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ARAB DEVELOPMENT ASSISTANCE:

FOUR DECADES OF COOPERATION

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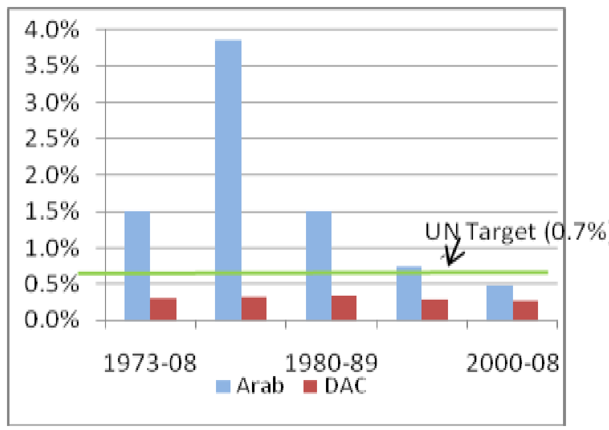
Introduction: Over the past four decades, Arab aid, which has been relatively under-studied, has played an important role in global development finance. Arab donors—predominantly the Kingdom of Saudi Arabia (KSA), Kuwait and the United Arab Emirates (UAE)—have been among the most generous in the world, with official development assistance (ODA) averaging 1.5 percent of their combined gross national income (GNI) during the period 1973-2008, more than twice the United Nations target of 0.7 percent and five times the average of the OECD-DAC countries. Arab Official Development Assistance (ODA) accounts for 13 percent of total DAC ODA on average and nearly three-quarters of non-DAC ODA.

In addition to government-to-government aid, Arab donors have established a number of specialized financial institutions to provide development assistance to low-income countries. Assistance through these institutions increased substantially by 4.4 percent per year in real terms over the period 1990-2008.

There are good reasons to believe that Arab aid will continue to play an important role in international development assistance into the foreseeable future. Arab donors have recently increased their aid volumes, and Arab financial institutions are well capitalized, with the capacity to scale up assistance.

Figure 1: Arab ODA as a Share of GNI (%)



Overview and Trends in Arab ODA: As shown in Figure 1, the share of Arab ODA in GNI was exceptionally high in the 1970s, peaking at over 12 percent for UAE and at about 8.5 percent for Kuwait and KSA in 1973. About one-third of all ODA during the 1970s was from Arab donors. High levels of Arab ODA in the 1970s and 1980s were primarily a reflection of high oil prices and, to some extent, the substantial start-up costs associated with establishing aid programs and capitalizing development funds and banks.

From this extraordinarily high starting point in the 1970s and early 1980s, levels of Arab ODA declined, although they remained well above OECD-DAC averages as a share of GNI. The downward trend can be explained by a combination of several factors. First, the levels witnessed in the 1970s and early 1980s were

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very high by international standards and could not be sustained over time. Second, fiscal space in these countries has been reduced as a result of declining oil revenues and growing national spending on wages, transfers, debt service, and social services for a growing population. Third, external factors such as regional security concerns have also reduced to some extent the fiscal space.

Aid levels have increased since 2002, both in volume and as a share of GNI, as oil prices have risen and post-conflict reconstruction needs have expanded. As in the past, most aid comes from KSA, Kuwait, and UAE, respectively. Arab ODA from these countries accounts for the bulk of non-DAC ODA, averaging nearly three-quarters during 1991-2008.

Preliminary estimates for 2008 indicate an even higher volume of aid (around US$ 6 billion and 0.7 percent of GNI) in spite of the global financial and economic crisis, with KSA accounting for the bulk of aid. The Arab ODA-to-GNI ratio remains more than twice the average of 0.3 percent of GNI among OECD-DAC members for 2008.

The Reach of Arab ODA: Over time, Arab donors have expanded their reach in terms of recipient countries—beyond Arab and predominantly Muslim countries—and in terms of sectors—beyond infrastructure. At present, Arab ODA covers a wide range of countries, and especially poor countries in sub-Saharan Africa such as Mali, Mauritania, Senegal, Somalia, and Sudan; and in Asia such as Cambodia, Bangladesh, Nepal, Pakistan, Sri Lanka, Tajikistan, and Vietnam. The Kuwait Fund, the Saudi Fund and the OPEC Fund are the most global in focus, also financing projects in Europe and Latin America. The sector focus of Arab ODA has broadened over time to include agriculture, health, education, and social services.

Focal Countries for Arab ODA: Arab aid has played a major role in total ODA flows to some countries. In Syria, Arab ODA accounts for over 70 percent of total ODA from all sources. In Morocco, Lebanon, Yemen, and Jordan, Arab ODA represents between 20 and 40 percent of total ODA. Arab ODA also accounts for 10-20 percent of total ODA in West Bank and Gaza, Somalia, Sudan, Turkey, Egypt, Mauritania, and Djibouti.

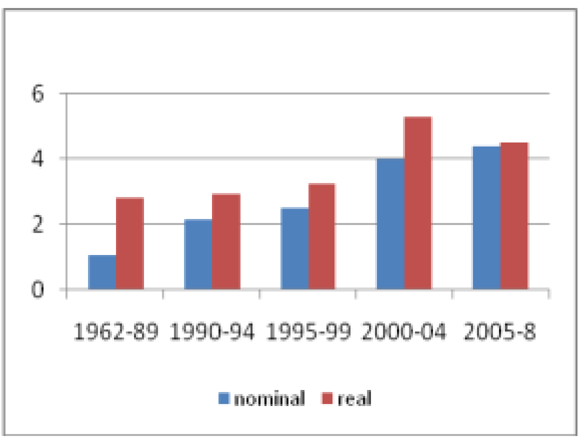
Composition of Arab ODA: The composition of Arab bilateral ODA has shifted significantly in the last decade. Until 2000, over two-thirds of Arab bilateral ODA was in the form of grants. Since then, the share of grants has dropped to 40 percent; most aid is provided in the form of soft loans. The bulk of Arab ODA (87 percent) has been provided bilaterally. The average ratio of multilateral to total ODA among Arab donors was less than half of the OECD-DAC norm (13 percent as compared to 30 percent). Of the 11 percent of Arab ODA provided through multilateral sources during 1995-2007, some 4 percent has been channeled through Arab financial institutions, 4 percent through the World Bank, 2 percent through UN agencies and just under one percent through the African Development Bank (AfDB). Other ODA, for humanitarian purposes, has been directed through the Red Crescent Societies and other non-governmental organizations, for which consolidated sources of information are not available.

Arab Financial Assistance Institutions: In the 1960s, and more importantly the 1970s and early 1980s, Arab donors established a number of specialized financial institutions to provide development assistance. Kuwait, KSA, and UAE established national aid agencies. In addition, five main regional funds were established: the Arab Fund for Economic and Social Development (AFESD), Arab Bank for Economic Development in Africa (BADEA), Islamic Development Bank (IsDB), OPEC Fund for International Development (OFID), and Arab Monetary Fund (AMF). Strictly speaking, IsDB and OFID are not exclusively Arab-financed institutions, but Arab countries provide the largest share of their funding. In addition, the Arab Gulf Program for United Nations Development Organizations (AGFUND) plays a special role in financing technical cooperation and humanitarian assistance through its support for specialized UN agencies. These institutions have grown to become major providers of external financial assistance. With the exception of AGFUND, these agencies have financed their operations primarily from capital subscriptions and loan reflows.

Financial assistance commitments of the nine major Arab financial institutions reached a cumulative total of US$ 155 billion (in 2007 prices) over the period 1962-2008, which is five times the combined paid-up capital of these institutions. Commitments increased significantly in both nominal and real terms (Figure 2); annual average increases were estimated at 4.4 percent in real terms for the period 1990-2008.

Originally created to provide financial assistance to low-income Arab countries, Arab financial institutions have broadened their reach to cover a wide range of low- and lower-middle-income nations. These organizations traditionally financed infrastructure, but now place a greater emphasis on agriculture, social sectors, targeted poverty reduction programs, and private sector development.

Figure 2: Yearly Average Commitment of Arab Financial Institutions
(US$ billions)



Arab financial institutions have also participated in debt relief operations (through rescheduling) and have provided balance of payments and budget support.

Regional Integration and Arab ODA: In addition to national projects, Arab financial assistance agencies support projects that foster regional economic integration, particularly in roads, energy and hydropower infrastructure, and South-South cooperation. For instance, in 2007, BADEA financed five road projects to promote trade between Burkina Faso, Chad, Sierra Leone, Rwanda, and Cameroon. AFESD's contribution to Arab regional integration is the financing of the Arab Electricity Grids Interconnection Projects. In the area of capacity building and research, AFESD joined with the World Bank to establish the Research Initiative for Arab Development. IsDB has also supported regional integration in Africa through assistance to, for instance, the Trans-Sahara and Trans-Sahel roadways. There is a growing effort among Arab financial institutions to promote South-South cooperation, as illustrated by the IsDB Capacity Building Program (Box 3.1). South-South cooperation is one of the hallmarks of Arab aid, and its effectiveness and lessons merit careful study.

Though Arab financial assistance is predominantly in the form of concessionary credit, some institutions provide grants to finance capacity building, project preparation, and technical advice. Arab agencies also provide consolidated support to UN Specialized agencies, Red Crescent Societies, and non-governmental organizations (NGOs) for humanitarian assistance. Arab financial assistance is noteworthy for its partnership and solidarity with recipient countries—in practice, this is interpreted to mean that Arab donors do not attach policy conditions to the loans they provide.

Arab financial agencies coordinate policies and procedures and co-finance projects through a Coordination Group hosted by AFESD. Reports suggest that the use of common procedures has enabled Arab agencies to reduce transaction costs, foster greater transparency in project management, and improve project safeguards and accountability. Co-financing is the principal mechanism through which these agencies collaborate among themselves and with other development partners. The Coordination Group also participates in global initiatives to foster aid harmonization and alignment.

Reporting Practices and Arab ODA Agencies: Reporting practices among Arab ODA agencies are evolving. The establishment of a central agency to coordinate ODA in the UAE and efforts made to bolster the visibility of KSA's aid program bode well for the future development of Arab ODA reporting systems. Furthermore, the Coordination Group Secretariat is engaged in a capacity enhancement partnership with OECD-DAC

Looking Ahead: Arab financial institutions are well positioned to meet the challenges posed by the global financial and economic crisis. Being well capitalized and financially conservative, these institutions may be able to help offset some of the slack that may be created by declining ODA from other sources. Over the medium to long run, these growing and maturing institutions will be well placed to tap into capital markets to increase the scope of their operations.

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