

PAPER DETAILS

TITLE: THE EFFECTS OF FOREIGN AID ON ECONOMIC DEVELOPMENT IN AFGHANISTAN
(2001-2015)

AUTHORS: MÜJGAN DENİZ,Zubeyr Ghulam HAIDAR

PAGES: 110-138

ORIGINAL PDF URL: <https://dergipark.org.tr/tr/download/article-file/841408>

THE EFFECTS OF FOREIGN AID ON ECONOMIC DEVELOPMENT IN AFGHANISTAN (2001-2015)

YABANCI KAYNAKLI YARDIMLARIN AFGANİSTAN'IN EKONOMİK GELİŞİMİ ÜZERİNDEKİ ETKİSİ (2001-2015)*

Müjgan DENİZ**
Zubeyr Ghulam HAIDAR***

Abstract

The aim of this study is to realize the issue of foreign aid disbursements as practiced in Afghanistan by using objective perspective to specify the effects of foreign aid on economic growth. This research study will recognize the impacts of foreign aid disbursements on economic development as affected by the political and strategic considerations and also by corruption levels which could have significance to future foreign aid programs in developing and post-conflict countries similar to Afghanistan. This research uses secondary data and both qualitative and quantitative methods which is conducted by collecting information from books and articles also collecting socio-economic statistics from reports and surveys to analyse the conditions in Afghanistan. The study examines both advantages and disadvantages of foreign aid on economic development using theory, as well as empirical analysis of transnational countries. The results indicate that foreign aid programs alone are not sufficient and efficacious for the economic growth of post-conflict states like Afghanistan. However, after two decades of foreign aid inflows to Afghanistan, the socio-economic conditions has not been improved, in order to make contribution to development process of poor countries, the potential advantages assists as providing resources to improve infrastructure, agriculture, education and transfer of technology. The GDP growth of Afghanistan has been declined, level of corruption has been increased, poverty rate has been risen and unemployment has been increased in this period. The intended conclusion is to provide recommendations to make foreign aid programs in Afghanistan useful and beneficial to its economic development.

Keywords: Afghanistan, Foreign Aid, Economic Growth, Accountability, International Financial Institutions, Economic Development

Jel Classification: O1, O19, I30

* This paper is derived from a master thesis written by Zhubair Ghulam Haidar and supervised by Müjgan Deniz.

** Corresponding Author. Istanbul University, Faculty of Economics, Department of Economics, Beyazıt-Fatih, İstanbul. E-mail: hacioglu@istanbul.edu.tr, Orcid: <http://orcid.org/0000-0002-3151-5838>

*** Istanbul University, Institute of Social Sciences, Department of Economics. E-mail: zubeyrkhan@live.com, Orcid: <https://orcid.org/0000-0003-3108-2443>.

Öz

Gelişmekte olan ülkelerde ekonomik büyümenin desteklenmesinde dış yardımın rolü ve yoksulluğun azaltılmasında etkinliği, kalkınma bağlamında yoğun bir tartışma konusu olmuştur. Çalışma kapsamında, geçiş ülkelerine yönelik yapılan gerek teorik ve gerekse de ampirik analizlerden istifade edilerek, ekonomik kalkınma için sağlanan dış kaynaklı desteğin avantaj ve dezavantajları irdelenmiştir. 2001-2015 yılları arasında sağlanan dış destek tutarına ve ekonomik büyümeye bağlı unsurların incelenmesi, hangi teorilerin Afganistan'a özel koşullara en uygun şekilde uyarlanabileceğine karar verilmesini sağlayacaktır. Sonuçlar, yabancı kaynaklı finansal desteklerin tüm olumlu etkilerinin kısa süreli olduğunu ve Afganistan gibi savaş geçirmiş fakir ülkelerin ekonomik kalkınmaları için yapılan dış yardımların yeterli ve etkin çözümler olmadığını göstermektedir. Ele alınan dönemde (2001-2015) Afganistan'ın GSYİH büyümesi azalmış, yolsuzluk seviyesi artmış, yoksulluk oranı yükselmiş ve işsizlik artmıştır. Bu bağlamda, çalışmanın nihai hedefi, Afganistan'a verilen dış kaynaklı desteklerin ülkenin ekonomik kalkınmasına daha etkin katkıda bulunmasını sağlayabilecek politikaları tavsiye etmektir.

Anahtar Kelimeler: Afganistan, Dış Yardım, Ekonomik Büyüme, Hesap Verebilirlik, Uluslararası Finansal Kurumlar, Ekonomik Kalkınma

JEL Sınıflandırması: O1, O19, I30

I. Introduction

This study analyses the cost and benefit of foreign aid on economic development in Afghanistan with a focus between the years (2001-2015). It is a fact that after the cold war era and invasion of Afghanistan by United States (US) lead coalition forces, the international community with the leadership of U.S has been trying to stabilise Afghanistan for the last two decades. Afghanistan after the crumble of Taliban rule in 2001 has been one of the biggest foreign aid recipient counties. It has been allotted over \$100 billion by the U.S. led international community concerning assistance to the reconstruction of Afghanistan and to fix its troubled economy. (Special Inspector General to Afghanistan Reconstruction, April 2018: 13) Despite a few progress in GDP per capita, life expectancy, poverty reduction, education and infrastructure, the ratio of improvements is relatively low by comparing it to the amount of aid given to Afghanistan. Contrary to expectations, this huge amount of aid flows to Afghanistan has been resulted in more dependency of state agencies on foreign aid. (Samim, 2016) However, the main concern to foreign aid reliance of a state is that when the foreign aid stops, the state faces economic and political instability.

As of 2010, the GDP of Afghanistan has been aid dependent at a ratio of 71%, and while around 51% of given aid has been spent on the stability operations and security sector. (Bjelica & Rutting, 2018) The country is still facing significant problems concerning security, stability, unemployment and corruption. Since the aid effectiveness in Afghanistan has been a national and international topic of debate lately, then there should be a critical look at aid ineffectiveness and recommendations for policy changes to make foreign aid programs more effective and beneficial Afghanistan thus provides a test case for analysis on the impact of foreign aid on promoting economic growth in emerging countries.

The study examines both advantages and disadvantages of foreign aid on economic development using theory, as well as empirical analysis of other transnational countries. Initially it will present the challenges of foreign aid ineffectiveness upon Afghanistan and an overview of the background and history of foreign aid to Afghanistan. As the list of research questions, assumptions, and definitions will be contained first and then it will present the limitations of this research study. In this context, the main research question is: *How has the foreign aid affected long-run economic development and political stability in Afghanistan?* Also, secondary research questions in this study are as follows;

1. How is the public perception of foreign aid in Afghanistan?
2. How are Technical Assistance and Afghanistan National Development Strategy affecting economics development in Afghanistan?
3. How is foreign aid affecting government expenditure of Afghanistan?
4. In the context of foreign aid, how is Official Development Assistance (ODA) impacting Afghanistan's economic development?
5. What are the international perceptions of foreign aid to Afghanistan?

It is the swiftly changing nature of its political history, that Afghanistan has an overwhelmingly unstable and volatile political economy, the role of foreign aid in supporting economic development and decreasing poverty might not be effective for every post-conflict state. Therefore, this study scrutinizes the responsibility and accountability of foreign aid disbursements and focuses on the socioeconomic costs related with foreign aid in Afghanistan. It aims to take a closer look at the results of the economic and political effects of foreign aid and will try to find an answer whether has there been any positive impact on the country's development in the real sense? The aim is to recommend a course of actions and policies to make foreign aid programs more effective on economic development and governance in Afghanistan.

This research study aims to determine how foreign aid is affecting economic development and political stability in Afghanistan. The aim is to understand the issue of foreign aid disbursements as practised in Afghanistan and approach it from a neutral perspective to specify the effects of foreign aid on economic development. This study will recognise the effects of foreign aid disbursements on economic development as affected by the political and strategic considerations and also by corruption levels and could be of significance to future foreign aid programs in developing and post-conflict countries similar to Afghanistan. The intended conclusion is to provide recommendations to make foreign aid programs in Afghanistan useful and beneficial to economic development

This study assumes that the international community, particularly the western nations, the United States and its allies will continue to engage in global efforts to provide foreign aid for weak economies. It also assumes that foreign aid programs are not efficient. However, to serve as a benefit for developing countries, the potential benefits serve as providing resources to improve infrastructure, agriculture, education and transfer of technology. The intended conclusion is to provide recommendations to make foreign aid programs useful and beneficial to economic

development in post-conflict countries. Afghanistan thus provides a test case for analysis on the impact of foreign aid on promoting economic growth in developing countries.

2. Literature Review

Initially the aim is to evaluate and analyse the contemporary or existing literature relevant to this study and find similarities and gaps. In order to understand the effects of foreign aid on economic development in Afghanistan, first, we have to have a better understanding of what is foreign aid. This study firstly will address literature in four areas; definition and a brief history of foreign aid, economic and political theories of foreign aid, then foreign aid and growth relationship and finally empirical literature on the effects of foreign aid on long-run economic development and political stability in developing countries. Examination of factors associated with economic growth and foreign aid amounts from 2001 to 2015 determine which theories best apply to conditions in Afghanistan. This study will help to identify problems between donor and recipient countries, also improving aid effectiveness. This study also identifies the empirical evidence on foreign aid and economic growth relationship.

2.1. Defining Foreign Aid

Foreign aid is the voluntary transfer of resources from one country to another. This transfer includes any flow of capital to developing countries. (Intelligent Economist, 2018) There are several definitions of aid in literature. According to Hans Morgenthau (1962: 301), "Foreign aid is one of the real innovations which the modern time has introduced into the practice of foreign policy". Morgenthau refers to six distinct types of foreign aid, "Humanitarian foreign aid, foreign military aid, subsistence foreign aid, bribery, prestige foreign aid and foreign aid for economic development." He also states that out of these six types only foreign humanitarian aid is provided for non-political purposes. However, it can be used as a political purpose if it operates under a political context. Since foreign aid has often been linked to the interest of donor and recipient countries, like a state's foreign policy, it is not easy to understand.

The word aid generally refers to the flow of technical and financial resources from developed countries to the developing countries. Lancaster defined foreign aid as the voluntary transfer of resources from one independent country to another independent country, a Non-Governmental Organisation (NGO), or international organisations, aimed at achieving better human conditions in the aid recipient country. (Lancaster, 2008: 9)

Foreign aid is termed as Official Development Aid (ODA) by Organization for Economic Cooperation and Development (OECD). A valid origin for definition, data and information of foreign aid is the Development Assistance Committee (DAC) of OECD. The primary goal of ODA is to promote economic development and welfare for the aid recipient countries. OECD explains ODA as: "Flows of official financing administered with the promotion of the

economic development and welfare of developing countries as the main objective, and which are concessional in character with a grant element of at least 25 percent (using a fixed 10 percent rate of discount)”(OECD, 2018). The modern concept of foreign aid dates back to 1950s during the cold war and when the competition between the Soviet Union or communism and the U.S. or capitalist west intensified. Walt Rostow an American economist and political theorist were one of the people who suggested the idea of providing foreign aid for long-run development. (Lancaster, 2008: 66)

2.2. Framing Foreign Aid

Foreign aid has always been a controversial topic of debate. A complete frame of literature exists in the subject of foreign aid and economic growth with different viewpoints and mixed empirical results. (Islam, 1992) However, according to Anisul evaluation of these different viewpoints represent that, there are mainly two distinct views, the traditional pro-aid view and the radical anti-aid view.

Economists like William Easterly, Peter Bauer and Milton Friedman have strongly opposed foreign aid policy. Critics of foreign aid argue that foreign aid has always been used as a political tool which resulted in corruption, patronage and more wealth and power of only dictators or elite groups in low-income countries. Some argue that foreign aid has negligible effects on economic growth and frequently has done more negative than positive impact on the world's poor. They point to African and South Asian countries where despite five decades of foreign aid still most people live under poverty line and they have a terrible record of growth, such as Haiti, Papua New Guinea, and Sudan. (Radelet, 2006) These would be helpful for having insights into the negative or neglected impact of foreign aid on economic growth.

Friedman stated that foreign aid did more harm than benefit by helping and strengthening only the central governments. (Boone, 1996: 289) Bauer inspired by Friedman argued that every country has started as an emerging country at first, and if the vicious circle of poverty theory were accurate, then there would be no developed countries today. According to Bauer, the key to success in development was private profit, not the government control. He stated that Foreign aid has politicised economies, with handing the monetary assistance to the governments instead of handing it to profitable businesses. Thus, aid increased patronage and enriched only elite groups in the recipient countries. (Boone, 1996)

Not all transfers from rich countries to emerging countries are considered as foreign aid. According to DAC, in order to be counted as foreign aid, the aid should meet two criteria; 1 – its main objective should be to promote economic development and welfare (excluding military aid or other aids given for no developmental purposes). 2 – it must be provided in grant or subsidised loan. The ODA can also be in the forms of technical assistance like capacity development or policy advice. It can also be in the form of bilateral agreement among two states, and through multilateral institutions. (OECD, 2018) These several definitions of foreign aid have a common

point which is the flow of resources from one place to another. Defining foreign aid is vital for the considerations of public opinion and the effects on the public because the public often has a different understanding and perspective of the aid word.

2.3. Historical Background of Foreign Aid to Afghanistan

Afghanistan's foreign aid reliance is not a new topic on the agenda. Throughout the history of Afghanistan, external assistance has performed an essential function in development process, even before the conflict era. Afghanistan throughout its history has mostly financed its expenditures from foreigners. This finance strategy was pioneered by Ahmad Shah Durrani "*the founding father of the modern state of Afghanistan*" when he conquered India: "*meet the dynasty's needs by extracting revenue from a foreigner*". (Barfield, 2010: 205) Since then Afghanistan has mainly been a "*rentier state*", whose revenues were primarily from flows of foreign aid. The first monetary assistance of Afghanistan dates back to the year 1857 when Dost Mohammad king of Afghanistan signed a treaty with the British Empire against Persian threat during the British rule in India. (Barfield, 2010: 128) Since Afghanistan's economic history with a limited amount of data to rely on is often linked to its political history throughout the 20th century, and it is the swiftly changing nature of its political history, that Afghanistan has an overwhelmingly unstable and volatile political economy, Therefore Afghanistan's economy has always been reliant on foreign aid. (Rubin, 2000)

The modern concept of financial aid traces back to 1945 with the establishment of the United Nations, the World Bank and International Monetary Fund. Regarding total amount of dollars given as aid, the U.S has been the largest donor followed by France, Germany, UK, Japan and others. (Perkins, Radelet, Lindauer & Block, 2006) However, regarding aid given to the ratio of income Sweden, Norway, Luxemburg, Denmark, and the Netherlands are top generous donors respectively. Official Development Aid (ODA) has been increased at a moderate level from the 1960s until its peak after the cold war in 1991. Then there was a decrease in the nominal level of aid for the following decade. However, with the beginning of the 21st century, the aid flows have been increasing again with the commitments of rich countries to assist generally all developing countries particularly assistance to Iraq and Afghanistan. (Perkins, Radelet, Lindauer & Block, 2006)

The process of modernisation continued at a moderate pace till the mid-1950s. which was then accelerated by king Zahir Shah, these further attempts also included industrialisation and the spread of education. In 1953 when Daoud Khan became prime minister, he also accelerated the tempo of economic development in the country. (Cullather, 2002) After 1950s the economy of Afghanistan was closely associated with the cold war. During the 1950s and 1970s Afghanistan received military and economic assistance from both Soviet Union and the U.S., which was often nicknamed as "Economic Korea". Although there have been controversial claims on amount foreign aid to Afghanistan, according to the Ministry of Finance of Afghanistan (MoF) from

2002 to 2013, the international community has delivered around \$60 billion out of \$90 billion committed aid to Afghanistan. (MoF of Afghanistan, 2011)

Although more than sixty countries supported the reconstruction of Afghanistan, the U.S. has been on the top of the list in aid given to Afghanistan. The U.S. has appropriated \$122 billion on security and stability operations in Afghanistan since 2002. (SIGAR, 2018: 13) Despite increasing signs of ineffective spending of the existing funds, foreign aid flows continued to increase until 2010. The U.S. appropriated foreign aid was at its peak of \$17 billion in 2010, after that foreign aid has started to decline each year respectively. International funding also increased in the same period, in 2009 Official Development Assistance was amounted to around \$6 billion. (SIGAR, 2018: 14-5)

Regarding total amount of dollars given as aid, the U.S has been the largest donor followed by France, Germany, UK, Japan and others. However, regarding aid given to the ratio of income Sweden, Norway, Luxemburg, Denmark, and the Netherlands are top generous donors respectively. Official Development Aid (ODA) has been increased at a moderate level from the 1960s until its peak after the cold war in 1991. Then there was a decrease in the nominal level of aid for the following decade. However, with the beginning of the 21st century, the aid flows have been increasing again with the commitments of rich countries to assist developing countries particularly assistance to Iraq and Afghanistan. (SIGAR, 2018)

After U.S. led invasion of Afghanistan in 2001, Afghanistan has received large amounts of foreign aid for political stability, economic growth and improving socio-economic conditions. However, general conditions throughout the country has not been improved. Despite all of the efforts and vast amounts of aid inflows to Afghanistan, Afghanistan is still among Least Developed Countries (LDC) with the majority of its population suffering from poverty. Most of the aid money has been spent outside of government system rather than focusing on the priority needs of the public, thus making Afghanistan more reliant on foreign aid. Therefore, the theories suggesting foreign aid has beneficial effects on economic development requires to be examined and correlated to the situation of Afghanistan. In fact, Afghanistan throughout its history has mostly financed its expenditures from foreigners and financial assistance of international institutions. Finally since 2001, invasion of Afghanistan by US lead coalition forces, Afghanistan has become an engaging country in the international community's agenda for support and assistance.

2.4. Basic Intentions of The Donor Governments For Allocating Financial Aid Reimbursements

Initially, the donor government provides financial aid to friendly states for political, military or economic objectives. Also, much of the bilateral aid is being tied to purchase from donor government, which many of these incentives have nothing or little to do with growth and development. Even if the intended aid is targeted for development purposes, the donor government can have wrong or strange ideas for spending it. They may decide to spend development projects

on their own companies and contractors operating abroad, which money will turn back to home country. The role of bribes, lobbying and campaign contribution in donor countries that influence the foreign aid decisions explains much of this. (SIGAR, 2018: 15) Suppose that this aid is intended for actual development purposes by bilateral or multilateral agencies. These agencies and institutions have their plans and constraints on how to spend the provided aid.

Even if the intended aid is targeted for development purposes, the donor government can have wrong or strange ideas for spending it. They may decide to spend development projects on their own companies and contractors operating abroad, which money will turn back to home country. The role of bribes, lobbying and campaign contribution in donor countries that influence the foreign aid decisions explains much of this. Easterly further states that foreign aid is given as loan or grant to developing countries for development purposes, often and in many instances have been stolen by officials receiving it as their basic instinct. The aid money gets wasted or consumed by developing countries leaders, ministers, officials or other bureaucrats who all want a share.

As the donor countries want to provide aid for national priorities, the recipient government also want to spend it on projects which are harder to monitor and more accessible to steal. This problem is severe in foreign loans particularly given by IMF and WB, and the consequences could be dramatic. Because these wasted loans by government officials have to be repaid by the citizens, which often results in not repaying and criticism of the donor country or agency itself for providing aid. Western and developing governments both have troubles in spending money efficiently. The lessons learned from development economics lately is that *there has been massive corruption, fraud, waste and misallocation of resources at all stages*. This problem may undermine the development process in receipt country, because of undermining the political and institutional processes. Foreign aid might undermine the underlying contract between the state and its citizens by interrupting the connection between state resources and its ability to tax. These adverse impacts of foreign aid might prevail to its beneficial impacts.

2.5. Public Perceptions, Surveys and Government Reports

The Brookings institution provides Afghanistan Index. (Livingston & O'Hanlon, 2015) The index provides updated and historical information on different statistics such as unemployment and infrastructure. It also provides quantitative measures and indicators for Afghanistan's economic and quality of life, governance and the rule of law, security and public opinion. Besides, the Asian Development Bank provides A Survey of the Afghan People. Their 2015 survey polled around 9500 citizens and provides public opinion on a wide range of issues related to growth and development of Afghanistan. (Hopkins & Warren, 2015) These will provide measurable sources on the effect of foreign aid on development outcomes also public opinion and national mood in Afghanistan.

Integrity Watch Afghanistan's research focuses on policy-oriented research evaluating progression, perception and exposure to corruption and corruption related issues including budget and public

finance management, security and aid effectiveness at the national level. (Torabi & Delesgues, 2008) The report is based on a survey of over 1000 individuals in Afghanistan. This will provide measurable sources to determine the level of perception and readiness of Afghanistan people towards ownership and accountability in foreign aid.

Special Inspector General to Afghanistan Reconstruction investigates all financial transactions to Afghanistan. Their report examines the U.S. government support for the private sector and economic development in Afghanistan since 2001. (SIGAR, 2018) This reports provide the basis for examination of U.S development assistance to Afghanistan. The Afghanistan National Development Strategy (ANDS) was the first paper strategy in the reduction of poverty in Afghanistan. (Shah & Garner, 2009) It was based on Millennium Development Goals (MDGs) and was organised in three sectors of (1) security, (2) governance and the rule of law, (3) social and economic development. The core findings from the reports of ANDS during the five year implementation period (2008-2013) will provide measurable sources relative to expected outcomes.

The Central Statistic Organization of Afghanistan provides the Afghanistan Living Conditions Survey (ALCS), which is a valuable source of information about the socioeconomic conditions in Afghanistan. (CSO, 2017) The survey provided information at national and provincial levels and covered around 19000 households and 150000 individuals with continuous data collection method during a cycle of 12 months. This provides measures for socioeconomic indicators (poverty and employment) and development indicators (education, health and water).

3. Research Design

The theories suggesting foreign aid has a positive impact on economic development need considered and compared to the case of Afghanistan. By applying appropriate empirical models will determine the impact of foreign aid on the economy of Afghanistan. These theories and models will determine if the donors' actions in Afghanistan are convenient and if the money provided in aid is having the desired effects.

In this study, combinations of qualitative and quantitative approaches by using secondary data are considered. The research analysis will focus on case studies, empirical research, survey responses, and data analysis of foreign aid relative to economic growth indicators, particularly gross domestic product (GDP) levels. The findings will specify which theoretical works or empirical analysis best apply for the testing of foreign aid effectiveness on economic development in Afghanistan. The primary focus of this paper will be transnational scholarly studies which closely relate to the situations in Afghanistan. The survey responses will confirm the data and technical evaluations. Major significant reports such as *the reports of Brookings Institution, Integrity Watch Afghanistan, Special Inspector General to Afghanistan Reconstruction, A Survey of the Afghan people, and Afghanistan Living Conditions Survey* will provide quantifiable sources for actual effects of foreign

aid on economic development in Afghanistan by population. These reports provide the bases for the hypothesised effects of foreign aid on the economic development of Afghanistan in this study.

The hypotheses for each of the secondary questions in this study are below:

1. Afghanistan perceive foreign aid as a moral duty of the international community, and that the public and government of Afghanistan have no reason to be active subjects of aid.
2. Technical Assistance and Afghanistan National Development Strategy have worked and positively contributed to economic development.
3. Foreign aid has expanded government expenditure.
4. Official Development Assistance has positively affected economic development in Afghanistan.
5. The international community and the U.S. perceive Afghanistan as weak and rentier state.
6. Foreign aid has a positive effect on long-run and sustainable economic development in Afghanistan. (Deniz & Haidar, 2018: 7)

World Bank and IMF provide annual data for macroeconomic indicators of Afghanistan. Also, the Organization for Economic Co-operation and Development provides data on the volume, origin and types of official development assistance (ODA) flow from donor to recipient countries. (OECD, 2018) Reports and detailed data provided by organisations mentioned above will provide a quantitative measure for GDP growth, GDP per capita growth, inflation, foreign aid and net ODA inflows to Afghanistan.

The empirical studies of foreign aid by Ekanayake and Chatrna (2010: 1), Rajan and Subramanian (2008), Bräutigam and Knack (2004), and Boone (1996) all indicate that foreign aid has no significant impact on growth and might have negative impacts on growth and development of developing countries. These studies indicate that foreign aid increases consumption rather than investment, reduces domestic saving and tax share. They also indicate that aid does not support growth nor it helps the poor. These studies also indicate that foreign aid contributes to weak governance and inefficiency. On the other hand the empirical studies of Hansen and Tarp (2001), Chenery and Strout (1966) Indicate that foreign aid support growth through investment. Empirical studies of Burnside and Dollar (2000), Durberry, Gemmell, and Greenaway (1998) Indicate that foreign aid has positive effects on growth conditional on the quality of institutions and stable macroeconomic policy environment. These studies provide correlations to the levels of foreign aid to GDP, Investment and other factors that exist or may develop in Afghanistan. These studies also provide possible indirect ways to make aid more effective through policy implications.

Alesina and Weder's study examined the relationship between foreign aid and domestic corruption. (Alesina & Weder, 2002) This study indicates that corrupt governments receive more foreign aid, and U.S. foreign aid is directed to the more corrupt government. This study also

indicates that foreign aid flows are not directed toward good governance. Svensson's (1999) study addresses the relationship between foreign aid and rent-seeking activities. His study offers that foreign aid increases corruption and other rent-seeking activities in countries suffering from divided policy control. This will serve as a reference for foreign aid increasing corruption. Table 1 summarises the sources and variable factors used in the analysis.

Table 1: Sources and Variable Factors

Source	Variable Factor
Integrity Watch Afghanistan, A Survey of Afghan People	Afghanistan's public perception
Brookings Institute, SIGAR, ALCS Survey	Afghanistan's index, economic and social indicators
World Bank and IMF	Macroeconomic indicators
OECD	Foreign aid and ODA flows
Burnside, Dollar, Brautigam, Knack Hansen, Tarp, Chenery, Strout, Durbarry, Gemmell, Greenaway, Ekanayake, Chatrna, and Rajan	Correlations of foreign aid and economic growth
Morgenthau	Realist perspective of the political theory of foreign aid
Friedman, Bauer and Easterly	Costs of foreign aid
Stiglitz, Stern and Sachs	Benefits of foreign aid

3.1. Aid and Economic Growth Relationship

Foreign aid has always been a controversial topic of debate. Aid has been an important topic of debate because of its role in the growth process of developing countries. A complete frame of literature exists in the subject of foreign aid and economic growth with different viewpoints and mixed empirical results. (Islam, 1992) However, according to Islam (1992) evaluation of these different viewpoints represent that there are mainly two distinct views, the traditional pro-aid view and the radical anti-aid view.

The research is conducted by collecting information from books and articles also collecting socio-economic statistics from reports and surveys to analyse the conditions in Afghanistan. Examination of factors associated with economic growth and foreign aid amounts from 2001 to 2015 determine which theories best apply to conditions in Afghanistan. Numerous empirical studies have been applied econometric analysis to study aid and economic growth connection in many ways. However, we can categories these results in three different viewpoints.

The empirical studies of foreign aid by Ekanayake and Chatrna (Eknayake & Chatrna, 2010), Rajan and Subramanian (Rajan & Subramanian, 2008), Brautigam and Knack (2004), and Boone (1996) all indicate that foreign aid has no significant impact on growth and might have negative impacts on growth and development of developing countries. These studies indicate that foreign aid increases consumption rather than investment, reduces domestic saving and tax share. They also indicate that aid does not support growth nor it helps the poor. These studies also indicate

that foreign aid contributes to weak governance and inefficiency. On the other hand the empirical studies of Hansen and Tarp, Chenery and Strout (1966) indicate that foreign aid support growth through investment. Empirical studies of Burnside and Dollar (2000), Durberry, Gemmell, and Greenaway (1998) indicate that foreign aid has positive effects on growth conditional on the quality of institutions and stable macroeconomic policy environment. These studies provide correlations to the levels of foreign aid to GDP, Investment and other factors that exist or may develop in Afghanistan.

3.1.1. The Positive Relations Between Aid and Economic Growth

Supporters of foreign aid argue that foreign aid has played a significant role in the process of economic growth and development in developing countries over the past five decades. Economists like Jeffrey Sachs, Nicholas Stern and Joseph Stiglitz state that, foreign aid may not work sound all the time and everywhere, but in general terms, it has positive impacts. (Radelet, 2006) Foreign aid supporters claim that aid has played a critical role in reducing poverty, accelerating economic growth and improving education in many developing countries, by giving an example of some prosperous foreign aid recipient countries such as South Korea, Indonesia and Taiwan. (Radelet, 2006) These claims reinforce common themes regarding the positive relationship between foreign aid and economic growth.

First, the classic view was that foreign capital or foreign aid increases saving, finances investment and promotes growth. In this view, the emerging countries were unable to close the large gap among saving and investment in order to achieve sustainable growth and emerging countries might be stuck in a poverty trap. Second, foreign aid could boost labor productivity via investments in human capital, education and health. Thirdly, foreign aid might promote growth by transferring technology and knowledge.

Therefore, supporters of foreign aid argue that foreign aid has played a significant role in the process of economic growth and development in developing countries over the past five decades. Economists like Jeffrey Sachs, Nicholas Stern and Joseph Stiglitz state that, foreign aid may not work sound all the time and everywhere, but in general terms, it has positive impacts. Foreign aid supporters claim that aid has played a critical role in reducing poverty, accelerating economic growth and improving education in many developing countries, by giving an example of some prosperous foreign aid recipient countries such as South Korea, Indonesia and Taiwan. (Radelet, 2006) These claims reinforce common themes regarding the positive relationship between foreign aid and economic growth.

Hans Morgenthau from a realist lens links foreign aid to foreign policy and political interest of donor. He argues that foreign aid for economic development purposes would fail if the goal of the donor nation is the political stability in the recipient country. Because successful foreign aid for economic development purposes will change the political and economic status quo of the existing ruling groups in emerging countries. However, foreign aid in the form of military aid, prestige

aid or bribe aid strengthens the political status quo of the ruling groups, which are deleterious to economic development. He also argues that foreign aid because of its political nature is not a science but an art. (Morgenthau, 1962) This theory is applicable in Afghanistan because most of the foreign aid to Afghanistan from the U.S. has been in the form of military and bribe for political stability.

3.1.2. The Negative Relation Between Aid and Economic Growth

Economists like William Easterly, Peter Bauer and Milton Friedman have strongly opposed foreign aid policy. Critics of foreign aid argue that foreign aid has always been used as a political tool which resulted in corruption, patronage and more wealth and power of only dictators or elite groups in low-income countries. Some argue that foreign aid has negligible effects on economic growth and frequently has done more negative than positive impact on the world's poor. They point to African and South Asian countries where despite five decades of foreign aid still most people live under poverty line and they have a terrible record of growth, such as Haiti, Papua New Guinea, and Sudan. (Radelet, 2006) These would be helpful for having insights into the negative or neglected impact of foreign aid on economic growth.

First, aid might encourage corruption, and much of aid would be lost to graft. Second, it would keep bad governments in power which will result in bad policies and postpone reforms. Third, foreign aid flows might reduce incentives for investment and decrease domestic saving in private and likewise in public via its effect on interest rate and inflation. Fourth, foreign aid can cause a considerable rise in the values of a country's currency known as Dutch disease.

Friedman stated that foreign aid did more harm than benefit by helping and strengthening only the central governments. Bauer inspired by Friedman argued that every country has started as an emerging country at first, and if the vicious circle of poverty theory were accurate, then there would be no developed countries today. According to Bauer, the key to success in development was private profit, not the government control. He stated that Foreign aid has politicised economies, with handing the monetary assistance to the governments instead of handing it to profitable businesses. Thus, aid increased patronage and enriched only elite groups in the recipient countries. (Boone, 1996)

In this respect, Joseph E. Stiglitz (1996) refers to the East Asian miracle. He argues that the miracle of East Asian countries showed that the factors which led to the remarkable development of these countries are much more than macroeconomic stability or privatisation. The governments played a crucial role in providing a stable financial system, and without a stable financial system, the impacts of privatisation and free trade will turn to rent-seeking instead of wealth creation if the market is not competitive. Free competition or "Laissez-Faire" economics is a crucial principle of free market capitalism, which opposes any government intervention in economics. However, since markets are not fair, the government must engage in economics. The Stiglitz suggestion of government role in providing good environment justifies government engagement in economic

activities if the markets are not fair and competitive. This perspective may have significance due to similar unfair market conditions in Afghanistan.

Peter Boone tries to relate the effectiveness of foreign aid to the political regime of recipient countries. He argues that poverty is a result of bad policies of politicians. In his empirical results he finds that aid programs have not caused or correlated with the primary components that led to investment and growth, nor did it encourage the government policies to improve primary human development indicators significantly. (Boone, 1996) His findings also suggest that little aid programs to new liberal political regimes may be more effective in reducing poverty and promoting growth. He argues that if these new liberal political regimes stay in power for enough time to increase education and healthcare, then the problem of poverty reduction would become self-sustaining. However, alternatively, these liberal regimes may not survive or promote growth, because of the factors that support these new political regimes root in historical, cultural and institutional factors which may not change with new political regimes. This study indicates that democratic regimes empower poor little more than other regime types, and also identifies a positive correlation between foreign aid and consumption, but consumption did not benefit poor. Based on this the rational conclusion is that foreign aid rises consumption rather than investment.

William Easterly argues that the empirical literature on the relationship between aid and growth lacks a clear theoretical model. He argues that the assumption that foreign aid finances investment and not consumption holds only if the investment was liquidity constrained and motives for investment were in desirable conditions. However, if the case with less investment is the weak incentives for investment, then foreign aid will increase consumption rather than investment. Also, foreign aid might deteriorate the incentive for investment, if the recipient becomes dependent on foreign aid in the long-run, by merely believing that future underdevelopment will bring future foreign aid (Samaritan's dilemma). (Boone, 1996) This theory applies to Afghanistan because of its dependency on foreign aid for long periods of time.

3.1.3. Mixed Impact of Aid on Growth

This perspective is based on the concept that foreign aid helps development under specific situations and suggests that foreign assistance supports economic development at best in some circumstances and not in every conditions, several studies have been reached to similar conclusions and mixed results such as Mosley (1980), Boone (1996), Burnside and Dollar (2000). Burnside and Dollar examine the relationship between foreign aid, growth, investment and policies. Through an empirical study in the neoclassical growth analytical framework, they develop linkages with growth and reasonable policies and finds them intrinsically related. They note that imperfect international capital markets and bad policy environments will prevent emerging countries from fast growth to a steady state. Economic, political and institutional policies all affect economic growth. This study finds a positive effect of foreign aid and growth in

a good policy environment. (Burnside & Dollar, 2000) Based on this study the logical conclusion is that without a good policy environment foreign aid would not necessarily foster growth. Hansen and Tarp study the relationship between foreign aid and GDP per capita. They include investment and human capital in the growth regression and found that without these variables aid does not affect growth. This study confirms the hypothesis that foreign aid fosters growth via investment and this is not conditional on good policy environment. (Hansen & Tarp, 2001) They suggest that more focus and stress should be put on more theoretical work before experimental works on cross-country regressions are used for policy goals.

Rajan and Subramanian (2008) attempt to examine the relationship between aid and growth in a transparent and generalising way, by using cross-section and panel data techniques. They found little robust evidence of a positive or negative relationship between foreign aid and economic growth of a country. They also found no evidence on the subject that aid might work well under good policies or better environments and different types of aid might have different impacts. This study indicates that there is no effect of foreign aid on long-run economic growth. Ekanayake and Chatrna analysed the effectiveness of foreign aid on 85 developing countries in Latin America, Africa, Asia and Caribbean between the periods 1980-2007. They found mixed results. In most cases, they found adverse effects of aid on growth and in some cases positive. (Ekanayake & Chatrna, 2010)

Alesina and Dollar's study explore the pattern of foreign aid from donors to receipt countries. They found evidence that foreign aid is influenced by political and strategic factors rather than economic needs and policy performance of recipient countries. The main foreign aid patterns are colonial past, political allies or UN voting. This study also found that the United States' flows of foreign aid are hugely influenced by its interest in the Middle East region. (Alesina & Dollar, 2000) This study shows that important factor in ineffectivity of bilateral foreign aid programs in promoting growth and reduction of poverty is the donor's political and strategic interest. This study is applicable in Afghanistan because the United State is the largest donor in Afghanistan, and Afghanistan is neighboured to the Middle East.

Durbarry, Gemmell, and Greenaway in a research paper tried to contribute to the empirical debate over do foreign aid foster growth in developing countries by using augmented Fischer – Easterly growth model. They found robust evidence that a large number of foreign aid flows have a positive effect on growth but conditional on stable macroeconomic policies in developing countries. Although low levels of foreign aid flows do not foster growth, however, extensive *Aid/GDP* ratios were also not optimal for growth. (Durbarry, Gemmell and Greenaway, 1998) This study indicates that foreign aid might foster economic growth but endless and enormous amounts of aid results in no improvement. There is an optimal level of foreign aid concerning its effect on growth. The optimal level is 40-45% aid/GDP ratio. This combines neoclassical economics observation of foreign aid with the law of diminishing returns.

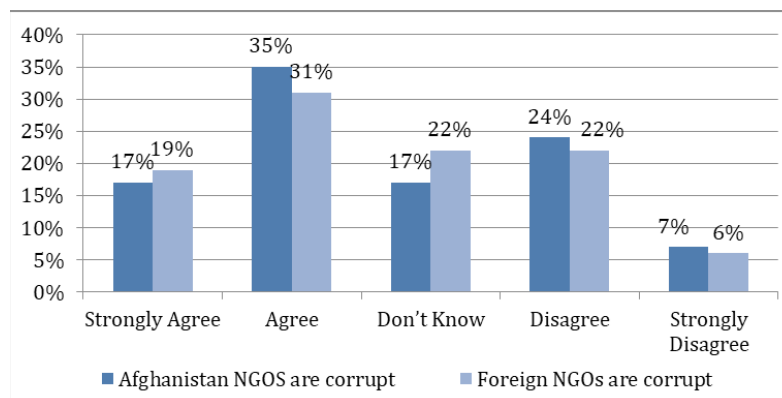
4. Analysis

The research analysis has focused on theoretical and empirical research, survey responses, and data analysis of foreign aid in respect to economic growth indicators, particularly GDP growth levels. The findings are going to specify which theories, academic studies and empirical analysis most relate to the testing of foreign aid effectiveness on economic development in Afghanistan. However, the primary focus of this study has been multinational academic studies which closely relate to the situations in Afghanistan. The survey responses also confirm the data and technical evaluations. However, in order to make contribution to development process of poor countries, the potential advantages assists as providing resources to improve infrastructure, agriculture, education and transfer of technology.

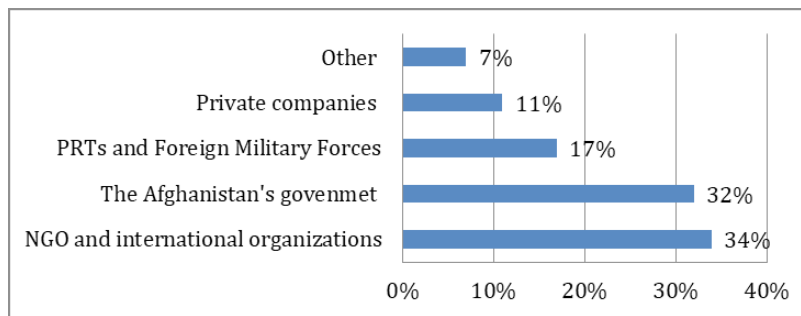
4.1. How is the Public Perception of Foreign Aid in Afghanistan?

Citizens of Afghanistan perceive foreign aid as highly associated with corruption, with unequal disbursement across provinces, but there is also partially positive public perception of aid delivery and its deliverers in Afghanistan. (Integrity Watch Afghanistan, 2008: 30) *Figure 1* shows the perceived level of corruption in domestic and foreign NGOs in Afghanistan from *Integrity Watch Afghanistan Report* which was constructed from interviews of principal aid actors and a survey of over 1000 Afghanistan citizens across 18 provinces in 2008. The report showed that a majority of respondents believed that different forms of corruption harmed foreign aid programs.

Figure 1: Perceived Corruption in Domestic and Foreign NGOs

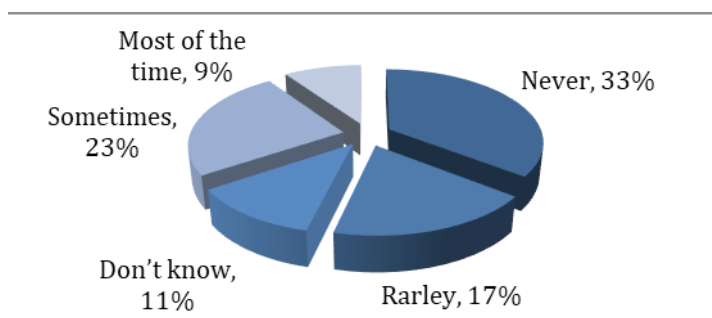


Source: Torabi, Y., & Delesgues, L. (2008: 30). Afghanistan: Bringing Accountability Back In: from subjects of Aid to Citizens of the State. Integrity Watch Afghanistan. <http://iwaweb.org/wp-content/uploads/2015/11/02> (accessed 5 March 2018).

Figure 2: Who Spends Most Of The Fund Given To Afghanistan

Source: Torabi, Y., & Delesgues, L. (2008: 31). Afghanistan: Bringing Accountability Back In: from subjects of Aid to Citizens of the State. Integrity Watch Afghanistan. https://iwaweb.org/wp-content/uploads/2015/11/02-bringing_accountability_back_in.pdf (accessed 5 March 2018).

Figure 2 shows that it is widely perceived that the international organisations and NGOs and Afghanistan Government have spent most of the funds. Most of the educated and male respondent believed that international organisations and NGOs were the leading implementers of aid, while female and illiterate respondents tended to believe Afghanistan's government as the leading implementer of aid.

Figure 3: How Much Do NGOs Seek People's Opinions in their Expenditure?

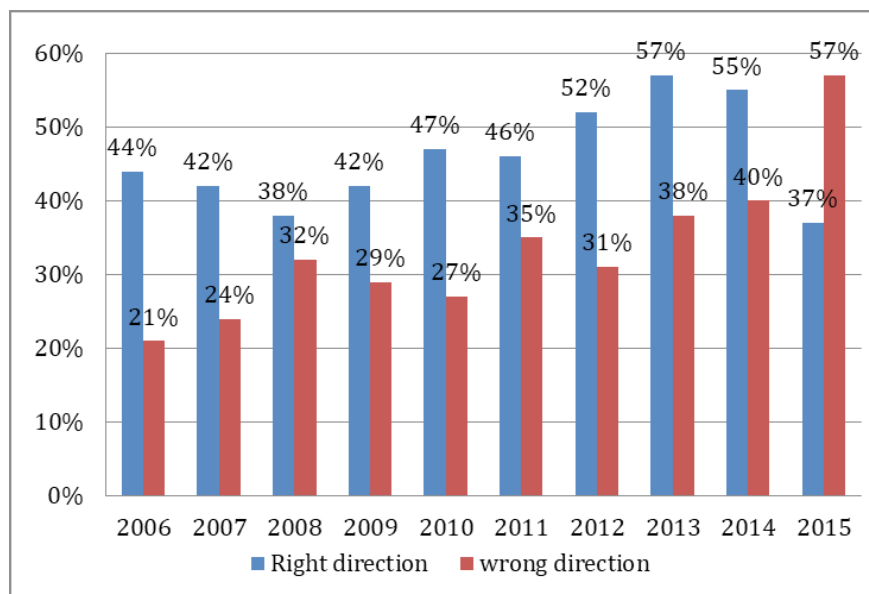
Source: Torabi, Y., & Delesgues, L. (2008: 34). Afghanistan: Bringing Accountability Back In: From Subjects of Aid to Citizens of the State. Integrity Watch Afghanistan: http://iwaweb.org/wp.content/uploads/2015/11/02-bringing_accountability_back_in.pdf (accessed 5 March 2018).

Figure 3 shows the public perception of how much NGOs seek public opinion in their expenditure. It shows that the majority of Afghanistan citizens believe that their opinions are not considered in NGOs expenditure. One respondent in three believed that their opinion was sought in NGOs expenditure somehow.

The reason behind the inefficiency of Afghanistan's government has been linked to corruption

and low service delivery. Since the majority of respondents believed that the government of Afghanistan was most affected by corruption, however, the majority of them also recommended that most of the aid should be channelled through Afghanistan's government. (Integrity Watch Afghanistan: 32-33) Majority of the Afghanistan citizens believed that around 40% of aid provided to Afghanistan was wasted through corruption. The government of Afghanistan as the aid administrator was believed as the most affected by corruption with two third of the respondents then followed by NGOs and international organisations with 13%, private companies with 8% and Provincial Reconstruction Team (PRT) with only 5%. There has been a considerable consensus in public perception that evaluation and monitoring improved the quality of projects. Majority of the respondents preferred the Afghan government for the job of monitoring aid. (Integrity Watch Afghanistan: 30-4) The mentioned factors indicate a lack of accountability, ownership and service delivery by the government, at the same time a significant increase in demand of citizens for more public accountability.

Figure 4: The Direction of the Country: National Mood (2006-2015)



Source: Ian S. Livingston and Michael O'Hanlon, *Afghanistan Index*, The Brookings Institute, 2015.

Figure 4 taken from Survey of The Asia Foundation polled from around 10000 Afghanistan citizens in 2015 shows an overall decrease in optimism and increase in pessimism in the last decade. According to figure 4, Afghanistan citizens believe that their country is moving in the wrong direction. The reasons behind the pessimism have been insecurity (44%), unemployment (25%), corruption (13%), a lousy economy (12%) and bad government (11%) in general. (Hopkins & Warren, 2015: 20-21)

The decline in optimism of Afghanistan citizens particularly in 2015 indicates the remarkable transition of political, security and economic transition that country experienced in 2014 presidential elections. Afghanistan citizens participated in the election with optimism for the future, but the corruption allegations harmed the election results. The uncertainty in the political situation and withdrawal of foreign forces has lowered investment. Also, a decline in foreign aid which composes a substantial portion of Afghanistan's gross domestic product (GDP) has impacted economic development and shaping public perception for Afghanistan's progress. (Hopkins & Warren, 2015: 15) According to Integrity Watch Afghanistan's report overall, the majority of Afghanistan's citizens wanted an increase in the Afghanistan leadership over aid. Despite high levels of corruption and disparities across provinces within aid, there is huge enthusiasm in Afghanistan citizens for taking ownership in aid programs. This shows that there is a vast demand in public perception in Afghanistan for being active citizens of aid rather than being passive subjects.

The majority of responses from the Integrity Watch Afghanistan report associate aid with corruption, weak accountability and lousy governance. As well as many other theories from economists, such as those from Milton Friedman, Peter Bauer, and William Easterly, when discussing foreign aid as policy associate foreign aid with corruption, patronage and more wealth of only elite people of the emerging countries. Besides, the study of Peter Boone associate foreign with an increase in the size of government, and the study of Alberto Alesina and Beatrice Weder also indicate that according to some measures of corruption, corrupt governments receive more aid rather than less aid. Since most of the failures of foreign aid to Afghanistan have been linked to corruption and similar activities like fraud, patronage and misappropriation, what could be the reason? The presence of corruption in foreign aid projects in emerging countries hinders growth and development, as expressed by Bauer and Easterly. (Shleifer, 2009: 379)

However, according to Integrity Watch Afghanistan's report overall, the majority of Afghanistan's citizens wanted an increase in the Afghanistan leadership over aid. Despite high levels of corruption and disparities across provinces within aid, there is huge enthusiasm in Afghanistan citizens for taking ownership in aid programs. (IWA: 6) This shows that there is a vast demand in public perception in Afghanistan for being active citizens of aid rather than being passive subjects.

4.2. How is Foreign Aid Affecting Government Expenditure?

The U.S Government Accountability Office (GAO) report indicates that even though, the international community has disbursed a tremendous amount of aid to Afghanistan, Afghanistan's domestic revenues still could not cover its total public spending. International donors also raised concern about Afghanistan's dependency on foreign aid to fund its public expenditures. (US GAO, 2013: 25) From 2006 until 2011 Afghanistan's domestic revenues financed around 10% of its total public spending. During the same period Afghanistan's domestic revenue raised from \$0.6 billion

to \$2 billion, a rise of 230%. Afghanistan's public expenditure also increased from \$5.8 billion to \$17.4 billion, a rise of more than 200%. During this period donors provided around 90% of Afghanistan's total public expenditure, with U.S funding 64% of that. About 80% of Afghanistan's total public expenditures were funded by the international community outside of the government budget (off-budget). It has been estimated that Afghanistan would be reliant on donor funding through 2024. (US GAO, 2013: 26)

4.3. The ODA's Impact on the Afghanistan's Economic Development

Official Foreign Aid has a mixed impact on economic growth in Afghanistan. Foreign aid has at best been successful at promoting economic growth in Afghanistan only in the short term. Positive effects of foreign aid on economic growth have been transitory and not sustainable.

The 2018 Oxfam and Swedish Committee for Afghanistan (SCA) joint report on aid effectiveness indicate that while foreign aid to Afghanistan has been decreased from \$6.5 billion in 2010 to \$4.2 billion in 2015, ODA provided by donors has been mostly fragmented and Afghanistan remains financially dependent on foreign aid. (ATR Consulting, 2018: 7) Even though domestic revenues has been tripled in the last decade, between the years 2017-2018 domestic revenues financed only 33% of Afghanistan's budget and the remaining 66% was funded by foreign aid. This reflects Afghanistan's continuing high level of foreign aid dependency. Donors provide aid for the development budget both on-budget through government and off-budget through international and non-governmental organisations. However, according to the report aid provided through off-budget channels have been more fragmented. (ATR Counsaling) This fragmentation in donor's aid disbursement and aid dependency of Afghan government indicates that foreign aid in Afghanistan has been ineffective.

Table 2 and 3 depicts the decline of Afghanistan's economy despite increasing international financial support between the years 2002 and 2015. OECD provides data for annual ODA disbursed to Afghanistan government for developmental purposes has increased from 2001 to 2011, then a decrease till 2015 and measured in billions of dollars.(OECD, 2018) The corruption perception index (CPI) lists countries according to how corrupt their public sector is perceived to be. It ranks countries on a scale of 0 to 10, where 0 indicates that a country is highly corrupt and ten indicates that a country is not corrupt. (Transparency International, 2015) However after 2011, the CPI index uses a scale of 0 to 100, so for better analysing and comparing of data, I divided the scores by 10 for the years 2012 to 2015. The CPI scores indicate a drastic decrease, thus a rise in corrupt activities. The CPI score has declined almost 1.4 points from a 10-point scale, from 2.5 in 2005 to 1.1 in 2015. GDP growth had fallen from 8.4 percent in 2003 to 1.3 percent in 2015, the unemployment rate had been increased from 8.2 percent in 2003 to 9.1 in 2014, and inflation decreased from 5.1 percent in 2002 to – 0.7 percent in 2015.

Table 2: Annual Economic Changes and Net ODA Received

Afghanistan	2002	2003	2004	2005	2006	2007	2008
CPI	x	x	X	2.5	2.5	1.8	1.5
GDP Growth (annual %)	x	8.4	1.1	11.2	5.5	13.7	3.6
GDP per Capita Growth (%)	x	3.3	-3.4	6.9	2.2	10.6	1.04
Inflation	5.1	35.7	16.4	10.6	6.8	8.7	26.4
Net ODA in \$Billion	1.31	1.594	2.311	2.838	2.962	5.077	4.875
Net ODA per Capita in \$	59.6	69.1	95.8	113.2	114.4	190.7	178.6
Net ODA (%GNI)	31.8	34.8	43.6	45.1	41.7	51.4	47.6
Unemployment(% of total labour force)	x	8.2	8.5	8.5	8.8	8.4	8.9

Source: Developed by the author using Transparency International, **Corruption Perceptions Index**, 2015.

Table 3: Annual Economic Changes and Net ODA Received

Afghanistan	2009	2010	2011	2012	2013	2014	2015
CPI	1.3	1.4	1.5	0.8	0.8	1.2	1.1
GDP Growth (%)	21	8.4	6.1	14.4	3.9	2.7	1.3
GDP per Capita Growth	17.9	5.4	2.8	10.7	0.5	-0.5	-1.6
Inflation	-6.8	2.2	11.8	6.4	7.4	4.7	-0.7
Net ODA in \$Billion	6.235	6.47	6.866	6.667	5.153	4.943	4.237
Net ODA per Capita in \$	222.6	224.6	231.1	217.1	162.4	150.9	125.6
Net ODA (%GNI)	49.7	40.4	37.9	32	25.1	23.8	21.8
Unemployment (% of total labour force)	8.1	8.7	8.9	8.5	9.2	9.1	X

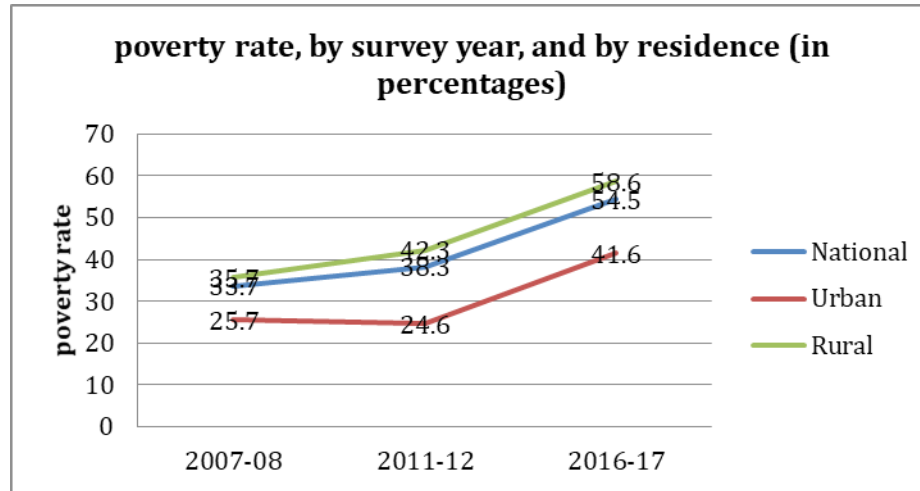
Source: Developed by author using Transparency International, **Corruption Perceptions Index**, 2015, (Accessed) <https://www.transparency.org/cpi2015>, 15 March 2018; World Bank, (Accessed) <https://data.worldbank.org/country/afghanistan>, 15 March 2018; International Monetary Fund, (Accessed) <http://imf.org/en/Countries/AFGcountrydata>, 5 April 2018; (Accessed) <http://www.oecd.org/dac/stats/idsonline.htm>, 10 April 2018, Ian S Livingston and Michael O'Hanlon, **Afghanistan Index**.

The data in Table 2 and Table 3 indicate that GDP growth of Afghanistan has declined 7.1 percent, from 8.4 percent in 2003 to 1.3 percent in 2015. (World Bank Development Indicators) This decline in GDP growth rules out the probability that foreign aid accelerated growth in Afghanistan. This is consistent with an empirical study of Boone and predictions of Bauer (1971) and Friedman (1958). Based on the Boone empirical model, foreign aid does not promote economic development because of distortionary policies of politicians, and politicians use aid flows to maximise the welfare of wealthy elite. (Boone, 1996)

Foreign aid has increased corruption in Afghanistan. The data in Table 3 and 4 indicate that the CPI score for Afghanistan has dropped a total of 1.4 points. (Transparency International) This drastic drop in value indicates an increase in corruption in the public sector and corrupt activities in Afghanistan. This is consistent with the empirical study of Alesina and Weder, which finds no evidence that less corrupt governments receive more aid, but on the contrary, more corrupt governments receive more foreign aid, and countries that receive high levels of foreign aid tend to have high levels of corruption. (Alesina & Weder, 2002)

Figure 5 plots estimates for poverty rate by using three surveys. These estimates are derived from 2016-17 survey of Central Statistics Organization of Afghanistan, which covered around 20,000 households and 155,680 individuals across the country. It also shows the difference between national, urban and rural poverty rates.

Figure 5: Poverty Rate



Source: Central Statistics Organization (CSO), (2018:101). **Afghanistan Living Conditions Survey 2016-17**, Kabul. (Accessed 2 June 2018) http://cso.gov.af/Content/files/ALCS/ALCS%202016-17%20Analysis%20report%20-%20Full%20report%2023%20_09%202018-ilovepdf-compressed.pdf.

This figure shows a slight rise in the national poverty rate from 33.7 percent (2017-2018) to 38.3 percent (2011-2012), then a sharp increase to 54.5 percent (2016-2017). (CSO, 2017: 101) It also indicates a high disparity among rural and urban poverty rates. Poverty rates are higher in rural areas where 70 percent of the population lives. This sharp rise in poverty rates confirms the slow-down of economic growth in Afghanistan. The reduction in foreign aid and international spending to Afghanistan after 2011 has resulted in a sharp deterioration in the welfare of Afghanistan's population.

The deterioration in the welfare of Afghanistan's population supports scholarly examinations of aid and economic growth relationship. According to Easterly one of the critical assumptions of the "financing gap" model is that aid finances investment rather than consumption. (Easterly, 2003: 23-48) However, this assumption makes sense only if the incentives for investment were favourable. However, if the incentives for the investment were poor, then aid would increase consumption rather than investment. Foreign aid will deteriorate the incentive for investment if the recipient faces the "Samaritan's dilemma", which means being dependent on aid in the long run and by assuming that future poverty would eventually bring future foreign aid. Boone links the effectiveness of foreign aid on alleviating poverty to the political regime of recipient country.

(Boone, 1996: 289-329) He suggests that all political regimes support only high political elite. However, democracies have a lower infant mortality rate. He links this to more empowerment of poor in the democracies. He suggests that short-term aid programs that support democracies could improve poverty if they lay the foundations for political and economic reforms. However, the essential elements that assist democracies are grounded in historical, cultural and institutional elements that are not impacted by new government. (Boone, 1996)

4.4. The Impact of the International Funding on the Long-Run Economic Development in Afghanistan

The answer to this question would be applying a summary of the findings from other secondary questions of this study. The main finding is that there are no indicators that foreign aid affected economic development positively in the long-run and in a sustainable way. All the benefits have been transitory and not permanent. The main benefits have been the wealthy and connected elite only.

Since the international and particularly U.S. government started funding and foreign aid to Afghanistan, there was a relative economic growth but after 2012 and decreasing foreign aid the economic and social situations have been deteriorated. GDP growth had fallen from 8.4 percent in 2003 to 1.3 percent in 2015; the unemployment rate had been increased from 8.2 percent in 2003 to 9.1 in 2014. This represents that all the economic benefits were short-term and not sustainable. As a result, the foreign aid *does not affect positively to economic development or political stability* for the country.

The CPI score had declined almost 1.4 points from 2.5 in 2005 to 1.1 in 2015. Trade deficit and imbalance has been increased, with the imports almost tripled while exports remain at the same rate. The poverty rate has been increased to around 55 percent at the national level. This indicates that foreign aid has financed consumption rather than investment. Therefore, negative correlation to the large amounts of foreign aid inflow into Afghanistan. The belief and support for the government are lower, and most of the citizens believe that the country is moving into the wrong direction, primarily a result of corruption, weak governance and deterioration of socioeconomic situations in Afghanistan. The main factor to the increased level of corruption in Afghanistan is allocating too much aid in short periods of time by the international community, particularly by the United States. Moreover, one of the major factors contributing to negative effects of foreign aid in Afghanistan is mainly dualism is the foreign aid programs, providing both bribe or prestige aid and aid for economic development purposes at the same time. The U.S. by providing foreign aid for economic development purposes actually performed as a function of bribe or prestige aid, because *it didn't disturb the status quo of ruling groups or wealthy elite, whose continuance was in the interest of U.S. government*

4.5. Findings and Analysis

Here are the followings summarise the overall findings of the research and the acceptance or rejection of the hypotheses which were made at the beginning of the study have been presented;

- **Reject hypothesis 1:** Afghans perceive foreign aid as a moral duty of the international community, and that the public and government of Afghanistan have no reason to be active subjects of aid.
- **Reject hypothesis 2:** Technical Assistance and Afghanistan National Development Strategy have worked, and positively contributed to development.
- **Accept hypothesis 3:** Foreign aid has expanded government expenditure.
- **Reject hypothesis 4:** Official Development Assistance has positively affected economic development in Afghanistan.
- **Accept hypothesis 5:** International community and the U.S. perceive Afghanistan as weak and rentier state.
- **Reject hypothesis 6:** Foreign aid has a positive effect on long-run and sustainable economic development in Afghanistan.

The deterioration in macroeconomic indicators of Afghanistan shows that foreign aid inflows have not resulted in sustainable economic development. The decrease in GDP growth and GDP per capita growth, increase in unemployment, poverty rate and corruption perception index confirms this. This would support several scholar observations of the partial or no impact of foreign aid on sustainable economic growth and development.

Growth in GDP has decreased by 7.1 percent, on the other hand unemployment rate and poverty have increased, and corruption has raised with a CPI decreasing of 1.4 from a 10-point scale. As of 2018, Afghanistan's budget was funded even 66 percent by the international community and 33 percent by domestic revenues. This problem has become apparent since it is weak and careless spending, lack of ownership by Afghanistan's government, fragmentation in donor programs and poor donor alignment.

Afghanistan citizens do not support lack of ownership by government and public of Afghanistan, instead of being passive subjects of aid they want to be active subjects of aid, as noted in the surveys. Donors particularly the U.S. foreign aid flows have mainly in the form of military and bribe aid for political and strategic consideration in Afghanistan. Thus this increased the level of corruption and a decrease in GDP growth.

The deterioration in socioeconomic conditions and increase in corrupt activities in Afghanistan, as indicated by survey responses of the public in Afghanistan and the decrease in CPI, has resulted in lowering the legitimacy of the government and raised political instability. Previously mentioned cases such as the changes in national mood, most of the Afghanistan citizens believe that country is not moving in a healthy direction, and optimism for future has been decreased.

Each and every of these impacts indicate to validate the theories that foreign assistance increases corrupt activity, and does not promote economic development.

Since 2005 foreign aid efficiency to Afghanistan has become a national and international topic of debate. The Paris Declaration on Aid Effectiveness in the 2nd March of 2005 was held among ministers of over 100 developed and developing countries responsible for promoting development and heads of aid development institutions. Thus, to monitor and reform how they deliver and manage the aid much more effectively. However, according to reports of monitoring the Paris Declaration survey in 2008, published by the Organization for Economic Co-operation and Development (OECD), the desired achievements were not satisfactory.

Despite all of the efforts and vast amounts of aid inflows to Afghanistan, Afghanistan is among one of the Least Developed Countries (LDC) with the majority of its population living under the poverty line. Most of the aid money has been spent outside of government system rather than focusing on the priority needs of the public, thus making Afghanistan more reliant on foreign aid. The recent decline in monetary aid and the withdrawal of foreign troops resulted in Afghanistan's dependency on its scarce domestic revenues and a rise in poverty, unemployment, insecurity and corruption levels. (The Economist, July 2012)

5. Conclusion

After focusing on foreign aid definitions, a brief history of foreign aid, its objectives and different aspects of foreign aid in the theoretical frameworks has been concerned. As it is mentioned at the beginning the aim was to realize the issue of foreign aid disbursements as practiced in Afghanistan by using objective perspective to specify the effects of foreign aid on economic growth. Since U.S. led invasion of Afghanistan in 2001, Afghanistan has received large amounts of foreign aid for political stability, economic growth and improving socio-economic conditions. However, after two decades of foreign aid inflows to Afghanistan, the socio-economic conditions has not been improved.

This research study has recognized the impacts of foreign aid disbursements on economic development as affected by the political and strategic considerations and also by corruption levels which could have significance to future foreign aid programs in developing and post-conflict countries similar to Afghanistan. According to Craig Burnside and David Dollar's study, foreign aid has little impact on growth, but in a healthy policy environment, foreign aid has a robust and positive effect on economic growth. Additional benefits of foreign aid include poverty reduction, increase in health and education indicators and transfer of technology or knowledge from developed countries to underdeveloped countries. However, the hypothesis that foreign aid directly benefited and fostered economic development is controversial, and few cases exist where foreign aid did not dictate undesirable economic costs.

Easterly further states that foreign aid is given as loan or grant to developing countries for development purposes, often and in many instances have been stolen by officials receiving it as

their basic instinct. The aid money gets wasted or consumed by developing countries leaders, ministers, officials or other bureaucrats who all want a share. As the donor countries want to provide aid for national priorities, the recipient government also want to spend it on projects which are harder to monitor and more accessible to steal. This problem is severe in foreign loans particularly given by IMF and WB, and the consequences could be dramatic. Because these wasted loans by government officials have to be repaid by the citizens, which often results in not repaying and criticism of the donor country or agency itself for providing aid. (The Economist, July 2012) Western and developing governments both have troubles in spending money efficiently. The lessons learned from development economics lately is that there has been massive corruption, fraud, waste and misallocation of resources at all stages. This problem may undermine the development process in receipt country, because of undermining the political and institutional processes. Foreign aid might undermine the underlying contract between the state and its citizens by interrupting the connection between state resources and its ability to tax. These adverse impacts of foreign aid might prevail to its beneficial impacts.

The conditions in Afghanistan indicate that foreign aid invites corruption and confirms analyses and predictions of economic and political scholars that argue “*foreign aid does not promote economic development and might undermine it* “. In particular, *the Afghanistan experience and involvement contradicts the theory that foreign aid promotes economic development*. Also, the study of Brautigam and Knack correlates weak governance with dependence on vast amounts of foreign aid, the study of Alesina, Weder, and Svensson Correlates corruption with foreign aid, and study of Morgenthau Relates foreign aid to political interest of donor countries all reflect that “*foreign aid does not foster economic development*”. To have a successful foreign aid program, one possible suggestion is that foreign aid programs targeted to countries with sound macroeconomic policies and fewer corruption levels may be more effective in promoting economic growth. However, the surprise is that foreign aid in most cases is needed in countries where the conditions are deplorable and environment required for effective functioning of foreign aid.

As a result, foreign aid has not promoted economic development in Afghanistan, on the contrary it has increased corruption, weakening governance and bribery. The international community, in particular, the U.S. government must put more significant efforts to provide responsible and effective foreign aid for economic development purposes. The government of Afghanistan should also take more ownership in foreign aid programs by putting its long-term development goals first and making foreign aid programs more accountable to its citizens. Both the international community and government of Afghanistan must promote reducing corruption as a key factor in foreign aid and development programs. In order to have real improvements in economic development, efforts must focus on ways to make foreign aid more effective. This study also assumes that the international community, particularly the western nations, the United States and its allies will maintain their engagement in international efforts to provide foreign aid for weak economies. However, there is a growing emphasis on effectiveness of foreign aid programs in post-conflict states like Afghanistan. Finally it should be pointed out that *domestic resources* have a direct and stronger impact on *economic development than external resources*.

References

- Aikins, Matthieu (2012, October). Contracting the Commanders: Transition and the Political Economy of Afghanistan's Private Security Industry. *Center on International Cooperation*, New York University.
- Alesina, A., Weder, B. (2002). Do Corrupt Governments Receive Less Foreign Aid?. *American Economic Review*, 92(4), 1126-1137.
- Alesina, A. & Dollar, D. (2000). Who Gives Foreign Aid to Whom and Why?, *Journal of Economic Growth*, 5(1), 33-63.
- Atr Consulting (2018). Aid Effectiveness in Afghanistan. Swedish Committee for Afghanistan (SCA) Oxfam, p.7(Accessed): https://swedishcommittee.org/sites/default/files/media/aideffectiveness_in_afghanistan_march_2018_0.pdf, 3 July 2018.
- Barfield, T. (2010). *Afghanistan: A Cultural and Political History*. Princeton University Press.
- Bissio, R. (2008). Paris Declaration on Aid Effectiveness. *Presentation at Human Rights Council, Session of the Working Group on the Right to Development*, High Task Force on the Implementation of the Right to Development, Geneva, p. 7-15.
- Bjelica, J. & Ruttig, T. (2018). The State of Aid and Poverty in 2018: A new Look at Aid Effectiveness in Afghanistan. *Afghanistan Analyst Network*, 17 May 2018, (Accessed) <https://www.afghanistan-analysts.org/the-state-of-aid-and-poverty-in-2018-a-new-look-at-aid-effectiveness-in-afghanistan/>, 6 September 2018.
- Boone, P. (1996). Politics and the Effectiveness of Foreign Aid. *European Economic Review*, 40 (2), 289-329.
- Bräutigam, A. D. & Knack, S. (2004). Foreign Aid, Institutions, and Governance in Sub-Saharan Africa. *Economic Development and Cultural Change*, 52 (2), 255-285.
- Burnside, C. & Dollar, D. (2000). Aid, Policies, and Growth. *The American Economic Review*, 90 (4), 847-868.
- Chenery, H. B. & Strout, A. M. (1966). Foreign Assistance and Economic Development. *The American Economic Review*, 56 (4), 679-733.
- Corruption Perception Index (2015) *Transparency International*, (Accessed) <https://www.transparency.org/cpi2015#results-table>, 26 March 2018.
- Cullather, N. (2002). Damming Afghanistan: Modernization in a Buffer State. *The Journal of American History*, 89 (2), 512-537.
- CSO – Central Statistics Organization (2017). *Afghanistan Living Conditions Survey 2016-17*, Kabul, (Accessed) <https://cso.gov.af/Content/file/ALCS/ACLS%202016-17%20Analysis%20report%20Fullcompressed.pdf>, 2 June 2018.
- Deniz, M. & Haidar, Z. G. (2018). *The Effects of Foreign Aid On Economic Development in Afghanistan (2001-2015)*. Basılmamış Yüksek Lisans Tezi, İstanbul Üniversitesi SBE.
- Durbarry, R., Gemmell, N. & Greenaway, D. (1998). New Evidence on the Impact of Foreign Aid on Economic Growth. *CREDIT Research Paper*, No. 98/8.
- Easterly, W. (2003). Can Foreign Aid Buy Growth?, *Journal of Economic Perspectives*, 17 (3), 23-48.
- Eknayake, E. M. & Dasha, C. (2010). The Effect of Foreign Aid on Economic Growth in Developing Countries. *Journal of International Business and Cultural Studies*, 3, 1.
- Hansen, H. & Tarp, F. (2001). Aid and Growth Regressions. *Journal of Development Economics*, 64 (2), 547-570.
- Hopkins, N. & Warren, Z. ed. (2015). *Afghanistan in 2015: A Survey of the Afghan People*. Asia Foundation, (Accessed) <https://asiafoundation.org/resources/pdfs/Afghanistanin2015.pdf>, 10 March 2018.

- Intelligent Economist. *Types of Foreign Aid*, (Accessed) <https://www.intelligenteconomist.com/foreign-aid/>, 24 February 2018.
- Integrity Watch Afghanistan. *Aid Effectiveness: Making Aid Transparent in Afghanistan*, (Accessed) <https://iwaweb.org/wp-content/uploads/2015/12/1-Aid-Effectiveness-Making-Aid-Transparent-in-Afghanistan.pdf>, 22 February 2018.
- Islam, A. (1992). Foreign Aid and Economic Growth: An Econometric Study of Bangladesh. *Applied Economics*, 24 (5), 541-544.
- Lancaster, C. (2008). *Foreign Aid: Diplomacy, Development, Domestic Politics*, University of Chicago Press, 9.
- Livingston, I. S. & O'hanlon, M. (2015). *Afghanistan Index*. The Brookings Institute, (Accessed) <https://www.brookings.edu/afghanistan-index/>, 2 March 2018.
- Lumsdaine, D. H. (1993). *Moral Vision in International Politics: The Foreign Aid Regime, 1949-1989*, Princeton University Press.
- Martens, B. (2005). Why Do Aid Agencies Exist?. *Development Policy Review*, 23 (6), 643-663.
- Mobariz, Ahmad (2016). WTO Accession of Afghanistan: Costs, Benefits and Post-Accession Challenges, *South Asia Economic Journal*, 17 (1), 46-72.
- Morgenthau, H. (1962). A Political Theory of Foreign Aid. *American Political Science Review*, 56 (2), 301-309.
- Mosley, P. (1986). Aid Effectiveness: The Micro-Macro Paradox. *IDS Bulletin*, 17(2), 22-27.
- Ministry Of Finance (MoF), News: Delivery Aid Through the Country System. *Afghanistan Aid Bulletin*, 1 November 2011, (Accessed) <http://mof.gov.af/Content/files/Afghanistan%20Aid%20Bulletin.pdf>, 25 February 2018.
- Radelet, S. M. & Clemens, R. B. (2004, February). Aid and Growth : The Current Debate and Some New Evidence. Center for Global Development.
- Radelet, S. (2006). A Primer on Foreign Aid. (Accessed) http://www.who.int/hac/techguidance/training/analysing_health_systems/a_primer_on_foreign_aid_06.pdf 8 March 2018.
- Rajan, R. G. & Subramanian, A. (2008). Aid and Growth: What does the Cross-Country Evidence Show?. *The Review of Economics and Statistics*, 90(4), 643-665.
- Rose-Ackerman, S. (1975). The Economics of Corruption. *Journal of Public Economics*, 4(2), 187-203.
- Rubin, B. R. (2000). The Political Economy of War and Peace in Afghanistan. *World Development*, 28 (10), 1789-1803.
- Shah, S. M. & Garner, R. (2009). Afghanistan National Development Strategy (ANDS) Formulation Process: Influencing Factors and Challenges, Afghanistan Research and Evaluation Unit, (Accessed) <https://areu.org.af/wp-content/uploads/2016/01/904E-ANDS-Formulation-web.pdf>, 6 March 2018.
- Taylor, R. N. (2008, 25 March). 40 % of Afghan Aid Returns to Donor. *The Guardian*, (Accessed) <https://www.theguardian.com/world/2008/mar/25/afghanistan.internationalaidanddevelopment>, 20 February 2018.
- OECD (2018, February). *Net Official Development Aid (ODA)*, (Accessed) <https://data.oecd.org/oda/net-oda.htm>, 13 March 2018.
- OECD (2009, May). *Evaluation Report Country Programme Evaluation Afghanistan*. P.11 (Accessed) <https://oecd.org/countries/afghanistan/47107291.pdf>, 26 February 2018.
- Samim, M. (2016, May). Afghanistan's Addiction to Foreign Aid. *The Diplomat*, 19 May 2016, <http://thediplomat.com/2016/05/afghanistan-addiction-to-foreign-aid/>, 12 February 2018.
- Shleifer, A. (2009). Peter Bauer and the Failure of Foreign Aid, *Cato Journal*, 29, 379.

- SIGAR – Special Inspector General to Afghanistan Reconstruction (2018, April). *Private Sector Development and Economic Growth*, p. 13-5. (Accessed) <https://www.sigar.mil/pdf/lessonslearned/SIGAR-18-38-LL.pdf>, 5 July 2018.
- Svensson, J. (1999). *Foreign Aid and Rent-Seeking*, The World Bank.
- The Economist (2012, 14 July). Afghanistan's Economy, the Hands that Feeds: More Aid is Pledged, but It will not Solve Afghanistan's Many Problems. The Economist, (Accessed) <https://www.economist.com/node/21558635>, 22 February 2018.
- The Government Of Afghanistan – MOMP. Turkmenistan – Afghanistan-Pakistan-India (TAPI) The Pipeline. (Accessed) <http://mom.gov.af/en/page/4717>, 7 June 2018.
- Torabi, Y., & Delesgues, L. (2008). *Afghanistan: Bringing Accountability Back In: From Subjects of Aid to Citizens of the State*. Integrity Watch Afghanistan. (Accessed) <http://iwaweb.org/wp-content/uploads/2015/11/02-bringingaccountabilitybackin.pdf> , 5 March 2018.
- U.S. Government Accountability Office. (2013, February). Afghanistan: Key Issues for Congressional Oversight. (Accessed) <https://www.gao.gov/assets/660/652075.pdf>, 10 March 2018.
- World Bank. <https://data.worldbank.org/indicator/NY.GDP.MKTP.KD.ZG?locations=AF> , 16 March 2018.
- World Bank. World Development Indicators. (Accessed) <http://databank.worldbank.org/data/views/reports/reportwindget.aspx?ReportName=CountryProfile&Id=b40fd57&tbar=y&dd=y&inf=n&z>, 26 May 2018.