

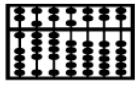
# A METHODOLOGY FOR ASSESSING THE IMPACT OF LOCAL HIRING AND LOCAL PROCUREMENT BY DEVELOPMENT PARTNERS

Peace Dividend Trust, October 2011

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## EXECUTIVE SUMMARY

When development partners set up offices and undertake projects in fragile states they hire local staff and procure goods and services from the local market. These activities mean that a partner or group of partners can become an extremely important source of demand in the local economy, particularly while that economy is recovering from conflict and problems with stability deter other potential market actors.

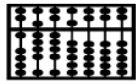
This can have negative consequences for local capacity and the local market when partners' demands exceed local supply. For example, demand for skilled labour often outstrips supply in fragile states and can lead to salaries being driven up by competition beyond what is affordable for national governments. Development partners can also have a positive effect through their hiring and procurement if they take advantage of excess capacity in the economy. For example, money spent on construction services, which have large inputs from unskilled labour, can inject much-needed cash into the local economy, create jobs and help to stimulate demand.

The countries of the G7+ have identified hiring and procurement policies of development partners as a critical gap in understanding and practice. Further examination is required in order for development partners to avoid doing harm and maximise positive effects. Once a donor or group of donors understands its impact on local markets for labour, goods and services, they can, in partnership with national governments, develop appropriate policy responses based on empirical evidence. For example, a survey of donor remuneration practices in Afghanistan clarified problems with inconsistencies, distortions and demotivation. The survey was linked to a policy process involving and supported by a wide range of stakeholders and is leading to policies that will create transparent and coherent pay scales for all employees of the Government of Islamic Republic of Afghanistan.

This methodology outlines how development partners and national governments can undertake joint in-country reviews of the impact of partner hiring and procurement practices. Table 0.1 summarises the different impacts considered by the methodology. Many of the issues presented in this methodology will be familiar to those working in any development context and are relevant to many markets, not just those in fragile states. What makes this methodology most appropriate to fragile states is that development partners are much more important as employers and buyers in the local market and the local market has the capacity to provide much less. Hence the impact of the wages offered and resources used by development partners is likely to be much greater. In addition, fragile states are likely to experience greater fluctuations in their labour force and ability to provide goods and services as conflict or tension flares up and dies down. This means it is imperative for development partners to monitor where bottlenecks may be arising and where the spare capacity is available in the economy so that they can adjust their practices to avoid undue distortions and take advantage of a country's strengths.

In order to implement this methodology development partners and national governments must:

1. **Agree on motivation for applying the methodology.** In order to justify the cost of the methodology, development partners and national governments need to understand how the information generated will be used to influence or change behaviour.
2. **Define the scope of the application of the methodology.** It is unlikely, given the time and resources required, that the methodology will be applied in full in each country. Factors affecting the scope include levels of political will and profile of particular issues.
3. **Review available data.** Use previous research to avoid duplication of effort and guide data collection priorities.
4. **Undertake additional data collection.** Surveys should be designed based on gaps in existing data. A summary of potential surveys to collect data is given in Table 2.1
5. **Analyse data and formulate recommendations.** Data should be analysed with a view to formulating recommendations that are focussed on influencing behaviour.
6. **Embed monitoring systems.** Monitoring data over time will inform partners and governments whether policies are working. This is particularly important in fragile states where economic conditions can change very rapidly.



**Table 0.1: Summary of impacts of development partners' hiring and procurement**

<b>Impact of hiring by development partners</b>		
<b>Type of impact</b>	<b>Brief description of impact</b>	<b>Important factors to consider</b>
<b>Impact on local capacity</b>	International organisations recruit qualified personnel away from local institutions by offering higher wages. This can lead to low capacity in national institutions and the local private sector and skilled workers working below their skill level. Such effects may be offset if development partners build the capacity of their employees and these employees return to national institutions.	<ul style="list-style-type: none"> <li>• UN pay scales are extremely influential.</li> <li>• Some partners have policies to avoid recruiting civil servants.</li> <li>• Often partners use top-ups to augment civil service salaries.</li> <li>• Other important factors in local capacity include emigration and size of the local private sector.</li> </ul>
<b>Harnessing the capacity of the diaspora</b>	Attracting skilled members of the diaspora to their home country can help to address the severe shortage of skilled workers. However tensions can arise based on the history of the conflict and salary difference.	<ul style="list-style-type: none"> <li>• Supply of skills must match local demand.</li> <li>• Returnees must have knowledge-transfer skills.</li> <li>• Local employees must have the capacity to absorb skills.</li> </ul>
<b>Impact on wage inflation</b>	When skills are in low supply people with these skills can command a premium. This pushes up salaries. Wage inflation may also spill over into the wider market if partners are large employers of unskilled labour. Wage inflation makes the local private sector less competitive and makes it hard for governments to maintain sensible budget policies.	<ul style="list-style-type: none"> <li>• Wage-setting policies need to be flexible to adapt to sudden changes.</li> <li>• Outsourcing services can help to reduce inflation.</li> <li>• Wage inflation will also be affected by mobility within the labour market and prevailing inflation in the local economy.</li> </ul>
<b>Money goes directly into the economy</b>	Hiring local staff injects cash directly into the local economy. Staff spend their wages on goods and services in the local economy and benefits will often be felt by the staff member's immediate and extended family. Employing a large number of local staff can lead to a negative shock when a partner leaves.	<ul style="list-style-type: none"> <li>• The health of the local economy will affect decisions to spend or save wages.</li> <li>• Negative shocks can be mitigated by slow phasing out and skills transfer.</li> </ul>
<b>Impact of procurement by development partners</b>		
<b>Type of impact</b>	<b>Brief description of impact</b>	<b>Important factors to consider</b>
<b>Money goes directly into the economy</b>	Procuring goods and services from local businesses can help to stimulate economic development and inject cash into the local economy. In addition profits from contracts are reinvested in local businesses.	<ul style="list-style-type: none"> <li>• Levels of 'tied aid'.</li> <li>• Preference policies for local firms.</li> <li>• Approach to managing risk in procurement in crisis situations.</li> <li>• Ability of local businesses to bid for international contracts.</li> </ul>
<b>Distorting the market</b>	The local market may become structured to serve the needs of development partners. This could distract from developing important manufacturing industries and could also lead to a negative shock on departure. Procurement practices may reduce competition if procurement officers stick only to businesses with a track-record with international organisations.	<ul style="list-style-type: none"> <li>• Transferability of skills and equipment.</li> <li>• Predictability of procurement plans.</li> <li>• Qualification criteria for bidding.</li> </ul>
<b>Inflation</b>	If a particular resource is scarce in the local market, procurement of that resource in large quantities may lead to inflation.	<ul style="list-style-type: none"> <li>• Prevailing market conditions and seasonal variation.</li> <li>• Share of market being procured.</li> </ul>
<b>Capacity of the local private sector</b>	Doing business with international organisations can increase capacity and productivity of a business as it increases its experience and acquires new skills. If partners provide a predictable level of income this gives businesses the incentive to invest in their own capacity and build up reliable supply chains.	<ul style="list-style-type: none"> <li>• Levels of training and feedback offered by procurement officers.</li> <li>• Need for specific capacity in the long term.</li> </ul>

## 1. Introduction

The International Dialogue on Peacebuilding and Statebuilding was established as an outcome of the High Level Forum on Aid Effectiveness in Accra in 2008 and provides a new opportunity for policy discussions that can improve national and international efforts in fragile and conflict-affected situations. It brings together partner countries, donors and international organisations and is guided by three overarching objectives:

1. to share peacebuilding and statebuilding experiences;
2. to gather and discuss good practices and constraints to delivering effective international assistance in support of peacebuilding and statebuilding; and,
3. to build consensus on a set of realistic peacebuilding and statebuilding objectives.

The first meeting of the International Dialogue took place in Dili, Timor-Leste in April 2010. The meeting produced the Dili Declaration, which identifies a set of peacebuilding and statebuilding goals, challenges to achieving these goals, and actions that can help accelerate progress on peacebuilding and statebuilding. The issue of hiring and procurement policies and practices of development partners and their impact on the local economy was identified as a critical gap in understanding and practice and thus warranted further examination. It was decided that this would be achieved through in-country reviews conducted jointly by national governments and development partners.

This methodology is intended for use as a guide for development partners and national governments that want to undertake these joint in-country reviews of hiring and procurement by development partners. The impact of hiring and procurement by development partners is considered only in relation to their impact on the local economy, labour market and capacity. The implementation of a policy should be considered in terms of its full costs and benefits; however, this is beyond the scope of this project.<sup>1</sup>

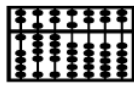
This methodology is designed to assess impact; it is not designed to offer particular solutions. However, the data collection and analysis undertaken as part of this methodology should equip the policy-maker with the right tools to develop context-specific responses.

Many of the issues presented in this methodology will be familiar to those working in any development context and in many markets, not just those in fragile states. What makes this methodology most appropriate to fragile states is that development partners are much more important as employers and buyers in the local market and the local market has the capacity to provide much less. Hence the impact of the wages offered and resources used by development partners is likely to be much greater. In addition, fragile states are likely to experience greater fluctuations in their labour force and ability to provide goods and services as conflict or tension flares up and dies down. This means it is imperative for development partners to monitor where bottlenecks may be arising and where the spare capacity is available in the economy so that they can adjust their practices to avoid undue distortions and take advantage of a country's strengths.

The report is structured as follows. Section 2 outlines the process of applying this methodology and outlines its limitations, particularly with respect to available data. The description of the methodology begins in Section 3 by first considering the impact of hiring by development partners. Section 4 goes on to consider the impact of procurement. For each aspect of impact considered, the methodology first lays out the potential impact of development partners and then describes factors that affect this impact, both in terms of partners' policies and in terms of the wider context. A table then takes the reader through the questions that need to be asked in order to assess impact in each area, potential sources of data that might answer these questions and suggested approaches to analysis. Section 5 concludes and presents a summary of the data collection effort required to follow this methodology.

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<sup>1</sup>In particular, many interviewees were concerned with the impact of local hiring and procurement on the effectiveness, timeliness and cost of operations. For a consideration of the impact of local procurement on operational effectiveness see Peace Dividend Trust (August 2010) *Risk and Opportunity: Local Procurement in Conflict-Affected and Fragile States*.



## 2. Research process and data considerations

### 2.1 Deciding to apply the methodology

When deciding whether to apply this methodology, it is important for governments and development partners to weigh the likely benefits of gaining a deeper understanding of partners' impact with the costs of data collection. These costs come from both the need to hire extra resources and the time taken by existing staff to contribute to data collection. In order to justify these costs, development partners and national governments need to understand how the information generated will be used to influence or change behaviour.

Data collected using this methodology can be used both to identify where new policies might be required and to help develop these policies, so that the negative effects of partners' hiring and procurement practices and the positive effects are maximised. Annex 3 highlights a case study from Afghanistan where the motivation for collecting data on the impact of partners' remuneration practices was clearly linked to a policy process involving and supported by a wide range of stakeholders. The data clarified the problems with current remuneration practices and is leading to policies that will increase cooperation between partners and create transparent and coherent pay scales for all employees of the Government of Islamic Republic of Afghanistan.

It should be stressed that this methodology addresses only the impact of partners' hiring and procurement practices in fragile states. In particular, this methodology is not concerned with evaluating the impact or effectiveness of projects funded by partners. In addition, in contexts other than fragile states, many of the impacts discussed below are likely to be less serious in more resilient economies where partners are not such significant players in the market.

### 2.2 Defining the scope

This methodology addresses a broad range of issues and requires a wide range of data. It is unlikely, given the time and resources required, that the methodology will be applied in full in each country. Therefore application of this methodology should begin with defining the scope of application through consultation between development partners, the national government and other key stakeholders from the local market, e.g. private sector representatives. Parameters that will define the scope include:

- **Cooperation.** This is probably the most crucial factor in the success of the methodology; much of the impact described in this methodology is dependent on the cumulative effect of development partners within a country. The most useful assessments will come when development partners in a country cooperate in this process and agree to share their data and give access to their staff. Priority should be given to those areas where development partners and government are most willing to share their data. Governments and partners may wish to restrict the scope of the methodology to particularly cooperative ministries or sectors of the business community.
- **Profile of issues.** Particular issues may be of greater interest in a particular context due to the history or current situation of the country. For example, a country may have a history of hyperinflation or emigration of skilled workers. Or a country might have a particularly high number of donors undertaking similar activities, e.g. reconstruction.
- **Other available research.** Where evidence already exists of particular impact it is clearly unnecessary to apply this methodology. However, research may indicate that the impact of development hiring or procurement practices is likely without providing definitive or quantifiable evidence. In this case application of the methodology will help to assess the extent of any impact and whether it is negative or positive overall.

Consultation with key stakeholders is also important for understanding the political implications and likely challenges of requesting data. Data on remuneration is likely to be particularly sensitive. Government ministries may fear cuts if disparities in remuneration are exposed, donors may fear risk to reputation or pressure to change practices, and private businesses sub-contracted by donors may regard this as sensitive commercial information. Even without political sensitivities, all data collection takes extra time and resources and this must be acknowledged and discussed.

For each type of impact, the most important questions to collect data on are highlighted with an asterisk (\*) in the relevant tables in Sections 3 and 4. These are the questions either that identify whether an impact is occurring at all, or those questions deemed of highest priority by stakeholders interviewed for this research (see Annex 2 for more details).

## 2.3 Reviewing available data and identifying need for new surveys

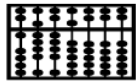
Once the scope has been defined, a thorough literature and document review should be conducted. This will determine the extent to which new data collection will need to take place. There are very few consistent data sets already in existence and in the public domain that contain data on fragile states - the exceptions to this are United Nations (UN) pay scales<sup>2</sup> and World Bank indicators. Hence this methodology will almost certainly require the collection of new data through surveys. These surveys are listed in Table 2.1.

**Table 2.1: Surveys for gathering data for the methodology**

Target of survey	Factors affecting feasibility of survey	Identifying the sample
National staff of development partners	Access will depend on level of cooperation of development partners.	Staff lists will need to be provided by development partners. Some subsectors, such as the diaspora, will be more difficult to identify.
National civil service staff	Access will depend on level of cooperation with national government. It may be best to concentrate on particular ministries.	Staff lists will need to be provided by relevant ministries. Some subsectors, such as the diaspora, will be more difficult to identify.
HR directors of development partners, national civil service and other major employers	Access will depend on level of cooperation of development partners, national government and private sector. Data on local hiring and wages may not be easy or possible to access and guarantees of anonymity will need to be given.  Opinions will be easier to collect than quantitative data.	Appropriate staff lists will need to be provided by development partners, national civil service and other major employers.
Local businesses	Easy to access and often willing to participate in surveys but may not keep accurate records of past contracts or levels of employment.  Opinions will be easier to collect than quantitative data.	Obtain lists through local business directories or chambers of commerce.
Procurement officers of development partners	Access will depend on level of cooperation of development partners. Data on local procurement may not be easy or possible to access and guarantees of anonymity will need to be given.  Opinions will be easier to collect than quantitative data.	Appropriate staff lists will need to be provided by development partners.
International businesses employing local staff	Level of cooperation will vary according to how engaged these businesses have been with national governments and development partners.  Opinions will be easier to collect than quantitative data.	List of appropriate businesses obtained in consultation with development partners and national government.

Each survey will touch on several different aspects of development partner impact as described in the methodology. Available data will vary from country to country and so a thorough review of

<sup>2</sup>UN pay scales are set based on annual surveys with a group of 'desirable employers' in the local area. A local committee nominates the group of desired employers. Care is taken to assign salary levels based on skills required to do the job rather than job titles or seniority.



country-specific reports and requests for information from relevant ministries and development partners should be made before embarking on a survey to provide data for the methodology.

## **2.4 Undertake data collection**

Surveys should be designed based on gaps in the data. Before roll-out surveys should be reviewed by key stakeholders and piloted with a small sample to ensure that they are collecting the necessary information.

Surveys are likely to receive a better response if they receive a strong mandate from a government ministry, senior politician or influential donor. If possible, surveys should be sent out from the offices of a government ministry or donor.

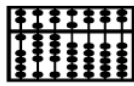
## **2.5 Data analysis and formulation of recommendations**

Once data collection has been completed, the data should be analysed as outlined in the methodology. Because the data is specific to the local context it will enable the formulation of country-specific solutions to enhancing positive impact and mitigating negative impact.

## **2.6 Embedding monitoring systems**

While this methodology is designed to provide a snapshot of impact at a given time it should also be used as a prompt for development partners to consider what information they should be collecting on a regular basis. Monitoring the data over time will inform partners and national governments whether policies are working and how they should be changed. Economic conditions in fragile states can change quickly and so partners should, at a minimum, regularly review their importance as employers and buyers in the local market. This means comparing the number of skilled and unskilled workers they employ to the size of the local labour market and comparing levels of procurement to available levels of goods and services. Partners should focus on collecting data on areas where harmful impact have been identified.

Again, cooperation amongst development partners and between partners and government will be key to the success of on-going monitoring efforts. Understanding the cumulative effect of development partners' hiring and procurement is crucial to developing appropriate policy responses.



### 3. Impact of partners' hiring policies and practices

When development partners set up offices in developing countries they will often seek to hire local staff to run the office and implement projects both inside and outside national governments. Development partners employ nationals as staff and on short-term contracts as consultants. Hiring locally is commonly seen as having the dual benefit of keeping costs low and providing valuable information about the local context. Indeed, hiring locally is also seen as a way of improving relations between development partners and the local community (Carnahan 2006).

#### 3.1 Capacity of the local labour market

##### Potential impact

'Brain Drain' is probably the most prominent concern related to development partner's hiring practices. This can occur when international organisations recruit qualified personnel away from local institutions by offering higher wages (Carnahan 2006, Secretary General on Peacekeeping 2009, Birdsall 2007). People may also choose to acquire skills that suit the needs of these organisations rather than the needs of national institutions (Carnahan 2006, Birdsall 2007). This has three negative effects.

The first is that national governments find it difficult to attract the people they need to build a strong civil service. Underscoring this notion is evidence that suggests that a high number of donors in a country has a negative impact on the administrative capability in that country (Rajan 2005, Knack 2007). In post-conflict and fragile states the pool of skilled workers is often very small and this limits the capacity for national governments to develop.<sup>3</sup>

The second is that skilled workers may be attracted into jobs that are below their skill level. Some anecdotes have been reported of university graduates being hired as chauffeurs because they speak good English. This means that not only is the national government missing out on valuable skills, those skills are actually decaying (Carnahan 2006).

The third is that not only does the national government find it difficult to attract skilled workers, but the local private sector does as well. This could harm the long-term growth prospects of the local economy.

However, it has also been argued that recruiting local staff could actually increase local capacity (UNDP 2009). This might be formally through staff training programmes or informally through the experience of working to international standards. If these staff then return to local institutions this could increase the pool of skills available to the local government or private sector. Development partners may also help to keep skilled workers in a country if there is brain drain to other countries in the region with better economic conditions.<sup>4</sup>

Carnahan (2006) argues that there is little evidence of national staff employed by UN missions moving to the government or private sector and that many continue to seek work with international organisations. In contrast, many development partners have anecdotes of former employees now holding senior positions in national governments.

##### Factors affecting impact

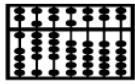
Clearly, wages set by development partners will affect the level of brain drain experienced in a country. The UN is often the first actor to set up shop in a country, and so wages set by the UN often become a benchmark with salaries offered by development partners generally being

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<sup>3</sup>There are reports that many UN missions are rarely able to fill all positions with people of the required skill level so it is possible for a mission on its own to drain the local economy of its most qualified people (Carnahan 2006).

<sup>4</sup>Interviews carried out in Sierra Leone by Peace Dividend Trust identified brain drain to other West African countries as more significant than brain drain to international organisations within Sierra Leone.





slightly higher and international non-governmental (INGOs) being slightly lower (Carnahan 2006). UN wages are set according to the Fleming principle that salaries should be “among the best prevailing local conditions” and so it is likely that the best wages are to be found within development partners (Consultative Committee on Administrative Questions 2006).<sup>5</sup> The impact of wage setting also depends on regional variations in wages. Some partners set uniform pay scales for a whole country, which results in wages outside the capital being even more out of line with local pay.

Many development partners try to mitigate brain drain effects by avoiding hiring people currently working for the civil service. This may be explicitly laid out in their hiring policies or acknowledged implicitly by country offices. Anecdotal evidence suggests that despite this, many ex-civil servants do end up working for development partners. Interviewees expressed concerns that such policies might prevent skilled workers from working for the civil service in the first place. It was also pointed out that such policies still do not prevent depletion of skilled workers in the private sector. Some interviewees suggested that responses to brain drain effects should concentrate on increasing the supply of skilled labour rather than reducing its demand.

Some development partners also use funds to top-up civil servants wages to make them more competitive, however the effectiveness of this approach is unknown and may contribute to wage inflation (see Section 3.3) (Birdsall 2007, OECD 2010). These policies are often not consistently and transparently applied and so while it may be the case that those receiving the top-ups are retained, considerable resentment can be generated amongst colleagues.

Donors are likely to have a more beneficial impact on local capacity if the training they offer employees is designed with input from partner governments about their needs, and if it forms part of a broader capacity-building strategy. Nelson (2006) cites evidence that training is most effective when priorities are determined at the institutional, rather than individual, level and is driven by demand from the employer (Nelson 2006).

Development partners' impact on local capacity will also be affected by the demand for skilled workers from the private sector, levels of emigration and the number of skilled workers in the local labour market.

## 3.2 Harnessing the capacity of the diaspora

### Potential impact

Development partners have recently become more interested in hiring members of the diaspora as a way of increasing capacity within a country. Attracting skilled members of the diaspora to their home country can help to address the severe shortage of skilled workers in fragile states (as discussed above). This impact could also have a multiplier effect if members of the diaspora are able to transfer their skills to locals. Members of the diaspora can combine understanding of the local context with that of the donor, which can make them valuable assets beyond the skills that they bring. Research by the Partnership for Democratic Governance (PDG) (2010) found that members of the diaspora tended to be more highly skilled than locals but this was off set to a degree by their lower ability to navigate local bureaucratic and political structures.

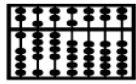
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<sup>5</sup>The Fleming Principle dates back to when the UN was first set up. At that time competitive salaries were necessary as it was operating in different countries than it does today.

**Table 3.1: How to assess the impact of development partner hiring on capacity of the local labour market**

Type of impact	Questions to assess impact	Suggested sources	Suggested benchmarks and analysis
<b>Development partners are depleting the pool of skilled workers</b>	*How many skilled workers are there in the local labour force?	<ul style="list-style-type: none"> <li>Local university and school records of numbers and types of graduates.</li> <li>Survey national government employees for skill level.</li> <li>Survey development partners, national government and other desirable employer HR directors for their demand for skilled workers and their ability to fill vacancies.</li> </ul>	<p>These data sets can determine the size of the pool of skilled workers. The appropriate measure for 'skilled' will vary according to the country context but the equivalent of a high school certificate and a bachelor's degree are useful. Comparing skills of employees in different organisations can be very difficult as it is common for people to be promoted due to length of service or social standing rather than ability to perform the job. Competency-based measures are also useful though much more difficult to assess.</p> <p>It is important to split skills out by sector as some may be more in demand than others (e.g. accountancy skills are often in high demand).</p>
	*How many skilled nationals do development partners employ?	<ul style="list-style-type: none"> <li>Development partner employment records.</li> </ul>	These data sets should determine how important development partners are in the competition for skilled nationals.
	How many skilled nationals does the civil service want to employ?	<ul style="list-style-type: none"> <li>Survey civil service HR directors.</li> </ul>	If employers other than development partners inside or outside the country are employing skilled nationals on a large scale then the behaviour of development partners may not have much impact on the local labour market.
	What are the other key employers for skilled workers inside the country?	<ul style="list-style-type: none"> <li>Survey of university students.</li> <li>Survey of skilled development partner employees.</li> </ul>	Suggested benchmark: if development partners are employing more than 10% of the estimated pool of skilled workers then their practices are likely to be affecting the local labour market.
	How many skilled workers are migrating?	<ul style="list-style-type: none"> <li>Official migration statistics.</li> <li>Immigration statistics of popular destination countries.</li> </ul>	
	Do development partners offer better wages than the national government?	<ul style="list-style-type: none"> <li>UN salary survey.</li> <li>National government pay scales.</li> <li>Development partner pay scales.</li> <li>Pay scales of other desirable employers.</li> </ul>	Comparing wages offered by development partners with those offered by the national civil service and other desirable employers will determine how attractive development partners are as employers in the skilled labour market. Benefits such as pensions and healthcare should be included in this comparison. Healthcare in particular is a major benefit for UN staff.
	What other benefits do development partners offer?	<ul style="list-style-type: none"> <li>Development partner HR policies.</li> </ul>	Even if development partners have significantly better compensation packages than other employers, this will only be significant if they are also large employers (see box above).
	How are these valued by employees?	<ul style="list-style-type: none"> <li>Survey of development partner employees.</li> </ul>	
	How many development partner employees are former civil servants?	<ul style="list-style-type: none"> <li>Survey of development partner employees.</li> </ul>	This will demonstrate whether partner policies to avoid hiring civil servants are working.

Type of impact	Questions to assess impact	Suggested sources	Suggested benchmarks and analysis
<b>Skilled workers working below their skill-level</b>	Do development partners offer higher wages than the national civil service, even for less skilled jobs?	<ul style="list-style-type: none"> <li>National civil service pay scales.</li> <li>Development partner pay scales.</li> </ul>	These data sets will determine how attractive a low-skilled job with a development partner would be for a skilled national.
	What is the skill level of those applying for less skilled jobs with development partners?	<ul style="list-style-type: none"> <li>Survey HR directors of development partners.</li> </ul>	Comparing salary scales will determine whether, in fact, skilled nationals are taking lower skilled jobs with development partners.
	*How often do development partner employees use their skills?	<ul style="list-style-type: none"> <li>Survey of development partner employees.</li> </ul>	Comparing skills of employees in different organisations can be very difficult as it is common for people to be promoted due to length of service or social standing rather than ability to perform the job.
	What are the skills gaps in the local labour market?	<ul style="list-style-type: none"> <li>Civil service assessments (World Bank).</li> <li>Survey of HR directors of development partners, national government and major private sector employers.</li> </ul>	<p>Comparing the scale of this phenomenon with skills needed in the economy will determine how serious this practice is, if in fact it exists.</p> <p>Skilled workers may be in low skilled jobs because there is low demand for their particular skill.</p>
<b>Development partners increase local skills</b>	What skills are the national employees of development partners learning?	<ul style="list-style-type: none"> <li>Survey of development partner HR staff.</li> <li>Survey of development partner national staff.</li> </ul>	These data sets, combined with data on local skills gaps, will determine whether the skills that national staff are learning are in demand in the local labour market.
	*How many skilled workers leave or intend to leave development partners to work in national institutions?	<ul style="list-style-type: none"> <li>Records of staff turnover at development partner.</li> <li>Survey of development partner national staff.</li> </ul>	These data sets will determine whether nationals trained by development partners are actually re-entering the local labour market. If there is a skills transfer from development partners to the local economy, understanding likely destinations of employees will help to determine whether staff are moving to the national civil service or into the private sector.
	How many people working for the national civil service have worked for development partners in the past?	<ul style="list-style-type: none"> <li>Survey of national civil service staff.</li> </ul>	The benchmark for this will depend on the scale of hiring by development partners and the scale of skills-gaps in the local labour market.
<b>Civil servants are retained through salary top-ups</b>	Are salary top-ups retaining staff?	<ul style="list-style-type: none"> <li>Staff turnover records of those with salary top-ups.</li> </ul>	These data sets will determine whether salary top-ups increase the likelihood of a skilled worker remaining in the civil service.
	Are salary top-ups causing resentment amongst colleagues?	<ul style="list-style-type: none"> <li>Survey of national civil service staff.</li> </ul>	These data sets will determine the extent of any negative effects of salary top-ups. Whether top-ups are considered fair and a reward for good work or are considered the result of patronage and are demotivating and tarnish the reputation of the donor.
	*Are salary top-ups consistently and transparently applied?	<ul style="list-style-type: none"> <li>Survey of national civil service staff.</li> <li>Survey of HR managers.</li> </ul>	



Unlike expatriates, members of the diaspora may stay for a long period of time and even re-settle back in their home country increasing the local skills-base permanently. This makes them suitable for filling long-term positions that may be unsuitable for expatriates. Simultaneously, members of the diaspora often come from countries with higher wages and standards of living and so can find local wages unsatisfactory. This can lead to interest in only higher-paid positions with international organisations (see discussion of donors and 'brain drain' issues in Section 3.1) and may be a contributing factor to wage inflation (see Section 3.3).

As well as being paid more, returnees can sometimes exhibit disdain and frustration for local people and systems, which exacerbates tensions. If returnees are perceived to have avoided the hardships of conflict this can also cause problems (Brinkerhoff 2008).

### **Factors affecting impact**

Little is published on hiring the diaspora by development partners themselves. The PDG (2010) gives a useful overview of how contributions of diasporas to fragile states can be maximised and some of these are also relevant to development partners.

Most importantly, the supply of skills that members of the diaspora bring must match local demand. Anecdotes of members of the diaspora being hired to do jobs that many locals could do, or finding that their skills are not valued are common (PDG 2010). Expectations are also important; if the salary, security and career expectation of individuals do not match up with reality then individuals are more likely to leave or fail to apply or transfer their skills.

In order to transfer their skills, members of the diaspora need also to have knowledge transfer skills and be given the time and mandate to train colleagues (IOM 2005). However there is empirical evidence that these conditions for effectiveness are rarely met (Brinkerhoff 2008). It should not be assumed that members of the diaspora will be better at transferring knowledge just because they have a link with the homeland. If returnees do not intend to remain in the homeland long-term then the emphasis on knowledge transfer is even more important and it is less appropriate to hire them for permanent positions.

Making the most of the skills that members of the diaspora bring requires a certain level of administrative structure that may not exist in fragile states. Hence development partners should consider whether there is sufficient capacity to absorb these skills before recruiting members of the diaspora to fill skill gaps (Beschel 2004).

As the successful use of skills of the diaspora are so dependent on individuals' personal circumstances (the situation in their home country and the networks they are able to fit into in their home country) any programme to recruit the diaspora back to the home country is likely to run into unique obstacles. Hence regular monitoring programmes and adaptation based on feedback is crucial to success (PDG 2010).

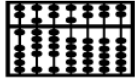
### **3.3 Impact on wage inflation**

#### **Potential impact**

When skills are in low supply, people with those skills can easily command a premium. High wages offered by development partners to skilled nationals may also spill over into the wider labour market and lead to wage inflation if they are significant employers of semi-skilled or unskilled labour (Carnahan 2006). In this case a wide range of other employers may need to offer higher wages to attract staff at all levels.<sup>6</sup> It is easy for partners to allow local salaries to rise as this spending is often such a small part of the budget.

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<sup>6</sup>This can happen even without full employment if the chances of getting a highly paid job with an international organization are high enough that a person would rather remain unemployed and leave open the chance of highly paid employment rather than take the low-wage job.



Wage inflation makes the local private sector less competitive regionally and internationally and makes it more difficult for the national government to maintain sustainable budget policies. The difficulty faced by some governments to pay high enough wages to attract skilled people has meant in some cases that governments ask donors to fund staff positions through technical assistance budgets, which are much larger than the budgets for hiring civil servants. For example, in Sierra Leone, many local consultants in ministries reportedly become operational staff. Such practices create a parallel civil service structure that is difficult to sustain in the long-term and causes tension and motivational problems due to differences in pay between staff and consultants (OECD 2010).

### **Factors affecting impact**

Development partners agree that it is good practice not to offer the best wages in the local area but there is no publicly available data on whether this actually happens. It is important for any policy around wage-setting to be flexible as the impact of these policies will change over time as the scale of hiring and the type of personnel hired by international organisations changes. The level of top-ups offered by development partners to retain skilled civil servants (see Section 3.1) may also have an inflationary impact.

The level of outsourcing to local companies by a development partner can make a big difference to the impact of local hiring on wage inflation. Local contractors will often hire local staff at or near market wages and so wage inflation is reduced. Many UN missions have outsourced cleaning and security contracts and this has led to both more locally appropriate wages being paid and has encouraged the development of some small- and medium-sized enterprises (Carnahan 2006).

The level of wage inflation will also be affected by mobility within the labour market of a country or region, the scale of hiring by international organisations and the prevailing level of inflation in the local economy.

**Table 3.2: How to assess the impact of development partner hiring on harnessing the capacity of the diaspora**

Type of impact	Questions to assess impact	Suggested sources	Suggested benchmarks and analysis
<b>Diaspora increases local capacity</b>	*What skills are members of the diaspora bringing back to the country?	<ul style="list-style-type: none"> <li>• Survey of development partner HR directors</li> <li>• Survey of returned diaspora.</li> </ul>	These data sets will determine to what extent the diaspora are returning with skills in demand in the local economy.
	*What are the skills gaps in the local labour market?	<ul style="list-style-type: none"> <li>• Civil service assessments (World Bank)</li> <li>• Survey of HR directors of development partners, national government and major private sector employers.</li> </ul>	
	Do members of the diaspora have knowledge transfer skills or experience?	<ul style="list-style-type: none"> <li>• Survey of returned diaspora.</li> </ul>	These data sets will determine the likely extent to which the diaspora are able to transfer their skills to local colleagues.
	Do national staff feel that they have learned new skills from returned members of the diaspora?	<ul style="list-style-type: none"> <li>• Survey of national staff of development partners</li> <li>• Survey of national civil service employees.</li> </ul>	This data will also help to identify barriers to knowledge transfer and amend programmes for diaspora recruitment if necessary.
	Do members of the diaspora feel that they are able to apply or transfer their skills? Why?	<ul style="list-style-type: none"> <li>• Survey of returned diaspora.</li> </ul>	
	Do members of the diaspora feel supported?	<ul style="list-style-type: none"> <li>• Survey of returned diaspora.</li> </ul>	
	What are the expectations of members of the diaspora?	<ul style="list-style-type: none"> <li>• Survey of returned diaspora.</li> </ul>	
	How long do members of the diaspora plan to stay?	<ul style="list-style-type: none"> <li>• Survey of returned diaspora.</li> </ul>	This data will determine whether it is best for returnees to be in permanent or time-bound positions. It will also indicate the timescale over which knowledge transfer will need to take place.
<b>Diaspora creates local tensions</b>	*Do national staff view members of the diaspora as bringing extra skills?	<ul style="list-style-type: none"> <li>• Survey of national staff of development partners</li> <li>• Survey of national civil service employees.</li> </ul>	These data sets will determine to what extent social factors are helping or preventing the diaspora from contributing and transferring their skills to the national civil service or national staff employed by development partners.
	Are members of the diaspora resented by national staff?	<ul style="list-style-type: none"> <li>• Survey of national staff of development partners</li> <li>• Survey of national civil service employees.</li> </ul>	

**Table 3.3: How to assess the impact of development partner hiring on wage inflation**

Type of impact	Questions to assess impact	Suggested sources	Suggested benchmarks and analysis
Are development partners contributing to wage inflation?	*Is there wage inflation in the skilled labour market?	<ul style="list-style-type: none"> <li>UN salary survey.</li> <li>Development partner and national civil service pay records.</li> </ul>	These data sets will determine whether there is a wage inflation problem. Salaries should be assessed at at least two points in time to get an estimate of inflation. Analysis should also be carried out on different employment sectors.
	*Is there wage inflation in the unskilled labour market?	<ul style="list-style-type: none"> <li>Survey local businesses.</li> </ul>	
	*What is the prevailing level of inflation?	<ul style="list-style-type: none"> <li>International Monetary Fund statistics.</li> </ul>	It should be noted that prevailing levels of inflation in LDCs are typically very high and that it is common for wage inflation to be a few percentage points above the standard inflation index.
	How does the scale of local hiring by development partners compare to the size of the labour market as a whole?	<ul style="list-style-type: none"> <li>Development partner project employment records.</li> <li>National statistics/standard estimates by World Bank/UN agencies.</li> </ul>	Comparing the scale of hiring by development partners with the pool of available workers will determine how likely it is that development partners are contributing to wage inflation if absolute measures of wage inflation are not available.  Suggested benchmark: if development partners are employing more than 10% of the estimated pool of skilled workers then their practices are likely to be affecting the local labour market.
	How much outsourcing do development partners undertake?	<ul style="list-style-type: none"> <li>Development partner procurement records.</li> </ul>	This data will determine whether development partners are avoiding wage inflation by outsourcing services to the local market.
	How willing/able are local/regional workers to move for work?	<ul style="list-style-type: none"> <li>Survey local employers.</li> </ul>	This data will determine whether wage inflation could be mitigated by mobility of labour.
	How many technical assistance posts are funded within the national civil service? How many of them are actually filling permanent staff positions?	<ul style="list-style-type: none"> <li>Survey of national civil service staff.</li> <li>Development partner records.</li> <li>National civil service records.</li> </ul>	These data sets will determine whether wage inflation is affecting the government's ability to keep civil service salaries at a sustainable level.
	Are development partners topping up civil service salaries?	<ul style="list-style-type: none"> <li>Development partner records.</li> <li>National civil service records.</li> </ul>	There is no available benchmark to determine an acceptable level of technical assistance-funded posts or top-ups. However, as an example, in the Budget Department of the Ministry of Finance in Afghanistan, more positions are funded by technical assistance than are funded from the government's core recurrent budget.
Is this top-up increasing or decreasing?	<ul style="list-style-type: none"> <li>Development partner records.</li> <li>National civil service records.</li> </ul>		

### 3.4 Money goes directly into the economy through wages to local staff

#### Potential impact

Hiring local staff is the most direct way that a development partner injects cash into the local economy. Staff are paid wages which they can then spend on goods and services in the local economy. The benefits will also often be felt by the staff member's immediate and extended family as wages from international organisations are often well above that required to maintain a basic lifestyle in the local area.

However, development partners are often concerned that employing a large number of national staff will lead to a negative shock when they leave if many people have to be laid off.

#### Factors affecting impact

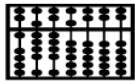
The impact of departure and withdrawing salaries from the local economy is highly dependent on the health of the local economy at the time of departure. Partners can mitigate the potential negative impact of withdrawing by phasing out their presence over a period of time and ensuring that staff have skills that are actually demanded by the local economy.

For example, personnel cuts in Bosnia and Herzegovina after withdrawal of the international peacekeeping deployment did not have a serious adverse economic shock. The key elements identified in this successful withdrawal were: investing in skills transfer, phasing out over an extended period, high academic and industrial training standards and consistently high GDP growth (Austrian Development Cooperation 2009).



**Table 3.4: How to assess the impact of development partner hiring on wages entering the local economy**

Type of impact	Questions to assess impact	Suggested sources	Suggested benchmarks and analysis
<b>Wages stimulate the economy</b>	*How much money is being spent in wages to national staff?	<ul style="list-style-type: none"> <li>• Development partner records.</li> </ul>	These data sets will determine how much money is entering the local economy through wages paid to national staff.
	How do local staff spend or save their money?	<ul style="list-style-type: none"> <li>• Survey of development partner national staff.</li> </ul>	Whether and how it is being spent, invested, or put aside in case of emergency should be analysed. This will determine to what extent wages are reducing poverty, encouraging investment, stimulating spending or providing resilience against future shocks.
<b>Labour market is distorted</b>	Do national staff of development partners have transferable skills?	<ul style="list-style-type: none"> <li>• Survey of development partner national staff.</li> </ul>	These data sets will determine the likely employment prospects of staff previously employed by development partners and can be used alongside data on the scale of hiring by development partners to estimate the size of any potential negative shock.
	Where is the growth in the private sector?	<ul style="list-style-type: none"> <li>• Survey of local businesses.</li> <li>• World Bank/national government reports.</li> </ul>	The extent to which skills of national staff match increasing demand from the private sector will reduce any negative shock.



## 4. Impact of procurement by development partners

Carrying out development projects typically requires a large amount of procurement. A range of goods and services is required, from construction materials and bottled water to training civil servants and designing accounting systems. While development partners have committed to increasing use of national systems for procurement,<sup>7</sup> many still procure using their own systems, particularly in fragile contexts. This section considers the potential impact of local procurement by development partners using their own systems.

### 4.1 Money goes into the local economy through contracts with local businesses

#### Potential impact

Procuring goods and services from local businesses can help to initiate economic development and inject cash into the local economy. This helps to create more local jobs and encourages investment. While foreign firms may hire local people, they will take a slice of the profit before subcontracting down. The profit from any contract goes to the foreign firm rather than being reinvested locally to buy equipment, train staff or build the capacity of the local firm to become more competitive and capable of meeting international procurement requirements (see Section 4.4).

However, local procurement does not automatically mean that money stays in the economy. This will be affected by whether owners do actually use profits for investment rather than banking it off-shore, the level of corruption in a country (and hence the proportion of money that is spent in the productive economy) and the capacity of the economy to deliver goods. Many fragile states have extremely weak manufacturing sectors and so many goods, even if procured locally, will be imported and thus not have such a high local impact.<sup>8</sup>

Smaller projects tend to see a greater proportion of money going into the local economy as these contracts are more accessible to local businesses. Such projects are also often favoured by development partners for their potential to create immediate employment opportunities at local levels in post-conflict settings (GTZ 2006).

#### Factors affecting impact

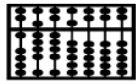
Historically, many development partners have 'tied' their aid, stipulating that a certain amount of aid money must be spent within the donor country. This practice is becoming less common, and increasingly procurement is being opened up to local, regional or international bidding. However the true extent of this is unknown due to poor data, particularly on the origin of procurement of technical assistance.

It is common for procurement policies to allow contracts to be tendered locally below a certain threshold and to offer a preference to local firms if they are within, for example, 10% of the price of the lowest tender. While clearly designed to increase local procurement, there has been no evaluation of whether these measures actually do so. Most interviewees cited risk aversion of procurement officers and capacity of local businesses as more important factors in reducing levels of local procurement than official procurement policy. It was also noted that while some procurement policies had provisions for emergency situations there was not clear guidance for on-going fragile situations.

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<sup>7</sup> Through the Paris Declaration on Aid Effectiveness (2005); Afghanistan Compact (2006); Accra Agenda for Action (2008) and Dili Declaration (2010), donors have committed to increasing local procurement.

<sup>8</sup> However, there may still be a positive local impact in terms of capacity-building (see section 4.4).



# *Peace Dividend* Trust

Building a Better Peace

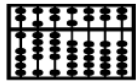
Probably the most well-known 'buy-local' policy is the US Government's Afghan First policy instituted in 2009 and then adopted by NATO in 2011. The impact of this policy is currently being evaluated. The results should be available towards the end of 2011.

Interviewees felt that the rules allowed for a large amount of local procurement and that there were provisions for favouring local markets, particularly in emergencies, but that many procurement officers are highly risk averse. This is often because they are held personally accountable when things go wrong. While local procurement can be risky, that risk can be manageable with appropriate monitoring for corruption and collusion amongst others. Partners' policies on accountability, designed for procurement in international markets, may be reducing levels of local procurement by cutting out many local businesses that do not have a track record or financial records of an international standard. A more flexible and actively managed approach to procurement risk where accountability requirements are relaxed if potential gains are large can both benefit the local economy and improve procurement objectives (Peace Dividend Trust 2010). The UN Practitioner's Handbook on Procurement outlines such a policy.

Levels of local procurement will also be affected by the ability of local businesses to compete for international tenders. Often they do not know where to learn about international contracts and may not understand what is required to prepare a bid. Beyond their technical capacity, local businesses can rarely access the credit required to complete a large order that will be paid on delivery. Partners' practices in terms of the size of contracts they put out to tender and structuring of payments will also determine the number of local businesses that win procurement contracts.

**Table 4.1: How to assess the impact of development partner procurement on money from contracts going into the local economy**

Type of impact	Questions to assess impact	Suggested sources	Suggested benchmarks and analysis
<b>Money stimulating the local economy</b>	*What is the total value of contracts going to local businesses?	<ul style="list-style-type: none"> <li>• Survey local businesses.</li> <li>• Development partner procurement records.</li> </ul>	These data sets will determine how much of development partners' money is directly entering the local economy.
	How are profits being used by local businesses?	<ul style="list-style-type: none"> <li>• Survey local businesses.</li> </ul>	The more the money from the contracts is re-spent with other local businesses or invested in human or physical capital, the more beneficial this money is for long-term growth.
	How much of partners' aid is tied?	<ul style="list-style-type: none"> <li>• OECD DAC data.</li> </ul>	These data sets will determine whether development partners are using the tools available to them to procure locally.
	How often is the margin for domestic preference used?	<ul style="list-style-type: none"> <li>• Survey development partner procurement officers.</li> </ul>	
	How are development partners managing risk in local procurement?	<ul style="list-style-type: none"> <li>• Survey development partner procurement officers.</li> </ul>	
	*What factors are preventing local businesses from bidding?	<ul style="list-style-type: none"> <li>• Survey local businesses.</li> </ul>	
	Is the local private sector aware of how to find out about and respond to tenders?	<ul style="list-style-type: none"> <li>• Survey local businesses.</li> </ul>	The difficulties faced by local businesses will be useful to any policy-maker considering how to increase local procurement by improving access.
	How many local bids do development partners receive for contracts? How does this vary with size and sector?	<ul style="list-style-type: none"> <li>• Survey development partner procurement officers.</li> </ul>	
<b>Jobs created</b>	*How labour-intensive are the contracts going to local businesses?	<ul style="list-style-type: none"> <li>• Survey local businesses.</li> </ul>	These data sets will determine how much local procurement is affecting job creation in the local labour market.
	When contracts go outside the country, how much is spent in the country (e.g. on local labour)?	<ul style="list-style-type: none"> <li>• Survey international businesses.</li> </ul>	



## 4.2 Distorting the market

### Potential impact

Some development partners fear that by undertaking a large amount of local procurement, the local economy will become structured to serve them rather than building up the competitive export industries which are commonly considered to be the best drivers of growth in developing countries. In addition, once the partner leaves, this will create a negative shock and the local market will find it difficult to adjust.

Development partners in a country should also be aware that distortion can occur even when a buyer does not undertake a large amount of procurement if a buyer is considered to be strategically important. For example, having previously serviced an international client can be extremely beneficial for a business trying to win contracts with other (possibly larger) customers and so businesses may invest a high degree of effort into winning such a contract even if that contract is small (DotEcon 2004).

Indeed, once a business has won a contract from a development partner that business is likely to experience 'incumbency advantages'. Because they now have a track record and have already invested in relevant assets they are in a better position to win future contracts. This could be a good thing if it builds the capacity of certain businesses (see Section 4.4) but it could also be bad if it limits the ability of other firms to compete.

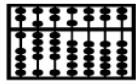
The benefits of creating incumbents are highly visible to the buyer – their risk is lowered, procurement processes are easier, the capacity of incumbents increases – while the disadvantages of reduced competition are harder to determine. Even if a development partner benefits from having a limited number of suppliers that have invested in delivering their contracts efficiently and cheaply, the resulting lack of competition is likely to harm other buyers in the market (for example, the national government) (DotEcon 2004).

### Factors affecting impact

The distortionary effect is likely to be greatest if businesses have had to invest in specialist assets that can be used only to serve the donor market and are not transferable. A crude example might be buying a special machine that makes buttons used only on uniforms used by the UN. By contrast, distortionary effects will be reduced if businesses invest in assets that could be transferred to another sector, for example a uniform factory could evolve to become a more general garment factory making clothes for all sections of the population (Tschirley 2007). Partners will distort the economy less if they concentrate on areas where there is excess capacity in the market. This is usually in industries with large inputs from unskilled labour.

One interviewee cautioned against interfering too much in the capacity of the local market, citing one experience where a development partner had developed a pool of local consultants and given them contracts on a loss-leader basis to build their capacity. However, they were always dependent on the development partner for contracts and so when that partner left they were left 'high and dry'. Clearly the predictability of donor spending will have an important impact on their distortionary effects. If withdrawal is gradual and predictable this will help resources to be allocated elsewhere in the economy.

Policies around qualification criteria for procurement may also affect distortions. Designing a procurement process that makes bidders more alike increases competition as bids are more comparable but it also increases the risk of collusion as fewer firms will be bidding (Tschirley 2007). However, strict criteria for procurement are likely to increase the risk that one group of traders is artificially strengthened at the expense of others. This is particularly the case when a sector is dominated by small, undercapitalized traders (Tschirley 2007).



### 4.3 Inflation

#### Potential impact

If a particular resource is scarce in an economy, procurement of that resource in large quantities by a development partner could lead to inflation and, in extreme cases, prevent households from purchasing basic necessities such as food and fuel. In order for a buyer or group of buyers to contribute to inflation they will need to be purchasing a significant market share. The World Food Programme considers 10% of surplus food brought to market to be a benchmark at which inflation becomes a danger (Tschirley 2007).

The scarcity of goods and hence inflationary pressure may vary according to the time of year. This is most particularly the case with locally grown crops but may also be the case for goods where a large component of the cost comes from transportation. It has also been observed that some producers will withhold produce from the market in anticipation of commanding higher prices from an international buyer (Tschirley 2007).

#### Factors affecting impact

Interviewees considered it good practice for procurement officers to be aware of prevailing market conditions such as price and supply and factor these into procurement decisions. The World Food Programme uses the price of food imports as a benchmark so that once the price of local food rises above the price of imports the World Food Programme will switch to procuring imports.

Unfortunately many goods and services are not traded in international markets and so it is much more difficult to find an appropriate benchmark or gather historic price data.

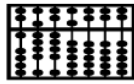
**Table 4.2: How to assess the impact of development partner procurement on market distortions**

Type of impact	Questions to assess impact	Suggested sources	Suggested benchmarks and analysis
<b>Local procurement distorting the local private sector</b>	*What proportion of the local private sector does procurement by development partners represent?	<ul style="list-style-type: none"> <li>• Survey of local businesses.</li> </ul>	These data sets will determine whether development partners are important enough as buyers in the local economy to be at risk of creating distortions.
	To what extent do local businesses view contracts from development partners as strategically important?	<ul style="list-style-type: none"> <li>• Survey of local businesses.</li> </ul>	Suggested benchmark: If development partners represent more than 10% of business in a particular sector then there is a risk that they are creating distortions in that sector. If local businesses view development partners as being particularly strategically important then there is a risk that distortions could occur even at lower levels.
	What are development partners procuring locally?	<ul style="list-style-type: none"> <li>• Survey of development partner procurement officers.</li> </ul>	These data sets will determine to what extent local procurement is making use of the capacity already existing in the economy.
	Where is the spare capacity in the economy?	<ul style="list-style-type: none"> <li>• Survey of local businesses.</li> </ul>	This is the least distortionary aspect of procurement as little adjustment is required from the local market to meet partners' needs.
	*Will local businesses be able to transfer their business to other sectors of the economy once development partners withdraw?	<ul style="list-style-type: none"> <li>• Survey of local businesses.</li> <li>• World Bank/national government reports.</li> </ul>	Comparing where capacity is being increased by development partners' demands with where demand is growing in the rest of the economy will determine how beneficial partners' procurement is for long-term growth.
	Do development partners' procurement contracts require specialised investment by bidders?	<ul style="list-style-type: none"> <li>• Survey of local businesses.</li> </ul>	Procurement will be most beneficial if it encourages investment in high-growth areas which enable local businesses to service markets beyond development partners. However these effects will only be significant if development partners are large purchasers in that sector (see above).
	Are development partners awarding contracts to the same businesses?	<ul style="list-style-type: none"> <li>• Survey of development partner procurement officers.</li> </ul>	This data set will determine whether development partner procurement practices are encouraging open and fair competition.
	Do development partners' qualification criteria encourage or discourage competition?		These results should be considered alongside partners' significance as purchasers in the market (see above).

**Table 4.3: How to assess the impact of development partner procurement on inflation**

Type of impact	Questions to assess impact	Suggested sources	Suggested benchmarks and analysis
Inflation in local markets	*How are prices changing?	<ul style="list-style-type: none"> <li>Market data (for goods traded on open markets).</li> <li>Survey of procurement officers and local businesses (for good not traded on open markets).</li> </ul>	<p>These data sets will determine whether and where there is inflation in the local market place.</p> <p>As inflation in fragile states is typically high, also look for fluctuations in inflation that could relate to fluctuating demand from development partners.</p>
	How do local prices compare to imports?	<ul style="list-style-type: none"> <li>Survey of procurement officers.</li> <li>Surveys of importing businesses.</li> </ul>	<p>When imports are cheaper than local goods this might be evidence of a bottleneck in the economy. When making this comparison it is important to compare true prices inclusive of taxes and tariffs.</p>
	Are local businesses finding that the prices of their inputs are increasing?	<ul style="list-style-type: none"> <li>Survey of local businesses.</li> </ul>	
	Are there seasonal pressures on the supply of goods sourced by development partners?	<ul style="list-style-type: none"> <li>Survey of local businesses.</li> <li>Survey of procurement officers.</li> </ul>	
	*How important are development partners in the markets in which they operate?	<ul style="list-style-type: none"> <li>Survey of local businesses.</li> </ul>	<p>This data set will determine how likely it is that any inflation is caused by the activities of development partners. Data should be analysed on a sector by sector basis.</p> <p>Suggested benchmark: If development partners represent more than 10% of business in a particular sector then there is a risk that they are contributing to inflation.</p> <p>Note that the portion of the market that development partners are buying can fluctuate a lot if there are sudden supply shortages or a large new partner-funded project begins.</p>





#### 4.4 Capacity of the local private sector

##### **Potential impact**

Doing business with international organisations can be of great benefit to local businesses far beyond the immediate profit of winning a contract. Some have even argued that the benefits of trading with international organisations is so great that it is more beneficial for growth than the development projects themselves (Adam 2004). Known as 'learning by doing', working with an international organisation can increase capacity and productivity of a business as it encounters international standards (in both quality and transparency), increases its experience and acquires new skills to complete the contract.

If a development partner is able to offer a predictable level of income, this will provide local businesses with an incentive to invest in their own capacity and in building up reliable supply chains. Local procurement can also help to bring more businesses into the formal economy and build the capacity of the government to raise revenue.

##### **Factors affecting impact**

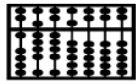
The extent of the capacity-building effect of local procurement will depend on how engaged both parties are in the procurement process. If development partners offer training to local businesses on their procurement processes and offer feedback on unsuccessful bids then it is possible for a wider section of the business community to benefit.

Whether benefits from this increased capacity are sustained beyond the presence of the partner in the country will be determined by the need for this capacity in the long term. For example, it is beneficial for a country to have the capacity to maintain and construct its own physical infrastructure.

Some development partners are eligible for tariff and tax exemptions on imports. This means that local suppliers may not be able to compete with international firms if they rely on imports. Claiming these exemptions can also mean a lost opportunity for partners to help build up revenue-raising capacity in the national government (Carnahan 2006; OECD 2010).

**Table 4.4: How to assess the impact of development partner procurement on capacity of the local private sector**

Type of impact	Questions to assess impact	Suggested sources	Suggested benchmarks and analysis
<b>Increased capacity of local businesses</b>	*Do development partners find the quality of bids increasing over time?	<ul style="list-style-type: none"> <li>• Survey of development partner procurement officers.</li> </ul>	This data set will determine whether or not the capacity of the local market is increasing over time.
	*Do development partners find the quality of work executed by local businesses increasing over time?	<ul style="list-style-type: none"> <li>• Survey of development partner procurement officers.</li> </ul>	This may be difficult to get feedback on due to high turnover of procurement staff.
	Do local businesses feel more confident about their ability to serve international markets?	<ul style="list-style-type: none"> <li>• Survey of local businesses.</li> </ul>	This data set will determine whether businesses themselves feel that undertaking international contracts has increased their capacity.
	Are they accessing international markets beyond development partners?	<ul style="list-style-type: none"> <li>• Survey of local businesses.</li> </ul>	
	Are development partners offering detailed feedback on failed bids?	<ul style="list-style-type: none"> <li>• Survey of local businesses.</li> </ul>	These data sets will determine whether development partners are doing as much as they can to improve the capacity of the local market through their procurement practices.
	Are development partners' procurement processes transparent?	<ul style="list-style-type: none"> <li>• Survey of local businesses.</li> <li>• Survey of development partner procurement officers.</li> </ul>	
	Are development partners' processes avoiding corruption?	<ul style="list-style-type: none"> <li>• Survey of local businesses.</li> <li>• Survey of development partner procurement officers.</li> </ul>	
	Are the types of capacities that are being built up useful for the longer-term?	<ul style="list-style-type: none"> <li>• Government strategy documents outlining priorities.</li> <li>• Survey of development partner procurement officers.</li> </ul>	
<b>Increased capacity of national government</b>	To what extent do development partners claim tariff or tax exemptions?	<ul style="list-style-type: none"> <li>• Survey of development partner procurement officers.</li> <li>• Interview with appropriate national government ministry.</li> </ul>	<p>This data set will determine whether development partners are operating within and supporting the tax systems put in place by the national government.</p> <p>This should be considered alongside the level of international support for the government's tax policies (are they grossly inequitable or punitive?).</p>



## Annex 1 – Sources

### Relevant literature

**Adam, C. and O’Connell, S. (2004)** *Aid versus trade revisited: Donor and recipient policies in the presence of learning-by-doing*. The Economic Journal 114

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**DotEcon (2004)** *Assessing the impact of public sector procurement on competition*, Office of Fair Trading

**GTZ (2006)** *Private Sector Development in Reintegration and Reconstruction Programmes*

**IOM (2005)** *Results of the Survey “Engaging Diasporas as Agents of Development”*

**Knack, S. and Rahman, A. (2007)** *Donor fragmentation and bureaucratic quality in aid recipients*

**Nelson, M. (2006)** *Does Training Work? Re-Examining Donor-Sponsored Training Programs in Developing Countries*, Capacity Development Briefs Number 15, World Bank Institute

**OECD (2010)** *Do no harm: International Support for Statebuilding*

**Peace Dividend Trust (2010)** *Risk and Opportunity: Local Procurement in Conflict-Affected and Fragile States*

**Rajan, R. and Subramanian, A. (2005)** *What Undermines Aid’s Impact on Growth?*, IMF Working Paper WP/05/126

Report of **the Secretary-General on Peacebuilding** in the Immediate Aftermath of Conflict A/63/881-S/2009/304 of 11 June 2009, paragraph 48

**Senior Advisory Group, UN Security Council (2011)** *Civilian capacity in the aftermath of conflict*

**Tchirley, D. and de Castillo, A. M. (2007)** *Local and Regional Food Aid Procurement: An Assessment of Experience in Africa and Elements of Good Donor Practice*, MSU International Development Working Paper

#### **Procurement and hiring policies of:**

- Department for International Development
- Deutsche Gesellschaft für Internationale Zusammenarbeit
- European Commission
- World Bank

### Organisations consulted

Department for International Development

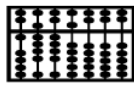
Deutsche Gesellschaft für Internationale Zusammenarbeit

Eurodad

European Commission

United Nations Development Programme

World Bank



## Annex 2 – Development of the methodology

This methodology is based on a literature review of appropriate documents and interviews of development partners (details can be found in Annex 1). While the majority of interviewees were aware of the issues raised in this report and were able to give anecdotal evidence on development partners' impact, there was almost no research conducted by development partners into their impact. Indeed few partners are collecting data on local procurement and hiring that would be necessary for such research.

This means that it was particularly difficult to provide benchmarks and comparisons to aid analysis in the methodology. The only clear benchmark found was the 10% benchmark used by the World Food Programme to determine how important it is as a purchaser in a local food market. The methodology also suggests using this benchmark in the context of labour markets in the absence of a more evidence-based benchmark. As more development partners and national governments conduct these in-country reviews, more benchmarks and comparisons should become available and be added into this methodology.

## Annex 3 – A case study for assessing impact: donor-funded remuneration in Afghanistan

In response to concerns about the different salaries and top-ups that are being paid to Afghan civil servants and/or the national consultant by development partners, the Government of Islamic Republic of Afghanistan (GIRoA) established a Presidential Commission in 2010 under the leadership of Ministry of Finance (MoF) and the Independent Administrative Reform and Civil Service Commission (IARCSC)<sup>9</sup> in Afghanistan to undertake a survey to development partners about their remuneration practices. The detailed analysis of the data through the survey process is expected to lead to policy recommendations in the following areas:

- Harmonization of Civil Service and NTA (National Technical Assistance) remuneration
- Harmonization of NTA remuneration among donors/implementers
- Harmonization of NTA remuneration in Kabul and in the Provinces
- Rationalization of donor-funded top-ups and allowances

### The approach

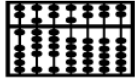
The MoF and the IARCSC sent out a survey to the GIRoA key donors. The survey requested information about the remuneration (including salary and top-ups) that the donors are paying to Afghan nationals working in GIRoA. Eighteen donors reported on 8,088 individuals who received or are continuing to receive salaries or top-ups, over a period starting from April 2003 until January 1 2010. The vast majority of the data was for individuals still receiving remuneration on January 1 2010; very little historical data was received.

### The findings

- A few major donors including the World Bank/Afghanistan Reconstruction Trust Fund (ARTF), the US, the UK, UNDP and UNESCO account for the vast majority of recipients paid and total expenditures spent.
- A small number of state institutions account for the majority of donor-funded remuneration recipients.
- Donor-funded remuneration is highly uneven. Monthly remuneration for current recipients ranges from \$20 to \$9,000, with an average of \$564. However, 68% receive no more than the average and only 10% receive \$1,500 or more.

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<sup>9</sup> The IARCSC is an independent government agency under the President of GIRoA with a mandate to lead and manage the administrative reform, civil service management, appointments and capacity development in the country.



- When controlled for grades, donor-funded salaries are generally 3-8 times the Pay and Grading Scheme the government is currently implementing, with the multiplier increasing as the grade goes up.
- Individual donors each show large salary spreads within each grade.
- Differentials between salaries are causing resentment and demotivation amongst civil servants.
- Payments as such by development partners cause market distortion and brain drain in government institutions.

## Options and Recommendations

The survey data reveals that lack of consistency in donor remuneration of civil servants in Afghanistan is a problem. Hence, the survey report helps the Commission recommend some policy options on four main policy areas:

A: Harmonisation of Civil Service and NTA remuneration: Development of an agreed NTA salary scale to be used countrywide. Through annual review of the scale the objectives of stabilizing NTA salaries in the short term and exerting downward pressure on NTA salaries in the medium term are achieved

B: Transparency and Accountability: Channel payment of NTAs through GIROA so GIROA has a complete knowledge of who must be paid and how much each NTA must be paid. Also, ensure the reporting relationship between the relevant NTA and GIROA institutions with clear terms of reference.

C: GIROA control of NTA: Develop mechanism on smooth control of NTA salary administration and transition to government positions

D: Top-ups and Allowances Framework for NTA: Develop mechanisms to correct obvious abuses e.g. where NTAs are receiving multiple top-ups. Link the remunerations to clearly defined outputs and delivery and establish more accurately which civil servants receive top-ups, how much, from whom, the reason and etc.

National technical assistance policy is now under development stage by the IARCSC with the support from Ministry of Finance and development partners.

## Data challenges and lessons

It is important for investigations of this kind to come with a strong mandate. This investigation came with a Presidential decree and was executed by the MoF and IARCSC. Despite this mandate, there was still serious under reporting of data. The extent of this under reporting was unknown. In addition, competition among development partners has made this process more complex and challenges the timely achievement of the commission work.

Knowledge of the context and having an established network of contacts in ministries and donors was extremely helpful for putting pressure on donors and chasing up information. Timing was also important. Some donors were more cooperative because data requests coincided with political pressure in their home countries to increase transparency and demonstrate effectiveness.

It is important to underline the need for more policy dialogue with the development partners at higher levels (political) to establish an understanding of the importance of this exercise and to ensure timely support and commitment in implementation stage.

For more information about this work, please contact Mr. Rohullah Osmani of the IARCSC (email: [rosmani@afghanexperts.gov.af](mailto:rosmani@afghanexperts.gov.af)).