

## Why Borrow for Capacity Building?

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### Abstract

This paper looks back at the history of development assistance and argues for the importance of capacity building along with infrastructure building. After all, people are the ones who operate and care for infrastructure. Are they not worthy of investment as well?

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Some sovereign nations do not want to borrow for capacity building. Yes, we see this all the time. But, I ask myself, why? That got me thinking and my thoughts went back to senior year in college.

My college thesis<sup>1</sup> starts out with this quote from Joseph Schumpeter: “Add successively as many mail coaches as you please, you will never get a railway thereby”<sup>2</sup>. The thesis applies theories of creativity to the development of Japan after the Meiji restoration in 1868. In the 1880s, the Ministry of Education spent 66% of its annual budget to hire foreign technicians to teach Japanese students.

Let’s fast forward, though. Today’s development banks originated in the Marshall Plan that financed reconstruction of Europe after World War II. The plan gave loans to Europeans who were already well educated, had well-developed civil societies and were able to manage their affairs effectively. They had the capacity to take care of their assets and manage to repay their loans.

The Marshall Plan led to the formation of the World Bank and likely influenced the establishment of other development banks. As the challenge in Europe receded, development funds began to flow into underdeveloped countries. During the Cold War, development funds went to places chosen by political expediency – to keep those dominoes from falling. Cold War over, we can still see how politics affects development aid in some places (Iraq or Egypt) but aid is more widespread now, going into every needy country in the world, albeit in differing amounts.

A lot of development aid in the period 1960-1985 went for large-scale infrastructure and engineers made up a significant proportion of development bank or agency staff. Some argue that when engineers look at a problem they are naturally disposed to solve it with an engineering solution – build something to solve the problem. We each play to our strengths, don’t we? So, by the late 1980s a lot of infrastructure projects had been built around the world.

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<sup>1</sup> Titled: *Developmental Economic Change: Motivation and Effect*

<sup>2</sup> In *The Theory of Economic Development*

By the late 1980s, infrastructure projects built 10-15 years earlier failed or operated at significantly less than capacity. Why? Development professionals concluded that lack of maintenance, spare parts, knowledge and lack of funds were to blame, etc. Enter the notion of capacity building or institutional strengthening with a focus on inventory, training and tariff setting.

Perhaps this was the embedded, but unrecognized problem: the Marshall Plan approach worked because loans went to countries and people who were already educated and had the capacity to take care of assets and repay loans. The infrastructure projects in developing countries went to countries and people who did not have the capacity of the Europeans of the 1940s. They did not have the education, well-developed civil societies or the discipline to repay loan obligations.

Were the development banks wise to take the same approaches with developing countries that the Marshall Plan took with Europe? Doubtful. It may have been better to recognize the weaknesses of developing countries and start with capacity building before making the loans for large infrastructure projects that were otherwise doomed to fail before their time.

Between the development banks and aid agencies, billions upon billions of dollars have gone into infrastructure projects over the last 25-30 years and yet we have not alleviated the problems of the poor as much as hoped. Why? Perhaps because there has been a lack of sufficient commitment or understanding in developing countries about good stewardship of assets and financial assistance. Perhaps the cart came before the horse in building valuable assets for people who did not have the capacity to care for them.

The mission of development banks is to make loans, assuming that bilateral aid agencies will do the capacity building. While this is an excellent idea in theory, especially in light of MDGs, it doesn't always work. If it did, we would see far less suffering among the poor and a lot more debt repayment. What we can see in some places is that bi-lateral agencies compete with each other, applying different approaches and philosophies that often clash. (One agency paid people in Fayoum, Egypt to come to meetings. So, naturally, people working with other donor-funded projects demanded the same payments. This was a problem for the new project because it could not make such payments.)

Reality plays out: country takes the loan, builds the infrastructure; infrastructure fails before its time and the country is not much better off – in fact, maybe worse off since now it has to repay the debt for an asset that no longer works. With exchange rate risk, this problem can become dire. With a country in dire straits, the banks “forgive” the loan and the whole “revolving fund” idea goes down the tubes along with any discipline the country might develop if “forgiveness” of the loan was not possible.

Let us go back to the Meiji in Japan the 1880s. They started with capacity building. They invested significant amounts of money. Combined with a sound cultural foundation, Japan became what it is today and the capacity building investment paid off over and over.

So, why should countries not borrow money for capacity building? This money is an investment in the people who will operate and care for the infrastructure. Are they not equally as important as the physical asset? Could capacity building loans precede infrastructure – or maybe even be a precondition for infrastructure loans. After all, countries that wish to join the European Union are required to qualify and this often means policy reform. If capacity building means that assets last longer, work better and contribute to the sustainability of a utility, then capacity building is not “soft stuff” – it is a good investment with a big payoff.

But, it seems, the words “Capacity Building” turn people off these days – I wonder why?

There have been many capacity building projects around the world over the last 10 years. Let me refer to the institutional strengthening projects of USAID in Egypt, which I know the best. In response to complaints that counterparts lacked spare parts, resources and knowledge, USAID began a number of projects in the early 1990s, which focused on training, tariff setting, inventory control, personnel policies, etc. While these projects did some good, their benefits were limited by national government policies and the legal framework for the utilities that restricted the extent to which they could reform and improve. In addition, project efforts focused in many cases on relatively low-level utility managers.

What can we learn from this: 1) the best way to do capacity building is in an environment that allows – or even encourages - people to change and improve. This means laying the foundation at the upper reaches of national governments and then building support for reform with the leaders of utility organizations. Otherwise, you run the risk of introducing new approaches and having them fail because of restrictions from above. It makes little sense to empower an organization if it has to live within a bad overall system. 2) Projects that focus on specific functions - like inventory control – will have some impact but not as great an impact as when these functions are part of a more comprehensive approach – like organization development.

We wrote the Guidebook to lay out a rational approach to build a strong foundation that would support further development and continuous improvement. It starts with the legal framework and then moves to leadership and commitment. In other words, it starts with the most important and pervasive influences on an organization – it does not start with inventory control.

Another reason that capacity building may have developed a bad name is that it often plays out into management training courses that often focus on changing behaviors with little or no attention to the building blocks of good management like job descriptions, mission statements, management reports or approaches like Managing by results. It doesn't do much good to train people in Team Building if they don't know what the team is supposed to accomplish. So, it is likely that many well-intentioned training courses have taken place around the world but they have had minimal effect because the students return to organizations without the fundamental building blocks of good management in place.

Again, we wrote the Guidebook to fill the void that we saw in many places – the void of attention to the building blocks for a strong foundation for management.

What would really good Capacity Building be like? Ah – the real question. We are all learning together all of the time. So any implied criticisms in this paper come with the knowledge that life is a journey not a destination – as we learn we find ways to improve and go further.

Great capacity building would start with top level commitment to effective reforms – not the kind of grudging “commitment” that governments are often forced into to get a larger support package.

The capacity building program would be one designed in conjunction with counterparts, based on their own realization of the need to improve. In other words, a capacity building effort without ownership by counterparts is no capacity building program at all.

There are few hard and fast requirements for a capacity building program but there are certain minimum areas of attention:

- ✦ **Management Foundation and Behaviors** – on the idea that any management system must be built – it doesn't magically appear
- ✦ **Functional Expertise** – on the idea that you cannot expect someone to be an accountant if they don't know the first thing about accounting
- ✦ **Management Information Systems** – on the idea that “if you can measure it, you can manage it.”

Isn't it time for us all to have a harder look at capacity building and do it better? After all, management capacity building is one of those empowering efforts that have benefits for years to come – if not decades.