THE DEVELOPMENT ASSISTANCE COMMITTEE:
ENABLING EFFECTIVE DEVELOPMENT

The accidental birth of "official development assistance"

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OECD DEVELOPMENT CO-OPERATION WORKING PAPER 24

Authorised for publication by Jon Lomoy, Director, Development Co-operation Directorate

OECD
BETTER POLICIES FOR BETTER LIVES

September 2015

OECD Development Co-operation Working Papers

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The accidental birth of "official development assistance"

Simon Scott[1]

Abstract

Official development assistance (ODA) has been the standard measure of foreign aid for 45 years, but its creation was largely accidental, and followed no plan. Its origins lie with efforts by the OECD's Development Assistance Committee (DAC) in the early 60s to soften and harmonise the terms of aid to developing countries. The DAC agreed a first Recommendation on aid terms in 1965, but its targets were complex and its quantities not adequately defined. An underlying difficulty was identifying which loans were soft enough to count as aid and thus be subject to the disciplines. Among metrics for valuing the concession embodied in loans, the "grant element" methodology proved the most fruitful, and it was used to refine the targets in a 1969 Supplement to the Recommendation. That Supplement introduced the idea of "official development assistance", but without defining it. It was not until the 1972 revision of the Terms Recommendation that ODA was fully defined. This included setting a minimum grant element for an ODA loan and a single target for the overall "softness" of aid programmes. Special terms targets were agreed for a new category of Least Developed Countries. Though not perfect, the 1972 decisions created an integrated and fully specified system for monitoring aid volume and softening aid terms. The process that produced this result turned on interactions between the OECD and the UN system that helped generate the required innovations in concepts and techniques.

Introduction

This paper aims to fill a gap in readily available information on the origin of the concept of official development assistance (ODA). It concentrates on how measures to improve the softness (concessionality) of aid terms over the period 1961-72 contributed to the ODA definition. This is an important but little understood chapter in the history of the official development co-operation machinery.

Discussion of the issue of aid concessionality is often dominated by controversies about the grant element test which the OECD's Development Assistance Committee (DAC) introduced into the ODA definition in 1972. Many have queried why this test effectively used a loan at 10% interest as its reference point, and why ODA loans only had to bear a grant element of 25% when measured against this standard. The questions are simple and legitimate, but the answers are embedded in the development of a wider control system over the terms on which aid is extended.

For the grant element formula was only a further step in a decade-long effort to harmonise the terms of aid among DAC members. Most of this effort occurred before the category of ODA was

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conceived, and for some time after ODA emerged, it did not itself include a grant element test. The need for one only became fully apparent once the United Nations had set a target level for ODA. That volume target then became the focus of policy attention, but it did not supersede the terms target, which, though less noticed, continued in force.

The approach taken here is chronological, but also attempts to explain the logic that guided major steps in the process. While the narrative finishes in 1972, and primarily aims to fill a gap in the historical record, it may perhaps also provide useful background as policy-makers seek to implement the decision of the 2014 DAC High Level Meeting to change the measure of ODA from flows to grant equivalents [OECD 2014; cf. Hynes and Scott, 2013].

1961-65: Softening the terms of official assistance

> ***From its inception, the OECD's Development Assistance Committee was concerned to soften the terms of official assistance. By 1965 it had agreed specific targets for this. In the absence of a definite concept of official development assistance, these targets applied to total official flows, which included export credits and tied aid.***

In 1993, reviewing his 33 years' service to the OECD's Development Assistance Committee, the head of its secretariat, Helmut Führer, pointed out that

defining and refining the concept of ODA has been a central preoccupation of the DAC from the very first meetings of its predecessor, the DAG [Development Assistance Group] [OECD 1994, p 3]

The DAG had been established in January 1960 on an initiative of the United States led by C. Douglas Dillon, Under-Secretary of State in the Eisenhower Administration. Its first meetings were indeed largely concerned with how to improve the information on financial assistance to developing countries. But at the time there was still no definite concept of what constituted official development assistance, and ODA would not exist as a recognisable acronym until almost a decade later.

What did exist in the DAG were strong political objectives, enunciated in its Resolution on the Common Aid Effort of March 1961, to improve the volume, terms and effectiveness of aid. Work on all three would eventually contribute to forging a definition of ODA. But the key role, as this paper will show, was played by work to harmonise and soften the terms of aid, and in particular to ensure that all DAC members gave the bulk of their aid either as grants, or loans at highly favourable terms.

The aim of liberalising aid terms was implicit in the DAG's 1961 Resolution, which observed that:

…the needs of some of the less-developed countries at the present time are such that the common aid effort should provide for expanded assistance in the form of grants or loans on favourable terms, including long maturities where this is justified in order to prevent the burden of external debt from becoming too heavy. [OECD 1994, p 11]

The DAC High Level Meeting of 1963 carried this further by recommending that members relate the terms of aid on a case-by-case basis to the circumstances of recipients, and suggested the idea of

providing grants and very soft loans for general development purposes while maintaining hard loans for specific projects. It also recommended that members

…should make it their objective in principle to secure a significant degree of comparability in the terms and conditions of their aid, and so far as possible to eliminate or reduce discrepancies between them. While this would not necessarily entail standard terms and conditions from all donors, it would involve a liberalisation of the terms adopted by some Members… [OECD 1964, p 44]

The drive within the DAC to soften the terms of aid loans soon received further impetus from the first UN Conference on Trade and Development (UNCTAD I), held at Geneva in 1964. This expressed concern about the growing debt service burden of developing countries and called for attention to be paid to countries' borrowing and repayment capacity when extending loans.

In response, the 1965 DAC High Level Meeting adopted a Recommendation on Financial Terms and Conditions which began by noting

…continuing serious increases in the burden of debt charges on the less-developed countries in spite of the progress of some D.A.C. Members in the past year in easing the terms of public loans. It was stressed that unless this trend was reversed, it might well result in diminishing the net flow of resources to the less-developed countries. The Meeting recommended that Members who do not already provide at least 70 per cent of their official assistance in the form of grants should endeavour to provide 80 per cent or more of their total official assistance at favourable terms, i.e. either as grants or as loans with long maturities (25 years or more), at low rates of interest (3 per cent or less) and that the average grace period[2] on loans should be 7 years.[3] [OECD 1965, p 16]

The Recommendation justified such specific numerical targets partly on the basis that

…continuing differences in terms provided by Member countries not only endanger the spirit of the common effort, but make it more difficult for those with the most liberal terms to maintain past gains which they have made. [OECD 1965, p 118]

Terms were to be adapted to each developing country's circumstances

…utilising such indicators as existing debt burden, income level, resource endowment, development performance and prospects, and other relevant factors [ibid.]

[2] The grace period is the span from the date of commitment of a loan to the first repayment of amortisation, i.e. the interval to the first repayment. Interest may still be payable during a grace period.

[3] This account by the DAC Chairman, Willard Thorp, is not precisely accurate, but it perhaps best expresses the intention of the Recommendation, which itself is formulated in a tortuous fashion. It first specifies the terms parameters observed for 1964 at the level of total DAC commitments: 81% were either grants or loans at 3 per cent or less interest, 82% were either grants or loans with 25 years' maturity or more, and the loans had an average grace period of 7 years. The Recommendation goes on to note that some members extended 70 per cent of their total assistance in the form of grants, and it then adjures those members that "do not reach" 70 per cent grants to "use their best efforts" to reach "within three years" the average 1964 terms for total DAC commitments. The injunction is then hedged about with qualifications – recognising that some countries would find it hard and take more time, it was nevertheless "recommended…that significant progress will have been made by those members during this period" and that "For these countries, the rate at which, during the three-year period, they will have progressed toward the agreed objectives is the important factor". [OECD 1965, p 120]

and harmonisation should

…In the light of the conditions present in most cases…be accomplished by the softening of terms by Members whose assistance carried the highest interest rates and shortest amortisation and grace periods. [ibid. p 119]

Thus, within its first four years of existence, the DAC had both established the rationale for harmonising aid terms, and adopted specific methods and targets for achieving this. The approach was extremely practical. It was recognised that different terms were appropriate for different borrowers, so lending members were to pursue harmonisation through existing consortia and other consultative arrangements for each developing country. The overall terms of each member's programme were to attain the average achieved by the DAC as a group in 1964. Performance was to be assessed every year for every member through the Annual Aid Reviews then undertaken.

All this was achieved before the concept of official development assistance had even been proposed. It was a formidable achievement, though it was recognised that there was some unfinished business. For in the absence of an ODA concept, the targets related to total official flows, and this total included official export credits, which were a disturbing influence on a number of levels. First, they were loans, often unsubsidised, that added to recipients' debt burdens and made terms targets harder to achieve. Second, the credits had as their prime motivation the promotion of the donor's exports, not the development of the recipient. They were thus outside the mandate of the DAC: control over them rested with members' trade officials, not their aid agencies.[4] Third, export credits overlapped with tied aid credits, which *were* within the DAC remit. Tied aid credits are official loans for development purposes under which procurement is restricted in ways that favour suppliers in the donor country. They thus impose conditions that potentially reduce the value for money of an aid commitment. The 1965 Recommendation devoted a separate section to aid tying, observing that

…balance of payments and domestic political considerations have led to considerable aid tying by regulation and administrative action. This development, however, can bring about cumbersome limitations on the freedom of the recipient to choose freely the most suitable sources of supply on the international market. [ibid. p 120]

The Recommendation affirmed that members should try progressively to reduce the scope of aid tying, and proposed several measures to palliate the effects, including ensuring competition among domestic suppliers, selective waivers, third-country sub-contracting, and allowing purchases to be made in other developing countries. However, no firm rules or targets were agreed.

Despite the "loose ends" of export credits and tied aid, by the end of 1965 the DAC could be well satisfied with its initial work to soften aid terms. Clear targets had been agreed to encourage the members making loans at hard terms to soften these to at least the DAC average, and a sound monitoring system was in place. What, DAC members may have asked themselves, could go wrong?

[4] The 1967 DAC Report observed that "the agencies which handle official guarantees for such transactions [export credits] are frequently not in close enough contact with their own external public lending institutions and may, indeed, apply quite different criteria in extending their guarantees. This is a matter on which the Staff of the IBRD has recently reported to UNCTAD and where DAC members clearly need to consider their own internal arrangements for better inter-agency co-ordination. It is particularly difficult because the interest in trade expansion may be in direct conflict with the concern over rising debt." [OECD 1967a, p 166] This problem would continue for decades.

1966-67: Problems with the Terms Recommendation and the flow target

> ***The 1965 Terms Recommendation aimed to soften hard loans towards the DAC average. Instead, soft loans hardened towards the average. The DAC then considered new approaches, including deducting interest when measuring aid. But a more promising method was to calculate the "grant element" of loans, which expressed their softness in a single number. During this period, definitional and practical problems were emerging with the UN target for total development flows of 1 per cent of donors' national income.***

Three problems quickly emerged with the new Terms Recommendation: hardened terms in practice, the lack of a clear comparator of performance, and problems in properly specifying its coverage.

The aim of the Recommendation was to encourage DAC members that were lending at hard terms to soften these terms towards the DAC average. But once those average terms had been established as benchmarks, the members lending at softer terms saw the opportunity to make less generous loans while still meeting the criteria. The DAC Chair reported in 1966 that

…some member governments, whose terms had been softer than the DAC average, hardened their terms, with the result that overall averages became harder.

The 1966 High Level Meeting found it

…a matter of general regret that so little progress could be reported as yet towards implementing the provisions of the 1965 Recommendation…The rapidly growing indebtedness and the greatly increased burden of debt service payments were repeatedly recognised as grave problems which required a co-operative effort by all concerned. Therefore, the Committee decided to continue its efforts to improve and harmonise the terms of assistance in the light of the circumstances of individual recipient countries. [OECD 1966a]

The meeting thus persisted with the terms targets that had been specified the year before, even though these were now more demanding than the latest DAC average. A few months later, the United Nations added to the pressure by passing a General Assembly Resolution urging the developed countries to meet the specific provisions of the Terms Recommendation "not later than 1968". [UN 1966]

A second problem arose from the complexity of the Recommendation's targets. As already noted, donors could meet it either by increasing the share of grants in total ODA to 70%, or by matching the 1964 DAC averages on each of the three loan parameters of maturity, interest rate and grace period. This was cumbersome, and impaired comparison of the performance of donors. For there was no overall quantitative measure of performance: one could only show which criteria each donor met.

The DAC's 1966 Report discussed two possible approaches to refining the assessment of loan terms. The first was to place more emphasis on "net transfers", in which case "not only is amortization deducted from gross new credits but current interest payments are subtracted as well". [OECD 1966a, p 53] This "reflects the impact on the [donor] government accounts and the budget…, making it clear that the net cost of foreign assistance to the government is well below the gross in

most cases." [ibid.] Deducting interest payments would help quantify differences in the softness of loans. But since deducting interest reduced the apparent effort, "net transfers" was not a method that appealed to donors eager to showcase their largesse. For the same reason, the method was much more popular among recipient country governments.

A more direct way of improving the assessment of the terms of aid was the new grant element method introduced by John Pincus of the RAND Corporation and developed by an economist at the OECD Development Centre, Göran Ohlin.[5] The grant element combined, in a single percentage, the softness afforded by a loan's tenor (maturity), interest rate, and grace period. Multiplying the grant element of each loan by its face value gave its "grant equivalent", and adding these to the volume of grants gave the total grant equivalent of official assistance. This total grant equivalent, expressed as a percentage of total assistance, in turn yielded the overall grant element of the assistance.

Thus it was recognised that the grant equivalent of each loan could be added to grants to form an alternative measure of assistance. Ohlin found grant equivalents by means of a simplified mathematical formula to compare loan repayment obligations with what those obligations would have been if loans had been made at some selected reference rate of interest. Grant equivalents could also be arrived at manually by discounting each future repayment on the target loan by the reference rate of interest, and subtracting the result from the face value of the loan. Either method would

…adjust for expected return payments by discounting to a present value [which offered the possibility that]…*Instead of recording a loan at its face value, it would be included only to the extent that its schedule of payments fell below that of some selected market rate of interest. Thus grants would be fully included and loans would be valued according to the softness of their terms including grace periods. (The choice of the appropriate rate for discounting presents some difficulty.)* [OECD 1966a, p 54]

The choice of the appropriate rate for discounting did indeed present some difficulty in future discussions. In a technical publication, the DAC showcased grant equivalents calculated both against a fixed discount rate of 10%, and against the average long-term official borrowing rates in each country in the year loans were made. [OECD 1967b, p 142] The DAC's 1966 Report advanced the idea that the grant element "endeavours to measure how much the country is giving up as compared with the productivity of investment in its own territory" [OECD 1966a, p 54] and its 1967 Report followed this logic in selecting a 10% discount rate, though with some caveats:

…The calculated grant element is substantially affected by the choice of the alternative rate of return which is used for discounting purposes. A uniform rate of 10 per cent has been chosen as an approximate indication of economic rates of return. In making precise comparisons among donors it

[5] For references to Pincus' early papers, see [Cooper 1965, pp v-vi]. Ohlin developed Pincus' ideas into formulas which assumed a continuous repayment stream, and thus were only approximations. More accurate tables, based on discrete payments at intervals, were produced in 1972. [Ohlin 1966, p 101f.; OECD 1972f, p 9] Pincus had used Ohlin's work to produce grant element tables using discount rates from 5% to 10% in [Pincus 1967, pp 312-3], and he also produced grant equivalent estimates of aid over the years 1960-5 using donors' costs of funds as the discount rate [ibid. pp 315-6]. [Riordan 1972, pp 23-6] reviews the contemporary discussion, including within the OECD, of the various possible bases for establishing discount rates. The circle was small: Pincus, Ohlin and Jack Stone (head of the relevant OECD division at this time) had been friends and graduate school classmates at Harvard in the mid-50s, while Cooper took his Ph.D there in 1962.

may be that one should take the relative interest rate levels of their domestic capital markets into account. However, for the present purposes of making inter-year comparisons the general use of 10 per cent provides a reasonable basis for the calculations. [OECD 1967, pp 77-8]

The 1967 Report was also quick to point out the limitations of grant equivalent figures:

It must be emphasised that while it is possible to express the grant element in terms of absolute amounts, this is an entirely notional figure. It does not correspond to an actual flow of funds or of goods and services nor is it in any way related to the net benefit of aid to the recipients. The grant element concept cannot be applied to private capital flows. For equity investment, future rates of return are not known… [ibid.]

Given these reservations, it is not surprising that the Report gave only limited weight to grant element calculations. It still devoted much more space to assessing the performance of individual members against the individual targets in the 1965 Terms Recommendation. The full potential of grant element calculations would not be realised for some time.

A third problem concerned the coverage of the Terms Recommendation. As the DAC had already noted in 1965, the inclusion of export credits was a disturbing influence in a number of respects. But from another angle, the coverage of the Terms Recommendation might have seemed too narrow. For a separate volume target had long been the subject of formal obeisance by DAC members, and it covered a much wider gamut of flows than the Terms Recommendation – including private flows that were entirely outside the control of the aid agencies represented in the DAC.

This volume target had initially been set by a UN General Assembly Resolution in 1960, which expressed the hope

…that the flow of international assistance and capital should be increased substantially so as to reach as soon as possible approximately one per cent of the combined national incomes of the economically advanced countries. [UN 1960]

But while "international assistance" was within the DAC's purview and subject to "explicit policy decisions", "international capital" reflected decisions taken by actors in the private market and it displayed "a much more erratic character". [OECD 1966a, pp 52]

The impossibility of controlling private flows did not matter much while the target was still an aspirational one for the developed world as a whole, rather a practical one applying to each individual donor. But the Recommendation on Growth and Aid approved at UNCTAD I in 1964 had converted it into a target for individual countries, though with some caveats, as follows:

Each economically advanced country should endeavour to supply…financial resources to the developed countries of a minimum net amount approaching as nearly as possible to one per cent of its national income, having regard, however, to the special position of certain countries which are net importers of capital….This is not intended to represent either a ceiling or a suitable method for comparing the appropriate quantitative or qualitative development assistance efforts as between different economically advanced countries. [UN 1967a, pp 65-6]

Despite these easements, the DAC's 1966 Review noted that "there are those that feel that this indicator already needs revision", that it "disregards certain problems of definition" and that the DAC was "conscious of the serious imperfections of the one per cent target". [6] [OECD 1966a, pp 49-50] Apart from the fundamental problem that private flows were outside government control, there was also an issue over the denominator – the "combined national incomes of the economically developed countries". The DAC had used *net* national income, which omitted amounts required to keep the capital stock intact (depreciation) and took prices before the addition of indirect taxes and subsidies. But the UN itself had used the higher *gross* national product as the denominator, which reduced the assessed performance of DAC members by between 10 and 25 per cent.

The DAC naturally preferred net national income as the denominator, as this flattered its members' performance. While the DAC's 1966 Report conceded that the interim report of a UN expert group recommended gross national product instead, it maintained that "pending the experts' final report and action thereon by UN bodies, the DAC is continuing to use [net] national income as the denominator". [OECD 1966, p 51]. But the UN expert group's final report gave no relief. It plumped for gross national product, despite the firm opposition of one its leading members, C. H. Harvie, who as Director of the Statistics Division of the UK Ministry of Overseas Development was a representative of a DAC member country. Harvie had missed the first meeting of the expert group that had produced the interim report and when at the second meeting he could not persuade the group to reverse its support for gross figures, he made a point of twice recording his dissent in the final report, insisting that "net national product better represents a country's capacity to give aid." [UN 1967a pp ix, xiv and 24] But the battle was lost.[7]

The thorn of the one per cent target became even more uncomfortable after the first ministerial meeting of the Group of 77 at Algiers in October 1967. This Group had been signatories to a Joint Declaration at the conclusion of UNCTAD I, and now

…Having reviewed the work of the international community for economic progress since the adoption of the Joint Declaration…Deem it their duty to call the attention of the international community to the following facts:

I The lot of more than a billion people of the developing world continues to deteriorate as a result of the trends in international economic relations

…which the signatories itemised in terms of developing countries' slow economic growth, growing disparities with the advanced countries, declining shares of world exports, increasing indebtedness,

[6] Successive DAC Chairmen repeatedly criticised the one per cent target as ill-defined and unworkable. The Chair at this time, Willard Thorp, was still complaining about it twenty years later, observing that it "was, of course, an entirely arbitrary figure based on no calculations of need or ability to pay." He conceded, however, that it "did exert an influence" and even admitted that "It gave the DAC Chairman [i.e., himself] effective arguments to the general public, the news media and government officials during his visits to Member countries." [OECD 1985, pp 46-7]

[7] Harvie was something of an activist. He had made his name with a 1959 work on the national income accounts of Sudan, published "with the help of eleven Sudanese assistants." [Young 2013, p 197] This claimed that excessive importance was being given to the sectors of the Sudanese economy (mainly cotton growing) on which data happened to be available. Harvie next took up the post of Chief Statistician of Malaya, a job he again attacked with vim, announcing to the papers on his arrival plans to hunt down data on previously unrecorded businesses. [Singapore Free Press 1959, p 2]

rising debt service obligations, technology gaps, and brain drain. The blame for this situation was put squarely on the advanced counties which according to statement were dragging their feet on new trade agreements, increasing the protection of their home industries, and even resorting to "synthetic substitutes… for competing natural products produced by developing countries." A Programme of Action proposed extensive remedial measures, including demands that:

(a) Each developed country should comply with the target of a minimum 1 per cent of its gross national product for net financial flows, in terms of actual disbursements, by the end of the United Nations Development Decade. A separate minimum target, within this goal, and progressively increasing, should be established for the official component of aid flows, net of amortization and interest payments;

(b) Any gaps remaining in the 1 per cent transfer each year should be made good by additional government transfers [UN 1967b]

Demand (a) insisted that performance against any future aid target be measured as "net transfers", i.e. deducting interest. This was contrary to the balance of payments treatment of capital flows, and would lead to negative net amounts over the life of a loan, so it was a proposition that donors were unlikely to accept.

Demand (b) was clearly unrealistic: DAC members could not know in advance the level of private flows from their countries, and raiding their budgets afterwards to make up any shortfall against the one per cent target was out of the question, as successive DAC Chairmen pointed out. Still, DAC members were now on the hook. They had accepted one per cent as an individual country target at the first UNCTAD in 1964 and repeatedly re-endorsed it at subsequent DAC High Level Meetings. Some escape route would have to be found, and the G77 declaration suggested a path to follow: a new measure confined to the official aid flows under DAC members' control. This would eventually allow a lower and more practical aid volume target to be set. It would emerge through the necessary reform of Terms Recommendation – to purge it of export credits and streamline its assessment of concessionality.

1968-69: The emergence of official development assistance

> ***The UNCTAD II conference in 1968 increased the pressure on DAC members to liberalise aid terms. A 1969 Supplement to the Terms Recommendation addressed this by setting new targets based on the grant element methodology. Coverage was for the first time restricted to "official development assistance", which took some time to define.***

After the G77 meeting in late 1967, the task of cleaning up the Terms Recommendation was given further urgency by the deliberations of UNCTAD II at New Delhi in February and March of 1968. First, the Conference confirmed gross national product as the denominator for the one per cent target. This decision reduced DAC members' performance against the one per cent target to around 0.75% of GNP and left them with the preposterous task of finding budget funds to make up for a variable and unpredictable shortfall of private financial flows to developing countries.

The Conference then came close to giving effect to a suggestion by its Secretary-General, Raúl Prebisch [UN 1968, p 419] for a new official aid target in line with the G77's call four months earlier at Algiers. However, being still without a firm concept of the "official component of aid flows", the Conference could only debate a target for total official flows, and this gained only limited support:

A number of developed countries stated that within the 1 per cent target defined above, they were prepared to attempt to provide a minimum of 0.75 per cent of their GNP by way of net official financial resource transfers. [UN 1968, p 39]

The donors also had a "win" at New Delhi when the agreed final specification of the numerator in the one per cent target remained on the "capital flows" basis [ibid., footnote 31], rather than the net transfer basis, which would have deducted interest receipts as the G77 had demanded. Nevertheless UNCTAD continued to lobby for net transfers in future years. [cf. UN 1975, p 6]

There was also considerable agitation at UNCTAD II for a further softening of the terms of aid, although

…the Group B [developed] *countries in the UNCTAD successfully minimised controversy on the question of terms by pointing to the review of the Terms Recommendation under way in the D.A.C.* [OECD 1968a, p 3]

Against this charged political background, the job of reviewing the Recommendation fell to the DAC's Working Party on the Financial Aspects of Development Assistance. Initially it aimed high:

Review of the objectives is called for this year in the 1965 Recommendation itself and is endorsed in the Agreed Texts on financing emerging from UNCTAD II with the "hope that it will result in further liberalisation of terms". The simplification involves replacing the present complicated array of alternative standards with a single more simply stated standard.[8] [OECD 1968b, p 3]

The single standard for aid terms, however, eluded them. After several rapid rounds of discussion, the first test from the 1965 Terms Recommendation – the 70 per cent minimum grant share – was retained unchanged. But the previous alternative test of reaching at least the 1964 DAC averages in respect of each of loan maturities, interest rates and grace periods was replaced with two new targets based for the first time on grant elements, urging members

[8] The central figure in these proceedings was the thrustful Jacob ("Bob") Everts. Since 1964 he had chaired the Working Party on Financial Aspects and he also represented the Netherlands at UNCTAD II where he was elected Chairman of the Third Committee dealing with such matters as aid terms and aid volume. In this capacity he submitted to the plenary [UN 1968, pp 300-5] specific proposals to tighten the targets in the Terms Recommendation to either an 80% grant share, or 90% either grants or loans at no more than 2.5% interest, with 30 years' maturity and a minimum grace period of 8 years. After the proposals came bracketed text observing that "The developed countries take note of these suggestions and are prepared to take them into account in the evolution of their assistance policies." [UN 1968, p 301] This package made it into the final decisions of the conference, slightly diluted by adding that developed countries "generally" took note of the suggestions. [ibid. p 40] Everts' proposals also included a suggestion of a 0.80% of GNP target for total official flows [ibid. p 305], which was again slightly trimmed to 0.75% in the final text. Thus Everts' diplomatic activism may well have contributed to the "successfully minimised controversy" over terms at UNCTAD, while increasing the pressure on the DAC to tighten its terms targets.

A to provide at least 85 per cent of their official development assistance commitments so that each transaction has a minimum concessional element of 61 per cent[9]*;*

or

B to ensure that 85 per cent of their official development assistance commitments contain an average concessional element of at least 85 per cent. [OECD 1969a, p 269]

The new Recommendation was no tighter than the old one. The grant share benchmark of 70% was unchanged, and the 85% of aid programmes targeted by the two new options was arrived at simply by recalculating the 1964 observed total share of grants and soft loans after excluding some export credits. [OECD 1969c, p 5] This meant that both the new A and B alternatives retained a "free area" of 15% of commitments which could be counted as aid regardless of their terms.

Some members deplored the complexity of the new Recommendation and

During the final discussion of the Recommendation several delegations expressed disappointment that the Recommendation could not go further and that it had not been possible to reach agreement on a simpler presentation of the objectives.

Most members, however, were content to leave a menu of objectives, which gave them "more than one way to skin a cat": having multiple objectives increased their chances of showing improved performance against at least one in the annual reviews then conducted. The full measure of the complexity that had now been introduced would not become apparent until the following year.

While it made little progress on its core task of liberalising terms, the new "Supplement" to the Recommendation represented a breakthrough and a radical overhaul in respect of its coverage and method. For it had at last expelled export credits from the coverage and thus, almost with its left hand, introduced the concept of official development assistance:

The objectives of the Recommendation apply to official development assistance, which is intended to be concessional in character. In addition, however, export credits have become of increasing importance as a source of finance and have contributed to the indebtedness problems of a number of developing countries. DAC Members, therefore, agree to review more fully, in consultation with other interested Committees of the OECD, the differences in their basic approaches to export credits, whether official or officially guaranteed, and their relationship to aid and development considerations. [OECD 1969a, p 268]

Note that at this stage "official development assistance" was not a formal name but merely a descriptive term that excluded commercial credits. There was no definition, and this task was

[9] The 61 per cent grant element was based on a model loan of 30 years maturity, 8 years grace period and 2.5% interest [OECD 1969d, p 2]. These terms are slightly softer than those used in the 1965 Recommendation (25 years maturity, 7 years grace and 3% interest), but this cannot be assumed to represent a tightening of the disciplines since the export credits still included in 1965 would have shortened average maturities and grace periods, and raised the average interest rate. Observe also that Everts had already proposed the same new softer terms parameters at UNCTAD, but for application to 90% of aid rather than the 85% eventually agreed.

remitted to a new ad hoc Group on statistical problems which had met for the first time in January 1969.[10]

The Secretariat's first attempt at definition, circulated to the ad hoc Group on 3 March 1969, was a mish-mash of institutional, instrumental, and intentional criteria:

Official development assistance is defined as all transactions with less-developed countries which are administered by government development assistance agencies or where funds are channelled through institutions considered as executive agents for government development assistance and welfare programmes. Contributions by state and local governments for these purposes shall also be included.

Official transactions which are primarily trade facilitating in character and over which governments exercise no direct control are excluded even if they are financed wholly or in part from official sources. [Such transactions are, nevertheless, considered to be official development assistance if their maturities exceed 15 years.]

Official contributions to multilateral institutions and voluntary agencies for development assistance and welfare purposes are to be included. [OECD 1969e]

This was obviously unsatisfactory and at the meeting on 17-18 March "discussion on this subject was inconclusive." [OECD 1969f] A second proposed definition issued ten days later is already close to the wording today:

Official Development Assistance is defined as all flows to less-developed countries and multilateral institutions (as defined for this purpose) provided by government agencies, including state and local governments, or by their executive agencies, which meet the following tests:

a) they are administered with the primary objective of promoting the economic development and welfare of developing countries; and

b) they are intended to be concessional in character, i.e. their terms are significantly softer than the market terms prevailing in the donor country. [OECD 1969b, p 2]

Focusing on flows, rather than institutions, and carefully enumerating the conditions which such flows would have to fulfil, gave ODA solidity and credibility as a statistical concept. But there was still a hitch over the last phrase explaining what was meant by "concessional in character". Amendments were proposed and at the next meeting on 3 June a new variant came close to securing agreement:

An amended version of criterion (b) of the definition of Official Development Assistance (O.D.A.), namely:- "they are intended to be concessional in character, i.e. their terms are significantly softer than the terms normally available for commercial transactions with less-developed countries (such as

[10] "The DAC has instructed the ad hoc Group on Statistical Problems to arrive at a definition and identification of official development assistance." [OECD 1969b, p 1]. The ad hoc group's first Chair was Mr C. H. Harvie of the United Kingdom, re-entering the lists after his experiences described above with the UN expert group on measuring resource flows to developing countries. Its Secretariat was headed by Bevan Stein, who would play a key role in preparing its subsequent work to define both ODA and other official flows for development. [OECD 2011, p 7]

guaranteed export credits)" was felt by many delegations to be an acceptable formulation, but the United States and the United Kingdom reserved their position. (The United States reservation was lifted later.) [OECD 1969c, p 3]

Yet there was still no agreement and the version of the ODA definition given in the annual report in December 1969 simply terminates with the words "concessional in character" without saying how this was to be assessed. In practice, though, much of the work had been done in the intervening months by simply identifying which of members' loan programmes would be included as ODA, and which would be relegated to the rump category of "other official flows":

The criteria for defining official development assistance as set out above are inevitably somewhat subjective and there are a number of borderline cases where the classification of a type of transaction as development assistance is particularly difficult. The DAC has, therefore, reviewed institutions and lending programmes in order to determine those transactions which, while official in character, should not be recorded as official development assistance. In the light of this review the following transactions will from now on be recorded as "other official flows" [OECD 1969a, p 242]

…whence follows a list of seven lending programmes in the United States, Canada, Germany, Japan and Italy along with "purchases by central banks and governments of bonds issued by multilateral development banks at market rates". The appropriate recording of guaranteed export credits by the Austrian Kontrollbank was "still under consideration".[11]

Further work would clearly be needed on concessionality, both to simplify the policy objectives in the Terms Recommendation and to clarify the definition in ODA. These workstreams now diverged somewhat, as separate OECD subcommittees took charge of them. The Working Party on Financial Aspects continued work to liberalise terms, while definitional issues went to the ad hoc Group on Statistical Problems[12].

All the same, by the end of 1969 solid progress had been made. The Terms Recommendation now excluded export credits and so could focus on developmental flows. Grant element calculations had been introduced to begin simplifying terms objectives. And the new concept of official development assistance would soon open the way to a new volume target based on a quantity that DAC members could effectively control.

1970: ODA takes over

> ***The new ODA concept allowed the UN to set a new target of 0.7 per cent of GNI for official aid flows only, largely superseding the 1 per cent target for total flows. The new target changed the incentives for DAC members: instead of trying to exclude less concessional loans from ODA so as to meet the Terms Recommendation grant element***

[11] A final settlement of this issue was not reached until 25 October 2002, when Austria agreed to report as ODA disbursements only the actual annual subsidy payments from the Ministry of Finance to the Kontrollbank. [cf. OECD 2004, pp 77-8] See the next section for discussion of the origin of the exclusion of some other countries' credits.

[12] The "ad hoc" was dropped in 1971 and the Group was upgraded to a Working Party in 1973.

thresholds, they would henceforth prefer to include them so as to meet the ODA volume target.

The need for further work to simplify terms objectives became evident in 1970 when performance under the 1969 Supplement to the Terms Recommendation was assessed for the first time. For a start, the Supplement had observed that several members

…are still far from the standards of the original 1965 Recommendation…These Members are urged, while keeping the new objectives in mind, to concentrate their efforts on first meeting the original objectives. [OECD 1969a, p 270]

This wording meant there were now two sets of objectives. It also gave the impression that the 1969 Supplement was more demanding than the 1965 Recommendation, but that was not necessarily the case. In fact, ten of the sixteen DAC member countries qualified under the Supplement, whereas only eight met the original objectives of the 1965 Recommendation.

A key reason was that the "simple" test of giving 70 per cent of assistance as grants – which in itself was unchanged from the Recommendation to the Supplement – in fact became easier to meet, since the new denominator, ODA, now excluded some of the loan programmes which had dragged down the grant shares of several members. As a result, the Netherlands and the United States met the 1969 Supplement while still failing the 1965 Recommendation.

Yet more countries would have qualified under the 1969 Supplement had it not also provided that

…countries whose volume at qualifying terms…is significantly below the DAC average as a percentage of GNP will not be considered as having met the terms target. [Footnote:] In statistical presentations of terms performance, official aid volumes would be shown. [OECD 1969a, p 270]

So not only were there now five separate tests of concessionality under the two agreements, but one of the two 1965 tests required fulfilment of three independent conditions, and all three of the 1969 tests were subject to a new criterion regarding aid volume. The complexity was unsustainable – and was not sustained. By the time 1970 performance was assessed in 1971, the annual DAC report had dropped assessments against the 1965 Recommendation, and the Supplement was increasingly being referred to as "the 1969 Terms Recommendation". [OECD 1971a, p 64]

Actual performance on terms remained disappointing:

It would not appear that the pressure exercised by the 1965 Recommendation on the terms policies of donors has caused major improvements, although it is not possible to know how much worsening of terms it may have prevented. [OECD 1970a, p 48]

But while the Terms Recommendation was going through a mid-life crisis, its accidental offspring, ODA, was showing rude good health. In late 1969 it had been extensively used in a landmark report, *Partners in Development,* commissioned by World Bank President Robert McNamara and headed by a former Canadian Prime Minister, Lester Pearson. The Pearson Commission observed that ODA was

…deliberately conceived as development assistance…provided by government and the amount of it can be increased and the terms improved by government decision…on concessional terms…and it can

be directed to sectors of high priority to the growth process [Commission on International Development 1969, p 148]

These features encouraged the Commission, in the light of previous calls at UNCTAD II for a new official aid target to

…seek agreement on a target for official aid which is simple, attainable, and adequate, without, however, limiting other forms of aid within the 1 per cent target figure. We therefore recommend that each aid-giver increase commitments of official development assistance to the level necessary for net disbursements to reach 0.70 per cent of its gross national product by 1975 or shortly thereafter, but in no case later than 1980. [ibid., pp 148-9]

The new concept of ODA was finally allowing progress to be made on a genuine aid target to supplement – or supersede – the flawed one per cent target. A year later, on 24 October 1970, the 0.7% target proposed by the Pearson Commission was adopted, essentially unchanged, by the UN General Assembly.[13] [UN 1970]

Meanwhile extensive work was going on in the DAC, and especially in its statistics Group, to nail down the coverage of ODA. Topics included the ODA treatment of debt relief, administrative costs, equity investment, guarantee schemes, and subsidies to the private sector. Several of the issues would take years to resolve: the ODA recording of debt relief was discussed at almost every meeting of the Group until 1976. In the case of administrative costs, rules were not finally fixed until 1979, though members quickly agreed that these costs should be included in principle even though they had been left out of the list of official flows specified by UNCTAD for measuring performance under the one per cent target. [UN 1968, p 39, footnote 31; OECD 1970d, p 4; OECD 1971b, p 1] The new logic of ODA – official spending on development – was prompting a rethink of coverage and classification issues.

There was also still the question of the concessionality criterion for ODA – exactly which official loans would qualify and thus be counted in the tests specified in the Terms Recommendation Supplement? Here members found they now had conflicting interests. The more loans qualified, the closer they would get to the 0.7% volume target – at least until repayments started coming in. But including more loans in ODA would at the same time reduce their scores against the ODA grant share and ODA grant element tests in the Terms Recommendation.

In 1969, while the focus was still on meeting the Recommendation, members had been keen to exclude loans from ODA coverage. Germany had even threatened to veto the new Supplement unless certain loans by its Kreditanstalt für Wiederaufbau (KfW) were excluded:

During the discussion on this matter the German delegation had stated that it would only be able to accept the new Terms Recommendation if it was understood that export credits extended by the KfW on its own account fell outside the applicability of the targets; the government exercise[s] no control over these transactions; they are largely financed through borrowing from the capital market and should, therefore, more appropriately be regarded as private transactions. [OECD 1969e, p 1]

[13] The only material difference between the Pearson Commission recommendation and the UN Resolution was the deletion in the latter of the compulsion to achieve the target by 1980.

This started a minor stampede to have loan programmes excluded:

The Delegations for the United States and Canada felt that, if the KfW export credits were to be excluded from the terms target, this would, in the interest of consistent treatment, also have to be the case for Export-Import Bank and ECIC transactions. These two governments have agreed to the Supplement on the understanding that transactions from their respective export-credit type institutions will be excluded from the terms recommendation… [ibid.]

But by 1970, with the volume target on the UN agenda, the balance of incentives switched towards including as many loans as possible by applying a low concessionality threshold. The matter was taken up by the ad hoc Group in March, based on a Secretariat paper which recalled that

It appears from discussions in the Ad Hoc Group that Member countries generally are prepared to set the test of concessionality with reference to "market terms". Difficulties were met, however, in specifying and measuring "market terms". In particular, it was not possible to obtain unanimous agreement that the terms of guaranteed private export credits provide an appropriate international benchmark.

At the same time, it was obvious from the way the discussion evolved that the difficulties were of a more fundamental nature, in that the benchmark could be seen from several viewpoints. As seen by a donor country, terms are considered as concessional if they are significantly softer than the market rate ruling in the donor country, which itself varies considerably from country to country. From a recipient's point of view terms are concessional if they are considerably softer than the market terms on which the recipient country might otherwise borrow. [OECD 1970b, p 2]

The document also noted that there was a range of terms for guaranteed private export credits, and pointed to other borrowing options that might be available to developing countries, namely "recourse to a loan from a multilateral organisation, and the flotation of a bond issue on a donor country's capital market." [ibid.] It then made a hard landing on practicalities:

As it is not possible to refer to all these simultaneously, any guideline must necessarily be arbitrary. At the same time, it must be realistic in terms of the various relevant indicators. Table 1 shows the typical range of terms practices in 1968 for each of the classes of market-terms borrowing noted above….Taking a round figure in the neighbourhood of the upper quartile as representing an approximation to cheap market terms, it is possible to develop a guideline for defining concessionality: broadly, that a loan whose grant element lies above a certain threshold is concessional, and vice versa. A formal definition is presented below, taking the threshold at 20%. [ibid., pp 2-3]

At the Group's meeting on 23 March, most members supported a threshold but were

…of the opinion that the figure of 20 per cent put forward by the Secretariat was too low. However, one delegation (Austria) considered this threshold too high, whilst two delegations (France and Switzerland) did not favour the concept, although the French view was that if a threshold had to be fixed it should be relatively low. [OECD 1970c, p 3]

The Secretariat of the statistics Group then produced a range of simulations showing the effect on ODA volume of thresholds of 15%, 20%, 25%, 30% and 50%. Straying onto the turf of the Working

Party on Financial Aspects, it also showed the effect of these thresholds on performance under the Terms Recommendation, noting that any threshold within this range had only a limited effect on countries' compliance. The conclusion was typically down-to-earth:

It is therefore necessary to find a compromise between the improvement of average terms and the smaller volume of commitments to which they apply. Here it should be noted that in the 1969 Recommendation the standards are based on the parameters observed for all the transactions considered. Given that the concept of concessionality had not been quantified at that time, the threshold chosen should be fixed as to minimise the disruption of comparability. The highest threshold involving the fewest repercussions, both on the ability to meet the criteria of the 1969 Recommendation and on the volume of commitments, is a 25 per cent grant element (at a discount rate of 10 per cent). Only Austria's programme would then be affected in such a way that the terms target would be met (for a smaller volume of transactions), whereas without the threshold these standards would not be reached.

This unapologetically practical solution would finally be adopted two years later. But the statistics Group gagged on it when it met on 11 June 1970. It failed to agree on a grant element threshold, and the meeting record, instead of the usual brief account of discussions, presents a negotiated statement to be handed up to the DAC. This explains that the Group has considered options for finding "market terms", but that "there is no single criterion which can serve as a universal benchmark". It then passes the hot potato back to the annual review process mandated by the Recommendation, adding that:

Nevertheless, the ad hoc Group recommends that in the Annual Aid Review, commitments whose grant element does not substantially exceed that conveyed in transactions at market terms should be scrutinised with particular attention to the reasons for their inclusion in the category of official development assistance…In this context, the Secretariat has been requested to draw attention during the Annual Aid Review to commitments made with a low grant element. [OECD 1970d, p 3]

But what was a "low" grant element? Australia, Canada and others, "would have preferred an explicit…figure" while Sweden believed that a definite threshold should be set "at a high level in order to have operational impact". Instead the meeting record spells out that the ODA definition is being left unchanged, with ODA classification determined "primarily…by the reporting country's view of its motive…[in other words, that] the intention to provide concessional terms should be present…" [ibid., p 4]

The ad hoc Group also sheepishly invited the Working Party on Financial Aspects back to the party, observing that it might "wish to conduct a one-time review of the profile of members' programmes as a means of surveying the dimensions of the problem." [ibid.][14]

1971-72: Refining the Terms Recommendation and the ODA definition

[14] Friendly rivalry and buck-passing between the Statistics and Financial Aspects Working Parties and their secretariats continued for many years. As attention shifted from terms to volume, the Financial Aspects group steadily lost relevance. A satirical "Glossary of DAC Terms" circulating among the statistical staff in the 1980s defined the Financial Aspects Working Party as "Fifty solutions in search of a problem."

The DAC realised that its 1969 Terms Recommendation was too complex, and that a precise numerical test was needed to exclude non-concessional loans from ODA. Resolution of these issues in 1972 established a system for assessing aid volume and terms that lasted in its essentials for over 40 years.

The Working Party on Financial Aspects was duly mandated by the DAC to take over the concessionality dossier, but at the time it was occupied with reviewing each member's performance against the existing Recommendation, and compiling indicators designed to help members harmonise terms according to the requirements of each developing country. The United States also started a major work stream designed to secure an agreement on aid untying, but this came to a sudden halt in mid-1971 when the United States itself introduced a raft of protectionist measures that made it impossible for it to sign up for additional untying.[15]

Some time was also spent considering a new measure of concessionality: Years to Zero Net Transfer, or YZNT, which had first been used in the 1970 Terms Scrutiny on 1969 flows, a document that was restricted to DAC members. The idea of YZNT was to compare loans on the basis of how many years it would take the borrower to pay back, in principal and interest, the amount borrowed. It was an ingenious suggestion that reduced loan terms to a single metric – time – that expressed the benefit a borrower was receiving. But it also had disadvantages, including not being in a unit where it could be added to grants – since the YZNT of a grant was infinity. Debate on YZNT proceeded for months before members spotted a crucial flaw:

A number of Delegations felt that the similarity of the concept to that of the "Net Transfer of Resources", which had been a source of difficulties in UNCTAD, could lead to embarrassment if it became known that D.A.C. was using the concept in its confidential terms analyses. [OECD 1971c, p 9]

YZNT was remitted for further study by the Secretariat "with a view to deciding whether its technical advantages were outweighed by the political and psychological drawbacks." [ibid.] It never saw the light of day.

Having disposed of these futilities, the Working Party was ready to take up its brief to settle the definition of ODA and revise the Terms Recommendation. A first Secretariat paper (31 August 1971) acknowledged the changed focus of international discussions since the introduction of ODA and the setting of a target for it of 0.7% of donors' GNP in the Strategy for the Second United Nations Development Decade. Noting this

…shift of interest towards a volume target for O.D.A., now formalised in the text for the UN Strategy for DD2…

it found that…

[15] The United States' delegate to the DAC High Level Meeting on 21-22 October 1971 explained that its "programme for dealing with its basic balance-of-payments problem had also obliged his authorities to postpone conclusion of participating in an untying agreement until the actions taken had proven effective. Their action did not mean that they had changed their basic view that all should seek to provide financial assistance on an untied basis, and he hoped that the day would not be far off when it would be possible to translate this goal into reality." [OECD 1972b, p 16]

The obvious conclusion of this trend of thinking is to look for volume targets in terms of the grant equivalent of O.D.A. or definitions of O.D.A. which set a very high threshold (61 per cent grant element or more) to individual transactions, so that O.D.A. becomes by definition a more homogenous quantity approximating the commonly understood meaning of the word "aid". [OECD 1971f, p 5]

The 61% grant element threshold was of course already in use in the "A-route" of the 1969 Terms Recommendation. Suggesting it as the minimum level of "softness" for an ODA loan, so as to make ODA "by definition a more homogenous quantity approximating the commonly understood meaning of the word 'aid'" was not an entirely new suggestion. In 1969, even before the ODA concept had been introduced:

…the Swedish delegation proposed…the delineation between transactions of an indisputable aid character and other flows…taking the terms of the transactions into account…[a]s to credits…one could…determine some "no harder than"-conditions as had been proposed for the revision of the D.A.C. 1965 terms resolution [OECD 1969g]

This now rather obscure wording in fact translates to a proposal for a 61% grant element threshold for ODA loans, since that was exactly the "no harder than" level eventually agreed for individual transactions in the 1969 "revision of the D.A.C. 1965 terms resolution." But since then the ad hoc Group had all but settled on a threshold of 25%, which would exclude export credits with minimum disturbance to existing ODA reporting. So the 1971 paper for the Financial Aspects Working Party, after briefly mentioning the 61% threshold, quickly added that the need to distinguish ODA from export credits could be met by a much lower threshold, e.g. 25%.

Faced with such widely divergent suggestions, the Working Party meeting on 9-10 September could agree on the need for "a more precise definition of ODA…based on individual transactions", but "felt that further consultations would necessary in order to reach agreement on this important matter." [OECD 1971g, p 3]

These further consultations on the ODA definition soon merged with the renegotiation of the Terms Recommendation which got under way at the end of the year. The discussions proved protracted – the new Recommendation went through five major drafts and the group met eight times before reaching agreement on 12-13 September 1972, just in time for the High Level Meeting in October.

As it turned out, two of the ODA issues were settled easily. On the ODA volume test in the Recommendation, there was no objection to continuing the Secretariat's practice of setting the floor for compliance at 75% of the DAC average.[16] Continuing use of the 10% discount rate also raised no controversy. While lower rates had been countenanced in both DAC documents [e.g. OECD 1967b, pp 141f.] and external studies [e.g. Pincus 1967, pp 312f.], by late 1970 the DAC was informed that even bonds issued by regional development banks were yielding "over 8 ½ per cent and money

[16] For details, see [OECD 1971e, p 13] [OECD 1972d, p 4] and [OECD 1972c, p 3]. The interpretation of "significantly below the DAC average" as less than 75% of that average was only ever agreed in DAC minutes, and never published – a sin of omission noted at the time: "In this context, the Delegate for Canada expressed his misgivings about the growing tendency to relegate important quantitative indications to the Agreed Minutes rather than incorporating them in the Recommendation itself." [OECD 1972e, p 4]

raised by the World Bank cost more than this amount in both Germany and the United States"[17] [OECD 1971d, p 47]. So 10% seemed reasonable, and in any case it was recognised that the effect of choosing a higher or lower discount rate could be mimicked by shifting the grant element threshold in the opposite direction.[18]

This threshold itself thus became the focus of the discussion, and it proved more difficult to pin down. While the statistics Group had all but settled in 1970 on a minimum 25% grant element for an ODA loan, the United States and Nordic countries held out for a higher figure[19], and in the end 25% was only agreed subject to a provision "to review the suitability of this figure in the light of the first year's experience". [OECD 1972c, p 3] In the event it would continue unchanged.

But the main bone of contention in the negotiations was not the definition of ODA but the fixing of a new benchmark for aid terms. Members agreed that having a complex array of targets weakened their effectiveness. So at the first meeting on the subject on 11-12 September 1971

…there was a consensus that the new target should apply to O.D.A. programmes as a whole and that a separate grant test could probably be dispensed with. [OECD 1972c, pp. 3-4]

So the 70% grant share, originally of total official flows, and since 1969 of ODA, was dropped, and attention turned to the two other means of satisfying the Recommendation. Both were considered as possible models for a new single target, which would now apply to "ODA programmes as a whole", not just to 85% of them as in the 1969 Supplement.

The "A-route" introduced in 1969 had been a "transaction-by-transaction" approach: in 85% of an ODA programme, each commitment needed to meet a 61% grant element. But if the Terms Recommendation were now to cover all and only ODA transactions, the grant element required of each transaction could not diverge from that of the ODA definition. So again at the first meeting

As to the…current route A…it was felt that it would lose much of its importance once an agreed O.D.A. definition was adopted... [ibid.]

This left a "general preference" for the B-route, the "programme approach" which had required an overall grant element of 85% in 85% of the ODA programme. Given the agreement to drop the 15% "free area", members started to discuss a minimum grant element for total ODA. Examination of members' actual grant elements indicated possible outcomes of between 80% and 86%. The battle zone soon narrowed to 82% to 86%, and the line of truce was finally drawn at 84%.

At last there was a single clear standard for the concessionality of ODA programmes as a whole, as well as a clear minimum grant element for each ODA transaction. The key had been the application

[17] The "current yield in the lending country concerned on IBRD bonds" had been suggested as a possible discount rate in the 1967 report of the UN expert group on flow measurement mentioned above. [UN 1967a, p 126, footnote b]

[18] Cf. [OECD 1971f, pp 7-8] which notes the similar effects of interest rate caps and grant element floors: "The interest rate element is probably not worth paying much attention to, because, for typical O.D.A. maturities, the grant element is particularly sensitive to the interest rate, so that fixing plausible maximum rates as part of the definition of O.D.A., e.g. 3 or 5 per cent, is tantamount to setting a grant element threshold..."

[19] "…the Delegate for the United States advocated a 50 per cent grant element threshold. This was supported by the Delegates for Denmark, Norway and Sweden, who believed in any case a threshold of 35-40 per cent was the minimum acceptable." [OECD 1972g, p 3]

of the grant element methodology developed by Pincus and Ohlin years earlier. Their innovation now also allowed a new target to be developed in pursuit of the DAC's long-standing objective of tailoring terms to recipients' needs.

This was also facilitated by a firm new list of what were termed the "weakest developing countries" - those which deserved to receive aid on the most generous terms. In 1970, the head of the OECD Financial Policies Division, Jack Stone, had taken a new job as Director of the Research Division at UNCTAD and in this capacity he soon became, as a colleague later told the UN History Project, "the father of the least developed countries concept". The new LDC category identified – on the basis of low per capita income, literacy, and manufacturing capacity – countries which the UN had previously referred to as "requiring special measures". [UN 2005, pp 237-8] The vague and ineffective reference to "special measures" for largely unspecified countries was thus replaced with an actual list of agreed countries after an intense campaign in 1970 and 1971 to get the group, originally proposed by the UN's Committee for Development Policy, endorsed by an UNCTAD expert group, the Trade and Development Board, the G77, UNCTAD II, ECOSOC and finally the UN General Assembly. [Jack Stone, personal communication, 31 May 2015]

The Working Party on Financial Aspects was able to agree on more favourable terms for the LDCs, though again it could not settle on a single measure. In the end there were two alternative LDC grant element targets: 86% to each LDC over a three-year period, or 90% each year to LDCs as a whole. [OECD 1972, pp 207-10]

The overall policy achievement was substantial. Over the previous decade the DAC had moved from merely expressing the desire to soften terms and adapt them to recipient country situations to an integrated and credible system for promoting and assessing this. Its work had also allowed the unworkable one per cent target to be largely superseded by a new target relating to a clearly defined quantity – official development assistance – that its members could actually control.

Envoi

Institutionally, the decade-long process of setting objectives for aid volume and terms was both a collaboration and a tug-of-war between the DAC (representing the donors) and the UN (dominated by aid recipients). The first UNCTAD in 1964 and its recommendation on Growth and Aid gave impetus to existing DAC work to agree a Terms Recommendation. At UNCTAD II in 1968, the DAC lost the battle for net national income as the denominator in the one per cent target, but retained net flows, rather than net transfers, as the numerator. The pressure there for an aid target and for further softening of terms led directly to a revised Recommendation, which introduced the ODA concept almost by the back door. Yet only 18 months later ODA became the subject of an iconic UN target. The 1971 "defection" of a DAC official to UNCTAD then spurred the creation of the new LDC category, for which the DAC agreed special favourable terms in 1972.

Within the DAC, divergences of approach gradually became more pronounced over this period. The United States had initiated the group to promote more and softer aid, though by the early 70s its own financial position made it more difficult to take a leading role. Nordic countries were emerging as the champions of large aid programmes at soft terms. Other members naturally wished to appear

generous, but were wary of spending more than necessary, and keen to see that the measurement system presented their efforts in the best light.

The DAC's basic approach to improving aid terms was the same throughout: adopt the observed average of all DAC members as a minimum goal for each. At the beginning of the period, however, the tools were lacking to compare terms among disparate aid programmes. Technical progress from 1965 to 1972 then introduced three main innovations. First the grant element methodology facilitated numerical assessment of the softness of loans, taking account of all key aspects of their terms. Second, the DAC arrived at a precise and credible definition of official development assistance, including minimum terms for loans. Third, the new LDC category enabled preferential terms to be recommended for a defined group of countries most in need.

Conceptually, the 1972 settlement allowed a separation of two monitoring functions, with different instruments to address aid volume and aid terms. Volume would be assessed as net ODA flows, particularly in relation to the new UN target of 0.7% of gross national product. Terms would be assessed as the grant element of total ODA, and ODA to LDCs, against the targets set in the Terms Recommendation. Both had an influence on donor behaviour. The ODA volume target was met by several countries during the 70s, though progress later stalled and the largest donors tended to reduce rather than increase their ODA/GNI ratios over the long run. The Terms Recommendation was more successful, with almost all members meeting it within a few years (Japan was an exception until 2000). Yet perhaps because of its success, the Terms Recommendation largely dropped from view, and neither its role in softening terms nor its importance as the source of the ODA concept is widely known today.

The new political emphasis on volume, rather than terms, was reflected organisationally in the DAC Secretariat. The ad hoc Group on statistical problems became the main forum for discussing what could be reported as ODA, and it thus determined reported ODA volume. By 1971 it was no longer "ad hoc" and by 1973 it had become a full Working Party. Even by 1970 it was trespassing on the terms issues previously reserved to the Working Party on Financial Aspects, which entered a long decline before being abolished in 2003, although not before finally achieving a Recommendation on Untying in 2001.

The work in these two "subsidiary bodies" of the DAC, though subject to repetition, hesitation and deviation, was of a high standard intellectually, and several of the participants later reached top positions. The Swiss DAC delegate, Arthur Dunkel, would be Director-General of the GATT by 1980. The Australian delegate Philip Flood rose to be Director-General of his country's aid agency and then Secretary of its Department of Foreign Affairs and Trade, while the young Mr Jospin who appears now and then for France would be prime minister of his country a quarter of a century later.

The 1972 settlement was not the end of this story. The Terms Recommendation was revised one last time in 1978, raising the required grant element of total ODA to 86%. A new ODA volume target for LDCs was set by the UN in 1981. And the grant element test for ODA came under challenge in every subsequent decade, and was eventually changed in 2014. But the challenges arose mainly from changes in the international financial environment and do not detract from the achievement of 1972. The aid concepts, quantities and methods agreed then lasted for over 40 years, providing a stable basis for global discussions and assessments of aid volume and financial quality.

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