

Politics of International Aid and the New Asian Donors: Prospects for Reconstruction and Sustainable Peace in Sri Lanka - Part I

Thursday 4 June 2009, by [SENANAYAKE Darini Rajasingham](#) (Date first published: 20 May 2009).

The United States' government that wields considerable influence at the International Monetary Fund (IMF) has sought to delay the US\$1.9 billion loan appeal by Sri Lanka in the context a humanitarian crisis in the island. The Sri Lankan government that is at the end of its endgame with the Liberation Tigers of Tamil Eelam (LTTE), is seeking funds for reconstruction of the northeast conflict-affected region, among other things. Colombo has argued that it was fighting a "war on terror". Sri Lanka needs the IMF loan to service its external debt as a result of soaring defence expenditure and external borrowings which are also related to controversial oil-hedging deals.

The United Nations (UN) Security Council had earlier determined that it would not block the IMF loan to Sri Lanka when the subject came up at an informal UN Security Council discussion. However, it may revisit this determination following what the UN has termed a "bloodbath" on the day after Vesak in the northeast. The UN Human Rights Commissioner has asked for an investigation into war crimes since both sides are bound by the Law of War. Earlier, the UN Security Council's president, Mexican Ambassador Claude Heller, had said that "all 15 members agreed that such a move or other steps to punish Sri Lanka were unnecessary." The island's two main donors, China and Japan, along with Russia and Vietnam on the UN Security Council regard the violent conflict between the Sri Lankan government and LTTE as an internal matter. China recently overtook Japan as Sri Lanka's largest donor. The island is strategically located on one of the world's busiest shipping lanes.

The currently pending IMF loan has re-opened an old debate on international aid; its relevance and effectiveness, both within and beyond Sri Lanka. The IMF and many of the supra-national banks had almost run out of relevance and, more significantly clients, in the developing world before the current global financial crisis. Many countries had started borrowing in private capital markets. This was partly due to the unpopularity of Structural Adjustment Programs and other aid-related policy conditionalities imposed by the Washington Consensus in the heydays of neo-liberal development thinking. The institution had also lost considerable credibility during its response to the East Asian financial crisis in the 1990s and handling of the Argentina crisis in Latin America, particularly in the wake of World Bank Chief Economist, Joseph Stiglitz's critique that IMF policies actually exacerbated these crises. Stiglitz, subsequently, lost his job at the World Bank but he won the Nobel Prize for Economics and now teaches at Columbia University.

The IMF's diminished relevance prior to the current financial crisis was also due to the emergence of new Asian donors with billions of dollars, such as China and India, moving into Africa and Asia on the account of the need for natural resources to sustain growth at home. Following the global financial crisis, this particularly Bretton Woods twin received a new lease of life to assist poor countries affected by the global economic downturn at the G20 Summit in London when it garnered pledges in the billions to help economic recovery. However, at the same London Summit, British Premier, Gordon Brown had also declared that the "Washington Consensus is dead". Perhaps he followed in the English tradition of announcing, "The king is dead! Long live the king!" In any event,

it appears that the IMF may now step in where the World Bank once trod; the latter being the Bretton Woods twin tasked with post-conflict reconstruction. It is generally agreed that Sri Lanka's current economic woes are more related to soaring defence expenditure, dysfunctional governance and corruption that has fuelled and has been fuelled by the extended armed conflict with the LTTE rather than the global economic crisis.

Three years ago, Sri Lanka turned down an IMF offer of the status of a Heavily Indebted Poor Country (HIPC Initiative) and the Mahinda Rajapaksa regime celebrated the departure of the IMF with fanfare, and the promise never to go back to western aid conditionalities which often included the privatisation of public corporations and assets, underperforming or otherwise. Since then, Sri Lanka's Central Bank had followed a path of borrowing from private capital markets, having concluded that concessionary loans offered by international financial institutions were too costly, given aid conditionalities, including over-priced technical assistance from donor countries that amount to "phantom aid". Not so long ago, the Governor of the Central Bank of Sri Lanka went on record to tell the IMF to put Washington's finances in order following the global financial crisis rather than advising Sri Lanka on monetary policy.

Sri Lanka currently suffers from a home-grown balance of payments crisis related to defence expenditure, a bloated public sector and inflation that peaked last year at 30 percent, when official reserves were whittled away defending an exchange rate peg at of 108 Rupees to the United States Dollar. According to Razeen Sally, Director of the European Center for International Political Economy, an apparent balance of payments crisis is also related to "corruption and institutional rot that set in long ago but has plumbed new depths". Currently, controversial oil-hedging deals are under investigation by the Bribery Commission on the complaint to the Central Bank, following a Supreme Court stop order on oil-hedging payments by the Ceylon Petroleum Corporation, including to Citibank and Standard Chartered Bank. Recently, the United National Party, the main opposition, raised questions about conditionalities attached to the IMF loan in parliament in Colombo. The Sri Lankan government has stated that it will not tolerate conditionalities from the IMF which would very likely welcome a client from South Asia given its declining clientele in the region.

Historically, Sri Lanka has been a little bit of a 'donor darling' and hence tends to receive disproportionate international media attention when compared with other conflict regions, particularly from the BBC of late. The country however tends to underutilise normal development assistance (at around 17-35 percent depending on the project) and has experienced 'hot aid flows' as was the case following the Asian Tsunami disaster of 2004 when over 500 donors and international non-government organisations arrived in the island to provide relief and stayed on for several years. The aid experience after the Asian Tsunami disaster gave rise to a local discourse that the island had been struck by an "aid tsunami" that had caused new problems of coordination, equity and lack of local ownership of recovery priorities and programme. Several studies indicated that a significant part of the funds for disaster victims were consumed by international experts from various UN Agencies, IFRC and related Red Cross partners and INGOs based in Colombo, rather than reaching affected communities.

Sri Lanka's lush tropical beauty, cultural openness, and tourist-friendly people and infrastructure despite and arguably because of cycles of conflict, peace building, reconstruction and destruction in the last quarter century, means that it has been a favourite place for aid workers and the international development and humanitarian industry. It has been known for a while that international assistance in post-conflict situations may either ameliorate or contribute to conflict. Aid dependence in conflict situations may lead to institutional de-development and a form of aid-induced Dutch disease that exacerbates the emergent conflict and poverty trap in places where long-term, low-intensity conflict prevailed. It is in this context too that the Sri Lankan government has been recently quite dismissive of western aid donors.

The Tamil Diaspora, Information War and Aid Fungibility

“Politics in an information age is not only about whose military wins, but whose story wins” as Joseph S. Nye has noted. The Sri Lankan government is facing increased international pressure as it nears the end of the long war with the LTTE. Last month, Tamil diaspora groups held protests outside the IMF in Washington D. C. over the impending loan. On 5 May 2009, the Secretary General of the Paris-based Reporters Without Borders wrote an open letter to IMF’s Managing Director, Dominique Strauss-Kahn, drawing attention to “the lamentable state of press freedom in the country and seeking “rule of law” and human rights aid conditionality if the loan is passed. The missive from Jean-Francois Julliard, Secretary General of Reporters without Borders, noted, “As you know, Sri Lanka is spending as much as US\$1.6 billion on defense in its 2009 budget, a 6.5 percent increase on the 2007 allocation, while neglecting social needs. Some army units are implicated in war crimes. Others are suspected of responsibility for many cases of violence against journalists and human rights activists.”

Many western donors and members of the Organization for Economic Cooperation and Development-Development Assistance Committee (OECD-DAC), with significant Tamil diasporas in their capitals, are troubled by the humanitarian situation in a small strip of land in the northeast controlled by the LTTE where civilians trapped by the LTTE as being killed on a daily basis in the crossfire. The French and British Foreign Ministers visited the island recently after Sri Lanka denied a visa to the Swedish Foreign Minister. Their visit was to persuade the government to have a humanitarian pause for help for trapped civilians in the conflict zone but they returned empty handed. The government had insisted that the LTTE would use such a humanitarian pause to strengthen itself as it has done in the past. But the immediate humanitarian crisis and the fact that there are significant Tamil diaspora groups in many OECD-DAC counties and that they have been holding protests may be only part of the problem with releasing an IMF loan. There is also the question of the fungibility of aid and the uses to which an IMF loan may be put by the Sri Lankan government.

If the IMF loan sought is US\$1.9 billion and the Sri Lankan government’s defense expenditure is US\$1.6 billion, the question of the fungibility of aid or the ability to transfer donor resources to non-targeted expenditure – a problem as old as foreign aid itself – inevitably arises at this time. The question remains – will an IMF loan subsidise the military machine of the government given fungibility? It is then arguable that conditionalities on an IMF loan should relate not only to immediate humanitarian conditions to assist suffering civilians in the conflict but also extend to a sustainable solution and good governance for conflict de-escalation.

In the past, western donors have worked in tandem with each other and offered carrots and wielded sticks at successive Sri Lanka government to encourage peace and reconciliation. Thus, for instance, the peace process that ran between 2001 and 2007 between the Sri Lankan government and the LTTE was sweetened by the “international community” with the promise of US\$4.5 billion that was pledged at the Tokyo Donor conference in 2003. The peace at reconstruction was to be bought and overseen by four Co-Chairs of the Peace Process –Norway, the official peace facilitator at the time; Japan, Sri Lanka’s largest bilateral donor; the United States; and the European Union.

New Asian Donors: China and India in Sri Lanka

The current international aid configuration in Sri Lanka reflects shifting structural dynamics in the international development architecture in the context of the critique of the Western aid system in the global south, and the emergence of new Asian donors, particularly China and India. Have these two Asian donors increasingly rendering the established international aid architecture irrelevant ?

P.S.

From Lines Magazine.

<http://lines-magazine.org/?p=813>