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Title: The Changing Grounds of Aid Effectiveness: the implications of aid as a financial flow amidst financialised global imbalances

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Abstract:

The difficulties with sustaining significant degrees of publically-funded redistribution from the developed to the developing countries in the current aid architecture is examined through an historical lens regarding overseas development assistance (ODA) as a financial flow within the broader context of global financial imbalances in the post-war period. The paper first explains the basic premise that aid effectiveness needs to be understood (and was understood by early aid advocates) as a function of allowing countries to finance development by running trade deficits and, by consequence, net capital inflows (discussed in Fischer 2009, 'Putting Aid in its Place,' *J. of International Development*). For structural reasons, late industrialization and other aspects of development in the post-war era have usually resulted in trade deficits. ODA could prevent such deficits from choking off intensive developmental endeavours. Conversely, this potential of aid is lost if countries run trade surpluses (or if deficits are not the result of developmental productivity-enhancing investments). This proposition is illustrated with historical data from South Korea. In the second section of the paper, aid is discussed in the context of two paradigmatic phases of the post-war period. In the first phase, up to the mid-1970s, the US was mostly in current account surplus and exporting net goods, services and finance abroad, thereby supplying and financing the trade deficits of Europe and then developing countries. In this context, aid was one among other forms of net capital outflow from the US supporting industrialization abroad, as best represented by the case of South Korea. In the second section of the paper, aid is discussed in the context of two paradigmatic phases of the post-war period. In the first phase, up to the mid-1970s, the US was mostly in current account surplus and exporting net goods, services and finance abroad, thereby supplying and financing the trade deficits of Europe and then developing countries. In this context, aid was one among other forms of net capital outflow from the US supporting industrialization abroad, as best illustrated by the case of South Korea, albeit this developmentalist dynamic was also underlain by a dialectical process of dependency, as best illustrated by various cases in Latin America. In the second phase, which started in late 1970s, the US moved into a position of persistently

large and growing current account deficits, therefore absorbing finance from the rest of the world and supported by waves of financial liberalisation in the US and globally. Capital account surpluses were underlain by significant net outflows of US FDI abroad, perpetuating similar FDI outflows in the first phase despite the overall absorption of finance from abroad, thus reinforcing processes of dependency despite the shift towards an anti-developmentalist dynamic for most developing countries besides a few. The prospects for aid effectiveness in this latter phase have been far from evident given that the dominant trend in global financial flows has been essentially regressive. The paper concludes that the key to creating a truly effective aid system must be found in genuinely redistributive financing mechanisms that enhance rather than undermine national development.