How international financial institutions and donors influence economic policies in developing countries

By Tiago Stichelmans • September 2016

A Eurodad discussion paper
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List of acronyms

CPIA Country Policy and Institutional Assessment
CPF Country Partnership Framework
CPR Country Performance Rating
CSO Civil society organisations
DAC Development Assistance Committee
DBR Doing Business report
DPL Development Policy Lending
DPO Development Policy Operations
DSF Debt Sustainability Framework
EC European Commission
ECDPM European Centre for Development Policy Management
EDF European Development Fund
EUMFA European Union Macro Financial Assistance
EUTF EU Trust Funds
FDI Foreign direct investment
FSA Financial Sector Assessments
FSAP Financial Sector Assessment Program
IBRD International Bank for Reconstruction and Development
IDA International Development Association
IEG Independent Evaluation Group
IEO Independent Evaluation Office
IFI International financial institutions
IMF International Monetary Fund
MoU Memorandum of Understanding
ODA Official Development Assistance
OECD Organisation for Economic Co-operation and Development
OP Operational Policy
PSI Policy Support Instrument
QPC Quantitative Performance Criteria
SCD Systematic Country Diagnostics
SSC South-South Cooperation
UN United Nations
Executive summary

This briefing analyses compliance with the ownership principle by the International Monetary Fund (IMF), the World Bank Group and the European Commission (EC). The ownership principle (see Introduction) is the idea that developing country governments – with the contribution of their parliaments, local authorities and civil society organisations (CSOs) – should define their own economic policies according to their development strategy. It also analyses the different channels through which international financial institutions (IFIs) and the EC influence economic policy-making in developing countries, impacting the ownership of their development strategies.

The list of channels analysed as part of this briefing is not exhaustive. It focuses on what Eurodad considers to be the most powerful channels of influence. The evidence presented is based exclusively on a review of the literature on this topic.

The following outlines the main characteristics of EU and IFI channels of influence on economic policy-making in developing countries, classified by institutions:

**World Bank conditionality**
- World Bank’s Development Policy Lending are loans or grants that are accompanied with conditions that take the form of prior actions, triggers and benchmarks.
- The Bank offers support in priority countries that have a positive assessment in terms of economic policies. Despite the Bank’s willingness to improve ownership, countries are consequently incentivised to adopt the World Bank’s preferred policies to receive funding.
- The current trend shows an increase of prior actions touching economic policies.

**World Bank research**
- The World Bank is one of the most important providers of research in development economics.
- Through its research activities, the Bank is in a position to justify its policy recommendations and the conditions attached to its loans. The World Bank’s researchers are influential among policy-makers themselves.
- The Bank’s research is often criticised – including by the last major external review – for their technical flaws and for being biased.
- Despite country-specific analysis, the Bank tends to advocate one-size-fits-all solutions.

**World Bank and IMF Financial Sector Assessment Program (FSAP)**
- FSAP is a joint IMF-World Bank programme analysing countries’ financial sectors to identify vulnerabilities that could trigger a crisis.
- Governments tend to implement the resulting recommendations with little debate.
- FSA assessments also have an important impact on the financial markets.
**IMF’s conditionality**

- IMF loans are in theory provided to countries facing balance of payment problems. They are accompanied by conditions that take the form of prior actions, quantitative performance criteria, indicative targets and structural benchmarks.
- In practice, it is very difficult for recipient countries to refuse the implementation of IMF’s policy prescriptions in the context of an IMF loan.
- Conditions increasingly touch sensitive economic policies (privatisations, economic deregulation, tax reform etc.). The number of such conditions per loan is also increasing.

**IMF surveillance**

- IMF surveillance activities, such as Article IV missions and reports, monitor the implementation of policies by the Fund’s members and encourage them to adopt certain economic policies.
- Surveillance activities are particularly influential in low-income countries and small emerging economies. They also receive a lot of media attention.

**IMF Technical Assistance**

- This is an IMF instrument that helps its members to design economic policies and manage their finances more effectively.
- The IMF reformed its Technical Assistance to give more space to local ownership. However, requests are prioritised through filters that favour countries with economic policies approved by the Fund.
- An independent evaluation of IMF’s Technical Assistance would be useful to assess how much local ownership is respected.

**IMF programmes and aid allocation**

- Bilateral and multilateral donors tend to favour countries with IMF programmes.
- IMF assessments are also used by donors to make aid allocation decisions, especially in low-income countries, where they often lack information on the country’s situation.
- Aid recipients have a great incentive to keep a good track record with the IMF to secure other funding sources.

**IMF programmes and Paris Club debt relief**

The Paris Club is an informal club of creditor governments meeting to provide debt relief on a case-by-case basis.

Among the eligibility criteria, there is the need to have a track record of implementing IMF-sponsored reforms. Additionally, countries need to have an IMF programme and no arrears with the Fund.

**European Commission Budget Support**

- The IMF and the World Bank have often been at the centre of criticisms made against conditionality policies. This briefing analyses EC Budget Support to compare its mechanisms with those of the IMF and the World Bank.
- EC Budget Support is a mechanism providing direct financial transfers to partner countries’ budgets. It accounts for approximately 25% of EU development aid.
- There are different eligibility criteria and different specific conditions for a programme or successive disbursements to be approved.
- Although EC Budget Support was designed to reinforce ownership, case studies show that EC Budget Support sometimes incentivises trade and economic liberalisation in recipient countries, even when those reforms are contradicting local development strategies.

**European Union Macro Financial Assistance (EUMFA)**

- EUMFA is a financial aid package that is provided to non-EU countries facing a balance of payments crisis.
- There are some general eligibility criteria and some specific conditions.
- Those conditions impose the adoption of specific economic policies with little consultation of local actors.
Introduction

This briefing analyses the implementation of the ownership principle by the International Monetary Fund (IMF), the World Bank Group and the European Commission (EC). In 2005, the Paris Declaration on Aid Effectiveness emphasised the need for more country ownership in the context of international aid. The Paris Declaration defines ownership as a situation in which “partner countries exercise effective leadership over their development policies and strategies and co-ordinate development actions”. The declaration also states that donors should “base their overall support on partners’ national development strategies” and “draw conditions from these strategies”.

The Paris Declaration’s definition of country ownership is narrow and is confined to a technical target measuring ownership based on partner countries having operational development strategies in place (Indicator 1). The conference on aid effectiveness held in Accra, Ghana in 2008 adopted an Agenda for Action that strengthens this principle. It notably acknowledges the critical role and responsibility of parliaments, local authorities and civil society organisations (CSOs) in ensuring ownership of development processes.

Some CSO groups welcomed the Accra Agenda for Action and notably how it enriches the country ownership principle. However, CSOs also pushed for a “rights-based democratic ownership” for the Busan Conference on Aid Effectiveness in 2011. The idea of democratic ownership puts people at the centre of aid and development effectiveness. This idea goes beyond what was agreed in Accra in the sense that it “centres the legitimacy of development priorities and processes on the rights of people to access democratic institutions [which] must fully engage all citizens [...] in processes for determining and implementing national development plans and actions.” However, the declaration adopted at the Busan conference did not bring any innovation to the ownership agenda.

Following this evolution in IFIs’ and donors’ commitments in favour of aid effectiveness, and also because of the failures of development and assistance programmes in the 1990s and early 2000s, the World Bank, the EC but also the IMF – which is not an aid agency – have revised their approach towards the design of aid or lending programmes to give more space to ownership.

Despite the fact that the IMF, the World Bank and the EC all signed the Paris Declaration and the Accra Agenda of Action, some CSOs, IFIs and donors have developed different visions of what ownership means. As a consequence, what is acceptable as a condition to aid allocation or lending programmes varies drastically between CSOs and IFIs/donors, as well as among IFIs/donors.

Conditions attached to aid and lending programmes can refer to the fiduciary management of the funds, the respect of international agreements protecting human, social and environmental rights or economic policy reforms – the latter commonly referred to as ‘economic policy conditionality’. Usually, CSOs do not question fiduciary conditions, when their objective is to make sure that development money is not used for other purposes. Also, they do not reject the respect for internationally agreed principles on the protection of human, social or environmental rights as conditions for the allocation and disbursement of loans or aid money. What some CSOs reject is the influence IFIs/donors have on economic policy reforms in developing countries, as it is the rights of the people living there to define development goals and the strategies to achieve them.

The first section of this briefing analyses how conditionality policies work and how they take account of the ownership principle. However, the ownership agenda has implications for broader issues than conditions attached to loans and grants to developing countries. International organisations have other means of influencing economic reforms. The second and third sections of this briefing will analyse different mechanisms through which the IMF, the World Bank and the EC influence the economic policy-making agenda of developing countries.
1. Conditionality policies

1.1 World Bank's conditionality

This section focuses on the conditionality policies and practices of the International Bank for Reconstruction and Development (IBRD) and the International Development Association (IDA), which are both part of the World Bank Group. The IBRD lends money to middle-income countries while the IDA offers grants or concessional loans to low-income and lower-middle income countries.

The World Bank’s main instruments for assistance to its clients’ countries are Development Policy Operations (DPOs) or Development Policy Lending (DPLs). A DPO can be a loan or a grant that provides financing “to help the borrower address the actual or anticipated development financing requirements.” DPOs take place through a programme with a policy and institutional focus that can target public finance management, the investment climate or the diversification of the economy to give a few examples.

According to the World Bank, DPOs emphasise country ownership, stakeholder consultation and donor coordination. The Operational Policy (OP) 8.60, which details the functioning of the Bank’s DPOs, states that the Bank makes its resources available if “the borrower (a) maintains an adequate macroeconomic framework, (b) implements its overall program in a manner satisfactory to the Bank, and (c) complies with the policy and institutional actions that are deemed critical for the implementation and expected results of the supported program.” Those criteria are determined in the context of the Country Partnership Framework (CPF).

CPFs are the basis of the World Bank’s country engagement. They are informed by Systematic Country Diagnostics (SCDs), which identify challenges and opportunities with regard to the Bank’s goals of eradicating poverty and increasing shared prosperity. SCDs are established using data and analytical methods, as well as drawing on consultations with different stakeholders. On the basis of SCDs, CPFs outline objectives to which the Bank can provide assistance through different interventions. In preparation for the CPF and SCD, the Bank consults with a variety of actors: government, private sector, civil society, development partners and other stakeholders in the country. The Bank considers this stakeholder engagement as a tool that aims to support local ownership.

If the Bank considers that a country respects the criteria determined through the CPF, it will then prepare a “Program Document”, which sets out the expected results of the country’s programme supported by the Bank. In the establishment of the programme, the Bank determines a set of policy and institutional actions that the recipient country has to undertake to make the programme successful. This is translated in the Program Document by “Prior Actions”, “Triggers” and “Benchmarks”. Prior actions are a set of policy and institutional actions that a country has to take before the Bank’s Board approves the programme. Triggers are the planned actions in the second or later year of a programme that will be the basis for establishing the prior actions for later operations. Benchmarks describe the content and results of the government’s programme in areas monitored by the Bank. Triggers and benchmarks are not legal conditions for disbursement and are therefore not considered by the World Bank as conditions.

Overall, the way DPOs/DPLs are planned and implemented challenge the principle of local and democratic ownership. The coordinators of a book on the role of the IMF and the World Bank in terms of policy reform summarise the issue: “on the one hand, DPL has the promotion of ownership as one of its key objectives. It envisages that the Bank would be involved in the consultation process on par with the other development stakeholders. On the other hand, however, the Bank will decide whether to support a country’s reform programme on the basis of the evaluation of the country’s macroeconomic, social and structural policies, its governance and its implementation capacity, taking into account the country’s track record (which is regarded as one of the more robust indicators of commitment). The possibility of a conflict with country ownership is abundantly clear, as ownership must be more than the freedom to accept the IFIs’ preferred policies.”

In 2005, the World Bank organised a review of its conditionality policy. This review showed that, although the number of conditions per operation was decreasing (from 35 in the late 1980s to about 12 in 2005), the number of benchmarks was increasing (from 15 to 24 for the same period). Based on the content of those conditions, the review highlighted a shift from short-term economic adjustments to medium-term institutional changes (in particular in public sector governance and social sector reforms). In terms of ownership, the review had two main messages:

1. The World Bank needs to address the practical challenges of assessing ownership and responding to changing policy environments.
2. The World Banks needs to balance predictability with performance in terms of flexible programmatic approaches.
Finally, the review suggests some good practice principles to improve the Bank’s conditionality policy:

- “Actively reinforce country ownership by relying on clear evidence of ownership informed by analytic work.”
- Agree up-front with the government and other financial partners on a coordinated accountability framework which includes both policy actions and outcome indicators.
- Customize the accountability framework used to evaluate country performance under the program and modalities of Bank support to country circumstances. Do not use the framework to leverage additional reforms outside the government’s agenda.
- Choose only actions critical for achieving results as conditions for disbursement.
- Conduct transparent progress reviews conducive to predictable and performance-based financial support.”

The World Bank reviews its use of Development Policy Lending every three years in a publication called Retrospective. The 2015 Development Policy Financing Retrospective provides some useful information regarding the evolution of the use of conditionality in the context of DPOs. Two lessons can be drawn from this:

- Overall, the number of prior actions is declining. It averaged eight per DPO in 2015, down from 10 per DPO in 2007. The decrease is more important for IDA clients – low-income and lower middle-income countries – than for IBRD clients (which are middle-income countries).
- While the share of prior actions on public sector governance and rule of laws has decreased, the share of prior actions touching economic policies has increased and now represents 22% of the total.

Box 1: World Bank’s operations in Liberia

Between 2008 and 2010, the World Bank funded a Development Policy Operation in Liberia called “Re-engagement and Reform Support Program”. Its third version had a focus on “improving land administration to reduce conflicts and enhance the investment climate”. This focus is explained by the fact that land disputes are considered to be the most important threat to Liberia’s post-war peace and because the Bank considers that Liberia could increase its gross domestic product (GDP) through the exploitation of the forest’s resources.

Among the conditionalities presented in the programme document, two are relevant for land administration issues:

- “Establish and adequately resource a Land Commission to identify, guide and facilitate reforms in land policy, law and program.”
- “Completion of assessment of the legal framework for a land (both statutory and customary law) to determine adequate amendment required to existing land laws.”

An Independent Evaluation Group (IEG) review of World Bank’s programmes in Liberia, however, finds that the Bank’s intervention did not generate any progress towards poverty reduction for populations living near forest concessions. “Little or no gains have accrued to the poor of the forest regions. Food insecurity around forest concessions is very high and few of the local residents are employed in commercial forestry.”

During the Bank’s interventions in Liberia, over 607,000 hectares were grabbed by palm oil and rubber giants. Some of these investors have been accused of displacing communities with little previous consultation and depriving them of resources and land.

According to the IEG, this result is explained by the Bank’s unbalanced focus on commercial goals in this sector. This focus encouraged the government to pursue an aggressive programme of forest concession. In addition, the Bank overlooked some of the government’s objectives such as capacity building and the promotion of added value in the sector. The focus on some of the government’s objectives poses the question of the ownership of the reforms as the authorities were advised to implement some reforms that espoused the Bank’s vision of agriculture.

Since the 1980s, the Bank has been pushing reforms in favour of an export-based agriculture, in which farmers are competing in global markets without state support. According to the Oakland Institute, “the institution continues to promote the notion that open markets for the private sector will bring growth and lead to better rural development than state-led programs. As a result, the Bank pressures governments to incentivize foreign direct investment (FDI), its silver bullet to replace public intervention in agriculture.”
1.2 IMF’s conditionality

IMF members may request IMF financial assistance if they have actual or potential balance of payments needs or lack sufficient financing on affordable terms to meet their international payments.

According to the IMF conditionality guidelines, countries borrowing from the IMF are responsible for selecting, designing and implementing the policies that will make the IMF-supported programme successful in resolving balance of payments problems. This is a way for the IMF to respect the country ownership of its programme.

When the IMF and client countries negotiate a loan, the programme is described in a letter of intent (which often has a memorandum of economic and financial policies attached to it). It describes the policy reforms that the recipient country intends to undertake during the programme. Disbursements can take place only upon its approval, or completion of reviews, by IMF’s Executive Board, which is dominated by donors’ countries – 14 of its 24 members are nationals from high-income countries, although some of them also represent developing countries through their constituency. Programme approval or reviews are based on various policy commitments agreed with the country authorities through the letter of intent. According to the IMF’s website, these can take different forms:

- “Prior actions are measures that a country agrees to take before the IMF’s Executive Board approves financing or completes a review [...]”
- “Indicative targets may be established in addition to QPCs as quantitative indicators to assess the member’s progress in meeting the objectives of a program [...]”
- “Structural benchmarks are – often non-quantifiable – reform measures that are viewed as critical to achieve program’s goals and are intended as markers to assess program implementation during a review [...]”

QPCs and Indicative targets do not prescribe policy changes. However, they may constrain the policy choices of governments – more specifically QPCs on budgetary and monetary issues, which are legally binding.

Prior actions and structural benchmarks contain most of the policy reforms agreed by the recipient country in the context of an IMF-supported programme. Although they are not legally binding, structural benchmarks are very influential as their implementation is frequently assessed by the Fund in the context of government performance reviews. A positive review is necessary for the release of a loan tranche. This is an example of how the power dynamics between the IMF and the recipient of its programmes make it very difficult for the latter to ignore policy prescriptions, even when they are not legally binding.

Box 2: World Bank’s IDA allocation matrix

For the World Bank’s International Development Association (IDA) – one of the largest sources of assistance for the world’s 77 poorest countries – concessional lending is decided through a formula that takes into consideration countries’ population, their Gross National Income (GNI) per capita and their Country Performance Rating (CPIR), which has more weight than the former elements. CPRs are established annually using the Country Policy and Institutional Assessment (CPIA). The CPIA is composed of four building blocks, each one of them weighing the same amount: Economic Management, Structural Policies, Policies for Social Inclusion, and Public Sector Management and Institutions.

Some of the indicators in the clusters are controversial. For instance, open trade regimes are given a higher score. Another example is the business regulatory environment, which uses the controversial Doing Business rankings (see below) among its indicators and rewards, for instance, high flexibility in firing decisions. On taxation, CPIA rewards problematic solutions such as a large use of sales/VAT and property taxes. Overall, the IDA allocation matrix matches the Bank’s conditionality policy in the sense that it rewards countries adopting policies that are judged favourably by the Bank.
Overall, the IMF claims that its recent reforms have changed the way it operates in relation to conditionalities. The Fund considers that only prior actions and QPCs should be considered as conditions and that they no longer contain sensitive economic structural reforms. However, the IMF has increased the number of sensitive economic reforms in its structural benchmarks. A 2014 Eurodad report finds that the number of policy conditions per loan has not declined. In addition, the report shows that those conditions are increasingly touching politically sensitive economic policy areas such as the privatisation of state-owned enterprises, the deregulation of the labour markets and tax reforms.

A recent article published by the Review of International Political Economy confirms this. The authors analysed 55,465 conditions in IMF loan agreements from 1984 to 2015 and found few changes in the IMF’s conditionality policy. Since 2008, the number of conditions per programme has increased. Regarding economic policy conditions, the study shows that, despite the IMF rhetoric, the decline in the scope of conditionality is limited. The majority of programmes still contain conditions related to state-owned enterprises (reforms or privatisations) or the business environment (legal systems, competition laws, business regulation, environmental policies and social protection issues). In addition, new borrowers have more conditions in these areas, which suggests that the decline for repeated borrowers could be explained by the fact that such reforms were already adopted through previous programmes.

In January 2009, the IMF signed a precautionary Stand-By Arrangement with El Salvador of US$ 800m. The following week, a left-wing government was elected in El Salvador where, according to the World Bank, 17% of the population lives on less than US$ 2 per day. The new government increased social spending that went from US$ 643 per capita in 2007 to US$ 753 per capita in 2012. This arrangement was signed to make money available "to stave off any adverse effects El Salvador could be facing in 2009 as a result of the global financial turmoil, the US recession and uncertainties related to the Salvadorian electoral cycle." The programme was endorsed by the two main candidates of the elections, who notably committed to keeping the public sector deficit to 2.8% of GDP in 2009. However, the financial crisis hit El Salvador harder than anticipated by the IMF and the deficit commitment was quickly broken. As a consequence, the following year, a new Stand-By Arrangement was signed between the IMF and El Salvadorian authorities.

Once again, the IMF predictions were inaccurate and the authorities could not honour the public deficit conditions imposed by the Fund. Concerned with the authorities’ reluctance to make cuts in social spending, the IMF used negotiations over a new loan to demand that all political parties agree to IMF-approved economic policies so that whoever won the 2014 elections would implement the IMF’s sponsored policies. This notably included a law, signed by the government without parliamentary debate, that foresaw the transfer of public services to public-private partnership (PPP) schemes. This case shows how the IMF’s programme conditions in a country facing a financial crisis can undermine local democratic processes, and the local ownership of reforms.

### Box 3: IMF’s programme in El Salvador

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1.3 European Commission Budget Support

According to the EC, its Budget Support – direct financial transfers to partner countries’ budgets – aims to foster partner countries’ ownership of development policies and reforms and to address the source of underdevelopment. In particular, it addresses five challenges:

1. Promotion of human rights and democratic values
2. Better financial management, macroeconomic stability, inclusive growth and less corruption and fraud
3. Sector reforms and sector service delivery
4. State building in fragile states and specific challenges in Small Island Development States (SIDS) and Overseas Countries and Territories (OCTs)
5. Better domestic resources mobilisation and less aid dependency.

This mechanism, which accounts for 25% of total EU development aid, is channelled through three facilities:

1. Good Governance and Development Contracts (GGDCs), which are used for objectives focused on good governance, government systems (public finance management and domestic resources mobilisation, for instance) and constraints to sustained and inclusive growth.
2. Sector Reform Contracts (SRCs), which focus on supporting sector policies and reforms or interlinked sectors.
3. State Building Contracts (SBCs), which support transition processes towards development and democratic governance in situations of fragility or transition. They focus on key state functions and the delivery of basic services to the population.

There are four criteria to be eligible:

1. “A well-defined national or sectorial development or reform policy and strategy
2. A stable macroeconomic framework
3. Good public financial management or a credible and relevant programme to improve it
4. Transparency and oversight of the budget (budget information must be made publicly available).”

The EC explains that the conditions are set to reinforce local ownership. When assessing a country’s eligibility, the EU’s delegation staff are supposed to take into consideration the context of the countries’ policies and cycles to give space to local ownership. One of the key factors for assessing the country’s macroeconomic framework is the relationship with the IMF and the country’s analysis provided by the Washington-based institution. In addition, programme approval and disbursements depend on meeting a set of conditions. If the EC considers that performance is insufficient, the disbursements are stopped until reassurances are given or measures are taken by the partner country. According to the EC guidelines, conditions are tailored to address the objectives and expected results.

The EC budget support is channelled using the recipient country’s allocation, procurement and accounting systems. The use of country systems makes them more likely to be aligned with the country’s development strategy and therefore more likely to respect local ownership, which was originally its stated objective. Over time, EC Budget Support has given more space for political conditions touching governance. This is particularly the case since the 2012 reform. However, there is a lack of clarity on how exactly countries’ assessments are undertaken and they seem to rely a lot on the views of delegation staff.

While it seems that EC Budget Support’s guidelines give ample space for local ownership, some cases show that the practice may be somewhat different. In an article published in the European Journal of International Relations, Mark Langan describes how EC Budget Support incentivises trade and economic liberalisation, whether part of recipient countries’ national strategies or not. Examining EU Budget Support to Tunisia, Ghana and Uganda in recent years, the author shows that disbursements have been linked to economic and trade liberalisation with regressive consequences for the poor of those countries. This is a contradiction of the stated objective of reinforcing local ownership.
1.4 European Macro-Financial Assistance to non-EU countries

Macro-Financial Assistance (MFA) is a form of financial aid provided by the EU to countries “geographically, economically and politically close to the EU” – and in particular EU candidates or potential candidate countries, or countries covered by the European Neighbourhood Policy, that are facing a balance of payments crisis. The purpose of an MFA is quite similar to IMF financing – which it complements – as its objective is to restore financial sustainability, while encouraging economic adjustments and structural reforms. Since 2014, the main beneficiary country of the MFA programme has been Ukraine, which received a total of €1.35bn. Other recent beneficiaries include Bosnia and Herzegovina, Jordan, Tunisia and Georgia.

MFA takes the form of medium- or long-term loans or grants. The EU does not have a fund to lend to the beneficiaries and borrow this money on capital markets. It lends the money to MFA beneficiaries with the same financial terms (interest rates, maturities, currency). The governance of this Fund is problematic with respect to the question of ownership. The ACP-EU Cotonou Agreement has governance based on co-management, notably for the EDF. With regard to the Trust Fund for Africa, while official documents state that national and local authorities will be consulted when it comes to establishing the priorities and projects, there is a lack of guidelines outlining how this will be done. According to research undertaken by the European Centre for Development Policy Management (ECDPM), there is so far “little evidence that ACP [African, Caribbean and Pacific] countries or institutions, let alone civil society, have been involved in designing this Trust Fund or will have a say on the allocation of EDF funds.”

In parallel to this governance issue, the ECDPM briefing shows that the establishment of the Trust Fund for Africa corresponds to a willingness from several EU member states to use aid money for their migration agenda. There is notably the possibility that the funds will be used for projects that aim to reinforce civilian security at the borders of target countries. In addition, the use of funds for countries that are important for migration routes do not necessarily correspond to their use where the development needs are higher. Overall, the establishment of the EU Trust Fund might give more weight to the European agenda on security and migration, undermining the partnership between EU and ACP countries.
The EU specifies some general ex ante conditions to be eligible for MFA financing and establishes specific conditions, which are enshrined in a Memorandum of Understanding (MoU) signed between the EU and the third country:

1. The first general condition is the respect of human rights and the presence of effective democratic mechanisms, including multi-party system and the rule of law.
2. The second is the existence of a non-precautionary credit arrangement with the IMF – an IMF programme with disbursements.
3. Finally, the third is the presence of a satisfactory track record of implementing IMF programmes reforms by the third country.

The EU establishes specific conditions after consulting the IMF, the World Bank and local authorities. They aim to strengthen macroeconomic and financial stability with a particular focus on public finance management, fiscal reform, trade, enterprise restructuring, business environment or financial sector reform. The successful implementation of those conditions is a requirement to receive the different tranches of the financing.48

In 2014, the EU and Tunisia signed an MoU for a loan of €300m to be disbursed over two years (2014-2015).49 Here is an overview of the conditions attached to this loan:

- Reform of the tax system to enhance tax collection
- Reform of the social safety net to compensate the energy price subsidies reform that was implemented as part of a previous IMF arrangement
- Strengthening of the independence of the central bank
- On trade, convert the existing system of industrial compulsory standards into a system aligned with that of the EU.

As we can see through the example of Tunisia, MFA financing influences economic policy-making in the beneficiary countries in a similar way as IMF programmes, which MFA financing is designed to reinforce. It must be noted that the content of EU consultation leading to the adoption of an MFA is not transparent. It seems that European authorities do not consult civil society actors and local parliaments, which is an obstacle to the local ownership of the reforms implemented in the context of MFA financing.

Financial flows from developing countries to other developing countries – also known as South-South Cooperation (SSC) – have increased over the past few decades. According to a report from the UN Secretary General, the share of SSC in total development cooperation increased from 6.7% in 2006 to 10% in 2011.50 The largest Southern contributors in financial flows are China, India, Saudi Arabia, Venezuela and Turkey. However, Brazil should also be mentioned for the importance of its technical assistance programmes.51

SSC has some features that differentiate its programmes from classic Organisation for Economic Co-operation and Development (OECD) Development Assistance Committee (DAC) donors. As non-members of the DAC, they are less restrained by its rules. This notably allows them to maintain aid institutions that lack transparency. India for instance tends not to publish its aid flows. Also, China does not publish its countries’ aid strategies.52 Non-participation in the OECD DAC allows emerging donors to pursue their national interests through SSC with more freedom than DAC members.53

Emerging donors also have the reputation of rarely using economic policy conditionality in their programmes. However, the lack of transparency of their development programme makes this claim difficult to assess. According to a UN Economic and Social Council (ECOSOC) report on SSC, emerging donors do not impose conditions on their programme, or align their programmes with IMF/World Bank prescriptions as DAC members often do.54

The absence of economic policy conditionality also has an impact on traditional donors’ conditionality practices. An empirical study analysed World Bank loans in 54 African countries between 1980 and 2013, and shows how Southern donors influence them. In particular, recipient countries assisted by China receive significantly fewer conditions attached to the loans they receive from the World Bank.55

Other types of conditions are nonetheless present in SSC. For instance, China tends to use its programmes to pursue political objectives (e.g. non-recognition of Taiwan) or commercial interests. India also attempts to gain support in multilateral institutions such as the UN from its recipient countries.56
2. Informal influence

In addition to financing activities, donors and international financial institutions can influence policymaking in developing countries and therefore undermine country ownership through their research, surveillance activities and technical assistance.

2.1 World Bank's research

The World Bank is one of the most important providers of research in development economics in the world. An independent evaluation analysing the Bank's activities in this domain from 1998 to 2005, undertaken at the request of the Bank in 2006, provides some interesting data. During that period, the Bank spent 2.5% of its total budget on research, drawing on the expertise of 93 researchers and 30 support staff in its research department. As a result of these capacities, the Bank is the most important producer and collator of data on development economics.57

This activity is explained by the twin goals of the Bank to eradicate poverty and boost shared prosperity. The aim of the Bank's research department is to "increase understanding of development policies and programs by providing intellectual leadership and analytical services to the Bank and the development community".58 In addition, recent years have seen the Bank repositioning itself to become "the knowledge bank", playing a more important role as a source of policy knowledge at the expense of financing activities. This shift has been one of the main goals of World Bank's president Jim Kim since his appointment in 2012.59

Regardless of the quality of World Bank research, which can sometimes be very valuable, this shift towards becoming a policy knowledge provider poses a few questions. First, the fact that the Bank is providing knowledge on development policies at the same time as being a lender for development policy support is problematic. This poses the question of complementarity between a development bank that provides both knowledge and conditions for its financing. This problem is summarised in a book focusing on the role of the IMF and the World Bank in policy reforms: "[...] the power to impose conditionality derives from the power over knowledge, that is, the power to decide what knowledge is and what is not."60

Second, and linked to the first issue, the Bank advocates a particular approach in its policy advice and research activities. The independent evaluation commissioned by the Bank shows that its research is often technically flawed while supporting strong policy positions. The technical flaws are actually attempts to find evidence of the Bank's policy lines. The evaluation says that this can be explained by the fact that researchers are "under pressure from the Bank presidency and elsewhere not to say things that go directly against the broad policy line that the Bank is espousing". This is the case in the integration for developing countries to the world economy and its implications in trade policies, for example, which are viewed by the Bank as an obvious and non-debatable strategy for development. The hiring of staff and its promotion also discourage any dissonant discourse in the Bank. This mechanism was characterised by Robert Wade, and later re-used by Robin Broad as "paradigm maintenance".64

Third, although the Bank has some tools for analysing countries' specific contexts – see above Systematic Country Diagnostic – it tends to advocate for 'one size fits all' solutions that are not tailored to countries' particular circumstances (see the example of the Doing Business report in Box 6).

The bias in favour of certain policy reforms in the World Bank's research would not be problematic if this research was not so influential. However, it wields a lot of influence. A Princeton University study evaluating World Bank research interviewed policy-makers from developing countries to assess the value they give to the Bank's research publications. It appears from these interviews that they give a lot of value to the Bank's research and often consult with their experts for technical advice. However, some of them pointed out that the policy conclusions of the research were not taking countries' circumstances sufficiently into consideration. According to the same study, this research – which is based on empirical 'evidence' – shows a link between poverty eradication, good institutional environment and openness to globalisation, and most notably trade liberalisation.65 This shows that developing countries' policy-makers tend to consider that the World Bank prescribes the adoption of a specific set of policies through its research publications.

The transformation of the World Bank into a knowledge bank at the expense of policy lending does not mean that its influence on economic policy-making will decrease and the objective of reinforcing local ownership should also be considered in this context.
2.2 IMF’s surveillance activities

Through its surveillance activities, the Fund can advise and influence policy-makers from its membership. The purpose of IMF surveillance activities is to monitor the implementation of policies that the institution judges crucial for the soundness of its members’ balance of payments. Surveillance activities are divided between bilateral surveillance – focusing on policy advice to member countries – and multilateral surveillance – which oversees regional dynamics or the world economy.

According to an evaluation made by the IMF’s Independent Evaluation Office (IEO), bilateral surveillance (e.g. Article IV) is more influential than multilateral surveillance (e.g. World Economic Outlook report), which is less frequently discussed by national policy-makers and to which the IMF dedicates fewer resources.72 Through its annual Article IV mission, the IMF exchanges with governments and central banks’ representatives. Other stakeholders (parliamentarians, representatives of business and labour organisations, CSOs) can also be consulted during the Article IV countries’ missions. At the end of the mission, the IMF staff present a report to its Board that then transmits its views to the member’s government.

The IEO report findings show that IMF members find the institution’s advice has marginal or no impact on their decisions. However, their survey shows differences among different groups of countries. In small emerging economies and low-income countries, the IMF advice is perceived as instrument to policy changes and is therefore highly influential. This is related to the fact that those countries are recurrent or potential IMF borrowers. This allows the IMF to advise countries to conduct certain reforms that are not included in the official conditions of a lending programme. 73

Another impact of the IMF surveillance is linked to market pressure. Considering the comprehensiveness and universality of information provided by the IMF, policy-makers believe that Article IV influences the decisions of market actors and are therefore incentivising prescribed reforms to increase the level of investments. However, it is debatable whether markets’ actors give much value to the information contained in Article IV reports. Nonetheless, the huge media coverage of these missions might influence local political debates and public opinion.

Box 6: Doing Business Report

Since 2002, the World Bank’s Doing Business report (DBR)66 has been ranking the business climates of 189 countries through 10 different indicators. Each indicator is built to assess the regulations applied to small- and medium-sized enterprises. Both the quality and the quantity of these regulations are assessed and ranked.

The DBR is designed under the assumption that there are ‘good’ and ‘bad’ policies and tends to promote deregulation as the best strategy for private sector development. At the same time, Doing Business does not assess important issues causing market failures. Geographic location, availability and cost of real estate, transport infrastructure, skilled workers and finance are key factors of a functioning market that are ignored by the report’s indicators.

Interviewed by the Wall Street Journal, one of the authors of the report claims that “for developing-country policy makers, focusing on rising in the Doing Business ranks could draw scarce resources away from more-substantive reforms that would help the government better administer and enforce business regulations”.67

Despite the controversies around its methodology, the DBR has a notable impact on policy-making, especially in the developing world. It is regularly used by donors, governments and academics in analysis and cross-country reporting and receives high-level media coverage. According to the World Bank, around 120,000 media articles have cited the Doing Business project since the first report in 2004.68

According to the IEG, 85% of policy-makers take into account the Doing Business rankings as a motivation for reform, although the majority of them do not consider those rankings as a guide of action.69 Nonetheless, the report would have influenced more than 525 policy reforms between 2003 and 2014, which represents 25% of regulatory reforms in favour in business recorded during that period.70 It has been used as the basis for reform programmes in developing countries such as Rwanda, Zambia and more recently India, where the government has set the improvement of the country’s ranking in the report as an objective of its reforms policies.71
2.3 IMF-World Bank Financial Sector Assessment Program (FSAP)

The FSAP is an initiative that aims to analyse countries’ financial sectors. It is undertaken by both the IMF and the World Bank in developing countries and emerging economies and by the IMF alone in advanced economies. There is also a division of labour between the two institutions on the content side. The IMF is responsible for financial stability assessments, through which it analyses the resilience of the financial sector, conducts stress tests, analyses systemic risks and analyses the financial sector regulations, among other activities. The overall goal is to identify vulnerabilities that could trigger financial crises. Financial Sector Assessments (FSA) are part of the IMF surveillance activities and are discussed by the Board together with the country’s Article IV report. Although FSAs are generally conducted at the request of members, they are a mandatory part of Article IV consultations in 29 jurisdictions that have a systemically important financial sector.

The World Bank is responsible for financial development assessments. These examine development needs and the quality of legal frameworks, as well as identifying obstacles to the competitiveness and efficiency of the financial sector and examining its contribution to economic growth and development with special attention on the development of domestic capital markets.

In 2014, the IMF review of the FSAP included a survey of members’ governments, which gave some interesting information on its impact, notably in terms of policymaking. It appears that governments tend to heavily implement or partially implement the FSA recommendations. At the same time, the survey shows that the FSAP does not promote a policy debate on the issues it covers. Finally, the market impact of the FSA assessments (e.g. through the release of documentation) is high, notably on the prices of bank’s stock (impact can either be positive or negative).

In 2005, the World Bank and the IMF developed the DSF with the objective of guiding countries, low-income countries in particular, and donors in mobilising finance needs while reducing the risk of debt crises in the future. Under the DSF, Debt Sustainability Analyses (DSAs) are regularly conducted and include several components:

- An analysis of the country’s debt burden project for the next 20 years
- An analysis of the risks of external debt distresses
- A set of recommendations for a borrowing strategy that limits the risks of debt distress.

This means that DSAs are used by the IMF to give policy advice. However, this policy advice is not the only influencing mechanism created by the DSF. They are also used by the IMF to determine access to financing as well as debt limits in IMF-supported programmes. In addition, the World Bank uses DSAs to determine the share of grants and loans in its assistance to low-income countries. Other donors also use DSAs to determine their lending policies. This is the case of the African Bank of Development, the Asian Development Bank, the Inter-American Development Bank and OECD donors.

The DSF is currently under review and a group of CSOs has developed a set of recommendations to improve the framework and notably to ensure it reinforces the Sustainable Development Goals.
2.4 IMF Technical Assistance

Technical Assistance is an IMF instrument that aims to help its members to design economic policies and manage their finances more effectively by strengthening their institutions and human capacities. The stated aims are achieving better economic outcomes and a more stable global economy. With lending and surveillance activities, technical assistance represents one of the three pillars of IMF’s activities.

It covers different areas:

- Monetary and financial policies
- Fiscal policies and management
- Macroeconomic statistical data compilation, management, dissemination and improvement
- Economic and financial legislation

Technical Assistance can take different forms: staff missions, trainings, seminars, workshops and online support. It accounts for 25% of the IMF’s operative budget. In 2013, around two-thirds of Technical Assistance was delivered in low-income and lower-middle income countries. That year, it focused mainly on fiscal issues, policies and management.

According to a 2005 Independent Evaluation Office (IEO) evaluation, Technical Assistance activities were driven in large part by the needs of IMF-supported programmes and Fund-wide initiatives rather than country-specific priorities. There was notably a very weak link between those activities and Poverty Reduction Strategy Papers – IMF-World Bank framework setting out a country’s macroeconomic, structural and social policies and programmes to promote growth and reduce poverty, as well as associated external financing needs.

Overall, it seemed that Technical Assistance did not have a proper strategy for local ownership. It was rather a means to improving the implementation of commitments made by the local authorities to the IMF. In this sense, Technical Assistance is a tool that aims to implement economic reforms agreed by the IMF and its programme members and therefore does have an influence over their economic policy-making. Technical Assistance is indeed usually requested during the negotiations of an IMF-supported programme or through IMF’s surveillance activities.

The IMF reformed its Technical Assistance guidelines in 2008, notably to give more space to local ownership, which is now seen as central to the provision of Technical Assistance. The identification of the Technical Assistance priorities now involves local authorities as well as the implementation and evaluation. However, Technical Assistance requests are prioritised through filters such as programme areas, policy initiatives, impact and commitment, availability of external financing and regional diversity. In addition, as a free service provided by the IMF, it can be argued that Technical Assistance can hardly be refused or reoriented by local authorities towards another sector.

A new evaluation of Technical Assistance by the IEO or by CSOs would be useful to provide a global picture of the implementation of its past recommendations and in particular recommendations to improve local ownership.

2.5 IMF programmes and aid allocation

In addition to its direct influence on developing countries’ economic policy-making – either through conditionality of informal mechanisms – the IMF influences the allocation of financing by other actors. This means that developing countries have an additional incentive to maintain a good reputation with the IMF and implement its policy recommendations.

A paper analysing the impact of IMF’s programmes on aid allocation highlights the correlation between IMF programmes and aid allocation by bilateral and multilateral donors. Using data for 136 recipient countries between 1986 and 2009, the study finds a correlation between IMF programmes and aid flows. The impact of IMF programmes is stronger in sectors linked to the IMF’s core competencies (debt and budget support) and less so for other areas. The impact of IMF programmes is also stronger on bilateral donors that have large voting shares in the IMF (e.g. United States, Japan) and weaker in others. As the biggest donors of ODA are influential members of the IMF (USA, Japan, Germany, UK, France...), low-income countries have an incentive to cooperate closely with the IMF to satisfy their bilateral donors.

This reality has been confirmed by an IMF paper analysing the impact of IMF supported programmes on donors’ allocation to low-income countries. It shows that donors, bilateral or multilateral, tend to favour countries with IMF programmes. In terms of budget support, this study shows that multilateral donors like the World Bank’s IDA and the EC give a higher proportion of aid to countries with IMF programmes. Overall, a survey conducted by the IMF in 2005 shows that 97% of donors use IMF assessments in their decision to assist low-income countries.
If we take the example of EC Budget Support, the EC assesses the stability of the macroeconomic framework of recipient countries using the analysis provided by the IMF. A good implementation of an IMF-supported programme (including PSI, see below) will be seen as a sign that the macroeconomic framework is stable or stabilising. In the absence of a programme, the EC uses Article IV reports. Another example is the EU’s Macro Financial Assistance, which is only available to countries that have signed a precautionary programme with the IMF.

The influence of IMF on other donors led to the recent creation of the IMF Policy Support Instrument (PSI). The IMF describes the PSI as a tool that “offers low-income countries that do not want – or need – Fund financial assistance a flexible tool that enables them to secure Fund advice and support without a borrowing arrangement. [...] The PSI helps countries design economic programs that deliver clear signals to donors, multilateral development banks, and markets of the Fund’s endorsement of the strength of a member’s policies.” Unlike traditional surveillance activities, PSI is an arrangement between a country and the IMF creating a framework that requires the country to meet expectations to receive the Fund’s approval. Conditional loans are also a signal to donors and official creditors, as a country has to respect precise standards to be eligible for IMF loans. PSI not only gives the signal that a country has sound policies from IMF’s perspective but also aims to provide donors with a guide for their allocation decisions and notably their terms, including the fund composition between grants and loans, and the volume.

This shows that aid recipients have a great incentive to sign deals and have a good track record with the IMF to secure other funding sources. In 2014, Ukraine signed a US$ 17bn Stand-By Arrangement with the IMF after months of political crisis and military tensions with Russia. This deal subsequently unlocked further credits from bilateral and multilateral donors of about US$ 15bn. The EU led a coordinating platform of international donors and organised a high-level meeting for this purpose in Brussels. However, it does sometimes happen that the IMF suspends its support to a country, which can provoke the suspension of financial support from the donors’ community. In April 2016, for example, after the discovery of a hidden debt of about US$ 1.4bn, the IMF decided to suspend its programme in Mozambique. An IMF official quoted by the Financial Times said: “Mozambique is close to a financial crisis if the authorities don’t take action to deal with the current risks” and warned that donors could freeze disbursements of about US$ 400m, potentially triggering a financial crisis. Following the IMF’s decision, a group of 14 donors including France, the United Kingdom, the EU and the African Bank of Development suspended their financial support to Mozambique.

2.6 IMF and Paris Club’s debt relief

The Paris Club, a voluntary, informal group of creditor governments, meets to provide debt relief to developing countries. Members of the Paris Club agree to renegotiate and/or reduce official debt owed to them on a case-by-case basis. Among its six principles defining how it works, the Paris Club defines some conditions for a country to be eligible for debt relief.

Those conditions notably imply that a country needs a track record of implementing reforms under IMF programmes. In practice, a country needs to have an ongoing programme supported by an IMF arrangement. The level of debt eligible for relief is defined by the financial gap identified by the IMF programme. In addition, the country needs to have no accumulated arrears and approval of the reviews of the IMF programme. This is another example of the influence the IMF holds over the donor community and this has significant consequences on the policy-making of developing countries.
Conclusion

This briefing analysed the implementation of the ownership principle by the IMF, the World Bank and the European Commission. The ownership of development strategies and policies by recipient countries has been recognised by the international community as a critical factor for aid effectiveness. As a consequence, we should carefully assess how these institutions influence economic policy-making in developing countries. This influence can take different forms: conditions attached to financing, research, surveillance and influence on donors’ aid allocation and debt relief decisions.

We must recognise recent efforts to reform conditionality policies by the IMF, the World Bank and the EC. However, there is a gap between the stated intentions and the reality. The IMF continues to attach problematic conditions to its loans, notably by suggesting reforms in sensitive economic areas. The World Bank continues to make loan decisions on the basis of the assessments made by its rich-country dominated board on the economic agenda of recipient countries. Finally, the EC’s Budget Support was originally created to support the local ownership of its recipients and its guidelines reflect that. In practice, it sometimes incentivises economic reforms that are not part of partner countries’ development strategies.

Conditionality policies have often been monitored by CSOs. However, multilateral and bilateral donors have other, more informal mechanisms through which they influence the economic policy-making of developing countries. The World Bank’s research department is very influential, particularly in some countries. This can be used to support the policy conditions attached to World Bank loans. In addition, despite the existence of tools to analyse each countries’ situation, World Bank research tends to make the same kind of policy recommendations in developing countries. The IMF’s surveillance activities and in particular Article IV’s reports also influence policy-making in the Fund’s membership and in particular in the poorest countries. The rich countries that dominate the IMF’s board influence these assessments. Finally, activities undertaken by the IMF’s Technical Assistance are driven by the economic thinking of the institution rather than by the priorities defined by its recipients.

In terms of influence on other donors’ decisions, the IMF is a critical actor. Empirical studies show that the aid allocation of important bilateral and multilateral donors is influenced by the existence of IMF programmes, or the countries’ assessments made by the Fund. The existence of an IMF programme is also an eligibility criteria for debt relief decisions taken by the Paris Club or financing provided by the European Macro Financial Assistance to non-EU countries.

This briefing highlights a significant gap between the commitments made by the EC, the IMF and the World Bank in favour of local ownership of development policies and their actual practices. The mechanisms to promote local ownership should therefore be reinforced in future to improve aid effectiveness.
Endnotes

2. Ibid.
10. Ibid. 7.
11. Ibid. 5.
17. Ibid. 15.
21. Ibid. 12.
30. Ibid. 29.
31. Ibid. 29.
32. Ibid. 29.
34. Ibid. 25.
35. Ibid. 29.
39. Ibid. 25.
47. For recent analysis on EU’s use of trust fund, see also K. Michaelowa, B. Reinsberg and C. Schneider (2016) Multi-bi aid in EU development policy: The role of capacity constraints and member state politics. Development Policy Review (forthcoming)
48. The ACP-EU Partnership Agreement, signed in Cotonou in 2000 is the framework for EU’s relations with 79 countries from Africa, the Caribbean and the Pacific (ACP).
52. Ibid. 44.
56. Ibid. 25.
57. Ibid. 29.
59. Ibid. 29.
61. Ibid. 29.
63. Ibid. 29.
65. Ibid. 29.
The European Network on Debt and Development (Eurodad) is a network of 47 civil society organisations (CSOs) from 20 European countries, which works for transformative yet specific changes to global and European policies, institutions, rules and structures to ensure a democratically controlled, environmentally sustainable financial and economic system that works to eradicate poverty and ensure human rights for all.

www.eurodad.org
Contact

Eurodad
Rue d’Edimbourg 18-26
1050 Brussels
Belgium
Tel: +32 (0) 2 894 4640

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