

Financing Public Investment Through Foreign Aid: Consequences for Economic Growth and Welfare

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Abstract

This paper explores the relationship between foreign aid and public investment in the context of a growing small open economy. Both tied and untied aid are considered, as well as permanent and temporary programs. We conduct a numerical analysis of the transitional dynamics and characterize the trade-offs between the degree of substitutability between public and private capital, investment costs, and welfare in response to different types of foreign aid programs. The dynamic consequences of co-financing public investment by domestic and foreign sources are also considered, thereby highlighting the desirability of tied and untied aid programs.

URL: <http://www.terry.uga.edu/people/schatt/Papers/foreignaid2.pdf>