take advantage of—I do not mean that pejoratively—a work force, the benefits of that are suitably gained by the local indigenous population. We need to ensure that Governments are poised to create that kind of development, much as you would have a parallel here of a Section 106 agreement in a local community. Do you think there needs to be much more help given to Governments to do that?

Elizabeth Stuart: Yes, absolutely I do, but it is also about policy coherence here at home. It is about the role we play in negotiating trade deals in terms of the business environment that is being established in a country. It has also got to do with the sorts of norms we are looking for and favouring in our aid allocations, which is also to some extent, in some countries, continuing to drive domestic policymaking around the business environment.

For instance, the World Bank Doing Business league tables have just been revised. However, they are still favouring very light-touch regulation, which is not necessarily going to be the kind of regulation that delivers decent work—as you said, the kind of work where the benefits can be captured by local communities.

Q5 Richard Burden: In your opening remarks, all of you have highlighted very well the huge agenda we are dealing with here. Responding to Jonathan, we are very clear that what we are trying to look at here is the future development co-operation, not simply the future of aid as defined by ODA.

However, that is part of what we are looking at, and I would like to ask you all a little bit about that, in particular the Middle Income Country issue that you have all touched on. As far as ODA is concerned, and I think you will be asking in a while a bit more about definitions of overseas official development assistance in the future, how far do you think it should be focused on poverty in Middle Income Countries, or growth in Lower Income Countries, or more widely on global public goods, in perhaps the context of a much broader definition of what development assistance is?

Jonathan Glennie: I just want to reply very quickly to Fiona Bruce's question. The international development community, insofar as there is one, focuses very much on specific aspects and sometimes neglects to realise the trade-offs that exist in developing countries that are political—there is politics going on. Primary education is one of the classic examples.

I was at the memorial of Meles Zenawi recently. He very famously rejected the idea that primary education should be the only focus of the money—or that it should be the primary priority, in fact. When countries try to transform themselves structurally rather than rely on outside finances, they need to invest in secondary and tertiary education. The current

Director of the UN Millennium Campaign, Charles Abugre, said that if he had only one goal out of the post-2015, it would be girls into secondary school. It is at secondary-school level that they start to transform their own villages. They get into jobs, and that is when society starts to change.

It is understandable why the international development community is focused on absolute poverty and the basic primary education. At the same time there are trade-offs, and we have to accept that. The same goes for the private sector. There has been a lot of focus on microfinance, and I strongly agree that we need to look much more at jobs than just growth, and much more at transforming local economies than just at microfinance.

On the question of Middle Income Countries, I very much take the way that you split that up. On the one hand, is there a role for the international community to support development in Middle Income Countries? I think the answer to that is quite clearly yes. Middle Income Countries are where the vast majority of the poor live. Apart from anything else, the vast majority of countries are Middle Income Countries. They are immensely important for security, climate and other sustainability issues. Does the international community, led by the UN, need to work with Middle Income Countries to support their development? They are also in danger always of regressing when they have not got the institutional structures strongly defined, so yes.

The next question is how, and is there a role for development finance? What kind of development finance? ODA is a particular kind of development finance, but there are many others. As I said before, my view is that we need to understand much better the role that aid, international public money, has played in countries that have never received large amounts. In other words, for very aid-dependent countries in Africa the role of aid is incredibly different; it is half of the economy sometimes, whereas in countries like Colombia, where I was living, it is 0.1% of the economy.

The role that aid plays in Colombia could not be more different from the role it plays in Liberia, but that does not mean it is not important. If you look at the Paris Evaluation, the independent evaluation of aid in Colombia, just as an example—I know it is not a big focus for Britain—that catalytic money focused on human rights and supporting civil society. I worked for Christian Aid in Colombia. It is very difficult sometimes in very unequal societies, and India would be another example, to get money behind those parts of the society that are fighting for change, human rights and equality. Often that is international money, so we need to be very clear that it is not just a huge capital input to build infrastructure. It can be very catalytic money, and it may well be that over time it goes down.

Then there is the question of global public goods. No one that I have read has really got a very good answer to this yet. We all know there is a huge amount of money that needs to be spent. Development now, and this is the big issue of planetary boundaries, is not just about development as we developed. It is a far more complicated task because it is development without screwing the planet up; it is green development. By most accounts, at the same time as hopefully giving benefits in the long term economically, in the short term that is going to be much more costly. Therefore countries need to be supported, and this is the basis of all the climate finance stuff, but it is quite an ambiguous area.

If we are saying we are reducing aid to India and South Africa and cutting aid to China, that makes perfect sense in our current understanding of aid. Yet with climate finance, we are quite clearly meant to be—and no one talks about it because you would probably find it very hard to sell to your constituents—increasing it to these very countries to help them grow sustainably. I think there is an ambiguity there. My view is that we need to do more thinking and research on it, but the answer is much more likely to be multilateral than bilateral. I suppose that is one message to DFID on that.

Q6 Richard Burden: The catalysing effect of aid was a theme that we developed in a number of reports, in the last Parliament in relation to assistance to China and, indeed, in this Parliament on the question of India. Could I just push you a little more? Part of that catalysing effect is spreading and generating best practice, and having a catalytic effect in that way. Another issue that you touched on was about combating inequality and spreading human rights. How far do you all feel that is a legitimate role for aid? Where do the limits of universal rights come up against national sovereignties?

Jonathan Glennie: I will come back to that with a very quick point, and I am sure Liz and Richard will also have comments, but there is no answer; it is incredibly complicated. Firstly, the international community has an absolute duty to focus on issues of inequality and human rights, which it does already. Again, though, it is more likely to be a multilateral than a bilateral response.

The attempts by DFID to use aid to improve human-rights situations in some of the aid recipient countries are unlikely to be successful in the long term. There is very little evidence; in fact, there is quite a lot of evidence that those kinds of conditions do not make long-term changes in highly complicated political societies. Nevertheless, the longer-term pressure from a range of agencies, multilateral attempts to focus on inequality and human rights, will make a change.

Women's rights are an absolutely classic example. In most countries in the world, there is a strong focus on girls going to school. In some countries that is an indigenous movement, but in other countries a lot of that is down to international pressure and people sharing ideas. These things become internationalised.

Chair: Can I just point out that we are halfway through the evidence session and we are on the second question? We are going to need some snappier advice, and I know that Chris White is getting very agitated.

Q7 Chris White: It is getting late. There was just a very quick point in your wide sweep of international development. You mentioned the words "a trade-off", and in that paragraph you mentioned a trade-off. Is there a trade-off between absolute poverty and secondary education, for example? How do you see that? Was that a casual remark, or is it one or the other?

Jonathan Glennie: Yes. I think there is a danger in international development. We see it as this kind of ideal, utopian way of working, whereas when you are working in politics in Britain, there are trade-offs the whole time. There are budgets to manage. The budget the current Government is managing is full of trade-offs.

Exactly the same is taking place in Ethiopia. There is a limited amount of money, so trade-offs have to be made. Will we focus all our money on primary and neglect, to some extent, tertiary education, and what will that imply? Hopefully, that will mean having basic services for many more people, but possibly not the kind of indigenous Ethiopian engineers and scientists that we need to really move on from independence. Will we, and this is a hard thing to sell, say that there is a trade-off? Invest in universities and secondary, and possibly you will be slightly slower in achieving the primary education. Of course there are trade-offs.

Chris White: My view is that you have got yourself a little stuck in the horns of a dilemma. You can actually do both of these things. I do not think there has to be a trade-off between one and the other.

Q8 Hugh Bayley: Can I start with you, Richard, as a former chairman of the DAC? Do you think security and peacekeeping activities ought to be included within the definition of ODA?

Richard Manning: We did some work on this when I was chair of the DAC, and indeed we made a few rather small changes. There are arguments both ways about this. I think it is quite important if we are going to sustain this category. It always comes back to the question about definition. We have to be quite careful how far we broaden it. I think a lot of people would get off the train if it appeared to be covering military assistance and things that went to build military capacity and so on.

Q9 Hugh Bayley: Would you distinguish between police and military capacities?

Richard Manning: At the moment the DAC does, yes. Everything that DFID does for police in developing countries counts as ODA; everything it does for the military does not. It is a very clear distinction.

The question is when the military is being used to do something. If you go to straight peacekeeping, the other thing you have to bear in mind is this is hugely expensive. I remember being involved with the Cambodian peacekeeping operation in the early 1990s, and the cost of the UN intervention was the same size as Cambodia's GNP. The military are very expensive, so you would have to reconfigure a lot of things if you made a step of that sort. Some countries, including the Dutch, have clearly argued for this.

Q10 Hugh Bayley: We observed that point in South Sudan—the comparison between the UN peacekeeping costs and the GNI. What about other global public goods? We have talked a little bit about climate change. What about global public health, for instance?

Richard Manning: Of course a lot of this is counted already. If you take climate change, I do not know of any country that is not including at least all of its adaptation expenditure as ODA. We are trying to eradicate polio. That is no doubt all counting as ODA, but its benefit will include huge benefits to the national health service in saving money; that has been clear all along.

I think this comes back to Jonathan's question as to whether, in the long term, the point of inter-government financial transfers is about broader global public goods than the definition that we currently have, which is around development—development itself, of course, being a word that is pretty elastic.

Q11 Hugh Bayley: It seems to me that you are arguing, and it is a view I share, that the foundation on which all ODA should be built should remain poverty alleviation. However, one needs to realise that, for example, work on polio eradication contributes to that. Work on environmental sustainability can contribute to that. I am putting words into your mouth; I do not want to.

Richard Manning: One has to recognise that the ODA definition does not say anything about poverty reduction or alleviation. It talks about development, if I am not wrong, which comes back a little bit to the conversation we have been having about whether Meles was right to invest in tertiary education.

Personally, I do not favour a very narrow international definition. I do not think it will work anyway. It has never been treated like that by anybody. It is better to do what we are currently doing, which is to set a series of outcomes that we all want to get. The MDGs are a very imperfect framework. There may be a better one under SDGs or post-2015, and then you can define in relation to that something that enables you to incentivise a reasonable amount of official flows across borders in support of those planetary objectives.

Q12 Hugh Bayley: Could I put one final question both to Elizabeth and Richard? It is a question that Jonathan has answered comprehensively—there is not very much difference between Lower Income Countries and Middle Income Countries at the margin, and many poor people's needs need to be addressed through ODA in Middle Income Countries.

Frankly, I do not share that view because the difference between China or India on the one hand, and Burundi or the DRC on the other, is that, if China or India, through public policy, chose to spend what was needed to get all children into school or to meet other development goals, they would have the resources to do so through taxing the better-off and middle class. However, we know in the DRC and Burundi those goals are completely unattainable without ODA.

China not only has higher, bigger foreign exchange reserves than the UK, but is bigger on a per-capita basis. The idea that we need to transfer money to a Middle Income Country such as China to help them abolish poverty is not a view I share. What view does Save the Children take from a policy-department perspective and, given your experience, Richard, what view do you take?

Elizabeth Stuart: I think you are absolutely right to say that there are big differences between countries such as China and India, and the DRC. This is not necessarily a Save the Children position, but I would argue that you should get rid of all these income categories because they are meaningless. As Jonathan said, they are totally arbitrary. You need to look at a set of criteria for each country based on how vulnerable that country is to falling back into a situation where you have higher levels of poverty or lower levels of per-capita GDP. You also want to look at non-income factors.

To answer the question specifically about China and India, it sounds strange and counter-intuitive but some very interesting research has been done on this by Martin Ravallion, who was at that time the chief economist at the World Bank, to show that India actually cannot fund its own poverty reduction. You would need such a high marginal tax rate to be able to do so; your tax rate would have to be in excess of 100% to be generating enough revenue. Clearly, that is not possible.

I would also counter the idea that India is not doing anything or has not been doing anything to relieve its own domestic poverty situation. For every pound that the UK was giving in aid, the Indian Government has been paying £400 in poverty-reduction spending. Clearly it is not the case that the country is doing nothing and other donors have been doing everything, and they can do it all themselves.

India is an example of a country that is not as wealthy as some Middle Income Countries, but it is not the poorest. There are Middle Income Companies that are more vulnerable as well, so the idea that you have these sort of arbitrary categories should not be dictating either our aid policy or our broader development co-operation and collaboration policies.

Richard Manning: Countries are clearly on a spectrum, and it is convenient to make some chops every now and then, as perhaps happens. The Martin Ravallion thing is quite a good place to start. Some countries can more or less do most of it from their tax, and some require some assistance. With these big countries, as Jonathan pointed out, aid has always been very small. The question is, is it catalytic? Does it change things?

From that point of view, I am quite sympathetic to the idea that one carries on some kind of relationship that encourages positive social change in countries like that. It is certainly the case that you need a very different kind of programme. It is also an area where less concessional flows are more the case, as with the climate finance example. No one is suggesting we give China lots of free money for climate change, but there is every reason to incentivise it through less concessional money for that.

Q13 Chris White: An increasing proportion of development assistance is now provided by non-traditional sources. I wonder if you could give me some examples of these new sources, and how do you think these new sources are impacting change compared with more traditional donors? This is a question to anyone.

Elizabeth Stuart: There are so many different examples. The Gates Foundation is an obvious one, a major philanthropic body, and new donors who have not traditionally been on the donor scene. Iran, for instance, is now a donor to the World Bank, which I think is quite an interesting dynamic. There is South–South co-operation, which is money, capacity building and knowledge sharing, which is a new resource transfer as well. There are an enormous number of examples. There are vertical funds, which did not used to exist.

There are many implications for traditional donors. That you have these new donors is obviously welcome. When recipient countries or partner countries have been surveyed and asked what they think about these new relationships, they have welcomed the fact that often aid is dispersed rapidly, with limited or no conditionality. In some instances, they would view it as better quality aid than aid from traditional donors. I am not sure they would be comparing that with UK aid, but with some poorer quality traditional donors I think they would say they prefer this new donor relationship.

The area where we would need to see some kind of improvement is that those new donors have not yet signed up to the same kind of aid effectiveness agreements that the traditional donors have signed up to. While they have done so on a voluntary basis through the Busan process, they have not done so in any binding way, and that is where we would need to see some movement. Broadly, though, they are laying down a gauntlet to traditional donors to improve the game.

Q14 Chris White: One of the most effective means we have seen in a number of countries we have visited is microfinance. What is your view of how effective microfinance would be?

Elizabeth Stuart: It is not something that I necessarily have a view on. I do not know.

Jonathan Glennie: I am not an expert on it; in fact Claire here, from *The Guardian*, has read quite a lot if you want to catch her later.

My analysis from a non-expert perspective is it has been wildly exaggerated as a magic bullet to development. Almost all the analysis coming out at the moment says that. Of course some entrepreneurs will do well when provided with small loans, but a huge amount will not. What happens then? There is an increasing amount of evidence suggesting that you need to invest in job creation rather than expect almost the burden of creating their own jobs to be placed on the poor. That is not how any of the developed countries developed. We developed industry.

I would like to answer your other question as well, but I would just very quickly like to respond to Mr Bayley. If one's vision of India as a kind of country doing well is everyone scraping by on \$5 to \$10 a day in a very precarious living, that is current. If Indian income was distributed equally—it is basically an entirely theoretical perspective that you are proposing because it is never going to happen.

Q15 Hugh Bayley: I am not suggesting that for one minute. I am saying if you go to a slum in Delhi and you suppose that the only way you could get a pit latrine dug every 100 metres through the slum is if foreign aid paid for it, that is not the case. Elizabeth makes the case that 0.25% of India's spending on development comes from aid, so it is clear that our money is not what is critical.

Jonathan Glennie: I could not agree more.

Hugh Bayley: Maybe our expertise is critical, and perhaps they should pay for it.

Jonathan Glennie: I could not agree more. If your position is that India should never have received aid, and nor should the whole of South America, or any country that hardly received any aid, then that is at least a coherent position. I respect that. The idea that India now is in a position to pay for poverty reduction, whereas a few years ago it was not, I do not think is a sensible position. If all India's money was spread equally, which is never going to happen, everyone would be dirt poor. There is not enough money in India to support—

Hugh Bayley: We should move on.

Jonathan Glennie: Yes. My answer to this is I would highly recommend some reports that ODI has carried out, called *The Age of Choice*, which look at the new donors, all the new sources of money, including some private sources. The reports look at it very much from a recipient-country perspective. In other words, we all know that there is this huge amount of money in the international ether, but when we look at Zambia and Cambodia, and look at which monies are doing what, I think that is quite a helpful perspective.

The role of DFID and its experience on effectiveness, value for money, issues like civil rights, checking on social environmental impact—all of those things we are seeing increasingly positively. A lot of the new money from new donors is much faster money, as Liz said, but may not have that focus on institution building or on social and environmental impact that has been such an important part of the last 10 years of aid effectiveness.

The work the African Development Bank and the OECD have done implies very much that, in Africa at least, there has been some implication that the Chinese especially are somehow in competition with DFID and other donors. There is probably an element of truth in that, in the sense that aid has complex motives. It is not just an altruistic action; it is very much related to politics and trying to get something. That is something that in Britain we sometimes prefer not to recognise. The evidence appears to suggest that the new aid is quite complementary to other forms of aid—focusing on infrastructure where currently traditional aid, OECD aid, focuses more on social areas. Politically, it is important to be wary of criticisms of Chinese aid based really on competition.

The third issue is that the difference between now and 10 years ago, and Richard has touched on this, is that foreign private flows have massively increased, especially to Middle Income Countries but also to Lower Income Countries. Revenue has massively increased within Lower Income Countries as well as in Middle Income Countries. That transforms the role of international public money. It is going to be decreasing in all of those countries.

My final point is: how will the post-2015 settlement be financed? We always start to look at this thing called the financing gap. It is a little bit like the climate finance, which is meant to be 100 billion. It is private and public funds thrust together in this kind of mélange of "We need this money to achieve X", but it does not look at the different role of different types of money. In other words, public money is very, very different, even if it is much smaller, than what private money can do.

Private money is basically motivated by profit and the market, whereas public money can be, hopefully, motivated by other objectives. I would urge the Committee, when they are looking at how much money is needed to require what development goals, not just to look at the quantity but also let's call it the quality or the different types of money going into that mix.

Q16 Fabian Hamilton: Jonathan Glennie, can I just pick up on that last point? We have been discussing India, and whether or not India still needs development aid. Can I just put to you, and perhaps it does build on what you have said, that the real problem in places like India, apart from the obvious problem of distribution of income, is actually infrastructure and governance? If you had really good sanitation, for example, and proper local government, then you would go a long way towards resolving the problems of distribution of wealth, because that would help the poor hugely. How would you react to that?

Jonathan Glennie: I do not know India deeply, but I would say precisely it is the classic development problem of how external actors can engage in those kinds of systemic institutional changes. No one has worked out the answer. Sometimes external actors have helped; sometimes they have played a really negative role. It is difficult to know when that is going to be the case.

My point is not that I know how to support development and poverty reduction in India. That is a complicated question. However, I am convinced that there is a role for international co-operation in all countries in the world. India is one of the poorest countries in the world without any shadow of a doubt. I am convinced there is a role for international co-operation. I am also convinced that there is a huge financial deficit in India. I do not buy at all the idea that there is money in India. There is hardly any money in India.

Fabian Hamilton: That is effectively what you said, Elizabeth, isn't it? There is not enough money in the whole of India to resolve its problems.

Elizabeth Stuart: Yes.

Q17 Fabian Hamilton: But I suggest that, like in the United Kingdom maybe 200 years ago, when we had rapid industrialisation and a very rapid growth of a middle class and the very rich through industrialisation, what helped equalise the distribution of wealth was local government and decent, proper sanitation—that actually helped public health enormously, and therefore the quality of life.

Can I just challenge you on one thing you said earlier in your opening remarks about the definitions of poverty? You used a dollar equivalent. Is there a definition of absolute poverty? Surely what $10 will buy you in the United Kingdom is very different from what $10 would buy you in Burundi or the Congo. How do we define what that money means? $1,000 a year is peanuts in the UK or the USA or anywhere in Western Europe, but it is worth considerably more elsewhere because it can buy more.

Jonathan Glennie: One dollar a day is actually worked out on what they call purchasing power parity. So it is the equivalent of having $10 a day in Britain, so it is incredibly poor. It is as if people were living with $10 a day in the UK.

Fabian Hamilton: I just wanted to be clear about that.

Jonathan Glennie: My line on that is yes, of course, we should focus on extreme poverty. I absolutely support that. These numbers—I think Ravallion might have come up with it—are useful to focus our minds on the poorest of the poor.

The danger is that sometimes there is the implication that, once the poorest of the poor are dealt with, we have eliminated poverty because there is no longer anyone living on under $2 a day. "Let's move on to different countries or to a different focus." No, that is extreme poverty. Let's now move on to $5 a day, $10 a day, which is still incredibly precarious, or $20 a day, $30 a day. For me, that is the future of international development rather than withdrawal from aid because we have eliminated the very worst types of extreme poverty.

Hugh Bayley: With great respect, the question is who is "we"? I used to be the Minister on anti-poverty strategy in the UK—abolishing child poverty in a generation. I would not have expected America, a richer country than ours, to pay for our tax credits. The question is whether there comes a point at which a Middle Income Country can fund its own continuing raising of the minimum standard.

Chair: I am going to bring in Michael McCann. We are obviously teasing out what the role of development assistance is when the majority of poor people are in Middle Income Countries. That is what we are teasing out of this inquiry, and what more the UK can do. Do you want to comment on that, Elizabeth?

Elizabeth Stuart: Yes, just very briefly. Again, this is not an official Save the Children position, but we seem to be talking a lot about Martin Ravallion and his thinking, in this Committee. Here is an idea from him, and it comes again from this concept of what an appropriate tax rate is. If you are looking at affordability, when is it that countries can afford to pay for their own poverty reduction? He suggests that what seems to work in the majority of countries—a figure that there seems to be enough empirical evidence to support—is around $4,000 per capita GDP. That seems to be about the level at which a country could have tax rates that would be sustainable and would raise sufficient revenues to start dealing with these problems. There is an answer.

Chair: We will put that in the pot, thank you.

Q18 Mr McCann: Can I ask some questions about the most topical subject in international aid issues over the last couple of years? That is the 0.7% target. Richard touched in his opening remarks on the history of it, going back 40-odd years. I was just wondering, perhaps starting with Richard, if you think that the 0.7% aid target is both realistic and appropriate for the longer term.

Richard Manning: It has been effective in a number of countries—one has to say a limited number of countries. It obviously now includes the UK, which used not to take it seriously at all and in the last 10 years has taken it extremely seriously. You can throw all sorts of stones at it. I mean, if you try to construct exactly why it should be 0.7% rather than 0.6% or 0.2%, you could spend a lot of time doing that.

So part of me takes a sort of conservative attitude to your question, which is, "We have got something; let's not get rid of it." Let's encourage people to move towards it. Clearly, intellectually, and taking a longer term view, there would be reasonable grounds for saying, "Why don't we try to look at this again?" Whether you will get an international consensus on what a figure should be, and what kinds of things it should cover, comes back to the peacekeeping point. You have got to decide what you put in this box if you are going to open it up and say, "Well, we should have a target for this."

As I say, the point of a target is to incentivise people to move in that direction. It is never going to be a legally enforceable thing. It is not a bad idea, given that co-operation is one of the harder things to encourage Governments to invest in, because it is not immediately helping their citizens. Quite honestly, I am still torn between thinking, "We have this thing; let's go with it, and keep it going for some longer time," and thinking 2015 is a reasonable time to start thinking what sort of international effort is needed if we want to deliver outcomes by 2013, and what that implies.

Elizabeth Stuart: As I said in my response to the first question, I think there is still very much a need for it right now. I would agree that at a time when we are finding it difficult to find universal agreement on development co-operation and global public goods and all sorts of multilateral questions, we have got this and it is agreed. There is public support for it, we are delivering it, other countries are delivering it and other countries are committed to deliver it. It would seem to be an absurdity to back away from that now.

Going back to first principles, what is the money there for? What is it going to do? We have done some calculations, and Britain's 0.7% is going to send—we have talked a lot about children in school—an additional 16 million children into primary school, lift another 10 million people out of hunger, and avert 250,000 additional avoidable child deaths. This has real consequences, and it is money that can be spent and will be delivering development outcomes. I think it is very clear that we want to keep it there.

Just reflecting on something that Richard said, we have some concerns about some of the mission creep in terms of definition and use. Looking at the conflict pool, we are very supportive of the fact that DFID is prioritising governance and human-rights issues, which is what some of this money is being spent on within the conflict pool. We would be concerned if any more ODA was spent through the conflict pool, not least because it has a tripartite management structure, which means the allocation decisions are not always going to be driven by poverty reduction and humanitarian imperatives.

Also, we would be concerned if it were conflated or joined with other pools, such as the counter-narcotics pool, the counter-terrorism pool, where again they have explicit national security imperatives rather than development and poverty reduction imperatives.

Jonathan Glennie: The 0.7% target analytically does not make any sense at all; it is a number. The only discussion I think for the Committee is its political importance, and I leave that to you and Liz and those people engaged in the politics of it. I can quite believe that it is a useful target. In terms of what it actually means—not very much. Possibly moving towards a 1% target is quite a good idea. There are a couple of things I want to share with you—a little bit of what it might look like.

Firstly, the UN is very much more likely than the OECD or DFID to be making these decisions. If there is a point at which 0.7% is re-discussed, or the definition of ODA is re-discussed, countries like Brazil, China—South Africa has got its aid agency—and all of those countries are going to be very interested in how it is redefined. It is not going to be any more a decision for the OECD countries. The best idea I have heard about it, and Richard mentioned it earlier, was that politically it is important. If it incentivises countries/people/Governments to do the right thing, then it is important.

Q19 Mr McCann: With the greatest respect, Jonathan, speculating on whether it can be changed or increased is pie in the sky. The bottom line is it was set in 1969, 1970, and it has only latterly been achieved by very few countries, some of them very, very small indeed. We are the biggest nation that has achieved it, which is a significant milestone.

To play devil's advocate, isn't there a danger that we are going to become isolated as a country? There is a lot of public support for it, but equally there is very much public anger about it as well, and it would be wrong to ignore that. Therefore if the UK stands out there, one of the biggest nations in the world delivering 0.7% alone when other EU states are not delivering it, isn't there a danger that we will end up in a situation where those who describe it as a vice rather than a virtue are going to have their voices heard more strongly?

Jonathan Glennie: Again, that is a political analysis that you would be much better placed to know than I. I just go back to the idea that these targets generally are to incentivise good behaviour or best practice.

To answer some of the questions about military, the US famously delivers a very small percentage: 0.1% or 0.2%. When you take into account US citizens' contributions to global development, it is vastly bigger probably than the state contribution—bigger than what Britain does. I think those kinds of things also need to be incentivised. Private companies need to be incentivised to spend their own money on development. Why not?

Yes, military spending can be incredibly important for development. In some countries it is the most important thing that countries can do for development. Why is that not recognised? I am not saying it should be part of ODA necessarily, because again that is a political decision and you open the Pandora's Box, but why not recognise that?

The best way I can think about it is some kind of annual award ceremony. "This year the US enabled private citizens to give a lot of money through charities. This year France delivered a lot of military spending for security and development. Britain delivered 0.7% aid." It is those kinds of things, rather than seeing ODA as this kind of sacrosanct idea; there is actually lots more international spending required. Again, this is over the next five or 10 years, and that might be a way of responding to it.

Q20 Mr McCann: Perhaps Richard and Elizabeth can touch on the point I have made about whether Britain is in danger of being isolated. That would be useful, but the other part and final question from me would be whether there is a risk that climate finance, giving a focus on that particular issue, is going to overwhelm ODA in the coming years.

Richard Manning: Let me respond to that very briefly. First of all, it is very important that one has a much better handle on concessionality. At the moment, we are mixing apples and oranges too much, so that some countries are able to produce figures that require rather little effort from them because they are counting flows that are not really concessional because of how the OECD has chosen to do that.

The same goes for a lot of climate flows, because many of them will not be grant-type flows. As under CDM, they will be investment-type flows, so one needs to calibrate all this both according to what is the money being used for, and how concessional it is. Those two dimensions always need to be kept in mind.

Elizabeth Stuart: Implicitly and explicitly, public support is 0.7% because all three major parties stood on a platform at the last General Election that had 0.7% in as a commitment, so there has been public support for it. There are different surveys that show differing levels of support, and it depends on the questions. Sometimes when it is explained to people how the money is being spent, there is evidence of much higher support for UK aid.

It is an imperative for all of us, though, and particularly for NGOs, to be championing UK aid—that it is high quality and it is delivering. We need to be doing a better job of telling the story of what your pound does, how it is spent and how it is delivering good value for money and how it is making real change in countries. There are implicit and explicit benefits for the UK as well, so we are not just being good neighbours. There are positive externalities for the UK economy as well, and we need to keep telling that story.

Chair: There are sectors of the media that do not want to buy that story.

Jonathan Glennie: In my view, what Liz has just described is probably a mistake, and it is a mistake that has been made by charities for a long time. The danger is that all we do is become cheerleaders for aid. Aid does not always have a good impact. Certainly the recipient country public know all about the problems of aid.

I think the British public see through the NGO line on this, and I think analytically we should be much more open about aid sometimes doing a good job and sometimes doing a bad job. When we just present all the good things, one immediately just says, “Okay, but you are saying that because you are trying to sell me the thing.” We could say, “Look, most of it is really well used; a lot of it is really badly used.” When I read the *Daily Mail*¸ when I read Ian Birrell and Andrew Gilligan having a massive go, they are making some decent points. I think we should integrate that into our analysis.

Chair: Yes, they are making some decent points. In some cases, they are making completely biased, uninformed points quite deliberately.

Jonathan Glennie: That is true.

Q21 Chair: We have to deal with that. Some of the time you are forced on to the defensive because you are under an unfair attack. Other times, I think you are absolutely right. This Committee, I think, has a reputation for being constructively critical, and we have been critical and we will be critical.

The debate has to be focused on what the real impact is, not what the perceived impact is. I give the example of our report last week on food security, and indeed the one we did on women and girls. I am coming to Pauline Latham. On our food security debate, the *Daily Mail* had a front-page lead that said, “Mad MPs want to ban eating meat”. All we said was eating meat on the level that we have in the West is unsustainable for 9 billion people; we may have to think about it. A perfectly reasonable proposition to make, but you would not have thought so if you were reading the front page of the *Daily Mail.*

Fabian Hamilton: The *Daily Mail* is not reasonable.

Chair: Sorry, did you want to comment on that, Jeremy?

Q22 Jeremy Lefroy: Mr Glennie, in the 1950s the target was 1%, but it did not specify what should be official and what should be private and what should be any other source. Are you really arguing that we should go back—and I think there is an argument for it—to that more global target? Should we be saying that, for people to be raised out of poverty throughout the world, we need to have this kind of percentage of GNI from the world or from the wealthy countries, which will be a mixture of ODA, private-sector remittances and so on, and that we are not particularly bothered how that is cut?

Jonathan Glennie: No, I would not quite say we are not bothered, but I think we should recognise and incentivise good things. Incentivising remittances would be a good thing. I am not saying that should be counted in the same number. I made this suggestion to a group of African countries a few months ago. I thought they were going to say, "What a foolish idea." I was suggesting that countries like Liberia begin to contribute to international development, and the response was, "It is not such a bad idea." Politically, the message that sends is relevant for Dr McCann's question.

Mr McCann: You've promoted me.

***Jonathan Glennie*:** Oh, Mr. Sorry, yes, Mr McCann.

Chair: It can only be a matter of time.

Jonathan Glennie: If you have got countries like Liberia and Sierra Leone demonstrating that, although they are poor, they are contributing some money to global public goods, it is hopefully an easier sell in countries such as this to say, "All countries are now contributing something to global public goods. We are richer so we will pay a bit more, but it is broadly the same proportion." That is a new vision for international development finance rather than rich to poor. It is everyone contributing something according to their means.

Two more quick points: there is a danger that we are massively focused on aid. Everyone knows that aid, while being important, should probably be number 10 on the list of things that Britain needs to do to support international development. I am so pleased that taxes have become this mega campaign. It is far, far more important. Let's spend an amount of time on aid proportionate to the importance it has to poor people around the world, and that is quite limited. The other things are way more important. Let's spend time on that: climate change, taxes, regulating business—all those kinds of things.

The second idea that may or may not work is that there is quite a lot of evidence—and Charles Kenny's book last year, *Getting Better,* is quite a good one—demonstrating that research travels well. Improvements in health around the world are not necessarily down to growth; they are down to 50 years of improvements in medicine. Improvements in climate research might well save our planet, not because of aid but because solar panels get cheaper. What if we took 100 billion of the 150 billion aid budget and invested it in research? And yes, including in Britain. Would that solve some of Mr—Dr McCann's problems?

Chair: Professor McCann.

Chris White: Major.

Jonathan Glennie: British people were saying, "Why aren't you investing in Britain?" Well, it is investing research in Britain, but for international development problems.

Q23 Chair: Richard, do you want to comment on that?

Richard Manning: First of all, of course research does count as ODA, and a lot of it is financed that way, so it is already incentivised. Secondly, on Mr Lefroy's question, I would not favour a target that included commercial and private flows because they move up and down correctly in response to commercial decisions, so it is usually a meaningless target. If you look at any time series, it goes up and down like this all the time.

Jeremy Lefroy: We include CDC, which is commercial private flow.

Richard Manning: But you are including there a body that is given its resources by the state, and it is operating within that frame. Again, I do not really believe you need to incentivise remittances by this. What you do with remittances is cut the cost of doing it, and then people will do it themselves. The bit you need to incentivise is this official bit, which is otherwise hard to justify.

Q24 Pauline Latham: Last week we published our report on violence against women and girls. The issue is obviously incredibly important to DFID. What do you think are the implications for the spending of DFID because they are prioritising women and girls?

Elizabeth Stuart: Clearly, as Save the Children, it is an issue that we see as very important as well and we would favour you seeing it as a priority. It is very hard to measure impacts, so we need to do more research. So what is the metric you are looking for? That is where we need to be careful.

Richard Manning: It is a very tough issue, and a lot of it has to be done both with Governments but also very much with civil society. You are trying to make long-term societal changes here. Obviously, you can improve the framework in which that takes place, but it has to be regarded as something that is very consistently addressed for a very long period in very smart ways.

Jonathan Glennie: I agree. Again, with the rise of other donors and pressures in the international sphere, I think that the role of DFID on this will become increasingly respected and important—not just DFID but some of the, let's say, traditional donors that have made this a focus of their work. I think it is really relevant in almost all countries; when the international community is focusing on these issues, it really does make a difference.

Q25 Chair: There is a lot of cost involved in supporting civil society organisations. That is actually where the focus is. Do you see a significantly increased proportion of DFID's budget going into that? We saw in Ethiopia that the Ethiopian Government has allowed DFID to fund local groups to run effectively educational social awareness programmes, which are quite intense in terms of having to get right round the country and having quite a lot of people to mentor and lead.

Richard Manning: Potentially. Obviously, the situation is different in different countries as to what you can and cannot do. I think particularly building civil society capacity in developing countries, not just for service delivery but also for challenging and monitoring what is going on, is a hugely important part of progress in almost every country.

Chair: Thank you very much. You have thrown quite a lot of things into the pot, which will stimulate further discussion both within the Committee and with other witnesses. Thank you very much.

If on reflection there are any things that occur to you that you feel you can add into the mix, please do not hesitate to get back in touch with us; we are very happy to have any further comments or supporting evidence. Thanks to the three of you very much indeed for coming in.

Examination of Witnesses

Witnesses: **Peter Chowla**, Co-ordinator, Bretton Woods Project, **Matthew Martin**, Director, Development Finance International, and **Professor Stephany Griffith-Jones**, Columbia University, gave evidence.

Q26 Chair: Good morning, and thank you very much for being here. I think you were all in for the previous session, so you have got some flavour of what we are about. For the record, could you introduce yourselves?

Peter Chowla: I am Peter Chowla, from the Bretton Woods Project.

Professor Griffith-Jones: I am Professor Stephany Griffith-Jones. I am the Financial Markets Program Director at—sorry, it is a long title—the Initiative for Policy Dialogue at Columbia University, and I am research associate of ODI.

Matthew Martin: I am Matthew Martin, director of Development Finance International.

Q27 Chair: As you know, we are looking at the future of development assistance right across the piece. The previous discussion demonstrated it is not just about money; it is about ideas and policy priorities.

One of the things we are interested in is the actual mechanisms and instruments. I wondered if you could very briefly give us a flavour of how the world is changing. We have seen a whole mixture of different capital flows going from developed countries to developing countries. Some of it is obviously private, perhaps not always effectively monitored. On the other hand, some of it goes through very specific institutions.

I wondered if you could perhaps also tell us where you think development banks fit into that process. We really want to consider the role of development banks, and how DFID can best engage on that front. I do not know who wants to start with that.

Matthew Martin: It is a fairly rapidly changing landscape, but sometimes people exaggerate the scale of the change, particularly for the types of countries that DFID is focusing its resources on. Of course there is foreign investment, remittances and all the other things out there. If you actually look at the key countries DFID aid is intended to help, the key source of net financing, and I say that very deliberately, is concessional flows.

Why do I say “net” deliberately? There are a lot of figures out there that talk about foreign investment and forget to count in remittances, profits and dividends that come out on it, which often countries do not record very well. That takes away somewhere between two-thirds and three-quarters of the benefits to the countries in terms of foreign exchange. If one was looking within the concessional flows, again there is a diversification. If you had about 180 billion globally of those flows in 2011, about 10% of that was South–South co-operation.

I was hearing in the previous session Jonnie saying that it would be a good idea for countries like Sierra Leone and Liberia to be contributing. They already are. Every country in the world is giving some degree of co-operation to others. We work in partnership with several West African organisations that are funded out of the budgets of those poor countries, and help other countries in their region. There is about 10% of that, and that is up a lot from about 3% 10 years ago. About 15% is coming from civil society organisations and foundations.

In terms of what actually gets to Lower Income Countries’ budgets to finance their investments in reducing poverty, still about 60% to 65% of that is concessional money, whether from DAC donors or South–South. If you look at that landscape, we work with about 50 Lower Income Countries to help them work out what they prefer in terms of financing, and what will do the best in terms of impact and value for money. They say that they prefer the really good bilaterals, like DFID. They prefer the multilateral organisations for various reasons, which I am sure we will come back to later.

Then they would put the global funds, because although they have very high results, they do not engage very well with local civil society or local government. Finally, they would put things like development banks and development financing institutions in the last place. I think they would say that fairly publicly. Most recently there is a letter going to G20 Finance Ministers at the moment from all Lower Income African Countries saying, "We would like to see you give really good replenishments to IDA and the African Development Fund rather than putting money into bilateral development banks or global funds."

Professor Griffith-Jones: You broad point is of course very important; I think there is a very significant change across the world. Last week, I was speaking here at another panel about the possible emergence, for example, of a BRICs Bank. As there is a shift in economic power to the emerging powers, there are of course greater foreign exchange resources and a greater ability to fund South–South co-operation. Nevertheless, I think that the level of resources that Martin has referred to is still relatively small. As regards private flows, they are first of all very concentrated, and a big part of them are very volatile. For example, at the moment we see great enthusiasm with so-called exotic markets in Africa, but we have seen that before. Sometimes that withdraws in a very volatile and cyclical way.

The main point I am making is that aid and concessional flows still have a very important role to play, even though the landscape is changing very rapidly. One of the very interesting issues among those that you were raising in the overall questions we were sent is whether part of the grants for countries that are not so poor and vulnerable could be used as concessional loans, as a number of donors have been doing—the French, Germans, Japanese and others. This may be quite an interesting trend that it will be quite valuable for you to consider in the sense that this allows more leverage. If you have more blending, you obviously have more leverage.

There is a nice paper by Nick Stern, Amar Bhattacharya, Romani and Stiglitz that shows the scale of the needs just in infrastructure and climate mitigation. It is massive across the developing world. If you need more financing to support the growth of this actually happening in developing countries, aid on its own may not be big enough—particularly in the context of some developed countries cutting back aid. The UK, of course, is an honourable exception, as you discussed earlier.

There is this idea that you could do more with less, but they have to be there. Another advantage is the issue of moral hazard, in the sense that if you have to pay it back, even if it is at very low interest rates and very long maturities, I think there is some kind of incentive to spend the money better. I would not push that argument too far, but I think it is important.

Of course there are risks. One risk is the avoidance of future debt crises. The second risk is to continue funding concessionally very poor countries and activities where social benefits are much higher than commercial returns, such as climate adaptation and so on. If you take care of that, for example by having mechanisms like the French have, which are interesting—the counter-cyclical lending of the Agence Française de Développement, which gives debt holidays in years when countries are hit by shocks—that could facilitate protecting countries from having costly debt crises, and protect donors from having to deal with that. I think that is also a shift that is occurring, this shift towards the possibility of blending. I understand that may be something you are considering.

Q28 Chair: Peter Chowla, perhaps I might ask you to comment. In a way, Matthew Martin, when you said what they prefer, they would say that, wouldn't they? If you say to somebody, "Would you like us to give you money or would you like us to lend you money?" I do not think it is much of a choice. Surely the point Professor Griffith-Jones is making is it actually might give you more options and more flexibility and extend the money. I think that is what we are trying to tease out.

I have no doubt at all that people like grants, but I think the question we are wanting to establish is whether DFID is inhibited by the fact that it only gives grants other than funding multinationals. Of course, 60% of its money goes through those, so indirectly DFID is of course giving loans, but not loans that are directly administered by it. So I do not know whether Peter Chowla would like to comment on that.

Matthew Martin: I was not commenting on grants and loans. I am sure we will get to that later, and I have got quite a lot to say about that. I was commenting on institutions—what types of institutions they feel produce the best results and work best on the ground.

Chair: All right, but there was a connection between the way they deliver it.

Matthew Martin: No, I am in favour of concessional loans, but we will come back to that, I am sure.

Peter Chowla: I think it is very important also to think about the orders of magnitude we are talking about in terms of resources available for development. So while private flows have been increasing dramatically, and Stephany has talked about some of those, we also have to remember that domestic resources are always much bigger than anything that is available, and the more we can do to benefit countries able to garner and generate more domestic resources, the better off they are going to be.

I think you heard a bit of that this session when Jonnie talked about tax revenue being a key driver of how countries can invest. I think that is quite important, because if you look down through the list of different kinds of international cross-border flows, you are talking of the order of 20% to 30% of GDP in terms of domestic revenue and going down to a couple of per cent when you talk about aid or private borrowing or overseas investment, FDI. So those things are quite small.

Coming on to how that works in development banking, it is important to also recognise that development banks have started to change quite drastically in the last 10 years, moving towards greater emphasis on private-sector investment and private-sector flows. We are not clear that that has always been well borne out by the evidence as delivering good value for money or effective development results. So whereas the World Bank had only about 10% of its resources working on private-sector investment where it did the most work about 10 to 15 years ago, it now has a full third of its resources working on private-sector investment, roughly speaking; it is about a third of the total. You will see the same trends happening in the African Development Bank, less so, as well as the Asian Development Bank and Inter-America Development Bank. You will see some of the same efforts moving in towards more private-sector investment.

At the same time, you have also seen more resources moving in towards financial deepening, which is the word they use to describe investment in the financial sector of developing countries, or of financial-sector investments related to developing countries, rather than in projects. An important trend to recognise is that, as we move towards this, we have less information about value for money and development impact. That is one of the important things to think about as we think about development banking models, how they are changing themselves, and whether they are going in the right direction, which is the point that Jonathan Glennie made in the first session about matching the type of resources to the type of investment you want.

Aid money has a particular usefulness because of its public nature. Development banking money, which might be in the private sector, has a different usefulness, and might need to focus on different sectors or different kinds of outputs or investments and outcomes. Public-sector concessional loans from multilaterals or from bilateral agencies, which are debt creating in nature, also need to think very carefully about what they are being invested in, so that we are not putting them all in a pot together and saying, "Well, there is this massive pot of money, and now let's use it." They need to be carefully and strategically used for different kinds of things because of the debt-creating nature of them, the governance arrangements over how they are controlled, and potentially the purposes and strings that might be tied to them.

Q29 Jeremy Lefroy: One of the reasons why we are asking this question about development banks and development finance is that on our visits we have increasingly seen that as DFID, quite rightly in my view, concentrates more on the private sector than it has in the past, which in the past has been very limited, we are seeing money go into things that could be repaid, and yet are not being repaid. If they are repaid, it is then just left in the country.

We saw an example with Pakistan, where there were guarantees that we thought were very good for small and medium businesses, but once the guarantee has been used or not used, that money, in our view, should have been returned, but was not returned. There was no particular instrument for DFID to use. At the moment, if you take the World Bank as a comparison, DFID has its equivalent of the IDA, which is DFID itself, and it has the equivalent of the IFC, which is CDC, but it does not have the equivalent of the IBRD.

We have wondered why that was the case, and whether indeed we should be considering that, as I say, particularly because of the emphasis of DFID in the private sector, and that includes clearly agriculture, particularly small-scale agriculture. The question is: do you believe that DFID does have the right mix of bilateral financial instruments at the moment, or do you think it should be expanded? Given that DFID is widely recognised as doing what it does very well, that would to some extent also enable it to set an example in terms of how a good development bank could operate.

Professor Griffith-Jones: Just a point of clarification: my understanding is that DFID does not really have its own IDA, because it does not lend in concessionary terms.

Jeremy Lefroy: I understand that, but it just makes grants.

Professor Griffith-Jones: Exactly. So one of the first discussions is whether you want to precisely expand the functions of DFID to also finance highly concessional loans to relatively poor countries to, as you point out, go into profitable projects where the money is there to be paid back.

I would say in principle that that could be a good idea—also because the reflows then of the money, even though the maturities are long term and so on, would contribute to greater availability, and you could scale up the contribution. Generally, if you ask developing countries, they will say, "Yes, we want more money and we do not want to reduce grants and reduce concessionality," but on balance I get a feeling that developing country Governments increasingly want scaling up of flows for things like infrastructure. So I would have thought that that expansion of DFID, which as I said has been done by the Germans, the French, the Japanese, the Spanish and others, would strengthen the battery of instruments.

One area that we discussed informally yesterday with Matthew Martin is how it should be done in a very cost-effective way, to the extent that DFID could also, for example, co-finance loans with institutions like the regional development banks, the African Development Bank and others, or indeed with other donors or lenders, like the European Investment Bank, which I have studied quite a lot and seems to work quite well, and KfW, which also seems to have a good record.

In fact, KfW, Agence Française de Développement and EIB have an informal consortium where each one takes a lead in particular projects, and that is a model that could perhaps be replicated with DFID joining them. If DFID is interested in particular countries or sectors, it can take the lead, getting co-financing from the other countries to avoid excessive transaction costs, but putting a particular mark from its development perspective and the perspective of the developing country in the way it channels the flows. This is an advantage over just giving the money through the World Bank or other multilateral channels.

Overall, it is a good issue to think about, taking the precautions of avoiding future debt crises and taking away funds from important projects, which may require grants or a highly concessional loan. I think there is a third level, where you could then, as for example KfW does, make almost market loans to Middle Income Countries or very advanced LMICs, but that is a bit different.

Peter Chowla: I might leave some of the questions around debt sustainability to Matthew, because I am sure he is more expert in those questions than I am. However, I understand that has to be a key element, because though we have committed a lot of money to debt relief through the MDRI process in the UK, it is not clear that many countries have emerged from debt overhangs.

There is a wide variety of countries, and one of the most important criticisms that civil society has had is that the Debt Sustainability Framework, which is what the World Bank and IMF use to determine what type of concessionality to use, has not been as effective as it should be in terms of monitoring private sector debt, which has an impact on the potential for financial crisis, or for dealing with the questions around social needs—whether countries have sufficient levels of resources to invest in education, health, job creation or anything else that they want to invest in. So there is some worry about the Debt Sustainability Framework and, as I said, I think Matthew is a bit more expert in that than I am, but that has to be a key element of it.

Secondly, you mentioned that DFID could potentially be a good model of how a development bank would work. It is important to recognise that, to do development banking well, there is a lot of infrastructure that would have to be built around that—an incredible amount. As you will see from some of the civil society work that we have referenced in our written submission, the supposed expert institutions in this that we work on—for example, the European Investment Bank, the IFC, the World Bank—have not yet got there in terms of the internal institutions they need to do this well, in terms of measuring development impact effectively, doing results, doing independent evaluations and accountability mechanisms, and social and environmental safeguards.

In all those areas, there is still much work to be done; these are institutions that have been doing it for 30, 40, 50 years and still have not cracked the right model. So I am very, very wary about setting up new institutions thinking that the UK could become a model provider so quickly, because it is really complex, particularly where you are doing things like private-sector work or project work on the ground and you are doing loans for these things.

The social and environmental safeguards are really complex and the need to have people on the ground to monitor, supervise, course-correct and take feedback, and even project design at the very beginning, is very intensive. My understanding is that, so far, the perspective from secretaries of state both in the previous Government and this one has been to try to reduce DFID's overheads and administrative footprint, if you will, in terms of number of staff.

Q30 Jeremy Lefroy: Can I just come back to you on that? That is not the case. On the projects, the DFID staff have increased greatly, and the ones they have recruited have a lot of those skills that you have just been describing as necessary. So I would say that it is a very good value-added use of these people that they have those skills already, the ones who DFID has been recruiting, so you would not need vastly to increase the infrastructure.

Peter Chowla: To scale up the amount of resources you provide in this way, you will have to scale the number of staff commensurately, and I think currently DFID staff is probably not at the level where you could provide large levels of resources on borrowing terms with this level of assessment and supervision of projects. It is about the scale.

Professor Griffith-Jones: I think that Peter has made some really good points, but you could, for example, work very closely, where they exist, with national development banks or local Governments. Therefore, you can start reinforcing their capacity. Also, you can work, as I mentioned before, with existing institutions like the World Bank or, even better maybe, the regional development banks, where there is a lot of expertise, and you have your own expertise as well.

So I do not think that the resources have to be so burdensome. Also, I have been at meetings with developing countries, and a person who is still a minister in India said, "What we value most from the World Bank is not the money but the engineers and the technical expertise, which we transfer." In that sense, the UK and DFID could do that well.

Matthew Martin: There are two different questions here. One is what we think about concessional loans, and the other is whether that means we need a development bank. On the concessional loans, I think most countries would be relatively happy if DFID were in a position to offer them. They are already borrowing quite a lot of concessional loans and, indeed, being pushed to fund infrastructure and so on into much more expensive loans. You will have noticed some of them are borrowing on bond markets; some of them are doing off-budget PFI deals in very much the rather regrettable, extremely high-cost way that we have sometimes done in the past here.

So I think the alternative of having lower cost concessional loans would probably be very welcome to them, provided of course that we do not make a profit out of this. As was mentioned in the previous session, some others are already lending at more than their cost of borrowing. It seems to me a bit usurious if you are going to start lending at 2% or 3%, so we would need to keep it pretty concessional at 1% interest or less.

On what we would need to do to have safeguards, clearly we would need to have not just the World Bank and IMF Debt Sustainability Framework and a very low risk of countries having a debt crisis in future, but our own assessment within DFID of whether the country would be able to afford to repay. Focus those loans on high-return projects, so that would mean really transformative infrastructure projects where we could see that that was going to have a high impact on growth and development. Focus above all on public-sector projects, because that is where the real funding gap is.

On the capacity issue, it seems to me that you could rely a lot on other institutions' capacity and you could develop a certain amount of capacity yourself to assess project returns and work with local Governments. It would also be important that DFID developed the capacity to do the creditworthiness assessments and also probably provided more support for debt-management capacity in those countries that are receiving the money, which they have pretty much abolished in recent years. If you are going to start lending, it seems to me we should be helping countries to be responsible borrowers as well.

That does not mean that we should then move into establishing a development bank. For me, the really good model for all of this is something like AFD. I know that officially under French law that is a bank, because it has to be, but what it is is an executing agency for French Government development policy, grants and loans and, indeed, equity. It does not set up a separate institution. It does not have all the risks and some of the negatives that have been seen over the years in places like JBIC, which is why the Japanese Government merged the Japan Bank for International Co-operation back into JICA.

There are all the risks of fragmentation, of donor-driven projects, of informal tie-in, where the relationship between the private sector and the contractors and the development bank is so close that always the British contractors, in this case, would find out about things before anybody else and there would sort of be a tie-in and, therefore, a very severe risk of reduction in value for money and increase of costs. So there are all kinds of real disadvantages to setting up another institution. Above all, in a situation where we have budget constraints and we are having our bonfire of quangos and trying not to set up more independent institutions, the idea that DFID, when there is already the degree of public controversy there is about the aid budget, would be in the process of setting up a whole new institution would seem really likely to undermine public support for development assistance in this country.

For me, you could have something that I would call a "virtual" bank, where you would say, "DFID will now lend money for the countries that can afford it and for high-return projects," but keep it within the programming and planning framework of DFID. The goal would be poverty reduction, funding the private sector, making sure it is untied and focusing on DFID's key countries, and bringing in the idea that you would then co-finance, so you would need less investment and a huge amount of extra staff capacity and overheads within DFID. That would seem to me to be an ideal midway solution that one could adopt.

Professor Griffith-Jones: There is one thing that I think we may need to bring in. I broadly agree with what Matthew has said in the current context, but one interesting thing is that, for example, the Labour Party is talking about a British investment bank and a national development bank for the UK. Indeed, this Government has a Green Bank and so on. So one could think that, if you had a significant development bank for UK purposes, as the EU has with the EIB or Germany has with the KfW—I am not sure we are going with exactly that model, because that is not exactly the tradition, but there may be some trend towards that—there may be a case that within that there would be a lot of synergies and spill-over effects towards doing something similar for developing countries.

I am talking about this more in the medium term as this Green Bank evolves or as a British investment bank is created. Then there could be a part of that—say, 10%—that would focus on lending to developing countries. Obviously, it would have the disadvantage, as the EIB lending to developing countries has, for example, that there is not enough focus on development, but it would have the big advantage of having all these trained engineers and people who work in the same sectors.

Chair: We have a series of questions that are about how a bank might work.

Pauline Latham: My questions have been answered.

Chair: You are satisfied with the answers given. We understand DFID is considering whether or not it should establish a bank, so I am going to ask other colleagues whether they want to pursue the questions just to establish, if it did, what it could or could not do.

Q31 Fiona Bruce: I am very interested, Matthew, in hearing you talk a little bit more about the French model, because on one of our visits to France we did talk with a representative from the French bank and were very interested. If I am right, that is their exclusive route for aid, apart from private-sector donation. Am I right? How would that work if we had one working in parallel with DFID's other aid delivery?

Matthew Martin: The answer is it would be best not to have one working in parallel with DFID's aid delivery. The last thing you want and the negative experience of JBIC as well as KfW from the point of view of recipient countries—and, indeed, that is why the previous German Government spent about 10 years trying to merge the three different institutions they have—is that when you are on the ground in a developing country, you have a massive amount of fragmentation.

I have seen this recently in the last few years in relation to German and Japanese aid in quite a few countries, where you effectively have a Government talking with two different voices, with different priorities, with different things that they are telling you. Frankly, you are never really sure, as a developing country Government, whom you are dealing with. You have one lot of people telling you, "Infrastructure is our top priority," and another lot telling you, "Poverty reduction is our top priority," to caricature it slightly. You are never quite sure whom you are talking to and how to really get an effective dialogue with the Government, so I think it would undermine Britain's credibility and leverage in dialogue to have two separate institutions.

Why I was saying that AFD is a positive experience is essentially that it is the implementing arm of all French aid. It is a bit like Swedish SIDA or Canadian CIDA, until it was abolished recently, where you have the ministries taking the political decisions about what they would like—so the Ministry of Foreign Affairs, the Ministry of Finance in France—and you have an implementing agency, and it does grants, it does loans and it does equities. My view would be that, if you were going to do this, you could do it within DFID. You could have some kind of unit whose responsibility it was to say, "We will assess creditworthiness and we will work out the return on the projects, make sure that it is a good idea to lend in this case, and organise the co-financing with the other organisations."

The other really bad thing is it is not just about policy and dialogue; if you have two different organisations, you risk having to do lots of procedures, and that can really complicate everything. You are never quite sure why the delay is happening, who is really responsible for the project not delivering its impact, apart from all the issues Peter raised about accountability and results and so on, which a lot of those development banks do not have a great record on.

For me, the reason I raise the AFD model is it is not about splitting it. It is about bringing those loan opportunities into the existing development institution.

Q32 Fiona Bruce: So if we were going to go down this route and build the capacity within DFID, what kind of recruitment would we need to undertake?

Matthew Martin: I do not think you would need a lot. I would like to think that DFID would want to focus on some pretty large transformative projects where you could really have the extra impact in the money that you could use in a development bank. It would be, for example, in multi-country regional infrastructure projects that would connect up the whole of Africa and make intra-African trade much greater, or in power projects or in telecoms projects that would bring IT to everybody. There are lots of those really big projects that you could join in.

The projects exist. You often hear that there are no bankable projects out there, but there are a lot of bankable projects out there. The two problems are that people have problems preparing them and they do it very slowly, so if DFID were in a position to be co-financing these other organisations, it would give them a chance to have leverage over them and really kick them to move faster in terms of preparing things and getting things done.

The other one is the problem that, as DFID, you might not have specific skills in infrastructure. I already knew a bit, but I am very glad to hear that DFID has been recruiting people on the infrastructure side, because that is important. However, I do not think you would need to have massive numbers of additional bodies in DFID, because you could say, "We just need to be sure that we are happy with this." So a few extra skills on the debt management side, on the creditworthiness assessment side and on the infrastructure side, and then you could say, "To some degree we will rely on these other organisations, but we will still have the choice to say no to a particular country or a particular project if we do not want to fund that for our own bilateral reasons."

Q33 Fiona Bruce: One of the advantages that I perceived was, effectively, you were circulating this money. You were lending it many times over, when it was recovered, and that was a really exciting alternative to our current approach.

Matthew Martin: That is true, and particularly if you did not, over the long term, use that as an excuse for reducing the new flows, but you would be getting it back and be able to build on the new flows. Effectively, what would then happen is that your 0.7% growing over time with GDP could probably be financed or partly financed by the reflows from those loans.

Q34 Fiona Bruce: Do you not think the administrative burden then on the recipient countries would be that much greater, because those projects are already, by and large, going to happen?

Matthew Martin: Yes, they already have debt-management systems. As I said, some additional investment by DFID in supporting that debt-management capacity would be helpful to some of them, but they all have debt-management systems. They all have projects that they are already doing with other organisations, so I think it would be a question of DFID fitting into that additional structure. Provided you did not have the two parallel organisations, which would create an additional administrative burden at the other end, it would work very well.

Q35 Richard Burden: In the various models we have been talking about and you have been talking about today, where would CDC fit into the picture, if anywhere?

Peter Chowla: I might come back on one point that stems from something Matthew said about the regional transformative projects. There has been a lot of concern among some civil society actors about how these are prepared and what they are aimed at. It comes to some of this question about what role the private sector plays in how these projects are being designed and delivered.

A lot of the worry about some of projects that are being developed is that they tend to be more about extraction of resources or export-oriented models without dealing with the internal development of markets in Africa, like Matthew talked about. I think that is an important distinction. Whether projects are considered pro-poor and dealing with job creation prospects for giving decent work, as they talked about in the morning, or whether they are oriented towards export infrastructure is an important distinction. One of the things that we think is very important is how you engage with recipient priorities, both recipient Governments and the ultimate beneficiaries, who are the people of these countries. We have particularly had worries about the ability to take in beneficiary feedback or priorities for infrastructure development.

That comes to the CDC question, because the CDC largely invests through private equity funds—well, previously only through private equity funds, and now still predominantly through private equity funds—in emerging markets. We have a lot of questions about the development impact of that and the ability of that model of lending to really reflect the priorities of poor people or their needs in terms of infrastructure or other kinds of projects.

DFID did a CDC review a few years ago. We have a new model as of about a year ago. The jury is still out on whether the CDC is effective in terms of implementing this new model and whether this brings it far enough. As I alluded to earlier, we have had a lot of evidence that development impact is not well measured in the private sector. The more that private-sector projects can be driven by the priorities of the Governments in recipient countries and by beneficiaries or people, the ultimate beneficiaries, rather than profit-oriented interests, the more likely we are to see that those projects have good development outcomes.

We have been quite critical of the commercial orientation of a lot of development finance and the seeking of very high levels of return, above what you would expect from domestic investment in a rich country. For a few years, the IFC was making 20% to 30% returns on equity. That sounds fabulous if you are a private investor, but does not sound very good if your purpose is the real transfer of resources from rich countries to poor countries. When you are taking 20% to 30% back every year, after three or four years you have now taken out more than you may have put in. That is not a particularly helpful perspective when what you are aiming for is the real transfer of resources from rich countries to poor countries.

I am not clear about reforming CDC again as a separate, stand-alone institution or trying to bring it into DFID. I think it is quite clear that the model CDC has followed for the last 10 years has not been effective in delivering development results.

Chair: The Government has tried to change it or is in the process of trying to change it.

Peter Chowla: It has, yes, and as I said I think the jury is still out on whether those changes have gone far enough and are effective, and I do not think we know enough yet; it has been too soon. As future development co-operation agendas are set, it is important to look at that again to see whether this reform has been enough. We are quite sceptical of the model the CDC uses, and especially having it as a stand-alone institution, without the mandate, oversight and supervision that might come with being within DFID, makes it even harder to ensure that it is effective as a development outcome provider.

Q36 Richard Burden: If there were a virtual bank, the way you have been talking about that, there are two questions. First of all, what would the relationship be, if at all, between CDC and that virtual bank or would that just be separate, whether reformed or not? The second thing is, if there were a virtual bank, I am still trying to get my head around what it would do. I can see that it could be the executive arm, say, for implementing DFID's programmes, but if it was a virtual bank as opposed to just a virtual executive arm, could it borrow money itself on the market?

Professor Griffith-Jones: I was thinking about that. If you are lending to Middle Income Countries, yes, it could borrow money, because then it could borrow more cheaply, like the EIB or the African Development Bank does. Then it would transfer that cheapness to developing countries. However, if it is to lower income or even lower middle income countries, I think the subsidy element is very important, because you really want very low interest rates and long maturities, and you will not get that on the market.

You may do some different kinds of blending, but I think there would be a very significant contribution precisely from the grants. I do not know if you can separate the financial engineering. In your next session you will have people from KfW and they could maybe discuss it. I tried to talk to them, but it was not very clear from the material they sent me whether they raise money in the market for financing these very subsidised loans.

Chair: The French Bank does, I think.

Jeremy Lefroy: The AFD does.

Matthew Martin: Yes, exactly. The AFD does as well. I would probably say that, ultimately, if CDC is about development and not just purely a private equity fund with a little bit of Government capital, it should probably be brought back into DFID as a private-sector wing, if you like. What they do in AFD is have a thing called PROPARCO, which basically does all of their private sector financing through a combination of quite expensive loans and equity financing. They have other equity funds as well, the details of which I will not bore you with.

So I think you could quite easily envisage CDC continuing to be an equity provider. The fundamental reform that has been made in recent years is CDC does not give loans, because they were not very good at them and were quite a major contributor to the debt crisis that we saw before. So I would say CDC's relationship with a virtual bank would be different, because why have a virtual bank?

Essentially, you want to fund public-sector, high-return projects in developing countries, notably infrastructure projects but maybe some productive support ones as well. You also want to be sure that you have a unit at least where you are able to keep a very close eye on whether countries will be able to repay and what the likely return of the project is going to be. That is why you have a virtual bank rather than just do it through DFID regional departments at the moment—to have some kind of unit where you can do that.

On Stephany's point about the British investment bank and Middle Income Countries, it might well be that, if we ever got to the stage where we had a really well functioning Green Bank, British investment bank, we might want to consider letting that institution invest or lend to Middle Income Countries on commercial terms.

However, I do not think we should mix that up with giving concessional loans for probably lower return projects in Lower Income Countries, which is DFID's function. It may well be that that British investment bank could make some very good returns in China and South Africa and other places where it might want to invest to help develop green technology and so on, but that would not seem to me to be something where you would want to use subsidised UK resources. I would separate the two.

Professor Griffith-Jones: There are, for example, experiences like Norfund in renewable energy that I have been studying a little bit, and they seem to do quite well. They argue that they get commercial returns; it is not as high as Peter is saying, rightly, 25% or 30%, but they say that on average they make about 13% a year for investment in renewable energy in relatively poor countries—in Central America, but also in sub-Saharan Africa.

I found that very interesting, because when I talk to a lot of the private pension funds and insurance companies about investing in renewables, they first say to me how much they would love to do it, but then they say, exactly as Peter said, "We want 25% or 30% return. We are not getting that, and because it is so risky, we are not going to do it." The people at Norfund said, "No, no, we can handle the risks in Africa," and they were very businesslike about doing it, and they seem to be quite effective. If you have that kind of spirit, I think that might work rather well, but that is a little bit further down the line.

Peter Chowla: Can I make one further point? Peter and Stephany have brought out the issue of blending. Part of the idea is that you might take public resources, grant resources, aid resources and blend these with commercial loans from the private sector. This needs to be done very carefully, because, number one, you put yourself at risk of subsidising corporate profits. They already have access to finance. We have seen this a lot with the IFC investing in Marriott Hotels and Coca-Cola bottling plants. The parent companies have plenty of resources. We do not need to use development resources for these things, so we need much more careful assessment of the development and financial additionality of some of these things.

It is very clear that you would have to try to build in a very important factor for social benefit—public goods, if you will—if you are going to use public resources to invest concessionally in the private sector. You would not want to put in your public resources for any old business opportunity. That is not the point of some of our aid resources, which are limited. You would want to use these much more clearly for things that might have a lower commercial return or potentially no commercial return, but have public benefits associated with them.

Things like renewable energy are exactly the kind of example of where, right now, we are facing a need for climate change mitigation; you might consider there are broader social benefits that might be subsidised in that effect, but you have to be very careful. You talked in the first session about the *Daily Mail*; imagine it getting hold of stories about subsidies for corporate welfare for executives who get paid £1 million and fly around in private jets. That is not going to look very good either, so you have to be very careful about how you do those sorts of things.

Chris White: That is not new.

Peter Chowla: More of them I suppose is what I mean.

Q37 Mr McCann: Can I ask you a couple of questions about the relationship between multilateral and bilateral aid? DFID is routinely praised for being a world leader in the international development field, yet they give 60% of their budget away to multilaterals. Therefore, if six-tenths of the budget is going to multilaterals, the argument could be that we are very, very good at giving our money away.

The one thing that has always perplexed me is, if we are the only major nation in the world that is going to reach 0.7%, we are in a situation where the Government is artificially trying to hold back administration costs on its core budget but yet seems quite content and happy to authorise administration costs of nearly 5% in the EU, 8% in the World Bank and possibly even more than that in other multilateral organisations.

My question is: do we have the right balance between bilateral and multilateral aid? We have had answers in the past about economies of scale and why multilaterals operate in areas where we do not, but are you saying that multilateral aid is a good model? Do you believe it is working well on the ground?

Peter Chowla: Multilateral aid has its benefits and its detractions. We have to be very clear there is no silver bullet, and I think you heard some of that this morning. When you come at it from the aid effectiveness agenda, so when you look at the issues of donor harmonisation and fragmentation, it is quite clear that putting more money through multilaterals would be better, because you will have fewer donors for recipient countries to negotiate with.

However, at the same time, you will also then empower a certain institution in a negotiation with a recipient country, and whether that institution is working effectively then becomes very, very important, if you are talking about the African Development Bank or the World Bank or any of the other regional development banks. By putting money through multilaterals you amplify the power of that multilateral and its potential faults, as they were. Some of the paper that Jonathan Glennie referenced, *The Age of Choice*, talked about how competition of some type between different providers of resources can help recipient countries in their negotiating positions to get resources that have the maximum benefit for their citizens, if they are well organised and strategic about how they do that. That is a big "if". That is about good governance states in recipient countries that are effectively maximising the use of those resources.

We have been quite critical of multilateral institutions. We think there is lots of room for improvement. We have the luxury of doing that in the UK because DFID is such a very good provider of aid on its bilateral programmes. For me, it is very easy to be critical of multilaterals, where our option is quite good; DFID is quite a high performing aid-giver. It is much harder for our colleagues in other countries around Europe to make that argument, because they know that their bilateral resources are not flowing in the most effective way. So there always has to be a trade-off, and which is going to be the most effective needs to be assessed in every situation.

One thing the UK can do is work much harder to make the multilaterals more effective. There has been a lot of great work done from the UK and it has been a leader in pushing multilaterals on things like gender, fragile states, and the results agenda. Those are very welcome improvements in the multilaterals that DFID is largely responsible for, as the leading agency asking for those things. Where it can do a lot more is on the independent evaluation and accountability front. This is where I think a lot of the multilaterals are still falling down in terms of learning from mistakes, taking on board lessons from evaluation, not being defensive about failures, and ensuring greater accountability to the beneficiaries of projects or programmes in developing countries where citizens have a complaint about how things have operated.

I think DFID could do more in pushing those things and governance reform at the World Bank and the other multilaterals to ensure that multilateral resources are more effectively used, not only DFID's own but those of others.

Professor Griffith-Jones: I think this is very important to increase the effectiveness of the multilaterals, but it must not be done by being too intrusive and intervening all the time at every step, particularly in adding all these things—what we used to call "Christmas tree conditionality" in the 1980s. It is important to listen a lot to what the developing countries are saying.

I found it interesting that Matthew was saying that African developing countries like the World Bank and the African Development Bank more than others. I think it is very important not to add too many conditions, even if it is done with the best of intentions, and to listen a lot to the developing country Governments—and, indeed, also to the direct beneficiaries, as Peter said. That is quite a tricky thing to do, because the idea is always to try to micromanage things, and I think that may be dangerous, even though done with the best intentions.

The philosophy of strengthening the multilateral system is a good one, which has been the British approach. I think overall it is a good one. There have been problems with excessive conditionality and so on of the Bretton Woods institutions, but there is a natural answer to that in the emergence of these new donors and these new development institutions, like the Chinese, the Brazilians and others, and the possible BRICs bank. This comes back again to your initial question, Mr Chair, of the changing architecture as the flows are rapidly changing. That is something that should be kept in mind as you are designing the new architecture for the UK.

Q38 Mr McCann: With the greatest respect, our job as a Committee is to scrutinise the work of DFID and to make sure we are getting value for money for the British taxpayer. Peter makes the point that multilaterals fall down in certain areas. Therefore, you cannot just say that there is a recognition that they fall down in certain areas and then do nothing about it. Surely there has to be a conclusion reached.

If certain multilaterals are not delivering what we want them to deliver, and if we are seen as being a good bilateral deliverer ourselves, why wouldn't we, for example, ramp up the programme in Ethiopia to deliver on our plans there about violence against women and girls? Why wouldn't we do that—divert money from the multilaterals and put it back into our bilateral programme, where we believe we can get more value for money? Would that lead you to the conclusion that the balance between bilateral and multilateral should change? You cannot recognise that there is a problem with some, but then not propose a solution.

Matthew Martin: Just to come back to what I said at the beginning, there are some very strong reasons why people on the ground see multilaterals as being preferable not, I would say, to DFID bilateral money but, for example, to some of the other rather less well performing bilateral development banks and so on. Those have to do with them genuinely aligning with the country's own development priorities and making sure that there is national-level ownership.

For example, particularly the African Development Bank has been decentralising to country level, so that it can be closer to the local recipients, and that has been very much appreciated. So there are a lot of reasons why the multilaterals are preferred, and they also came in, notably in the case of the African Development Bank, very quickly to help with the impact of the global economic crisis when it first hit countries.

From a DFID point of view, what they offer is the possibility for wider reach, because they can fund countries that DFID has no intention of setting up country programmes in. In recent years, when we have reduced the number of countries that we have put money in, we have said to Burundi or Latin America, or whatever it may be, that we will now channel money to them via the multilaterals, so there is a reasonably strong case for that.

What I would urge you to do, as a Committee, is to look much more closely at the administrative cost issue, because I think the multilaterals are much more honest and transparent about the level of their administrative costs than some bilaterals are. They do not eliminate the administrative costs relating to country programmes or to individual projects and put them down as country projects or country programme costs. So you might want to ask the multilaterals to report their admin costs on that basis, broken down into different types of admin. Then you would see that they come much closer to the levels of admin costs that bodies like DFID have, or at least the more effective ones do. I entirely agree that, if they are ineffective, you should not be giving them money, and I was glad to see that you eliminated money to a few in the last Multilateral Aid Review.

Just on this issue of how you influence the multilaterals, because I think that is really important, there is no doubt that DFID has been punching above its weight, partly because it has been increasing the amount that it gives to these organisations, and has achieved a huge amount in changing the way they behave. There is a lot more still to do, but giving the money gives you the power to do that.

I am not necessarily convinced that we would need to carry on increasing the share of multilaterals. I think 50/50 would be a perfectly reasonable balance. One of the things that Stephany mentioned when we were talking briefly about this yesterday was co-financing the projects that we were talking about earlier on in terms of infrastructure. That would still give you the leverage, and it would give you the option to say to the World Bank or the African Development Bank, "We are not going to fund this particular project, because we think it is rubbish," or "we do not like the Government" or "we think you have taken too long to design it" or "it does not have the returns we want".

This sounds an awful cliché, but I think you need to treat them mean to keep them keen. You need to basically say, "We would like to carry on supporting you, but we would like to give you money in a co-financing format and for particular projects where we think you have been doing a really good job." That would help, as well as continuing to give a major core contribution to them, to encourage them to do better, but I think co-financing would help.

Q39 Chair: Can I pick up on that, because I have a couple of questions and we are three-quarters of the way there? It has been said to us that DFID gives 40% to core funding and about 20% effectively in partnership—exactly the kind of co-financing we do. Is there scope for them to do more in that context?

One thing I am interested in exploring is, for example, having regional offices that could do bilateral programming outside the bilateral programmes, where appropriate. One of the points that have been made to us is that we are quite effective at knowing what the World Bank is doing in those countries where we are partnering them bilaterally. We are much less effective in knowing what they are doing with our money where we are not.

Perhaps having a regional office, say, in South America or an Africa office or a South Asia office that specifically has a small capacity to engage bilaterally with the World Bank or the Asian Development Bank or the African Development Bank on agreed projects in that context can increase the accountability. What you were suggesting, Matthew, seemed to me to imply that that might be a way to go.

Matthew Martin: Partly. I am sure the others will want to talk about this, but there is one thing I would say. That sounds like a very good idea, but I would really strongly urge you to think about something that allows DFID to get the money out quickly and to have the maximum impact with the least administrative cost.

Quite a lot of that 20% is currently trust funds and separate earmarked trust funds for multilaterals, which typically have 20% overheads taken off them immediately and also need a lot of admin time for DFID and for the multilateral concerned; they are a terrible idea. So what I am not suggesting is that we should go around creating more trust funds.

Chair: I meant joint project funding.

Matthew Martin: Joint project funding—yes, exactly, for the type of projects we were talking about earlier and for the loans.

Professor Griffith-Jones: I think the regional office idea is a very good one, having people on the ground, and also making sure that the World Bank listens. I remember I was on a mission in Eastern Europe and we had a meeting with the same minister about the same sector, and there were World Bank representatives waiting; I was representing the UK. He said, "Why don't we merge the meeting?" and they said, "No, because we are the World Bank."

That kind of attitude has to change, and in that sense you are both right to say that you need more accountability, but having more presence would be very necessary. We are talking about a virtual bank and all that, but if you are disbursing money in loans, it would be good to have some more engineering skills in the projects. If you are going to be doing, say, regional infrastructure, you will need more, and you can have people in the countries or in the regions, plus you work even more closely with local Governments, local development banks, where you are using more the local expertise and not relying just on the World Bank, the EIB and so on.

Peter Chowla: A key addition to that is further internal accountability and transparency within the World Bank. Where DFID has regional offices, that is great and can help, but the more the World Bank can internally do its own independent evaluations, much like we have ICAI here, and to do them more publicly and more transparently, the more that will help DFID know what is happening to its money.

Chair: That is fair enough.

Q40 Jeremy Lefroy: With other countries reducing their ODA quite substantially, what you are getting is an increasing pressure on the UK to increase its contributions to multilateral organisations. For instance, the Global Fund wants the UK to put up its contribution quite substantially. IDA has its replenishment coming up in 2014 to 2016. The UK has traditionally been one of the highest donors—either the first or, in the current round, the second largest.

It seems to me that, because these organisations see DFID's budget as, indeed, increasing this year and then stable, it is often the country that they are coming to almost first for that. I see that as a real problem. Do you think DFID should be much tougher on them and say, "We will not increase unless we see other countries increasing. We are not prepared to make up the gap. You may say you need €21 billion in the next IDA round, but frankly, other people need to step up to the plate. We are not going to fill the gap"?

Professor Griffith-Jones: It is a very difficult question. One interesting issue there is whether the decreases in aid of the other donors are temporary, hopefully, or permanent. To take one example, the Spanish had been increasing aid quite significantly and then they have just slashed it now because of the crisis. This is understandable because of the depth of the crisis in that country, but I do not know, if the crisis were to be resolved relatively soon, whether they would then recover a certain level of growth, although perhaps less than now.

If it became a permanent trend, I think you are super right that you cannot continue to carry the entire burden. If it was a bit more temporary, perhaps you would be more willing, up to a point, obviously, to do that. I am not sure. In the World Bank I have been arguing very strongly for increasing the voice of developing countries on the boards. One way of doing that is also from the financial perspective, because if you do that, you would get money from the Chinese, the Brazilians and a lot of the Asians. There is a source of money there that particularly certain countries, not necessarily the UK, do not want to give up, so that might be an alternative to reflect these new trends in the world economy.

Matthew Martin: I would say two things. One is there are already a lot of developing countries making increasing contributions to multilateral organisations. Some of the biggest funders are making between 25% and 40% of their money available—notably Brazil, for example—through multilateral organisations, so they are aware of this. We could probably do more to encourage them in that direction.

If I take the analogy of the 0.7%, I would hope that no British Government would have said that because nobody else is trying to reach 0.7% we should not try, and we should not try to use that as means to encourage them all to do better. I think a lot of the softening of the cuts in other countries, except in extreme circumstances like Spain, where they have no choice, has been because of the comparison effect—people do not want to look completely out of step, so they will not slash their aid budgets. They will still pretend they are increasing them or increase them a bit.

On the same grounds, I certainly do not think it would be appropriate for Britain to say, "We are not going to give any more money to these organisations, because nobody else is." That would just be encouraging everybody to cut back and those organisations to have no funds. My view would be that Britain ought to be demonstrating a strong commitment to those organisations, as it has done for the last 10 years or so. Maybe that is about where we are getting to in terms of a limit of the share of DFID's money that could be allocated via those organisations, but the real issue for me is: if we are putting money through them, how do we make sure they deliver?

Some of this slightly more complicated leverage—that we do not just put money into core funding but we think about co-financing individual projects or co-financing for countries where we feel there is a need to get involved and where we cannot get involved as DFID because we do not have a country programme—is probably part of the way round that.

Peter Chowla: I would concur with the first half of your statement, which is that we need to be tougher on them when we are giving these replenishments and deciding whether we should increase. However, we should condition that not on whether other donors are delivering but whether the organisations are delivering and whether they are reforming internally to deliver appropriately and effectively.

That includes governance reform, which needs to be a key metric of whether the institutions are adapting to the new international environment. It also includes things like development effectiveness, development impact monitoring and accountability on environmental and social issues, etc.—all the issues we talked about earlier, which are the things we need to see them delivering better. Those are the metrics we should be using in terms of whether we should be committing more money to things like the IDA or the African Development Bank.

Chair: Thank you very much indeed. First of all, you have commented on some of our ideas and put a lot of your own into the framework. I will say the same to you as I said to the others: if, on reflection, you have any further thoughts, please feel free to feed them in to us. This is very much the beginning of our inquiry, and at the moment we are teasing out a number of different avenues.

We have no preconceived views. Individual members of the Committee are leaning one way or another, but I think we genuinely want to get the evidence as to what might be the best centre of gravity for what DFID might do. Clearly, it is going to have to change, but there are quite a lot of different options for the way it changes, some of which obviously have more merit than others. Your contribution has been really helpful towards helping us think that through, so thank you very much indeed.