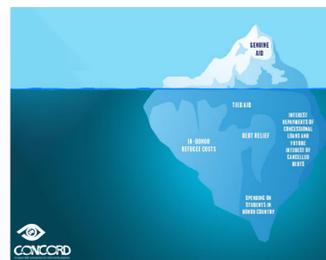
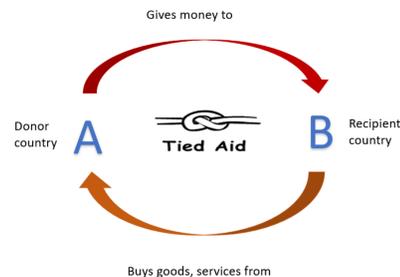


How private sector instruments could threaten progress on aid untying: A key question for the ownership agenda

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Background – The increasing role of the private sector in development

- Since its creation in 1961, the OECD Development Assistance Committee (DAC) has worked to improve the effectiveness of aid, including the untying of aid – i.e. removing the legal and regulatory barriers to open competition for aid-funded procurement. This work culminated in a 2001 Recommendation to Untie Official Development Assistance (ODA) to the Least Developed Countries, which has been updated since then. This recommendation has led to some improvements in the levels of untied aid. However, additional efforts are needed to fully untie aid formally and informally.
- In 2018, OECD DAC members agreed reporting rules for Private Sector Instruments (PSI) as ODA. Eurodad research shows that the reporting of PSIs is already undermining the quantity and quality of ODA (Caio, C. & Craviotto, N., 2021). This is part of a broader trend that is weakening the quality of aid (Craviotto, N., 2022).



Purpose of this research

- Understand the threats to (formal and informal) tied aid emanating from the reporting of Private Sector Instruments (PSIs) operations as aid.

Research questions & Methods

Research questions

- What do the latest figures on tied aid tell us regarding both formal and informal tied aid?
- What are the issues at stake for formal and informal tied aid, particularly in connection to the current discussions and potential negotiations that shall lead to a permanent agreement on the reporting PSIs?

Methods

- Review of key standards on tied aid and its reporting, primarily those contained within the OECD DAC Statistical Reporting Directives and their addenda, and key international agreements on effective development cooperation and on financing for development; review of the OECD-DAC agreement on the reporting of PSIs as ODA.
- Data research and analysis, notably the analysis of quantitative data from the DAC's 2020 Report on the DAC Recommendation on Untying, and ODA statistics from the OECD Creditor Reporting System (CRS).
- Interviews with relevant stakeholders and peer review process with experts in the field.

1. Latest trends in formal and informal tied aid

- In 2018, DAC members reported US\$22.1 billion of tied aid. In 2016, ODA reported as tied was US\$ 25 billion (approx).
- However, there is also “informal” tied aid – i.e. procurement processes linked to aid projects that can create informal barriers for suppliers outside the DAC member country to access contract opportunities under the scope of the aid project. This can be tracked for example, by investigating where contracts are actually awarded in practice.
- Our research shows that 52 per cent of all untied contract awards reported to the DAC were awarded to suppliers in the DAC member's own country. In contrast, only 11 per cent of reported untied contract awards went to suppliers in Less Developed Countries (LDCs) and Heavily Indebted Poor Countries (HIPC). In 2016, these figures were 51 per cent and 7 per cent respectively.
- We estimate that the total level of formally and informally tied aid in 2018 was minimum US\$32.3 billion.
- The following Table shows that tied aid translates into very real costs for people in the global south. Our estimate indicates that, in 2018 alone, the direct short-term cost of this practice was at least US\$1.7 billion and potentially as much as US\$6.7 billion (due to tied aid being prioritised instead of cost). Using the same methodology and range of assumptions, the equivalent figures in 2016 would have been US\$1.9 billion and US\$5.8 billion (rising to US\$6.2 billion if slightly less cautious assumptions are used).
- These figures suggest that despite small fluctuations there has been little progress in improving formal and informal tied aid levels, which has important costs for people in the global south.

Estimated short-term direct costs of tying ODA in 2018

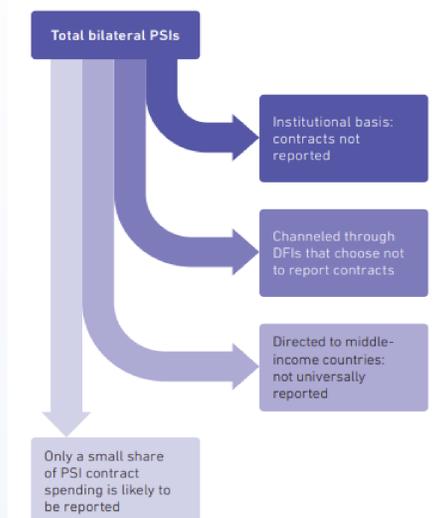
	Price would have been prioritised in 1/3 of spending	Price would have been prioritised in 100% of spending
Total tying (minimum) = US\$27.5bn	US\$2.0 billion	US\$5.9 billion
Total tying (illustrative) = US\$36.3bn	US\$2.3 billion	US\$7.0 billion

2. Tied Aid in the context of ODA channelled through Private Sector Instruments

Since 2018 DAC members can report the use of PSIs – such as loans to the private sector, guarantees, equities and mezzanine finance – as ODA. Our research identifies three overlapping sets of risks that threaten to increase tied aid levels in the years to come:

- Risk-1:** Some key stakeholders, such as Development Finance Institutions, grapple with a potential tension between the objective of contributing to the economic development of countries in the Global South, versus the objective of supporting the expansion of firms from their countries, which affects the governance and ownership of development projects.
- Risk 2:** Transparency risks. The requirements in the “untying recommendation” could be bypassed in the case of PSIs operations (see figure here).
- Risk 3:** The expansion of the definition of ODA for PSI operations from concessionality to additionality. This could bring additional tied aid into ODA. Eurodad is concerned about the fact that export credits operations could be reported as ODA (in 2019 export credit operations amounted a total of US\$ 53 billion reported as aid).

DAC Recommendation on Untying Aid – only a small share of PSI contract spending is likely to be reported



3. Policy implications and key measures relevant to this agenda

- Donors need to adopt mechanisms to mitigate the risk that governance-related aspects of PSIs lead to increased levels of tied aid.
- Any further agreement on PSIs needs to state clearly that benefits for domestic firms should never be an objective of PSI schemes.
- Donors need to tackle the transparency risks related to the monitoring of formal and informally tied aid in PSIs.
- Donors need to tackle the ODA definitional risks related to potential changes in the rules for reporting PSI.

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