

Unclassified

DCD(2005)4

Organisation de Coopération et de Développement Economiques
Organisation for Economic Co-operation and Development

12-Jan-2005

English - Or. English

DEVELOPMENT CO-OPERATION DIRECTORATE

Cancels & replaces the same document of 11 January 2005

SENIOR LEVEL FORUM ON DEVELOPMENT EFFECTIVENESS IN FRAGILE STATES

Aid Allocation Criteria: Managing for Development Results and Difficult Partnerships

Report by Oxford Policy Management (OPM)

13-14 January 2005
Lancaster House, London
United Kingdom

This report, prepared by Stephen Jones, Roger Riddell and Katarina Kotoglou of OPM, was commissioned by the DAC Learning and Advisory Process on Difficult Partnerships (LAP), and is submitted as one of the key documents for consideration at the Senior Level Forum on Development Effectiveness in Fragile States to be held in London, United Kingdom on 13-14 January 2005. (Annexes B to K available upon request.)

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JT00176804

Document complet disponible sur OLIS dans son format d'origine
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Acknowledgements and disclaimer

This study was commissioned and funded by the UK Department for International Development as part of a wider set of studies being undertaken for the OECD/DAC. However the report is the responsibility of the consultants alone and any conclusions should not be attributed to DFID or the OECD/DAC.

Thanks are due to Sophie Pongracz of DFID, Ali Gillies of the World Bank, Paul Isenman and Karim Morcos of OECD, and Damien Navizet of AFD for comments on an earlier draft of the report.

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ABBREVIATIONS

AA	German Federal Foreign Office
ACP	Africa, Caribbean and the Pacific
AFD	Agence Française de Développement
ALA	Asia and Latin America
ASEAN	Association of South East Asian Nations
AusAID	Australian Aid
BMZ	German Federal Ministry for Economic Cooperation and Development
C2Ds	Contracts for Debt Reduction and Development
CAP	Country Assistance Programmes
CAR	Central African Republic
CARDS	Community Assistance for Reconstruction, Development and Stabilisation (Balkans)
CCA	Country Conflict Assessment
CHAD	Conflict and Humanitarian Assistance Division (DFID)
CICID	French Inter-ministerial Committee for International Co-operation and Development
CPIA	Country Policy and Institutional Assessment
CSP	Country Strategy Papers
DAC	Development Assistance Committee
DAF	Sub-Saharan Africa Department (Dutch Ministry of Foreign Affairs)
DAM	North Africa and Middle East Department (Dutch Ministry of Foreign Affairs)
DFID	UK Department for International Development
DGCID	French Directorate-General for International Co-operation and Development
DG DEV	Development Directorate General
DGIS	Dutch Directorate General for International Cooperation
DG RELEX	External Relations Directorate General
DOM-TOM	France's overseas departments and territories
DMV	Policy Theme Departments: the Human Rights and Peacebuilding Department (Dutch Ministry of Foreign Affairs)
DMW	Environment and Development Department (Dutch Ministry of Foreign Affairs)
DP	Difficult Partnership
DPT	Document de Politique Transverse
DRC	Democratic Republic of Congo
DVF	United Nations and International Financial Institutions Department (Dutch Ministry of Foreign Affairs)
EBRD	European Bank for Reconstruction and Development
EC	European Commission
ECB	Economic Cooperation Bureau
ECHO	European Community Humanitarian Office
EDF	European Development Fund
EP	European Parliament
ESF	Economic Support Funds
EU	European Union
EU MSs	European Union Member States
EVI	Economic Vulnerability Index
GAERC	General Affairs External Relations Council
GBS	General Budget Support
GNI	Gross National Income
GNP	Gross National Product

GTZ	German Agency for Technical Cooperation
HCCI	French High Council for International Cooperation
HDI	Human Development Index
HIPC	Heavily Indebted Poor Countries
IDA	International Development Association
IFIs	International Finance Institutions
IMF	International Monetary Fund
ISD	Indicator of Social Development
JBIC	Japan Bank for International Development Cooperation
JICA	Japan International Development Cooperation
KfW	German Bank for Reconstruction
LDCs	Least Developed Countries
LICs	Low Income Countries
LICUS	Low Income Countries Under Stress
LOLF	French Institutional Act on Financial Legislation
MAE	French Ministry of Foreign Affairs
MCA	Millennium Challenge Account
MCC	Millennium Challenge Corporation
MDGs	Millennium Development Goals
MEDA	Mediterranean and the Middle East
METI	Japan Ministry of Economic Trade and Industry
MFA	Dutch Ministry of Foreign Affairs
MICs	Middle Income Countries
MINEFI	French Ministry for Economic Affairs, Finance and Industry
MJSP	Multi Year Strategic Plan (Dutch Ministry of Foreign Affairs)
MoF	Japan Ministry of Finance
MOFA	Japan Ministry of Foreign Affairs
NCI	Needs Country Index
NGO	Non Governmental Organisation
NIP	National indicative Programme
OA	Official Assistance
ODA	Official Development Assistance
OECD	Organisation for Economic Co-operation and Development
OTI	Office for Transitional Initiatives
PART	Program Assessment Rating Tool
PCI	Performance Country Index
PNG	Papua New Guinea
PMO	Programme Management Office
PPP	Purchasing Power Parity
PRDE	Poverty Reduction in Difficult Environments Team (DFID)
PRSP	Poverty Reduction Strategy Papers
PSA	Public Service Agreement
RAP	Resource Allocation Priority
SAF	Structural Adjustment Facility
Sida	Swedish International Development Agency
SSA	Sub Sahara Africa
TACIS	Eastern Europe and Central Asia
TICAD	Tokyo International Conference on African Development
UN	United Nations
UNDP	United Nations Development Programme
UNHCR	United Nations High Commissioner for Refugees

UMICs	Upper Middle Income Countries
USAID	United States Agency for International Development
VCI	Vulnerability Country Index
WFP	World Food Programme
WIDER/UNU	World institute for Development Economics Research/United Nations University
ZSP	Zone de Solidarité Prioritaire

EXECUTIVE SUMMARY

1. This report describes the different factors that donors take into account when determining their allocations of aid to countries, with a special focus on those that do not achieve “good performer” status. The study involved a review of literature, analysis of the policies and practices of the main bilateral agencies, and an analysis of data on trends in (bilateral) aid allocation. An underlying concern within the international community has been that a move towards an increasing emphasis on measures of performance or of effective governance in aid allocation decisions may be leading to a situation in which some countries that are potentially effective users of aid, but that have deep governance problems and a poor record of performance, are being allocated a lower share of total aid resources than is desirable.

2. A first observation of the study is the need to distinguish clearly between aid allocation according to (i) poverty criteria, (ii) need (taking account of absorptive capacity and demand and current supply of aid) (iii) performance in poverty reduction (i.e. results achieved), (iv) proxy indicators of expected future performance (i.e. prospects of achieving future results), and (v) (relatedly) *by* results as opposed to *for* results. The strong emerging empirical evidence about the differential impact of different *types* of aid in different contexts also calls into question the centrality of aggregate allocation decisions, as opposed to the choice of instruments and forms of engagement.

3. Empirical studies of aid allocation have generally shown the following patterns:

- A disproportionate share of aid has gone to middle-income and less poor countries, and to smaller countries as against larger countries, compared to what a pattern of allocation driven just by poverty criteria would imply.
- A stronger larger/richer country bias for bilateral compared to multilateral aid, but with substantial variation between donors.
- Aid allocations are motivated by a variety of objectives in addition to poverty reduction – including domestic political, geo-political, commercial and security objectives. Developments particularly since 2001 tend to suggest that relatively (compared for instance to trade creation objectives) poverty reduction and regional and geo-political strategic considerations have been dominant, and have contributed to substantial increases in aggregate in bilateral aid flows.
- There is evidence that aid allocations and policies of donors have become both more poverty-driven (as the international consensus around commitment to the MDGs has grown) and more “selective” (as evidence on the determinants of aid effectiveness has become clearer) in the sense of being influenced by past or anticipated future poverty reduction performance. The potential bias against “poor performers” that the latter (limited) change may imply has been offset for those failed or failing states that are regarded by some donors as significant for regional or global security and for geo-political reasons. However, those countries that do not attract this level of engagement or international interest may risk being under aided.

4. The policies of the donors reviewed for this study may be distinguished in the following respects:

- Donors whose aid policies are principally and explicitly driven by and assessed against poverty reduction criteria including the MDGs, those which have adopted policies that are poverty- and MDG-focused - but with commitment to this in the process of being operationalised, and those

for whom poverty reduction is one among a range of objectives with geopolitical or regional considerations appearing to be of decisive significance.

- Donors whose policy-making processes involve an explicit and relatively centralised process of decision-making about bilateral resource allocation between recipient countries, and those where overall allocations are the results of decisions made across several agencies. Several countries also have explicit policy commitments on the total level of aid and/or the share that should go to specific groups of countries.
- The extent to which performance and results-based assessment are institutionalised within the agency's accountability framework, and the extent to which resource allocation models are used to inform allocation decisions. Explicit or implicit models generally pay significant attention to political governance considerations. The European Union's (EU) European Development Fund (EDF) stands out as an example where aid is allocated against explicit criteria (mainly related to policy) and within the context of an international agreement, while the United States' Millennium Challenge Account (MCA) provides explicit criteria for qualification that are entirely performance-based. Otherwise models are used for providing benchmarks and guides for bilateral donors (typically within groups of countries). In none of the cases reviewed were model-based allocations used as the sole or main driver of aid decisions.

5. The main features of donor policies towards "difficult partnerships" can be summarised as follows:

- Increasing analytical attention to the problem of how to engage most effectively with these countries (prompted in part by increasing concerns with international security issues and the threat of terrorism associated with failed states), and recognition of the need for a more nuanced set of definitions of different types of problem.
- Attention to the World Bank's Country Policy and Institutional Assessment (CPIA) and other measures of governance in decisions on aid levels and forms of engagement.
- A general view that the formal and explicit identification of a particular group of problematic countries is not of value for policy purposes, and hence the avoidance of the use of special criteria to determine allocations to these countries.
- The use of a range of aid instruments, with humanitarian aid often being the most significant, with a recognition that new instruments and forms of engagement that focus more explicitly on security and conflict prevention/resolution may be required.
- Channelling a limited amount of aid funds to and through non-governmental agencies, including the private sector and especially local and international Non-Governmental Organisations (NGOs) particularly in instances where recipient government commitment to development or corruption are identified as key impediments to aid delivery and impact.
- A policy (at least among larger donors) of seeking to maintain engagement with difficult partner countries combined with a strong interest from bilateral donors in continuing engagement with countries that are of particular political or economic significance to them, especially near neighbours.
- Bilateral aid to difficult partnership countries (based on the World Bank's definition of Low Income Countries Under Stress (LICUS) has increased in the most recent years, though with the

level of aid being relatively highly skewed to certain countries seen as of wider global or regional significance (such as Afghanistan).

6. The overall conclusion is that donors are undoubtedly trying to ensure that their aid expenditure is being used more effectively. However, the specific concern that these policies are leading to aid to “less effective” countries being reduced more than is desirable do not appear to be borne out in general, though some countries are significantly underaided and may be “aid orphans”. The analysis by Levin and Dollar (2004b) suggests that this is overwhelmingly a regional phenomenon, concentrated on a band of countries across central Africa, which were (for the smaller countries) disproportionately affected by reductions in French aid, reinforced by similar reductions from other donors and from IDA, and which for the larger countries (DRC, Nigeria, Sudan) reflects very difficult relations with donors over long periods of time.

7. This is the result of a combination of factors. First, the objectives of bilateral donors include concerns about security and the risks of state failure – these concerns are prompting continued or increased engagement in those countries that are seen as presenting a particular risk to the international community or to particular donors. Second, donors are using different forms of engagement and aid modalities as a way of dealing with poor performers.

8. The critical conclusion for international policy is that donor policies in aggregate do little to ensure that aid allocations to individual countries are predictable, clearly criterion-based or relatively stable, and there is no point within the international architecture of aid decision-making where a coordinated view is taken on the aggregate distribution of aid between countries on an agreed basis (between donors or within the wider international community. In the absence of such a process, individual donor initiatives to rationalise their own resource allocation decisions may be of limited impact, and potentially may have a perverse impact, when allocation models do not take account of the activities of other donors.

9. The study also concludes that there are still strong reasons to think that poverty- and to a lesser extent “performance-” based reallocations of aggregate aid (for a given total level of aid) would improve the prospects for global poverty reduction compared to current patterns of allocation. There are also particular reasons for a donor focus on countries at risk of state failure or of collapse into (or back into) conflict – however the *form* of engagement (which may include political or military action) is at least as important as the level of aid allocated.

AID ALLOCATION: MANAGING FOR DEVELOPMENT RESULTS AND DIFFICULT PARTNERSHIPS – MAIN REPORT ON DONOR PRACTICES

1. INTRODUCTION

10. This report describes the different factors that donors take into account when determining their allocations¹ of aid to countries, with a special focus on those that do not achieve “good performer” status. The Terms of Reference (Annex B) require a review and collation of the approaches to aid allocation being used by different agencies, including the use of formal aid allocation models and aid agreements that embody specific links between recipient performance and aid allocations, with a particular focus on the criteria used to make allocations to difficult partners. It was agreed that the study should look exclusively at bilateral donors (but including the European Commission) with a view to providing coverage of all the main providers of bilateral aid. It was felt that the time and resources available for the study precluded adequate coverage of both bilateral and multilateral agencies.

11. The study has involved three main tasks:

- A review of the empirical and policy literature on aid allocation (Annex A).
- Preparation of summary Background Reports (Annexes C to J) on the largest providers of bilateral aid and more summarised material on a selection of other donors.² These have been based on donor policy documents and interviews with agency staff.
- A descriptive analysis of trends in aid disbursement (using data from the OECD DAC database and World Development Indicators) (Annex K).

12. The main report summarises the main findings on donor practices. It is structured as follows. Section 2 discusses some issues for the study. Section 3 examines the evidence on the factors that govern aid allocation decisions drawing on the background reports on donors. Section 4 examines issues relating to aid allocation to difficult partnerships. Section 5 summarises the conclusions of the study (drawing also on the literature review and data analysis).

¹ For the purposes of this study we have taken “allocation” to cover both ex ante decisions (commitments) and ex post outcomes (disbursements).

² The major donors covered are the European Commission, France, Germany, Japan, the Netherlands, the UK and the US. An additional case study has also been prepared on Sweden, and material on Australia is presented in a text box. A questionnaire (Annex A, attachment 2) was used to guide interviews and to provide a checklist of issues. The countries were selected to ensure full coverage of the policies of the six largest providers of bilateral aid. The European Commission was included because, although it is classified by OECD as a multilateral donor, the profile of its aid (and the process by which decision-making occurs) is more similar to those of bilateral donors (e.g. a relative focus on aid to geographical near-neighbours, and the influence of non-poverty considerations in aid allocation) than of most large multilateral donors. Australia was not the subject of a full case study but detail of its approach to difficult partnerships was included because of the heavy focus of its aid programme on these countries.

2. ISSUES FOR THE STUDY

13. The Terms of Reference for this study state that:

“Recent years have seen a rationalisation of the way aid is allocated among developing countries. An international consensus emerged that bilateral and multilateral official development assistance (oda) is most *effective* when directed at countries that exhibited a specific set of *conditions* that promote economic growth, provide an appropriate role for the state etc. On the presumption that the existence of these conditions is essentially within the remit of the Governments in charge, the global aid community endorsed the policy of channelling aid to the “good performers”, where performance is measured by a set of *proxy indicators* reflecting the economic and governance environment.”

14. The Terms of Reference also note three factors that may call into question this consensus – (i) a widening of the implicit objective of aid from promoting economic growth to incorporate other human development indicators, (ii) a recognition that institutions rather than policies are what fundamentally determine performance, and (iii) concerns about the reliability of commonly used proxy indicators for performance.

15. An underlying concern is whether the use of performance measures and considerations to guide aid allocations between countries, in the context of wider moves towards a greater emphasis on results-based approaches to the management of public finance in many donor countries may lead to some countries that are judged as poor performers but that are in need of aid and are potentially effective users of it receiving less aid than would be desirable. There is also a danger that individual donor decisions that are not effectively coordinated will lead to a suboptimal aid outcome (for example where donors each individually focus their allocations on countries regarded as strong performers leading to a situation where aid to that country exceeds its absorptive capacity while other potential recipients are neglected).

16. Levin and Dollar (2004a) provide evidence that aid in aggregate has become substantially more selective in terms of both poverty and of policy and institutional quality, comparing the period 1999-2002 to 1984-9 – in the earlier period they conclude (p. 1) that “aid overall was allocated indiscriminately without any consideration to the quality of governance”. They find that multilateral aid is generally more selective against both criteria than bilateral aid, and that the same donors that score high on poverty selectivity tend to score high also on poverty and institutional selectivity – among bilateral donors this includes Denmark, the UK, Norway, Ireland and the Netherlands. Some of the largest bilateral donors (notably the US and France) are not particularly selective on either measure, while Japan scores highly on the policy/institutional selectivity index but far down the poverty selectivity index (reflecting the focus of its aid on Asian countries that are relatively well-governed but not in many cases very poor).

17. Levin and Dollar (2004b) examines the pattern of aid allocation to Difficult Partnership countries³ and concludes that controlling for population, poverty and performance, DPCs receive on average around 43-44% less aid “than their policy and institutional strength predicts they will be able to absorb”,⁴ primarily due to disproportionately low flows from bilateral donors. However, the variance

³ Defined as countries that are both low income and in the bottom two quintiles of the CPIA.

⁴ Some care is needed in interpreting the conclusions of this analysis. The model used imposes a log linear coefficient on each of the variables, including the index of institutions and policies (CPIA). Since the difficult partnership dummy must be highly correlated with the index of institutions and policies, the two variables in the regression are not independent, and the addition of the DPC dummy is equivalent to allowing a less restrictive functional form for the model (i.e. the relationship between aid and CPIA may not be linear or continuous at low levels of the CPIA score). Countries that emerge as “aid orphans” under this analysis can

within the DPC group is very high, with some (particularly post-conflict countries) receiving much higher levels of aid than poverty and policy/institutional quality would predict and others much less – with this latter group characterised as including very large, very small (including landlocked countries and small island states), very poor, very badly governed and countries with a small number of donors.

18. The focus of this study is therefore to examine the features of bilateral donor policies and practices that may account for these empirically observed outcomes, as well as to examine the possible impact of ongoing and planned policy reforms.

19. Several important distinctions and issues for the study can be identified:

- First, although both poverty and performance have received increasing prominence in the policy literature, it needs to be established empirically whether (i) patterns of aid allocation have actually shifted in line with the findings of this literature and (ii) if such a shift has occurred, whether it is the result of deliberate policy decisions based on this analysis, or of other factors. In cases where absorptive capacity is limited, disbursement of aid (ex post allocation) may not closely track commitments of aid (ex ante allocation).⁵
- Second, allocation according to poverty criteria (e.g. distance from achieving the MDGs) is conceptually distinct from allocation according to performance in poverty reduction (rate of progress achieved towards the MDGs) and from allocation according to *prospects* of good performance in poverty reduction (judged by proxy indicators such as the CPIA and based on assumptions about the relationship between these and aid effectiveness). The level at which poverty reduction goals are being defined also has implications for allocation decisions – i.e. the allocation implied by a target of achieving the MDGs for Africa as a whole (all else being equal implying a focus of aid on large countries with many poor people) would differ from a target of achieving the MDGs for individual African countries.
- Third, a distinction needs to be made between allocating aid on the basis of poverty levels and allocating on the basis of need. Most (bilateral) donors make decisions about who to aid and how much aid to provide with little reference to an overall assessment of the country's aid needs or to the allocations of other donors. There may be some tension between a formula-driven allocation of aid between recipient countries and alternative approaches that are more demand-driven and based on assessment of need and absorptive capacity both by donors and by aid recipients
- Fourth, there is increasing empirical evidence that the *type* of aid provided is of critical importance for determining its impact, and that the most effective type of aid is likely to vary according to context as well as timing. This strongly suggests that a focus on aggregate allocation levels alone as a key determinant of likely aid impact or whether a country is receiving an optimal level of aid (whether it is “underaided”) is generally misplaced. In particular, if the general proposition that the effectiveness of aid increases with the quality of the policy and institutional environment is accepted, then the implied focus of attention for countries with low quality policy and institutional environments should be much more on the type of aid than its aggregate level (and in particular on ways of strengthening the policy and institutional

be described as relatively disadvantaged in aid allocation in some sense, but it cannot be concluded from this analysis alone that they are capable of absorbing more aid unless a strong empirical case can be made that the relationship between CPIA and capacity to absorb aid effectively is linear over the distribution of the CPIA indicator.

⁵ Preliminary assessment of data however concluded that using disbursements or commitments did not significantly affect the analysis in aggregate.

environment). If particular donors have a comparative advantage in providing particular types of aid⁶ or aid to particular countries this would provide a rationale for donors to adopt different criteria for deciding aid allocations.

- Fifth, a move towards results-based approaches to management (as part of a wider move to increase accountability in public spending in donor countries) does not necessarily imply a move towards aid allocation on the basis of results. For example, performance information could be used as a basis for improving aid management in each country, rather than changing allocations towards countries that achieve good performance. A further issue is the extent to which judgements of aid effectiveness can meaningfully be made (i.e. impact attributed) at the level of individual donors. Recognition of the limitations of the extent to which firmly empirically grounded assessments of attribution can be made must limit the extent to which the measured impact of aid can determine allocations. A further issue is the extent to which incentives within development agencies are well-aligned with the objectives of the agency overall. The theoretical and empirical literature suggests several reasons why this problem may be particularly problematic in government agencies dealing with development assistance.⁷
- Sixth, in using “Difficult Partnerships” and related concepts, it is important to distinguish between (i) poor performers (on the basis of outcomes – which may or may not be outside government control) (ii) countries with low levels of capacity and (iii) countries with governments that exhibit low levels of commitment to poverty reduction objectives.⁸ Commonly used proxy indicators such as the CPIA tend to conflate elements of each of these.
- Finally, aid allocation decisions are *a priori* policy decisions but when comparisons are made between these decisions and total aid disbursements then one risks not comparing like with like because total disbursements include humanitarian and emergency aid whose allocations are not decided in the same manner. Many poor performers receive relatively high levels of humanitarian assistance, and some forms of aid (particularly military and security assistance) that are not formally classified as ODA.

⁶ While the concept of donor comparative advantage is often discussed, bilateral donor policy statements do not in general seek to define comparative advantages in particular types of aid instruments, nor do these considerations appear to be influential in overall aid policy.

⁷ See for example Ostrom et al. (2002), and Martens et al. (2001). Martens notes (p.17) in particular that “a unique and most striking characteristic of foreign aid is that the people for whose benefit aid agencies work are not the same as those from whom their revenues are obtained... This geographical and political separation between beneficiaries and taxpayers blocks the normal feedback process: beneficiaries may be able to observe performance but can not modulate payments (rewards to the agents) in function of performance.” He further concludes (p. 30) that “the *nature* of foreign aid – with a broken information feedback loop – combined with the *nature* of public administrations (including aid agencies in general) – with multiple hard to measure objectives and often multiple principals too – put a number of inherent constraints on the performance of foreign aid programmes. Ostrom (2002) examines in detail the incentive structure within Sida, and a similar study is currently underway for DFID.

⁸ It is also debatable to what extent “political commitment” can be regarded as an exogenous explanatory factor. DFID’s “Drivers of Change” approach, for example, seeks to understand the underlying structural and institutional factors that influence the extent to which policy choices reflect poverty objectives.

3. AID ALLOCATION POLICIES

3.1 Overview of main features

20. Table 1 summarises information on aid allocation policies for the largest bilateral donors (including the European Commission) and for Australia and Sweden. In terms of overall policies, a distinction can be made between donors whose aid policies are principally and explicitly driven by and assessed against poverty reduction objectives including the MDGs (Netherlands, Sweden and UK), those which have adopted policies that are poverty and MDG-focused but with this commitment in the process of being operationalised (France, Germany), and those for whom poverty reduction is one among a range of objectives, with geopolitical or regional considerations appearing to be of the most decisive significance (Australia, the European Commission [excluding EDF], Japan and the US).

21. A second type of distinction can be made between donors whose policy-making processes involve an explicit and relatively centralised process of decision-making about bilateral resource allocation between recipient countries (Australia, EDF, Netherlands, Sweden and the UK) and those where overall allocation decisions are the result of decisions made across several agencies (EC External Action, France, Japan, Germany, the US). France, Germany and the US are all however strengthening the processes of inter-agency coordination and centralisation in decision-making. Several countries (Germany, Netherlands, Sweden, UK) have made explicit policy commitments on the total level of aid and/or the share that should go to identified groups of countries (such as LDCs, Sub-Saharan Africa).

22. A third distinction relates to the extent to which performance and results-based assessment criteria influence allocation decisions. The UK's Public Service Agreement (PSA) framework provides the most explicit link between the justification for spending on aid and poverty reduction targets in terms of the MDGs. The US uses results-based management as the basis for reporting and justifying spending. The EDF uses an assessment of country performance as one indicator in determining allocations between ACP countries. Both France and Germany are moving towards more explicit accountability against results as part of wider reforms to public expenditure management.

23. Most donors have classified and identified groups of countries that will serve as the focus for their bilateral programmes and with which it is considered that there will be a continuing bilateral relationship over time. For DFID, this includes sixteen countries in Africa and four in Asia that whose performance is specified as a target in the PSA. The Netherlands, Germany and Sweden have lists of partnership countries, and France identifies the ZSP group as a particular focus. The EC, has an intergovernmental agreement with 77 ACP countries. Once such a group of countries has been identified, explicit policies on allocations and the use of allocation models tend to be focused just on this group.

24. Two particular instruments stand out as involving aid allocation against explicit criteria. The first is the EDF, which is an intergovernmental agreement between the European Union and the ACP countries, with allocations based on a formula, and subject to explicit eligibility criteria, which define the conditions under which aid through this agreement can be suspended (under Articles 96 and 97 of the Cotonou Agreement). The second, very different, example is the Millennium Challenge Account, which defines criteria for eligibility for aid resources according to demonstrated performance, governance criteria and commitment to particular economic policies and invites potential recipients to apply for funds.

25. Explicit allocation models are used for analytical purposes by the Netherlands, UK and USAID. France is in the process of developing such a model. In each case the model is used to inform but not to determine allocation decisions.

26. The allocation models (including EDF) all share a focus on poverty (e.g. GNI per capita with a negative weight) and population with a positive weight (though in the case of DFID, the EDF, and the Dutch allocation model with a relative bias towards smaller countries built in) and quality of governance (e.g. CPIA quintiles) with a positive weight. The Netherlands and (from 2004) DFID both incorporate a measure of *need* in relation to the level of aid received from other donors and debt levels (Netherlands only) into the model. Each of the models involves a number of other adjustments to take account of other factors including economic vulnerability and prospects for reaching the MDGs for DFID,⁹ and is used principally as a benchmark for examining allocations *between* countries that have already been identified as focal for bilateral aid for that donor.

27. There is evidence to suggest that a significant number of donors are giving more attention to selectivity and bilateral donors in particular do explain why they provide aid to their chosen recipients and most refer to needs/poverty as an important criterion (See DFID, 2002). A large study of more than twenty donors conducted by Berthelemy and Tichit (2003) found that “most donors pay a great deal of attention to political governance when making their aid decision.” DFID’s Africa and Asia Performance Funds are examples of an attempt to allocate aid to “good performers”, as is the MCA. The criteria for making decisions on allocation from the DFID Performance Fund are however not explicit or formula-driven. The main use¹⁰ envisaged for the Fund is to provide additional budget support within year to strong performers – however careful design of the use of the instrument would be required if this use is to be consistent with promoting predictability in the availability of budget support resources and to avoid exacerbating volatility. While several other donors (such as the Dutch) are seeking to build performance measures more directly into their allocation models and processes, this generally has not yet happened on a significant scale.

28. One additional point of significance is that while the concept of global public goods as providing a justification for aid has received prominence in the literature and is in some cases cited among donor policy objectives, country allocation decisions and allocation models do not appear explicitly to take this into account, and donors have not articulated views on the level of funding required or the appropriate funding mechanisms for global public goods in general.

3.2 Main features of donor approaches

29. For the ACP countries, the **European Commission** uses a structured, formula-based approach which is based on an intergovernmental agreement (the Cotonou Partnership Agreement). While aid allocation within the framework of this agreement is based on transparent criteria (with a formal mechanism of consultation and review in situations where a recipient government fails to meet governance and other criteria), the same cannot be said for the Commission’s overall allocation of aid between regions and within other regions between countries. EC aid is not strongly poverty-focused principally because aid to countries of strategic and security interest to the European Union (especially potential members, neighbours or near neighbours in Eastern Europe and the Mediterranean) is much higher as a share of total aid than would be justified by poverty considerations alone. The Commission is discussing a common approach to guide allocation of funds, possibly using a more formula-based approach as with the EDF. However, the lack of a clearly defined overall foreign policy for the Commission to implement and to serve as a means of setting overall priorities, and the complex objectives that underlie the Commission’s aid (at least outside the ACP framework) in relation to the Member States may militate against a more transparent and criterion-based approach to aid allocation.

⁹ However, the combined impact of the economic vulnerability and MDG prospects measures for DFID is limited, amounting to around 5% or less than the total modelled allocation in all cases.

¹⁰ A supplementary use is more like a general contingency and reserve to deal with crises or unforeseen developments (such as the current crisis in Darfur) that exceed the resources earmarked for humanitarian interventions.

30. A coherent approach to aid allocation decisions in **France** is made difficult by the division of responsibility for aid decisions across a number of government ministries. There is therefore currently no single comprehensive aid budget, multiyear budget planning of aid. However, far-reaching reforms are underway (driven by wider reforms aimed at strengthening public expenditure management in France), combined with a political commitment to increase aid levels substantially (reversing the substantial fall in aid that occurred over the second half of the 1990s) and make French aid more poverty-focused. As a result, a methodology to guide allocation decisions (initially of the additional aid provided) is currently being developed, and an overall policy and aid budget is also being prepared for the first time. At the moment, the 54 ZSP countries (40 of which are in Africa) are given particular priority in allocations.

31. **Germany** uses a quite structured framework to inform the allocation of aid by country and sector; but it does not have a formal allocation model and is not likely in the near future to adopt any model which would on its own determine aid allocations. As in France, government-wide reforms (the Global Structural Policy) aimed at improving transparency and accountability in the use of public funds is leading to a strengthened focus on results-based management and policy coherence across different government programmes. Current decisions about how much aid to give do not include any formal assessment of how much aid other donors are giving – though “other donors” is an influence (among others) in the prior decision concerning the selection of countries to which Germany should prioritise in giving aid. Likewise, the current approach does not provide much room for Germany to respond to other donors’ appeals to allocate aid either to needy countries to which Germany does not currently provide aid, or to allocate significantly more aid to those to which it currently does give aid, outside the annual planning process.

32. Germany acknowledges that aid performance and impact vary from country to country and that in different ways, in some countries aid impact is particularly problematic. However, the main thrust of German policy is to try to stay engaged, though not to increase aid in such circumstances. When relationships are particularly problematic, Germany will tend first to deploy a different range of instruments and where it is feasible aid to activities aimed at enhancing and improving capacity of the recipient. Especially when these avenues are foreclosed, Germany will encourage NGOs and Germany political foundations to provide more aid to particular target groups, though it is recognised that this is not an easy option and aid levels in poor performing countries could well fall. In such circumstances it is German policy to try to encourage other donors to increase their disbursements in order that needs continue to be addressed.

33. **Japan** does not use a country-based allocation system, but rather one that is based on instruments and the budgets of different organisations, and one that has traditionally been “request-based” rather than driven by an overall country envelope. Allocations of aid across regions are made on the basis of regional policy statements and other policy commitments, but are not based on explicit criteria or allocation models, though the revised ODA Charter sets out the broad objectives of Japanese aid.

34. Aid from **the Netherlands** is coordinated within the Directorate General for International Cooperation of the Ministry of Foreign Affairs and includes a process of setting three budget allocations plans at the country level to be agreed with Dutch Embassies – this system is moving towards one of multiyear strategic planning. Bilateral aid is focused on a list of 36 partner countries with which it is envisaged that the Netherlands will have a long-term development partnership arrangement. Within the partnership group, an aid allocation model is used in each resource allocation round as a guide. This takes account of poverty, debt, population (with a bias towards small countries), and total aid receipts, along with IDA eligibility and CPIA quintiles. However, this modelling exercise is used only as a guide and other considerations (quality of proposals, performance of the Dutch country programme, presence of other donors, the political situation) are also brought into consideration. Revisions to the model are intended to strengthen the role played in allocation decisions by the performance of the country programme.

35. **Sweden** has a record of aid allocation policies that are strongly focused on the poorest countries, but does not use an aid allocation model or a framework with specific allocation criteria when deciding on aid allocations. There is a focus on countries with “long-term development cooperation,” though the number of countries with which Sweden maintains aid programmes is under discussion.

36. **The United Kingdom** provides DFID with a clear responsibility for aid policy and delivery, against a set of objectives and detailed targets defined in the Public Service Agreement and Service Delivery Agreement. These objectives are closely based around the MDGs. This provides in principle an extremely clear framework of accountability. There are specific policy commitments relating to the overall level of aid, aid to Africa and for HIV-AIDS, and the share of aid to be provided to low-income countries. An aid allocation model based principally on GNI,¹¹ the CPIA quintiles, and with an adjustment to reflect the level of aid provided by other donors, is used as part of the process of developing budgets and reviewing allocation decisions. The model is used within DFID’s regional groupings, rather than to inform overall allocation decisions, and other considerations are also brought into decision-making. In addition there is in practice a significant degree of flexibility at the country and regional level for aid to be re-allocated between countries, so that ex post allocations may at least in the short-term differ significantly from ex ante plans. In recent years as aid volumes have expanded rapidly, a growing amount of aid has been retained unallocated ex-ante to be disbursed in a flexible basis as different needs arise during the year.

37. While in principle DFID’s performance management framework provides an exceptional degree of clarity about DFID’s objectives and specific targets, attention has been drawn in the recent past to a number of studies to the underlying weakness of DFID’s performance assessment and evaluation systems. In particular, the lack of a clear link between DFID’s activities and organisational effectiveness, and the high level MDG targets creates some problems for determining the overall effectiveness of UK aid.

38. Following a prolonged period of decline, **US** aid levels have increased rapidly in recent years. However, the most recent, and major increases of the last two years are unlikely to be sustained. Thus in the near term, overall US aid levels will remain volatile and unpredictable, though the long term trend is likely to remain on an upward path. Particularly since the 2002 Monterrey conference, the United States has played a growing role in encouraging the overall increase in aid levels at the global level, while channelling proportionately less of its own aid to and through multilateral channels. Its New Compact for Development, announced in 2002, places particular importance in collaboration between US and other donors.

39. The administration and oversight of US aid has always been extremely complex – with no single foreign aid budget and responsibilities shared across more than 50 government agencies and departments and more than 40 budget lines, all subject to Congressional influence and approval. USAID has been the most important single agency but now handles less than half of total American aid and this can be expected to fall further. The changes announced as part of the New Compact for Development have increased this complexity – through the establishment of the Millennium Challenge Corporation, the use of supplementary aid and special funding arrangements for Afghanistan and Iraq, and the allocation of significant amounts of aid to Global Funds to fight HIV/AIDS, TB and malaria.

40. However, there are initiatives also to improve overall policy coordination in particular through the development of a Joint Strategic Plan for USAID and the Department of State, and the establishment of mechanisms to improve cooperation. One consequence of the establishment of the MCC (focused explicitly on strong performers) is an increased attention of USAID towards failed and failing states.

¹¹ Versions of the model used before the current year included an explicit bias towards countries with small populations (allocation was proportional to population^{0.6}). In the current model, however, a cap on modelled aid to India has been imposed.

Through the MCA, 12% of US aid was allocated to 16 countries identified based on commitment to good governance, investment in health and education and economic policies that foster enterprise, open markets, sustainable budget policies and support for individual entrepreneurship.

41. The US has operated within a Results-Based framework since the 1993 Government Results Performance Act. USAID has developed a Strategic Budgeting Model to help align aid need and commitment, and to ensure funds are used as effectively as possible. The model is based on development need, country commitment, foreign policy importance, and programme performance (based on a performance rating tool).

Table 1. Summary of donor allocation policies

Country	Role of MDGs	Country Allocation Policy	Allocation Model	Role of Performance Criteria
Australia	Relations with neighbouring regions and countries main influence	Based on bilateral decisions.	No	No formal role. The decision to increase aid to for example Papua New Guinea and the Solomon Islands in 2003 was a response to continued deterioration in the governance climate and its implications for local and national prosperity
EC	Poverty reduction main objective of development policy but overall aid allocation across regions does not reflect this (within regions aid should be directed to poorer countries). No overall criteria for External Action budget – multiple objectives	Formal policy for EDF External Action budget influenced by variety of decisions. No overall allocation policy though need to place more emphasis on results in allocation decisions	EDF Allocations directly determined by model criteria and formal intergovernmental agreement	Performance Country Index one component of EDF Financial Allocation Framework
France	Poverty reduction adopted as “main thrust” and increasing attention to the MDGs	No centralised allocation policy, but this will change by 2005. Focus on ZSP countries	Initiative to develop methodology for allocating additional aid resources	Reforms to be implemented under legislative changes from 2006 will strengthen management by objectives and use of results-based indicators
Germany	MDGs central to “Programme of Action 2015” but this remains to be fully operationalised. BMZ Task Force to support process of mainstreaming poverty goals across aid instruments.	BMZ carries out annual review of allocations. Policies for 30% bilateral aid to Sub-Saharan Africa and 30% to LDCs. Identification of priority partners	No formal model but quantitative and qualitative factors taken into account (governance, economic and social context, crisis/conflict, aid performance and commitment to global agenda)	KfW and GTZ have results-based framework but not fully operational and does not drive allocations. Moves towards results-based management of federal spending. Aid performance assessment one factor in allocation decisions

Country	Role of MDGs	Country Allocation Policy	Allocation Model	Role of Performance Criteria
Japan	Poverty reduction one of four priority issues in ODA Charter as revised 2003	Instrument and institution, rather than county-based allocation, and "request based" approach Country Assistance Programmes define overall nature of aid relationship with each country	No formal allocation model	No formal role.
Netherlands	MDGs defined as means to achieve poverty reduction which is main policy objective of 2003 Policy	50% of bilateral budget to Africa Minimum level of aid set for each core country Model used to guide allocation decisions to countries (through embassies) for Partnership Countries	Allocation model based on need (GNP pc, debt pc, ODA pc) and performance (CPIA, IDA eligibility). Adjustments for LDC and SSA	Intention to use country performance tracking system and build into model
Sweden	Policy traditionally strongly focused on poverty reduction and poorest countries. Achievement of the MDGs are central in Swedish development policy, but the MDGs are not used as criteria for selection of partner countries	Three year country plans set indicative allocations Focus on partner countries At least 0.25% GNI to LDCs	No formal model or framework for allocation	No formal role for making allocation decisions. Results against the MDGs are one part of the results based management approach, together with periodic general assessments of the impact on poverty of domestic and external measures in specific countries and regions.
UK	PSA defines DFID objectives and targets in terms of MDGs	Commitments to total aid for Africa and 90% to LICs. Models used to provide overall guides for allocation but do not determine decisions	Used as guide for allocations between LICs within three regions (Africa, Asia, Europe/Middle East/Americas). Based on GNI, and CPIA quintiles with minor adjustments for vulnerability and prospects for achieving MDGs and large	"Performance Fund" and use of CPIA in Allocation Model Accountability against MDG outcomes

Country	Role of MDGs	Country Allocation Policy	Allocation Model	Role of Performance Criteria
			adjustment for other donor flows.	
US	Multiple objectives, agencies and instruments Aid has vital role in supporting US geo-strategic interests MCA as means to increase aid to good performers and committed developers (not necessarily poorest)	Rapid expansion of ODA from low levels relative to GNI Joint Strategic Plan between USAID and Department of State to improve coordination Commitment to increase aid funds through the MCA Africa identified as a priority.	USAID Strategic Budgeting Model based on development need, country commitment, foreign policy importance and programme performance. Model informs rather than determines allocations	Results-based management established from 1993 – PART assessment MCA based on eligibility criteria – good governance and sound economic policies. Assistance to achieve criteria for countries judged to be committed Key goal is to expand assistance to countries achieving good governance

4. AID ALLOCATIONS AND DIFFICULT PARTNERSHIPS

4.1 Summary of data

42. The “difficult partnership” concept broadly understood covers a range of countries with very different features and problems and for some donors is not regarded as an analytically meaningful one.¹² In addition, the countries cited by different donors as “difficult” varied considerably and in some cases countries judged as relatively good partners under some criteria were classified as difficult by other donors using different criteria. As a result, it is by no means easy, or uncontroversial to select data to describe the characteristics of allocations to “difficult partnerships.” For the purposes of this study, the LICUS definition (see 4.1 above) has been used.¹³

43. Table 2 summarises bilateral aid to LICUS countries over the three years to 2002 for which information is available. They show substantial increases in the absolute amount of aid to these countries and in their share of total bilateral aid for the US, Netherlands, EC, UK, Norway, Germany, Canada and to a lesser extent France. Absolute amounts fell for Japan and Australia, and were unchanged for Sweden.

¹² For example, it was pointed out that in terms of the terminology used by the Netherlands, the concept was oxymoronic. For agencies engaged in lending the concept is probably more clearly defined since it can be seen as relating quite directly to creditworthiness.

¹³ It should be noted that the list of countries classified by the World Bank as LICUS is not in the public domain.

Table 2. Donor ODA net disbursements to LICUS countries 2000-2002¹⁴

	US\$			% total aid		
	2000	2001	2002	2000	2001	2002
Australia	343	254	287	51%	46%	48%
Canada	76	85	199	12%	13%	25%
EC	426	664	765	7%	10%	10%
France	345	319	403	11%	11%	10%
Germany	274	313	440	12%	13%	15%
Japan	642	500	487	8%	8%	9%
Netherlands	136	304	427	10%	16%	22%
Norway	122	142	213	18%	21%	26%
Sweden	122	108	123	14%	14%	16%
UK	201	220	393	10%	11%	15%
US	419	485	1368	7%	8%	15%

Source: OECD/DAC Statistical Database

44. In a number of cases, bilateral aid to LICUS countries was dominated¹⁵ by one or two donors (e.g. The US and EC in Angola (16% respectively) and Liberia (28% and 20% respectively); France and Japan in the CAR (28% and 25% respectively); France in Cameroon (18%), Comoros (41%), Congo Republic (28%) and Niger (15%); France and Germany in Togo (34% and 15% respectively); the EC and France in Chad (18% respectively); the EC in Burundi (26%) and Guinea-Bissau (30%); the EC and Norway in Somalia (17% and 15% respectively); The EC and Australia in Solomon Islands (44% and 43% respectively); Australia in PNG (79%); Japan in Lao PDR (35%), Myanmar (48%), Cambodia (25%), and Zimbabwe (22%); Japan and the US in Uzbekistan (29% and 30% respectively); and the US in Guinea (16%), Haiti (45%), Nigeria (18%), Sudan (15%), and Tajikistan (29%).

45. Levin and Dollar (2004b) identify nine DPC countries as unambiguously “aid orphans” in 2002 in that they received substantially lower aid than would be predicted (Burundi, CAR, DRC, Congo Republic, Niger, Nigeria, Sudan, Togo and Uzbekistan). By contrast, Cambodia, Guinea, Laos, Papua New Guinea and Sierra Leone received substantially more aid than would have been predicted. Trends in aid to these countries are discussed in Annex K.

46. The striking feature of this list is that eight of these nine are located in a practically contiguous band across central Africa, with six of these eight countries being francophone. This suggests that regional factors are likely to be decisive in explaining the low levels of aid that they have received. These include the following:

- Other than for France (and with the exception of Nigeria as an oil producer and mineral exports from some of the other countries notably DRC and Niger), the region has been of limited strategic, security or commercial interest to other bilateral donors (in contrast to, for example, Cambodia, Laos and Papua New Guinea), while there have been intractable problems of conflict and political uncertainty across the region.

¹⁴ LICUS countries here are those classified as such according to the World Bank in at least two of the three years given.

¹⁵ The average percentage share of total aid disbursements for the period 2000-2002 to the recipient country coming from one donor exceeds 15%.

- A number of these countries have traditionally been large recipients of aid from France and so have been particularly affected by the sharp reductions in French aid from the mid-1990s until French aid began to recover in 2002. This was a particular factor in CAR, Congo Republic, Niger and Togo. Aid from other bilateral donors generally followed a similar pattern to that of France. IDA aid also fell sharply in CAR and Togo, though by contrast IDA aid increased in Niger and was particularly erratic in the Congo Republic.
- The larger countries within the group (DRC, Nigeria, and Sudan) have gone through prolonged periods of civil war and/or military rule during which relations with donors were extremely difficult or hostile. Nigeria has emerged from military rule but seen only a limited increase in aid (which in 2003 was still lower in absolute terms than under military rule in 1993). DRC saw a twelvefold increase in aid in 2003 (to over \$6.4 billion) driven by extremely large commitments from bilateral donors (US, France, Belgium, Germany and Italy). In Sudan, there were substantial falls in aid from all major bilateral donors after the early 1990s until US and EC aid led an increase after 2000, with an even sharper fall in IDA provision (which ceased after 1994).

4.2 Donor policies towards “difficult partnerships”

47. Among the donors reviewed for this study, only Australia (which as shown in Table 2 is the donor which is proportionately most engaged with LICUS countries) appears to have a fully articulated policy relating to engagement with what are defined as “poor performers” as part of a “Graduated Strategy.” Otherwise, the main formally articulated policies that are relevant relate to the conditions under which aid can be suspended. In the case of the EDF, these (and the consultation and decision processes involved) are formally defined under the Cotonou Agreement.¹⁶ Japan’s ODA Charter allows for the suspension of aid if defined principles of development cooperation are breached.

48. The main features of donor policy can be defined as follows:

- Increasing analytical attention to the problems of how to engage most effectively with what are variously termed “poor performers” and “fragile” or “failed states,” with post-conflict countries, and with those that are falling furthest behind in achievement of the MDGs.
- As noted in the previous section, the use of the CPIA and other measures of governance as one criterion to take account in aid allocation and more general engagement decisions.
- A general view that, while it is important to understand what forms of engagement work best in different circumstances, the formal identification of a particular group of problematic countries (like the LICUS group) will not be of value for policy purposes. This is partly because it is felt that any such classification will necessarily group together countries for which the most appropriate response or form of donor engagement may be very different, because of doubts that the measures available to provide a basis for classification are reliable or objective enough, and because of a recognition that country circumstances can quickly change. As a result, it is not generally the case that specific criteria are used in determining allocations to problematic countries – rather that judgements on allocations and choice of instruments are made on a case by case basis.
- In terms of the choice of aid instruments, humanitarian aid is usually (much US aid for southern Sudan during the war years was not strictly speaking humanitarian aid) the main form of aid for countries in conflict or where it is not considered possible to work effectively with government

¹⁶ Article 96 relating to human rights abuse and weak governance, Article 97 relating to corruption.

on wider development objectives (such as Zimbabwe). However, it is difficult to generalise about the choice of aid modalities. For instance, Australia has used budget support as an instrument in PNG and Solomon Islands, in cases where it has effectively taken a high degree of control of government finances through placing staff in key positions.

- A recognition that appropriate responses and forms of engagement vary most significantly between countries that have weak institutions but are generally committed to development and poverty objectives, those whose governments are regarded as not committed to development objectives or are at loggerheads with the international community (e.g. Myanmar, North Korea, Zimbabwe), and those where the state apparatus has broken down (e.g. Somalia).
- The development of new instruments (such as the Dutch Stability Fund and the EC Africa Peace Facility and Stability Instrument) that are intended to promote and maintain peace in post-conflict or conflict-threatened countries (which may not necessarily be among the poorest, and which may cover forms of assistance like the financing of regional peace-keeping forces that may not be included within agreed definitions of ODA).
- A policy (at least among larger donors – smaller donors may more often decide that) of seeking to maintain engagement (a policy that is particularly explicit with the US) within difficult partner countries, and to seek where feasible to continue or establish programmes that are capable of reaching the poor or of promoting the prospect of change, if necessary operating outside government and through civil society organisations, and through the provision of humanitarian assistance.
- In the case of the US, a refocusing of USAID’s attention on failed and failing states (i.e. those not regarded as close to eligibility under the MCA).

49. The increasing concerns with international security issues and terrorism have raised the attention given to the problem of state failure and its likely spill over effects. This has led to an increased focus on, and provision of aid to, particular countries. In general, which countries have received the greatest attention (and from which donors) has been determined by the degree of the wider international risk and threat from developments in the country, rather than the scale of the direct poverty or humanitarian problem in the country and its neighbours.

50. Table 4 provides a summary of the way in which different donors understand and use difficult partnership concepts. Further details of what this means in practice can be found in the different case studies (Annexes C to J).

Table 3. Use of difficult partnership concepts

Country	Use of Difficult Partnership Concept
Australia	“Graduated Strategy” for “poor performers. ”Fragile States” central to Australian development policy with approaches that builds on the World Bank’s LICUS approach
EC	9 th EDF allows suspension of aid under Articles 96 (human rights, governance) and 97 (corruption) after appropriate consultation, and use of MTR to adjust aid provision to performance and need Definitions of “difficult partnerships”, “effective partnerships” and “post conflict situations” articulated

Country	Use of Difficult Partnership Concept
	Use of Country Conflict Assessment as tool for increasing awareness of conflict issues and risks
France	<p>No formal use of concept but increasing attention to appropriate policies and choice of aid instruments for “fragile states” and states emerging from conflict. Establishment of grant-based window for post-conflict countries.</p> <p>Approach will tend to be to try to maintain aid (high proportion of ZSP countries fall within DP or similar classification) and to use humanitarian aid</p>
Germany	<p>No formal use of concept but identification of five criteria to influence nature and volume of aid to particular countries, with strong focus on good governance.</p> <p>Growing focus on post-conflict countries.</p>
Japan	<p>Japan has articulated its understanding and definition on “fragile situations”, “vulnerability”, and “difficult partnerships”. The review and the development of a different set of criteria and standards which the recipient government and NGO’s must meet when receiving aid in “fragile situations” are underway.</p> <p>Does not consciously use CPIA or related criteria in aid decisions</p> <p>Post conflict countries identified as priority.</p> <p>Charter allows suspension of programmes if principles of development cooperation breached</p>
Netherlands	<p>Failed states identified and defined as cases where government to government partnerships not effective</p> <p>CPIA quintiles used in aid allocation model</p> <p>Stability Fund identified as instrument to support fragile states</p>
Sweden	<p>No formal use of DP concept.</p> <p>Poor performers identified and defined in Parliamentary report as having insufficient capacity or will to implement poverty reduction policies – implies different approach and instruments to be used.</p>
UK	<p>CPIA quintiles used in aid allocation model</p> <p>No systematic use of concept in decision-making</p> <p>Developing approach based on “difficult environments” where the state is unable or unwilling to harness domestic and international resources effectively for poverty reduction</p>
US	<p>Lack of political will and commitment seen as the key factor determining capacity to use aid effectively</p> <p>Identification of fragile and weak states as of major foreign policy importance – critical need for engagement.</p> <p>Fragile states classified as (i) failing states with growing inability or unwillingness to assure provision of basic services and security (ii) failed states where government does not exercise effective control or provide services for key parts of the country (iii) recovering</p>

Country	Use of Difficult Partnership Concept
	<p>states, which are weak but on an upward trajectory.</p> <p>USAID focusing increasingly on failed and failing states – including Office for Transitional Initiatives</p>

5. CONCLUSIONS

51. The main conclusions of the review of donor policies and the wider literature review can be summarised as follows:

- First, while the literature on aid allocations is dominated by the development/growth/poverty use of aid and its impact, and some donors are explicitly reallocating “development” (as opposed to humanitarian aid and thus not ALL aid) aid to take account of these factors, current aggregate aid allocations are still significantly shaped and informed by other criteria of which the most significant relate to concerns about regional (Australia, EU Japan) or global (US) security and political relations. Former colonial links remain significant in explaining the aid allocation patterns for France and the UK – but more in determining the countries with which there is a bilateral relationship rather than ensuring particularly high or stable levels of aid.
- Second and flowing from this, the aid allocation literature provides strong evidence to suggest that if aid were allocated differently, providing more to the countries that needed it in terms mainly of the levels of poverty and current levels of aid, then it could have a far greater effect and impact on poverty alleviation. A second group of countries that may be of critical importance in relation to overall development outcomes is those at risk of state failure or collapse into conflict. A review of the pattern of aid allocation to post-conflict countries and the evidence of the dire development consequences of state collapse and civil conflict suggests that effective action (which may or may not be in the form of aid allocation, but is more likely to involve decisive international political, and in the last instance military, intervention) to prevent this would provide the greatest dividends.
- Third and more recently, the literature not merely shows that policies, content and commitment by recipient matter in terms of impact and effectiveness, but also that if aid were additionally allocated to those countries which both needed it and were able to use it better then even more people would be lifted out of poverty. The empirical size of this effect is disputed – however it appears that reallocation according to poverty and need factors (including population size) would be of greater significance in terms of poverty impact than allocation according to performance, at least above some minimum criterion in terms of capacity to use aid effectively.
- Fourth, there is growing evidence to show that as donors are being influenced by and trying to focus more on results-based management approaches, they are increasingly open to considering how to link aggregate allocations of aid with aggregate impact, though the practical outcome of this still varies enormously across donors.
- Fifth, as donors focus on trying to marry allocations to effectiveness (and to justify aid budgets against results, notably in terms of achievement of the MDGs), pressing questions are raised about how to address the needs of poor countries and poor people in poor countries where aid is clearly less effective. In the context of still significant shortfalls in overall aid levels, to the

extent that aid is channelled more to those who need it and where it appears to be better used, less will be available to those who need it but where the impact appears less good.

- Sixth, even allowing for the overall biases in aid allocation policies noted above, the aid allocation practices of bilateral donors do not appear *prima facie* to be sufficiently well-coordinated to even out the very wide differentials in aid receipts between countries. For instance certain favoured recipients (for example Mozambique and Uganda) have seen large increases in aid from several donors simultaneously. While there are reasons to think that these countries are relatively effective users of aid, it is not clear that this remains the case at the margin as aid increases to levels that may exceed 50% of total public spending. Bilateral aid disbursements also exhibit very high levels of year to year volatility which could militate against aid being used effectively by recipients.
- Seventh, in relation to allocations and policies towards “difficult partnerships,” it is not generally the case that specific factors or allocation principles are used, and the formal identification and classification of such countries is not generally felt to be desirable, other than in extreme cases where there is non-compliance with key principles of partnership or formal aid agreements such as to render government to government aid impossible or require it to be severely restricted. The general approach of all donors (other than in cases where decisions are taken by smaller bilateral agencies to restrict the number of countries in which they seek to engage) is to maintain engagement where possible, and this approach has become more explicit as the concern about the potential spill over effects of state failure have grown. While there is a tendency to try to operate more through NGOs and through independent project modes of intervention, France, the European Commission and Australia have all used budget support in LICUS countries.
- Eighth, aid from the largest bilateral donors is being provided for motives that are not purely based on poverty reduction objectives although the latter have been made more explicit in recent years and are formally the sole or major justification for development assistance for some donors. Security and regional relations are the most significant drivers of aid allocations for donors (cultural issue are particularly important in the case of France) with poorer and/or potentially unstable neighbours (Australia, Japan, the EU) and for global superpowers (now just the USA, but in the past the Soviet Union). An interesting phenomenon is that the bilateral aid of EU member states appears to be becoming increasing poverty-focused in its allocation, while aid provided through the European Commission is increasingly heavily focused on its Eastern and Southern neighbours and driven by considerations of economic, political and security relations.
- Ninth, in the light of this clear multiplicity of objectives, the validity of assessing all aid purely in terms of its poverty reduction impact may be questioned.

52. The overall conclusion is that donors are undoubtedly trying to ensure that their aid expenditure is being used more effectively. However, the specific concern that these policies are leading to aid to “less effective” countries being reduced more than is desirable do not appear to be borne out in general, though some countries are significantly underaided and may be “aid orphans”. The analysis by Levin and Dollar (2004b) suggests that this is overwhelmingly a regional phenomenon, concentrated on a band of countries across central Africa, which were (for the smaller countries) disproportionately affected by reductions in French aid, reinforced by similar reductions from other donors and from IDA, and for the larger countries (DRC, Nigeria, Sudan) reflects very difficult relations with donors over long periods of time.

53. The continued engagement of donors with difficult partnership countries is the result of a combination of factors. First, the objectives of bilateral donors include concerns about security and the risks of state failure – these concerns are prompting continued or increased engagement in those countries

that are seen as presenting a particular risk to the international community or to particular donors. Second, donors are using different forms of engagement and aid modalities as a way of dealing with poor performers.

54. The critical conclusion for international policy is that donor policies in aggregate do little to ensure that aid allocations to individual countries are predictable, clearly criterion-based or relatively stable, and there is no point within the international architecture of aid decision-making where a coordinated view is taken on the aggregate distribution of aid between countries on an agreed basis (between donors or within the wider international community. In the absence of such a process, individual donor initiatives to rationalise their own resource allocation decisions may be of limited impact, and potentially may have a perverse impact, when allocation models do not take account of the activities of other donors.

55. The study also concludes that there are still strong reasons to think that poverty- and to a lesser extent “performance-” based reallocations of aggregate aid (for a given total level of aid) would improve the prospects for global poverty reduction compared to current patterns of allocation. There are also particular reasons for a donor focus on countries at risk of state failure or of collapse into (or back into) conflict – however the *form* of engagement (which may include political or military action) is at least as important as the level of aid allocated.

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ANNEX A: LITERATURE REVIEW

A1. Introduction

1. This Annex to the Report provides a brief overview of the existing, especially the more recent (and rapidly evolving) literature on the allocation of official development assistance. The issues involved are wide-ranging and complex, potentially encompassing influences on aid allocation decisions which go beyond a more narrow development focus, as well as the literature on the evidence of the impact of both development and humanitarian aid and the extent to which this evidence informs and shapes decisions about how much aid is - or should be allocated by individual donors or donors as a whole, and in what form. Clearly in the space of just a few pages it is not possible to go into any issue in great depth. Thus the approach taken here is to highlight the core issues and themes and refer readers to the key texts in the literature where the detail can be found.

2. The Appendix is divided into five sections. The next section provides an overview of trends in aid and highlights the key issues around which there is broad disagreement on allocations and linked policy issues. Section 3 reviews the general literature on aid allocations and Section 4 focuses on the literature discussing aid to poor and problematic recipient countries. Finally, Section 5 identifies a number of gaps in the existing literature of particular concern to donors wishing to give more prominence to poor and problematic aid recipients, focusing on six areas where additional work might help to fill some of these gaps.

A2. Background and context

3. The amount of aid allocated to different countries is in part related to the total amount of aid provided by each donor. In this section, we provide an overview of aggregate quantities of aid provided in the recent past and current assessments of future aid flows and summarise the contemporary consensus about aid's impact.

A2.1 Trends in aggregate aid allocations

4. Over the past ten years, aggregate trends in aid levels show that the overall volume of ODA from DAC donors first contracted in real terms and then, after 1997, began to expand again, rising by almost four percent in 2003. By 2003, ODA volumes (net disbursements) in real terms were a third higher than the level recorded in 1997, but only 9% higher than in 1994.

5. Yet these recent upward trends in aid volume mask differences across the donor community. Between 2002 and 2003, net disbursements from 10 DAC donors fell in real terms, with falls of over 10% recorded for five donors, following contractions reported by eight donors in from 2001 to 2002, and eight from 2000 to 2001. In contrast, between 2002 and 2003, 13 DAC donors (including the EU) reported increased aid in real terms, with increases of over 10% recorded by four donors. In the four years since 2000, of the six largest DAC donors, four have significantly increased their aid volume in real terms (UK, US, France and the EU), two have seen significant falls (Japan and the Netherlands) while German aid in real terms has begun to expand again, albeit modestly, after almost a decade of steady decline. Japan, which in the early 1990s was the single largest aid donor, has reduced its aid budget by 27% in the six years to 2003. Over the past ten years, when the aid provided by the two largest donors – Japan and the

United States – moved in the same direction, either expanding or contracting, overall aid flows similarly moved.

6. What are the prospects for aggregate aid levels in the coming few years? At the meeting in Monterrey Mexico in March 2002, donors committed themselves to rapid increases in aid to 2006. OECD/DAC expectations in early 2004 were for total ODA to rise to \$75 bn (at 2002 prices and exchange rates) by 2006 (2004:21). These expectations may well prove to be exceeded as the volume increase will be significantly higher if agreement is reached on the introduction of the International Financing Facility (IFF) (see HM Treasury, 2003). Additionally, particular donors have already announced substantially higher aid volumes than previous years. Thus in its 2004 spending round the United Kingdom announced annual increases in aid averaging 9.2% a year to 2007-8, while France has recently committed itself to raise ODA progressively - to 0.42% of GNI in 2004, 0.44% by 2005, 0.5% by 2007, and to 0.7% by the year 2012. Most notably since 2002, United States' aid flows have almost tripled from \$12.9bn in fiscal 2002 to \$33.2bn in fiscal 2004, including \$18.6bn for Iraq (Woods *et al*, 2004), though they are expected to fall back to \$16.2 bn in 2005, still 24% higher (in current prices) than in 2002.

A2.3 *Aid, its purpose and impact*

7. How do recent trends in aid flows as well as near-term projections of future aid volumes compare with the amounts of aid needed? The aid literature has always included warnings of the dangers and adverse consequences of too much aid: the aid dependency literature flourished particularly, in the decade from the mid-1980s to the mid-1990s (see, for example, SIDA, (1996) and provided some useful insights into contexts where aid was likely to be less productive (see Azam *et al*: 1999 for contexts in which aid is likely to be less productive and the problems arising from Dutch disease). Yet the current prevailing view is that there is still insufficient aid provided to poor countries: see for instance Devarajan *et al* (2002) which suggest that aid volumes need to be raised by between 100% and 200% above prevailing levels and UN, 2003:11. However, ongoing work by the UN Millennium Project (UNMP) and summarised in its draft preliminary final report (September 2004) suggests that even these high targets for aid based on need are likely to fall well short of what is likely to be required to meet the MDG targets: very preliminary estimates suggest that ODA needs to be \$156bn a year in the period 2005-7, rising to \$188bn by the years 2013-15, indicating a threefold increase above current levels. Relatedly, following discussions of “aid fatigue” especially prevalent in the early 1990s, in spite of some largely short-term downward and country-specific trends (for instance in Japan where support has fallen and Germany here it has never been particularly strong), there still seems to be significant public support for aid across the DAC donor countries (over 80%) including some countries where there is strong support for increase in aid (see Rogerson *et al* (2004) and Stern (1998)).

8. Public support for aid is, in turn, in part related to the linked views that overall aid “works” (ie it is effective) and that we know more and more about the circumstances and contexts in which it does not work. Particularly influential here in recent years has been the work of the World Bank and the seminal contribution by Burnside and Dollar (1997 and 2000), updated in Burnside and Dollar (2004) which outlined core criteria and the context under which aid was found to be effective, namely when provided to poor countries which have in place policies and institutions, including governance attributes, conducive to its being used effectively and productively. Although the work of Burnside and Dollar has been subject to some strong challenges and critiques (see below), the work that they, as well as some of their critics have done, has helped to shape a broad consensus on a number of key issues about aid and its effects. Substantially eclipsed from current debate about aid and its effectiveness have been those contributions which have argued on the basis of evidence that there are no virtuous effects of aid (of which the most recent influential was Boone (1994 and 1996) or on theoretical grounds (of which perhaps the most well known was Peter Bauer).

9. Building on this last discussion, we end this section by highlighting four areas/issues from the wider literature on aid which inform and in certain circumstances help to shape the discussion on aid allocation, and around which there is broad agreement across the donor community.

1. Especially in the decade of the 1990s, a core purpose of official development assistance was increasingly seen as contributing not merely to development “in general” but to poverty alleviation in particular. Humanitarian aid (emergency and distress relief) was to be provided to address immediate and urgent needs. However, as discussed below, the aid budgets of some agencies have, in more recent years, been influenced by security priorities, some of which do not sit comfortably with poverty-focused aid allocations. Nevertheless, donors (and recipients) are committed to the achievement of the (11) Millennium Goals, including halving the numbers of people living in poverty, by 2015, and, by implication, by ensuring that resource-poor countries have sufficient resources to enable them to achieve these goals. It is widely agreed among donors that more aid is needed by poorer countries both because a high proportion of poor countries live in poverty and because they have fewer opportunities to access non-concessional funds and resources.
2. Yet it is considered no longer sufficient to judge aid and aid levels merely on whether it is needed. Influenced by changes occurring in other areas of government, there is a growing, and now strong, consensus that aid needs to be judged on the results achieved, on outcomes rather than on aid inputs and even on aid outputs. More and more DAC donors have are developing tools, methods and approaches to assess the results of their interventions through different forms of results-based management (for a summary, see Lavarge, 2002).
3. The impact of aid is related to the context in which it is inserted – in short there are factors (though precisely which ones and their importance are still debated) which enhance and others which reduce its impact. Understanding how aid “works” in turn shapes decisions on either or both how much can (effectively) be provided and the different forms in which it should be channelled.
4. As noted above, there is broad agreement that aid’s impact and effectiveness will be shaped by the context in which it is provided, including especially the wider institutional and policy environment in which it is placed and the capacity of the recipient to use the aid funds effectively. Donors are also agreed that effectiveness will be influenced markedly by the relationship between donor and recipient, by the degree of overlap between the donor and recipient on strategies and approaches to address poverty and the priority, and by the commitment of the recipient (and the donor) to development. Against this backdrop, there is widespread agreement among donors that aid effectiveness is best achieved by developing “partnerships” between donors and recipients and the concomitant political commitment, ownership of and minimal ability to implement poverty alleviating strategies. Indeed most donors would concur with the OECD/DAC view that aid will “only work where there is a shared commitment all the partners” (OECD, 1996:1) and with the February 2003 Rome Declaration on Harmonisation: “We attach high importance to partner countries’ assuming a stronger leadership role in coordination of development assistance... The key element ... is a country-based approach that emphasises country ownership- and government leadership...” (OECD, 2003:65).

A3. The overall allocation of aid: trends, debates and discussions

10. Aid allocation studies have been conducted for well over 30 years and the overall literature is voluminous and growing. The literature on aid allocations falls into distinct clusters.

- A group of studies which describes the way that donors, individually or together, allocate their aid funds, both currently and over time. Over time, individual aid allocation studies of the US, the UK, France, Germany, Japan and Germany have been particularly prominent though there have been recent studies of multilateral aid.
- A group of studies which attempts to analyse the allocation of aid over time, including by both donor and types of recipient. Some of these studies have included discussion on the why donors do or might have allocated their aid in particular ways.
- A major focus of many of these studies has been the attempt to test the degree to which donor interest, as opposed to and contrasted with recipient need has influenced and helped to shape the allocation of aid.
- Another focus of these studies has been to try to unpackage how much aid different countries might need/require. Some studies have highlighted the volatility of aid allocations and accompanying problems this causes (for example, see Nunnenkamp (2002)).
- Finally, and most recently, some aid allocation studies have attempted to incorporate and track dimensions of aid quality into the quantitative analyses of trends (see for instance the work of Roodman, 2004).
- Some aid allocation studies have attempted to ascertain the extent to which the allocation of aid has been shaped and influenced not merely by recipient need but by the likely impact of that aid – in short, in a climate where the results and impact of aid have been seen as increasingly important, has more aid tended to be channelled (proportionately or absolutely) to those recipients where it is likely to be “better used” and less aid to those where the conditions for its effectiveness are deemed to be less benign?
- Some studies are prescriptive and have strong normative conclusions and recommendations, such as those by Collier and Dollar (1999) and (2002) and Clemens et al (2004) and, as will be seen below, some of the conclusions and recommendations drawn are still quite sharply contested. Methods of analysis have become increasingly sophisticated over time; in particular the use of econometric models have allowed analysts to incorporate donor interest, recipient need and policy performance variables into a single model which, it is argued reduce the bias (and biased conclusions) of earlier studies. In recent years, the work of McGillivray and those emanating from the Center for Global Development, and earlier, of McKinlay and Little have been particularly important.
- A group of studies undertaken by individual donors who wish to develop more rigorous approaches to aid allocations for themselves, some of whom have developed, with differing amounts of rigour, their own aid allocation models.

11. What do these different studies tell us about the allocation of aid? That aid is provided for an array of different reasons, the importance of which varies between and across different donors. The older aid allocation studies are of less interest to contemporary policy debate not merely because most used fairly crude techniques (see above) but because the reasons donors give for providing aid have constantly changed over time and, for some donors, this has influenced the allocations made. In recent years, the OECD/DAC has commissioned work on aid allocation, one indicator of the importance of the issue to the donor community as group. What is of particular interest to the OECD/DAC is to discern any change in the allocation to different recipients, and in particular to ascertain the extent to which the evolving consensus on the factors which enhance, or inhibit, aid effectiveness are altering the ways in which

different donors allocate their aid. Thus the rest of this section briefly summarises some of the key findings of especially some of the more recent aid allocation literature by means of some key questions which donors are currently asking of aid, its allocation and its effects. The discussion sets to one side the cluster of issues related to aid allocations and “difficult partnerships”, which is the subject of the Section 4.

A3.1 Do political and strategic factors influence aid allocations and if so to what degree?

12. Not surprisingly, the studies confirm that the allocation of aid has been shaped by a wide array of influences – domestic political, geo-political, colonial histories, strategic, trade and commercial - as well as developmental. However, it would appear that political/strategic, though probably not commercial, influences became less pronounced in the immediate post cold-war era of the 1990s, reflected in part in reducing the share of tied to non-tied aid (Berthelemy and Tichit, 2002). Yet they have remained important for some donors. Baulch (2003) highlights the United States, Japan and the European Union, France and Germany as leading donors who have channelled significant amounts of aid to middle-income countries in some cases for security/strategic reasons. McGillivray (2003a) finds that the development criteria had a larger influence on allocations in the cold war period than earlier studies had maintained.

13. Understandably, given how recently they have been a focus of attention, the literature throws less light on the likely overall impact of the post 9/11 era on aid allocations. But this is now beginning to change. For instance, Woods *et al* (2004) review recent aid flows and future commitments made by some leading donors in the context of assertions that the current and future allocations of aid have been and in future increasingly will be shaped by security and geo-strategic, eclipsing the global war on poverty. Geographic aid statistics for 2002 and 2003 confirm massive shifts in commitments to countries such as Afghanistan. Woods *et al*'s analysis, based on commitments beyond 2003, shows that the post 9/11 period has seen significant increases in aid levels and that these have indeed been shaped by security and geo-strategic concerns, with almost all major donors (the US, Japan, the UK, France, Germany and the EU) channelling significant aid into Afghanistan and massive increases in aid commitments to Iraq, dominated by the United States. However their view is that, thus far, there has not been a widespread diversion of existing aid to new security imperatives: it has been new flows and not existing aid flows which have been channelled to the “frontline of the war on terror”. But when these supplementary allocations of aid fall away, as they argue they soon will, donors will be faced with increasingly hard decisions about aid allocations as they weigh up their commitments to the MDGs and the complex interaction between security and development goals. Recent work by Neumayer (2003) confirms the long held view that multilateral agencies (though not all) tend to allocated aid more on the basis of development than other criteria, with UN agencies focusing more on human development and regional development banks more on “economic need”.

A3.2 Which aid recipients have been most favoured by which donors?

14. Overall, the allocation of aid on the basis of need (most often analysed by income per capita, more recently as a “proxy” for poverty, would appear to have had the most profound influence on allocations of aid. Yet the literature tends to confirm a number of prevailing conventional wisdoms: that a “disproportionate” share of aid has gone to middle-income and less poor countries; that smaller rather than larger countries tend to receive proportionately more aid in terms of per capita; and that there has been more of a large country/richer country bias in relation to (most) multilateral as opposed to bilateral donors (Berthelemy and Tichit, 2002, and Baulch, 2003). Baulch's study, using aid concentration curves and the Suits index, examines aid disbursements for the six largest bilateral donors (the United States, Japan, Germany, the United Kingdom, France and the Netherlands) and for the two largest multilateral donors (the EC and the World Bank/IDA) for the year 2001. His data show that the United States, Japan and the European Union allocate their aid to small relatively well off countries and that France and Germany do so, but only partially.

15. Recent work by McGillivray (2003b) and Collier and Dollar (1999 and 2002) among others have drawn up lists of which recipients should receive more or less aid on the basis of need (defined differently but including income-related measures, including for some the HDI): Collier and Dollar using a growth dominated poverty reduction approach, Llavador and Roemer using an equal opportunity utility function, and McGillivray and White using need and absorptive capacity but providing an unbiased weighing for population size. The lists tend to differ sharply. Tables B1 and B2, reproduced from McGillivray (2003b), provide a useful (if now somewhat dated) summary of aid allocations by recipient contrasting actual aid or commitments for 2000 with allocations based in different need-based criteria from the studies by Collier and Dollar (2002), McGillivray and White (2003) and Llavador and Roemer (2001).

“A dominant feature of these results is that most countries would receive less aid than they actually, and a relatively small number of countries would receive significantly more aid – there would be many losers and few winners. According to approaches of Collier and Dollar, Honduras, Lesotho and Uganda would receive far more aid than was actually the case in 2000. China, Indonesia, Poland and Russia are among the countries that would receive far less. Ethiopia, India, Nigeria and Pakistan would receive more aid and Poland, Russia, Malaysia, China and Colombia would receive much less according to the McGillivray and White approach. Thailand and Korea would be the big winners under both the Equal Opportunity and Utilitarian approaches of Llavador and Roemer. (McGillivray, 1993a:13-14).

16. A recent initiative from the Center for Global Development, which builds on the work of McGillivray but is still being developed, (Roodman 2004a and 2004b) unpackages and manipulates raw aid data measures (notably net ODA) to produce an “index of donor performance” which attempts to factor in key aspects of aid quality, such as tax policies that favour charitable giving, the spread of aid to different recipients, “project proliferation”, and the extent to which aid is tied. The 2004 quality adjusted aid allocations for the major donors produce the following scores as a percentage of gross ODA: France, (33%), German, (40%), Japan, (27%); Netherlands (55%), UK, (64%), US, (40%), IDA (45%) and the EC (46%).

A3.3 To what extent are aid allocations influenced by recipient policies and capacities?

17. This issue has become one of the most keenly debated in the literature. A clutch of influential studies, most originated from the World Bank, have not only argued that aid is effective if channelled to those needy recipients (minimally) able and willing it use it well, but have provided evidence to show that this has increasingly been influencing the pattern of aid allocations. One of the most recent World Bank studies (Levin and Dollar, 2004a) confirms the overall trends, but cautions that because some large donors such as France the US and Japan and not very selective, “overall, bilateral aid is not very selective” (p. 14).

18. Tables 5 and 6 below show the rankings of the largest bilateral donors (including the EC) in terms of the responsiveness of their aid to policy (CPIA) and poverty (per capita GDP).

Policy Elasticity Index Ranking

	1999	2000	2001	2002
EC	17	21	14	12
France	31	29	34	30
Germany	22	10	11	14
Japan	2	5	8	16
Netherlands	3	2	4	9
UK	10	6	5	3
US	28	28	32	27

Source: Levin and Dollar (2004a)

Poverty Elasticity Index Ranking

	1999	2000	2001	2002
EC	30	32	23	25
France	25	29	28	29
Germany	27	25	24	26
Japan	23	34	30	35
Netherlands	7	7	11	10
UK	19	18	12	16
US	15	16	22	20

Source: Levin and Dollar (2004a)

19. These studies (Burnside and Dollar, 1997, 2000, 2004; Collier and Dollar, 1997 and 2002) have been particularly influential as they have argued that millions more people can be lifted out of poverty merely by reallocating aid to different recipients. While some of these findings have been confirmed by other scholars (see Berthelemy and Tichit, 2002), both propositions have been challenged by a series of studies emanating from three main centres: WIDER/UNU, the Center for Global Development and the University of Copenhagen (see bibliography). One part of the critique (see Hansen and Tarp 2000) challenges the view that aid has performed better in countries where particular (better) recipient policies, institutions, governance policies and approaches and commitment have been present. For instance Clemens et al (2004) argue that when aid is disaggregated into humanitarian aid and development aid that could potentially impact on aid in the short and long term, then the results differ significantly, with only aid channelled to short-term development having the assumed positive and robust relationship. The other part of the critique questions whether aid allocations have in fact changed and can be shown to have shifted more to those recipients deemed to have the potential for using it better. Among others, Tarp and Neumayer argue that they haven't, while Radelet (2004) suggests that in the more recent period, from 1996 to 2002, there has been no appreciable change in the share of aid going to poor countries with better governance. Relatedly, work from within the World Bank (see for instance Kaufmann and Kraay) highlight key difficulties in using different governance indicators as a basis for allocating aid. Whether significant changes in overall allocations have changed in the recent past, emerging conclusions from the UN Millennium Project contends that there remains a huge gap between the needs (including the aid needs) of the poorest countries and the levels of aid currently provided and expected to flow to them. The Project's preliminary research suggests that even if each low-income country governments mobilize an ambitious 4% of its own GNP each year, to meet the MDG financing needs at the country level will require an average of \$84bn annually to 2007.

20. Another strand of impact work that could potentially have an influence on aid allocations is that which focuses on the effects of different types of aid. As noted above, Clemens et al (2004) divide aid up into three categories: humanitarian and long and short term development aid and highlight very different impacts of these different sorts of aid with humanitarian aid seemingly correlated with (though not necessarily causing) a fall in economic growth. Within the ambit of the literature on aid fungibility, recent work by Mavrotas (2003) finds that project and food aid seem to cause a fall in aggregate public investment whereas programme aid and technical assistance are positively related to higher public investment.

A3.4 Donor approaches – general literature perspectives

21. Clearly an important dimension of the discussion of donor aid allocations needs to focus on the views of donors themselves. This is a core part of the current study. Here we summarise some of the key findings from the general literature on donor views and perspectives. There is evidence to suggest that a significant number of donors are giving more attention to selectivity and bilateral donors in particular do explain why they provide aid to their chosen recipients and most refer to needs/poverty as an important criterion (See DFID, 2002). A large study of more than 20 donors conducted by Berthelemy and Tichit (2003) found that “most donors pay a great deal of attention to political governance when making their aid decision. Most donors have developed quite elaborate and in some cases (such as the EC) quite formal and complex criteria for allocating aid below the country level – including aid to different sectors and whether and when to provide aid in the forms of budgetary support or through sector-wide approaches. It is beyond the scope of this literature review to go into the details of this vast and rapidly evolving literature.

A3.5 What are the key overall messages emerging from the aid allocation literature?

22. There are some five key messages for donors flowing from this review of the literature on aid allocation.

- First, while the literature on aid allocations is dominated by the development/growth/poverty use of aid and its impact, current aggregate aid allocations are still significantly shaped and informed by other criteria notwithstanding the efforts of some donors to allocate their aid in a more focused way on those countries which need it most.
- Second and flowing from this, the aid allocation literature provides strong evidence to suggest that if aid were allocated differently, providing more to the countries that needed it, then it could have a far greater effect and impact on poverty alleviation.
- Third and more recently, the literature not merely shows that policies, content and commitment by recipient matters in terms of impact and effectiveness, but if aid were additionally allocated to those countries which both needed it and were able to use it better then even more people would be lifted out of poverty.
- Fourth, there is growing evidence to show that as donors (almost across the board) are being influenced by and trying to focus more on results-based management approaches, they are increasingly open to considering how to link aggregate allocations of aid with aggregate impact, though the practical outcome of this still varies enormously across donors.
- Fifth, as donors focus on trying to marrying allocations to effectiveness, pressing questions are raised about how to address the needs of poor countries and poor people in poor countries where aid is clearly less effective. In the context of still significant shortfalls in overall aid levels, to the extent that aid is channelled more to those who need it and where it appears to be better used, less will be available to those who need it but where the impact appears less good.

23. It is to this issue that we turn in the next section of this Appendix.

A4. The allocation of aid to poor and problematic aid recipients

24. There is little controversy among donors that aid impact is important and that it should help to inform and shape the allocation of aid. But if aid is channelled increasingly to those recipients where it has a clear positive impact – or even a discernibly better impact than when provided to other recipients - then

what should happen to those recipients where aid's impact is not positive, possibly adverse or cannot easily be judged? These questions are becoming increasingly urgent for two linked reasons. Firstly, because - on different counts - the numbers of poor people living in countries which are grouped among those where aid's impact is problematic range from between 500mn to 1bn, the latter figure constituting over 80% of those estimated to be living in extreme (income) poverty (Macrae *et al* , 2004:viii). Branchflower *et al* (2004) suggest that excluding India and China, two thirds of all people living in absolute poverty live in such countries. Secondly, the Millennium Development Compact commits donors (though also recipients) to give particular priority to those countries "left behind", especially those with the lowest human development and those that have made least progress in the last decade (UN, 2003:15). Among these are a significant number of countries which receive insufficient aid and where aid's impact has been particularly problematic. Encompassing the different ways in which problematic aid recipients are classified and defined, Branchflower *et al* judge that between 46% and 62% of the countries defined by the UN as least developed fall within this grouping (2004:18).

25. There is unanimity across the donor community that poor people in these difficult countries should be helped. The question is precisely how they could and should be helped. Should aid be provided in larger amounts and if so should it be provided in a different form, or through different mechanisms, or over a different time-frame? Or would it be better to provide less (or even no) aid and try to help in a different way?

A4.1 The OECD/DAC's difficult partnership initiative

26. One way these problems have been approached has been through the difficult partnership initiative of the OECD/DAC. At the heart of the OECD/DAC's overall approach to aid and its effectiveness is the notion of partnership: without an effective partnership between donor and recipient aid is not likely to be effective. It follows that aid impact is likely to be particularly problematic in contexts where partnerships are likely to be strained or, at the extreme, where the ingredients for good partnerships are deemed completely lacking. It is against this backdrop that, since the early 2000s, the OECD/DAC has paid particular attention to difficult partnerships countries. Difficult partners are those where the relationship between the donor and recipients is poor due to a combination of a lack of political interest or commitment to poverty eradication and weak state and non-state institutional capacity to implement policy. Thus the concept of difficult partnerships embraces the notions of capability, capacity and commitment which are likely to be linked and inter-related: "a lack of political commitment is most often exacerbated by weak capacity in the government to develop and implement policy as well as institutional weaknesses of non-state actors (OECD, 2002:2). In difficult partnerships "the key elements of ownership and commitment are missing so partnership cannot function properly according to the DAC partnership model" (OECD, 2001:9). Finally, it should be noted that the OECD/DAC views difficult partnerships as a "continuum from very poor to very good" (OECD, 2002:2). Thus, looked at negatively, "difficult partnership" countries are not classified by assessing their development performance over time, or the impact of the aid received: rather, they are countries grouped together in terms of an assessment of relationship, capability, capacity and commitment. In short, this is an input and not output or outcome focus.

27. As a companion study to this one, the OECD/DAC commissioned a study reviewing trends in aid going to difficult partner countries and comparing this with aid to other recipients. [Difficult countries were defined for the purposes of this analysis as low income countries who are ranked in the lower two quartiles of the World Bank's CPIA.] Among the main findings of the study were the following (Levin and Dollar, 2004b).

- Difficult partner countries had received less aid (disbursements) in both absolute and per capita terms than low-income countries with higher institutional capacity ratings (those in the top three

quintiles of the CPIA) , and exhibit a lower ratio of disbursements to commitments, and that aid to such countries has been more volatile than to the other two groups. Aid to difficult partner countries also tended to be more volatile than to other LICs.

- Aid per capita to the sub-group of “post-conflict” countries has been higher than to non-post conflict countries with multilateral donors providing proportionately more aid to such countries than bilateral donors (holding everything else in the regression constant).
- Difficult partner countries are also characterised as being poorer (in terms of GDP per capita and key social indicators) than the wider group of low-income countries.
- Finally, the study examined some trends in aid modalities, comparing on-budget (budget support, programme aid and technical assistance) with non-budget grants. It found that while difficult partner countries received proportionately less non-budget to budget support than middle-income countries, they appeared to receive no lower a share than low-income countries with stronger institutional capacity.
- Thus, overall the study’s findings confirm that difficult partner countries are both more needy, in terms of their poverty profiles, and also receive less aid, largely because of differences from bilateral agencies though there are marked country by country differences.

28. The literature from the OECD/DAC arising from the on difficult partnership initiative has made a series of initial recommendations to donors about how to inter-relate with such partners. First and foremost, it strongly advocates continued engagement with difficult partners and nowhere suggests that aid levels to such partners should be reduced (nor that it be increased), though it does suggest that not all donors need to or should remain engaged (OECD, 2002:5). One of the main arguments given for allocating aid to difficult partners is the cost of inaction: failure to support such countries with aid risks having to outlay even more in humanitarian aid in the future and in trying to contain the costs of violent conflicts which could spill over into neighbouring states. It proposes action in three broad areas:

- Promoting the enabling conditions that would make political systems more able to respond and actually be more responsive to the voice and legitimate interests of poor people (both through engagement with the state and outside state structures, including with the private sector);
- maintaining support for services to the poor through a pragmatic selection of those governmental and nongovernmental agencies that share a commitment to poverty reduction and as appropriate help them strengthen their capacity; and
- adapting donor coordination (which it views as a “key to improving difficult partnerships”) and furthering policy coherence so that the effectiveness of the international community’s effort are enhanced and not relaxed.

A4.2 The World Bank’s LICUS initiative

29. In November 2001, the World Bank established a task force to consider how the development community could effectively assist “chronically weak-performing” countries get onto a path of self-sustaining growth and poverty reduction. As part of this work, it has grouped together countries where aid does not work well under the nomenclature low-income countries under stress or LICUS countries. These are countries which are characterised by weak polices, weak institutions and weak governance and in these environments “aid does not work well because governments lack the capacity or inclination to use finance effectively for poverty reduction” (World Bank Task Force, 2002:1). More specifically, LICUS countries

are IDA-eligible countries which combine poor policy performance or low service delivery capacity and a lack of responsiveness to their citizens based on indicators for policy management capacity, service delivery capacity and citizen influence on government. Particularly influential has been the Bank's Country Policy and Institutional Policy Assessment (CPIA). Countries are classified as LICUS if they score 3.0 or less on the CPIA. One consequence of this classification is that the LICUS grouping is not fixed: they can move in and out of the grouping. More recently, there has developed a twofold classification of countries within the LICUS framework, namely post-conflict and other countries. Thus, importantly, the LICUS classification is not one which is based on development results or aid effectiveness but on capacity and capability assessments and is a classification based on relative assessments: in short there will always be LICUS countries as long as there are low income countries.

30. The literature from the World Bank outlining its approach for dealing with LICUS countries involves engaging in dialogue with the government and continuing to provide assistance, but (probably) at a lower level than with the non-LICUS low income countries. It argues that total engagement carries with it its own risks especially cross border spill over effects, crime and the spread of disease. It proposes engagement strategies are based on in-depth political and economic analysis, promoting domestic demand and the capacity for change, supporting simple entry-level reforms and exploring different (innovative) methods of service delivery. It also places strong emphasis on donor coordination, noting in particular the importance of a "greater consensus ... on the principles of aid engagement and country-specific priorities" (World Bank (2003:1). In practice, the Bank has sought to engage and re-engage with most LICUS country governments and has highlighted the need to engage pro-actively with domestic reform in "weak transition" countries.

A4.3 United Nations Development Programme (UNDP)

31. The UNDP has been pivotal in mustering support for the achievement of the Millennium Development Goals and that context a strong advocate for increases in aid which contributes to poverty alleviation. As part of its work, it has highlighted the importance of what it terms Top Priority and High Priority countries. These are countries where, on recent trends, it is likely that the MDGs will not be met (actual progress is less than half that required to meet the 2015 target for at least three goals). These priority countries are those where either income per capita has fallen since 1990 or there has been marked fall on the Human Development Index (the two are in part linked). In its 2003 Human Development Report, UNDP lists 59 Top and High priority countries.

32. The UNDP list of priority countries differs from the OECD/DAC and LICUS approach in that it focuses on performance measurements and in calling for an increase in aid to these countries (UNDP, 2003: 146). However, it also stresses that the increase in aid to the top and high priority countries should be accompanied by a focus on efforts to enhance aid effectiveness, focusing on three specific measures: stronger governance, increased ownership and better aid practices, aligning itself to the principles emerging from the Monterrey conference (2003: 147).

A4.4 An overview of the wider literature's discussion of problematic recipients

33. There have been comparatively few detailed and comprehensive independent studies that focus explicitly on problematic recipients; the subject area seems to have been dominated by donor or donor-initiated studies. One exception is Macrae *et al* (2004) which provides a critical and lengthy overview of "poorly performing" countries approach. While their study welcomes the attention given to some of the very poor living in hostile environments, it contends that it is far from easy to distinguish clearly between good and bad performers (a view consistent with the approach to difficult partners of the OECD/DAC and the CEC as well as with the LICUS initiative). The study is helpful in highlighting those factors that shape and sometimes play a crucial role in determining development performance and aid impact which lie

outside the influence of donor and recipient. These include: the original conditions in a country and its geographical location, other structural constraints, changes in the external environment, a range of vulnerabilities, and the nature of state-society relations (2004: 83). It also helpfully draws attention to the different types of approach and engagement that are often required to attempt to address poverty indirectly, through attempts to enhance pro-poor growth and directly by addressing different manifestations or attributes of poverty more directly – through provision of education, health, water or other services.

34. The Macrae *et al* study suggests that countries are likely to be difficult to assist where at least two of the following conditions prevail: the juridical or legal basis of the state is contested; empirical sovereignty is weak; and international support and recognition of the government is either withheld or ambivalent (2004: xi-xii). It makes a number of specific proposals.

- Donors need to weigh seriously the wider and longer-term costs of disengagement which would caution them against withdrawal: thus disengagement is “not an option”.
- A greater effort should be made to make more use of humanitarian aid in general and of different humanitarian aid modalities in particular in some difficult partnership countries, building on the growing recognition in the humanitarian literature (see Darcy and Hofman, 2003) that there is often overlap between humanitarian and development aid activities.
- Poor performance needs to be “unpacked” as very few recipients perform poorly in all areas over a very long period of time, and
- Donors need to re-examine the merits of project aid and non-state actors in bringing basic services to the poor in countries where states are unwilling or unable to do so.

35. A number of studies confirm that problematic recipient countries are “under-aided” - usually meaning that they require more aid than they currently receive, but sometimes also meaning that they have the capacity to receive more aid – the latter point confirmed by the companion study to this one (Levin and Dollar 2004b). As noted above, Tables B1 and B2 (below) provide a summary of data on the allocation of aid by recipient comparing this with (three) different “need” criteria, reveals the “aid deficit” in a number of low-income countries. It is instructive to compare these data with the UNDP’s list of the 31 Top Priority countries (UNDP, 2003). The UN classifies 31 countries as “Top Priority”, but the McGillivray and White and the Collier and Dollar studies do not include data from 19 of these: over 60% of these Top Priority (“needy”) countries. For the remaining 12 for which there are data, according to the Collier and Dollar criteria, more aid should be provided to seven (Cote d’Ivoire, Ethiopia, Madagascar, Mauritania, Niger, Rwanda and Zambia), while according to the McGillivray and White criteria, more aid should only be provided to four: Ethiopia, Guinea, Indonesia, Niger and Nigeria.

36. From the donor side, the Baulch study uses concentration curves to show which donors allocate their aid proportionately more or less to the poorest countries, indicating which recipients are proportionately under-aided by main donor. Some parts of the literature argue that far more emphasis should be placed on donor responsibility to ensure that the poor in *all* poor countries receive the benefits of aid – by implication at least suggesting that the recent emphasis on policy as the driving force in judging where aid should be channeled has gone “too far”. The UN agencies in particular tend to pursue such arguments within the framework of a “rights-based” perspective, arguing that it is there are obligations, especially from the international community to provide aid to “problematic recipients” and if current approaches are not working well, the choice does not lie in re-allocating aid to those who use it better but in working out new forms of aid for those where more traditional forms do not work.

37. These sorts of arguments are also voiced by those coming from the ethical and social justice perspective such as Llavador and Roemer (2001) and Cogneau and Nauder (2004). Collier and Hoeffler (2002) suggest that there is far more potential for channelling aid effectively to (some) post-conflict countries but that in practice a rapid increase in aid to assist countries emerging from conflict has too often been followed by a fall in aid when their absorptive capacity remains positive/high. McGillivray follows Collier in arguing that far more aid should be given to a sub-category of problematic recipients, namely those emerging from conflict, but adds another grouping – those who are “structurally vulnerable” (2003b:7). This sort of argument is developed further by the UNDP (2003:76) which provides a check-list of the areas where it believes aid could be effective for those countries “stuck in the poverty trap”: investment on the social sectors; investments to raise agricultural productivity; investments in infrastructure – roads, power, ports and communication; and industrial development policies to bolster private activities.

38. Other parts of the literature, though fairly sketchy in detail and depth of analysis, take more of the opposite view, by arguing that there is merit in withholding aid especially from those problematic recipients whose commitment to poverty-alleviating strategies is in question. For example Radelet explicitly suggests that “poorly governed countries should receive less money”, and for two main reasons: that it can be used more effectively elsewhere, and because it can help sustain bad governments or further weaken the quality of governance (2004:17). He goes on to suggest the forms of aid most appropriate to such countries as well as addressing the timing question, arguing for project aid (“program aid and budget aid are out of the question”), aid that helps provide basic services for the poor, humanitarian relief and, overall, what he terms rapid quick-return aid. While welcoming the attention given by donors to post-conflict countries, he expresses concern that when rapid inflows of aid to such countries are followed by equally rapid withdrawal this can be extremely destabilising.

39. Radelet also addresses the question of who should be using the aid provided to problematic recipients. He favours non-state actors as a channel through which to reach poor people, and in particular NGOs, though emphasises the need to choose which NGOs to use carefully. He is also sympathetic to idea of establishing “independent service providers” as another mechanism through which to channel aid to those who need it, helping to avoid the inefficiencies and “leakages” related to channelling aid through administratively weak and sometimes corrupt state officials and institutions.

40. A linked question is who should be providing aid to problematic recipients? There is no doubt that because bilateral aid is largely a government-to-government relationship, when the problematic recipient is ruled by a government whose human rights record is in question, then it can be easier for bilateral agencies to channel aid through multilateral agencies, or through non-state agents (as occurred very successfully in apartheid-rule South Africa and Pinochet’s Chile). Another proposal that has been on the table for many years (see Hyden 1993 and 1995) is to establish politically independent, accountable and transparent development trusts/trust funds which distance both the donor and the recipient from the political linkages which government to government aid relations necessarily carry with them. Such a proposal certainly sits comfortably with three strong recommendations from the literature on problematic recipients: that different forms of aid to those of “ordinary partnerships” need to be developed; that aid coordination is even more important in such contexts; and that two of the major factors creating a reluctance of donors to support such recipients are the lack of transparency and accountability at the recipient end.

41. An influential indicator used to judge the capability of recipients to absorb aid effectively is the administrative and institutional capacity of recipients. Not surprisingly, instead of taking this as a “given” and as the basis for reallocating aid to those where the institutional setting is more favourable, parts of the literature use this constraint as the launch-pad for setting forth proposals for improving their institutional capacity, some using this as an argument for providing more aid to those thus constrained. These sorts of

arguments are to be found in a paper by Ikhide (2002) one of whose recommendations is for a supranational institution to be established to give overall direction to such initiatives. Bossuyt (2001) takes this argument one step further by suggesting that institutional development is so central to the whole aid effort that it needs to be the focus of all aid efforts by donors. He argues that this is “not simply a question of improving aid effectiveness ... (but) a way to prevent development cooperation from becoming an obsolete tool”. Taken one step further, these sorts of perspectives could be used to suggest that if aid effectiveness is impeded by weak institutions, one solution might lie not in reducing aid but in providing more of it but in amounts and in forms which substantially address these problems.

42. In part linked to the specific literature on the discussion of aid to conflict and post-conflict countries, a number of authors have focused on the cost of neglect: the need to remain engaged and help to reduce conflict both because of the increased costs of having to intervene after conflict and because of the likely spill-over effects of conflicts into neighbouring countries and the risk of their heightening regional conflicts. These concerns have arisen particularly from experiences in Africa (Rwanda/Central Africa and Sierra Leone/Liberia/West Africa) and parts of Asia (Myanmar/Cambodia). As *Dyer et al* observe, conflict typically has contagion effects regionally (2003: 35). The importance of these issues are discussed, *inter alia*, in Torres and Anderson (2004: 5ff) and Collier *et al* (2003: 173ff) and their implications for donors highlighted in OECD (2001: 17) and, though less directly, in OECD (2003). Bulř and Hamann’s work on aid volatility and predictability (2003) also has implications for the spill-over regional effects of under-aiding difficult countries.

43. The draft preliminary report (September 2004) from the UN Millennium Project takes up a number of these themes. Its over-riding message is the need substantially to increase levels of aid especially to the poorest countries because, without additional aid, and in spite of efforts made by the countries themselves, they will not achieve the MDGs without such increases. Against this backdrop it discusses how best to assist those countries where the prospects for aid effectiveness are particularly poor.

44. It acknowledges the centrality of good governance and government commitment to achieve aid impact and isolates three groups of countries characterised by weak governance and lack of commitment. The first “genuinely corrupt governments”, termed *thugocracies* where there is little to no will to achieve broad-based development goals. In such cases the UNMP suggests that modest flows of aid, mainly to address humanitarian and public health concerns, channelled mainly through NGOs. The second group are those countries which suffer from weak governance including corruption but which is caused not so much by the ill-will of leaders but by the lack of state resources and capacity to manage an efficient public administration. In such countries – and in contrast to some of the main-stream literature – the UNMP advocates both more aid and a significant increase in resources to strengthen institutional capacity. It challenges as incorrect the view of many donors which perceive capacity constraints as barriers to scaling up. The biggest challenge it sees as the need for a rapid scaling up in the face of low incomes, weak governance and major capacity constraints that need to be overcome.

45. The UNMP’s third group relates to those countries where governance breaks down because of violent conflict which, in turn it sub-divides into three: those countries at risk of conflict, those in conflict and those emerging from conflict. It argues that there is an important role for aid in all three cases, though the form in which aid should be provided will tend to differ in each case. Those countries at risk of conflict need aid focussed especially on building institutions and infrastructure and with an ability to mobilise aid rapidly as the situation changes. Countries in conflict, require immediate humanitarian assistance, especially by using tried and tested mechanisms to by-pass hostile formal administrative systems, but can also be expanded and extended to support for basic health and education services. Finally in countries emerging from conflict, a major emphasis is given to peace building, reconciliation and demobilisation and especially the rehabilitation of women and girls, because data show that countries emerging from conflict show a 50% tendency to relapse back into conflict within the first five years. Additionally, emphasis is

given to large scale investments to build and rebuild the basic infrastructure as well as focusing on political processes which ensure that the interests and voice of marginalised groups are addressed.

46. The UNMP's draft preliminary report is critical of current donor approaches to those countries where the gap between aid needs and current aid levels is particularly wide, including those countries where the context is not conducive to high levels of aid effectiveness. The UNMP's proposals for coordination comprise eight specific points, summarised thus:

5. ODA levels should be set for each country according to MDG financing gaps and donors should work collectively to ensure that these levels of aid are met by the donor community as a whole.
6. ODA should be directed mainly at the support for public sector investments rather than pet projects of individual donors.
7. Donors should make firm multi-year disbursement commitments that are predictable.
8. ODA support of public investment be given a direct and untied budgetary support.
9. Donors should increase the amount of aid they provide through multilateral rather than bilateral channels, especially for financing the scaling up of public investments.
10. Bilateral aid should be provided mainly for technical assistance, people-to-people exchanges, scholarships and support for NGOs.
11. ODA should be provided as grants in low-income countries; debt sustainability should be redefined as the level of debt consistent with the achievement of the MDGs.
12. An independent technical group should be set up to publish independent evaluations of donor policies and donor coherence.

A5. Gaps in the literature: potential new research areas

47. The final section of this literature review provides some initial indications of key gaps in the literature, especially of problematic recipients and points to some areas of possible research.

48. *Definitional issues.* It is not merely an outstanding problem that donors use different definitions when referring to "problematic poor aid recipients" but it is particularly serious when some donors use definitions which focus on outputs and outcome and others focus on definitions that focus on inputs and processes. All donors have problems with some recipients but it is likely that the reluctance among some donors to be drawn into current debates and discussions of such recipients lies in varying degrees of dissatisfaction with current definitions. There is clearly merit in trying at least to narrow down the terminology used.

49. *Learning from the recipient end.* With certain exceptions (such as some of the LICUS work from the World Bank) the current literature shaping donor policy has a donor-end bias. Yet the policy lessons that need to be mulled over need to come from the experiences in the problematic aid recipient countries. There would seem to be great benefit in drawing together the wealth of experience and the views of both donors and recipients in these countries about what forms or types of aid seem to work better and what do not and why.

50. *The importance of emergency/humanitarian/relief aid.* The discourse on aid with problematic poor recipients predominantly takes place within the (often unstated) assumption that the focus of attention

is development aid. Clemens *et al* (2004) have highlighted the importance of distinguishing between humanitarian and long term and short term development aid for the purposes of understanding better how aid work the implications of this threefold distinction needs to be more clearly worked through into policy discussion. Besides Clemens *et al.*, this distinction has also been recognised by Roodman (2004b), excluding emergency aid from his analysis on donor performance, as well as by Levin and Dollar (2004a) and Levin and Dollar (2004b), excluding debt forgiveness grants from their analysis. But the emergency/humanitarian aid component needs to be focused on more directly in its own right. Randel and German's work (2002) shows that as a share of total aid, emergency and distress relief doubled over the past ten year to at least 10% of total ODA disbursements by 2000. It is highly likely that this proportion is far higher for the sub-group of problematic poor aid recipients. The literature also suggests (see Macrae, 2002) that poor/difficult recipients could, and have the capacity to absorb far more of such aid than they are currently receiving. Finally, there is a literature on the evaluation and assessment of humanitarian aid which is distinctly different from the development aid assessment literature which needs to be fed into the wider discussion (see Hofmann *et al*, 2004, Darcy and Hofmann, 2003 and Macrae 2002b). There is much to mull over here and a number of areas of possible research that the donors concerned with problem aid recipients could benefit from being more widely exposed to.

51. *Institutional issues.* The existing literature is unanimous in putting great emphasis on the need for far more and great coordination among donors when working with problematic poor aid recipients than with others. Part of the literature also strongly contends that the "conventional" partnership approach will not work in such contexts. There is clearly work that needs to be done on reflecting on alternative approaches, building both on some of earlier aid literature (see Hyden's work in the late 1980s and early 1990s) as well as incorporating the lessons from different forms of aid coordination which have been tried in conflict/emergency situations (such as Somalia and Afghanistan) more centrally into donor discussions (see Macrae 2002b: 38ff). Institutional issues are also linked to different aid modalities. Some of the literature (e.g. Radelet) strongly contend that programme aid and budget support are forms of aid wholly inappropriate to problematic poor aid recipients. Some donors, such as the EC, are less convinced, arguing that no instrument should be ruled out *a priori*. Ironically the independent trust literature in part argues that it is in precisely the most difficult contexts that the strongest arguments for an independent aid trust can be made. And in such circumstances, the most appropriate form of aid modality could be a form of "country programme aid" even more "high level than SWAPs or budget support. There is much here that could be learned from further work and research.

52. *Incorporating the insights of a rights-based perspective.* The discourse on poverty alleviation that has had the most profound influence on the donor community is that based on "needs" which have to be met. As noted above, there is a strong consensus among donors that the needs of the poor are to be addressed even when governments appear to be more an obstruction to than a facilitator of progress. Increasingly, poverty is being re-cast, re-shaped and viewed from a "rights-based perspective", an initiative which the UN and some of its specialised agencies have been particular leaders. Much work has been done on developing approaches to ensure the right to food, the right to education and the right to water is operationalised in the development approaches of poor country governments. There could be merit in the donor community as a whole reflecting on how the rights-based perspective might inform the debates and discussions taking place among donors about how to assist the poor in problematic poor aid recipient countries, and, importantly, how donors can address and operationalise evolving international obligations in such countries,.

53. *More on different aid modalities.* Finally, work could usefully be done to marry more systematically the evolving/emerging literature on how to help the poorest poor countries develop and the contribution of aid to such efforts. Work emanating from UNCTAD (and other UN agencies) suggests that a critical way to help the poorest and most marginalised economies is to focus on structural changes to help them diversify out of commodity-based exports (see, for instance, UNCTAD, 2002). A core element of this

approach is the building of the necessary physical (transport and communication) and informational infrastructure. These needs override the short term problems of particular governments and suggest significant ways in which aid might be used within a longer-term perspective than is currently conceived. Work in this area could contribute to the wider discussion of aid modalities.

54. A useful point of reference in assessing current aid arrangements and the policies of individual donor countries may be to identify in general terms what might be the broad characteristics of both a globally optimal and a potentially politically feasible process for allocating aid in pursuit of a common objective (such as poverty reduction). The empirical literature on aid provides an entry point for this (through providing evidence that the global poverty impact of aid is increased to the extent that aid provision is focused on countries with many poor people and with relatively effective policies and institutions), but focuses only on the implied optimal aid allocation and not on the process or (explicitly) on incentive issues. One way to conceptualise both an optimal and a feasible aid allocation process would be in terms of interstate fiscal relations within a federal polity characterised by high levels of inequality between the states. Under an optimal process (from the point of view of poverty reduction), financial transfers would be made from the richer to the poorer states to assist the poorer states in achieving the shared poverty reduction targets. Characteristics of such an optimal relationship would be likely to include:

- Transparent, predictable and formula-based transfers against jointly agreed observable criteria (which might include population size, average incomes, numbers of people below a common poverty line, distance from achieving various MDGs, and special factors such as vulnerability to natural disasters, being landlocked or otherwise geographically disadvantaged, very small size).
- A transfer might take the form of an unconditional grant or loan, or might be tied towards particular types of use (for instance in education or health).
- Jointly agreed performance and accountability criteria. These would include the ability to account adequately for the use of resources transferred provided against results, and a commitment to agreed policies in areas judged important to the achievement of joint objectives.
- An incentive element, including a linking to tax effort, and possibly “Challenge Fund” arrangements under which resources could be transferred in support of particular proposals.
- Provision for special arrangements (typically within a federal state the assumption of some degree of direct rule or control from the centre but possibly also involving the provision of technical assistance to perform key functions) when states are unable to meet performance and accountability criteria or where governance breaks down because of conflict.

55. The concept of a “politically feasible” aid allocation process would also take into account the fact that if such a system were to be established through international negotiation, this process would be influenced by the relative bargaining power of the partners involved. One point in particular is that recognition of the principle of sovereign equality between states in any decision-making process would be likely to lead to a relative bias in favour of small states in the allocation formula. A negotiated process would also be likely to influence the criteria applied in determining transfer allocations relatively in favour of those objectives of most interest to the most powerful participants.

56. An obvious point is that such a model would be one in which aid (interstate transfers) would be multilateral rather than bilateral. If the arrangement had to work through bilateral channels, the principal requirement would be a high degree of coordination between the net contributors to ensure that their individual actions summed up to the globally agreed outcome. Any constraints such as aid tying would militate against this.

57. Such a model would also only be operational under conditions of sufficient consensus among both the net contributors (donors) and net beneficiaries (aid recipients). A “difficult partnership” in this context might accord with the circumstances envisaged under the last bullet point above – a situation which can be seen as particularly problematic in the absence of an agreed supra-state central authority to implement the “special arrangements”. In practice such a position might be taken by a hegemonic power or group of powers.

Prescribed and actual allocations

Table 1
Prescribed and actual allocations

	Actual ODA or OA commitments 2000		Prescribed ODA or OA commitments											
			Collier & Dollar				McGillivray & White				Llavador & Roemer			
			Headcount US\$2		Headcount US\$1		Equal opportunity		Utilitarian					
Total ODA	Swedish ODA	Total ODA	Swedish ODA	Total ODA	Swedish ODA	Total ODA	Swedish ODA	Total ODA	Swedish ODA	Total ODA	Swedish ODA			
Algeria	259.96	0.39	0.00	0.00	0.00	0.00	89.41	0.88	176.80	1.30	0.00	0.00		
Belarus	38.93	7.63	0.00	0.00	0.00	0.00	16.26	0.16						
Botswana	31.18	0.25	0.00	0.00	0.00	0.00	1.22	0.01	16.90	0.12	40.33	0.30		
Brazil	254.50	1.46	0.00	0.00	0.00	0.00	377.96	3.72						
Bulgaria	429.57	0.10	0.00	0.00	0.00	0.00	16.26	0.16						
Chile	69.09	0.85	0.00	0.00	0.00	0.00	12.19	0.12	558.71	4.10	0.00	0.00		
China	2977.49	4.78	0.00	0.00	0.00	0.00	1881.67	15.54						
Colombia	1267.37	9.05	0.00	0.00	0.00	0.00	65.03	0.64	763.31	5.60	0.00	0.00		
Costa Rica	84.10	1.81	0.00	0.00	0.00	0.00	1.63	0.02	532.27	3.91	0.00	0.00		
Côte d'Ivoire	385.50	0.24	1357.95	13.38	0.00	0.00	170.69	1.68	41.05	0.30	0.00	0.00		
Czech Republic	211.52	0.04	0.00	0.00	0.00	0.00	0.81	0.01						
Ecuador	180.88	0.44	0.00	0.00	0.00	0.00	28.45	0.28	275.90	2.03	0.00	0.00		
Egypt	1779.37	1.33	0.00	0.00	0.00	0.00	422.67	4.16	126.05	0.93	0.00	0.00		
Estonia	105.22	2.75	0.00	0.00	0.00	0.00	0.81	0.01						
Ethiopia	561.53	10.80	1974.49	19.45	1702.02	16.77	2991.70	29.47	40.17	0.29	0.00	0.00		
Guatemala	239.66	13.34	0.00	0.00	1972.12	19.43	65.03	0.64	119.97	0.88	0.00	0.00		
Guinea	199.73	0.07	0.00	0.00	101.65	1.00	203.20	2.00						
Guinea-Bissau	87.98	0.40	1324.85	13.05	1480.19	14.58	609.61	6.01						
Honduras	511.59	11.80	2812.73	27.71	3777.62	37.22	24.38	0.24	28.37	0.21	0.00	0.00		
Hungary	312.44	0.21	0.00	0.00	0.00	0.00	0.81	0.01						
India	1587.61	7.40	78.38	0.77	66.08	0.65	11826.50	116.51						
Indonesia	1986.33	0.87	0.00	0.00	0.00	0.00	3169.99	31.23	5184.12	38.05	0.00	0.00		
Jamaica	144.31	1.22	0.00	0.00	0.00	0.00	406.00	0.04	3.09	0.02	0.00	0.00		
Jordan	574.23	0.13	0.00	0.00	0.00	0.00	8.13	0.08						
Kazakhstan*	302.80	0.86	0.00	0.00	0.00	0.00	32.51	0.32						
Kenya	784.33	28.05	1053.16	10.38	1240.86	12.22	207.27	2.04	57.88	0.42	0.00	0.00		
Korea	0.00	0.00	0.00	0.00	0.00	0.00	2.03	0.02	9086.48	89.52	1056.67	77.52		
Kyrgyz Rep.	276.05	0.82	2648.25	26.09	873.87	8.61	16.26	0.16						
Lesotho	38.46	0.07	313299.00	30.87	3594.68	35.41	20.32	0.20						

Table 1 continues

	Actual ODA or OA commitments 2000		Prescribed ODA or OA commitments											
			Collier & Dollar				McGillivray & White				Llavador & Roemer			
			Headcount US\$2		Headcount US\$1		Equal opportunity		Utilitarian					
Total ODA	Swedish ODA	Total ODA	Swedish ODA	Total ODA	Swedish ODA	Total ODA	Swedish ODA	Total ODA	Swedish ODA	Total ODA	Swedish ODA			
Lithuania	237.46	19.96	0.00	0.00	0.00	0.00	81.00	0.01						
Madagascar	383.80	0.22	1129.48	11.13	1201.40	11.84	300.74	2.96	23.16	0.17	0.00	0.00		
Malaysia	1189.92	0.00	0.00	0.00	0.00	0.00	16.26	0.16	1186.73	8.71	0.00	0.00		
Mauritania	240.09	0.21	1623.35	15.99	1482.26	14.60	81.28	0.80						
Mexico	369.30	0.15	0.00	0.00	0.00	0.00	93.47	0.92	2634.19	19.33	0.00	0.00		
Moldova	111.18	2.67	0.00	0.00	0.00	0.00	243.85	2.40						
Morocco	693.12	0.00	0.00	0.00	0.00	0.00	2.44	0.02	376.86	2.77	0.00	0.00		
Nepal	402.05	0.93	894.85	8.82	1004.85	9.90	556.78	5.49						
Nicaragua	455.21	27.70	1994.39	19.65	2773.38	27.32	24.38	0.24						
Niger	304.37	0.07	1113.14	10.97	1115.21	10.99	406.41	4.00	8.47	0.06	0.00	0.00		
Nigeria	311.14	0.78	598.35	5.89	630.01	6.21	2970.85	29.27	301.50	2.21	0.00	0.00		
Pakistan	1188.07	1.15	1646.60	16.22	0.00	0.00	3267.53	32.19	419.50	3.08	0.00	0.00		
Panama	42.46	0.00	0.00	0.00	0.00	0.00	2.03	0.02						
Philippines	1079.15	1.71	0.00	0.00	0.00	0.00	203.20	2.00	672.58	4.94	0.00	0.00		
Poland	1606.05	1.08	0.00	0.00	0.00	0.00	2.44	0.02						
Romania	966.08	0.00	0.00	0.00	0.00	0.00	20.32	0.20						
Russia	1550.12	22.14	0.00	0.00	0.00	0.00	365.77	3.60						
Rwanda	385.11	9.83	1516.11	14.94	1376.14	13.56	231.65	2.28						
Senegal	560.83	0.18	2228.06	21.95	2585.26	25.47	170.69	1.68	21.90	0.16	0.00	0.00		
Slovak Republic	147.25	0.09	0.00	0.00	0.00	0.00	1.22	0.01						
South Africa	430.64	13.61	0.00	0.00	0.00	0.00	36.58	0.36						
Sri Lanka	467.98	26.39	0.00	0.00	0.00	0.00	36.58	0.36	214.71	1.58	0.00	0.00		
Tanzania	1401.90	47.08	1023.33	10.08	441.24	4.35	1036.34	10.21	0.00	0.00	0.00	0.00		
Thailand	1106.50	3.42	0.00	0.00	0.00	0.00	170.69	1.68	2966.45	21.77	7067.88	51.88		
Tunisia	578.24	0.38	0.00	0.00	0.00	0.00	16.26	0.16	205.45	1.51	0.00	0.00		
Turkmenistan	20.31	0.00	0.00	0.00	0.00	0.00	8.13	0.08						
Uganda	848.19	31.35	3700.78	36.46	3472.35	34.21	621.81	6.13						
Venezuela	114.84	0.65	0.00	0.00	0.00	0.00	20.32	0.20	693.86	5.09	0.00	0.00		
Vietnam	1776.42	18.52	1740.70	17.15	2779.84	27.39	2357.17	23.22						
Zambia	881.18	7.14	2094.83	20.64	2015.74	19.86	121.92	1.20	0.00	0.00	0.00	0.00		
Zimbabwe	156.08	7.01	0.00	0.00	0.00	0.00	32.51	0.32	19.78	0.15	0.00	0.00		

Source : McGillivray (2003b)

Differences between prescribed and actual allocations

Table 2
Differences between prescribed and actual allocations

	Actual ODA or OA commitments 2000		Prescribed ODA or OA commitments											
			Collier & Dollar				McGillivray & White				Llavador & Roemer			
			Headcount US\$2		Headcount US\$1		Equal opportunity		Utilitarian					
			Total ODA	Swedish ODA	Total ODA	Swedish ODA	Total ODA	Swedish ODA	Total ODA	Swedish ODA	Total ODA	Swedish ODA		
Algeria	259.96	0.39	-259.96	-0.39	-259.96	-0.39	-170.55	0.49	-83.16	0.91	-259.96	-0.39		
Belarus	38.93	7.63	-38.93	-7.63	-38.93	-7.63	-22.67	-7.47						
Botswana	31.18	0.25	-31.18	-0.25	-31.18	-0.25	-29.96	-0.24	-14.28	-0.13	9.15	0.05		
Brazil	254.50	1.46	-254.50	-1.46	-254.50	-1.46	123.46	2.26						
Bulgaria	429.57	0.10	-429.57	-0.10	-429.57	-0.10	-413.31	0.06						
Chile	69.09	0.85	-69.09	-0.85	-69.09	-0.85	-56.90	-0.73	489.62	3.25	-69.09	-0.85		
China	2977.49	4.78	-2977.49	-4.78	-2977.49	-4.78	-1095.82	13.76						
Colombia	1267.37	9.05	-1267.37	-9.05	-1267.37	-9.05	-1202.34	-8.41	-504.06	-3.45	-1267.37	-9.05		
Costa Rica	84.10	1.81	-84.10	-1.81	-84.10	-1.81	-82.47	-1.79	448.17	2.10	-84.10	-1.81		
Côte d'Ivoire	385.50	0.24	972.45	13.14	-385.50	-0.24	-214.81	1.44	-344.45	0.06	-385.50	-0.24		
Czech Republic	211.52	0.04	-211.52	-0.04	-211.52	-0.04	-210.71	-0.03						
Ecuador	180.88	0.44	-180.88	-0.44	-180.88	-0.44	-152.43	-0.16	95.02	1.59	-180.88	-0.44		
Egypt	1779.37	1.33	-1779.37	-1.33	-1779.37	-1.33	-1356.70	2.83	-1653.32	-0.40	-1779.37	-1.33		
Estonia	105.22	2.75	-105.22	-2.75	-105.22	-2.75	-104.41	-2.74						
Ethiopia	561.53	10.80	1412.96	8.65	1140.49	5.97	2429.64	18.67	-521.36	-10.51	-561.53	-10.80		
Guatemala	239.66	13.34	-239.66	-13.34	1732.46	6.09	-174.63	-12.70	-119.69	-12.46	-239.66	-13.34		
Guinea	199.73	0.07	-199.73	-0.07	-98.08	0.93	3.47	1.93						
Guinea-Bissau	87.98	0.40	1236.87	12.65	1392.21	14.18	521.63	5.61						
Honduras	511.59	11.80	2301.14	15.91	3266.03	25.42	-487.21	-11.56	-483.22	-11.59	-511.59	-11.80		
Hungary	312.44	0.21	-312.44	-0.21	-312.44	-0.21	-311.63	-0.20						
India	1587.61	7.40	-1509.23	-6.63	-1521.53	-6.75	10238.89	109.11						
Indonesia	1986.33	0.87	-1986.33	-0.87	-1986.33	-0.87	1183.66	30.36	3197.79	37.18	-1986.33	-0.87		
Jamaica	144.31	1.22	-144.31	-1.22	-144.31	-1.22	-140.25	-1.18	-141.22	-1.20	-144.31	-1.22		
Jordan	574.23	0.13	-574.23	-0.13	-574.23	-0.13	-566.10	-0.05						
Kazakhstan*	302.80	0.86	-302.80	-0.86	-302.80	-0.86	-270.29	-0.54						
Kenya	784.33	28.05	268.83	-17.67	456.53	-15.83	-577.06	-26.01	-726.45	-27.63	-784.33	-28.05		
Korea	0.00	0.00	0.00	0.00	0.00	0.00	2.03	0.02	9086.48	89.52	10561.67	77.52		
Kyrgyz Rep.	276.05	0.82	2372.20	25.27	597.82	7.79	-259.79	-0.66						
Lesotho	38.46	0.07	3094.54	30.80	3556.22	35.34	-18.14	0.13						

Table 2 (continued)
Differences between prescribed and actual allocations

	Actual ODA or OA commitments 2000		Prescribed ODA or OA commitments											
			Collier & Dollar				McGillivray & White				Llavador & Roemer			
			Headcount US\$2		Headcount US\$1		Equal opportunity		Utilitarian					
			Total ODA	Swedish ODA	Total ODA	Swedish ODA	Total ODA	Swedish ODA	Total ODA	Swedish ODA	Total ODA	Swedish ODA		
Lithuania	237.46	19.96	-237.46	-19.96	-237.46	-19.96	-236.65	-19.95						
Madagascar	383.80	0.22	745.68	10.91	817.60	11.62	-83.06	2.74	-360.64	-0.05	-383.80	-0.22		
Malaysia	1189.92	0.00	-1189.92	0.00	-1189.92	0.00	-1173.66	0.16	-3.19	8.71	-1189.92	0.00		
Mauritania	240.09	0.21	1383.26	15.78	1242.17	14.39	-158.81	0.59						
Mexico	369.30	0.15	-369.30	-0.15	-369.30	-0.15	-275.83	0.77	2264.89	19.18	-369.30	-0.15		
Moldova	111.18	2.67	-111.18	-2.67	-111.18	-2.67	132.67	-0.27						
Morocco	693.12	0.00	-693.12	0.00	-693.12	0.00	-690.68	0.02	-316.26	2.77	-693.12	0.00		
Nepal	402.05	0.93	492.80	7.89	602.80	8.97	154.73	4.56						
Nicaragua	455.21	27.70	1539.18	-8.05	2318.17	-0.38	-430.83	-27.46						
Niger	304.37	0.07	808.77	10.90	810.84	10.92	102.04	3.93	-295.90	-0.01	-304.37	-0.07		
Nigeria	311.14	0.78	287.21	5.11	318.87	5.43	2659.71	28.49	-9.64	1.43	-311.14	-0.78		
Pakistan	1188.07	1.15	458.53	15.07	-1188.07	-1.15	2079.46	31.04	-768.57	1.93	-1188.07	-1.15		
Panama	42.46	0.00	-42.46	0.00	-42.46	0.00	-40.43	0.02						
Philippines	1079.15	1.71	-1079.15	-1.71	-1079.15	-1.71	-875.95	0.29	-406.57	3.23	-1079.15	-1.71		
Poland	1606.05	1.08	-1606.05	-1.08	-1606.05	-1.08	-1603.61	-1.06						
Romania	966.08	0.00	-966.08	0.00	-966.08	0.00	-945.76	0.20						
Russia	1550.12	22.14	-1550.12	-22.14	-1550.12	-22.14	-1184.35	-18.54						
Rwanda	385.11	9.83	1131.00	5.11	991.03	3.73	-153.46	-7.55						
Senegal	560.83	0.18	1667.23	21.77	2024.43	25.29	-390.14	1.50	-538.93	-0.02	-560.83	-0.18		
Slovak Republic	147.25	0.09	-147.25	-0.09	-147.25	-0.09	-146.03	-0.08						
South Africa	430.64	13.61	-430.64	-13.61	-430.64	-13.61	-394.06	-13.25						
Sri Lanka	467.98	26.39	-467.98	-26.39	-467.98	-26.39	-431.40	-26.03	-253.27	-24.81	-467.98	-26.39		
Tanzania	1401.90	47.08	-378.57	-37.00	-960.66	-42.73	-365.56	-36.87	-1401.90	-47.08	-1401.90	-47.08		
Thailand	1106.50	3.42	-1106.50	-3.42	-1106.50	-3.42	-935.81	-1.74	1859.95	18.35	5961.38	48.46		
Tunisia	578.24	0.38	-578.24	-0.38	-578.24	-0.38	-561.98	-0.22	-372.79	1.13	-578.24	-0.38		
Turkmenistan	20.31	0.00	-20.31	0.00	-20.31	0.00	-12.18	0.08						
Uganda	848.19	31.35	2852.59	5.11	2624.16	2.86	-226.38	-25.22						
Venezuela	114.84	0.65	-114.84	-0.65	-114.84	-0.65	-94.52	-0.45	579.02	4.44	-114.84	-0.65		
Vietnam	1776.42	18.52	-35.72	-1.37	1003.42	8.87	580.75	4.70						
Zambia	881.18	7.14	1213.65	13.50	1134.56	12.72	-759.26	-5.94	-881.18	-7.14	-881.18	-7.14		
Zimbabwe	156.08	7.01	-156.08	-7.01	-156.08	-7.01	-123.57	-6.69	-136.30	-6.86	-156.08	-7.01		

Source: McGillivray (2003b)