TIME TO SAY "NO THANK YOU" TO FOREIGN AID?

Ali Naseer Mohamed

Foreign aid is popular. It is perhaps more popular in the Maldives where it has a welcoming home, and where its intentions are rarely questioned. There is a deeply held belief in the Maldives that foreign aid promotes social and economic growth in the country. President Gayoom, in his very first Presidential Address to the Maldivian Parliament in February 1979, declared that the Maldives would seek foreign aid "until such a time when the country is able to stand on its own feet with a resilient economy". Although the country had been receiving a significant amount of foreign aid for the previous four years (since 1975, averaging USD 3 million a year), it was the first time that the Government announced a policy towards mobilising foreign aid. Forty-two years since then, it is worth starting a discussion on whether the country has reached (or will it ever reach) a point where it is able to "stand on its own feet with a resilient economy".

Broadly defined, foreign aid—more formally known as the official development assistance, or ODA—is the transfer of resource by government "that promotes and specifically targets the economic development and welfare of developing countries". A few weeks before the Maldives announced its aid mobilisation policy, the Government made a radical change, in January 1979, to the institutional architecture for aid mobilisation and development coordination. A Presidential Directive established the External Resources Section within the Ministry of External (later Foreign) Affairs, with the exclusive mandate of mobilising foreign aid to the country and in the coordination and implementation of foreign aid funded projects. The National Planning Agency (NPA), set up in January 1979, had the task of identifying and prioritising development projects in collaboration with the Foreign Ministry. With that change, the inflow of foreign aid increased sharply, jumping from USD 6.2 million in 1979 to USD 20.9 million in 1980, contributing to a whopping 78 per cent of Government revenue; a level that the Maldives would never reach again.

Bitter first experience

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The Maldives experience with foreign aid had an inauspicious beginning. The country made its first international appeal for foreign aid in 1953 during the time of the First Republic. The country had not fully recovered from the famine caused by the travel blockade imposed in the Indian Ocean during the Second World War. The restrictions did not allow Maldivians to import basic food items and materials required for the upkeeping of the fishing vessels, the dhoni. As a result, hunger was widespread, and people were dying of starvation. Ceylon and Pakistan came to Maldives rescue; the former providing a credit facility, and latter supplying 500 tons of rice as grant aid to the Maldives. No other country bothered to care.

In the mid-1950s, the Maldives Government requested the country's "protective power", Britain, for financial aid to buy a cargo ship that can travel between Malé, and Ceylon and India. The British agreed to the proposal in principle, but also sought the agreement of the Maldives for establishing a British military base in Gan in Addu Atoll. The Maldives Prime Minister agreed, but in doing so not only did he lose his job, but the subsequent developments took the country to the brink of an internal conflict. Ibrahim Nasir, who became Prime Minister in December 1957 and President in 1968, decided not to accept the cargo vessel donated by Britain (according to Ali Umar Maniku, who led the country's international commerce during the period). Indeed, for some time, Nasir viewed bilateral aid with a measure of suspicion, especially from countries that were perceived to have strategic and expansive interests in the Indian Ocean. For example, when the Maldives received an offer for Gan from the Soviets in the late 1970s, Nasir famously declared that "the Maldives is not for sale".

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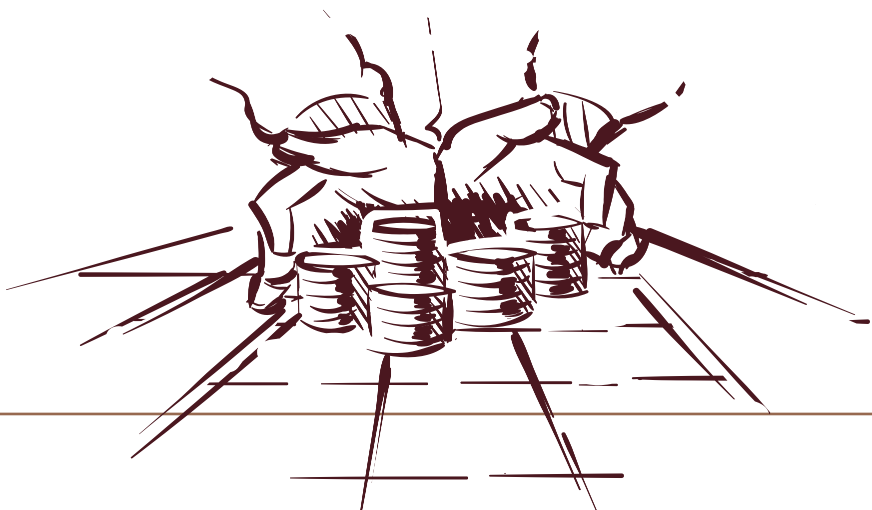
It was that thinking therefore that guided the Maldives to have a very clear preference for multilateral—the UN agencies and the Colombo Plan—over bilateral sources of aid. There were a few exceptions, however. Britain extended some economic aid, as provided for in the agreement signed between the two countries in 1960. The largest and most important British aid to the Maldives was the construction of the Government Hospital building (where ADK Hospital stands today) in Malé and technical support for education planning and modernisation of schools in capital.

When aid was good

Prime Minister Nasir introduced a radical change to the Maldives approach to aid mobilization in the mid-1970s. He realised that the economic assistance coming from the UN and the Colombo Plan were not up to the scale that the country required. As such, the Maldives approached Kuwait, Saudi Arabia, and the United Arab Emirates for financial support in establishing a satellite earth station in Malé. In 1980-81, the Maldives approached the same countries for concessional finance in constructing an international airport in Hulhulé. These two were the largest projects (in terms of monetary value) in the country at that time, and brought about two important changes. It helped Maldivian political leadership to view bilateral aid much more favourably; bilateral funding had scale, which the multilateral agencies were unable to meet, and they helped bringing foreign investors, too. Companies, such as Cable and Wireless of UK, and NEC and Mitsui of Japan made visible presence in the country and would later become key actors in the economic development story of the Maldives.

The Maldives also started holding more informed and regular dialogue with the members of the Development Assistance Committee (DAC) of the Organisation for Economic Co-operation and Development (OECD) on the need for increased foreign aid for the country. The Maldives attended the UN's Least Developed Country (LDC) Conference held in Paris in 1981, where it gained more knowledge about the possibilities that exist for the Maldives to mobilise aid. Although the Maldives had been an LDC since the category was created in 1971, the country did not, until the early 1980s, engage with the donor community to explore the benefits accorded to this category of countries.

Donors also found it easier to support and work with the Maldives. It had a quite low base to begin social and economic development, and therefore, growth rate was consistently high. At the beginning of 1980s, the Maldives GDP per capita was just over USD 280, life expectancy was 53, and there were very



few formal schools in the islands outside the capital Malé. Japan provided grant aid for the construction of primary schools in various islands, including Malé. By the time the Maldives was graduated from the LDC category, Japan had constructed a total of 15 primary schools in the atolls and three in Malé. The UN development agencies provided support in constructing community schools in the rest of the atolls. The UN also supported construction of regional hospitals and atoll health centres. The government partnered with the UN in conducting highly successful disease control programmes that were administered in the islands by family and community health workers trained by a UN supported training centre in Malé.

The DAC countries (currently 30, and referred to as the "traditional donors"), such as Britain, United States, and Australia provided a high number of undergraduate and postgraduate scholarships to help train Maldivians with university education. Others, such as Denmark, Norway, Germany, and the Netherlands, provided both grant aid and loan financing at highly concessional terms to support projects for economic growth. Multilateral development banks (MDBs), such as the World Bank, International Development Association (IDA), Asian Development Bank (ADB), and Islamic Development Bank (IsDB) complemented, and at times led the funding for programmes in specific sectors. The level

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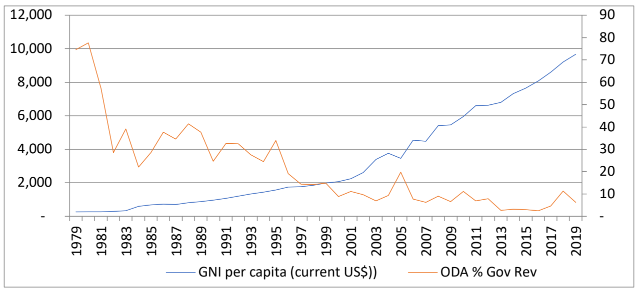
of net ODA to the Maldives remained consistently high, contributing, on average, 39 per cent of government revenue per year in 1980s, and 24 per cent per year in the 1990s.

Per capita income and foreign aid (R) as a percentage of government revenue



Source: World Bank data

Resilience gained

The trend in ODA inflow to the Maldives started to change after 1997, when the UN's Committee for Development Policy found that the Maldives had "demonstrated the steadiest and fastest progress" in economic growth among all LDCs. But the year 2000 was the defining moment in the country's development trajectory. All key development indicators suggested that the Maldives had reached a point where the country could start believing that it can indeed "stand on its own feet" and that its economy has sufficient resilience. In that year, per capita income of Maldivians reached USD 2,070 and life expectancy was at 70 (up from 40 at the country's independence in 1965), and primary school enrolment reached over 96 per cent. The Maldives outperformed every single country in the list of 48 LDCs in almost every social or economic indicator.

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The donors, especially the DAC countries, took note of the progress that the Maldives had achieved. For the first time since 1979, foreign aid's share of government revenue fell below 10 per cent, and the total net ODA fell from USD 30 million to 18 million. Key donors, such as the Netherlands, Germany, and the Scandinavian countries decided to withdraw from the Maldives once the on-going projects were completed. Japan also did not approve new general grant aid projects for several years after 2002.

Aid is addictive. Once a country develops a dependency on aid, it will find it extremely hard to believe that progress on the path of development can be achieved without foreign aid. And that was precisely the situation that the Maldives found itself in the first few years of the new millennium. The Maldives tried very hard to not to graduate from the LDC category. In fact, a UN report on the Maldives, prepared in 2003, has a section with the heading "The history of Maldives non-graduation". The UN passed a resolution in December 2004—just a few days before the tsunami hit the country—to graduate the Maldives from the LDC category.

South-South "Aid" is costly

The Maldives knew that the UN's decision on graduation was inevitable. As such, beginning from around 2001, the country started approaching the emerging donors for grant aid. These donors are mainly in the developing world, whose foreign aid is often described as South-South cooperation. The emerging donors showed more willingness in providing grant aid for projects that DAC countries had earlier declined to consider for support. The result was impressive-looking government office buildings and university complexes were constructed with grant aid. The focus, however, was more on the housing sector, where there was a substantial demand at various income categories, which the government wanted to meet and with an increased urgency.

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The in-flow of bilateral (government to government) aid from the emerging donors gave rise to new challenges unfamiliar to the aid coordination community in the Maldives. One was the lack of transparency in selecting contractors. While aid from DAC countries were also tied (materials and contractors must be sourced from the donor country), the Maldives had the opportunity to contribute to making such decisions. But the Maldives found out that the emerging donors do not want to disclose anything about how the contractors were selected or how the costs were calculated.

Second, the opportunity cost can be extremely high. For example, the Maldives submitted a proposal to an emerging donor in 1983 for the construction of a building to train personnel for the tourism sector. The project began only in the early 2000s and took nearly ten years to complete. The Maldives believed that it was not in a position to withdraw the initial request made for fear of possible diplomatic repercussions. In the meantime, trainings were conducted at makeshift locations for preparing professionals to lead the most important economic activity in the country.

Third, there is no accountability mechanism of any kind for the emerging donors, which often places the Maldives, a small state with limited diplomatic power, in precarious positions. For the DAC countries, the peer-review process (a DAC country reviewing a fellow DAC country's ODA policy, using a common guideline determined by OECD) has become a key instrument to set a certain normative standard in providing foreign aid. Moreover, since the reviews are also published and available to the public, there is an additional pressure on the donors to follow the normative principles of ownership, alignment, harmonisation, managing for results, and mutual accountability set out at in the Paris Declaration on Aid Effectiveness. On the other hand, some emerging donors are themselves net recipients of ODA and therefore have shown resistance in introducing mechanisms to monitor their own aid to the other developing countries.

Fourth, the moral appeal of foreign aid is that it helps save lives. Some, therefore, might consider it ethically wrong for the Maldives to seek foreign aid from countries that have millions of people living in extreme poverty. The World Bank defines "extreme poverty" as living on less than USD 1.90 per person per day. While the Maldives is the richest country in South Asia, this is also the region where there are more than 300 million people in extreme poverty.

Extreme Poverty in South Asia in 2016

	Sri Lanka	India	Bangladesh	Pakistan	Nepal	Maldives
No of people living on less than $1.90 per day (in millions)	0.2	284.6	22.9	8.1	4.0	0.0*
Poverty rate as %	0.9	22.5	14.5	4.0	15.0	0.0*
Per capita income	3,886	1,732	1,401	1,368	899	9,209

* According to UNDP, "the proportion of extreme poor living below $1.9 a day is close to zero, and that of multidimensional poor is less than 1%": UNDP 2020.
Source: World Bank data

Crafting smart solutions

The solution for the Maldives, then, is to move towards more innovative financing and bring about a paradigm shift in the way external resources are mobilised and in the type of partnerships developed.

The first step in such a shift could be to start using more blended finance solutions to achieve development goals. Blended finance is a structuring mechanism that combines resources from the government, multilateral developments banks (MDBs), philanthropic organisations, and the private sector. When pooled together, investments from these actors will have the potential to achieve the scale required for even the larger infrastructure projects. In blended finance, the MDBs will take the lead by injecting catalytic capital to the project to ensure (a) the potential or perceived risks is minimised, and (b) bring the cost of borrowing to the recipient country to a level below market rate.

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The second step needed to attract innovative financing is to re-structure the projects, align them more closely with the Sustainable Development Goals (SDGs), and re-define its social and economic impact. It would also be fruitful to re-evaluate the mechanisms identified in the project for cost recovery, employing the "user-pay principle" especially for infrastructure projects implemented in the larger population centres. Another important dimension that needs to be added to the structure of the project is the role of the private sector and the interaction between the various actors who have invested in the project.

Such a restructuring has significant potential for blended finance. For example, SDG6: Clean Water and Sanitation, SDG7: Affordable and Clean Energy, SDG9: Industry, Innovation, and Infrastructure, and SDG13: Climate Action are areas most popular in blended finance, while they are also the most prominent in the development landscape in the Maldives, too. Moreover, the water, sanitation, and hygiene (WASH) sector—perhaps highest in demand for finance among the PSIP projects in the Maldives—is experiencing the sharpest growth in the global blended finance, in particular, among the ethical impact investors.

Third, there is a need to achieve greater synergy between the key ministries in formulating and implementing development programmes, and in shaping and executing external resource mobilisation strategies. The implementation of such a strategy should be made the focus of the country's diplomacy. But the desired results will not be realised unless the Maldives is able to integrate all the expertise in the government—economic, financial, strategic, and diplomatic—and harness them towards achieving the goals set out in the resource mobilisation strategy. If different agencies operate in silos, the results will continue to remain sub-optimal.

Fourth and finally, the Maldives will be able to attract innovative finance if the country is able to leverage its diplomatic capital with the ability to forge and foster partnerships with the MDBs, philanthropic organisations, and the high net-worth individuals (HNWIs). Diplomacy, if used more innovatively, can be the key in unlocking the potential of blended finance. The Maldives Missions overseas are ideally placed to use the privileged platforms that they have access to, and convince philanthropic organisations, HNWIs, and even the more conventional investors to want to make social impact investing in the Maldives with the objective of producing shared outcomes. The fact that the Maldives enjoys the image as being among the most exotic travel destinations makes such a goal more achievable. Yet, diplomacy will be successful only by repositioning the Maldives missions overseas with a more clearly defined objectives and with diplomats who have the skills specifically built and nurtured for that purpose.

The Maldives is fortunate to have one of the most generous social protection systems in the developing world, funded by domestically mobilised resources. As the richest country in South Asia, it would be unethical, and indeed reprehensible, if the Maldives were to seek or accept foreign aid from countries that have tens of millions of people living in extreme poverty, with hundreds of them dying from hunger every day. To reach the next level in its development trajectory, the Maldives requires external finance at scale and at affordable terms. That can be achieved by moving away from the conventional idea of foreign aid to the more innovative methods and techniques in external resource mobilisation. Smart use of diplomacy, backed by credible policy, will help achieve that goal.

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