POVERTY AND FOREIGN AID: POLICY TRADE-OFF

Economic Theory

by YULIA MINAEVA

4244348

Major Paper presented to the

Department of Economics of the University of Ottawa

in partial fulfillment of the requirements of the M.A. Degree

Supervisor: Professor Yazid Dissou

ECO 7997

Ottawa, Ontario

August 2007

Table of Content

List of Tables

List of Figures

1. Introduction

For more than four decades, a key feature of the Third World has been the aid relationship with donor countries. Foreign aid is a complex international process through which several billions of dollars are provided to developing countries every year and hundreds of thousands of people are employed in this global multilateral organization (Hjertholm and White, 1998, 3). Over the years foreign aid regime has fundamentally redirected its original focus from the reconstruction of European countries' infrastructure in the 1950-60s toward implementing Structural Adjustment Programs (SAP) in the 1980-90s and applying participative anti-poverty policy at the international level at the end of the century.

Notwithstanding these changes in historical trends, the ability of foreign assistance to meet the shortage of capital, foreign exchange and technical knowledge, as well as to provide public goods and social overhead capital i.e. communication systems and law enforcement to less-fortunate nations, has been of significant importance (Sandler and Arce, 2007). Nowadays poverty alleviation packages encompass bilateral and multilateral funding, grants, technical assistance, and debt relief programs. However Official Development Assistance (ODA) supplied by the Organization for Economic Cooperation and Development (OECD) member countries accounts for 70 percent of the total aid industry.

A lively debate on the effectiveness of foreign aid, or the lack of it, has been developed both in academia and among practitioners as several resources had been devoted to various aid programs and most of the developing countries became heavily dependent on them. Even if the result has been mixed, this debate has brought about a new and interesting analytical focus on the role of involved financial institutions and on the incentive structures targeting the poverty alleviation. Several researchers believe that aid essentially has positive impact on growth in typical policy environments (regarded as a combination of budget surplus, inflation and openness) (Burnside and Dollar, 2000) and that is why significant increase in foreign aid and investment across the board is vital for poverty eradication (Sachs, 2005). Moreover, aid would be more efficient if it was distributed in the form of "short-impact" aid package –typically four years (Clemens et al., 2004) or in the form of ex-post (based on relative performance) as opposed to ex-ante (conditional on reform or outcome) (Svensson, 2003b).

On the contrary, the critics of aid programs are based on the three following arguments. According to the first argument, poverty is caused by distortionary policies introduced by politicians, so that in this framework aid increases consumption and does not promote economic development (Boone, 1996a). The second argument assigns all the responsibility for policy and institutional aid failures on the recipient governments as a result of their persistent dysfunctional behavior such as corruption, misspending and transfer of the recourses (Paul, 2006). Nevertheless, donor countries do not deploy less foreign aid to more corrupt governments (Alesina and Weder, 2002) and rent-seeking persists as a serious problem in the developing world (Svensson, 2000). Consistent with the third argument aid does not necessarily work better in an improved policy environment (Rajan and Subramanian, 2005; Burnside and Dollar, 2000; Easterly et al., 2004b) or with increased intensity of structural adjustment lending (Easterly, 2005c). More recent research conducted by (Pattillo et al., 2007) questioned the findings obtained by (Burnside and Dollar, 2000 and Easterly et al., 2004b) and ascertained significant pitfalls in the applied calculation technique that does not leave a solid ground for the justification of their results.

The motivation for this study is captured by a substantial controversy in academic literature over the effectiveness of foreign aid which, in turn, suggests the need for a critical reassessment of donors' approach to poverty reduction. It is understood that the relations between foreign financial aid and elimination of poverty are rather complex, as they involve numerous socio-economic and political factors, and addressing all these areas of interest is not practical in an individual research framework. Given the fact that the inefficiency of foreign aid policies have been just admitted and declared by donor countries, this paper attempts to make a contribution to clarify the causes behind foreign aid failures as well as the future of foreign aid by conducting comprehensive research on this area and encompassing the following objectives: (i) analyze the historical trends in the volume and composition of foreign aid, (ii) review empirical studies on the impact of aid on growth in developing and transition economies, and (iii) examine aid policies undertaken by the bilateral and multilateral financial agencies in regards of the developing countries with a special emphasis on the Russian Federation between 1991 and 1998.

This paper does not provide an economic guideline to address issues such as the desirability of increasing aid. The author acknowledges the relevance of an amount of aid to be provided, yet strongly believes that the donors motivation, structure, technique and conditions of foreign aid play more important role in bailing out developing countries. A special emphasis is placed on the role of foreign aid in the transition of the Russian Federation towards market economy and on disproving the myth that "aid has no impact on recipient countries".

The remaining of the paper is as follows. Section two explores different features of foreign aid and summarizes the most important results of the available literature on foreign assistance. Section three provides evidence on bilateral aggregate aid flows and deliberates a particularly acute problem of aid allocation as well as investigates the philosophy of the IMF programs for transition economies, its social and macroeconomic consequences on the example of the Russian Federation. Also the future challenges and some policy implications are addressed taking into account the lessons learned from the previous practices. Section four concludes.

2. Characteristics of Foreign Aid

2.1. Classification of Foreign Aid

The first prerequisite for the development of a sound foreign aid policy is the recognition of the diversity of aid programs. Despite the multiplicity of foreign aid categories and the various objectives they pursue, there is one common aspect in all aid packages: the transfer of goods, financial resources or services from one government to another. Also there are certain criteria that should be implemented by the recipients in return of donors' financial assistance such as: (i) conditionality that requires recipient countries to carry out adjustment policies, and/or (ii) restrictions that predetermine the expenditure type, and / or (iii) accountability that implies disbursement and audit of provided funds. Although this paper distinguishes among different types of foreign flows, it must be mentioned that in the real world, countries are always engaged in a provision of foreign aid mixture. Nevertheless, the provision of funding must be hinged on the evaluation of previous donors' achievements as well as on the existing gap in order to avoid overlapping policy decisions.

Foster and Leavy (2001) made a successful attempt to classify the instruments for delivering aid. They differentiated the following six forms: (i) balance of payment support and/or (ii) general budget support, (iii) aid funded debt relief, (iv) sectoral budget support, (v) project aid, (vi) funds form NGOs and (vii) multilateral aid. The first type is assigned for the support of policy reform measures. In general, it requires an application of the structural adjustment programs under the supervision of Bretton Woods sister institutions- the World Bank and the IMF. The onset of this assistance began in the early 1980s and primarily, it was a chance for developing world to decrease debt burden and to adjust trade balances. In the case of general budget support, the conditionality mainly includes agreement to the overall budget priorities, as set out, for instance, in a medium budget and expenditure framework.

The debt relief program was launched in 1996 by the World Bank and was intended for the heavily indebted poor countries (HIPCs). As of this year, 31 countries have already received this program and 10 countries are potentially eligible for it (World Bank, 2007e) . In order to be qualified for HIPC category a country must face unsustainable debt situation. Unsustainable debt situation implies that country's debt-to-export level is above a fixed ratio of 150 percent (World Bank, 2007). Moreover the prerequisite for lending is a development of Poverty Reduction Strategy Paper (PRSP) by recipient country and reconsideration as well as reduction of expenditure sector. From another perspective, unsustainable debt can be perceived as a financial liability that government will not be able to fulfill in the future. In this case large debt accumulation would serve as a hindrance for private sector investment because the government would have to raise tax burden to discharge its debt obligations. In general, the economies of the heavily indebted countries are more vulnerable for external shocks and depend continuously on the donors' financial assistance. From another point of view, debt relief refers to a moral hazard problem as it may encourage other countries to avoid debt servicing. In fact some countries prefer to be qualified for this category because once they are excluded they have to meet their financial obligations. A new debt relief program called the Multilateral Debt Relief Initiative (MDRI) was launched in 2006.

The sectoral budget support is very similar to the general budget support but it assigns the donors aid to specific expenditure categories within the particular sector of the economy. The project aid is a spending proposal designed and appraised by the donors. As usual, donor countries determine the disbursement procedures, and specific project account may be required. The controls over project as well as an assessment of the inputs and contribution are among donors' responsibilities. The project aid will result in a readjustment of government policy (Hefeker, 2006).

The growing role of the provision of aid service through non-government channels to developing countries is a subject of recent attention. There are numerous classifications of NGOs and the most part of them is recognized all over the world. It is a commonly used perception that these organizations can better reflect the interests of the poor. However, this guidance does not address supply of aid via Non-Government organizations.

Another category of aid is provided by the multilateral financial institutions such as African Development Bank, Asian Development Bank, European Bank for Reconstruction and Development, the WB, the IMF and etc. that are governed by the contributing countries. According to the fact that developed countries allocate their aid resources to some extent via multilateral institutions and partly through bilateral channels, it is very important to consider the linkage among these flows. The existence of multilateral institutions allows bilateral donors to express through dialog and coordination of efforts their views, commitments and capacities. This, in turn, ensures sound improvement in the development of aid mechanisms and precise resource allocation. (Dreher and Jensen, 2007; and Fleck and Kilby, 2006) considered the impact of member countries on the policy choice supported by the international financial institutions (IFIs). They concluded that in most cases policy decisions made by financial institutions are distorted by the influential member countries who are inclined to channel as much aid as possible toward supporting their own political and economic interests.

In addition to aforesaid (Sharma, 1997) identified the following external resource flows: (i) bilateral official development assistance (ODA), (ii) private direct foreign investment from transnational corporations (TNCs), and (iii) food aid and/or other types of humanitarian aid. Food aid is mostly defined as free, subsidized, or below the market price, cheap staple food supplied by rich countries to poor countries for emergency relief. The technical assistance that represents another type of aid can be described as a relocation of the educated personnel into developing countries to assist with a program of development.

The bilateral official development assistance (ODA) has been provided by 30 member countries of the Organization for Economic Cooperation and Development (OECD) to the underdeveloped ones and is of a particular interest. The OECD (2007) defined aid as: (i) it must be undertaken by the official sector; (ii) it should promote economic development and welfare as the main objective; (iii) it should have a 'grant element' of 25% or more. The framework of this development assistance needs to be understood in the context of Cold War. Over the last 20 years, annual ODA assistance has been between \$50bn and \$60bn but has reached over \$100bn in 2005. As one of the world's largest sources of the financial resources, the OECD has an important role to play in addressing the improvement of policy coherence and social and economic imbalances in the developing countries. The participation of the OECD countries in the development process and poverty alleviation programs suggests the need for further investigation of the historical trends of foreign aid flows in the following section.

2.2. History of Foreign Aid

The foreign aid regime has undergone a number of significant changes over the years. Understanding the evolution of foreign aid brings to light how every period in the history of aid has responded to the transformation of the needs of societies. This vision helps to build a better bridge between the foreign policies of the involved countries and the trends of foreign aid programs. Despite the fact that aid flows were initiated in the nineteenth century and further developed through until current era, the Second World War seems to be a turning point in the history of foreign aid. For this reason, this paper will focus on the evolution of aid policies in the postwar era. The important tools of today's aid structure were established in a wake of this military worldwide conflict. The unstable currency exchange rates, the absence of an intergovernmental consultation institution and the usage of restricted trade policies significantly exacerbated the global economic situation in the interwar years.

The Bretton Woods conference was held in July 1944 in New Hampshire to discuss the post -war reconstruction of Europe as well as the creation of new international financial institutions that would stabilize exchange rates and boost international trade. To facilitate these objectives Bretton Woods Agreement signed by the delegates of 45 countries created two international financial institutions: the International Monetary Fund (IMF) and the International Bank for Reconstruction and Development (IBRD: later known as the World Bank). The IMF was financed by the member countries contributions "quotas" in gold and their own currencies. In case of payment problem each county had had to withdrawal 25% of its quota immediately. The primary objective of the IMF was to advise countries with the imbalance of financial payments, export and import disproportion and basically wherever there was a chance to remedy the economic disorder through purchasing a foreign currency with gold or the member's national currency (Fieleke, 1994). It is worth noticing that at the very beginning the IMF mandate was not provisional to impose any policy reforms or to interfere with countries' internal affairs.

The IMF sister institution the World Bank was also established to support the reconstruction of Europe and Japan after World War II. The IBRD was involved in financing at reasonable rates of interest large scale infrastructure projects such as building airports, dams, highways, and etc. Later on as Japan and European countries reached certain levels of income per capita the World Bank redirected its focus entirely on developing countries. After 1941, the IRBD expanded its structure to the group of development agencies. Since the early 1990s it has been providing financing to the post-socialist states of Eastern Europe and the former Soviet Union. The IBRD's current mandate essentially involves alleviation of worldwide poverty by promoting sustainable development through loans, risk management products and advisory services (Noel and Therien, 1995).

Another important agency, nowadays known as the United Nations (UN), began its development during the war in 1943 as "The United Nations Relief and Rehabilitation Agency" (UNRRA). The UNRRA was engaged in providing a broad range of services to the post war countries. As such, the establishment of the UN and its charter was seen as a source of international development law which highlighted the "duty" of the society of states to promote co-operation in the economic and social fields (Jackson, 1990). The Marshall plan also known as the European Recovery Program was launched in June 1947 by General George C. Marshall and aimed at facilitating post war recovery in certain European countries. The huge success of Marshall Plan led to the consideration of the foreign aid as a part of its foreign policy. Between 1948 and 1952 the Marshall Plan provided transfers in the amount of US$13 billion which was equivalent to more than 2% of the USA's GNP (Wood, 1986). As far as it relates to the context of this study, it is particularly important to stress that the Marshall Plan made possible the constitution of "a body of operating principles and procedures that remain an integral part of the aid regime (Therien, 2002, 461)."

A final feature of the post-war international scene was to address the first wave of independence from colonial rule, creating a constituency for aid. The first meeting of the Non-Aligned Movement in 1955 gave a focus to this voice, as did the various members of the UN (Ehrenfeld, 2004). In short, 1940s can be described as planning donors' ideology focusing on reconstruction mainly through Marshall Aid Program.

Until 1955 about 90% of aid from developed countries was provided by three countries alone: the USA, the UK and France. The USA used it as an instrument of containment; the UK and France turned it into a substitute for colonial domination. The US foreign aid was targeted towards a group of countries located on the periphery of the Sino-Soviet block (OECD, 1986). In the early 1950s the Soviet Union launched a program of technical and economical assistance to the underdeveloped nations in the form of a low-interest loans or long –term commodity purchase agreements. With the collapse of Soviet Union the economic assistance was discontinued.

The 1960s can be considered as an onset of the bilateral programs. The motivation behind the bilateral programs was the US call for the proper sharing in the provision of aid assistance. As a result of the wave of independence, some of the already independent countries (notably India) that were struggling financially prompted the emergence of greater amounts of the bilateral programs (Hjertholm and White, 1998). Bilateral aid has been provided as a technical assistance, budget support or multilateral supported projects. The importance of the 1960s period was marked by the institutionalization of aid provision as countries began to create development agencies. For instance, in 1960 Canada set up an "External Aid Office" which was renamed in 1968 to Canadian International Development Agency (CIDA). In 1961 France established the Ministry for Cooperation responsible for the economic assistance to developing countries mainly African countries. The United Nation Development Program originated in 1965, the International Development Association (IDA) and the Development Assistance Committee (DAC) were established in the early beginning of 1960s accordingly. The foundation of the latter two organizations was very central to the history of aid regime as they led to the concentration of aid policies in developed countries. Basically, the lending was provided using two lending windows: IBRD – for middle income countries and IDA-to the poorest LDCS countries that lack creditworthiness to borrow from the World Bank. The IDA was created as a result of pressure from developing countries for a more accessible lending agency, lending without interest or at very low interest rates. The DAC was established as a principal branch of the Organization of Economic Cooperation and Development (OECD) for the purpose of monitoring and coordinating aid offered by the bilateral donors. By the end of 20th century the DAC has become one of the major institutions with regards to development aid.

After gold standard was eliminated in 1971 and replaced by a floating exchange rate regime, the IMF's mission with regards to the maintenance of currency value in relation to gold disappeared and the IMF role was limited to being a development bank for poor countries (Meltzer, 2000). The foreign aid spending shifted from Europe and Japan to poor countries in Sub-Saharan Africa and South Asia. By 1969, the aid system grew and its channels also multiplied and became tangled. There were calls for unnecessary duplication in economic reporting and feasibility studies (Cassen, 1994). In 1970, the UN development agencies accounted for more multilateral official development agencies than any other institutions. By 1978, however, they had been overtaken by the World Bank Group, while the regional development banks, such as the African Development Bank, the Asian Development Bank and the Arab Fund for Social and Economic Development, grew exponentially in their import (Cassen, 1994) Concisely, the era of 1970s was devoted to the expansion of multilateral agencies and to the re-evaluation of the aid policies from the past decades.

The 1980s period marked a turning point in the history of development assistance as the market-based policy reforms were introduced in many countries. Shortly after the end of Vietnam War in 1975 the early 1980s witnessed the debt crises as a result of simultaneous fall in commodities prices and a hike in the real interest rate. In turn, the developing countries faced the balance of payments problems accompanied by the accumulation of large external debts. The debt burden of the Third World increased from US$639 to US$1341 billion between 1980 and 1990 (Corbridge, 1993). In this climate of crisis, structural adjustment programs (SAP) monitored by the IMF and the World Bank were imposed to these countries as a prerequisite for obtaining foreign aid (Wood, 1986). The SAP and its impact on the recipient countries as well as the changing mandate of the sister institutions will be further discussed in details in section 3 of this paper.

Aside from the structural adjustment issue, (Non Governmental Organizations) NGOs also played a leadership role in the emergence of new priority areas, such as the protecting environment, supporting women and the promotion of human rights. The

1980s were characterized as the period of macroeconomic reforms and debt relief programs supported by the market-based donor principles. After 1989, issues such as democracy and human rights were voiced with rising intensity by the donors (Stokke1996). The end of Cold War began with a collapse of Berlin Wall in 1989 and concluded with the breakup of the Soviet Union into 15 sovereign countries in 1991.

Since the beginning of the 1990s the unprecedented changes from bipolar international system to the multipolarity in the world economy has brought a new issue to the debate in the history of foreign aid regime at the international level (Olsen, 1998). Yet some remarkable tendencies were dominating after the collapsed of the Soviet Union. The aid flows dropped significantly as a result of peace. The Eastern Europe and the countries of the Soviet Union were transformed from being aid donors to being aid recipients. The provision of foreign aid by donor countries was based on the good governance of the borrower country as opposed to the provision of aid during the 80^{th} that depended on the borrower regimes having good ties and friendly relationship with the West.

Whereas the 1980s and 1990s were accompanied by the concepts of structural adjustment and economic development, the end of the century experienced the creation of a global coalition against poverty. However, the provision of foreign aid is still based on the adoption of market-friendly policies. The new "millennium targets" were specified in the paper entitled *Shaping the 21st Century: The Contribution of Development Co-operation* (OECD–DAC, 1996). This report pinpointed some new priorities such as poverty reduction, social development and the environmental protection as the provisions related to foreign aid. Specific objectives such as the reduction by half of the proportion of impoverished people living on a dollar per day basis, the decrease in the infant mortality rate in developing countries by two third and the provision of a primary education for all were planned to be achieved by the end of 2015. It should be noticed that achievement of these goals by 2015 is greatly debated and questioned in the world. Therefore, the main features of the contemporary development aid transformed to "software" rather than "hardware" (Chang et al., 1999). By 2000 the consensus on the mentioned above targets had been broadened to incorporate the World Bank and International Monetary Fund in the process. World Bank devoted its World Development

Report to the acknowledgment of a large-scale impoverishment of the population and to the development of a poverty alleviation program as a key objective to achieve a reasonable economic development all over the world (World Bank, 2000b). After the terrorist attacks of September 11, 2001 a new approach quite similar to the logic of Cold War that considered foreign aid as a mere component of the security policies of the rich countries has been (Barber, 2002).

It remains to be a fact that poverty is unavoidably a moral and political concept. For whatever different purpose, it serves the interests of both borrower and lender countries, and hence is accordingly affected by their political objectives and moral aspirations. In order to analyze how the moral initiatives of countries can drive their political initiatives in the processes of participation in anti-poverty aid programs a comprehensive appreciation of the countries' political complexity is necessary. It implies the need for further extension of a broader political and economic study of the foreign aid impact on recipient countries as well as the borrower states. The interaction of global and local world views on this topic is discussed in the following section.

2.3. Literature Review

The role of foreign aid in the development of less-developed countries (LDCs) is of an obvious importance. Determining the optimal levels and the optimal allocations of aid across countries requires information on the effectiveness of different types of aid in recipient countries, and the channels through which they operate. A theoretical literature on the effectiveness of foreign aid is large and extensive; however, a recension of all previous studies in this paper is not practical. The context of all literature can be approximately divided into two categories: (i) the literature that covers the impact of foreign aid on the receiving countries and (ii) the literature that investigates the determinants of foreign aid, such as why and to whom donor countries deliver their financial resources.

In this section attention will be drawn to the first type of literature. Acknowledging the importance of the nexus between countries' prosperity and poverty alleviation, general empirical analysis have been concentrated on the macroeconomic side of aid transfers measuring the effects of aid on economic growth, savings, and investment in the recipient counties. Notwithstanding the fact that several key results have been established, it would be a fair statement that these findings have not yet arrived at a consensus. The following theoretical investigation is a part of relevant research that applies the tools of modern economics to the issue of aid flows. The first paper in this volume is a contemporary representative of the above mentioned traditional strand of literature providing an overall assessment of the correlation between the aid flows and policies of developing countries. (Collier, and Hoeffler, 2002; and Collier, and Dehn, 2001) argued that the impact of aid depends on the policies of recipients. More favorable outcome of aid scenario can be accomplished in countries with better policy regime (Burnside and Dollar, 2000, 847) demonstrated that "aid has a positive impact on growth in developing countries with good fiscal, monetary, and trade policies but has little effect in the presence of poor policies". Moreover, they showed that the amount of aid disbursed does not seem to affect the quality of the policy choices made by the recipients. Later on (Collier and Dollar, 2002) proved that aid increases economic growth positively responding to policy improvements. (Boone, 1996a, 294) concluded that short-term aid targeted to support democratic/liberal political regimes may be a more successful means of reducing poverty than current aid programs under highly repressive regimes that do not lead to the empowerment of the poor. The World Bank (1998a, 14) also exposed its position by arguing that aid works in a "good policy environment", and suggested that donor agencies need to redirect their large-scale financial assistance to developing countries with good policies.

Investigating aid–policy dependence (Verschoor, and Kalwij 2006) hypothesized that: (i) aid contributes to poverty reduction when it is given to a government that pursues not only good economic policies but also good social policies, (ii) aid tends to increase the pro-poor orientation of the composition of public expenditure, and (iii) aid can decrease the infant mortality if it is redistributed through Non-Governmental Organizations (NGOs) because they are more likely to pursue the interests of the poor. Azam and Laffont (2003) focused on the issue whether aid and conditionality can increase the welfare of the ordinary people by diminishing the transfers that elite can take to its own from the rest of the population. The authors argue that aid contracts can be beneficent if they are tailored to the potential heterogeneity of the poor countries. They tested the ability of aid to reduce the level of distortionary taxation so as to leave more income to the ordinary people. They concluded that it would be too costly to encourage "good" governments to behave properly if aid is also given to "bad" governments.

On the basis of these observations abundant comments have been elicited while several researches demonstrated the fragility of this evidence. Hansen and Tarp (2000) and Dalgaard and Hansen (2001) claimed that Burney- Dollar model is unfair because it depends on the omission of a few observations. They applied their model again and got a positive effect of aid on growth in any policy environment. Lu and Ram (2001) noted that policy related aid model may not be strong enough due to the following inaccuracy: (i) the exclusion of five outliers and (ii) inappropriate use of standard error term. Even Easterly et al. (2003a) re-estimated the model and discovered that there is no significant relationship between the amount of aid and economic growth of the recipient countries even after controlling for policy variables.

Furthermore some other studies highlighted a positive effect of aid on recipient countries irrespective of the policy regime. Lensink and White (2001) have found that aid boosts economic growth in all countries but only up to a certain point. Karras (2006) applied two alternative approaches for measuring foreign aid. The first approach was based on the total net official development assistance (ODA) receipts per capita. It was shown that increasing foreign aid by $20 per person of the receiving country results in a permanent increase in the growth rate of real GDP per capita by approximately 0.16 per cent. Second approach considered total net ODA receipts as a fraction of GDP and it was shown that a permanent increase in aid by 1 per cent of the receiving economy's GDP permanently raises the per capita growth rate by approximately 0.14 to 0.26 per cent. Encompassing research on the dependency of country's policy regime and aid flows Schwalbenberg (1998) found very little statistical evidence that foreign aid is a key determinant of country's choice of distortionary economic policies. It was indicated that an increase in foreign aid leads to a decrease in taxation and/or provision in subsidies for social services, and a growing support for the domestic policy regime. However, aid should be given to the countries that are able to redistribute it very wisely. McGillivray and Noorbakhsh (2004) investigated correlation between the impact of aid on human development index (HDI) and on a conflict issue by applying an econometric analysis for twenty-six conflict-affected countries. They concluded that aid does not offset a negative impact of conflict on human development. Gounder (2001a and 2002b) and Feeny (2005) provided case-specific analysis of Fiji, Solomon Islands and Papua New Guinea, respectively. Each of these studies concludes that growth in the countries under consideration would have been lower in the absence of aid.

The volatility of aid flows as a result of uncertainty in donor-recipient relations and the shocks to the economy are now becoming a greatly debated issue due to it relevance to the achievement of the Millennium Development Goals (MDGs). Gemmell and McGillivray (1998) and Pallage and Robe (2001) analyzed cyclical behavior of aid receipts and noted that aid is often among the most volatile sources of foreign exchange income essentially because of the severe output fluctuations in developing countries. Lensink and Morrissey (2000) and Bulir and Hamann (2003) proved that aid instability has significant and negative effect on growth via its deterioration effect on the level of investment. More recently, Fielding and Mavrotas (2005) examined data for 66 aid recipients during the period 1973–2002. They drew a conclusion that open economies which are more likely to be smaller and richer countries, are often associated with more volatile sector-aid flows.

Considering the effect of foreign aid, it would be unfair not to cover skeptical views of the researchers on the financial assistance. This view was recently developed by Easterly et al., (2003a) who showed in his analysis that aid is perfectly uncorrelated with economic growth and that is why it cannot be considered as a factor that contributes to the poverty eradication in the Third World. His predecessor (Cassen, 1994, 16) stated that the aid –growth linkage appeared empirically weak and that aid has no significant impact on savings or investment and can increase unproductive public consumption (Jepma, 1997b) presented a broad survey of the literature on foreign assistance and in concluding remarks author stated that, for the most part, foreign aid crowds out private saving, supports public consumption, and has no significant positive impact on the recipients' macroeconomic policies and growth.

Abdiweli and Hodan (2006) and Rowley (2000) tried to explain the failure of aid policies in African countries. They arrived at an interesting conclusion that African countries experience lack of entrepreneurial skills essential for production. The countries are trapped in this situation and the only way out is to diverse resources (often provided via multilateral agencies) from productive economic activity to bank accounts in foreign countries. These findings support the argument that aid is more likely a transfer of wealth rather than creation of wealth and thus can be wasted very quickly if it is not used properly. In most cases foreign assistance can be described as a contract between governments. This implies that government has the full control over the distribution, composition and allocation of aid flows. In most cases this approach diminishes the role of a private sector in aid distribution. Friedman (1958) and Bauer (1972) criticized foreign aid as an institution that creates a wedge between the public sector and the private sector.

This paper is in agreement with the view of North (1981) who pinpointed factors that have enhanced or hampered economic progress historically. The scarcity of financial resources has never prevented nations from development, but the lack of proper institutions and policies hindered economic performance. The North's fundamental outlook will be ascertained in the following sections. Taking into account that this issue is not going to be resolved very promptly for the next decades, one must understand that if the researchers had relaxed constraint on the parameters of foreign aid and distinguished between the different types of aid, the significance of their results may have been weakened or strengthened at any meaningful level. For instance, Ram (2004) assessed the difference between donor motives, aid conditionality, and donor-recipient relations. In his case little evidence was left to support a widely disseminated view that good policies make aid significantly more effective in promoting growth or reducing poverty.

This literature analysis was not conducted in the purpose of indicating which of the numerous studies should be preferred. Instead, it was simply documented that the impact of aid is still a challenging area and the outcome may differ depending on the approach and the determinants used for the evaluation of aid distribution. Different aid instruments not only encompass different grounds for an intervention at macro, sector, and sub-national levels of the economy but also reflect the degree of consensus on policies and the capacity of the recipients to implement them. Governments' ability to engage explicitly in policy dialog calls for the extension of a detailed political and economic analysis of the interaction of interests between bi- and multilateral agencies and the recipient countries in the following chapter.

3. Poverty and Bilateral Assistance

3.1. Demand side: The Third World

The demand side of aid problematic is exemplified by the developing countries that are impoverished in living standards and do not have a stable political, social, and/or economic environment associated with the democratic freedoms. According to the World Bank's country classification using Gross National Income (GNI) per capita, the following countries received ODA financial assistance in 2006: (i) 50 Least Developed and 18 other Low Income Countries with GNI of $ 875 or less, (ii) 48 Lower Middle-Income Countries and territories with GNI of $876 up to $3.465, (iii) 35 Upper- Middle-Income Countries and territories with GNI of $3.466 up to $10.725 (OECD , 2006). A country is classified as a Least Developed Country based on the following criteria: (i) its three-year average GNI per capita is of less than $ 750, (ii) it faces human resource weakness in terms of nutrition, health, education and literacy, and (iii) it experiences economic vulnerability in terms of production, export, economic smallness or displacement of population as a result of disaster. Based on the above description Nigeria is known as the Least Developed Country in the World in 2006 (OECD, 2005).

Various tools and techniques have been developed to evaluate and measure poverty in the Third World, most of which have been based on incomes and consumption levels. Based on the World Bank (2002c) description of poverty, a person is considered as a poor if his or her consumption or income levels fall below some minimum level necessary to access basic needs such as food, water, education, health and etc. and indicates a poverty line as a "dollar-a-day". According to the World Bank 1.1 billion people had consumption levels below $1 a day and 2.7 billion lived on less than $2 a day. About 60 percent of the population live in Low-Income Countries and 25 percent of the population reside in the Middle-Income Countries. Table3.1 shows poverty projections based on the real per capita income growth rates and the (re)distribution of income within population. As a result of different types of aid programs the number of people who lived on less than $1 per day fell from nearly 1.220 billion in 1990 to almost 1 billion people in 2002. East Asia and the Pacific region had essentially eliminated extreme poverty even by half by

2002. Nearly 7 million people were lifted from abject poverty in Latin America and the Caribbean region, which lowered the percentage of their total impoverished population from 11.3 to 9.5.

Table3.1: Breakdown of "dollar-a-day" poverty distribution in developing countries

Region	1990		2002		2015	
	Millions of people	Percent of population	Millions of people	Percent of population	Millions of people	Percent of population
East Asia and the Pacific	472	29.6	214	14.9	14	0.9
Europe and Central Asia	2	0.5	10	3,6	4	0.4
Latin America and the Caribbean	49	11.3	42	9.5	29	6.9
Middle East and North Africa	6	2.3	5	2.4	3	0.9
South Asia	462	41.3	437	31.3	232	12.8
Sub-Saharan Africa	227	44.6	303	46.4	336	38.4
TOTAL	**1.218**	**26.1**	**1.011**	**22.5**	**617**	**12.9**

Source: (Ratha et al., 2006, 9)

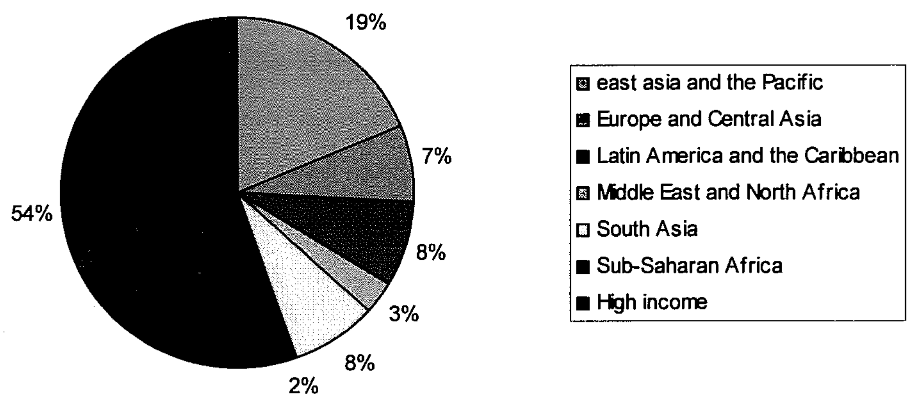
At the same time Middle East and North Africa region kept relatively low level of poverty between 1990 and 2002 as of 2.3-2.4 percent. On the other hand though, Europe and Central Asia region demonstrated increase in poverty from 0.5 in 1990 to 3.6 percent in 2002 but it is expected that by 2015 poverty rate will be only 0.4 percent and this is lower than in 1990th. More than 400 millions of people were living in extreme poverty in South Asia region in 2002. However, it is anticipated that this region will be able to catch up and decrease poverty ratio by half. With the exception of Sub –Saharan Africa, all regions are expected to reduce poverty by 50 percent by 2015. By then the total number of people living less than $1 per day is anticipated to be 617 million. In contrast, in Sub-Saharan Africa poverty incidence remains 46 percent in 2002 and declined in 2004 to 41 percent. Despite this positive tendency, the number of poor would be more than 300 million.

As it can be seen results are rather mixed in terms of the global fight against poverty. It is understood that foreign aid has been more effectively deployed in some cases and hence have yielded better improvements to trim down the poverty. In contrast, in some regions severe famine continues to escalate despite the implication of poverty reduction efforts. Different explanations of the ineffective aid results are offered in the academic literature. Langhammer (2004, 83) examined aid trends to African countries and argued that there was significant decline in foreign aid flows after 1990 as a result of a slight recovery after two oil price shocks so that the decrease in aid was coincident with the rapid increase in returns of financial assistance. Fukuda-Parr (2004) ascertained that stagnation and reversals in African Countries is caused by a scourge of HIV/AIDS that, in turn, led to the dramatic decline in life expectancy to 44.7 years and by a significant fall in income in the transition countries of Eastern Europe and the Former Soviet Union. Abdiweli and Hodan (2006) assumed that mismanagement of aid resources as a result of pursued non-development agenda by recipient governments and/or misallocation of aid were among the key reasons behind insufficient aid output in the Third World.

In another prospect, the United Nation Development Program (UNDP) applies a different framework to the estimation of poverty. The UNDP developed "Human Poverty Index" (HPI) that measures "deprivations in the three basic dimensions such as a long and healthy life, knowledge and a decent standard of living. The 2006 Human Development Report devoted to the eradication of poverty and water crises highlights the number of poor at a county level as a percentage of the total population. According to this report, more than 90 percent of the population in Least Developed Countries is impoverished (Watkins, 2006). The escalation of famine is accompanied by the growing inequality, income disparity and the absence of convergence between the rich and the poor. As indicated in the 1999 Human Development Report (Jolly et al., 1999, 14) the long–trends of the distance between the richest and the poorest countries was about 44 to 1 in 1973 and 72 to 1 in 1992. Income of world's 200 richest people is growing at $500 per a second! The combined wealth of the world's 200 richest people hit $1 trillion in 1999; the combined incomes of the 582 million people living in the 43 least developed countries are $146 billion (UNDP, 2000).

In 2005 the total output of the world was equal to $61.3 trillion and as it can be seen from Figure3.1 that depicts the countries' contribution to the world's income developing countries account for 46 percent. Especially East Asia and the Pacific region have shown promising productivity. One of the significant reasons behind the above results is that in fact Third World countries are relatively high in natural resources and almost 80 percent of total commodities are manufactured in such regions. However the countries wages are drastically low varying from $1 to $2 per day whereas in developed countries the average wage is generally set from $6 to $8 per hour.

Figure3.1: Contribution of developing countries to the world's output in 2005



Source: (World Bank, 2007)

The pattern of famine and unequal food distribution perpetuates hunger as so many impoverished people can not afford to buy food staples. In most cases, food is produced in areas of hunger and supplied to meet the consumer demand not the needs of the poor (Katima, 2005, 6). This implies that the mechanisms through which the received aid is distributed among the needy class of the developing countries in order to reduce the poverty do need special care and reassessment. Of all human rights failures today, those in economic and social areas affect by far the larger number and are the most widespread across the world's nations and large numbers of people (UNDP, 2000). Some researchers believe that the international co-operation policies are more responsive to a development model which corresponds to the interests and values of the developed countries (Grant and Nijman, 1998). It remains to be an undeniable fact that in the real world interests of "have communities" may not always superpose on the same as of "non-have communities"; and as a result the regulation of distribution of foreign aid is rather set to satisfy the position of donor countries who essentially play the dominant role in the foreign aid trade. In the face of such enormous external influence, the governments of poor nations and their people are often powerless. Governments of Low-Income Countries generally do not have sufficient information, mobility or power to make choices among aid providers (Rogerson et al., 2004, 12). In October 2003, at a United Nations conference, UN Secretary General Kofi Annan noted that "Funds should be moving from developed countries to developing countries, but these numbers tell us the opposite is happening. Funds that should be promoting investment and growth in developing countries, or building schools and hospitals, or supporting other steps towards the Millennium Development Goals, are, instead, being transferred abroad." (Annan, 2003). Despite all these uncertainties and imperfect scenarios, fight against poverty continues in 2007 and leaves more room for new strategies as well as remedies and improvement in the previous shortcomings and slow progress. The allocation of foreign aid in terms of donor countries' priorities will be further investigated in the following section of this paper.

3.2. Supply side: The OECD Countries

3.2.1. Countries' Share in Aid Provision

Official Development Assistance is provided by 22 OECD member countries in accordance with the United Nation General Assembly Resolution; it does not include any private capital flows or investments. Almost 36 years ago, several countries committed to promote the global development by reaching a minimum net amount of 0.7 percent of their Gross National Product (GNP) which is defined now as Gross National Income (GNI) to aid at market *prices* (UN Resolution , 1970, 43). The amount of development flows can be measured using the following criteria: (i) as percentage of Gross National Income (GNI) or (ii) in real terms (US billion). Table3.2 presents the provision of foreign aid among the member countries in 2006. In 2004, $79.410 million was provided by the contributing country members; in 2005 they significantly increased their commitments up to $106.777 million (0.33%) and in 2006 development assistance fell 5.1 percent. Between 2001 and 2004, international aid rose again, but much of it was due to the geopolitical concerns of the donor such as fight against terrorism. The increase observed in 2005 was largely due to the enormous debt relief for Iraq, Nigeria, and some other one-off large cases.

Table3.2: Net Official Development Assistance in 2006

	Country	**USD billion**	**As a percentage of GNI**
1	United States	22.74	0.17
2	United Kingdom	12.61	0.52
3	Japan	11.61	0.25
4	France	10.45	0.47
5	Germany	10.35	0.36
6	Netherlands	5.45	**0.81**
7	Sweden	3.97	**1.03**
8	Spain	3.80	0.32
9	Canada	3.71	0.30
10	Italy	3.67	0.20
11	Norway	2.95	**0.89**
12	Denmark	2.23	**0.80**
13	Australia	2.13	0.30
14	Belgium	1.97	0.50
15	Switzerland	1.65	0.39
16	Austria	1.51	0.48
17	Ireland	1.00	0.53
18	Finland	0.83	0.39
19	Portugal	0.39	0.21
20	Greece	0.38	0.16
21	Luxembourg	0.29	**0.89**
22	New Zealand	0.26	0.27
	TOTAL	**103.94**	**0.30**

Source: (OECD, 2007)

Table3.2 suggests that all countries overall failed to fulfill their commitments. Currently Overall Developing Assistance (ODA) represents only 0.3 percent of GNI of donor countries, although some countries such as Sweden, Luxembourg, Norway, Netherlands and Denmark have reached and even surpassed their committed target. It is a very interesting observation that the most wealthiest and developed nations in the World are not as generous and dedicated as anticipated. The United States and Japan are among leading countries in providing aid in real terms yet at the same time they allocate a very small portion of their GNI as opposed to Luxembourg or Norway. Despite the above deficiencies, the amount of aid provided in 2006 was the second largest amount after 2005 and governments pledged to spend 0.56 percent of GNI on poverty reduction by 2010 and 0.7 percent by 2015. In return, poor countries committed themselves to taking concrete steps to improve governance, establish development priorities, and adopt sound policies for growth. Since then, calls for "scaling up" aid have become increasingly influential in the international development agenda (Menocal and Mulley, 2006, 12).

Bilateral aid is still known as a more preferred tool for the delivery of foreign assistance by both donors and recipients due to several reasons. First, bilateral aid often includes a large grant element or non-concessional loan that is favored by the recipients. For instance, in 2005 the OECD member countries provided $ 22.699 million of the total development assistance in the amount of $ 106.777 million devoted grants to debt relief. It was noted that $13.9 billion and $ 5.5 billion of the above amount were given to Iraq and Nigeria respectively (OECD, 2005). Secondly, bilateral aid unlike multilateral funding does not impose much conditionality associated with the releases of aid finance in the future. The common form of conditionality is tied aid that according to the OECD implies official or officially supported loans, credits or Associated Financing packages where procurement of the goods or services involved is limited to the donor country. In 2001, DAC member countries agreed to fully untie their aid to the Least Developing Countries. However as much as 42 percent of Official Development Assistance remained untied in 2006, which, in turn, indicates that 58 percent of financial assistance has been tied to the export of commodities or services from developed countries. Jepma (1991a, 9) proved that aid tied by the OECD donor counties had important consequences for recipient countries by increasing development costs by 20-30 percent. Even donor countries recognized that this form of aid that is essentially an export subsidy serves the trade interests of donors and distorts competition in international trade often to the detriment of recipients. As a result Nordic countries, the United Kingdom, Germany and France considerably limited the usage of tying aid mechanism as opposed to the United States, Spain and Canada.

Moreover, the lack of sufficient funds or an uncertainty of the economic rate of return for potential investors in developing countries may hinder the provision of public goods that is crucial for a sound economic development. In this case foreign aid can serve as a substitute for private capital or international loans at a high interest rate (Morrisey, 2004). For donor countries bilateral aid, in most cases, is applied as a useful means for influencing recipient countries in areas like trade, investment, and defense.

3.2.2. Allocation of Foreign Aid

The rationale for foreign aid can receive a broad range of support among the global communities. Developed countries acknowledge that it is necessary to implement an effective redistribution of resources from rich to poor. Usually the problem emerges when there is both a divergence of interests in the provision of international public good and asymmetric information between agents and recipients (Paul, 2006). In other words, donors do care about the needs of the recipients, but at the same time they also use aid to further their self-interest. In this particular issue they do not agree about how best to help Least Developed Countries to "catch-up" and reduce poverty by half by 2015 while at the same time maintaining economic growth in rich countries. They are not sure whether to bail-out a few very poor nations a lot for a short time with only loans or to assist many less-poor people a little for a long time with a range of financial services (Schreiner, 2002). At the same time they all share a consensus that: (i) the poor lack empowerment as well as income and basic needs, (ii) economic growth does not necessarily result in swift poverty reduction, and a specific pro-poor strategy is required, and (iii) a pro-poor strategy is only likely to be effective if the partner government is committed to it, and externally imposed conditions are rarely effective in generating such commitment (Cox and Heale, 1998).

The lack of consensus in the academic literature about what factors increase the effectiveness of aid in poverty reduction contributes to the extensive debate on how a donor allocates cross-country aid. Of all the factors, donors may be mainly concerned with such issues as geopolitical situation, mutual gains, and potential economic benefits for themselves, poverty reduction, equity, and international security. In the mid 1990th an international consensus to fight against poverty led to the development of a "poverty-efficient" approach. Poverty–efficient aid allocation is one that lifts the largest possible number of people out of poverty ((Cogneau, and Naudet, 2005, 4). This, in turn, implies that more aid must be allocated to the countries where the effectiveness of aid in lifting out of poverty is relatively high. This approach received much support because it is believed that aid should not always be allocated for commercial or geo-political interests only. On the other hand, this poverty-efficient allocation may be inequitable in a sense that it does not guarantee that more aid goes to the countries with higher levels of poverty. The main reason is that severely impoverished countries are often (although not necessarily) less effective in reducing poverty. Another view on the poverty-efficient aid allocation that was considered in the previous section is based on the quality of recipient country's policies and the yardstick of better institutions. The more recent assessment to poverty eradication highlights "country-by-country" methodology. This may result in a smaller reduction of poverty at a global level but would prevent concentration of aid in a specific country. In this case governments are not penalized for the low levels of aid effectiveness and instead relatively more aid allocated so nations can achieve approximately the same reduction in poverty as countries with higher levels of aid effectiveness.

Some researchers have argued that it is the moral responsibility of rich countries to contribute in reducing global poverty and enhancing economic development in poor countries regardless of their self-interest. But neither the advocates nor the critics of foreign assistance have adhered to a careful distinction between self-interest and ethical consideration (Ruttan, 1989). It was stated that there should be compensation by the rich countries to the poor countries for the past injustices stemming from political domination and economic exploitation. A second entitlement argument is based on the uneven distribution of natural resources. It has been argued that natural resources are part of our global heritage and that those areas that are favorably endowed have an obligation to share rents from differential natural resource distribution (Beitz, 1979).

These idealistic prospects clearly contrast with a large literature that has argued that economic and strategic foreign policy concerns rather than altruism explain the pattern of foreign aid. Cox and Heale (1998) indicate that Denmark, Finland, the Netherlands, Sweden and the UK have poverty reduction as their overarching goal and that is why they have the most comprehensive formal commitment. The European Community has a number of resolutions related to poverty, but it is only slowly developing operational strategies. For instance, Germany and Italy considers poverty reduction as a priority among others. France and Spain do not have an explicit strategy for poverty reduction. French agencies do not consider that there are identifiable groups of poor for whom a special strategy is required. Table3.3 displays top ten recipients of the Official Development Assistance.

Table3.3: Top ten recipients of the ODA in 2005

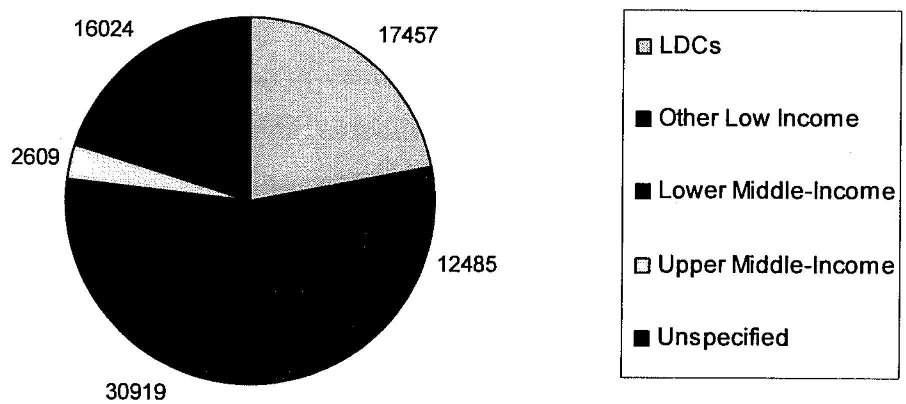
	Country	USD million	Population 2005 (000s)
1	Iraq	12.924	25.861
2	Nigeria	3.160	141.115
3	China	2.682	1.307.802
4	Afghanistan	1.946	30.430
5	Indonesia	1.867	220.558
6	India	1.785	1.094.583
7	Ghana	1.394	21.306
8	Egypt	1.319	69.907
9	Viet Nam	1.312	82.966
10	Sudan	1.163	35.226

Source: (OECD, 2005)

It is well presented that Iraq, Afghanistan and Egypt are among the main recipients and the most populous African country Nigeria received three times less funding. This table indicates that foreign recourses went to countries that are not at the edge of poverty.

It is a harsh reality that developed countries allocate more aid to Lower Middle Income Countries than to Least Developed or other Low Income Countries even realizing the extent of needs and population size of the recipients. Levin and Dollar (2005, 2) examined disbursements of aid per capita between 1992 and 2002 and proved that Low Income Countries receive around 40 percent less aid than predicted by their policy and institutional indicators such as population, poverty and performance. According to their research, very large and very small countries as well as heavily impoverished and very badly-governed countries are likely to become "aid orphans". Beynon (2001) pointed out that if current aid flows were reallocated on the basis of equalizing aid per capita and on country specific levels of famine, the number of people lifted out of poverty would have risen by 3 million. Figure3.2 represents allocation of aid based on income group in 2004. It can be noted that Least Developed Countries are not the main recipients of aid findings. More than $30 million were allocated to Lower Middle –Income countries such as Iraq or Egypt. This discrepancy remains to be addressed by decision makers as a significant issue of concern aid allocation.

Figure3.2: Distribution of aid by income group in 2004



Source: (OECD, 2005)

Although the international community has made the commitment to significantly increase the volume of development aid, the issue of selectivity remains high on the agenda. Alesina and Dollar (2000, 6) proved the aforesaid figures by arguing that the U.S. has targeted about one-third of its total assistance to Israel, Egypt and Afghanistan. Indeed in 2005 the United States allocated $6,926 million to Iraq, $1 million to Afghanistan and $750 to Egypt. France has given overwhelmingly to its former colonies such as Senegal ($363 million in 2005 and Congo Republic ($582 million in 2005). Japan's aid is highly correlated with United Nations voting patterns in a sense that countries that vote in tandem with Japan receive more assistance. The Nordic countries however do not have the same sharp focus on the Middle East and respond more to the "correct" incentives, namely income levels, good institutions of the receiving countries, and openness. They also found evidence that democratizing country receives a 50 percent raise in aid. Top three recipients of Sweden were Tanzania, Mozambique and Ethiopia. The complexity of the determinants of aid flows is well documented by a recent study by (Schraeder et al., 1998). They restrict their attention to Africa and easily reject an altruistic vision of donors' motivation especially Japan and the United States. They also highlight interesting differences between donors, related to their position in the world order, strategic interest and relationship with former colonies. Authors indicated that Japan allots aid in accordance with its economic interests such as: (i) access to vital to the Japanese industry raw material like Zambia, Zaire (copper), Niger (uranium) and Madagascar (chromium) and (ii) access to the major economic markets for Japanese export like Kenya and Nigeria. In 1990the the United States allocated aid to those countries (Nigeria, Ghana, Senegal and Kenya) that enjoyed important trade relationships relative to other countries in Africa.

Berthélemy (2006) found that most donors behave in a rather egotistic way: they target their assistance to their most significant trading partners. Nevertheless some of them such as Switzerland, Austria, Ireland, and the Nordic donors (with the relative exception of Finland, and possibly Sweden) behave to some extent altruistically towards recipient countries. Conversely, Australia, France, Italy, and to a significant extent Japan and the United States, are more egoistic than the other donors On average, Denmark, the Netherlands, and Norway have over the 1980s and 1990s the highest aid performances with total aid to GNI ratio close to 0.9 percent. White and McGillivray (1995, 165) pinpointed that while large donors such as France, Germany, Japan and the United States grant aid to almost all recipient countries listed in the OECD's aid statistics, smaller donors such as Denmark and Sweden are highly selective at the first stage of the allocation process, i.e. in deciding whether or not a recipient receives aid. Nunnenkamp and Thiele (2006, page 1199) highlighted that few donors clearly preferred recipient countries offering promising conditions for aid to be effective. None of the major donors responded to changes concerning the rule of law and control of corruption in a way that could have improved the allocation of aid. Post-colonial ties remain an important aid determinant for France, Netherlands and the United States which appears to be in conflict with the notion that aid has increasingly been targeted to the needy and deserving. Applying different approaches to assess whether donors favored poor recipient countries with good governance, it typically turns out that targeting was particularly weak for French and Japanese aid. In the case of France, poor targeting can be attributed to a lack of both poverty and policy orientation. Japanese aid lacks any poverty orientation, and its policy orientation appears to be a side effect of the concentration of aid on neighboring Asian trading partners. Woods (2005, 397) analyzed the patterns of foreign aid flows and discovered that the U.S. almost tripled its funding since 2002. Most of the increase in foreign aid was devoted to different security projects and the fight against terrorism in the Middle East in the wake of September 11.

On the other hand Trumbull and Wall (1994) debated that donor countries are motivated by the well-being of recipients that is why ODA allocation is determined by the recipient needs such as infant mortality and political-civil rights and not by the recipient's income levels. Kohama et al. (2003, 8) investigated consistency between poverty reduction and aid allocation. They found that in the late 1990s, grant allocations of Japan, the Netherlands, U.K., Canada, Norway, and Sweden were consistent with the necessary condition of optimal poverty targeting.

In the consideration of fair aid allocation it has been argued recently (Devarajan et al., 2002 and Sachs, 2005, 247) that a substantial "push-up" in current aid levels must be assigned for Least Developed and Low-income countries. At the same time however, concerns (Anderson and Waddington, 2006, 7) have been expressed about the potential to absorb more aid for many countries that are currently "off-track" in halving $1-a-day poverty. Foster and Killick (2006, 6) pinpointed that only few developing countries have budget systems strong enough to provide reasonable assurance that aid and budget allocations reach intended beneficiaries and, in this case, an aid surge may have serious macroeconomic ramifications. While the envisaged doubling of aid would bring real benefits, there is a risk that it could be accompanied either by exchange-rate appreciations or counter-productive excesses of spending over absorption. Serious declines in the quality of public spending may also occur, which would reduce the benefits derived. Moreover, scaling-up aid will lead to increased liquidity and if it is not properly managed, inflation will rise.

Foster and Keith (2003) highlighted the existing strong aid dependency in developing countries as a proportion of GNI and as a result of aid surge, Dutch-disease may occur and aid will peak at over 20% of countries' GNI. Dutch disease refers to a situation whereby high aid transfers can have a negative effect on the competitiveness of the economy and hence on growth prospects.

It can be concluded that great variations exist in the interpretation of poverty and in identification of most feasible ways to fight against famine. Part of such confusion is related to the multidimensional character of poverty which allows agents to pursue their own agenda and priorities. It is understood that not only recipient countries' governments, but all global participant members are involved in the aid and development process, following their own special interests in this process. This spectrum in countries self-interest normally influences the outcome of their individual policies, actions and commitments toward the allocation of foreign aid. As a result, the full responsibility of aid failures can not be regarded as to the recipient governments or to the donor countries only. Several factors such as the nature of aid relationship and the aid distribution patterns, as well as the aid agencies' own political constraints and incentive structures must be taken into account in the evaluation of aid results (Gomanee et al., 2005).

A substantial part of the academic literature views skeptically the role of foreign aid in poverty reduction and especially in the achievement of Millennium Development Goals by 2015. Considering the past experience, the reduction of worldwide poverty by 50 percent by 2015 rather seems to be an optimistic target. However, it must be noted that any progress achieved in this process will be another significant step to overcome this global dilemma. As it was discussed donor countries has already been able to successfully eradicate poverty in some regions of the world. However it was also demonstrated that the allocation of aid recourses based on donors' interests outweighs the aid deployment set based on the recipients needs and as a result the most nations still live in hopeless poverty. Pragmatically some donor countries do not even consider poverty reduction as a priority in their agenda or do not have specific strategic plan and methodology to alleviate the worldwide poverty.

In short, it is conferred that more progress would have been made in terms of reduction of poverty if the short and long term interests of the recipient countries have been considered in the first place when setting the poverty agenda by the prosperous developed countries. Hence, the challenge still remains to be taken up by the other contributing donors in this century. Next section of this paper will be devoted to the role of multilateral financial institutions in the development of the Third World.

4. Poverty and Multilateral Assistance

4.1. Role of the IMF reforms in Russia in 1992

In the last year of *perestroika* (1991), Russia faced cascading economic and social problems such as a drop in production and in supply of goods and services, substantial budget deficits, difficulties in repayment of international debts of soviet era, decline in foreign trade position, and escalating inflation (Samal, 2005). At the same time, some external political factors also aggravated Russia's position in controlling its economic situation as the republics of the Soviet Union began to claim more independence.

Western experts believed that the Russian "shock therapy" contained all the essential elements necessary for rapid transition to the market and in 1991, the IMF granted for Russia financial aid in the form of an Extended Fund Facility -a three-year loan-plus-reform package to ease the transition (Murrell, 1993, 124 and Easterly, 2006d, 61). Boris Yeltsin (the first president of the Russian Federation) announced these neo-liberal political, economic and social reforms to cope with the critical situation on January 1st 1992. Liberalization, privatization and globalization were the important features of the IMF aid- plus- reforms package in transition economies. However, the currency devaluation remained a key pre-conditionality recommended by the IMF and was never mentioned formally. As a result of devaluation, banks liabilities raised in value significantly while Rubble-based loans and assets became almost valueless (Cohen, 1999). After the dollarization of prices took place, the government was unable to finance fiscal deficit with seignorage anymore and exchange it for good and services. On the other hand the Central Bank lost control as a lender to domestic banking system and demand for the national currency as well as the money supply went down significantly. Following the IMF instructions, the government considered cuts in official fiscal sector and rise in taxes as the only reasonable source of its revenues in order to cover budget deficit. The scarcity of liquidity in the real sector also had adverse impact on the government short term macroeconomic plans that had been already weakened by budget deficit. Between 1992 and 1993 the direct response to the requirements of the IMF, which has been monitoring and supervising Russia's structural adjustments, had devastating consequences on the economy of the Russian Federation.

Severe cuts in the government spending were addressed especially to the enterprise sector: the governmental subsidies to the enterprise sector dropped from more than 10 percent of the GDP in 1992 to around 2.5 percent in 1999. The sharpest decline in these official enterprise subsidies occurred in 1995 (–50 percent) (Buch et al., 2000). The taxes never came due to the insufficient privatization process as a result of which almost all the formerly state-owned profitable public enterprises had shown decline in their performance, poor financial and physical conditions, and could not be considered as the main source of government's income anymore. The major tax debtors were particularly the industrial enterprises belonging to the energy sector. In turn, large enterprises have been supposed to finance the small indebted firms by offering products on the Russian market at a price lower than in the world market. Government's incapability of compensating for the declines in revenues by the expenditure cuts inevitably led to the chronic deficit and permanent budget crisis.

The first phase of privatization programme known as a *voucher privatization* started in October 1992 with the transformation of small-size enterprises. The vouchers, each with a nominal value of 10000 Rubbles were distributed among Russian citizens either for the purchase of enterprises' shares, reselling or investing in voucher funds. Around 70 percent of all small-scale enterprises were privatized through tenders under provisional agreements. More than one million small shops and over 15,000 state-owned enterprises were privatized by the end of the 18-month period (December 1992 to June 1994) of mass privatization programme (Samal 2005, 4). However, the privatized proceeds as a percentage of the GDP were negligible as shown in Table4.1.

The second phase of privatization known as a *post-voucher privatization* was launched in mid-1994. After July 1st 1994 the foreign investors could buy enterprises' shares at money auctions for bidding the highest price. Political and legal inefficiencies and economic instabilities were among the reasons why the process of post-voucher privatisation failed to achieve its original goal which was to introduce fresh funds into enterprises. Due to these instable situations new investors were unwilling to purchase shares in enterprises held by few individuals (Desai 2005b, 35).

Table4.1: Financial indicators of privatization in Russia, 1992-1998

Indicator	Units	1992	1993	1994	1995	1996	1997	1998
Privatized enterprises	Nos. thousand	47.041	42.929	21.905	10.125	4.997	2.743	2.129
Privatized proceeds	Billions of Rubbles	0.16	0.45	1.07	3.82	3.23	26.23	17.54
Do	Billion of US dollars	0.71	0.48	0.84	0.48	0.63	4.53	1.76
Do	% of GDP	0.83	0.26	0.17	0.24	0.15	1.02	0.65

Source: (Grigoriev, 2000)

The failure of post –Soviet macroeconomic reforms and de-industrialization of national economy became obvious during the first three years. Real wages collapsed, the purchasing power of the population declined and private investment was almost non-existent. High interest rates, an incapability of banking sector to facilitate private investment, the hard struggle for survival of enterprises on the one hand and large-scale cuts in jobs, inability to compete with importers, almost non-existence of a competitive marketing system on the other hand exacerbated the situation. The social effect of such Western aid on a critical economic situation was even harsher. The number of Russians in poverty has risen from 2 million to 60 million since the IMF came to post-Communist Russia. Male life expectancy has dropped sharply from 65 years to 57. Economic output decreased by at least 40 percent (Shestakov, 2000).

4.2. Macroeconomic Prospect (Between 1994 and 1998)

The period between 1994 and 1998 is characterized as the government's feeble attempts to stabilize the Rubble and to fight against inflation. In order to reach these objectives the Russian government basically considered two strategies: first borrowing on the international and domestic financial markets, and second non-payment of wages. The budget deficit was mostly financed by the international creditors allowing debt burden to go sky-high. Though the Russian government and international financial institutions declared the beginning of the economic growth in 1997, the reality of foreign assistance was quite different.

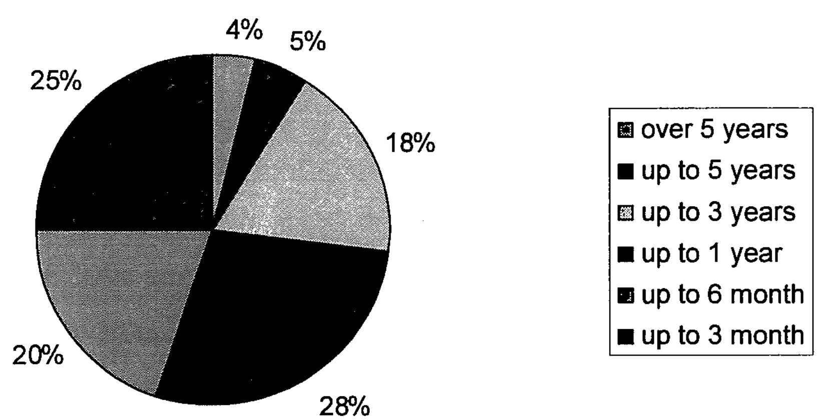
There were 75.84 billion Rubbles (approximately $12.5 billion) unpaid wages in the country by August 1, 1998. The most sever strike was in sectors like such as health care (a 33% increase in non-payments), culture and arts (28%), education (17%), housing (10%), science and research programs (7%) and communal services (3,8%) (Kagarlitsky 2000). Increases in the budget deficit accompanied by rise in tax arrears had been a clear sign of the Russian economy for a long period of time. The non-payment of wages, in turn, had unfavorable consequences on the living conditions of people. It decreased the purchasing power of the population and reduced the volume of money in circulation. Prior to the IMF financial aid all social programs were subsidized by the government. After the implementation of the IMF policy all social programs forced to become self-financing and at the same time spending on public sector were cut. This could be interpreted as the collapse of the welfare state in the Russian society. No private investor made investments where the federal government stopped providing services simply due to the lack of funds.

The macroeconomic targets for 1995-96 set earlier by the IMF included fixing the exchange rate, replacing money printing with Rubble treasury bills (GKO) and bonds (OFZ) and other market borrowings, and implementing fiscal and structural reforms. But due to the political uncertainty and strong opposition from communists, practically no reform took place in 1996, however, that year was very important for Yeltsin as a year of re-election. The first round of the presidential elections took place on June 16, 1996. Boris Yeltsin won the second round and the inauguration took place on August 9, 1996. The pre-election was accompanied with budget deficit rise. A large amount of money was spent on pre-election gifts in the presidential race which, in turn, exacerbated budget deficit (Sachs, 2005, 144).

Government borrowing by elites from international financial institutions for resolving internal problems became a sort of addiction. Following the advice of foreign "*consultant friends*", the Russian government had created a market in short-term state bonds. Sales of these bonds, it was hoped, would allow the government to cover its deficit and reduce price rises and to service an additional debt (Kagarlitsky 1998, Malki 1999, Margolin 2000). The creditors learned from the first lesson that lending money to the Russian government was a risky gamble unless at least there was an opportunity of big returns. As a result the real annual interest rate in the Russian bond market exceeded 100 per cent.

Why would the lenders invest their money in long-term projects , endure high risk, wait for years and at the end get a lower returns as they could have got by giving high interest loans to the government for three or six months? The answer to this question is obvious. They would not. That explains the decline of private investment in the Russian economy between 1994 and 1998. Figure4.1 depicts an increase in the portion of short-term loans in the government debt structure in 1998.

Figure4.1: Maturity structure of Rubble debt in May 1998.



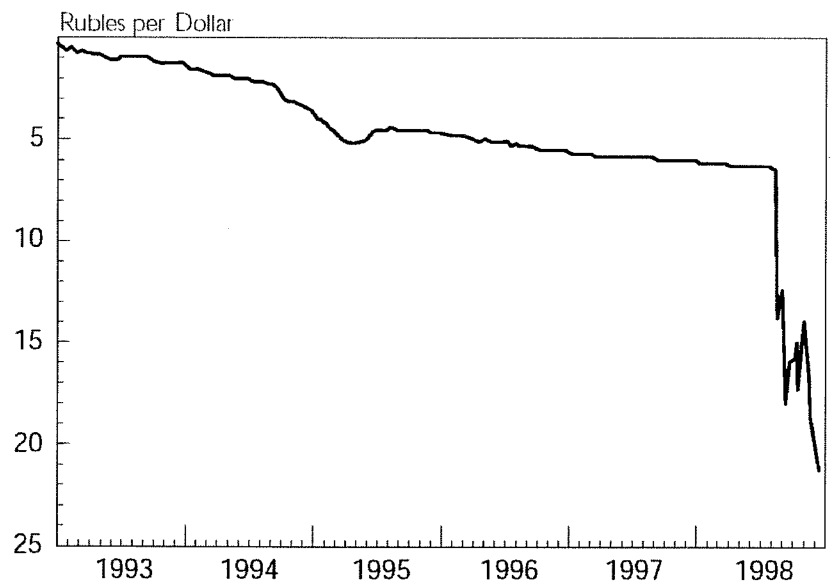
Source: (Helmenstein and Krylova 1998; and Komulainen, 1999)

What the government could do when it was in short-term debt trap? The only reasonable way out of this situation was to borrow even more money in order to be able to meet the payments on its bonds. Not only the economic decline but also the debt burden continued to escalate. The federal government, for sure, did not count only on borrowed money to lower its budget deficit. The main problem occurred when the government significantly reduced its spending, including public investment. Huge skyscrapers, staff numbers as well as salaries of the Russian Central Bank and the publicly-owned State savings rose rapidly (Kagarlitsky, 2000). However the expenses of the banking institutions were never mentioned by the IMF. The only issue emphasized by the IMF was the necessity of cutting spending on education, social welfare, healthcare and etc.

Despite foreign loans Russia was not able to prevent and handle the currency crisis in 1998. The author believes that foreign aid along with other external factors triggered the crisis by imposing conditional provisions and preventing the Russian government from searching a realistic solution to the country's acute problems using domestic resources. Under the IMF monitoring Russian Federation occupied such an embarrassing position according to which banks and trade were developing at the expense of industry. The IMF also contributed to Russia's new image as a totally uninterested in long-term domestic economic projects after the enormous possibilities of the public sector had been wiped out.

Lengthy petitioning by the Russian government resulted in a pledge of US$22.6 billion, mostly from the International Monetary Fund, in mid –July 1998.Towards the end of July the IMF delivered the first package of its aid. In the weeks that followed a reported US$3.8 billion of the IMF loan fund was handed over to the bondholders" (Kagarlitsky 2000). The continuing decline in the real economy built up pressures on the banking sector and at the same time state short-term bonds were loosing their values as a source of liquidity. It turned out that many Russian banks suddenly were close to bankruptcy. Bankers understood that the Kremlin would use new state securities as a payment on its bonds not money. The above–mentioned loan did not help and instead tension was heightened. Barter, non-payments and offset increased. "By 1998, about half of the inter-enterprise payments were made in barter, around one-fourth in money surrogates and only one-quarter in actual cash, because they facilitated tax avoidance and evasion " (Samal 2005, 26). Later on the Russian Federation would announce default on its international financial obligations and domestic debt. A 90-days moratorium was imposed on the foreign debt payments. GKO payments were suspended. The crisis actually happened on August 17, 1998. In this critical situation the government could devalue the currency immediately, and keep its remaining reserves of gold and foreign currency intact, or put the devaluation off for perhaps four or five months, by which time the country would have lost its reserves for gold. *Russia was forced by Western reformers to devalue the Rubble on August 17, 1998.* It was on September 2, 1998 that the Rubble began to float following a decision of the CBR. In August 1998 the Rubble collapsed from about RUR 6 for USD 1 to 20-25 RUR per dollar (Sutela, 1999). Figure4.2 shows the collapse of the national currency (Rubble) in 1998.

Figure4.2: Russia's exchange rate collapse



Source: (WEFA – Cohen 1999)

Many observers believed that the IMF financial aid to Russia did not actually go to Russia; all IMF money disbursed to Russia was physically held at the IMF and used to pay off the prior IMF loans to Russia (Weissman, 2001). The IMF thought it did not make any fundamental mistakes in lieu of the Russia's economy. From the IMF perception, the Russian government failed to implement full-scale IMF-style reform. According to the former IMF Managing Director- Michel Camdessus- who made a statement on September 1999: "*Russia's economic shortcomings represent not so much the failure of reform as the effects of 70 years of central planning and the incomplete implementation of reform policies — itself a result of a lack of domestic political* *consensus on reform"* (Shestakov 2000). Odling-Smee (2006, 154) also argued that economic reforms did not progress more smoothly due to the lack of consensus in favor of liberal economic reforms among the Russian leadership and the weakness of the Russian state. Rogoff (2002) pinpointed that Russia has been on the right path even if she used the recipe of the West instead of creating her own path of transition. However, extreme corruption and less- than-perfect implementation of the reforms in Russia made it difficult to move towards the market economy. Norsworthy (2002) hypothesized that the Russian transition has been difficult than expected due to an economic structure based on the central planning, poorly regulated financial sector and weakening authority in a central complex federal system.

On the contrary, contagion effect of the Asian crises accompanied by the collapse of the East Asian currencies starting in mid 1997 can be characterized as an exogenous factor in the origination of the crises. Furthermore a constant decline in raw material and oil prices "from $23 a barrel in mid- 1997 to $11 a barrel a year later" (Desai 2003a, 145) caused the value of Russia's oil exports- its main source of foreign currency earnings- to fall significantly and the investors to begin removing their funds from Russia. Fuel and energy comprise about 50% of total Russian exports, with Russia holding 5% of world oil reserves and producing 10% of world oil output (Selim, 2005); as such a decrease in the price of oil and nonferrous metals hit the country's export position and dramatically affected its trade balance.

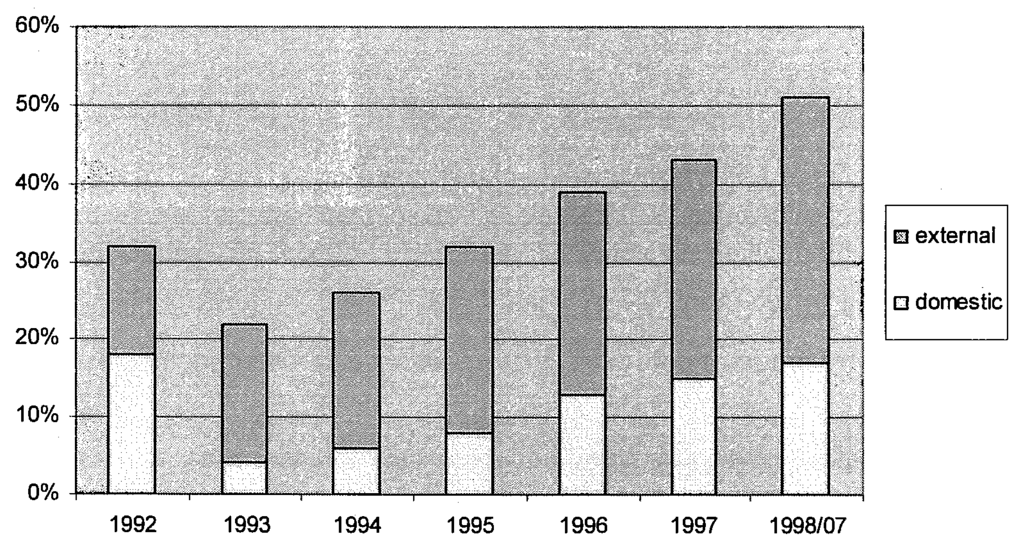
4.3. The Structure of Debt

The size of a country's foreign debt definitely has a key impact on its ability to service its liabilities. After disintegration of the Soviet Union in 1991, Russia, as the biggest successor country, assumed foreign liabilities and a significant share of foreign assets of the former USSR. After several rescheduling arrangements and repayments, the approximate value of these obligations as of the end of 1999 totaled around US-dollar 90 billion, or more than 50 percent of total foreign currency debt. The largest shares in the post-Soviet constituted the debt obligations against multilateral creditors as Paris Club and London Club. The Russian federal government was the main debtor to the foreigners. The relative proportion of the domestic and foreign debt is shown in the Figure4.3

between 1992 and 1998. It also shows that the amount of the foreign debt has been almost doubled between 1992 and 1998.

Russia received its first loan from the IMF in April 1992, for $1 billion. In 1993, the Kremlin was given another loan, this time for $1.5 billion. A year later the IMF provided still another $1.5 billion. Prior to March1996, the largest amount of money given to Russia from the IMF was $6.8 billion in April 1995. By December 31, 1995, the Russian central government had borrowed over $10 billion through the IMF. When on March 26, 1996, the IMF and the Russian central government reached a final agreement on a new loan of $10.2 billion—the second-largest loan package ever made to any borrower by the IMF-many outside observers were dumbfounded (Cox, 2000). With the 1996 loan, the Russian central government had borrowed over $ 20 billion from the IMF alone.

Figure4.3: Stock of federal debt as percentage of GDP



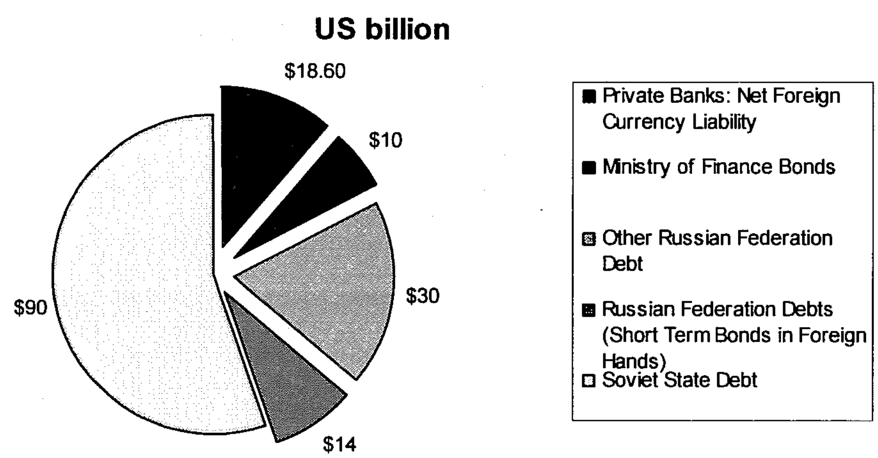
Source: (OECD, JPMorgan, Fitch IBCA, Goskomstat and RECEP. The internal debt includes Treasury bills and bonds (GKO, OFZ, and OVVZs) and no other debt items- Komulainen 1999)

A further $30 billion in direct bilateral assistance had been given to the Russian central government by Germany, the United States, and other countries. The debt crisis of 1998 and the strong devaluation of the national currency have worsened significantly foreign debt indicators of the Russian Federation. The Russian treasury market was showing signs of collapse as a high sky interest rate failed to attract foreign investors.

By July 1998, Russia's foreign currency reserves had fallen to $12 billion, down more than $3 billion from the month before (Cox, 2000). As a result the Clinton administration and the IMF chose to proceed with the new aid package. On July 20, 1998 the IMF board gave out the first tranche in the amount of $4.8 billion from $22.6 billion loan to the federal government.

In 1999 Russia owed more than $150 billion to the West, including over $90 billion from its Soviet-era debt to Western governments (the Paris Club), and $51 billion of post-1992 Russian Federation debt. This *new* debt involves $19 billion to the IMF; $18 billion to Western commercial banks (the London Club), Eurobonds, and bilateral foreign government loans; and $14 billion in Rubble-based short-term treasury bills (GKO) and short-term bonds (OFZ) held by the foreigners (Cohen 1999). Figure4.4 shows Russia's debt structure in 1999.

Figure4.4: Structure of Russia's foreign debt (Total Debt in 1999: $ 148 billion)



Source: (WEFA 1999; and Cohen 1999)

Debt servicing capability of Russian Federation strongly depended on the development of current account surplus, which , in turn, was determined by the evolution of the real exchange rate and the world market prices of country's main export products such as oil and gas. Sustainable decrease in global prices during 1998 has been one of the major reasons for the Russia's failure to fulfill its liabilities. In addition, in November 1997, after the onset of the East Asian crisis, the Rubble dramatically lost its value and the CBR that preserved the national currency, lost approximately $6 billion (U.S. dollars) in foreign-exchange reserves. (Choido and Owyang 2002, 12). The vulnerable credit market, out of the government control escalating fiscal deficit and the expectations of devaluation or rising inflation have been the major factors of a speculative attack trigger.

The Clinton strategy and the IMF prescription of the considerable aid surge to the federal government as a substitute for the construction of a free enterprise system and as a reliable remedy from growing indebtedness in Russia had proved a historic mistake of financial proposition. The decision makers as well as the executives immediately began to build a wall between their policy and its consequences.

4.4. Macroeconomic Consequences

The disaster spread immediately through Russia and a wave of chaos followed on August 17, 1998. In just 24 hours, some retailers raised prices by more than 30% (Bohlen, 1998). The government was neither able to finance itself nor to pay off its financial liabilities. Banks, both foreign and national, at the edge of bankruptcy could not collect debts from the government. Companies dependent on banks were unable to get credits from banks. Most of the enterprises had incredible wage arrears. The state and some of the major banks repudiated the payment of their domestic and foreign debts. There was a burst of inflation. In1998, the GDP decreased, industrial production fell and the inflation rate was 84 percent (Samal 2005, 6).

Reckless privatization of various sectors caused most of the state enterprises to be sold out at far lower price than their actual value used to be. As a response to this, the government involvement in the economy increased and de facto re-nationalization took place. The financial assistance and reforms were costly so that GDP shrank by 4.9 percent in 1998 (Pinto et al., 2004).

Pursuant to the August 1998 financial crisis, temporary restrictions were imposed on all capital accounts and foreign exchange transactions operated by Russian residents. The withdrawal of deposited funds was allowed only in Rubble transactions, even from accounts established in U.S. dollars. Individual deposits in Russian banks totaled $ 27 billion before August 17, which fell to less than $12 billion in total value (Cox, 2000). Millions of ordinary men and women lost their savings. Numerous credit institutions became insolvent and disappeared. Disappointed depositors besieged bankrupt banks demanding their money and finding out how ridiculously they have been annihilated. Unemployment spurt the country. Those who were still employed soon realized their salaries would be frozen. Finally receiving salaries, "the average Russian saw his or her wages drop by two-thirds, from $160 to $55 per month" (Boone and Johnson, 1999b). The number of people surviving below the official poverty line was close to 40%. The standard of living for the average Russian, already destroyed by the Western reforms, dropped by another 30% (BISNIS 2000). During only six month of the 1998 crash, Russia's economy declined by more than two-thirds. From $422 billion in 1997, Russia's GDP decreased to only $132 billion by the end of 1998 (Cox, 2000). The Russian stock market lost 90% of its value in 1998 alone (Boone and Johnson, 1999b). Figure4.5 shows the free fall of Russia's stock market exchange rate in 1998.

Foreign investment in Russia plummeted by 60% due to the panic among investors. By the first week of September, the Rubble had lost 60% of its value. (Freeland, 1998). The effect of aid-plus-reform package has already been visible in 1998 but has become even more pronounced in March 1999 when the Rubble had lost 75 % of its value (Cox, 2000). With the Rubble dropping abruptly in value every day, retail stores were closed repeatedly during the day, just to calculate how much to charge. Those Russians who had been using Western products could not afford it any more because of exorbitant import prices. The destruction of international trade not only diminished the supply of foreign goods, but also affected Russian-made goods with foreign components. De-indexation of wages reflected purchasing power and declined personal consumption. The scarcity of liquidity in circulation forced Russia to barter economy. Farmers were wiped out by the 1998 economic crash and especially by the sudden Rubble devaluation as their grain harvests fell 30% below 1997 levels (Bohlen, 1998). Due to the lack of food staples in particular meat and cooking oil humanitarian food aid from the West was considered on an emergency basis.

Figure4.5: Russian stock market exchange rate between 1995 and 2000

Source: (Choido and Owyang 2002)

Understanding that many well-connected insiders had avoided consequences of default and devaluation by converting their Rubbles into hard currency was very exasperate for ordinary Russian people. Strong suspicion that the IMF bail out had been used to provide insiders with *some* financial assistance was fuelled by the Russian Central Bank decision to select several banks for government credits and restoration of their liquidity. The banks included those held by several powerful oligarchs. A month after the devaluation Dmitry Vasiliev, former chairman of Russia's Federal Security Commission told the *Los Angeles Times: The (IMF) money is all spent, It went to foreigners and Russian speculators, including the Central Bank. They got payments for their GKO, converted the Rubbles into cheap dollars, and took the money out of the country"* (Cox, 2000).

4.5. Social Consequences

Dramatic changes in the patterns of employment, life style, and life expectancy were the indirect outcomes of the foreign aid and experienced crisis that will be discussed in this section. Any crisis has negative social consequences, and Russia's has been no exception. The number of impoverished people increased sharply after the crisis. In addition to the unemployment, lost wages and pensions, and financial hardship, there has been an evident social crisis. Those who were sick or under a doctor's care were badly injured by the crash. Russia's healthcare system, in poor conditions even before August 1998, suffered a run on medicine that quickly reduced supplies in hospitals and pharmacies below the Soviet-era levels (Willimas, 1998).

The 1998 economic disaster also contributed to Russia's demographic crisis. "According to the Russian Statistics Agency, Russia's population has fallen every year since 1992. (Yablokova, 2000). Deaths outnumbered births by 784,000 in 1999, the year following the crash (Cox, 2000). Organized crime and overall economic depression accompanied by the deterioration of living conditions increased drug addiction and alcoholism, Russia's chronic problem. Russia's economic productivity had dropped by half and its investment had fallen by three-fourths since 1991, with no recovery conceivable. Statistical records revealed that the economic and social collapse resulted in more than two million premature deaths since 1991, due to dramatic increases in alcoholism, murder and suicide, infectious diseases, and stress-related disorders (Kotz, 1998). This has been the meaning of the Western-inspired "aid and reforms" to a majority of public and private sector workers in Russia. Any visitor to Russia could see the impact of the IMF policy package. In fact, developing Russian economic programs was never discussed with its own economists or parliament. The situation was sensible though; the Russian government should have granted the IMF consent before receiving its financial aid, and that was why the IMF systematically advised, publicly supported and worked with the Russian elites (Desai, 2006, 32). As a result, a survey conducted in December 2004 showed that 70 percent of the Russian population thought the country was headed in the wrong direction in 1999 and 41 percent of the population viewed the economy's performance as "poor" (Easterly, 2006d, 65).

Russia's distinctive economic problems -most significantly its debt burden challenge and corruption- could have been a useful lesson for other transition economies. Understanding the concept of Russia's foreign aid package leads to the fact that a sustainable macroeconomic stabilization will not be possible unless a strong budget is made available for the enterprises before and during the reforms. The impact of macroeconomic policy on country's prosperity is closely related to the real sector through real exchange and real interest rates. A macroeconomic environment restricted by the insufficient fiscal policy (with foreign debt, budget cuts, wage arrears and non payments) will fall short of its basic objectives and eventually overturn the economic stabilization (Pinto et al., 2004, 25).

Another valuable lesson to be learned is that devaluation as a remedy should be considered with suspicion if it is implemented in an environment of: (a) weak growth perspectives, (b) an appreciating real exchange rate, and (c) escalating fiscal deficits. This mixture can only mean that increasing public debt through aid surge is a warning alarm for any economy and will eventually lead to a collapse in economic welfare. In fact government's efforts to shrink inflation at the cost of running huge fiscal deficit would never be a justifiable policy and it should be considered as a trigger of potential financial difficulties.

The other significant point is that the macroeconomic and social costs of the aid-plus-reforms package must be carefully interpreted. In Russia's case, rescuing enterprises through the non-payment system led to the public debt accumulation. "If Russia is to learn any lesson from the past debacle, it must at a minimum make financial market participants (including banks) fulfill their primary role in a functioning economy - to provide financial resources for economic development" (Semilutina and Burt 1999, 2).

After the failure of aid reforms, the government had developed emergency measures to recover economy from a long period stagnation. The main measures were directed on shrinking aid from the foreign investors, increasing role of the government in leading economic development, strengthening and protecting domestic industries as well as domestic market, repaying wages and pensions and etc.

5. Concluding Remarks

This paper considered "foreign aid" from a broad theoretical background as an integral part of the governments' foreign policy and as an essential instrument that contributes to the development process. It was demonstrated that financial assistance has undergone a number of significant structural changes including the decline of multilateral aid, the significant increase in the share of Nordic countries and Japan in the provision of foreign aid, and a shift in the allocation of resources from Asia to Africa. The paper established the argument to show that despite the allegedly valid criticisms, poverty would be higher in the absence of external recourses because foreign aid creates positive benefits for poor and stimulates their participation in the growth process by increasing public expenditure and providing access to health care, education, water resources and etc.

Based on the relevant data available from previous empirical studies, the paper hypothesized that a significant share of aid has been allocated and distributed based on strategic, commercial, or short-term political reasons, while an insignificant amount was left to initiate and support long-term infrastructure development projects. This, in turn, led to large fluctuations and volatility in the amounts of external capital flows that made it impossible for the recipients to utilize aid for long-term investments. In addition, aid tying policies often practiced by bilateral donors posed other problematic restrictions in the process of economic development such as transfer of inappropriate technology, suboptimal use of both aid and national funds, rent-seeking in the donors' economy and economically unjustified projects. The paper also concluded that poor countries did not have the opportunity to take an active role in the process of policy formation, distribution and allocation of aid. Due to these reasons foreign recourses were misallocated and did not correspond to the gap between the actual recipients' needs and the aid provided.

The above-said arguments were also discussed for a practical case study. The context was established to address the role of multilateral financial assistance in the onslaught of Russia's economic meltdown; the factors included: (i) an implementation of the loan-based macroeconomic conditionalities under the IMF supervision, (ii) ballooning fiscal deficits and debt, and (iii) accelerating full spectrum of the market reforms. Using different approaches, the paper showed that Russia following the advice of Western economists experienced serious crises in 1992 and 1998, which in turn, were accompanied with drop in personal income, rapid impoverishment of population and the fastest privatization process ever seen in the world economy. The government role on banks, retails, service providing sectors, and import/export trade became limited as urged by the IMF advisors. The implemented macroeconomic policy led to the dramatic and irreversible changes in many aspects including huge budget cuts, new pricing system, handover of the small-size industry and property ownership to the private sector, restructured tax regulations, and free fall of the national currency. The necessity of investment in development of domestic production, manufacturing, agriculture and local industry sector was meaningfully overlooked and instead replaced by addicted government borrowing. It was shown that transition toward market economy was far from its original objectives.

The paper also showed that the absence of certain fundamental economic regulations has been the main cause for the significant increase in the risk of foreign and domestic investments. The comments invited on the previous practice of financial aid provided by multilateral institutions could be used as constructive lessons for economic relieve of the emerging economies suffering from debt burden and the shortage of liquidity. The major lessons included: (i) implementation of the reforms in vital sectors of economy through gradual staging instead of accelerating reckless development; (ii) wise consideration of advices from the international financial institutions and avoidance of the long-run dependence on foreign aid; (iii) maintenance of the government's intervention and supervision role during and after the foreign contribution rather than dismissal of the government's controlling function.

In reality, foreign aid and poverty reduction programs are subject to policy trade-offs, rather than policy solutions. Considering the fact that regulatory agencies and policy institutions, such as markets, are not absolutely perfect in their functions, the paper concludes that the "solution" to this potential problem may not be always feasible or easily found. For instance, the Poverty Reduction Growth Facility launched by the IMF in 1999 was meant to replace the role of SAP and improve the Foreign Aid system. Yet the new program entailed only minor changes and based on the empirical evidence it is still far behind its expected targets in terms of the global economic development. The paper believes that foreign aid offered to developing countries is an essential initiative because of their incapability to employ their own deficient resources. However, it must be noted that since the external capital alone is not able to stimulate and maintain sound economic development, foreign aid should not serve as a permanent substitute for the mobilization of their domestic resources.

As a general proposition, significant changes in the mechanism of delivering foreign aid may result in boosting investment and an economic activity. It is concluded that donor countries should: (i) minimize the usage of tied bilateral aid and increase debt relief programs, (ii) consider recipient interests as a principal determinants of their bilateral policy, (iii) encourage regional integration of developing countries to mitigate their disadvantages such as a small size of the economies, (iv) wisely consider aid surge by applying case-by-case approach and by taking into consideration the absorptive capacity of the recipients in order to avoid excessive spending, (v) employ initiatives that increase the reliability and predictability of aid, (vi) improve the allocation of external resources by deliberating recipients' needs, population size and performance, (vii) ensure participation of the poor countries in the identification, design and implementation of the aid programs, (viii) monitor the acceleration of reforms aiming at tackling corruption by poor countries, and (ix) simplify, coordinate and harmonize the process of aid programs to decrease the burden on developing countries.

Taking into account the recent pledges of donor countries to significantly increase the allocation of foreign aid, the future challenges for research should rather focus on: (a) identifying the impact of temporary and permanent increase in different types of aid, (b) proposing remedies to the experienced economic damage, and (c) refining the future strategic economic plans for the Third World.

REFERENCES:

Abdiweli, M. A., and Hodan S. I. (2006) An Empirical Analysis of the Determinants of Foreign Aid: A Panel Approach." International Advances in Economic Research, Vol. 12, Page 241–250.

Alesina, A. and Weder, B. (2002) "Do Corrupt Governments Receive Less Foreign Aid?" The American Economic Review, Vol. 92, No. 4, Page 1126-1137.

Alesina, A., and Dollar, D. (2000) "Who Gives Foreign Aid to Whom and Why?" Journal of Economic Growth, Vol. 5, Page 33–63.

Anderson, E., and Waddington, H. (2006) "Aid and the MDG poverty target: How much is required and how should it be allocated?" ODI Working Paper No.275.

Annan, K. (2003) "Development funds moving from poor countries to rich ones" UN News Center, http://www.un.org/apps/news/story.asp?NewsID=8722&Cr=financing&Cr1=development# (August 13, 2007).

Azam, J. P. and Laffont, J. J. (2003) "Contracting for aid." Journal of Development Economics, Vol. 70. Page: 25-58, Page26.

Barber, B. R. (2002) "Beyond Jihad vs Mcworld: on terrorism and the new democratic realism, The Nation Magazine, Vol. 274, No. 2, Page 11-18

Bauer, P. T., (1972) "Dissent on Development: Studies and Debated in Development." Economics, Cambridge: Harvard University Press.

Beitz, C. (1979) Political Theory and International Relations Princeton University Press, N.J, Page.136-143.

Berthélemy, J. C. (2006) "Bilateral Donors' Interest vs. Recipients' Development Motives in Aid Allocation: Do All Donors Behave the Same?" Review of Development Economics, Vol., 10, No.2, Page 179–194.

Beynon, J. (2001) "Policy Implications for Aid Allocations of Recent Research on Aid Effectiveness and Selectivity" revised version of the Paper presented at the Joint Development Centre/DAC Experts Seminar on "Aid Effectiveness, Selectivity and Poor Performers",OECD, Paris, Page 1-61.

BISNIS, Department of Commerce, Commercial Overview of Russia, http://www.bisnis.doc.gov/bisnis/new_bisnis.cfm (August 13, 2007)

Bohlen. C. (1998) "Ruble's Crash Sets Off Boom in Survival Strategies" N.Y. TIMES, (August 30), Page A1.

Boone, P. (1996a) "Politics and the Effectiveness of Foreign Aid." European Economic Review, Vol. 40, No. 2, Page 289-329.

Boone, P. and Johnson, S. (1999b) "Russia After Yeltsin: Economic Alternatives: Boom or Bust or Both," paper prepared for "Russia Post Yeltsin," Wye River Conference, (August 19-20).

Buch, C. M., Heinrich, R. P., Lusinyan, L., and Schrooten, M. (2000) "Russia's Debt Crisis and the Unofficial Economy." Kiel Institute of World Economics Working Paper No. 978.

Bulir, A. and Hamann A. J. (2003) "Aid volatility: an empirical assessment." IMF Staff Papers, No. 50. Page 65–89.

Burnside, C. and Dollar, D. (2000) "Aid, Policies, and Growth." American Economic Review, Vol.90. No.4, Page 847-868.

Cassen, R. (1994) Does Aid Work, Second Edition." Oxford: Clarendon Press, Pages 15, 16, 203 and 210.

Chang, H.S., Fell A. M., and Laird M. (1999) "A Comparison of Management Systems for Development Co-operation in OECD/DAC Members." Paris: OECD, Page 14.

Chiodo, A., J. and Owyang, M.T. (2002) "A Case Study of a Currency Crisis: The Russian Default of 1998." The Federal Reserve Bank of St. Louis. (November/December), Page 7-17.

Clemens, M. A., Radelet S., and Bhavnani R., (2004) "Counting chickens when they hatch: The short-term effect of aid on growth." Center for Global Development Working Paper, No. 44, Page 1-71.

Cogneau, D., and Naudet, J. D. (2005) "Who deserves aid? Equality of opportunity, international aid and poverty reduction" Ibero America Institute for Economic Research (IAI) Discussion Papers, No 110. Page 1-28.

Cohen, A. (1999) "What Russia Must Do To Recover From Its Economic Crisis?" The Heritage Foundation Backgrounder No. 1296.

Collier, P. and Dehn J. (2001) "Aid, Shocks and Growth." World Bank Policy Research Working Paper, No 2688. Page 1-21.

Collier, P., and Dollar, D. (2002) "Aid Allocation and Poverty Reduction." European Economic Review, Vol. 46, No. 8, Page 1475-1500.

Collier, P., and Hoeffler A. (2002) "Aid, Policy and Growth in Post-Conflict Countries" World Bank Policy Research Working Paper, No.2902. Page1-23.

Corbridge, S. (1993) Debt and Development, Oxford: Blackwell, 1993, Page 81.

Cox, A., and Heale, J. (1998) "Promises to the Poor: the Record of European Development Agencies" ODI Poverty Briefing, http://www.odi.org.uk/Publications/briefing/pov1.html (August 13, 2007)

Cox, C. (2000) "Russia's Road to Corruption- Chapter 8 -1998: Years of Bad Advice Culminate In Russia's Total Economic Collapse" The Report provided to the House of Representatives, Washington, D.C. http://www.fas.org/news/russia/2000/russia/part08.htm (August 13, 2007)

Dalgaard, C. J., and Hansen, H. (2001) "On Aid, Growth and Good Policies." Journal of Development Studies, Vol.37, No.6, Page 32.

Desai, P. (2003a) Financial Crisis, Contagion, and Containment- From Asia to Argentina. New Jersey: Princeton University Press.

Desai, P. (2005b) Conversations on Russia. New York : Oxford University Press. Page 35.

Devarajan, S., Miller, M., and Swanson, E. V. (2002) "Goals for Development: History, Prospects and Costs." World Bank Policy Research Working Paper No. 2819.

Dreher, A. and Jensen, N. (2007) "Independent Actor or Agent? An Empirical Analysis of the Impact of US Interests on IMF Conditions." Journal of Law & Economics, Vol. 50, No.1, Page 105-124.

Easterly, W. (2005c) "What did structural adjustment adjust?: The association of policies and growth with repeated IMF and World Bank adjustment loans." Journal of Development Economics, Vol. 76, Issue 1, Page 1-22.

Easterly, W. (2006d) The White Man's Burden: Why the West's Efforts to Aid the Rest Have Done So Much Ill and So Little Good, New York: Penguin Press. Page 61.

Easterly, W., Levine, R., and Roodman, D. (2003a) "New data, new doubts: Revisiting 'Aid, Policies, and Growth." Center for Global Development Working, Paper No. 26. Washington.

Easterly, W., Levine, R., and Roodman, D. (2004b) "New Data, New Doubts: A Comment on Burnside and Dollar's article [Aid, Policies, and Growth- 2000]" The American Economic Review, Vol.94, Issue 3, Page 774-780.

Ehrenfeld, D. (2004) "Foreign Aid Effectiveness, Political Rights and Bilateral Distribution" The Journal of Humanitarian Assistance, http://www.jha.ac/articles/a128.htm, and http://jha.ac/2007/01/01/pre-2007-archives/ (on-line Journal accessed in August 01, 2007)

Feeny, S. (2005) The impact of aid on economic growth in Papua New Guinea. Journal of Development Studies. Vol.41, No.6, Page 1092-1117.

Fielding, D., and Mavrotas, G. (2005) "The volatility of aid." Discussion Paper 2005/2006. UNU–WIDER, Helsinki.

Fieleke, N. S. (1994) "The International Monetary Fund 50 Years After Bretton Woods." New England Economic Review, Page17-30.

Fleck, R. K. and Kilby, C. (2006) "World Bank Independence: a Model and Statistical Analysis of US Influence." Review of Development Economics, Vol.10, No.2, Page 224-240.

Foster, M. and Leavy, J. (2001) "The Choice of Financial Aid Instruments." Overseas Development Institute, Center for Aid and Public Expenditure Working Paper No. 158, Page 1-40.

Foster, M., and Keith, A. (2003) "The Case for Increased Aid" Report to the International Department for Development, Vol. 1: Chelmsford: UK.

Foster, M.., and Killick, T. (2006) "What Would Doubling Aid do for Macroeconomic Management in Africa?" ODI Working Paper, No. 264.

Freeland, C. (1998) "Ruble [sic] plunges to 13.46 against dollar," FINANCIAL. TIMES.

Friedman, M., (1958) “Foreign Economic Aid: Means and Objectives.” Yale Law Review, Vol. 47, Page 24-38.

Fukuda-Parr, S. (2004) “The Millennium Development Goals: The Pledge of World Leaders to End Poverty Will Not Be Met With Business As Usual.” Journal of International Development, Vol.16, Page 925-932.

Gemmell, N., and McGillivray, M. (1998) “Aid and tax instability in the government budget constraints in developing countries.” CREDIT Research Paper 98/1. University of Nottingham: Nottingham.

Gomanee, K., Girma, S., and Morrissey, O. (2005) “Aid, Public Spending and Human Welfare: Evidence From Quantile Regressions.” Journal of International Development, Vol. 17, Page 299-309.

Gounder R. (2001a) Aid-growth nexus: empirical evidence from Fiji.” Applied Economics, Vol. 33 .Page 1009–1019.

Gounder R. (2002b) “Empirical evidence of the relationship between foreign aid and economic growth: the case of the Solomon Islands.” In New Perspectives on Foreign Aid and Economic Development, Mark Arvin B (ed.), Praeger: Westport.

Grant, R., and Nijman, J. (1998) The Global Crisis in Foreign Aid New York: Syracuse University Press, Page186–190.

Hansen, H., and Tarp F. (2000) “Aid Effectiveness Disputed.” Journal of International Development, Vol.12, Page 375-398.

Hefeker , Carsten. 2006. “Project Aid or Budget Aid? The Interests of Governments and Financial Institutions.” Review of Development Economics, Vol. 10, No.2, Page 241–252.

Hjertholm, P. and White, H. (1998) “Survey of Foreign Aid: History, Trends and Allocation.” Institute of Economics, University of Copenhagen, Discussion paper # 00-04, Page 1-126.

Jackson, R. H. (1990) Quasi-states: Sovereignty, International) Relations and the Third World, Cambridge: Cambridge University Press, Page120.

Jepma, C. J. (1997b) “On the Effectiveness of Development Aid.” World Bank, unpublished document.

Jepma, C. J.. (1991a) “The Tying of Aid” Development Center of the Organization for Economic Co-operation and Development. OECD, Paris, Page 1-37.

Jolly R., Fukuda-Parr, S., Jahan, S., (1999) “Human Development Report: Globalization with a Human Face”, Published for the United Nations Development Programme (UNDP), New York, Page 14.

Kagarlitsky, B. (1998a) "Collapse of the Russian Ruble", Red Pepper (Global Policy Forum-New York)

Kagarlitsky,B.(2000b) “Kagarlitsky on Russia/IMF”, http://www.nadir.org/nadir/initiativ/agp/free/imf/europe/russia.htm (August 13, 2007).

Karras, G., (2006) “Foreign Aid and Long-Run Economic Growth: Empirical Evidence For A Panel of Developing Countries.” Journal of International Development, Vol. 18, Page: 15-28.

Katima, J. (2005) Katima, J. (2005) “Poverty Reduction And Environmental Management: Challenges and Opportunities” Proceeding of the Discourse on Engineering Contribution in Poverty Reduction, Annual Engineering Day 2005 Conference, Page 1-10.

Kohama, H., Sawada, Y., and Kono, H. (2003) “Aid, Policies, and Growth Reconsidered” Page 1-14. Paper presented at an experts’ research workshop on "Quantifying the Impact of Rich Countries’ Policies on Poor Countries” at the Center for Global Development (CGD).

Komulainen, T. (1999) “Currency Crisis Theories –Some Explanations for the Russian Case Bank of Finland.” BOFIT Discussion Papers, No. 1.

Kotz, D. M. (1998) ”Capitalist Collapse How Can Russia Recover?” Dollars and Sense magazine, (November/December). http://www.thirdworldtraveler.com/Economics/CapitalistCollapse_Russia.html (November 19, 2006).

Langhammer, R. J. (2004) “Halving Poverty by Doubling Aid: Is There Reason for Optimism?” The World Economy, Vol. 27, Issue 1, Page 81-98.

Lensink , R. and Morrissey O. (2000) Aid instability as a measure of uncertainty and the positive impact of aid on growth. Journal of Development Studies , Vol. 36, No. 3, Page 31–49.

Lensink, R., and White, H. (2001) “Are There Negative Returns to Aid?” Journal of Development Studies, Vol. 37, No. 6. Page 42–64.

Levin V., and Dollar, D. (2005) “The Forgotten States: Aid Volumes And Volatility in Difficult Partnership Countries (1992-2002)” DAC Learning And Advisory Process On Difficult Partnerships, Page 1-56.

Lu, S., and Ram R. (2001) “Foreign aid, government policies, and economic growth: further evidence from cross-country panel data for 1970–1993.” International Economics, Vol. 54. Page 15-29.

Malki, E. (1999) "The Financial Crisis in Russia", Working Paper Series in Economics, WoPEc http://129.3.20.41/eps/mac/papers/9901/9901001.html (August 13, 2007).

Margolin, R. (2000) "The Russian Financial Crisis: From Craze to Crash", The Stern Journal, New York University.

McGillivray, M., and Noorbakhsh F. (2004) “Aid, Conflict and Human Development.” Paper presented at the conference “Making Peace Work”, World Institute for Development Economics Research, United Nations University, Helsinki, Page 1-21.

Meltzer, A. H. (2000), “International financial institutions reform: report of the International Financial Institution Advisory Commission”, International Financial Institution Advisory Commission , US Congress.

Menocal, A. R., and Mulley S. (2006) "Learning from experience? A review of recipient government efforts to manage donor relations and improve the quality of aid" ODI Working Paper No.268.

Morrisey, O. (2004) "Aid and Poverty in Sub-Saharan Africa" Paper for the IV Mediterranean Seminar on International Development, Africa's Tragedy, University of the Balearic Islands, Palma de Mallorca.

Murrell, P. (1993) "What is Shock Therapy? What did it do in Poland and Russia?" Post-Soviet. Affairs, Vol. 9, No. 2, Page 111-140.

Noel, A., and Therien, J. P. (1995) "From Domestic to International Justice: The Welfare State and Foreign Aid." International Organization, Vol. 49, No. 3, Page 549.

Norsworthy, A. (2002) "Assisting Russia's Transition: An Unprecedented Challenge." World Bank Operations Evaluation Department Precis. No. 225 http://lnweb18.worldbank.org/oed/oeddoclib.nsf/DocUNIDViewForJavaSearch/D3510EBF43FA332B85256C3100554D61/$file/Precis_225_Russia.pdf (August 13. 2007).

North, D. (1981) Structure and Change in Economic History, New York: Norton.

Nunnenkamp, P., and Thiele, R. (2006) The World Economy. Targeting Aid to the Needy and Deserving: Nothing But Promises? Vol.29, No.9. Page 1177-1201.

Odling-Smee, J. (2006) "The IMF and Russia In The 1990s." IMF Staff Papers, Vol.53, No.1. Page 151-194.

OECD (1986a), Report - Twenty-Five Years of Development Co-operation – A Review (Efforts and Policies of the Members of the Development Assistance Committee), Paris: OECD. Page 92-98.

OECD, (2005c) "Development, Donor Aid Charts" The information adopted from the OECD on-line website http://www.oecd.org/dataoecd/17/39/23664717.gif (August 13, 2007).

OECD, (2005d) "Glossary of Terms used in the 2005 draft outcome document for the UN World Summit" The information adopted from the OECD on-line website, http://www.oecd.org/document/13/0,2340,fr_2649_33721_35320141_1_1_1_1,00.html (August 13, 2007).

OECD, (2005e) "OECD Final Oda Data For 2005", http://www.oecd.org/dataoecd/52/18/37790990.pdf (August 13, 2007).

OECD, (2006f) "DCA list of ODA recipients effective from 2006 for reporting on 2005, 2006 and 2007", The information adopted from the OECD on-line website, (August 13, 2007) http://www.oecd.org/dataoecd/23/34/37954893.pdf

OECD, (2007j) "OECD Net Official Development Assistance In 2006", http://www.oecd.org/dataoecd/14/5/38354517.pdf (August 13, 2007).

OECD, (2007h) The information adopted from the DAC's on-line website glossary; (August 13, 2007), http://www.oecd.org/glossary/0,3414,en_2825_293564_1965693_1_1_1_1,00.html

OECD-DAC, (1996b) "Shaping the 21st Century: The Contribution of Development Co-operation." Paris: OECD. Page 1-24.

Olsen, G. R. (1998) "Europe and the Promotion of Democracy in Post Cold War Africa: How Serious Is Europe and for What Reason?" African Affairs, Vol. 97, No. 388, Page 343-367.

Pallage, S., and Robe, M. A. (2001) Foreign aid and the business cycle." Review of International Economics, Vol. 9, Page 636–667.

Pattillo, C., Polak, J., and Joydeep, R. (2007). "Measuring the Effect of Foreign Aid on Growth and Poverty Reduction or The Pitfalls of Interaction Variables", IMF Working paper, No. WP/07/145. Page 1-15.

Paul, E. (2006) "A survey of The Theoretical Economic Literature on Foreign Aid." Asian-Pacific Economic Literature, Vol. 20, No.1, Page 1-17.

Pinto, B. Gurvich E., and Ulatov, S. (2004) "Lessons from the Russian Crisis of 1998 and Recovery." Managing Economic Volatility and Crises: -A Practitioner's Guide, Cambridge University Press.

Rajan, R. G., and Subramanian, A. (2005) "Aid and Growth: What Does the Cross-Country Evidence Really Show?" IMF Working Paper, No. WP/05/127, Page 1-49.

Ram, R. (2004) "Recipient Country's Policies and The Effect of Foreign Aid On Economic Growth in Developing Countries: Additional Evidence." Journal of International Development, Vol. 16, Page 202.

Ratha D., Shaw W., and Dadush, U. (2006) "Report: Global Prospects Overview and Global Outlook" Development Prospects Group (DECPG); The International Bank for Reconstruction and Development / The World Bank, NW, Page 9.

Rogerson, A., Hewitt, A., and Waldenberg, D. (2004) "The International Aid System 2005–2010 Forces For and Against Change." ODI Working Paper No. 235.

Rogoff, K. (2002) "Has Russia Been on the Right Path?" A Commentary. International Monetary Fund, www.imf.org/external/np/vc/2002/082602.htm (August 13, 2007).

Rowley, C. K., (2000) "Political Culture and Economic Performance in sub-Saharan Africa." European Journal of Political Economy, Vol.16, Issue 1, Page 133-158.

Ruttan, V. W., (1989) "Why Foreign Economic Assistance?" Economic Development and Cultural Change, Vol. 37, No. 2, Page 411-424.

Sachs, J. (2005) The End of Poverty: Economic Possibilities for Our Time, New York: Penguin Press, Page 204.

Samal, K. C. (2005) "Transformation of Enterprises in Russia." The Journal of Entrepreneurship- Sage Publications, Vol.14, No.1, Page 21-37.

Sandler, T., and Arce, D. G., (2007) "New Face of Development Assistance: Public Goods and Challenging Ethics." Journal of International Development, Vol. 19, Issue 4, Page 527-544.

Schraeder, P., Hook, S., and Taylor, B. (1998) "Clarifying the Foreign Aid Puzzle: A Comparison of American, Japanese, French and Swedish Aid Flows," World Politics, Vol.50, No.2. Page 294–320.

Schreiner, M. (2002) "Aspects of Outreach: A Framework For Discussion of The Social Benefits of Microfinance." Journal of International Development, Vol.14, Page 591-603.

Schwalbenberg, H. M. (1998) "Does Foreign Aid Cause the Adoption of Harmful Economic Policies?" Journal of Policy Modeling, Vol. 20. No.5.Page 669–675.

Selim, T. H. (2005) "A Comparative Essay on the Causes of Recent Financial Crises" The American University in Cairo, Egypt, www.aucegypt.edu/academic/economics/papers/wk7.pdf (August 13, 2007).

Semilutina, N. G. and Burt.J.A. (1999) "Financial Crisis in Russia: Ignoring Fundamentals." Russian Commerce News; Russian-American Chamber of Commerce, Vol. 7. No. 3.

Sharma, S. 1997. "Changing Pattern of External Resource Flows." Social Scientist, Vol. 25, No. 11/12, Page 48-63.

Shestakov, V. (2000) "IMF versus Russia." Ecological North West Line , St. Petersburg, Russia, http://www.nadir.org/nadir/initiativ/agp/free/imf/europe /imf_russia.htm (August 13, 2007).

Stokke, O. (1996) Foreign aid Towards the Year 2000: Experiences and Challenges, London, Page 74.

Sutela, P. (1999) "The Financial Crisis in Russia." BOFIT Discussion Papers, No. 11.

Svensson, J. (2000a) "Foreign Aid and Rent-Seeking", Journal of International Economics, Vol. 51, No.2, Page 437-461.

Svensson, J. (2003b) "Why Conditional Aid Doesn't Work and What Can Be Done About It?" Journal of Development Economics, Vol. 70, No.2, Page 381-402.

Therien, J. P. (2002) "Debating Foreign Aid: Right Versus Left." Third World Quarterly, Vol 23, No 3, Page 449–466.

Trumbull, W. N. and Wall, H. J. (1994) "Estimating Aid-Allocation Criteria with Panel Data" Economic Journal, Vol. 104, Page 876-882.

UN Resolution, (1970) "International Development Strategy for The Second United Nations Development Decade". United Nations General Assembly Resolution 25th Session Report No 2626 (XXV), United Nations, Page 39-49.

UNDP, (2000) "Human rights and human development" Human Development Report 2000, http://hdr.undp.org/reports/global/2000/en/ (August 13, 2007)

Verschoor, A., and Kalwij A. (2006) "Aid Social Policies and Pro-Poor Growth." Journal of International Development, Vol. 18, Issue 4, Page 519-532.

Watkins, K. (2006) "Beyond scarcity: Power, poverty and the global water crisis" Human Development Report 2006 Published for the United Nations Development Programme (UNDP).

Weissman, R. (2001) “Twenty Questions on the IMF.” Third World Traveler, http://www.thirdworldtraveler.com/Globalization/Twent_Questions_DGE.html (August 13, 2007).

White, H., and McGillivray, M. (1995) “How Well Is Aid Allocated? Descriptive Analyses of Aid Allocation: A Survey of Methodology and Results,” Development and Change, Vol. 26, Page 163-183.

Williams, D., "Russian Crisis Sapping Health Care System," WASHINGTON POST. (September 10). 1998. Page A26.

Wood, R. E. (1986) From Marshall Plan to Debt Crisis: Foreign Aid and Development Choices in the World Economy, Berkeley, CA: University of California Press, Pages 29 and 272.

Woods, N. (2005) “The Shifting Politics of Foreign Aid” International Affairs, Vol. 81., No.2, Page 393-409.

World Bank, (1998a) Assessing Aid: What Works, What Doesn’t, and Why? New York: Oxford University Press, Page 1-118.

World Bank, (2000b) World Development Report: Attacking Poverty New York: Oxford University Press.

World Bank, (2002c) “Gender and Poverty”, The information adopted from the World Bank (-Database of Gender Statistics) on-line website, (August 13, 2007) http://genderstats.worldbank.org/techPoverty.asp (August 13, 2007).

World Bank, (2007d) The information adopted from the 2007 World Development Indicators on-line website, http://siteresources.worldbank.org/DATASTATISTICS/Resources/WDI07section4-intro.pdf , (August 13, 2007).

World Bank, (2007e), The information adopted from the World Bank on-line website; (August 13, 2007) http://www.worldbank.org/ieg/hipc/about.html

Yablokova, O. (2000) "Population Takes Biggest Plunge Yet," MOSCOW TIMES, (January 26).