

STATE 189715
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From: USAID Administrator

THE ROLE OF RESOURCE TRANSFERS IN U.S. ECONOMIC ASSISTANCE

1. I have been concerned about a number of current and planned USAID-funded projects and programs that provide substantial amounts of resources to governments for commodities, physical capital or credit with inadequate attention to the effectiveness with which such resources are employed. Scarce USAID resources should have the maximum possible sustained impact on the recipient country's development. This means we need to ensure that our assistance: (a) is provided in a sound, market-oriented economic policy environment that reinforces its development impact, or is provided in a way that leads the country to undertake the reforms that produce such an environment; (b) strengthens the country's private and public institutional capacity to solve its developmental problems; and (c) results in widespread application of more productive technology that accelerates the growth of production, employment and incomes.

2. I recognize that this is a complex area and that major USAID policy papers addressing several of these subjects in greater depth have recently been approved for transmittal to the field. These include policy papers on approaches to policy dialogue, private enterprise development and institutional development. These papers should be read along with the following guidance, which seeks to provide some clarification of my concerns about resource transfers and the circumstances under which we provide them.

3. Strictly speaking, all forms of concessional assistance involve a transfer of resources, even if only the funds to cover the costs of training and technical expertise for technical assistance. Resource transfers in the sense used here refer explicitly to USAID-funded projects and programs, including DA, ESF, PL 480 and HIGS, that provide substantial amounts of resources for the importation of commodities and capital equipment as well as local costs for construction, credit and recurrent expenses.

4. To help ensure that resource transfers have the greatest positive developmental impact, USAID's programs and projects have been linked to technical or institutional change or policy reform. For example, many USAID projects combine a resource transfer with technical assistance leading to technical and institutional change -- e.g., financial assistance to construct or rehabilitate physical structures of a

irrigation system linked to technical assistance and training (human capital formation) to strengthen the public and private institutions (e.g., water user associations) required for improved water management. Similarly, policy changes linked to resource transfers can improve their effectiveness and lasting impact --e.g., elimination of subsidies or converting to private sector distribution as part of fertilizer assistance; interest rate reform as part of assistance for agricultural credit.

5. Accordingly, USAID will provide resource transfers when: (a) other sources of financing have first been explored, including possible co-financing arrangements between USAID, other donors and/or private sources; and (b) such assistance is linked to changes or effective performance (as agreed by USAID and the recipient country) in the areas of institutional development - technology transfer or technology development, and/or economic policy. Country performance will be closely monitored and evaluated to determine whether such assistance should be continued.

6. These requirements must be satisfied unless justified by exceptional circumstances, such as the existence of over-riding foreign policy objectives. The burden of proof in such cases will rest with the mission.

7. In general, economic policy, technical and institutional changes that (a) support sustained, broadly-based economic growth; (b) strengthen free markets and encourage private enterprise; (c) stimulate savings, investment and employment; (d) result in the development, transfer, adaptation and/or application of more productive technology; and (d) encourage local community initiative are desirable and therefore legitimate subjects for policy dialogue between missions, governments and other donors.

8. While I believe that most country and project situations that we encounter present opportunities for needed policy changes that will increase the effectiveness of our resource transfers, I also want to observe that policy change is not, repeat, not at end in itself but rather a means to achieving development objectives. Therefore, missions should not view the emphasis on policy change as a mechanical, "checklist" requirement. If a mission believes the policy environment for the provision of assistance is adequate, it may take this position but it must explain why this is so.

9. Furthermore, the policy dialogue must be selective. That is, the desire policy change or changes must (a) be important for the accomplishment of the intended development objectives of the proposed economic assistance; (b) represent real, not trivial, differences between USAID and the host government; and (c) be amenable to host government action in existing political and socio-economic settings. These and

other considerations important to the conduct of policy dialogue are thoroughly treated in the forthcoming policy paper on approaches to policy dialogue.

10. Some illustrative examples of projects with varying degrees of effective linkages to policy, technological or institutional change are presented below. These examples are purely illustrative and are intended merely to suggest only a few of the ways such linkages have (or have not) been established:

(a) The DA funded fertilizer distribution and improvement project in Bangladesh constitutes a positive example. The project (1) induced the government to transfer retail and first level wholesale distribution from the government to the private sector; (2) strengthens the Bangladesh government's technical ability to assess programs and to assess the economics and technical characteristics of different fertilizers. An extension included agreement to test the de-control of retail prices of fertilizer in one of the country's four regions as a condition precedent to the project.

(b) On the other hand, a project for fertilizer imports in India was not approved for the last tranche on the grounds that it did not involve policy or institutional reforms or technology transfer, including any reforms that would have de-controlled prices or increased private enterprise participation in the fertilizer sector.

(c) The Rajasthan medium irrigation project in India is a positive example that involves, along with financial assistance for construction, significant improvements in the planning and design of irrigation projects at the state level, e.g., bringing water closer to the farm (by servicing smaller units), using more supervisory engineers in the field, and paying greater attention to related inputs such as fertilizer and agricultural extension services.

(d) Balance of payments support to Jamaica to assist the country's new government in its efforts to bring about economic recovery and re-expansion of the private sector required acceptance of the macro-economic policy framework negotiated by the IMF and World Bank. A condition for disbursement of the major portion of the first USAID cash transfer funded by ESF was acceptance by the government of Jamaica of the terms of an IMF extended fund facility loan. Two conditions precedent to disbursement of the major portion of the second cash transfer were compliance with the conditions of agreement with the IMF, and agreement by the government of Jamaica to the terms of a proposed World Bank structural adjustment loan.

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(e) The Senegal PL 480 Title III program calls for reform in three areas: (1) decentralization of development through reform of government regional development agencies and encouragement of greater farmer and private sector initiatives; (2) reform of rural cooperatives, including expansion of functions and greater responsibility at the village level; and (3) review of marketing and pricing policies in order to expand agricultural production and diversification.