

# PUTTING AID IN ITS PLACE: INSIGHTS FROM EARLY STRUCTURALISTS ON AID AND BALANCE OF PAYMENTS AND LESSONS FOR CONTEMPORARY AID DEBATES<sup>†</sup>

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**Abstract:** Recent debates on aid and development are waged on narrow terms in comparison to earlier debates in the 1950s and 1960s. The principal concern of the ‘structuralist’ pioneers of development economics, and the key absence in the current debates, was an understanding of the structural impediments faced by countries going through late industrialisation and rapid urban growth. These result in chronic trade deficits, shortages of foreign exchange and persistent balance of payments disequilibria. The positive potential of aid was understood to lie in its ability to mediate these imbalances in the context of national industrialisation strategies. By the same logic, this potential is lost if countries run trade surpluses. Current debates on aid mostly overlook this dual logic, despite the fact that both positive and negative experiences of post-war development largely vindicate these structuralist insights, particularly in light of current global financial imbalances. Copyright © 2009 John Wiley & Sons, Ltd.

**Keywords:** aid; balance of payments; development economics; global financial imbalances; industrialisation; structuralism

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## 1 INTRODUCTION

In the swathe of recent mainstream literature on aid and development, there is generally a derogatory view of the early structuralist development economists, most iconically represented in the writings of Easterly (2006a, 2006b) and Collier (2007). However, this literature for the most part misses the point of these early structuralists on aid, which

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concerned the role of aid in relation to the overall balance of payments position of a country undergoing late industrialisation and rapid urban growth. The financial and technological demands required by these transformations were understood to produce particular internal and external structural impediments to growth. The external impediments result in chronic trade deficits which, in the absence of sufficient capital flows, lead to chronic shortages of foreign exchange and persistent balance of payments disequilibria. Hence, aid effectiveness was identified in the potential for aid to permit late industrialising countries to run trade deficits. Conversely, by the same logic, we would not expect aid to be particularly effective if countries are exhorted to run trade surpluses while abandoning active industrial policies, as has been the orthodoxy of 'good policy' over the last three decades.

Besides some problematic references to Dutch disease or abbreviated summaries of earlier gap models in development economics, more elaborate considerations of this relation between aid and balance of payments are largely absent from the current literature on aid. The lacuna is not only characteristic of mainstream aid critics who largely ignore the early development economists, such as Burnside and Dollar (2000), Rajan and Subramanian (2005), Easterly (2006a, 2006b) or Collier (2007); it is also characteristic of aid protagonists who acknowledge the legacy of some earlier development economists in a positive light, such as Morrissey (2001), Sachs *et al.* (2004), Sachs (2005) or Addison *et al.* (2005). As a result, even though the question of how to make aid work better has received profuse attention, the larger context in which aid was originally intended to work, and the implications of an inversion of this context, have been mostly overlooked in the recent debates despite the continual relevance of these earlier frames of reference.

This article seeks to correct this oversight by redirecting attention to the bigger picture of balance of payments disequilibria in the context of late industrialisation, as originally emphasised by the early structuralist development economists. The article is not a survey of these early structuralists or of the literature on aid. Rather, it draws selectively from the literature in order to elicit reflection and remembrance. Section 2 briefly reviews the big picture as understood by the early structuralists. Section 3 offers several snapshots of important post-war development experiences, including Latin America, South Korea and China, in order to demonstrate the origins and continuing relevance of this understanding. Section 4 highlights a few of the dominant approaches taken in the recent aid debates as a means to illustrate the lack of this understanding. The Conclusion reflects on the fundamental contemporary challenges to genuine global redistribution.

## 2 THE BIG PICTURE AND THE SMALL ROLE OF AID ACCORDING TO EARLY STRUCTURALISTS

The early development economists from the 1940s onwards generally conceived of the role of aid within the much broader perspective of the relation between late development and balance of payments disequilibria. Given that industrialisation was almost universally regarded as a necessary (although not necessarily sufficient) condition for development, these economists were particularly concerned about the obstacles to late industrialisation in the context of a decolonising post-war world. It was understood that developing countries were attempting to 'catch up' to the industrially-advanced countries in the face of increasingly large technological gaps and the increasing dominance of large oligopolistic multinational corporations based in these advanced countries. Simultaneously, the

developing countries were entering into a new phase of rapid population and urban growth, at a pace much faster than that experienced by Europe a century earlier but with much less resources and many fewer options for emigration. Attention to these issues led the most prominent pioneers of development economics to highlight various structural impediments to growth that emerge through the course of development, including internal impediments (e.g. food production or technological capabilities) and external impediments (e.g. import dependence and foreign exchange constraints).

This understanding was precisely the reason why many of these pioneers called themselves 'structuralists', from Paul Rosenstein-Rodan and Ragnar Nurkse, to Gunnar Myrdal, Arthur Lewis, Alfred Hirschman, Paul Singer and Raul Prebisch. These early structuralists generally differed from modernisation theorists in that impediments were seen as structurally-inherent aspects of late development already unleashed, rather than characteristics of some pre-transitional or market-obstructing institutional setting. Thus, while modernisation theorists such as Walter Rostow placed emphasis on socio-cultural factors as impediments to progress, the structuralists emphasised the large financial and technological requirements demanded by industrial and urban growth (when the latter occurs with the extension of modern urban infrastructure rather than slums). These requirements were considered to be particularly intense for a 'late-comer' given dependence on capital-intensive imports from industrially-advanced countries and on foreign exchange to finance these imports. Moreover, such dependence intensifies the more a country is a late-comer given increasing lags from the technological frontier, or else the more a country is late in the demographic transition given more rapid population growth and subsequent urban growth. The more critical of the pioneers, such as Nurkse, Prebisch, Singer, Lewis and Myrdal, further emphasised that the entrenched, peripheral and subordinate integration of most poor countries into the world economy accentuated these constraints by exacerbating terms of trade declines or outflows of wealth at the expense of import capacity.

The classic formalised understanding of structuralism from this period is often represented by way of the two-gap model of Chenery and Strout (1966).<sup>1</sup> Their model was structuralist in that it recognised limits to the capacity of industrialising countries to expand export earnings rapidly enough to earn the foreign exchange required for complementary imports of capital and intermediate goods. However, their model was far from the first expression of this idea. It had been a commonly accepted view since the 1940s. It was expressed much earlier by Prebisch (UN, 1950), who recognised that industrialisation in export dependent economies would manifest tendencies to external disequilibrium in the form of a 'trade gap', alongside internal disequilibria in the form of inflation and repressed production and consumption due to constrained import volumes or supply rigidities in domestic food production. Similarly, Hirschman (1958) associated himself to structuralism by identifying the domestic food producing and the foreign exchange earning sectors as structural bottlenecks to industrialisation. The earliest theorisations of dependency in the 1950s and 1960s, by colleagues of Prebisch such as Celso Furtado and Osvaldo Sunkel, essentially extended the structuralist logic by highlighting two patterns of disequilibrium generated by dependent and peripheral late industrialisation; one internal in the form of polarisation and marginalisation in the domestic economy, and one external in the form of

<sup>1</sup>See Morrissey (2001: 39–40) for a brief discussion of the Chenery and Strout model and a limited selection of subsequent authors extending the 'gap models'. Note that this family of gap models, which distinguish between foreign exchange gaps and savings gaps, should be differentiated from the savings-gap model promulgated by Sachs *et al.* (2004) which, as pointed out by UNCTAD (2008: 56), borders on tautology.

outflows of wealth on the income and capital accounts, which exacerbated foreign exchange constraints.

Regardless of their differences on specific points or theoretical approaches, there existed a strong consensus that countries attempting late industrialisation would have a chronic tendency to run trade deficits. In a world with limited capital movements, as was the case in the 1950s, these countries therefore tended to experience chronic balance of payments crises. Alternatively, if they ran trade surpluses, they often did so through import austerity. The issue was not about export orientation versus import substitution, but about exports keeping up with the financial and capital requirements of industrialisation that, by the very fact of being late, implied import substitution through one means or another.

From this perspective, it is clear that these structuralists conceived of aid as constructive only insofar as it enables an industrialising country to run persistent trade deficits, albeit deficits that result from productive accumulation rather than simply terms of trade or other contractionary shocks. Aid was understood as a means to avoid choking the capital and infrastructural needs of poor countries in their attempts to industrialise. This is quite different from the savings-gap model of Sachs *et al.* (2004), who argue that the savings gap derives from poverty itself while ignoring industrialisation or the distinction between domestic savings and foreign exchange. Rather, if aid was to have any constructive role at all, it was seen as a strategic injection to overcome particular financial vulnerabilities faced once development was already well underway.

### 3 THE BIG PICTURE IN HISTORICAL PERSPECTIVE

Unfortunately, the fundamental framing of these earlier discussions concerning the role of aid in development has been more or less ignored by contemporary mainstream debates.<sup>2</sup> This has been no doubt due to the paradigmatic shift in economic orthodoxy that started in the 1970s and became known as the 'Washington Consensus' by the late 1980s. To a large degree this shift was predicated on misrepresenting structuralism, as best represented by the work of Bhagwati and Krueger (1973), Krueger (1974, 1983) and Lal (1985, 2002 [1983]). These 'new guards' were successful in reframing mainstream policy discourse by positing the state as oppositional to markets, import-substitution as oppositional to export-orientation, and active industrial policies as causes of failure rather than long-term solutions.

Much has been written on these points by prominent dissenters in development economics, including Joseph Stiglitz, Dani Rodrik, Sanjaya Lall and Ha-Joon Chang. However, less emphasis has been given to the equally important consensus forged by the new orthodoxy; that developing countries should strive their utmost to run trade surpluses (rather than simply expanding export capacity in order to increase import capacity). The uptake of this new consensus in the recent aid literature has obscured the roles that aid has or has not played in mediating balance of payments disequilibria in the important post-war development experiences. Indeed, clarification via several snapshots of these experiences, including Latin America, South Korea and China, provides strong vindication of the early structuralists.

An obvious starting point is Latin America in the 1950s. During this early post-war period, Latin American countries were already approaching the end of the easier phases of

<sup>2</sup>Indeed, there is little or no serious discussion of industrialisation or active industrial policy in Sachs *et al.* (2004) or Easterly (2006a; 2006b). The only passages in which Collier discusses manufacturing beyond brief alluding references are framed within the context of his wider advocacy for trade liberalisation (e.g. 2007: 166).

import-substitution industrialisation (ISI), which was compounded by the simultaneous end of a mineral export boom. As a result, several of the most industrialised economies in the region and the developing world, particularly Chile, Argentina and Brazil, were experiencing economic stagnation, resurgent inflation and chronic balance of payments problems.

The crisis led to a debate over inflation and growth between Latin American structuralists and monetarists.<sup>3</sup> In what became a preliminary to similar disputes regarding structural adjustment in 1980s, the monetarist option led by US creditors and the IMF was austerity, with the aim to purge the way for a private sector revival. The Latin American economists leading the structuralist side of the debate agreed that inflation could be reduced in the short term through fiscal austerity and tight monetary policy. However, they argued that this would not solve the fundamental causes of inflation, which was rooted in the foreign exchange constraint alongside other structural factors. For this, what was needed was concessionary lending to enable these countries to ride through their transitory vulnerabilities, together with a variety of redistributive reforms that would reorient growth along a more solid domestic footing. Otherwise, they argued that monetarist policies would jeopardise long-term economic progress, impose excessive social costs and accentuate the extremely skewed distribution of income (which was nonetheless less skewed than it is today). The monetarist option won out, but revival never really happened and the systemic external vulnerability of Latin American industrialisation remained unresolved. The only option left for these countries was to continue plodding through the more difficult phases of ISI, which was nonetheless facilitated by the surge in Eurodollar liquidity from the mid-1960s onwards.

There is a consensus that Latin American countries had chronically overvalued currencies throughout this period. However, overvaluation in the 1950s and 1960s was not necessarily due to a 'resource curse', as is often argued of late in the mainstream political economy literature.<sup>4</sup> After all, why would this have been the case if they were running trade deficits? Rather, Latin American currencies tended to be overvalued because governments were following expansionary monetary policies as short term means to overcome both stagnation and balance of payments problems in the absence of alternative funding sources (much as the US is doing today, except without the seigniorage rights). This in turn led to inflation and overvaluation of real exchange rates. Massive inflows of debt then maintained the overvaluation from the late 1960s until the 1982 debt crisis. Hence, overvaluation occurred despite persistent current account deficits and recurrent attempts to correct both through monetarist means.

Such counterintuitive outcomes are not merely the result of market distorting interferences. They can also be produced within a fully liberalised setting. For instance, a strong parallel can be made to the international carry trade that was booming in 2006 and 2007, as described in UNCTAD (2007: 15–22). During these final years of financial ecstasies before the meltdown in 2008, the real exchange rates of many 'emerging markets' were steadily appreciating despite large current account deficits (in the case of Turkey and Hungary) or despite fairly high inflation rates and only slight current account surpluses (in the case of Brazil). Rather, exchange rate movements were being overly determined on capital accounts by the international interest rate arbitrage of large hedge funds. While high

<sup>3</sup>See Seers (1983) and Kay (1989) for summaries of this debate.

<sup>4</sup>For instance, see Collier and Goderis (2007: 15–17). In line with this literature started by Sachs and Warner (1995), they offer no significant discussion of industrial policy.

rates in these emerging markets were originally intended as a means to control inflation, in a context of open capital accounts they resulted in asset bubbles and loss of competitiveness, thereby worsening trade deficits or sustaining inflation. In sum, two decades worth of structural adjustment did not solve the structural vulnerabilities of these peripheral late industrialisers, although it definitely made them more unequal.

The logic of these mechanisms was mirrored in the 1982 Latin American debt crisis. As argued in the seminal post-mortem analysis of the debt crisis by Diaz-Alejandro (1984), Latin American governments were able to generate substantial foreign exchange surpluses very quickly within a year of the crisis by simply sending their countries into crushing depressions. Stiff devaluations caused sharp reductions in imports while exports barely responded due to lack of capacity or lack of external demand. The import reductions then crippled domestic manufacturing. In most cases this was combined with monetary restrictions, fiscal austerity and a 'violent reduction in investment, which impaired not only present but future growth. . .' (p.363). He also pointed out that none of this solved the problem of high inflation (p. 365). Rather, the main goal achieved was that these economies were released from their foreign exchange constraints, thereby allowing the rapid repayment of foreign debt and removing international creditors from any major danger of default.

There were alternatives. A strategic injection of aid at this point, primarily through a massive increase in concessional lending without the pro-cyclical conditionalities attached, could have averted this outcome. Alas, such a strategy was not in favour in Washington, nor in the eyes of Sachs (1984). Indeed, in a reply to Diaz-Alejandro, the young Sachs argued that the IMF focus on reducing budget deficits through austerity was a crucial step for restoring private-sector confidence in local currency assets. It was therefore an appropriate strategy to encourage previous capital flight to return to the region as private investment, presumably through the channel of open capital accounts and flexible exchange rates (pp. 399–400). Unfortunately, large net transfers of capital continued to flee out of the continent for the rest of the decade.<sup>5</sup> The double standard is to be noted, given that Reagan was simultaneously inflating his own economy out of recession from 1983 onwards through a surge in deficit-spending, boosted by the injection of fleeing capital from the south.

Moving east, an understanding of the structural financial vulnerabilities faced by peripheral late industrialisers helps to explain the critical role of aid in certain successful cases. Notably, South Korea experienced chronic and escalating trade deficits in the 1960s due to its ISI strategies, similar to Latin America in the 1950s. Net capital inflows also increased rapidly, but these only partly covered the rising trade deficit. However, unlike Latin America, the substantial shortfall was covered by aid throughout the 1960s and well into the 1970s.<sup>6</sup> The argument that aid *alone* caused South Korea to emerge from its 'poverty trap' obviously does not hold water. However, aid definitely played a key role in allowing South Korea to pass through several very vulnerable stages of its intensive industrialisation strategies, among other factors such as privileged treatment by the US. Without aid, it is plausible that chronic balance of payments crises would have choked the potential provided by the other crucial ingredients leading to South Korea's success,

<sup>5</sup>Palma (2003: 131) cites that negative transfers abroad from Latin America (excluding IMF loans) reached 650 billion US between 1982 and 1990. Odious debt and other tales of corruption, as told by Collier (2007: 91–93), obviously accounted for part of these transfers, although it is important to remember that most were legitimate capital movements on newly opened capital accounts. See Diaz-Alejandro (1984: 377–379).

<sup>6</sup>See Rhee (1973); I am indebted to Min Joung Park for referring me to this paper.



namely land reform, active industrial policy and a strong developmental state able to implement plans.

From this perspective, contemporary China would seem to present a puzzle, insofar as it has been industrialising rapidly and maintaining massive levels of investment while, at the same time, running large current account surpluses.<sup>7</sup> Indeed, China seems to be the inspiration behind the ‘Keynes-Schumpeter’ hypothesis stipulated in UNCTAD (2008: 69–70), which argues against the conventional wisdom that current account deficits are better for growth. However, it is important to recall that China’s balance of payments exceptionality only began in the mid to late 1990s, more or less as a mirror image of the equally exceptional US trade deficits, particularly after 2001. Before this time, China behaved like any other developing country; periods of spurting industrial growth led to both inflation and trade deficits, which in turn were only resolved through austerity. In the last bout of such disequilibria, the current account fell into deficit in 1993 and consumer price inflation surged to over 24 per cent in 1994. The deficit ended with an enormous surge of net capital inflows lasting from 1992–97, which set China decidedly on its current path as mass global manufacturing hub, reinforced by an even greater surge of net capital inflows lasting from 2001–05.<sup>8</sup> Nonetheless, the recent experience of trade deficits sheds important light on the insecurities of the Chinese leadership with regard to the external vulnerabilities still potentially faced by the country.

If China’s recent escape from chronic deficits were only due to export-oriented industries buttressed by a surge of FDI inflows from 1992 onwards, then we might ask whether China is going Latin, following the Brazilian miracle of the 1960s except on a much greater and dramatic scale. However, there appears to be much more behind their recent exceptionality. Besides a host of internal factors, several very non-orthodox ingredients seem to play a key role on the external front. These include: closed capital accounts until recently (and still relatively closed); heavy intervention in foreign exchange markets in order to maintain a currency fixed to the US dollar (up until 2005 and then carefully regulated after that); and a largely state-owned and directed financial sector that prioritises investment over profitability.<sup>9</sup> The last ingredient in particular has led many commentators to condemn Chinese banks as moribund without continuous government support, although it actually constitutes classic late-comer strategy, as analysed by Gershenkron (1962). In other words, with control over internal and external financial tools, the government has been able to pursue a strong industrial policy with a very visible hand,<sup>10</sup> while avoiding chronic trade deficits, or recourse to aid or large amounts of foreign lending.

In this sense, the case of China would in fact seem to vindicate the early structuralists, insofar as it has taken very strong interventionist measures to overcome its very real external financial vulnerabilities. Similar to the case of South Korea, China shows that there is no lack of insight on how aid or other financial tools might support planning for industrial-led growth, when there is the political will and ability to do so. However, this requires confronting the fundamental tendency of late industrialisers to run chronic trade deficits, due primarily to structural causes rather than ‘bad policies’ or ‘bad institutions’.

<sup>7</sup>The surpluses are well known. Levels of investment in China have been above 40 percent of GDP since 2003 (until 2007, the latest data available in CSY 2008: Table 3–2).

<sup>8</sup>Data are taken from various China Statistical Yearbooks.

<sup>9</sup>On the issue of state ownership and control of banking, see García-Herrero et al (2006: 306–312).

<sup>10</sup>See Nolan (2001) and Rodrik (2006) on Chinese industrial policy.

#### 4 HIGHLIGHTS OF TRIVIALITY IN RECENT AID DEBATES

In light of these insights from the pioneers and from recent history, we can see how there is in fact no sense in discussing whether aid is good or bad for development, or whether more or less aid is required for development, outside of a much broader understanding of what is required for development to happen, namely industrialisation and large sunk investments in urban and other infrastructure. These in turn usually require that developing countries run trade deficits rather than surpluses. This rule has been broken by the recent exceptionality of China, although its replication on a broader scale is questionable if only because the ability of the world economy to sustain such massive disequilibria between current and capital account surpluses and deficits has probably reached a limit. Indeed, Chinese surpluses are now falling in the face of the global financial crisis, although it remains to be seen whether this will be cyclical or structural.

The role of aid must be considered in this light, because aid will have very different macroeconomic implications depending on whether a receiving country is in current account deficit or surplus. This point seems lost in most of the recent mainstream literature.<sup>11</sup> For instance, Rajan and Subramanian (2005) launched a critique of aid along the lines that increasing aid to poor countries could result in the 'Dutch Disease', i.e. currency appreciation and the undermining of competitiveness in domestic tradable sectors. Whether or not this concern is justified, it is *only* applicable if and when a country runs a current account surplus (holding all else constant). Assuming that aid flows have a neutral impact on the capital account (and that exchange rates are flexible), only then will an increase in aid cause currency appreciation. On the other hand, this warning is irrelevant if and when a country is able to run a current account deficit correspondent to the amount of aid received, as in the case of South Korea discussed above.<sup>12</sup> The argument might be made in the Korean case that aid prevented a necessitated devaluation and that South Korea would have performed better in its absence, but this we shall never be able to prove. In any case, if the Dutch Disease were a valid concern, it would make much more sense to apply it to an analysis of open capital accounts given that capital movements usually far exceed aid flows, but this is rarely done by proponents of this line of argument.

From this perspective, it is meaningless to argue that large increases in aid would produce better development (as Sachs does) without examining the international mechanisms set in place to deliver aid, which for much of the last three decades have encouraged a haemorrhaging of human, physical and financial resources from poor to rich countries. The same can be said of arguments that aid effectiveness could be improved by improving incentive mechanisms within poor countries (e.g. Easterly's argument), irrespective of the globalised incentive mechanisms that play a strong role in disorienting local incentives. The frivolity of these arguments is best highlighted by the massive US current account deficit, many times the size of the annual aid budget of the OECD countries and largely financed by the developing world.

Moreover, even if a country is in deficit, aid would presumably have very different effects on growth depending on whether the deficit (or surplus) is due to productive

<sup>11</sup>See Easterly (2006a: 39–45) for a very exclusive review of this literature.

<sup>12</sup>Collier (2007: 122) implicitly recognises this logic by recommending that one way out of the Dutch Disease aid dilemma is for countries to import more, including technical assistance. However, he does not place this recommendation within the broader context of industrial policy. Nor does he explore why countries would be in a current account surplus in the first place, besides the resource curse. This is ironic given his earlier assertion that SAPs did not work in many African countries because elites resisted their implementation (Collier, 2007: 67).



investment and accumulation, or simply due to terms of trade and other contractionary shocks (as discussed in UNCTAD, 2008), or to austerity and structural adjustment programmes (SAPs) in the case of a surplus. Indeed, many of the arguments on aid and growth are rendered trivial by their lack of consideration of these broader structural considerations. For instance, Easterly often argues that there is little or no association between aid and growth given that Sub-Saharan Africa has received the most aid (as a proportion of GDP) over the last fifty years but has recorded the worst economic performance. Moreover, its aid increased while its performance worsened. The point is that the region suffered a crushing depression in the 1980s and into much of the 1990s. The wider global economic shifts contributing to this depression were so overwhelming in this region that we would not necessarily expect to see any correlation between aid and growth, regardless of whether aid is generally good or bad for growth. Perhaps hinting at this, Easterly criticises Sachs (2005) for only focusing on the period after 1980, while ignoring the significant growth experienced by poor countries from the 1950s to the 1970s (see Easterly, 2006b: 100). However, he does not integrate such passing reflections into the mainstay of his arguments. Rather, he falls foul of his own criticism in setting out his case for bad government by focusing only on indices from 1984 onwards (*ibid.*: 100–101). Hence, we are led to believe that aid will not function well in a context of bad (market) institutions and policies, even though it is not truly explained why these countries were poorly performing by the early 1980s in the first place.

More pertinent is the fact that Africa was experiencing net outflows of capital over these years that far exceeded any inflows of aid. Collier (2007: 91–93) discusses this point to some extent but does not place it within the context of the systemic shifts in global economic structures and ideologies that produced these outcomes. This is to be expected, given that he broadly positions himself within the hegemonic paradigms and institutions of this period, as do Sachs and Easterly. Indeed, Collier (2007) mostly avoids mention of the 1982 debt crisis altogether and seems to imply that SAPs themselves constitute good economic policy.<sup>13</sup> However, Collier is probably right in his contention with the simplicity of Sachs, even though he avoids the elephant in the room. Under the current setting, even a doubling of aid levels can probably do pitifully little to counteract the overall trend of capital outflows from poor to rich countries. If anything, they might even reinforce it, particularly when the ‘technical assistance’ of northern academics and their host of graduates results in fallacious policy guidance.

Similar obfuscations are committed in the influential paper by Burnside and Dollar (2000), who merge together data from two entirely different epochs of development; one before the debt crisis when many poor countries were still growing at decent rates, and one after, in the context of SAPs and economic breakdown for much of the poor world outside South and East Asia. In blurring the two periods through problematic cross-country regressions, it is logical that the overall association of aid with growth is neutral, except in the presence of ‘good policies’. Good policies in turn are defined deceptively, attributed to countries such as China where growth has had very little to do with aid or SAPs.<sup>14</sup>

Comparable ambiguities are even committed from less mainstream angles. For instance, Addison *et al.* (2005) conclude from a survey of mostly cross-country regression studies

<sup>13</sup>For instance, Collier does not explain why international banks were no longer willing to lend to Nigeria in the mid-1980s (2007: 41). Notably, Nigeria had good access to international commercial bank lending in the 1970s and thus, like Latin America, it was severely hit by the US ‘Volcker Shock’ in 1981–1982.

<sup>14</sup>A similar problem underlies the related work of Dollar and Kraay (2002).

that aid broadly works, without differentiating the radically different structured settings in which aid might or might not work. Similarly, Morrissey (2001) gives some consideration to the 'gap models' of an earlier period, albeit focused exclusively on the abstract formal modelling of Chenery and Strout (1966) and later variants, although once he turns to the econometrics, he does not consider the inverse implications of the logic of these models; that while aid might broadly help growth in the context of a trade deficit, it might not in the context of a trade surplus. Rather, a trade surplus would tend to lead to capital outflows, thereby reinforcing the transfer of resources from surplus poor to deficit rich.

## 5 CONCLUSION: LOOKING TOWARDS A FUTURE OF REAL REDISTRIBUTION

Viewed in this way, it is important to recall that the so-called age of developmentalism of the early post-war period was structured by US trade surpluses up until the mid-1960s. The US produced more than it consumed and financed the rest of the world to consume its surplus. Hence, for better or worse, there was a net transfer of resources from rich to poor countries, even though the way these were instituted led to new types of problems, as articulated by dependency theorists. The poor countries that broke through in this earlier context were those that received net transfers *and* were able to practise active industrial policies.

Today, the global momentum is for a flow of resources away from poor countries, which together produce more than they consume and finance the US to consume their resulting trade surpluses. The critical turning point was the 1982 debt crisis, which resulted in a decade of deep depression in Latin America, two decades in Africa, and massive net transfers of capital from these two regions to rich countries, primarily the US. The pattern was extended to Asia during the Asian Financial Crisis in 1997–98. Since then, the one poor country that has truly managed to break through—China—stands accused by many as mercantilist, although it can be hardly blamed for this given that it has been simply very skilful in navigating a very skewed playing field. Nonetheless, the final verdict on China is yet to be seen given that the country is still effectively quite poor and increasingly unequal.

The inverse of the current global imbalances—that the US produces more than it consumes—might not be feasible or desirable in the current global setting. Nonetheless, it offers an audacious clue of where we must go in order to return to a developmental agenda that is truly redistributive, rather than one based on the survival of the fittest few who can manage to swim upstream against a surging current of global net capital flows. Only under a structured setting where the gravitational trend of global imbalances is for capital to flow from rich to poor will it be possible to fashion the constraints and opportunities of an aid system that might have a chance of supporting a new and improved developmentalism.

In other words, aid could have a positive productive effect if poor countries would be allowed to run chronic trade deficits, rooted in productive investment directed by active industrial policies, and without being penalised by financial markets. In this context, the provision of sustained long term concessional forms of finance could help to insure that there is in fact a net transfer of resources to the poorest of countries, all things considered. We are now a long way off from such a structured global setting and the path to return there is most likely fraught with much instability and turmoil. Yet in recognising this quagmire, at the very least we should recognise the hypocrisy of current mainstream development discourses, which obsessively focus on domestic institutional change in poor countries

while ignoring the countervailing institutions and structures at the global level that constrain and undermine these same countries.

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