



Speech at EADI / EDC 2020 event

*Fighting the global recession's storm:  
Implications for European development co-operation*

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Bodo Ellmers (EURODAD)

Many developing countries are currently facing a collapse of private external financing due to the crisis: The IMF estimates a financing hole of US\$ 165 billion dollars for the 38 poorest countries for 2009.<sup>1</sup> We are therefore observing two remarkable trends in development finance:

1. Official Development Finance gains more relevance again as developing countries cannot rely on private capital flows (including export revenues and remittances) to such an extent as in the boom years until 2007.
2. Especially the Non-Debt-creating inflows to developing countries have decreased, while most of the crisis response measures, for example the 1.1 trillion dollar package proposed by the G20 at the London Summit, are debt-creating flows such as IMF emergency loans, Development Bank loans, export credits)

Having said that, let us see what the European Commission suggests to support developing countries in coping with the crisis. I would like to focus on five topics:

1. Plans to frontload official development assistance
2. Counter-Cyclical Financing through non-traditional channels, especially the European Investment Bank
3. The ominous Whole of the Union approach
4. Accelerated implementation of the aid effectiveness agenda
5. Dealing with foreign debt

## **1. Frontloading ODA**

The Commission desperately tries to disburse more ODA faster. Frontloading ODA is definitely a good strategy in times of crisis, and the Commission is in a good position to do so, because its aid is to a large percentage disbursed as budget support which can theoretically be disbursed quicker than project finance. However, there are some concerns:

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<sup>1</sup> IMF (2009): the Implications of the Global Financial Crisis for Low-Income Countries, p. 34

- The Member States do not seem to support the Commissions activism. After the May GAERC, Commissioner Louis Michel complained that the Member states only welcomed the Commission's frontloading plans but did not endorse them.
- Frontloading puts the sustainability of Commission development finance at risk, since it has a given amount of money for a given time in its instruments such as the EDF. Frontloading in 2009 either means that there is less Commission ODA available in the following years, or we would need an early replenishment of the EDF. The latter may not be supported by Member States. Some recipient governments are refusing to accept frontloaded money as they do not trust that the shortfall will be made up in future years...
- ... Especially because we see a trend in the opposite direction at the moment on Member States level. Italy, Ireland and Latvia have cut their aid in 2009, and it is likely that more countries will follow. So the Commissions efforts to disburse more ODA are voided out by the Member States aid cuts.
- The Commissions own bureaucratic procedures may not be favourably for rapid reactions such as frontloading. Traditionally it is the other way around: As Sasja Bökkerink of Oxfam International wrote in the last year's Reality of Aid Report, backloading is in fact the general rule. More than one quarter of Commission aid comes late due to burdensome bureaucratic procedures.<sup>2</sup>

## 2. Counter-cyclical financing

Lack of better alternatives makes the European Investment Bank the EU's main tool for Counter-cyclical measures. As seen, the potential to frontload ODA from traditional development financing instruments such as the EDF or the DCI is very limited, and the EBRD lacks the external lending mandate to operate in certain regions of the developing world where counter-cyclical finance is desperately needed at the moment. So it is especially the Commission who wants to bring the EIB in.

Enhancing and strengthening the EIB's role as development finance institution was promoted very strongly in the Commissions April Communication Package where ten of 28 policy recommendations concerned the EIB. But this was already much weaker in the 18<sup>th</sup> of May GAERC Conclusions on "Supporting developing countries in coping with the crisis", what indicates that, here as well, the Member States do not fully support the Commissions ambitions.

The European Council invited the EIB to lend quicker and more flexibly to the financial and infrastructure sectors, as well as financing small and medium enterprises – but only on the basis of its own capital resources. And the Council made clear that more flexible implementation procedures to frontload disbursements, including for budget support, shall avoid putting the sustainability of EIB lending at risk.

Development NGOs, including in the Eurodad membership, are concerned to see the EIB's role strengthened. The EIB is quite obviously an investment bank, not really a development bank. It lacks experience in operating in a developing country context. It has introduced some environmental and social standards and safeguards in recent years, but these are not very elaborated, and anyway the EIB lacks the capacity and expertise to assess compliance with these in project appraisal and implementation. It is also not very well prepared to ensure and

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<sup>2</sup> Bökkerink, Sasja (2008): European Commission. Providing the Kind of Budget Support that is Needed?, in: The Reality of Aid 2008. Aid Effectiveness, Democratic Ownership and Human Rights, p. 103-110

assess positive development and especially poverty reduction impacts of its lending activities.<sup>3</sup>

To say something positive about the EIB: It is a very efficient institution with relatively lean processes and low transaction costs, and it imposes less conditionalities on its clients than other development banks. Having access to EIB loans could also increase policy space for developing countries which are currently very dependent on World Bank financing.

The fact that the EU is about to dedicate development tasks to institutions which are not really development institutions leads us to another novelty. The ominous “whole of the Union approach.”

### **3. Whole of the Union approach**

This new approach has been unveiled for the first time in the EU’s April Communication package, where the Commission proposed to “use all instruments available to leverage assistance aimed at stimulating growth, investment and job creation.” Such a whole of the Union approach shall include “export credits, investment guarantees and technology transfers for the benefit of development”

Since then, the list of ingredients gets longer and longer. What has been added in the May Council Conclusion is development-oriented support in research and technology, peace and security, migration, renewable energies and climate change.

On the one hand, more policy coherence in development is desperately needed. A whole of the Union approach could be a step towards more policy coherence in development. But to be holistic it would have to address the upsides and downsides of European policies and also include a frank assessment of capital flight via European tax havens. It should also ensure that any additional types of funding that are counted as contributions to development comply fully with the approaches that Eurodad has set out in its responsible finance charter.<sup>4</sup> This – which sets out a series of measures to make loan contraction more accountable and builds in measures for changing payment or other terms if circumstances change - is the only way to prevent a new wave of bad debts.

On the other hand, it is very suspicious that such a new approach comes up at a time when many European donors fail to deliver on their commitments to increase ODA, and some have even cut their development spending. So the new approaches’ main intention could be to distract from ODA, and from the EU’s presumable failure to keep the promise on increasing the traditional development assistance.

### **4. Aid Effectiveness**

Another crisis response measure is to accelerate the implementation of aid effectiveness commitments as outlined in the Paris Declaration on Aid Effectiveness and the Accra Agenda for Action. DG Development is currently doing research on the cost-savings of full implementation, and in the April Communication package they have already unveiled the figure that these would amount to 5 to 7 billion Euro annually, so to roughly 10 percent of Europe’s combined (and inflated) ODA. Commissioner Louis Michel and DG Development director Stefano Manservigi seem to have the hidden agenda to use the aid effectiveness reform process to strengthen the role of European institutions in the aid architecture. They tend to sell this figure to the public as “the costs of non-Europe in development assistance”,

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<sup>3</sup> See for example the critique of the “Counter Balance”-Network: <http://www.counterbalance-eib.org/>

<sup>4</sup> Eurodad (2008): Charter on Responsible Financing; available at: <http://www.eurodad.org/whatsnew/reports.aspx?id=2060>

obviously referring to the fragmentation of the European aid architecture where each Member State has its own institutions and mechanisms to channel aid and implement projects.

The European Council identified four areas in its May Conclusions in which “the Union can really make a difference”: division of labour, use of country systems, predictability of aid and mutual accountability for results, including less conditionality. Member States were invited to prepare individual action plans for implementing the existing commitments.

The Council called for advanced implementation of the existing code of conduct of Complementary and Division of Labour. It also identified other areas in which joint EU approaches or codes of conduct could be useful, i.e. the use of country systems, technical assistance, vertical funds and incentives.

While the Commission’s ideas are tempting there is in reality very little progress in implementing the Paris and Accra commitments. When Eurodad asked its Member Organisations which European States are actively having country-level action plans for implementation, we found out that so far only Germany has a final plan. And only the UK, Denmark, Sweden and the Netherlands are currently preparing plans. And there is quite some pressure to bend aid more to the needs of suffering European exporters rather than to the needs of impoverished people in low-income countries.

## **5. Foreign debt**

On foreign debt, the EU’s crisis response is shockingly weak. This is particularly worrying, and here I am coming back to where I have started, since we are currently observing the collapse of non-debt creating financial flows to developing countries, which are replaced by debt-creating emergency finance from the IMF, development banks and export credit agencies. This will quite obviously raise debt levels in developing countries, in many cases to unsustainable heights, and eventually lead to new debt crisis - and not to forget to less fiscal space to finance development and poverty alleviation in the coming years when loans have to be paid back.

The May Council Conclusions dedicate one single paragraph to an issue which might soon become critical in a world financial crisis. And this paragraph contains no news. The Council stated that burden sharing is crucial, that involvement of all creditors in international debt resolution mechanisms is necessary to ensure debt sustainability of low-income countries. It furthermore pledged to continue supporting the existing debt relief initiatives HIPC and MDRI, and it “supports discussions, if relevant, on enhanced forms of sovereign debt restructuring mechanisms, based on existing frameworks and principles”

This is insufficient. HIPC and MDRI are almost over, most of the limited number of countries which were allowed to participate, have reached the completion point, and there is no follow up strategy in place. Regarding the new institutional approaches to deal with sovereign debt, it was disappointing to read in the Financing for development paper of the April Communication package that “only a minority of Member States so far acknowledges a need for a sovereign debt restructuring mechanism to deal with future cases of debt distress in developing countries”. Keeping in mind that all Member States have committed to explore enhanced mechanisms in the United Nation’s Doha Declaration, and these future cases of debt distress might soon occur in many countries. The EU, and the international financial architecture in general, is not adequately prepared to tackle this situation.

Civil society organisations organised in Eurodad and the EuroIFInet have frequently called on governments to introduce a fair and transparent arbitration process to deal with cases of

unsustainable sovereign debt.<sup>5</sup> And such an institutional innovation should be introduced soon, because it might soon be needed. As a short-term response to the crisis, CSOs have called for an immediate and unconditional debt moratorium for those developing countries which are hardest hit by the crisis. Such a debt moratorium could be implemented immediately, if there was political will to do so, and has on the short run no budgetary implications for the creditor countries involved.

Such a debt moratorium was also supported by the Secretary General of UNCTAD who said: “In the current global crisis situation both debtor and creditor countries would probably be better served if scarcer foreign exchange earnings in the debtor economies were used for the purchase of imports rather than for debt servicing.”<sup>6</sup>

It should be clear that, when donor countries fail to increase and/or frontload aid disbursements they should at least abstain from demanding money from poor countries in times when they need it most to fight the global recession’s storm.

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<sup>5</sup> The latest EuroFINet positioning paper is available at:  
<http://www.eurodad.org/whatsnew/articles.aspx?id=3458>

<sup>6</sup> UNCTAD Press Release, 30 Apr 09:  
<http://www.unctad.org/Templates/Page.asp?intItemID=4819&lang=1>