



Aid to Vanuatu – Successes and Failures

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Why Vanuatu?

Because it has seen more than a doubling aid in the past decade in real terms and there have been lots of analysis of the situation

- **Academics at the time**
 - Jayaraman and Ward (2006) on “Aid Effectiveness in the Pacific island Countries: The case of Vanuatu
 - Raghuram Rajan and Arvind Subramanian (2005)
 - Feeny (2000)
- **Policy “wonks” at the time**
 - Steven Radelet, Michael Clemens, and Rikhil Bhavnani (2005 Aid and Growth)
 - Internal Vanuatu Government brief Tevi, Shing and Soni – 2004
 - “The umbrella brigade”
- **Commentators after**
 - Howes & Soni (2008)



The facts – success **economics**

- Economic growth has been rapid over the medium term **averaging over 5% in real terms over the past seven years** and this has not been resources driven
- Rural incomes have increased and inequality has decreased – **gini coefficient reduced from 0.58 to 0.41**
- Official poverty figures fallen from 41% (ADB2000) to 8% (VanGov, AusAID 2009).

The facts – success **business**

- Vanuatu rises to first in the Pacific in terms of Cost of Doing Business Survey (2010)
- Deregulates air space
 - Overtakes Palau in terms of tourism arrivals
- Deregulates telco market
 - Massive impact of arrival of digicel in terms of economic activity, prices and access

The facts – success **financial management**

- US Treasury rates Vanuatu's PFM system and the FMIS "the best they have seen in any developing country"
- Rapid increase in volume of aid flows through direct budget mechanisms
- IMF rate FMIS and working relationships between the Central Bank and the Ministry of Finance in Vanuatu as "the model for the pacific"
- A decade of macroeconomic stability

The failures?

too many to list !

- Some improvements in health and education indicators
 - Poor quality data
 - Impacts may be deferred
 - Increasing dependence on donor programs to affect service delivery
- Education levels fail to meet the needs of the economy creating dependence on overseas workers
- Lack of focus on urban development
 - Growth in peri urban poverty

How did this happen? Success get the macro right

- It is important that the size of the aid should be given in relation to the size of an economy
 - If not then it complicates the role of central banks in exchange rate and monetary policy formulation – sterilizing the inflows to curb inflation and to address competitiveness issues
 - The experiences in Vanuatu so far revealed that monetary policy challenges have been managed well. For instance, the US MCC Fund of US\$65 million has been managed well since the majority of funds were placed abroad

How did this happen? **Success** get the fiscal right

- Use fiscal policy to help. For example, keep project funds in foreign currency accounts and pay as many suppliers as possible in foreign currency & through the budget. This means outsourcing to overseas where local capacity is not enough:
 - Education – increase overseas scholarships
 - Use foreign contractors for infrastructure – new and maintenance
 - Retire foreign currency debt, take out no new foreign currency borrowing and use extra grant aid to cover the difference
 - When liquidity is tight domestically retire domestic debt to inject funds into the economy

How did this happen? **Failure** **make it simple**

- Too many complex “innovations” particularly in the social sectors – programs such as SWAPs etc failed to take off especially in the social sectors
- Too many international priorities – prevent Governments from sticking to national priorities
 - MDG’s
 - Free Trade
 - Climate Change



How did this happen? Failure not trying to use Government systems

- Find out which parts of the system and use them
- Find out which parts of the system don't work and then strengthen them, after that use them
 - This means losing an element of control from the donor side
 - It also means creating ownership from the government which is far more important
- Try to avoid creating parallel systems

Conclusions?

- IMF and VanGov were correct – different types of aid deliver different results and there is room for all:
 - Institutional support has a long term impact – difficult to measure in the short term, but can increase absorptive capacity
 - Emergency aid is always necessary, especially given increasing frequency and intensity of natural disasters
 - Economic growth directed programs like GFG have a clear short and medium term impact especially if they are able to build on earlier institutional strengthening success

Conclusions?

- AusAID and Vanuatu Government were correct to try and build innovative innovations using Government systems and people:
 - Following on from the “Drivers of Change Analysis” a new program called “Governance for Growth” was designed
 - Uses local systems
 - Driven by the Government
 - Devolved responsibility to Port Vila from Canberra makes it incredibly flexible
 - Built around a “trust” relationship between AusAID and local staff – this is based on a long term relationships through various intermediaries



Some thoughts

- Aid is ultimately a form of social venture capitalism
- International development is ultimately about
people, power, politics and money
- Vanuatu has shown that it is possible to increase aid, it is possible for it to be absorbed, it is possible for the funds to have a positive macroeconomic impact and it is possible for aid moneys to improve the political affiliations between nations.
- But to achieve this you have to take risks, accept losses and make long term investments in people, institutions and the economy