Living up to Policy Coherence for Development? The OECD's Disciplines on Tied Aid Financing

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Contents

List of Abbrevations

AQuA	Aid Quality Assessment
DAC	Development Assistance Committee
DAC/FA	DAC Working Party on Financial Aspects of Development Assistance (OECD)
DDR	Differentiated Discount Rate
ECG	Export Credit Group
EU	European Union
GATT	General Agreement on Tariffs and Trade
HLF	High Level Forum
ICB	International Competitive Bidding
IMF	International Monetary Fund
LDCs	Least Developed Countries
MDGs	Millennium Development Goals
ODA	Official Development Assistance
OECD	Organization for Economic Co-operation and Development
ORIO	Facility for Infrastructure Development
PCD	Policy Coherence for Development
PG	Participants Group
PSD	Private Sector Development
SDGs	Sustainable Development Goals
SDR	Special Drawing Right
UN	United Nations
WB	World Bank
WTO	World Trade Organization

Abstract

With tied aid credits donors aim at boosting the international competitiveness of domestic enterprises while simultaneously contributing to development in recipient countries. Though regulated through the Arrangement on Officially Supported Export Credits, tied aid credits claim a place amongst the instruments of development policy and are eligible as Official Development Assistance (ODA). This begs the question whether the international regulatory framework is equipped to safeguard the presumed development goals. This paper examines the consistency of the tied aid disciplines of the Organisation for Economic Co-operation and Development (OECD) with the development principles coined by the Development Assistance Committee (DAC). Thereby, the extent to which the OECD lives up to its own promise of Policy Coherence for Development (PCD) is scrutinised.

***Key Words**: policy coherence for development, tied aid, export promotion, OECD/DAC*

1. Introduction

With the 2015-deadline for achieving the landmark Millennium Development Goals (MDGs) approaching at a fast pace, debates in the United Nations (UN) on a post-2015 framework that 'goes beyond aid' have gained momentum. Though it remains to be seen if agreement on a new framework with binding commitments will be achieved, the thrust of the discussion so far suggests that the post-2015 development agenda will probably be substantially widened, as suggested by the outcomes of the Rio+20 Summit. The latter resulted in agreement among the participating states to set-up Sustainable Development Goals (SDGs) which shall feed into the post-2015 process.

Associated with the discussions on a post-2015 agenda are considerations over the types of resources that public and private actors should provide in support of the international development policies, with the relative importance of ODA possibly further diminishing as private sources are being tapped. Amongst the many instruments that are currently reviewed, range soft loans. Originally conceived as a tool of export finance, tied soft loans have from the 1980s onwards successively been brought under regulation through the *Arrangement on Officially Supported Export Credits* (the Arrangement) as part of the OECD's export promotion framework. These institutional roots in the export promotion field notwithstanding, tied soft loans claim a place amongst the instruments of ODA. Resulting from the officially stated motivation to contribute to economic development and welfare in the recipient country and conveying the 25 % grant element required by the DAC, the concessional part of such loans is ODA-eligible and contributes to a donor's overall ODA-performance. While tied aid credits may be a 'hybrid', they endeavour to contribute to development, are included in ODA-statistics and might use resources from the aid budget. Therefore, their appropriateness to finance development should be expected to be subjected to the same criteria as any other ODA-flow. This calls for an assessment of the extent to which the corresponding international framework for tied aid financing provides the means to safeguard coherent policies.

By drawing on qualitative content analysis of OECD archive footage[1], expert interviews (50 interviews in five countries) as well as on an analysis of policy documents, this paper seeks (i) to trace the role which development policy aspects and interests have played in the evolution of the Arrangement and upon that basis (ii) to assess the extent to which the resulting tied aid disciplines are coherent with the OECD's standards for development policy. For that purpose three highly intertwined and largely DAC-driven debates have been identified: the aid effectiveness agenda as reflected in the Paris Declaration, the idea of PCD as well as the long-lasting call for aid untying. This assessment of the tied aid disciplines of the Arrangement against the backdrop of the DAC's ideas on effective development co-operation also constitutes an analysis of the OECD's internal coherence.

This seems relevant for several reasons. Firstly, the historical vantage point chosen allows to unfold the interlinkages between the two fields of reference and the respective institutional actors, which have shaped the design of the instrument over four decades. Secondly, despite the OECD's role as knowledge producer, little is known about the interplay of different departments and intra-organisational dynamics. While other international and regional organisations such as the World Bank (WB), the International Monetary Fund (IMF) or the European Union (EU) have raised considerable interest among academics in various disciplines, the OECD as a whole and the DAC in particular have been subject to

1 Initially more than 1500 documents of three groups – the DAC Working Party on Financial Aspects of Development Assistance (DAC/FA), the Export Credit Group (ECG) and the Participants Group (PG) – dating from 1978-2005 were retrieved from the OECD archives. Based on a first screening our analysis focused on the DAC/FA and PG, largely leaving aside complementary discussions in the ECG.

comparably little academic scrutiny. This lack of academic literature on the OECD is all the more puzzling considering one of the fundamental pillars of the Organisation: transparency (Martens/Jakobi 2010b: 269). The DAC and its ODA-statistics figure as prominent examples for the discrepancy between being a knowledge producer on the one hand and being the subject of research on the other. Practically the entire donor community relies on publications and statistical records produced by the DAC, but little academic literature has so far dealt with the inner-workings of the DAC, asking about dynamics behind drafting DAC positions, or how in- and outside influences and political motivations are shaping them. Some of the few publications on the OECD, touching also upon the DAC, are the publications by Carroll and Kellow (2011), Mahon and McBride (2008), Martens and Jakobi (2010a), and Woodward (2009). Likewise, soft loan financing in general and its contribution to development policy in particular have not yet been unfolded by academic literature. Thus, the relevance of this paper lies in bringing transparency into the soft loan field, which has been widely neglected by academic research.

The remainder of this paper is structured as follows. Section 1 elaborates on the concept of PCD and builds the conceptual framework for the subsequent analysis. Section 2 introduces the international regulatory framework covering tied aid credits and examines the role of different actors in setting up the current body of rules. In this vein, the extent to which development policy found its way into the existing disciplines is assessed. Departing from the hybrid nature of tied aid credits, Section 3 inquires the compatibility of the OECD's tied aid disciplines with the DAC's principles for development co-operation, mainly those set out in the Paris Declaration and reiterated in the Accra Agenda for Action and the Busan Declaration. Ultimately, this allows us to assess the extent to which the OECD lives up to its own promise of PCD.

2. Policy coherence as analytical framework

The discussion on the effectiveness of aid is embedded in the context of achieving the MDGs and is inextricably linked with major systemic questions of international development. These concern matters of coherence on a European and a global level, but also of different intra-national policies. A substantial definition of effectiveness goes beyond the domain set by the Paris indicators and encompasses all policy areas that have repercussions on the goals of development policy. Eventually, the behaviour of global players within the WTO or the trading policies of the EU, for instance, constitute the central policy arena in which the effectiveness of development efforts is fought (Six 2006: 27). In this respect, PCD is rooted in the frustration of the aid community that saw its efforts being spoiled by contradictory policies in other policy fields (OECD 2005: 164).

Although the idea of coherence (associated with development co-operation) was already spelled out in the Maastricht Treaty of the European Community (1992)[2], it was the Millennium Summit (2000) that gave fresh wind to the coherence debate. Donor administrations realised that aid alone was hardly sufficient to meet the declared goals and that other policies and their effects on development efforts had to be addressed as well. Consequently, the goals formulated at the Summit went beyond the realms of development co-operation. This broader scope is best reflected in Goal 8, which aims at the establishment of a 'Global Partnership' between industrial and developing countries (Obrovsky 2006: 72). By targeting the development of a 'trading system that is open, rule-based, predictable and non-discriminatory', MDG 8 appeals to the necessity of coherent policies for development

[2] The Treaty states: '[...] the Community shall take account of the objectives referred to in Article 130U [which refers to development co-operation] in the policies that it implements which are likely to affect developing countries' (European Union 1992). The 2005 'European Consensus on Development' further upgraded PCD and attributed it a central role in European Development Co-operation (for a more detailed discussion see Keijzer 2012).

(UN 2003: 38). In combination with the term development, the newly created buzzword PCD found its way into development discourse and was coined by the DAC in the early 1990s (OECD 2005: 39-40). The DAC's political mandate was agreed upon in 2002 (DCD/DAC, Final Communiqué 16/05/2002) and enlarged in 2008 with the adoption of a ministerial declaration, which stressed the need to invest in measuring impacts of OECD members' policies and evaluate results achieved through joined efforts to promote PCD. Since the early 2000s, PCD has also been given a more prominent role in the OECD Peer Review Process by paying attention to efforts made with regard to overall policy changes (OECD 2005: 39, 135-6). Furthermore, the recent *OECD Strategy on Development* has declared strengthening members' capacity to achieve PCD as a top priority (OECD 2012: 9). Also in the current debates on an overhaul of the international development agenda and architecture, the OECD highlights PCD as an important enabler of inclusive and sustainable development. Only by creating well integrated and mutually reinforcing policies, it is argued, can the international community succeed in tackling the multifold global challenges (OECD 2014: 3, 16).

Despite the omnipresence of the concept in OECD communications, definitions of PCD have remained vague (OECD 2005: 27). The concept implies both the elimination of negative effects of non-aid policies as well as the call for an active contribution towards development, with a focus-shift from the former do-no-harm towards the latter pro-active approach observable over time (OECD 2014: 16)[3]. These two facets of the concept are reflected in the following definition:

> 'Policy coherence ... involves the systematic promotion of mutually reinforcing policies across government departments and agencies creating synergies towards achieving the defined objective' (OECD 2005: 28).

This also implies that donors work to

> 'ensure that the objectives and results of a government's (or institution's) development policies are not undermined by other policies of that government (or institution), which impact on developing countries, and that these other policies support development objectives, where feasible' (ibid.).

In the case of tied aid credits, a do-no-harm approach as stipulated in the second part of the quote and traditionally applied to assess the coherence of a distinct policy area with the field of development policy is too narrow considering the postulated goal of contributing to development processes. As tied aid credit policies are here considered to be part of both development policy and trade policy, the call for a proactive approach appears justified. By assessing the compatibility of the regulatory framework for tied aid credits with the DAC's principles of ownership, harmonisation and alignment, we transplant the concept of PCD from the national to the international level and scrutinise the coherence of an international organisation in the field of tied aid financing. Thus, the emphasis does not lie on an assessment of national policies or even individual projects, but on the consistency of the OECD's regulations with its own development principles. Considering that the international framework decisively shapes the design of such credits, this analysis is expected to provide results indicating the potential of the instrument as a tool for effective development policy more generally.

[3] More sophisticated definitions of PCD differentiate between internal coherence, intra-country coherence, inter-donor coherence and donor-partner coherence (Picciotto 2004: 8; Van der Hoeven 2010: 30-31). Notably, this definition implies a focus on national policies. For the purpose of our analysis, it does not seem necessarily to explicitly follow this distinction. However, by assessing the compatibility of the regulatory framework for tied aid credits with the DAC's principles of ownership, harmonization and alignment, inter-donor coherence as well as donor-recipient coherence are scrutinised.

3. Setting the stage: actors and international regulation

The three most important fora where export credits and tied aid credits are being discussed are the Export Credit Division of the OECD (the Export Credit Group and Participants Group), the World Trade Organization (WTO) as well as the OECD/DAC. Most prominently soft loans are regulated by the *Arrangement on Officially Supported Export Credits*. The Arrangement has interfaces with several other sets of rules and guidelines, most notably the DAC principles for development co-operation and the WTO's *Agreement on Subsidies and Countervailing Measures*. In addition, it has been incorporated into EU directives (Council Directive 98/29/EC). In the following, the emphasis lies on the evolution and *status quo* of the tied aid disciplines spelled out by the two bodies affiliated – albeit to differing degrees – with the OECD, namely the Participants' Arrangement and the DAC's principles for development co-operation. For that purpose the Participants Group is treated as part of the OECD despite its *de jure* autonomous character. Considering that the group is served by the Secretariat and that the participating states are for the most part OECD and DAC members, this seems appropriate.

3.1 The Participants Group and 'their' Arrangement

The Arrangement, first agreed upon in 1978, constitutes the main regulatory framework for officially supported export credits, including tied aid credits. Its scope covers any form of official support for the export of goods and/or services provided by governments or by institutions acting on behalf of a government. The main purpose of the Arrangement is to limit market distortions by fostering competition among exporters based on quality and price, rather than on the best financial terms (OECD 1998: 17). Disciplines on tied aid credits constitute an integral part of this rule-set. Notably, the Arrangement is not a legal act of the OECD and peer pressure is the force disciplining compliance with the rules. While the first version of the Arrangement had initially been drafted by members of the OECD's Export Credit Group (ECG)[4], later in 1978 a new informal body, the Participants Group (PG), was established and given the task of developing further the provisions. Due to the loose link of the group to the OECD, the Participants have not been legally bound by the OECD rules of procedures[5] (West 1998: 22).

Historically, tied aid credits have been inextricably linked with traditional export credits. The gradual tightening of rules on traditional export credits in the late 1970s/80s paired with a severe debt crisis in the developing world, had placed tied aid credits at the heart of export policies of many industrialised states (DCD/DAC/FA(93)3). In these circumstances, the motivation was one of gaining competitive advantages for domestic enterprises; development goals were at best pursued as an add-on that should conceal the trade distorting effects of the practice. The term 'aid' in tied aid credits, therefore, was not necessarily to be associated with development of recipient countries, but might rather be interpreted as aid to national industries, which saw their international competiveness declining (Ray 1995: 28). Throughout the 1980s concerns grew that tied soft loans were used as backdoor subsidisation of national industries. In reaction, the Participants gradually increased the minimum permissible grant element (later renamed concessionality level) hoping that this would discourage these harmful practices. An increasing number of tied loan notifications after a renewed rise of the concessionality level in the *Wallén Package* (1987),

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4 The full name of the ECG is 'Working Party on Export Credits and Credit Guarantees'. Contrary to what its name might suggest, the ECG does not hold the competence over the Arrangement. Instead, it deals with complementary issues such as anti-bribery, environmental standards or sustainable lending.

5 This allows them to invite non-OECD members to join the Arrangement – as it was the case when Brazil signed the new Sector Understanding on Export Credits for Civil Aircraft in 2007. Negotiations leading up to this signature had been surrounded by the so-called 'Embraer case' – a WTO dispute case between Brazil and Canada. For further information see Sanchez Badin, 2008.

however, proved this mechanism insufficient. With the *Helsinki Package* (1991/2) the Participants shifted their strategy and introduced the concept of commercial non-viability, which should henceforth ensure the separation of commercially-motivated export credits and development-motivated tied aid credits (TD/PG(2005)20: 4). The concept placed the ability of a project to financially sustain itself at the heart of the disciplines and complemented the earlier strategy of increasing concessionality requirements as a means to disincentive the use of soft loans. In trade terms, this could be compared to a shift from 'tariffs' to 'quotas' (Interview VI). The basic idea was that government aid funds should be reserved for projects with considerable external benefits, which were, however, unable 'either to generate sufficient financial returns to make them attractive enough for commercial financing or to attract officially supported export credits' (TAD/PG(2012)9: 21). Aid funds deployed according to this logic would be truly 'additional'. Ensuring aid quality of the projects would remain the responsibility of aid agencies.

Up to today the tied aid disciplines (*Helsinki Disciplines*) are centred on two key tests examining the financial viability of a project as well as the access to finance in the recipient country. Exemptions from the project eligibility tests are provided for highly concessional transactions (concessionality>80 %), tied aid credits to Least Developed Countries (LDCs) and de minimis transactions (<Special Drawing Rights 2 million) (TAD/PG(2014)6: 22). The adoption of these rules translated into a sharp decrease of the volume of tied aid credit notifications in the early 1990s. After a 2-year transition period following the adoption of the *Helsinki Package*, the volume of Helsinki-type tied aid stabilised and has remained at a fairly constant level ever since (Schweiger 2013: 53).

Tied Aid Credits

The main definition of tied aid credits can be derived from the minimum conditions laid down in the Arrangement. Throughout this paper the terms tied aid credits and tied soft loans are used synonymously, the former being the *terminus technicus* which is predominant in official documents at the OECD level. Following the Arrangement, tied soft loans are defined as official, state supported credits that are procurement-tied, contain a concessionality level[6] of at least 35 %/50 %, which in principle is ODA-eligible, and can be used to finance commercially non-viable projects in a limited pool of recipient countries (TAD/PG(2014)6). This working definition only applies to officially procurement-tied concessional loans, while the term 'soft loan' comprises a broader spectrum of credit-based financing without *prima facie* indicating the tying status.

Source: TAD/PG(2014)6

In order to discuss controversial cases, the *Helsinki Package* introduced a consultation mechanism. This has given any Participant the opportunity to request consultation for projects the eligibility of which was thought to be questionable (Ray 1995: 98-99). A Participant may demand a full *Aid Quality Assessment* (AQuA), which is to be conducted in accordance with the *Checklist of Developmental Quality* (TAD/PG(2012)9: 28-29; Annex IX). With these consultation processes a body of experience developed and was formalised in the *Ex Ante Guidance for Tied Aid* (Ex Ante Guidance) assisting aid and export credit agencies in ex-ante evaluating the commercial viability of a project (TD/PG(2005(20)).

Looking back at the history of tied aid credits reveals that on an international level these instruments were originally used by most industrialised countries in order to boost their respective exports in a situation of worldwide economic depression (Cutts/West 1998: 12). Keeping the resulting export credit 'war' of the 1970s/80s (and the succeeding 'tied aid credit

[6] Just as the grant element used by the DAC, the concessionality level assesses the softness of a credit and reflects its financial terms i.e. the interest rate, maturity, and grace period of a commitment. While the method of computation is the same as in the case of the DAC's grant element, the discount rate differs. For the latter, a market-based discount rate, a so-called differentiated discount rate (DDR) is used (DCD/DAC 2012b: 2).

race') in mind, it becomes evident that the emerging rules were designed from a liberal economic perspective striving first and foremost to eliminate trade distortions and hence appeal to a very limited extent to aid quality matters. Everything explicitly referring to development was left to be dealt with by the DAC. While this implies an acknowledgement of the DAC's expertise, it also entails shifting responsibilities for the developmental impact of tied aid financing to the DAC and its national counterparts. Whether this is conducive to PCD or provides the breeding ground for incoherent policies will be assessed in the subsequent section.

3.2 The role of the DAC

Tied aid credits have also been a matter of concern within the DAC and fall due to their explicit development goals into its working area. For the purpose of increasing the development orientation of these transactions which unlike export credits may fall in the ODA-category, a Working Party on Financial Aspects of Development Assistance (DAC/FA) was created within the DAC as early as 1975 (Chang et al. 1999: 5). From the early 1980s onwards the main task of this group was to monitor the Participants and to ensure that development aspects were sufficiently considered in the negotiations of the main regulatory body (DAC/FA(85)2: 21). The DAC/FA discussed the usefulness of the instrument against the backdrop of the indebtedness of many recipients on the one hand, and the scarcity of aid resources on the other. The degree of additionality of resources channelled through tied aid credits was assumed to be indicative of their usefulness for development policy. Implicit to the DAC/FA's reasoning was the question of how these public monies would have been invested alternatively (Fritz 2013: 158).

Prior to Helsinki, the DAC/FA warned that mostly commercially-motivated tied aid triggered the distortion of aid flows from countries most in need to those countries and projects that promised to be profitable for donors' businesses. It was certainly the tied-ness of the instrument that was the biggest thorn in the DAC/FA's side. Confronted, however, with the reality of aid politics, a strategy of containing the most harmful effects was chosen, joining the Participants' efforts to design the instrument in a way that would lead to less aid and trade distortions. For that purpose the DAC adopted a series of guidelines to increase the transparency of tied aid policies and to enhance their development orientation. Although the Working Party had put its focus on aid quality much earlier, it was in the 1990s that discussions on how to achieve this goal were the most intense (DCD/DAC/FA/M(93)2-PROV). These concerns are yet another expression of a general rethinking of development co-operation in the immediate post-cold war era when the effectiveness of aid was seriously challenged and an aid fatigue translated into reduced ODA-volumes (Wood et al. 2008: 5). One of the most emphatically pursued proposals by the DAC/FA was the call for a greater role of aid agencies in the design and implementation of projects financed with tied aid credits (Fritz 2013: 122). Furthermore, the DAC Secretariat repeatedly urged that estimates of the gap between the economic and the financial internal rates of return would indicate the development contribution of projects (DCD/DAC/FA (94)9: 5).

First guidelines were adopted in the 1980s and continuously developed in parallel to the Arrangement. The most important ones were the *DAC Guiding Principles for the Use of Aid in Association with Export Credits and Other market Funds (1983)* and their successor the *DAC Guiding Principles for Associated Financing and Tied and Partially Untied Official Development Assistance* (1987). The DAC/FA's efforts to contribute to disciplining tied aid financing culminated in the adoption of *New Measures in the Field of Tied Aid* (1992). These consist of the tied aid relevant elements of the Arrangement and a set of additional development-oriented principles such as the provision of a checklist of considerations along which the development priority of projects/programmes should be assessed (Chang et al.

1999: 88). The most apparent 'intervention' of the DAC into the Participants' work was the preparation and subsequent incorporation of the AQuAs into the Ex Ante Guidance. It is here most visible that the DAC/FA straightforwardly influenced the work of the Participants. In the mid-1990s, when implementation difficulties became apparent and in view of the unsatisfactory quality of many AQuAs, the DAC/FA emphasised the importance of AQuAs in confidence building among tied aid giving states and made proposals for improving this mechanism (DCD/DAC/FA/M(94)1/PROV; DCD/ DAC/FA(95)1). Despite such efforts, in the Arrangement development content and aid quality of projects remain conceptually restricted to the notion of commercial non-viability.

4. Assessment of the tied aid disciplines against DAC principles

Departing from the OECD's vehement call for PCD the extent to which the Organisation lives up to its own principle of coherence shall be scrutinised. Due to their hybrid nature and the myriad of institutional actors involved, tied aid credits are perfectly suited for studying the OECD's intra-organisational coherence as well as the internal coherence of policies subsumed under the umbrella of ODA. Accordingly, also the DAC's *Illustrative Checklist on Policy Coherence for Poverty Reduction* identifies mixed credits as one of several policy areas requiring due diligence with regard to coherence (OECD 2001: 103). This section brings together the jigsaw pieces and assesses the *Helsinki Disciplines* against the conceptual framework provided by the DAC's principles for effective development co-operation. We put the emphasis on the Paris Principles of harmonisation, ownership and alignment. The remaining two – managing for results and mutual accountability - are due to their technicality not discussed in length, but referred to when suitable. Additionally, the untying debate is taken up because it clearly is one of the development policy relevant dimensions of soft loan financing. Where appropriate the subsequent analysis takes into account both the process of negotiating the rules as well as the resulting international disciplines, which decisively determine the basic design of national policies.

4.1. In line with the Paris principles on aid effectiveness?

In an assessment of the *Helsinki Disciplines* conducted in 1998/9, the DAC Secretariat found them to be broadly compatible with and to be actively promoting the goals and objectives of the DAC's *Strategy for the 21st Century* (OECD/DAC 1996; DCD/DAC/FA(99)8: 8) – the key document paving the way to the Paris Declaration.

As part of the assessment, the DAC Secretariat circulated a questionnaire among its members asking them to present their views on the effectiveness of the existing framework and its compatibility with the DAC's strategy (DCD/DAC/FA(98)4: 5). Answers concerning the compatibility of the *Helsinki Disciplines*, varied considerably. While some saw them as not fitting in well with the concept of partnership, others stressed that the Disciplines' preference for untied aid promoted the strategic goals and modalities of the DAC's strategy (DCD/DAC/FA(99)8: 8). Building on these findings, this section further explores the consistency of the OECD's rules for export promotion via tied aid credits with the Organisation's development co-operation principles. Given the centrality of the Paris Principles to the DAC's work, the question arises whether the tied aid disciplines actively promote compliance with these principles, strengthen these or are potentially even counteracting the DAC's objectives and its members' commitments.

4.1.1. Harmonisation

The idea that harmonised donor policies enhance aid effectiveness led to the adoption of the *Rome Declaration on Harmonization* and was reiterated at several occasions, most notably at the second High Level Forum (HLF) in Paris, where DAC members upgraded the principle of harmonisation to one out of five pillars of effective development co-operation (OECD 2005-2008: 6).

Undoubtedly, the adoption of the *Helsinki Disciplines* has contributed to the convergence of soft loan policies. By agreeing on a common set of rules, the Participants succeeded in levelling the playing field and contained a disguised export credit race. Up to today the minimum conditions laid down in the Arrangement provide a common ground for soft loan financing. Nevertheless, for instance the fact that the concessionality level may lie between 35 % and 80 % of the loan amount provides a considerable range for diverging national practices, which in turn influences the presumed development orientation of a project (Fritz 2013: 166). With regard to implementation procedures more generally, the loose character of the Arrangement – as such the product of negotiations between sovereign states on a sensitive issue of national interest – leaves considerable room for manoeuvre to national actors. Most notably, the Arrangement does not spell out any preference for which type of national agency should be in charge of soft loan programmes. Hence, the implementing agency might or might not have a development mandate to fulfil. It is conceivable that the governmental institution in charge of development co-operation does not have any decision-making power with regard to the selection, implementation and/or evaluation of projects. This in turn bears the danger that the developmentally effective allocation of aid funds is not ensured. Considering the general mandate of the DAC and the composition of delegates in meetings of the DAC/FA, it comes as little surprise that from the 1980s onwards one of the main topics dealt with by the Working Party concerned the role of aid agencies in tied aid financing (ibid.: 122). Given the ODA-eligibility of the concessional element inherent to the instrument, it should be expected that the implementing agencies have the necessary development competences in order to attain the alleged goal of promoting development. Our analysis of the institutional set-up and the role of key agents of development co-operation in four donor countries revealed that this expectation is only met to varying degrees in the systems scrutinised. While in some cases the bodies in charge of development policy are responsible for the implementation of soft loan programmes, in others they do not play any decisive role (Fritz et al. 2014, 402-3).

4.1.2. Ownership

At the HLF in Paris, DAC members declared that partner countries should 'exercise effective leadership over their development policies, and strategies and co-ordinate development actions' (OECD 2005-2008: 3).

Any analysis of the space given to ownership within the regulatory framework must set out with an examination of the process of rule-setting itself. The screening of Participants' documentation has shown that recipient countries did not participate in the negotiation process and that their perspectives were not explicitly taken into account. This is linked to the nature of the forum that was chosen for the negotiations - an informal group under the auspices of the OECD – and raises the questions why export credits were not from the very onset the domain of GATT or why the authority over official export credits was not transferred to the WTO later. One interviewee affiliated with the Export Credit Division argued that export credit and tied aid disciplines were negotiated by the Participants and not in a more inclusive framework (in terms of membership) such as the WTO[7] out of political calculation. The following statement illustrates this political reasoning:

> 'There is a strong view on this in the US that the donors should control the disciplines. Because it's coming out of donor tax payers' money, you know, he who provides the money should have the say in how it is used. And the recipients may have mixed feelings but in the end there is a financial incentive to try to get as much as they can and so not to be so anti-subsidy.' (Interview VI)[8]

Similarly, Hall (2011: 660-1) argues that the OECD was chosen because it

> 'allowed the US to target key tied aid players while excluding potentially obstructive third parties. .... More importantly, confining negotiations to the OECD precluded the presence of aid recipient countries. Such states benefiting from aid diversion into export promotion and donor competition over terms would have a strong incentive to block agreement'.

In more general terms Woodward (2009: 72-73) finds that states negotiate legal agreements (in our case rather a soft law arrangement containing elements of hard law) in the OECD (in our case a group loosely linked to the OECD), because it enables them to deal with issues affecting OECD countries disproportionately. He argues that 'especially in areas where divergences between OECD and non-OECD members would obstruct a formal treaty in an international institution with a wider membership' (ibid.), the OECD figures as negotiation framework. In any case, the fact that recipient countries were left outside the negotiation room raises questions with regard to the OECD's self-obliged commitment to ownership of and partnership with recipient countries in setting development policies. One might argue that ownership had not yet been as big an issue at the time the *Helsinki Disciplines* were negotiated. However, also today, with the principles of ownership and partnership ranging high on the OECD's agenda, active engagement of recipient countries has not been sought. A possible way of integrating the recipients' perspectives and expectations towards the instrument would have been to hold consultation meetings with groups of recipients, such as the G77.

A second important component of ownership concerns the role of recipient countries and their possibilities to express their views at the project level (DCD/DAC/FA(95)3/REV1: 7). With the principle of 'managing for results', both donors and partner countries committed themselves to monitor and evaluate progress in meeting development goals (OECD 2005-2008: 10). The current tied aid disciplines do not provide any mechanisms for ex-post evaluation in a systematic manner and do not contain any means to safeguard 'managing for results'. Hence, it is incumbent upon the donor's national institutions to provide sufficient space for exchange and to build functioning feedback-loops[9]. Likewise, the Arrangement remains largely silent on how to steer mutual accountability in the soft loan field.

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7 In 1980 the Subsidies Agreement of the GATT came into effect, prohibiting the use of subsidised export credits to gain competitive advantages. Up to the present the Agreement, now having the status of a WTO Agreement, has provided a 'safe harbour' for those export credit practices that are in conformity with the Arrangement. Consequently, a breach of Arrangement rules also entails a violation of the Subsidies Agreement, which provides legal remedies (Mendelowitz 1989: 5). The latter has hence 'multilateralised' its scope, meaning that any WTO member – Participant to the Arrangement or not – 'would be deemed to comply with WTO obligations' (Bonucci 2010: 51). This incorporation into WTO law gave international effect to what used to be (and in itself still is) a non-binding agreement, which has been negotiated by an exclusive circle of countries over decades.

8 Early documentation of the discussions on the impact of mixed credits in the DAC/FA supports such arguments. In a note by the DAC Secretariat it says: '[d]eveloping countries draw substantial benefit from the subsidisation of export credits' (DAC/FA(81)1: 17). In another note they are even considered the sole beneficiaries from such policies. However, in later documentation it becomes clear that these benefits might be rather short-term effects that only occur in case of true 'additionality' of the resources provided in the form of mixed credits.

9 According to Owen Barder (2009: 10) the broken feedback-loop, which is challenging aid administration, results from the political and geographical dispersion of donors and beneficiaries. The author argues that the feedback-loop is not functioning in foreign aid, 'because there is a lack of both information and political influence connecting decision makers to the intended beneficiaries' (ibid.: 11).

Finally, at a fundamental level, the tied-ness of the instrument appears to raise concerns with regard to its compatibility with both ownership and alignment claims such as stipulated in the Paris Declaration. Several studies (Hancock 1989; Morrissey 1998; Petermann 2013) find that due to the high probability of being supplier-driven, tying practices might interfere with ownership of recipients in their development processes. Tied aid in general is judged by the DAC to be incompatible with ownership principles and in contradiction with the call for demand-driven purchases as particularly stressed in the Accra Agenda (OECD 2005-2008: 16).

4.1.3. Alignment

With the Paris Declaration donors committed themselves to 'base their overall support on partner countries' national development strategies, institutions and procedures' (OECD 2005-2008: 3). Part of this commitment to align donor interventions with the recipient country's poverty reduction strategies is the target of making continuous progress in untying aid (ibid.: 10).

At the level of formal statements, the Participants' guidelines, in particular the Ex Ante Guidance, take this call for alignment into account. For instance, as part of an AQuA, donors should demonstrate the 'consistency of the project with the recipient country's overall investment priorities' (TD/PG(2005)20: 10). The underlying reasoning reflects the spirit of the Paris Declaration and recalls the importance of aligning donor practices with recipients' development priorities so as to respect ownership of the latter. In calling for donor co-ordination, also the principle of harmonisation is considered. Although the Ex Ante Guidance was last adapted in 2005, the Paris Principles are not referred to, not even in the part on AQuAs, which was prepared by the DAC itself.

Despite the formal acknowledgement of the need for alignment, several contradictions are inherent to the instrument and undermine the principle of alignment, the most obvious relating to its tied nature. Especially indicator 8 of the Paris Declaration recalls the principles laid down in the DAC *Recommendation on Untying* and formulates the goal of untying aid to LDCs (OECD 2005-2008: 5). Thereby, untying is seen as a means to a greater end, such as the development of local and regional markets and the local creation of value. In Accra donors reiterated their commitment to alignment by reaffirming that they 'will promote the use of local and regional procurement by ensuring that their procurement procedures are transparent and allow local and regional firms to compete' (ibid.: 1). This way, aid's 'value for money'[10] is thought to be boosted (ibid.: 18) and the local economy is expected to develop, hence rendering the impact of a project sustainable.

In the attempt to solve these contradictions or at least to limit drawbacks in effectiveness, the DAC Secretariat encouraged donors *inter alia* to transfer procurement responsibility to recipient countries and to promote as best as possible linkages between soft loan projects and the local economy (DCD/DAC/FA(95)2/REV1: 10). At a conceptual level, one salient feature of tied aid credits – their tied-ness – remains in contradiction with the alignment principle. By means of the above measures a second-best option was hoped to be achieved, considering global untying as the first-best (but non-feasible) solution. In the context of tensions between tied aid and the importance given to local procurement in fostering sustainable development, one specific Arrangement provision requires examination: the permissible share of local costs. In 2007 the Participants raised the maximum threshold from 15 % to 30 % (OECD 2008a), allowing for more local creation of value. This was the Participants' reaction to an increasingly globalised economy paired with the necessity of

[10] This is assumed to be the case because the price for the procured goods and services is lower due to the competitive market environment, in which the procurement takes place. Numerous DAC documents refer to the concept of 'value for money' (VFM), which is described as 'a way of thinking about using resources well' by 'striking the best balance between ... economy, efficiency, effectiveness' (Jackson/OECD/DCD 2012).

procuring certain local goods/services when setting up a project. Assuming that the higher the permissible share of local costs, the more goods/services are locally procured, and the greater the presumed impact on development will be, this change might be judged advantageously from a development perspective (Interview I).

4.2. Untying: mutual concern and ongoing struggle?

The untying of aid has been an issue of controversy ever since the DAC's inception in 1961 (DCD/DAC(2010)34/FINAL: 3). Yet it is still timely. In 2002 the European Commission identified tied aid as one of the main obstacles on the way to greater aid effectiveness (European Commission 2002: 68). Morrissey (1999: 379) considers the extent of tying as an expression of the degree of incoherence within the aid policy. Being aware of such drawbacks, the DAC Secretariat examined strategies for the promotion of untied aid. In this vein, the compatibility of untying with other OECD policy objectives was stressed and the 'goal of leveling the playing field among exporters' was identified as a mutually reinforcing goal (DCD/DAC/FA(97)8: 3). This implicit reference to the Participants' endeavours illustrates the common quest for untying. Albeit for different reasons, both groups perceive(d) untying (or at least the restriction of tied aid to certain projects/countries) as a means to achieve their respective ends: export competition based on liberal market forces and recipient-led development policies ensuring aid's best value for money. While the untying debate was initiated by the DAC, the Participants' objective of limiting export promotion in the guise of tied aid boosted the DAC's efforts. Partially, this mutual interest stems from the OECD's liberalisation agenda ingrained in its Convention. In Article 1, contributing 'to the expansion of world trade on a multilateral, non-discriminatory basis in accordance with international obligations' is declared as one of the Organisation's main goals (OECD 1960, quoted in Jepma 1991: 2). The call for a non-discriminatory trading system implies a rejection of distorting market intervention and a reliance on competition based on price and quality. Hence, subsidising financial terms contradicts this philosophy (DAC/FA(82)2; TC/ECG/82.4: 14). Petermann (2013: 212) argues that Article 1 also built the basis of the DAC's free trade philosophy which eventually became an important 'normative pillar' of the untying initiative. Interestingly, the tying of aid, thus, unites critics from various fields and with potentially diverging ideological backgrounds.

Although the *Helsinki Disciplines* were not introduced with the principle aim of reducing the use of tied aid, the DAC Secretariat found some *prima facie* indication that 'the Disciplines may have had some impact on the recorded decline in both the volume and share of tied aid in total bilateral aid' (DCD/DAC/FA(98)4: 11). While prior to the inception of the Helsinki rules, tied aid notifications, expressed as percentage of the volume of bilateral ODA, accounted for roughly one fifth, the relative importance of tied aid experienced a downward trend ever since. As of 2005 tied aid constitutes only a small fraction (~4 %) of bilateral ODA. Although DAC members disagreed whether the *Helsinki Disciplines* were an initiating or a reinforcing factor of older trends, their contribution to the reduction of aid resources channelled into tied aid projects was widely acknowledged (DCD/DAC/FA(99)8: 7).

After agreement on the Helsinki rules had been reached, both the Participants' and the DAC/FA's focus shifted from disciplining tied aid credits to propagating untying, thereby pushing negotiations to the next level. This shift was prepared by the *Helsinki Package*, in which the Participants agreed to develop targets for the global untying of aid, judging this to be 'one of the best ways to reduce trade distortions' (Lammersen 1998: 64). Not only did the Participants declare their will to co-operate with the DAC in developing such targets, but also acknowledged the DAC's expertise (TD/CONSENSUS(92)12). The *Helsinki Package* provided the DAC with a quasi-mandate to take steps towards untying and gave leverage to its agenda. A look at DAC/FA documentation from 1981 onwards suggests that the group was torn between calling for untying (and thus for the elimination of tied aid credits) on the one hand and trying to improve the development quality of the instrument (hence de-facto tolerating their very existence) on the other. In a pendulum-like fashion the DAC/FA had promoted the untying of aid in the 1960s/70s. Confronted with the reticence of members to adopt corresponding measures, in the 1980s the DAC/FA joined the Participants in the more moderate attempt of disciplining tied aid use, that is accepting their existence, but under more stringent conditions. Once disciplines had successfully been set up and in the light of a general shift in development policy from 'donor interests' to 'recipient needs' after the end of the cold war (Petermann 2013), the DAC/FA reiterated its call for the untying of aid altogether. The DAC appears to have managed to make use of external developments in the field of export promotion in particular and the international trading system in general to push one of its utmost concerns, the untying of aid (Fritz 2013: 157).

The post-Helsinki movement from tied to *de jure* untied aid credits, which were not touched by the new provisions, made transparency in aid procurement become an ever more indispensable condition for the elimination of distorting practices (Ray 1995: 108). Already in 1993, several Participants expressed concern about insufficient transparency of untied loan financing and the potential circumvention of Arrangement rules (TD/CONSENSUS(93)46). In response, the DAC/FA and the Participants held a joint meeting on the need for greater transparency in the use of untied loans (TD/CONSENSUS(94)12). As in the case of untying, the DAC/FA claimed leadership in further sharpening definitions of untied aid, thereby contributing to filling this transparency gap. Based on findings of a series of *'Shadow' Helsinki Review of Untied Aid Credit Notifications* with input of the DAC Secretariat (TD/PG(2005)8), the Participants finally concluded the *Agreement on Untied ODA Credits Transparency* (2004)[11], which complements both the *DAC Recommendation on Untying* and the *Helsinki Disciplines*.

As a result, traditional soft loans have increasingly come under pressure to justify their very existence, which has pushed several OECD countries to end their schemes, untie these or at least to evaluate their programmes (Clay et al. 2009). For instance, Germany untied its Financial Cooperation throughout the 2000s, the Netherlands their ORIO grant facility in 2009 and Denmark added an untied window to its Danida Business Finance in 2002. Notably, in most cases first steps concerned the introduction of an untied pillar for LDCs (Fritz et al. 2014: 397-398). Despite the attempts to enhance transparency of untied loan financing concerns regarding the circumvention of the Arrangement via *de jure* untied loans (Stafford 1998: 49), as well as the embellishment of aid flows prevail. In an article in July 2014, the Economist urges that a growing share of export finance, such as untied aid, falls outside the scope of the Arrangement and calls for widening its coverage (The Economist 2014: 76). Firstly, conceptual ambiguities in the determination of the tying status might lead via informal practices to a situation in which untied programmes have similar effects in terms of the delivery from the donor country as tied ones. While the definitions provided in the DAC *Guiding Principles for Associated Financing and Tied and Partially Untied ODA* might seem straightforward, in reality, the borderline between them is often blurry (Jepma 1991: 20). Flows declared as untied might be *de facto* tied, for instance through hidden contract clauses or by opaque calls for International Competitive Bidding (ICB). Secondly, untied loans might be provided on significantly harder terms because they are not required to comply with the 35/50 % concessionality thresholds of the Arrangement, but only the 25 % grant element of the DAC calculated with a uniform 10 % discount rate. These and other ODA-reporting practices have triggered discussions about the – as of now not benchmarked – criterion 'concessional in character' and show the importance of refining decades-old practices (DCD/DAC 2012a; Lømoy 2013; Manning 2013). Lastly, discussions on the

[11] In order to increase transparency and prevent de facto tying, untied aid credits should be notified on the so-called Untied Aid Notification Bulletin Board, see https://community.oecd.org/streamPage.jspa?cwsDb=Xuntied&community=2249

discount rate used to calculate the softness of a loan reveal incoherent practices within the OECD. Unlike the DAC, the Arrangement requires calculation using market-based interest reference rates, resulting in discrepancies in the estimation of the softness of one and the same loan (DCD/DAC 2012b).

4.2.1. Provisions for LDCs

According to the Arrangement tied aid credits to LDCs require a 50 % concessionality level but do not have to pass the two key tests. This exemption was designed to reduce donors' administrative burden and to encourage lending to LDCs in order to maximise total flows to those countries. In contrast, DAC members have agreed to untie their aid precisely to this group to the maximum extent (OECD/DAC 2001). While one forum – the development co-operation body – emphasises the importance of untying especially for LDCs (because here the impacts of tying might be particularly detrimental), another forum – the export credit body – does deliberatively exclude flows to this same group from certain requirements because the poorest countries do not range among the main beneficiaries. This inconsistency might lead to forum shopping – a situation in which inconsistent rules can be played off against each other (Interview V). This might be negligible as long as LDCs are not attractive for donor domestic enterprises. However, in a situation in which African markets with high growth potential come to the fore of business interests, this incoherence might be used to legitimise continued tying practices such as allowed by the Helsinki rules and excluded from the commercial non-viability criterion. Lastly, the credit-based nature of the instrument provokes controversy with regard to the associated debt burden. Already in 1978 and reiterated at several occasions especially in the wake of the devastating debt crisis of the 1980s, DAC members agreed that ODA to LDCs should be provided in grant form (OECD/DAC 1978: 2). Although the Arrangement sets a higher concessionality level for tied credits to LDCs, they essentially require repayment. In order to counteract a potential debt spiral, the ECG followed the Bretton Woods Institutions and adopted the *Principles and Guidelines to Promote Sustainable Lending Practices in the Provision of Official Export Credits to Low-Income Countries* (TAD/ECG(2008)1).

5. Conclusion

The main objective of international development policy as formulated by the MDGs is the eradication of extreme poverty. This implies that development co-operation should be directed at the poor in developing countries and should promote development processes along the interests of its recipients. Yet, other goals such as the promotion of donor business interests are accommodated in aid policies as well. By tying a concessional credit to procurement in the donor country, OECD countries endeavour to bridge their export promotion and development policies. The resulting policy amalgam builds on the assumption that the respective goals of export promotion and development co-operation are mutually reinforcing. Our assessment of the *Arrangement on Officially Supported Export Credits* against the backdrop of the DAC's Paris Principles suggests that the simultaneous achievement of these twofold goals must not be taken for granted. Clearly, to a limited extent development policy safeguards are integrated in the international framework. While this might simply reflect the Arrangement's main purpose, which is to eliminate trade distortions, from the perspective of PCD the regulatory framework appears insufficiently suited for producing policies conducive to development. Even more so, in view of the ODA-eligibility of the instrument, our discussion has highlighted several incoherences:

1) *Ownership vs. supplier-driven policies*

   The Arrangement does neither in its core text nor in its annexes provide for tools to increase the ownership of recipients and to ensure demand-driven project planning. For instance, though not prohibited by Arrangement provisions, the existing framework does not create incentives for donor states to conclude bilateral agreements for soft loan financing.

2) *Local procurement and Private Sector Development (PSD) vs. procurement-tied aid*

   At a conceptual level, the contradiction between tied aid and the DAC's call for local/regional procurement is irresolvable, thus rendering global untying the first-best solution. Even in the *status quo*-situation of continued tying, the options to maximise the development orientation of tied aid credits have not been fully exploited. For instance, with regard to the permissible share of local costs, set at 30 %, room for manoeuvre to increase local procurement prevails. Likewise, a clear-cut ban for tied aid to LDCs rather than their exemption from Arrangement provisions could improve the coherence of the *Helsinki Disciplines* with the DAC's development agenda.

3) *Lack of monitoring and evaluation provisions vs. ensuring effectiveness and sustainability*

   While the Arrangement, in particular the Ex Ante Guidance, provides some means to assess development dimensions of prospective projects, the international framework remains silent on reporting on progress and impact during and after project implementation. Considering the omnipresence of concepts as 'value for money' and 'managing for results', it seems remarkable that the interest towards a proper assessment of projects' ability to meet the stated objectives by applying, for example, ex-post evaluations is limited.

In light of these shortcomings, the ongoing discussions on the future of financing for development might provide an opportunity for change, allowing to improve the coherence between development policy and export promotion goals.

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DCD/DAC/FA/M(93)2/PROV

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DCD/DAC/FA(94)9

DCD/DAC/FA(95)1

DCD/DAC/FA(95)2/REV 1

DCD/DAC/FA(95)3/REV1

D/DAC/FA(97)8

DCD/DAC/FA(98)4

DCD/DAC/FA(99)8

Participants Group

TD/CONSENSUS(91)31

TD/CONSENSUS(92)12

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