COMMODITY AID AND COUNTERPART FUNDS IN SUB-SAHARAN AFRICA: SOME MACROECONOMIC ASPECTS

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If you want to understand the causes that existed in the past, look at the results as they are manifested in the present. And if you want to understand what results will be manifested in the future, look at the causes that exist in the present.

— Buddhist Sutra

1 COMMODITY AID, COUNTERPART FUNDS AND MACROECONOMICS

In the 1980s, food and other commodity aid, their monetisation, counterpart funds and macroeconomic policy have become prominent in applied analytical and applied policy dialogue and practice in sub-Saharan Africa (SSA) for quite specific contextual reasons.

First, twenty-five years of low growth of food production, falls in earned import capacity, deterioration of infrastructure and war have created growing malnutrition and vulnerability to famine in most of SSA. Upsurges of drought and war in the first half of the 1980s triggered massive food aid, both for destitute refugees and for urban populations who did not lack purchasing power so much as physical access to food.

At the same time, the perceived need for quick disbursing assistance to halt the throttling of infrastructure maintenance and of directly productive sectors by import strangulation operation led to balance of payments support funding. Like much food aid, this was in large part sold to enterprise resulting in flows of counterpart domestic currency.

All this ran in parallel with the concern of external assistance providers in the 1980s that wrong macroeconomic policies in Africa (usually perceived as excessive interference with markets and inadequate presence of good governance) were the chief cause of its economic decline. That concern in turn led to rising determination to utilise external transfers as a means to influence or control recipient state policy and practice — especially macroeconomic policy and government accounting (see Green 1991b). The domestic currency counterpart flows were seen as an effective and available instrument for utilizing food and other commodity aid to alter recipient government allocations of, and accounting for, resources.

In practice, counterpart funds were large relative to state spending in only a minority of cases and for a few suppliers, so that the potential leverage tended to be overestimated (see Bruton and Hill 1991). And because donor policies and accounting frames were both in flux and divergent, largely relating to a shift from the old ‘capital budget aid — good; recurrent budget support — bad’ dichotomy to a more analytical and contextual one; the pressures on recipients were inconsistent. At a high opportunity price in scarce personnel time, the divergencies meant they were also evadable/avoidable. This confused situation was made even less coherent by the traditional view that food aid should both feed the hungry directly today and if monetised (traditionally frowned upon) tomorrow as well, via use of counterpart funded rural investment and the new Human Condition/Adjustment With A Human Face/Absolute Poverty Reduction focus (see Green 1991a; World Bank 1989; World Bank 1990).

As is distressingly common in development theory, analysis and praxis, the new attention to food aid/counterpart funds has not been informed significantly by the earlier experience of the 1950s and 1960s (see FAO 1955; Dandekar 1965). Historical memory — both institutional and academic — has proven to be both fragmentary and occasional.

2 MACROECONOMIC ANALYTICAL FRAMEWORK

The commodity aid/counterpart fund official and quasi-official analysis has reached a certain consensus (Maxwell 1991 and in this Bulletin). There is agreement that, in general, the combination of commodity transfers, monetisation and first round expenditure is inherently neutral as to government budget balance, household/enterprise account and — less clearly — balance of payments. This assumes a rapid completion of counterpart fund disbursement (see Clement 1989; Roemer 1989).

In fact, this conclusion is not a general result, but one contextually related to SSA in the 1980s and probably in the 1990s. Import constraints cripple production and revenue constraints choke off even services that all commentators agree are both crucial and state business. Therefore, commodity transfers do raise imports and utilized counterpart funds increase government spending by virtually their own amount.
However, that is really a first round analysis of monetary GDP at current prices. If increased government spending, balanced by commodity aid receipts, allows provision of more services, there will be a balanced budget multiplier (increase in real GDP). To the extent real public sector wages are raised, the balanced budget multiplier will be reduced unless higher real wages are offset by productivity gains. Given the below efficiency level wage/salary structure of many SSA states, such a rise in real wages or fall in unit labour cost of services is by no means implausible.

The assumptions behind the consensus assume a brief time lag from effective real resource transfer (aid eaten or put into a production process) and counterpart fund expenditure. Most monetisation and fund use procedures do not, in fact, result in brief lags. Longer lags make resource transfer/monetisation deflationary (households/enterprises pay; government does not spend) and lagged spending inflationary (government spending rises at a time real resource supply is not raised). The neutral result can then be obtained when disbursements (out of previous sale proceeds) approximate extractions (from sale of current aid) (Roemer 1989).

Further, there are sectoral specifications which modify the macro results. Neither by product nor by region are extractions (enterprise/household payments reducing demand) likely to correspond exactly to injections (government spending), rather than be above or below (Maxwell 1991). Further, construction demand is likely to rise and be inflationary given that sector's characteristics.

More serious, the consensus concentrates on first round effects — not continued impact over time. This is particularly relevant in respect to GDP and the balance of payments. Post first round spending should raise GDP. But that will inevitably raise import requirements (as indeed will balanced initial round additional government spending, albeit that could be balanced by commodity aid for state import requirements, e.g. drugs, textbooks, vehicles and spares, fuel). As a result, the macroeconomic consensus is narrow and short term in outlook; not at all the ideal basis for using commodity aid and counterpart funds as an input into structural adjustment’s medium term, real output enhancement strategy.

This limitation is inherent in slow disbursing counterpart funds but applies more generally to all such funds not large enough relative to total recipient spending to allow serious forward macro or sectoral impact analysis or to limit fungibility (switching other resources away from use funded through monetised commodity aid). They are exacerbated if the commodity flow is variable and unpredictable in amount and timing — as is most food aid and some other CA.

To overcome these limitations requires analysis and allocation in a genuinely national macroeconomic and articulated sectoral perspective, with clear attention to policies as well as spending. Further, if commodity aid is highly variable, then it needs to be evaluated and assessed in conjunction with other types of resource transfer.

Whether these conditions suggest streamlined, more broadly focused, coordinated counterpart funds, or an overall dialogue on resource use with the proceeds of monetised commodity assistance flowing directly into general revenue, is an open question. Assuming a reasonable degree of effective governance and accountability on the part of the recipient state, the latter goal — in effect ending counterpart funds as a means of channelling counterpart receipt flows — would appear desirable.

However, some recipient states are not noted for accountability or good governance and some donors perceive themselves as having vested interests in controlling (or appearing to control) the uses of funds derived from the sale of their grant or soft loan assistance. In such cases, a conflict is likely to exist between effective control and assisting in capacitating the recipient state. Tight limits on spending, externally designed rules on monetisation procedures, substantial expatriate involvement in all stages of transfer-monetisation-spending, and preparing special accounts to a format quite different from the basic national budgetary one, all marginalize and fragment the recipient and reduce its capacity for good governance.

Despite these potential contradictions, there are a number of areas on which operational reform of the counterpart fund process and of overall dialogue leading to practice on spending should be both attainable and attained. Further, that process would help clarify more basic issues and, perhaps, thereby facilitate their longer term resolution (cf. e.g. Riley 1990).

3 MACRO TO CF: SOME LINKS AND ISSUES

3.1 The initial CF question is generation. This requires either specific (e.g. food) or generalized (e.g. import support) commodity transfers which are made to a recipient state which monetises them by sales to enterprises or households. To be an efficient component in meeting import capacity requirements all commodity aid needs to be in the framework of broadly agreed financial and commodity requirements. Similarly, CF levels — as a whole
— should be related to an agreed estimate of government financing needs to provide broadly agreed levels of services. In practice, not all resource transfers are CA nor are most government receipts from CFs (under 5 per cent in most cases albeit 15 per cent to 25 per cent in a few) so that the exercise is both difficult and, at specific CA/CF level, inherently requiring flexibility and, therefore, at risk from fungibility (or made efficient by fungibility if one assumes the recipient has sensible import and expenditure priorities and procedures!).

3.2 Monetisation is necessary for CFs (albeit not for CA directed to government — e.g. pharmaceuticals — or final beneficiary — e.g. potential famine victim — use). It is also necessary for efficiency and cost control in distribution, sustaining or enhancing the domestic marketing system and providing a framework within which to provide positive incentives to domestic production.

For food aid, the usual logical pattern is sale of physical food in urban areas with the proceeds used to buy domestically as near vulnerable populations as possible. Indeed, if domestic markets are in working order, paying wages to recipients to buy food (if necessarily partly supplied by food aid) makes better sense than traditional food for work (cf. World Bank/WFP 1990; Green 1986).

3.3 Collection and release of CF revenues are integral to avoiding deflationary/inflationary sequences from lags, as well as to the allocation of domestic state expenditure provided for under the CF agreement being effective. The lags result from the state being the de facto working capital supplier to wholesalers, manufacturers and retailers (public or private sector) buying the goods. IMF credit ceilings set with no real attention to working capital requirements, government sloth in collection and purchaser desire for interest free, extended credit contribute to that result.

If possible, the state should sell to wholesalers for cash with the wholesalers using commercial bank credit to pay and repeating the process vis-à-vis retailers. If this is not practicable, then credit periods (say 60 days) for wholesalers should be set by the state selling unit and analogous ones (say 30 days average) by wholesalers to retailers. Given off-loading/sale to wholesaler time that implies 120 days from CA arrival to CF receipts.

3.4 The public/private issue need not be central on the recipient side. In terms of physical use, monetised commodity aid is used by the private sector. Retailing usually, and wholesaling sometimes, is by private sector enterprises. The CF revenue utilization by the state is — or can be — perfectly consistent with providing human investment, basic services and safety nets, physical infrastructure and enabling policies which stimulate enterprise and household initiatives and production growth (cf. World Bank 1989).

The donor side has a more integral — and distorting — public sector involvement. Much commodity aid (food, fertiliser and some import support) is enmeshed in national production support and support cost minimization (or transfer to another budget head, such as aid). The lack of attention to normal contractual provisions safeguarding the recipients (as to suitability, quality, arrival date, loss en route) are a function of donor bureaucracy which would not apply were the recipient free to buy from a low cost source and secure a normal commercial contract.

Commodity aid can also seriously damage third party (often Southern) potential suppliers who cannot afford to provide soft loans or grants. This can be offset by triangular transactions (e.g. EEC, Netherlands, USA and Australia's grain purchases in Zimbabwe for Southern African food deficit states) but that remains the exception not the rule (as Australia, Thailand and Argentina have repeatedly pointed out with limited results).

Positively, public sector involvement is needed if 'fair' (breakeven but below scarcity or imperfect market) prices or selectively subsidised (e.g. inferior staple) prices are desired. Payment has to be by the donor or recipient public sector and distribution via a monitored (albeit quite possibly private) selling structure. In practice a CF may be a useful means to finance such a subsidy (billing the CA at commercial cost and then financing the agreed subsidy expenditure as back to back transactions in a way beneficial to transparency and accountability with minimal personnel or procedural cost).

3.5 Valuation should be at commercial border price for low cost sources and routes — which may not be the book value as seen by the donor. Any other valuation is inherently distorting. However, that assumes a plausible exchange rate. CA/CF negotiations are a very poor forum for setting
exchange rates, but severe over-valuation does reduce CF purchasing power and provides an implicit subsidy to the CA users which may or may not be desirable, depending on who they are.

3.6 But CF receipts are not the only price issue relevant to CA/CF. If a 'fair' or 'free market' price interacts with domestic security, transport and/or production problems to create a ruinous domestic grower price, then food aid (or other commodity aid by analogy) may act as a disincentive and distort production structures. Using CF (or other) funding to offset abnormal costs, to bolster producer prices in the short run, and to invest in cost reducing means to remove the distortion in the medium, is a possible approach. It is worth noting that this distortion effect is particularly likely if exchange rates are severely over-valued and the commodity provided is a close substitute for a different domestic one (e.g. wheat for sorghum and millet in the Sudan and Somalia). The cost reduction use of CF is an example of the need to view producer incentives more broadly than a unique focus on prices — costs and ability to respond to prices also matter, for SSA food producers usually more than prices taken in isolation.

3.7 CF use need not in macroeconomic logic have any relationship to the commodity providing the domestic currency flow and still less to projects or programmes whose import costs are financed by the particular CA donor. However, in practice some links may be psychologically or politically useful. Two examples are, first, the use of CF (especially from food aid) to increase entitlements of absolutely poor households by funding extension of basic services and, secondly, holistic support packages with project — technical assistance — domestic currency (from CF) components.

3.8 Accounting and reporting are essential to accountability in both the narrow and the broad senses and for both providers and recipients. In principle, they should be an integral part of a coherent recipient government accounting and reporting system, with any alterations to other formats made by the donors. In practice, donors insist on reports in their own, very diverse, formats and make limited progress in trying to coordinate among themselves, still less with recipient systems (cf. Riley 1990; Riley et al 1990). Many recipient accounting/reporting systems are ill-designed and/or inadequately operated. The hauling out of portions of accounts and reports in separate systems to satisfy (or fail to satisfy) donors has the result of further enfeebling and decapacitating the overall national system to which they should relate.

3.9 Coordination goes beyond accounting. Logically it means integrating CA provision and CF utilization into an agreed medium term macro and sectoral economic strategy with rolling budget on both the external and fiscal sides. That implies the dialogue should be around the national import and government expenditure budgets and the policies underlying them. In practice this rarely happens — at least explicitly. Donor coordination tends to focus on increasing ease of CF operation and effectiveness of CF policy leverage as perceived by them. Consultative Groups rarely handle CA in any detail and tend to focus on PFP (priority public investment finance programme), not foreign exchange and fiscal budgets.

3.10 NGOs have become a factor in CF discussion because they are a current fashion, are sometimes financed by CFs and have CF relationships which tend to hamper most streamlining and coordination proposals. In practice, the discussion has turned on external NGOs, whereas logic would suggest CF allocations should be to domestic NGOs. In either case coherence and accountability suggest that transfers to NGOs should go via the CF to the domestic government budget and thence to the NGOs and that the level of allocations to them should be negotiated in the same way as of those to, e.g. basic health services, rural public works, primary education or agricultural extension.

4 TOWARD IMPROVED CA/CF USE

Proposals for CA/CF improvement are necessarily general if written at the level of CA to and CFs in SSA. In any particular case, some variations are likely to be necessary and/or appropriate.

One fairly general set of exceptions exists in respect of donors for whom and countries to which commodity aid is a small proportion of total recipient fiscal operations. In these cases, the administrative nuisances and institutional time opportunity costs of running CFs are large enough relative to gains that allowing CA monetisation proceeds to go direct to general revenue would appear optimal, with the most plausible alternative being direction of all CF type receipts to NGO programme support.

A second exception concerns donors who are now willing to have CA (and Import Support) proceeds go
to general revenue after an overall dialogue on budgetary priorities and specific concerns within them. In these cases there is no very evident reason why they should set up 'their' or join in 'joint' CFs. Their perception that CFs do not in fact add to leverage in any way not better facilitated by dialogue is arguably correct, as has been pointed out forcefully in a recent consultant's report to the EEC (Goreux 1990). This view is, perhaps paradoxically, shared by the IMF for countries with which it has Programmes (see Clement 1989 and in this Bulletin) and would probably be supported by many World Bank officials in respect to at least some SAP/Consultative Group countries. Certainly the arguments of the Long Term Perspective Study (World Bank 1989) for backing ongoing country initiatives, not designing new conditional programmes externally, points in that direction.

The first main guideline for better CA/CF use is to start from nationally proposed, and subsequently agreed in dialogue with donors, foreign exchange and government source and uses budgets, covering combined import support, investment and emergency heads on the external side and recurrent, capital and emergency (or calamity) on the government side.

From that base a real resource transfer and a real augmentation of government revenue target can be derived. At that point it is appropriate to identify commodities available for CF purposes which are needed in the recipient and not available domestically which could be supplied by CA in addition (or largely in addition) to financial transfers and which would not cost substantially more on CA terms than the financial counterpart of low cost source commercial purchases. The main commodities in this cluster are likely to be maize, wheat, rice, vegetable oil, sugar and milk powder, albeit, for specific countries at specific times, other standardized commodities (including fertilisers, newsprint, textbooks papers and pharmaceuticals) may also figure.

To the extent the commodities are not for direct government or refugee/disaster victim consumption, a strong case exists for monetisation (see World Bank/World Food Programme 1991). In that case the proceeds become part of the resources available for meeting the augmentation of government revenue target. Assuming that the overall foreign exchange requirements have been estimated with reasonable accuracy, they can be expended on government domestic purposes without directly or indirectly unbalancing the external accounts. Bringing CA direct to project or programme on budget involves only nominal monetisation, e.g. back to back cheques from Finance to Health and Health to Finance for donated drugs. Its value is in providing accountability — an intelligible, complete picture of sources and uses both ex ante and ex post.

This exercise should end with a set of foreign exchange/external resource commitments equal to the pre-exercise external gap, and with a set of commitments to government revenue equal to the pre-exercise government funding gap. These will not necessarily be the same sum; indeed they will not be unless all external grants and loans to enterprises/households are put through the budget which is rather unlikely.

Because the exercise has some aspects of a jigsaw puzzle, it needs for efficiency's sake to be done at one place and time, with as few details and loose pieces as possible needing to be followed up later. This implies the locus should be at an annual Consultative Group/Forum meeting of the recipient with its external cooperating partners. The central working documents (external and governmental budgets), and their back-up studies of programmes and projects plus the overall strategy paper informing them, should be presented by the recipient. No other entry point is capable of generating a full capacitating process, nor of making the government feel the agreed programmes belong to it.

In the SSA context, these guidelines would be consistent with substantially more food aid and balance of payments support transfers. However, that is likely to be efficient only if food aid is billed for CF purposes at low cost commercial source c.i.f. price; if balance of payments support is freely usable on whatever exports from the donor are actually competitive (or better still is untied); and if triangular food aid is expanded and made standard practice in respect to buying from maize and sorghum/millet surplus countries with a view to establishing subsequent commercial intra-African grain trading and physical food security interaction.

CFs should receive the c.i.f. commercial price value of monetised CA promptly. It should then flow into the budgetary process — to pre-agreed users — automatically. That requires an annual estimation exercise (including unused balances and desired end of year balances to provide a cushion against sharp, short term instability in transfers), not budgeting past livelihood rehabilitation, might reduce this target to 11 million tonnes a year versus 5 million actual average 1984/89 food aid deliveries. (See Green 1991:31, and sources cited there for greater detail.)
receipts which enforces an 18 month lag from sale to release.

CA/CF programming should be set up to minimize unintended distortions, consistent with meeting resource allocation and human condition targets.\(^2\) Nationally, this does not rule out ‘fair price’ systems or self-targeting (e.g. ‘inferior staple’) subsidies, nor financing safety net income transfers from CFs, but does warn against pricing and procurement which disable domestic markets and de-incentivize domestic producers. Globally, it implies third country procurement, whenever this is the least cost source, and some margin above that for enabling the build-up of sustainable regional trade in food and food security programming.

CF use should be in the context of overall project/programme requirements to attain strategic aims. Any agreed domestic currency cost head may be suitable. Both psychological/symbolic and convenience/technical efficiency reasons do suggest some packaging may be useful, e.g. of food aid and rural development or of CF, and perhaps CA, with financial transfers from a single donor to a single project or programme.

The purposes of accounting and reporting are to ensure comprehensive transparency and accountability (in the broader sense). Proper budgetary processes at analytical, formulation, allocation, funding, disbursement, monitoring and evaluation turn on adequate, timely accounting and reporting (on real as well as financial out-turn with divergences from targets explained).

In many SSA countries, to achieve these standards requires alteration or broadening of present systems. For example, it should be possible to determine rapidly at national, provincial and — for most programmes, e.g. primary health care, road maintenance — for what the physical as well as the financial performance was targeted to be and is. With computerized systems, this type of multiple pattern retrieval is simple if the initial entry forms are properly devised. In virtually all SSA countries, more trained personnel and better equipment are needed to operate such systems. Both training/equipping and system improvement are logically mutual recipient/cooperating partner concerns and training at least is a logical CF allocation area.

CF reporting should provide data by programme, project and geographic unit (at least to province and perhaps district level) on receipt and disbursement by spending unit and on physical out-turn. Where CF is not the only funding source, the disbursement/physical out-turn data reasonably requireable are for the whole agreed programme/project not the CF component alone. CF reporting should be within the national accounting/reporting process and therefore should both be uniform and compatible with the recipient’s national governmental accounting/reporting coverage and format. Insistence on different coverages, formats and time periods by CA donors is a serious barrier to improving the national system and decapacitates recipient accounting and budgetary processes. It is this, and not multiple CF accounts, which is the basic problem to be faced and overcome.

Some SSA governments do not have coherent goals, plausible budgets or accounting processes and/or have revealed preferences in respect to additional spending which donors are not prepared to support. In such cases the process of integrating CA/CF into national strategies and of untying CFs has evident limitations and drawbacks. Capacity building assistance can allow a start to be made if the problems are of institutional strength, procedural design and personnel training and/or numbers. The bottom line problem is in respect to states whose goals CA providers decline to finance; but in whose programmes they find some activities they are willing to support. The problem is real but not unique to CA/CF; nor soluble primarily in that context.

The use of CA/CF to facilitate implementation of national strategies supported by donors articulated via specific projects and programmes is impossible without coordination. Ongoing monitoring and problem resolution needs to be primarily recipient country based. To be effective and/or capacitating it also needs to be recipient led and driven, even though to a significant extent it will need to be donor serviced and fuelled.

These proposals are neither instantly attainable nor ‘academic’ or ‘long term goal’ in nature. Each could be implemented to some degree now in the majority of SSA states and all have a case for priority implementation, in full or large measure, over five years. Accepting and beginning to act on them now would provide time and incentives for recipient capacity building and supplier rethinking of procedures.

\(^2\) Like ‘treason’, ‘distortions’ never flourish. If intended they are described as allocations or interventions to redress market failure, to offset undesired side effects of other interventions or to provide safety nets.
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