



Better aid modalities: are we risking real results?

Literature review

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Contents

	Acknowledgements	i
	Contents	ii
	Abbreviations	ii
1	Introduction	1
2	Building a new typology of existing (and emerging) aid instruments	2
2.1	Key findings and main issues in the existing research	2
2.2	Summary: to what extent does the activity duplicate what has already been examined and usefully explore a new set of issues?	6
3	Understanding recipient government perceptions of effective aid instruments	7
3.1	Key findings and main issues in the existing research	7
3.2	Summary: to what extent does the activity duplicate what has already been examined and usefully explore a new set of issues?	11
4	Embedding political economy insights in aid instrument design	13
4.1	Key findings and main issues in the existing research	13
4.2	Summary: to what extent does the activity duplicate what has already been examined and usefully explore a new set of issues?	17
5	Designing portfolios of complementary aid instruments	18
5.1	Key findings and main issues in the existing research	18
5.2	Summary: to what extent does the activity duplicate what has already been examined and usefully explore a new set of issues?	21
6	Comparing the fiduciary risks of different aid instruments	22
7	Designing better frameworks for aid delivery options	23
7.1	Key findings and main issues in the existing research	23
7.2	Summary: to what extent does the activity duplicate what has already been examined and usefully explore a new set of issues?	27
8	Conclusion	29
	References	30

Abbreviations

ADB	Asian Development Bank
AfDB	African Development Bank
AIDS	Acquired Immune Deficiency Syndrome
APPP	Africa Power and Politics Programme
ARTF	Afghanistan Reconstruction Trust Fund
CDF	Comprehensive Development Framework
CFS	Centre for the Future State
COD	Cash on Delivery
CPIA	Country Policy and Institutional Assessment
DAC	OECD Development Assistance Committee
DCI	Development Cooperation Ireland
DFI	Development Finance International
DFID	UK Department for International Development
DRI	Debt Relief International
EC	European Commission
EU	European Union
FDI	Foreign Direct Investment
GBS	General Budget Support
HIPC	Heavily Indebted Poor Country
HIV	Human Immunodeficiency Virus
HSPF	Health Sector Pooled Fund (Liberia)
IDS	Institute of Development Studies
IFI	International Financial Institution
IMF	International Monetary Fund
INCAF	International Network on Conflict and Fragility
MDG	Millennium Development Goal
MOPAN	Multilateral Organisation Performance Assessment Network
MTDF	Multi-donor Trust Fund
MTEF	Medium-term Expenditure Framework
NGO	Non-governmental Organisation
ODI	Overseas Development Institute
OECD	Organisation for Economic Co-operation and Development
P4R	Programme for Results
PAF	Performance Assessment Framework
PEFA	Public Expenditure and Financial Accountability
PFM	Public Financial Management
PMF	Performance Management Framework
PRS	Poverty Reduction Strategy
RBA	Results-based Aid
SBS	Sector Budget Support
SBSiP	Sector Budget Support in Practice
SPA	Strategic Partnership with Africa
SWAp	Sector-wide Approach
TA	Technical Assistance
UK	United Kingdom
UNDP	United Nations Development Fund
UNICEF	UN Children's Fund

1 Introduction

In 2011, the Overseas Development Institute (ODI) hosted a meeting series on budget support. Its purpose was to allow prominent researchers, consultants and policy advisors to discuss some of the key questions and themes surrounding budget support today. The meeting was held in response to the current climate: growing political consensus around the results-based agenda and an expectation that, unless budget support can be shown to deliver broader development results without posing excessive reputational risks, the donor preference for it may diminish.

ODI then identified six specific topics for research to improve the range of policy options for delivering aid at the country level, drawing on the discussions and comments collected at the meeting series:

- 1 Building a new typology of existing (and emerging) aid instruments;
- 2 Understanding recipient government perceptions of effective aid instruments;
- 3 Embedding political economy insights in aid instrument design;
- 4 Designing portfolios of complementary aid instruments;
- 5 Comparing the fiduciary risks of different aid instruments; and
- 6 Designing better frameworks for aid delivery options.

The aim here is to examine the relevant literature that currently exists for each research topic. The literature review explores first the key findings and main messages in the existing literature and second whether the proposed research area duplicates existing research or does in fact propose to explore a new set of issues. The discussions at the meeting series made it clear that the research areas all address pertinent policy questions and dilemmas that face practitioners on a day-to-day basis. To help ODI to prioritise its activities, a literature review of all the research topics was proposed, to establish where ODI can add the greatest value. The results of this assessment are in the conclusion.

The literature review is made up of six sections, each exploring one of the individual research topics. Each section starts by explaining the proposed research area and then examines the key findings and main messages in the existing literature. It then provides a commentary on whether the proposed research area duplicates existing research or does in fact propose to explore a new set of issues.

2 Building a new typology of existing (and emerging) aid instruments

The aim of this activity is to develop a reasonably comprehensive mapping of aid modalities currently in use. It provides a working taxonomy which can be updated to reflect new hybrid forms identified or proposed through that research.

We assume that a spectrum of aid modalities exists, with a range of characteristics. Historically, attempts have been made to divide financial aid instruments into distinct categories, such as general budget support (GBS), sector budget support (SBS), integrated projects and stand-alone projects.¹ This division does not account for the variation in features of current modalities:² distinctive characteristics are developed to mitigate perceived risks identified by donor agencies. Examples include the multi-donor trust fund in Afghanistan (the Afghanistan Reconstruction Trust Fund (ARTF)) and the Protecting Basic Services project in Ethiopia. It is these modified features that often determine the effectiveness of an instrument, as well as its costs and benefits.

Some work has already been completed by the International Network on Conflict and Fragility (INCAF) for fragile states.³ This provides a possible starting point, especially to the extent that a fragile states lens is applied to the research.

Output: Detailed typology of aid instruments and hybrid forms

2.1 Key findings and main issues in the existing research

This section considers existing typologies of aid; the literature on the characteristics to take into account when developing a typology, such as the sectoral allocation of aid and political and economic conditions; the emergence of new results-based aid (RBA) instruments; and the need to view aid as a portfolio, given the interaction between different aid modalities.

There is a great deal of literature that broadly considers a small number of modalities (e.g. GBS, SBS, sector-wide approaches (SWAs), projects and technical assistance (TA)), but little discussion of the details of different instruments or variations in methods of implementation. Examples of broad typologies include the Development Assistance Committee (DAC) (2009) and World Bank (2007). There are reports evaluating the operation of budget support on a country-by-country basis, and the DAC joint evaluation report (IDD & Associates, 2006) brings together the findings of seven individual country studies, defining GBS and SBS and presenting a brief discussion of earmarking and additionality.

Specifics that would assist in the development of a detailed typology include characteristics such as financing, procurement, tracking and monitoring. The 'Extending the Aid Modalities in Ethiopia' report (DCI, 2005) outlines financing options and resource transfer features:

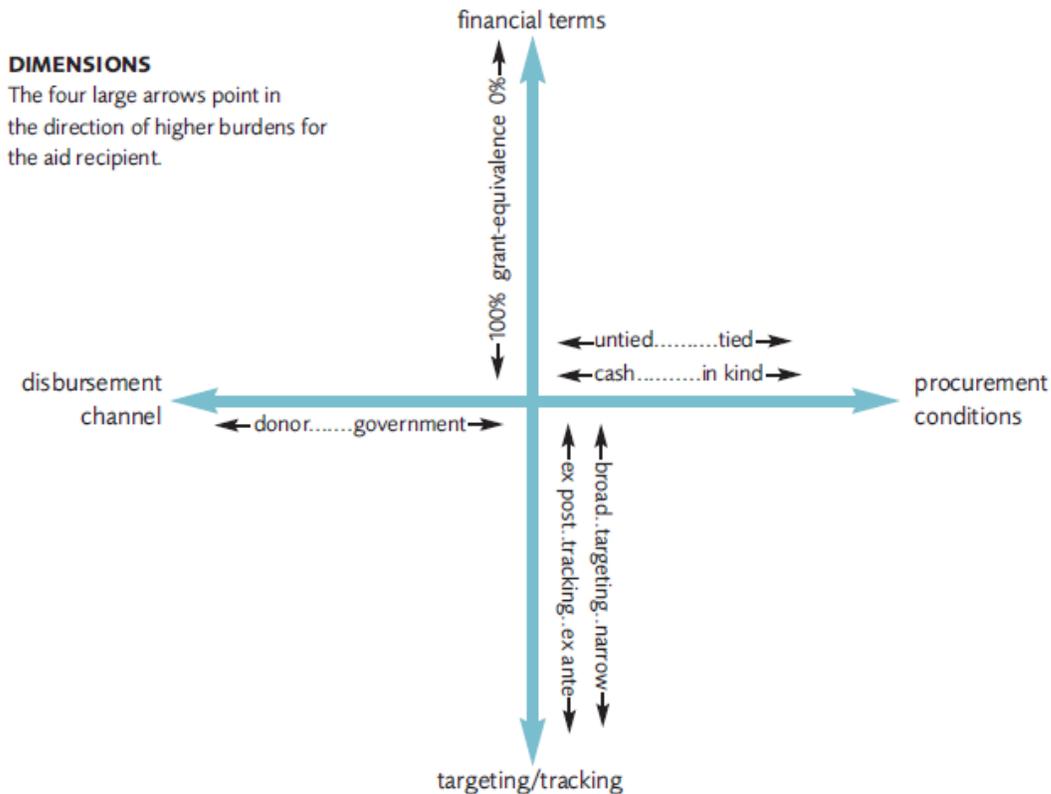
- Type and terms of finance (grants, loans);
- Procurement conditions (provision of cash or in-kind – skills or material – assistance and whether aid is tied to specific sources of supply);
- Targeting/tracking of donor resources (from tightly earmarked projects supporting a specific set of narrowly defined activities through *ex-ante* targeted and *ex-post* monitored/tracked funding, to completely un-earmarked GBS); and
- Disbursement channels, more or less aligned with government financial management systems.

1 See, for example, DFID (2008).

2 See, for example, Handley (2009).

3 See INCAF (2011).

Figure 1: Dimensions of aid terms and burdens



Source: Development Cooperation Ireland and Mokoro (2005).

Foster and Leavy (2001) characterise different forms of aid in terms of three types of obligations placed on the recipient: conditionality, earmarking and disbursement:

- Conditionality: policy measures which the partner government agrees to implement as a condition of the aid;
- Earmarking: limitations placed on what the aid must be spent on; and
- Disbursement channels and accountability: agreement on how the funds will be disbursed, accounted for and audited.

They then discuss in detail the range of options possible within each criterion by modality, including balance of payments support, GBS, SBS, sector earmarked support and project aid, distinguishing between that using government systems and that using parallel systems.

The country context determines two factors which have an impact on the operational characteristics of the instrument: i) the level at which donors work with government (upstream – advising on policy, assisting institutional reforms or funding policy changes; or downstream – supporting implementation through projects); and ii) the degree and nature of cooperation with other donors (none, working alongside each other or working through each other) (Development Cooperation Ireland and Mokoro, 2005). This context need not be captured explicitly in the typology, but it should be recognised that these extrinsic factors will influence the characteristics identified in the typology.

The DAC (2004) guidelines for budget support highlight the variability in the design of budget support instruments by discussing how to minimise transaction costs and volatility and enhance predictability, as well as the characteristics of conditionality. The discussion of SWAps distinguishes between these and traditional project approaches, drawing on country examples.

Some studies (Easterly and Pfütze, 2008; Hejerthome and White, 2000; White, 2002), while not presenting a typology of aid, discuss differences in characteristics, such as aid modalities, practices, specialisation, fragmentation and allocation, considering differences by agency type. White (2002) notes that official aid flows declined in the 1990s, with this negative trend offset by the movement towards untied aid and increased concessionality as grants have increased, although the World Bank continues to provide large amounts of aid as loans. White notes the dominance of DAC donors but the lack of concentration of aid, as it is spread thinly across many countries. Hejerthome and White (2000) present the historical pattern of aid flows by type of aid, sector and recipient geography and income levels. Allocative shifts of note are the decline in aid to the productive sectors and an increase to the services and social sectors. Regionally, Sub-Saharan Africa has dominated, with a decline in aid to other regions, related to their different stages of development.

It is important to understand the context in which aid is provided when considering the development of a typology. Tarp (2000) discusses the different types of aid, how it is accompanied by different political and economic conditions and the different purposes of aid. McGillivray (2003) and Alesina and Dollar (2000) note how historical and colonial links between recipients and donors influence aid patterns and discuss how aid is often allocated to reflect donors' interests. This relates to Outcome 3 and places aid in the context of international geopolitics.

Designing aid modalities for fragile states is more challenging, and the movement towards a robust state requires the development of institutional capacity, including mechanisms for accountability to citizens (OECD, 2005). A different approach for countries in transition is needed, one which may require a particular mix of instruments to facilitate off-budget delivery for activities such as humanitarian aid, gender and human rights-related activities and support to civil society. Financing should be sourced mainly from development budgets (INCAF, 2011). The European Commission (EC) Communication on budget support (2011) proposes a separate instrument for fragile states which has the potential to improve the appropriateness of aid delivery in different country contexts. The United Kingdom (UK) Department for International Development (DFID) recognises that the nature of the capacity limitations in fragile states may dictate the approach to the provision of aid, distinguishing between limited political will and limited state capacity to deliver core functions such as 'territorial control, safety and security, capacity to manage public resources, and the delivery of basic services' (DFID, 2008: 20). DFID stresses the importance of instrument flexibility in fragile states and obtaining the appropriate balance between institution building, service provision and social protection, and notes that insufficient political will suggests the need to support service delivery outside of government, whereas limited government capacity may require the use of multi-donor trust funds (ibid.).

Pooled funds may be particularly useful in fragile contexts, as they can get the money flowing quickly to obtain results on the ground and have the advantages of coherence, predictability, risk management and alignment with national priorities (INCAF, 2011). Sequencing may be important, such that different operational details are required at different stages of development: immediate results requiring flexible and rapid instruments managed and implemented externally; and sustained methods of support demanding jointly managed instruments working through country systems. The sustained mechanisms should show a clear link with national priorities and systems, particularly budgetary systems, with a view to moving towards budget support (ibid.). INCAF also supports the G7+ suggestion to implement mechanisms for additional oversight and controls to speed up movement towards using country systems.

Coppin et al. (2011) consider pooled funds and differences in their operation, developing an effectiveness scoring tool to assess good practice. They examine three pooled funds, two of which are considered effective and one which is problematic: the ARTF, the Liberia Health Sector Pooled Fund (HSPF) and the Southern Sudan Multi-donor Trust Fund (MDTF). They consider ownership, alignment, harmonisation, delivery of results and mutual accountability.

Mutalemwa and Mbilinyi (2006) categorise countries in terms of aid management systems:

- Category 1: countries that are highly rated – Botswana, Ghana, Tanzania and Vietnam;
- Category 2: countries that are doing fairly well but could do better – Burkina Faso, Cape Verde, Ethiopia, Mozambique, Rwanda and Uganda;
- Category 3: countries trying to improve but in fragile situations, thus with still many capacity gaps – Cameroon and Zambia; and
- Category 4: countries in a critical situation – Burundi, Haiti and Sierra Leone.

The increased focus on results has been reflected in the movement towards the monitoring of outcome indicators in performance assessment frameworks (PAFs) and, more recently, in the discussion of RBA as a modality and the early stages of piloting (DFID's pilots in Ethiopia, India and Uganda) and programme development (the World Bank's Programme for Results (P4R)). The development of RBA modalities is a response to increasing awareness of the deficiencies of traditional aid instruments, which are seen as 'cumbersome, invasive and prescriptive' (ODI, 2011a: 2).

The World Bank's P4R has been designed as an alternative to project and budget support, in an attempt to address situations where existing aid modalities are too restrictive. It will finance government projects, linking disbursement to results rather than inputs, although it also involves safeguards such as a project review, consideration of the results framework and a risk mitigation strategy, along with fiduciary, environmental and social safeguards (World Bank, 2011a). It remains to be seen how it will be implemented and whether the Bank's approval and assessment mechanisms will result in it operating closer to a project modality.

The Cash on Delivery (COD) approach provides more autonomy to the recipient country, as the degree of involvement of funders is responsive to the recipient's needs and can range from directly funding only the results, with no policy involvement, to advising on strategy if required. This approach differs from that of GBS as it focuses on a small number of indicators and necessitates independent verification. There is also, however, scope for GBS as an instrument to be adjusted to respond more clearly to results (ODI, 2011a: 3), and a question remains as to the extent to which existing instruments such as the European Union (EU) Millennium Development Goal (MDG) Contract could fulfil this purpose (Rogerson, 2011). A number of design features are currently being discussed, including how the reward tariff and indicator will be agreed on, whether it will be exempt from political suspension safeguards and how to respond to exogenous factors (*ibid.*).

The interaction and trade-off between aid instruments is important when considering a typology of instruments, as no modality is delivered in isolation.⁴ The acknowledgement of the complex reality of a portfolio of aid instruments stresses complementarities such as how the increased focus on government planning and budgeting systems through GBS can help in sector planning and performance, and can encourage the harmonisation of aid across other modalities as sector approaches may become more coordinated. The use of other forms of aid does, however, also reduce the harmonisation and transparency of aid achieved through GBS, particularly where projects continue to be off-budget and therefore less transparent. Furthermore, issues of wastage and quality of service delivery remain, pointing to the need for continued development of public financial management (PFM) systems and sector technical cooperation and dialogue (IDD & Associates, 2006).

The EC Communication on budget support (EC, 2011) recognises that GBS is a package of inputs and includes policy dialogue and TA and capacity-building support in addition to the transfer of finance. The Communication indicates a desire to explore COD, although its compatibility with the variable tranche approach is unclear. The Communication does not present targets for GBS, but stresses the importance of achieving the appropriate balance at the country level through a portfolio of different instruments. The rebranding of SBS as sector reform contracts also involves strengthening institutions and systems, but it is unclear to what extent the focus on frontline services overlooks the middle stages of service delivery.

⁴ DFID considers this in its paper on aid modalities (2008: 14).

Considering aid instruments as a portfolio, it remains unclear to what extent RBA as a new modality will channel some funding away from GBS or SBS, as, for the incentive effect to operate, substantial amounts of funding may be required (ODI Roundtable, 2011; Rogerson, 2011). This is a concern, as GBS has the advantage of offering an 'all of government approach', whereas RBA places the focus on an individual outcome. Although the requirement to receive RBA depends on performance within one sector, the disbursement can be channelled as the recipient desires and is therefore fully fungible (Rogerson, 2011). This may have implications for donor harmonisation, although there may be advantages in terms of developing an enhanced division of labour among donors.

2.2 Summary: to what extent does the activity duplicate what has already been examined and usefully explore a new set of issues?

No typologies were found that explore country differences or attempt to draw out the advantages and disadvantages of the different modalities in operation. There are presentations of simplified typologies by type of aid instrument and by financing features (DCI, 2005). The latter is considered more helpful, as it enables an examination of the operational details of the instruments and provides the scope to capture how mechanisms and procedures can vary in practice, characteristics that can be crucial in the effective implementation of aid.

Also, there is a need to take a forward-looking perspective and factor in new elements, such as the approach to aid for transition countries and fragile states; the rise of non-Organisation for Economic Co-operation and Development (OECD) donors; new financing methods that blend aid and private finance; and new policy focuses such as climate change and changes in risks as global security concerns increase. Uncertainties include a potential increasing interdependence between aid and other cross-border flows such as foreign direct investment (FDI), trade and remittances. The outcomes below pursue some of these factors, and the proposed structure of the typology offers the scope for the inclusion of these elements.

Based on the review of the literature, a suggested way to approach the typology is to build on DCI's categories with some expansions. For example:

- 1 Country classification (good performers, transition countries, fragile states; identification of country risks; and new categories such as stagnators);
- 2 Type and terms of finance (grants, loans, private finance, links to FDI, trade or remittances);
- 3 Procurement conditions (provision of cash or in-kind – skills or material – assistance and whether aid is tied to specific sources of supply);
- 4 Targeting/tracking of donor resources and timing (from tightly earmarked project supporting a specific set of narrowly defined activities or policies through to *ex-ante* targeted and *ex-post* monitored/tracked funding, to completely un-earmarked GBS; identification of new policy areas);
- 5 Disbursement channels (more or less aligned with government financial management systems); and
- 6 Bureaucratic procedures (signing-off requirements; joint with government or other donors).

A number of country studies could usefully be reviewed and feed into the development of a detailed typology. Examples include the DAC GBS evaluations, which detail how GBS is implemented in seven countries (IDD & Associates, 2006), and studies of the health sector in Mozambique, the education sector in Tanzania and the water and sanitation sector in Uganda (Williamson and Agha, 2008).

3 Understanding recipient government perceptions of effective aid instruments

This activity investigates and analyses the features of aid delivery that recipient governments find most positively supportive of their development objectives.

Work on aid modalities tends to assume a set of partner government preferences. This process is reinforced through donor-centric evaluation work. Limited cross-country data exist about recipient government preferences for aid instrument design and aid delivery, and about the criteria and assumptions underlying such preferences. Some recent evidence from fragile states suggests budget support is the preferred modality and project aid the least desirable form of aid.⁵ The characteristics of effective donor behaviours government officials identified for recent ODI research were predictability; responsiveness, timeliness and flexibility; recipient-driven alignment with government priorities; and degree of involvement.⁶

This proposed research will examine which features of aid modalities and delivery partner countries prefer and why. It will draw on the taxonomy developed in parallel work (1.1) and inform the future development and implementation of aid modalities. It will address both the technical issues associated with aid delivery, such as predictability and transaction costs, as well as political considerations, such as conditionality and the negotiation and management of contracts.

Output: Synthesis of data and findings on effective aid instruments; guidance for governments and donors

3.1 Key findings and main issues in the existing research

Summary of the different studies and methodology used

This area sees a number of routine surveys (e.g. Strategic Partnership with Africa (SPA) and Paris Surveys) of current donor practices but only a limited amount of research to gather recipients' views of the preferred features of modalities and delivery. ODI studies dominate the literature that directly surveys aid modalities. This section presents a summary of the studies (including the donor-centric surveys) and discusses the choice of methodology, as this is recognised as central in achieving reliable results that will contribute to Outcome 6.

The ODI studies are Burall et al. (2006; 2007) and Wathne et al. (2009). These are summarised in Wathne and Hedger (2010). Burall et al. (2006) consider the perception survey literature and present results from workshops in Bangladesh, Cameroon and the UK that gathered the views of representatives of finance ministries and civil society groups from 27 countries. They identify best practice criteria for different donors and rank donors against these.

Burall et al. (2007) carried out the first systematic survey of aid recipients. In a pilot study commissioned by DFID, they surveyed representatives from government, civil society, parliament and business from Bangladesh, Ghana, India, South Africa, Tanzania and Zambia. The survey aimed to obtain perceptions of the effectiveness of multilateral aid organisations and how additional aid should be delivered by assessing performance according to the three measures from the Paris Declaration – overall development effectiveness, harmonisation and alignment – and ranking agencies against 15 performance criteria related to funding and policies and procedures (adapted from Debt Relief International (DRI)) and in the order of preferred disbursement channel. The respondents were asked about their perceptions of seven organisations: the African Development Bank (AfDB); the Asian Development Bank (ADB), the

⁵ At a recent G7+ meeting, participants wanted to push for 100% of aid to be allocated in the form of budget support in partner countries.

⁶ See Burall et al. (2007) and Wathne and Hedger (2009) for previous ODI research on recipient perspectives on donor effectiveness.

EC, the Global Fund to Fight AIDS, Tuberculosis and Malaria, the United Nations Children's Fund (UNICEF), the United Nations Development Fund (UNDP) and the World Bank.

Wathne et al. (2009) carried out interviews based on a semi-structured questionnaire with senior government officials in Ethiopia, Sierra Leone and Zambia with 77 people. The questionnaires comprised i) an open-ended question on what makes for an effective multilateral donor; ii) questions related to partnership behaviour based on six predefined criteria; iii) questions related to the project cycle and donor effectiveness; and iv) questions about recipients' decision making regarding future funds.

Other studies that have been undertaken include a number of routine surveys and questionnaires which make assumptions about the preferred characteristics.

DRI has developed a methodology to assess the quality and performance of donor assistance in terms of concessionality, types of assistance, flexibility, predictability and conditionality. It considers disbursement methods, schedules and procedures, procurement rules and coordination. The report (DRI, 2007) rates the perceptions of government senior aid management officials and ministers to identify best practices.

Development Finance International (DFI) has developed a methodology to assess the performance of donors that has been applied since 2002.⁷ Through workshops in Heavily Indebted Poor Countries (HIPC), ministry of finance officials assign a score (one low to five high) against the following:

- Policies: concessionality, amount of assistance, type and channel of assistance, sectors and projects, flexibility, predictability, policy conditionality and policy dialogue; and
- Procedures: conditions precedent, disbursement method, disbursement procedure, procurement procedures, coordination and evaluation.

These scores are then used to assess the quality of donors. Governments also assess the impact of their own procedures on aid flows. The results are contained within a donor guide which summarises the performance of donors to provide a tool for recipient governments to identify which donors to work with. The October 2009 guide provided 48 donor profiles, of which 34 are bilateral donors, 11 multilaterals and 3 global funds.

The Multilateral Organisation Performance Assessment Network (MOPAN) surveys multilateral organisation staff to assess their partnership performance with national stakeholders and other donors using a questionnaire format compiled into a country report. Common Approach surveys have been conducted since 2004; the 2011 Common Approach will assess five multilateral organisations in 12 developing countries.

Three Paris Surveys (2005, 2007 and 2010) monitor the performance of donors against 12 indicators assessed by donor and government respondents, managed by a national coordinator. Questionnaires are designed to obtain qualitative and quantitative data. Large disparities in responses have meant extensive data reconciliation and point to the different perceptions of both groups of respondents (DAC, 2011).

The Public Expenditure and Financial Accountability (PEFA) assessment includes three indicators that rate donor performance: i) predictability of direct budget support; ii) financial information provided by donors for budgeting and reporting on project and programme aid; and iii) proportion of aid managed by use of national procedures. While not intended for cross-country comparison, the PEFA assessment aims to monitor changes within a country's PFM systems over time. Some country PAFs that accompany the provision of GBS have sections that monitor the performance of donors, based on agreed actions.

The SPA undertook an annual survey assessing the progress of 20 budget support donors in aligning and harmonising their activities in 15 Poverty Reduction Strategy (PRS) countries.

⁷ www.development-finance.org/en/services/guide-to-donors.html. Johnson and Matthew (2004) is a DFI publication.

Respondents rank the performance of donors between one (poor) and five (excellent) by completing a structured questionnaire with tick boxes and space for comment. The questionnaire comprises i) a joint government and donor response; ii) GBS donors individually; and iii) government representatives (SPA, 2008).

On an agency-by-agency basis, UNDP annually seeks perceptions of its performance from clients, and other multilaterals carry out sporadic assessments to feed into the development of new programmes. As part of its Comprehensive Development Framework (CDF), the World Bank monitored its partnership behaviour (Scott et al., 2008).

Other assessments evaluate the performance of organisations but do not capture the views of the aid recipients. DFID's Multilateral Effectiveness Framework was developed in 2003/04 to assess the performance of multilaterals from the perspective of their staff. Two Danish Performance Management Framework (PMF) surveys (2002 and 2005) have been undertaken to assess multilateral organisations using secondary data, including MOPAN; evaluations of some organisations; minutes from high-level consultations; minutes from board and annual meetings; data from results-based management systems; and perceptions of Danish multilateral representatives and embassies on organisational effectiveness (Royal Danish Ministry of Foreign Affairs, 2006; see also Burrall and Pallen, 2009).

At the sectoral level, Sundewalla et al. (2010) analyse stakeholder perceptions of the coordination of health sector aid in Zambia. However, rather than gathering perceptions of the end users of services, they compiled the views of donors and government involved in the sector, using a case study approach consisting of interviews and a review of secondary data.

Two studies assess perceptions in conflict-affected areas. CDA Collaborative Learning Projects (2011) gathered perceptions of how local people experienced and perceived aid efforts in 20 conflict-affected areas, covering almost 6,000 people over a period of four years through listening exercises in 20 countries in Africa, Asia, Europe and the Middle East. These exercises involved unstructured conversations with community members, government officials, community-based and civil society organisations, religious leaders, teachers, business people, health workers, farmers, traders and others who either had directly received assistance or had been involved in the aid process.

The Fritz Institute (2005) compiled views of people affected by the 2004 tsunami in India, Indonesia and Sri Lanka through a structured interview approach based on representative samples. In a survey of over 2,000 people affected, aid recipients' perceptions of the nature of the aid delivered, its impact and ongoing challenges were assessed by using rating scales.

Methodologically, the ODI surveys have used a mix of open-ended questions and pre-identified criteria. The open-ended questions have asked what should change about multilateral aid (Burall et al., 2007) and what makes an effective multilateral agency, with appropriate follow-up questions to identify donor effectiveness in terms of partnership behaviour and interactions within projects (Wathne et al., 2009).

Pre-identified criteria used are in the area of best practice behaviour (Burall et al., 2007). DRI (2007) rates the perceptions of government senior aid management officials and ministers against 34 criteria that are benchmarked against identified best practices, and the pre-Accra consultations also identified key issues.

A key observation is that the different methodologies produce different results: the open-ended identification of aspects of partnership behaviour resulted in only one respondent identifying transparency, but this was ranked as one of the top three aspects of partnership behaviour (Wathne et al., 2009). Methodological issues to be aware of include respondents not being fully aware of the meaning of the criteria they are ranking; difficulties in undertaking rankings owing to the complexity of the concepts; and time limitations leading to some sections of the questionnaire being given more attention than others (ibid.). This latter increases the risk of researcher bias, as under time pressure the researcher may actively interpret which part of the questionnaire is the most important.

Other challenges identified were that some interviews took place in groups, for example with political advisers present, making clear rankings more difficult to obtain. It was difficult to capture the interrelated character of some attributes using the ranking methodology, in particular the dimensions of partnership behaviour. It is likely that the attributes that present particular challenges are more likely to be focused on, therefore skewing the responses (Wathne et al., 2009).

The limited time for the identification of respondents and data collection may have had an impact on the quality of the results in India, South Africa and Zambia, as there was uneven representation across the different sample groups; the lengthy questionnaire was also a problem (Burrall et al., 2007). The use of a country coordinator to identify well-informed persons requires them to function as gatekeepers. This has the advantage of ensuring participants are well informed, but also carries the risk of biased findings, as participation may be restricted to a particular group of respondents, for example with a particular political affiliation.

The 2007 survey (Burrall et al., 2007) used different methods to interview respondents, from self-completion on paper as the most common method, followed by face-to-face and email; a small number were completed online. The use of different methods has the advantage of enabling follow-up as a method of increasing the response rate, but also holds the risk that the different approaches may elicit different responses as a result of the different ways in which the questions are presented. The report addresses key methodological issues of weighting to counterbalance different sample sizes by country, cautioning on non-responses, the small sample size and the use and interpretation of statistical testing. Non-response was a key issue, particularly in relation to the degree to which respondents were informed about the activities of the different agencies; for example, a large non-response rate may owe to respondents not feeling informed enough to rank organisations.

DRI (2007) notes weaknesses in indicators, stating that these should be improved in areas of flexibility, multiyear programming, disbursement scheduling, reducing conditionality, reducing counterpart fund requirements, capacity building, programme-based approaches, use of country systems and harmonisation of missions. In particular, there is a weakness in mutual accountability in relation to the insufficient monitoring of donor performance in comparison with that of recipient governments.

Findings

The findings across different studies on the nature of the financing produce some concrete recommendations for improvement. The levels and targeting of financial assistance could be enhanced, improving the focus of aid to fund complete projects and increasing the funds directed towards implementation and delivery (Wathne et al., 2009). The counterpart fund requirement for around one-third of aid often results in disbursement delays, by on average five months (DRI, 2007). The flexibility of financing is considered inadequate in response to exogenous shocks, and there are criticisms of continued high levels of inflexible conditionality for budget and sector support programmes (ibid.). Increased responsiveness to recipients' multiyear programming cycles (ibid.) and a reduction in tied aid (Wathne et al., 2009) would be welcome improvements.

The perception surveys carried out by ODI focused on gathering views of the behaviours necessary for a donor to be effective, with a focus on multilateral donors. From a list of six behaviours, three were considered most important: i) depth of commitment to development; ii) responsiveness to country circumstances; and iii) support for recipient-driven policy (Wathne et al., 2009).

Depth of commitment was found to be associated with the provision of long-term predictable aid and understanding recipients' capacity limitations in terms of not demanding unrealistically high levels of counterpart funding and recognising demands in relation to broader counterpart resources such as staff time and equipment. Aid predictability over the medium term is important for fiscal policy implementation and the reliability of national budgets, such that

donors should make multiyear commitments in line with recipients' planning and budgeting cycles and ensure aid is delivered accordingly.

Flexibility to respond to the needs of the recipient and changing circumstances in-country are particularly important. Adjustments may be necessary to respond to findings of mid-term evaluations and changing procurement costs during a project lifetime. In terms of aid procedures, the flexibility of donors to respond to country systems, such as budgeting and reporting requirements, disbursement conditions and the carryover of funds, is important and necessitates decentralisation to country offices. Delegation and decentralisation to country offices allows for the incorporation of donor understanding of country circumstances into policy. Donor advice is recognised as valuable, and the importance of donors adjusting their approach to the strategy of the government is noted as important, albeit with the caveat that governments should also recognise that their policies should to a degree address donor expectations (Wathne et al., 2009). It is the balance between addressing donor expectations and ensuring robust government ownership that can be particularly challenging in practice.

DRI (2007) found that donors performed better on policy than procedures, and that the rating of performance was lower than that of the Paris Survey, possibly because of the enhanced specificity of the indicators. Bilaterals perform better in terms of flexibility (having fewer conditions) and simplicity of disbursement procedures. Multilateral institutions perform better in terms of providing predictable and untied budget aid and effective TA. Among bilateral donors, the performance of emerging non-OECD donors was found to be generally less than that of OECD donors, but the difference was smaller than the international debate suggests, meaning there may be scope for enhancing their inclusiveness in international dialogue.

Multilateral agencies are valued for different attributes and rated differently according to stakeholder, country and sector (Burall et al., 2007; Wathne et al., 2009). There are some differences between agencies, but little overall variation (Burall et al., 2007). Both Burall (2006) and Burall et al. (2007) found the World Bank, UN agencies and the ADB to be the most highly rated, although in the former study the AfDB was ranked second. These findings differ from the analysis of Easterly and Pfütze (2008), who found UN agencies to be the worst performers, highlighting how researchers' analysis of performance indicators may differ from perceptions.

Results from the Zambia health sector study suggest donors and government are generally satisfied with the degree of coordination, although challenges in coordinating plans and agreements were identified (Sundewalla et al., 2010). The authors conclude that donor resources could be better integrated with the sector planning process and, to achieve this, a better understanding of the constraints of donor agencies is needed.⁸

Findings on perceptions of aid in conflict-affected environments highlight that, in many cases, aid has actually increased instances of conflict (CDA Collaborative Learning Projects, 2011). There are concerns about the politicisation of aid and the harmful effects of external agendas, and that policy and programming decisions that determine where, when, how and to whom assistance is provided can have significant impacts on local tensions and conflicts. Despite these findings, respondents did not call for the withdrawal of aid but rather greater attention to the delivery context and increased perception-gathering efforts to avoid unnecessary conflict.

3.2 Summary: to what extent does the activity duplicate what has already been examined and usefully explore a new set of issues?

No literature on recipient perceptions of new aid modalities could be found, and recipients' preferences for budget support in comparison with RBA are unclear (ODI Roundtable, 2011). There is scope for investigating the complexities of aid provision in detail, in particular perceptions of the interactions between aid instruments. An investigation of perceptions at the instrument and portfolio level would be illuminating.

⁸ The write-up on this is limited as the full study could not be obtained.

Also, an in-depth survey of perceptions should canvas the opinions of different stakeholder groups and capture the views of different subgroups and how they perceive different aid instruments. Interesting groupings at the country level might be civil society, recipients of services at the local level, the executive, the opposition, ministries of finance and line ministries; at a regional level, working with regional organisations may offer different approaches.⁹

The framing of the questions and exploring different methodologies may produce different findings; therefore, the design stage is crucial. The studies highlight the importance of pre-testing the questionnaire or survey approach prior to carrying out a larger study; ensuring sufficient time is allowed for sampling and data collection; and interviewing respondents individually (Burrall et al., 2007; Wathne et al., 2009). Also of importance is ensuring respondents are sufficiently informed – this is addressed in Burrall et al. (2007) by using a local contact to identify the sample – and ensuring all respondents understand the concepts. This could also be addressed by using targeted subsections of the questionnaire to different respondents, although this increases complexity at the data analysis stage.

The drawing out of the perceptions of aid recipients will highlight differences in the incentives donors and recipient countries face. In doing so, political economy influences and considerations can be reflected on, and a framing of these issues will add depth to the results of the perceptions survey.

⁹ In capturing the perceptions of civil society, the elite are likely to dominate as a result of issues of access.

4 Embedding political economy insights in aid instrument design

The aim of this activity is to provide evidence on the political economy of aid modalities and guidance on how to account for it more effectively in implementation.

It is widely acknowledged that decisions to give aid are affected by factors beyond the purely technical. Similarly, it is easy to accept that decisions about aid delivery reflect the forms of accountability facing donors and recipients. Such drivers are rarely accounted for well in the design and implementation of aid operations (e.g. budget support operations). Despite much discussion of political economy analysis and the recognition that some incentives and constraints facing donors and partner actors can be binding on their behaviour (Barder, 2009; Booth, 2011; Molenaers and Renard, 2011; Natsios, 2010), little has been done to analyse systematically such incentives or constraints and to use such knowledge in aid operations.

Facilitating a more candid dialogue between donor agencies and recipient governments about such constraints and adapting the design and implementation of aid modalities accordingly may improve their effectiveness by informing a more realistic and feasible set of policy options. This may in turn reduce the repeated rounds of negotiations related to policy actions that may not be politically feasible. Potentially, it would also help in identifying windows of opportunity, for which certain policy actions with certain actors are more likely to be achieved.

Output: Guidance and tools on the political economy of aid modalities

4.1 Key findings and main issues in the existing research

To consider these political economy issues, the existing literature is considered in relation to the following: i) the main constraints facing recipient governments and donors and ii) the impact these constraints can have on development outcomes.

Main constraints facing recipient governments and donors

Donors' interest in aid captures a variety of interests, from those of development to democratic, diplomatic and security interests (Molenaers and Renard, 2011; ODI, 2011b: Molenaers). A major constraint for donors relates to their responsiveness to domestic constituents, as they have to account to domestic tax payers for aid disbursements. Key issues are i) progress on poverty reduction and the efficiency of the expenditure, that is, the avoidance of waste and corruption (DFID internal communication); ii) the avoidance of disruption of aid such that disturbances or violence are avoided as they risk disrupting economic stability (North et al., 2007); and iii) the protection and enhancement of coalitions of investment that are in the donors' interests (Tilley, 2011). Easterly and Pfitze (2008) acknowledge the difficulties facing aid agencies owing to limited accountability to aid beneficiaries.

The recipient government has to present an external face to obtain foreign aid, but real legitimacy is sought from domestic, not international, sources. The issue is the extent to which the government, or the president specifically, can be perceived as seeking legitimacy from donors and still be accepted domestically. The political economy context in many recipient countries is that of a neo-patrimonial state. Neo-patrimonialism functions and depends on information asymmetry and the absence of a formal institutional framework. Therefore, interactions are highly personalised and depend on a narrow 'circle of trust', whereby the transfer of resources occurs through patron-client networks (Chabal and Daloz, 1999). Such transfers can be referred to as rents, which can be legal or illegal, and rent seeking is all activity that seeks to create, capture or re-allocate rents (Khan, 2004b)

The elite coordinate this activity, using rents to retain both their legitimacy and the stability and persistence of the state (Lindemann and Putzel, 2008). The elite dominate through

powerful groups that serve well-established interests and the elite bargain is the outcome that provides a competing group within the elite, the winning coalition, with incentives to be peaceful (North et al., 2007). This 'often requires off-budget "redistribution" through patron-client networks to achieve political stabilization [... involving] politicians [...] transferring resources to powerful clients and receiving, in exchange, their political support' (Khan, 2004a: 14). This relationship is sustained by the linkages between business and politics, used to identify opportunities and siphon off rents to allow redistribution to a wider group.

The impact of these constraints on development outcomes

This issue can be considered in terms of the conditionality relationship and the incentives of the government to allocate capacity to the aid relationship in the context of domestic influences on policy formulation. This is concluded by considering how these incentives operate together.

Donor influences on policy formulation: conditionality

The driving force of the use of conditionality is the desire of donors to influence policy and minimise risk. GBS as a modality necessitates increased risk taking by donors (ODI, 2011b: Molenaers), and the use of conditions is seen as a way in which donors can attempt to both influence the direction of policy and monitor outcomes.

There is a substantial body of literature on the limited effectiveness of conditionalities (e.g. Collier and Dollar, 2000; Killick, 1995; Tarp, 2000) and models of the operation of conditionality. Conditionality models address the extent of the divergence or convergence of views between donors and recipients (White and Morrissey, 1997) and short- versus long-term impacts of conditionality (Coate and Morris, 1996); game theory models highlight the nature and possible outcomes of the bargaining process (Kanbur, 2000; Mosley et al., 1995; Svensson, 2000); and the representativeness of government and the impact of policy reversibility (White and Morrissey, 1997).

We highlight here only the literature that presents insights into the political economy of aid through the policy formulation process.

Explaining the reasons for the persistence of conditionality, six objectives of conditionality have been identified: i) *paternalism* – donors believing they know what is best for the recipient; ii) *bribery* – persuading the recipient to change their behaviour; iii) *restraint* – the recipient agrees to reforms and conditionalities prevent policy reversal; iv) *signalling* – that the reform programme is genuine; v) *monitoring* – to ensure aid is having the intended effects; and vi) *supportive* – providing needed financing for reforms (Collier and Gunning, 1996, in White and Morrissey, 1997).

These different objectives can be expressed at different stages in the negotiation and aid delivery process by breaking the conditionality down into a series of game theory moves: i) the negotiating process on the terms of the conditions; ii) the implementation of policies by the recipient government; and iii) the donor's response in terms of future financing (Mosley et al., 1995). The bargaining strength of both players influences the outcomes of the first and the third stage, or *act*, and is based on their preferences as revealed in their utility functions.

The model notes the interests of different groups within the recipient and also the World Bank, such that the recipient groups that bear the political costs of the reforms (e.g. the line ministries) are often different from those involved in negotiating the agreement (the ministry of finance and the central bank) (Mosley et al., 1995). With the assumption that the reform interests differ between the donor and the recipient, even in the event of a repeated game, a recipient with a weak bargaining position can implement the conditionality on its own terms and still achieve follow-up finance, given that the interests of the donor are to disburse funds, thus discrediting the very basis of conditionality.

Kanbur (2000) identifies the incentives of donors to disburse and notes that these include broader economic issues but also can entail more personal incentives. He identifies four motivations: avoidance of economic chaos risked by non-receipt of aid inflows and a negative

impact on the poor; political clientelism; risk of non-servicing of debt; and the career interests of the aid agency personnel and the maintenance of the reputation of the agency. These are related to the ineffectiveness of conditionality.

Killick (2005) considers how an increasing awareness of the limitations of conditionality and the divergence of views of conditionality between international financial institutions (IFIs) and governments has allowed the movement towards a middle ground. Although there has been movement towards *ex-post* conditionality, the use of *ex-ante* conditionality does persist (Booth, 2011); this can be explained partly by donor incentives and perceptions of risk (Booth and Fritz, 2008; Tavakoli and Smith, 2011). Indeed, there is an indication of a move towards the renewed acceptability of policy and political conditionality (Molenaers and Nijs, 2009; Molenaers and Renard, 2011; EC, 2011).

The limitations of the Paris Declaration are that it does little to take into account the political realities of recipient countries (Booth, 2011) and, by extension, the constraints under which donor agencies operate. For donors to be effective in policy dialogue, they should understand the geostrategic importance of the country; the strength of government; whether the state is neo-patrimonial, developmental or both; and the nature and extent of developmental bottlenecks (Molenaers and Renard, 2011). Martens et al. (2002) explore incentives within donor agencies and inside partner country governments and how these can constrain the success of aid activities in different ways. With a focus on EU institutions, they find that multiple political principals and objectives can result in less clearly defined objectives.

Domestic influences on policy formulation

The rent-seeking influences of the political economy of the recipient extend to policy formulation, as the maintenance of stability requires the creation of opportunities for rent seeking (Khan, 2004a; Lindemann and Putzel, 2008; North et al., 2007). This results in cases where the policy priorities preferred by the international development community and captured in aid conditionalities are adjusted to allow payments to maintain the legitimacy of the elite that holds power. These domestic political economy influences must be weighed against the effectiveness of conditionality and the incentives of donors to disburse to determine the extent to which donors influence policy formulation. We now discuss the impact of this on the investment by the government in the aid architecture, looking first at conditionality.

An assumption remains implicit in some of the political economy literature that rent seeking is automatically unproductive. However, rent seeking may actually be productive, as argued by Khan (2004a; 2004b) and others. A developmental state is a function of the state's political and institutional capacities. In turn, these depend on i) the organisation of power in terms of the centralisation of the state; and ii) incentives through the rent process (the creation, seeking, distribution and utilisation of incomes and rents) (Kelsall and Booth, 2010; Khan and Jomo, 2000). These factors are based on the structure and incentives of the elite and the leadership and how they interact with society. This can be explored by examining which industries are most closely connected to the state, who are the members of the elite and how their interests overlap with developmental concerns such as technological adaptation and innovation. Concerning inequality and poverty reduction, the question is how narrow the elite is and the extent to which its persistence depends on networks that reach into wider society.

If incentives resulting from the rent process do not function in a way that results in a high growth outcome, then state intervention is necessary to create the conditions for transformation. These incentives, along with the time horizon of the leadership, provide the motivation for certain activities and therefore determine the extent to which growth-enhancing economic activities are pursued. This in turn is determined by the organisation and distribution of power among elite factions, and the competition between them has an impact on the emergence of the capitalist sector through the balance between state- and society-led rent seeking; the extent to which winners compensate losers; and whether state officials are political and economic value maximisers and whether they learn from mistakes (Khan, 2000).

How these incentives operate together

What is the balance between different influences on policy formulation – between donors and conditionality and domestic influences? Or to what extent can aid be transformative? Here, we consider the literature that weighs up these influences, the interrelationship between aid and domestic accountability and questions of political economy.

Harrison (2001) presents a picture of what he calls 'post-conditionality reforms', where the distinction between the external donor and the internal politics of African states is no longer valid, arguing that instead both work together intimately and build a set of mutual dependencies. The political economy literature reviewed above points to a different conclusion: that the mutual dependencies involve a pulling in different directions in pursuit of opposing interests in terms of the implementation of some reforms, although there is a coincidence of interests to disburse aid.

Devarajan et al. (2001) summarise 10 country case studies and find that major reforms are driven by political and economic crises and that domestic political economy plays the key role in policy formulation, therefore limiting the influence of aid and any associated conditionalities.

The impact of aid on domestic accountability is argued to be negligible, although the effectiveness of the channels through which accountability may be developed is associated closely with the country context. Also, different modalities have the scope for different domestic accountability influences, with projects and PFM transparency measures having large potential to increase the supply of accountability; however, here the focus will be the capacity for demanding accountability. Some literature points to a trade-off between accountability to donors and accountability to citizens; however, this literature takes a Northern or procedural approach to accountability (Tilley, 2011). Brautigam and Knack (2004) cite one country study that observed an increase in donor projects from 800 in 1989 to 2,000 in 2002; associated with this, they note the input from senior government officials required to facilitate such projects in the form of donor missions. In terms of accountability of policy, Gloppen and Rakner (2002) consider a more specific case where, based on the advice of the International Monetary Fund (IMF), donors have put pressure on governments to increase revenue collections. This can result in a situation whereby the government becomes accountable to donors for increased revenue collections, thus bypassing or even preventing the development of accountability with society.

This argument that aid crowds out domestic accountability rests on the assumption either that a social contract is in existence or that the conditions are in place for it to be developed. This assumption is made in a great deal of the accountability literature, yet it is frequently not examined thoroughly. Berry (1985) and Kelsall (2004) note that development in Africa is not yet associated with increased leisure and the growth of civil society – characteristics that are necessary for the development of a social contract. The constraints observed by Kelsall include demands of extended family; upward social status; and rural diversification both within and outside agriculture.

The assumption that collective action may emerge underlies the theories of state creation and rests on citizens accepting the limits to their individual actions in favour of collective representation (Daunton, 2001). However, in many developing countries, there is limited scope for effective collective action, given the plurality of different identities (Kelsall, 2004), the actions of the state to limit the influence of collective groups in some societies, such as in Tanzania (Tilley, 2011) and the limited independence and supply-driven nature of many organisations.¹⁰ Booth (2011) notes that non-governmental organisation (NGO) advocacy in most cases plays only a modest role in the monitoring of public policies. Drawing from the 2011 World Development Report (World Bank, 2011) and including political state legitimacy as a form of accountability allows for an understanding of patronage as a mechanism for

10 A detailed discussion of these influences for Tanzania can be found in Barkan (1994), Berg-Schlosser and Siegler (1990), Hyden (1994), Iliffe (1971), Kelsall (2004), Kelsall et al. (2005), Kiondo (1995), Pinkney (1997), Shivji (2006) and Sundet (2010). These are supported by general theory drawn from Hirschman (1970), Migdal (1988) and Sen (1999).

achieving accountability, and also highlights the lack of interaction between accountability to donors and domestic accountability.

Research projects that consider the interaction between recipient and donor influences include the ODI Africa Power and Politics Programme (APPP) and Institute of Development Studies (IDS) Centre for the Future State (CFS). Recent governance literature that focuses on the relational and argues for a movement away from an understanding of aid and development that is rooted in Western experience includes Booth (2011), Gulrajani (2010) and Unsworth (2010). Unsworth (2010) argues that the emerging, and increasingly mainstream, governance discourse has probed the edges of the pursuits of the international aid agenda with its indication of the importance of politics and questioning of what underlies formal institutions. However, its perceptions of rent seeking, clientelism and associated characteristics as 'pathologies' persist. Gulrajani (2010) critiques the dominant understanding of foreign aid for its implicit rationalist epistemology which assumes certain international best practices and standards and motivations of actors and agencies, and points to the need for a new approach that gives a greater weight to the relational.

Booth (2011: 13) acknowledges that the aid industry is politically led, directly in the case of bilateral agencies and indirectly in the case of multilaterals, and that the resulting incentives override the 'attitudes and the acquisition of skills' that would persist were these political incentives not dominant. Also, donors' inability to accept approaches to institutional reform that are not in line with their domestic democratic or market economy practices functions as a constraint, alongside their efforts to resist acknowledging the political component of aid and their risk adversity in relation to their own reputations. Booth proposes a re-education of politicians and the public in the North and a new understanding of development, beyond the provision of aid. He argues that country ownership needs to be reconsidered: it is not simply recipient country leadership of a reform plan, but rather the orientation of the political leadership.

ODI (2011b) supports this need for a new perspective, arguing that aid needs to be sold as a source of long-term institution building rather than as quick wins or an increased results focus. Kenny (2006) also notes this trade-off. The challenge of accommodating a longer-term perspective of aid within short-term political cycles remains.

4.2 Summary: to what extent does the activity duplicate what has already been examined and usefully explore a new set of issues?

There is a need for further research to consider the separation of political concerns from the disbursement of aid and how this varies among donors, as the foreign policy objectives of security and domestic investment highlighted above remain unreconciled with the rhetoric of aid. The literature does not cover the impact of these on aid allocations, disbursements and negotiations with recipient governments. However, this is a complex area, and the ODI APPP and IDS CFS research programmes have made solid progress in understanding underlying issues. In particular, the APPP is exploring issues around the relationship between rent seeking, development and public good provision. This research is related to the theories of change underlying the provision of aid; a possible area where value could be added is to directly relate this research to aid policies and modalities, along the lines suggested by Booth (2011).

A related area that remains uncovered is the factional nature of the elite, the extent of the competitive threat, the subsequent time horizons and the impact of the centralisation of power on economic reforms. Further research into this area could increase understanding of the areas of domestic policy reform that donors could support (Tilley, 2011).

5 Designing portfolios of complementary aid instruments

Donors frequently refer to the need to develop a portfolio of complementary interventions and aid instruments at the country level.¹¹ Some evidence suggests that certain aid modalities can have negative spill-over effects on other aid modalities (e.g. the existence of project aid alongside SBS can create additional transaction costs). Other research suggests that the full package of inputs (including dialogue, capacity development, TA) associated with SBS instruments is not sufficiently deployed (see Williamson and Dom, 2010a; 2010b; 2010c). The aim of the planned activity is to explore how donors, either individually at a country level or collectively at a programmatic/sector level, can design an aid portfolio that maximises the complementary effects of different aid modalities.

The work acknowledges the reality that for any given country or sector there will – almost unavoidably – be a portfolio of different aid instruments in use. It also takes note of the political realities that GBS is set to reduce as a share of donor aid and that some countries are constrained in their ability to work with country systems. Some formative work has already been completed to compare different aid instrument as delivery options for a given set of policy objectives.¹²

Output: Framework and evidence on portfolios of aid instruments

5.1 Key findings and main issues in the existing research

A number of studies point to the importance of considering the portfolio of aid allocated to a recipient country and drawing out the complementarities of different instruments. However, few studies consider the interplay between modalities in detail.

The GBS evaluation (IDD & Associates, 2006) stresses that donors should take a more strategic approach to developing complementarity between aid instruments. To achieve the aims of increasing domestic accountability, decentralisation and reducing corruption, GBS should be used alongside other instruments. For example, to achieve PFM improvements, the package of GBS inputs is needed (technical cooperation and policy dialogue in addition to the financial transfer). Furthermore, a portfolio of instruments is beneficial, as it allows donors to spread risk and can be mutually reinforcing, for example by having a specific sector focus alongside GBS.

Considering the complementary attributes of different aid modalities, GBS is found to coordinate, create forums for dialogue and make links across sectors for non-political cross-cutting issues (gender, HIV and AIDS, the environment) in Mozambique, Uganda and Vietnam (IDD & Associates, 2006). The GBS evaluation for Uganda observes that TA and capacity building are difficult to identify separately from budget support and recommends that the complementarity of aid instruments be maximised to build capacity. However, the Paris Partnership Principles do not assist in determining the most suitable combination of modalities by sector (Lister et al., 2006). In a discussion of the quality of partnership, a number of incentive effects operating around projects, SWAs and GBS in the health sector are highlighted. These include the difficulty of attributing results to GBS funds and loss of profile for donors, and how project funds circumvent medium-term expenditure framework (MTEF) ceilings, provide opportunities for personal gain through per diems and other allowances and allow for greater control of funds by middle managers (ibid.).

11 See reports from the ODI Budget Support meeting series 2011 www.odi.org.uk/events/details.asp?id=2647&title=budget-support#details.

12 See Highton et al. (2009) for a report on the options appraisal for DFID poverty reduction budget support to Malawi.

The DFID Key Sheet (DFID, 2003) on the choice of aid modalities lists criteria that need consideration to determine appropriate modalities, and points to the need to consider the blend of modalities in place. It highlights the importance of arrangements that are flexible and instrument 'blends' that allow for an evolution and an upgrading towards GBS. It also recognises the existence of a basket of donors with preferences for different modalities. The decision about which modalities to use should be based on:

- The degree of ownership of the PRS and involvement of the sub-national government in the planning process;
- The realism and consistency of the PRS with poverty reduction and the MDGs;
- The role of the state and the relationship between the state and the private sector such that private sector growth is encouraged and public goods are provided;
- Risks involved in moving towards GBS, such as fiduciary risk, the stability of the government and the likelihood of development outcomes;
- The momentum for donor harmonisation and other donors and government to ensure funding stability; and
- The degree to which donors can provide support without exerting an undue policy influence and how effectively development progress can be monitored.

Foster and Leavy (2001) and DFID (2008: 18) present decision trees for aid choices. Foster and Leavy analyse aid choices as a portfolio, presenting macro support or GBS as the starting point. In assessing the degree to which the conditions are in place to provide macro aid/GBS, they consider the role of complementary sector support, capacity building or TA. Conditions include whether policies have been agreed between donors and recipient governments, or the strength of the policy environment; the capacity of the recipient government to enforce fiduciary controls; the degree to which sector support can achieve additional benefits; and planning capacity at sector levels. This paper does not discuss variants of the instruments in depth and, being an early paper, does not discuss linking disbursements to results.

DFID's (2008: 18) decision tree considers only financial aid to governments and highlights agreement on policies as the starting point. It considers the scope for engagement in the context of the policy environment, central and sector-level planning and accounting capacity and the degree to which DFID can add value.

Highton et al. (2009) use cause and effect evaluation frameworks for GBS/SBS to assess the options for Malawi and the impact of switching aid instruments. Asking the question 'does GBS offer net benefits above and beyond alternative aid instruments?', the authors break down the outputs (Level 3 in the GBS evaluation methodology) to assess the costs and benefits of switching modalities. They consider the impact on policy dialogue, sectoral spending allocations, domestic debt, expenditure leakages from donor and government resources and transaction costs for donors and government.

Several papers (DFID, 2008; IDD & Associates, 2006; Roberts, 2003) consider the strengths and weaknesses of different instruments in relation to development objectives, highlighting how sector technical cooperation and dialogue can help to overcome the quality and equity deficit that has resulted from the expansion of services enabled by increased financing (through both GBS and SBS). DFID (2008: 13) considers the trade-off between instruments, cautioning that complementary off-budget projects risk being less transparent and reducing budget comprehensiveness and therefore reducing some of the gains of GBS. A table is presented that outlines each instrument's strengths and weaknesses in relation to specific development objectives. The paper poses some guidance on considering how financial aid instruments might be used together:

- Are the additional benefits worth the additional transactions costs involved?
- To what extent is sector financing a precondition for effective dialogue at the sector level?
- To what extent is sector financing a precondition for providing effective technical support to the sector?

- To what extent would sector financing from DFID encourage more upstream engagement by other donors in the sector?
- Are there other solutions available to lever effective engagement at the sector level that would add less transactions costs?

In developing a portfolio of aid instruments, it is necessary to consider i) the objective of the instrument in relation to capacity gaps and risk factors (such as weaknesses in budget execution that may be addressed through GBS); ii) the scale of funding to allow shifts away from other modalities and sustainable support; and iii) complementarity in the policy dialogue of different instruments.

A combination of SBS and GBS has the potential to encourage line and central ministries to work closer together, for example through supporting reform efforts at different levels; to achieve an improved balance between salary and non-salary expenditure and between primary and tertiary care; and to encourage other donors to move away from a focus on projects (DFID, 2008).

The Sector Budget Support in Practice (SBSiP) study, commissioned by the SPA, draws out the importance of approaching the use of aid modalities as a portfolio. While this study focuses on SBS, it also observes how different modalities interact and how the weaknesses of one can be compensated for by the strength of another. It examines SBS in 10 sectors in Mali, Mozambique, Rwanda, Tanzania, Uganda and Zambia. It considers how SBS can be used alongside GBS and what the supporting role for projects can be (Williamson and Dom, 2010a). While GBS is more appropriate for supporting cross-sector reforms, such as PFM or civil service reforms, it can be complemented by SBS enhancing the impact of these reforms at the sector level in service delivery.

Projects, in turn, can help to strengthen institutional capacity which enhances the effectiveness of SBS. The study notes that project aid should not be used for service delivery in a stable country environment. However, it considers cases where SBS has not addressed service delivery constraints and suggests that the complementary use of projects may have plugged these gaps. This 'missing middle' in service delivery is the gap where inputs should have transformed into quality service delivery outputs, through the 'capacities and systems needed for managing, supporting and supervising frontline service providers' such as school-level management (Williamson and Dom, 2010b: 2). To address this, the strengthening of institutions for service delivery is recommended as a core principle in designing and delivering SBS. This requires consideration of the ability of the government to address weaknesses in the strength of service delivery (upstream issues) and challenges to achieving high quality and equitable service delivery (downstream issues), including incentive-based human resource systems.

Indeed, the instances where SBS has not delivered on its potential are characterised by domestic political pressures that have a negative impact on service volume, access and quality. SBS has been found to reinforce such negative incentives as a result of the absence of a focus on service delivery or downstream issues (Williamson and Dom, 2010a). Many of the shortfalls are found to be related to weaknesses in cross-cutting issues, and insufficient cross-over between SBS and GBS programmes have failed to highlight this during programme delivery. Sector specialists in donor agencies are most comfortable working with their line ministries, and the economists who deal with GBS work with ministries of finance. The high turnover of staff in donor agencies limits their understanding of service delivery issues that are specific to the country and there is consequently a greater focus on policy and overall sector performance. On the recipient government side, sector specialists often have limited interaction with front-line service providers (ibid.).

As discussed above, aid modalities neither exist nor are chosen in abstract from politics or incentives. This is explored by Bandstein (2007) in a paper that attempts to understand the incentives that underlie the choice of aid modalities, and is part of a wider project: Aid Modalities – Relative Effectiveness and Complementarities. It proposes a conceptual framework for acknowledging how incentive structures impact upon decisions on aid modalities.

5.2 Summary: to what extent does the activity duplicate what has already been examined and usefully explore a new set of issues?

While there are no studies that explicitly provide a framework to assist donors in choosing a *portfolio* of aid instruments, a number of studies consider how different modalities interact and complement each other (DFID, 2008; IDD & Associates, 2006; Highton et al., 2009; Roberts, 2003). Some reports present decision trees to assist in the choice of instruments for each specific case (DFID; Foster and Leavy, 2001), and DFID presents the strengths and weaknesses of each instrument in relation to specific development objectives. It is suggested that these studies be used as a starting point for developing a framework for choosing a portfolio of instruments, as, while helpful for choosing instruments, there is a need to go further to explore the details of how instruments interact.

As most countries to which this framework will be applied are already recipients of aid, the starting point of a blank sheet should be avoided. There are costs and benefits involved in *changing* the mix of instruments, and it is these that should be assessed carefully in the design and application of any framework. A further complication to consider is the interactions of aid provided by different donors.

There are four ways to consider complementarity: between instruments; between donors; between sectors and central levels of government; and across countries. All of these aspects may have an implicit impact on the portfolio of instruments. While the context in each country will vary and will have an impact on how these elements interact, a generic framework could be developed which can then be adjusted to country nuances. For instance, decisions on aid portfolios may appear to be made independently on a donor-by-donor basis for a particular country, but the decisions of donors have an impact on each other through routes such as the absorption capacity of additional financing in sectors and capacity-building needs, domestic debt implications and the relative influence of different donors on policy dialogue. In determining country strategies, assumptions are made about the future behaviour of other donors, but in the development of support for a specific sector donors may work together explicitly to determine a portfolio of support. Williamson and Dom (2010c) suggest that a lack of systematic thinking and headquarter guidance is apparent in the design of SBS programmes, although they stress that programme design should emerge at the country level.

6 Comparing the fiduciary risks of different aid instruments

A major source of scepticism about budget support is the perception of fiduciary risk associated with its implementation. Past examples of corruption continue to haunt policymakers and are often mentioned in public debates about budget support. However, there has been little comparative research about the efficiency of budget support compared with other aid modalities. Outside budget support circles, there is limited discussion of the fiduciary risk and associated wastage from project aid (e.g. the risks that contractors are overpaid, staff and goods not priced competitively, services not used effectively). The purpose of this study is to measure the efficiency of budget support compared with other aid instruments, especially project aid. Using country case studies, the study will estimate and compare the unit costs of goods and services provided through different modalities (or systems).

The work will build on previous efforts at cost-benefit analysis of GBS in comparison with sector programmes and integrated projects.¹³ It will also use the taxonomy developed through other research (4.1) and contribute evidence to the study on portfolios of instruments (4.4).

Output: Case studies and synthesis report setting out data, conclusions and policy recommendations

Given limited resources it was decided to focus attention on the other five areas. Limited elements of this are captured in Section 7.

13 See Highton et al. (2009).

7 Designing better frameworks for aid delivery options

The purpose of this activity is to develop a new practical framework for designing aid modalities. It will take account of the principles of 'good aid delivery' and the types and degrees of associated risk. The output is intended to bring together findings and conclusion from the other studies under this work stream into an actionable toolkit for donor agencies and country officials.

The framework will cover:

- 1 The overarching objective of the aid instrument;
- 2 Good aid delivery principles, drawing on the original theory of change for using country systems (see Lawson and Booth, 2004) and more recent propositions on how aid contributes to development results over different time periods;¹⁴
- 3 Contextual risks facing donors and recipient countries;
- 4 Different features of aid instruments and parts of the aid delivery process; and
- 5 Different government systems and processes.

The framework will provide operational guidance for designing aid modalities which adhere to good aid delivery principles – particularly government ownership and strengthening country systems – while responding to donor risk management concerns. It will provide guidance on what parts of government systems and processes should be used given specific contexts (e.g. 2 and 3 above) and what features of aid modalities would enable this.

Output: Operational guidance on designing better aid instruments

7.1 Key findings and main issues in the existing research

The overall framework will account for four selected elements, each of which will be considered individually in terms of their coverage in the literature and factors that should be explored in the development of a framework.

The overarching objective of the aid instrument

The objectives of aid instruments can be interpreted through their policy focus, ranging from the aims of projects and TA to the policy and outcome monitoring framework that GBS or SBS supports. These may range from the macro (e.g. influence on growth, poverty reduction and economic policy) to the micro (operational features of different modalities) and embody a spectrum of different assumptions about how aid operates. The macro elements are considered here under the overarching objective of the aid instrument; the micro objectives are considered in the section below on good aid delivery principles.

Numerous studies have been undertaken considering the relationship between aid and growth. These can be grouped broadly into two schools: fiscal response and endogeneity literature. The fiscal response literature builds on the early aid/taxation studies, considering the impact of aid on key fiscal aggregates and therefore on tax revenue and in turn growth (Bacha, 1990; Chenery and Strout, 1966; Eshag, 1971; Kennedy and Thirlwall, 1971; Taylor, 1993; Thirlwall, 1999). The later fungibility literature allows for substitution between aid and tax revenue. The early fiscal response studies assume aid to be exogenous, whereas more recent works recognise the endogeneity of aid. Indeed, endogeneity, or selection bias in aid allocation based on factors such domestic revenue performance, are factors that are central to both the choice of aid instrument and those governing its operation (Bulir and Hamann, 2001; Ghura, 1998; Gupta et al., 2004; Odedokun, 2003).

¹⁴ See for example the new DFID Results Offers as part of the 2011 Bilateral Aid Review: <http://webarchive.nationalarchives.gov.uk/+http://www.dfid.gov.uk/news/speeches-and-articles/2011/bar-mar-oral-statement/>.

Highlighting the work of McGillivray (2003) and Doucouliagos and Paldam (2005), Kenny (2006) notes that aid effectiveness studies tend to find little or no significant link between aid flows and economic growth in general, but they do find a link if they narrow their parameters. This paper provides evidence and theory to counter the arguments that aid fosters economic growth by filling an investment gap, improving the quality of investment or improving policies.

The objective of the aid instrument must be considered in the context of assumptions about its effectiveness. The debate on the effectiveness of aid given the institutional context of the recipient country draws on a number of existing studies. To summarise, literature that argues that strong domestic institutions are required for programmatic aid to be effective includes Clemens et al. (2004), Dollar and Levine (2005), Doucouliagos and Paldam (2005) and Ruhashyankiko (2005) (in Kenny, 2006). Kenny focuses on programme and project aid and concludes that programme aid should be the instrument of choice for transferring financial resources in countries with strong domestic institutions and project aid should focus on transferring knowledge, piloting new approaches or supporting global public good provision.

Devarajan et al. (2001) consider the link between foreign aid and economic policy, measuring policy in terms of macroeconomic, structural, public sector management and social inclusion policies. By identifying the specifics of how and where aid has supported policy reform, it could be targeted more effectively. They find that, where bad policies are in place and aid prevents crises, aid sustains the bad policies. They also find that the composition of aid during the different stages of reform is crucial – TA and policy dialogue are most useful during the pre-reform period and finance (conditional loans) and policy dialogue during rapid reform; in the later reform stages, finance is important and conditionality is less useful.

Berg (2002) challenges the empirical finding of studies that conclude that aid has no effect on growth in countries with poor policy environments, pointing to a failure to examine inappropriate donor practices as often being an equal cause. As examples, he highlights poorly designed and badly supervised projects, inappropriate instruments and accounting requirements, a lack of coordination and the imposition of donors' own agendas. He notes that inappropriate diagnosis of problems has resulted in inappropriate reforms being proposed. He also argues that the emphasis on selectivity based on good policy environments, the move towards programme aid and the often resulting increase in donor intrusiveness is a symptom. He also stresses that a limited range of aid modalities is presented to address the problems, citing as an example the World Bank's focus on TA.

In the past decade, development theory has shifted from resting on the underlying assumption that inequality is an important driver of growth and development to one that brings political economy principles to the fore. There is now a recognition that inequality can lead to reduced income growth through encouraging rent seeking; threatening political stability; reducing the incentives of the rich to invest; underinvestment in the poor, notably in human capital; and population growth channels (Thorbecke, 2006).

This consideration of the literature highlights some of the principles required for good aid delivery and what the challenges may be for donors in applying such principles in practice. The micro objectives of aid instruments have adjusted to reflect changes in macro frameworks, and there has been an increased focus on good aid delivery principles, discussed below.

Good aid delivery principles: drawing on the original theory of change for using country systems¹⁵ and more recent propositions on how aid contributes to development results over different time periods¹⁶

The Paris Declaration on Aid Effectiveness (2005) identifies three general characteristics of effective aid: i) ownership of national development strategies and policies by recipient countries; ii) alignment of aid with recipient government policies and systems; and iii) harmonisation of aid between donors to reduce transaction costs. Alongside this, it points to the importance of mutual accountability and management for the delivery of results.

15 See Lawson and Booth (2004).

16 See for example the new DFID Results Offers (2011).

Easterly and Pfutze (2008) highlight the importance of aid agency transparency and routine independent evaluations, although limited consensus on how to conduct evaluations effectively remains a constraint.

Bourguignon and Sundberg (2008) identify two key features of a new model of aid: country ownership and aid allocation based on performance, as identified by indicators and within a general good policy environment and an environment of good governance. They note the movement towards placing these features at the centre of new models and cite the Country Policy and Institutional Assessment (CPIA) as an indicator. Berg (2002) discusses the limitations of using the CPIA as an aid allocation indicator, noting the high degree of clustering in the mid scores.

Considering the application of good principles from the perspective of a specific modality, the DAC guidelines for budget support highlight variability in the design of budget support instruments by discussing how to minimise transaction costs and volatility, enhancing predictability and the characteristics of conditionality. The discussion of SWAps distinguishes between these and traditional project approaches.

The theory of change underpinning GBS is based on the Paris Principles and assumes that, by empowering the partner government, political competition will move away from patronage to a focus on results; that the strengthening of government capacities and incentives will involve the application of pay and performance assessments; and that enhancing democratic accountabilities will allow domestic constituents to demand higher accountability. Except for one or two cases, the broad experience of countries that have experienced high levels of GBS for almost a decade does not support this theory of change. Instead, patronage politics persist, and there is little movement towards performance assessment and little effective demand for domestic accountability from civil society (ODI, 2011b: Booth). The discussion above on the political economy research stream highlights other literature that supports this argument.

Berg (2002) notes that only limited results may be achievable from changing the aid instrument, and suggests that a client-centred, rather than a donor-centred, approach should be developed. The difficulties of making such sweeping changes are recognised, and the risks that such a comprehensive change in approach would entail make its attainability uncertain. While not attempting to outline any specifics of a new aid system, Berg (2000) provides some ideas of what it might look like. He considers that donors' role in the poorest countries would change to one of helping to organise knowledge management, possibly along regional lines through regional institutions. Such a system would be more diverse, less intrusive, more regionally and nationally based.

Contextual risks facing donors and recipient countries, including various types and degrees of risk

The different sources and types of risk include risks related to different aid instrument, country context and variations in political economy, and by extension the underlying theory of change. These are discussed in turn. Bourguignon and Sundberg (2008) recognise a number of these challenges in aid allocation based on performance. They acknowledge the risks associated with time consistency, balancing allocations between good performance and greatest need, fragile states and fiduciary controls.

The variation of risk by *aid instrument* needs to be considered by each modality in turn, from the perspective of the portfolio of aid instruments and in terms of the transition from one instrument to another. GBS involves a greater degree of risk taking for donors and has been accompanied by high expectations of results, which, when not achieved, can result in disbursements being cut (ODI, 2011b: Molenaers). This in turn increases risks for recipients.¹⁷

Recent discussions around the new RBA modalities have considered the balance between GBS and RBA, with support to a portfolio approach. The interaction between the different modalities

¹⁷ This risk is discussed in relation to the political economy context below.

may increase the volatility of GBS and the risk for the recipient if it is the more flexible instrument, cushioning variations in disbursements made through other instruments.

The risk for donors is that there is a 'trade-off between a focus on results and the need for a general policy and political dialogue' as a movement towards RBA may reduce the scope for participation in dialogue (ODI, 2011a). Arguably, overall, RBA shifts the risk to recipients, as they have to bear a greater share of the performance and delivery risk (Rogerson, 2011). The risk for donors is reduced, as their accountability to their constituents is facilitated through the reporting mechanism and the direct linkage to results (Birdsall et al., 2010). However, the risk of wastage and misuse of funds remains (Rogerson, 2011), although the donor is automatically distanced from this in the design of the modality.

There is a risk that some initial funding may be required to achieve the results, although this may be overcome by a design feature that supports project implementation (Birdsall et al., 2010; Rogerson, 2011). The EC Communication on budget support (2011) approaches risk in a limited fashion, with only limited analysis. It points to a coordinated European approach to budget support, which raises questions as to whether this implies an increased risk for the recipient if donors respond in a coordinated fashion in their performance tranches.

The *country context* has two different interactions with risk: i) in terms of unanticipated economic or social events; and ii) in terms of the use of the appropriate modality for the country context.

The risk of unanticipated economic or social events is higher in fragile states. To address this, the use of different aid modalities, such as pooled funds, in the context of weak policy and governance contexts is proposed and discussed above.

The macroeconomic risk of 'Dutch disease' has been assessed in many papers on a country-by-country basis (World Bank, 2009a; Uganda: Adam and Bevan, 2002; Atingi-Ego, 2005; Nkusu, 2004; Zambia: Call and te Velde, 2007; cross-country papers include Adam and Bevan, 2006; Verbeke, 2007). DFID (2008) acknowledges this trade-off between an increase in fiscal space resulting from aid and the risk of exchange rate appreciation and a reduction in the competitiveness of the manufacturing sector. DFID presents clear approaches to the management of this risk, including a reduction in the volatility of aid, capacity development and macroeconomic advice provided alongside financial aid and directing additional aid spending to less inflationary areas and sectors. Implicit within this approach is the assumption that a full and accurate analysis of the macroeconomic characteristics of the country has been undertaken and that the government has the capacity to develop and implement policy accordingly. Addressing the political economy demands, as presented above, should be considered an integral part of this challenge.

There has recently been increased focus on the limitations of some modalities in terms of their application to certain environments. For instance, the increased focus on fragile states has led to a discussion of the higher risks involved with the use of GBS in this context (ODI, 2011) and how implementation procedures can be adjusted.

The EU's adherence to the underlying principles of GBS which 'must be based on [...] commitment to fundamental values of human rights, democracy and the rule of law' has been strengthened (EC, 2011: 3). This has the potential to increase the risk of GBS for recipient countries as it indicates a movement away from developing an understanding of the *political economy context* of the recipient country. Indeed, the movement to RBA provides a method of sidestepping political economy constraints and challenges, yet this may also result in donors being less engaged in government systems, as discussed further below.

In terms of the appropriate modality being applied with respect to the country context, to mitigate the risk of corruption, support to PFM reform has often been included in the GBS basket of support. Progress in PFM reform and PFM assessments has been viewed as key to the efficiency of GBS programmes. A reduction in corruption can be viewed as implicit in the theory of change underlying GBS, as accountability is strengthened and public sector incentives and capacities are enhanced. However, this is indirectly critiqued by some political

economy literature that illustrates the operation of other incentives that result in little increase in domestic accountability and the persistence of corruption in some countries.

Related to this, recent years have seen an increased focus on accountability as a mechanism to mitigate risk, with its explicit incorporation in PAFs and projects to enhance the capacity of parliaments and civil society. This approach is based on the traditional or Northern model of accountability comprising horizontal and vertical components and based on agencies of restraint and parliamentary democracy (Collier, 1999; O'Donnell, 1999).¹⁸ This model excludes patronage, yet patronage should be included in the view of accountability (World Bank, 2011). Accountability requires citizen–state relations, and in the state legitimacy perspective this functions through patronage, but in the narrower perspective the absence of a Western social contract is problematic.

Different features of aid modalities and parts of the delivery process¹⁹ and different government systems and processes

The use of GBS and SBS has encouraged the channelling of aid through government systems. While this has not automatically improved the functioning of government systems, it has increased donors' awareness of areas in need of capacity development, and this has been a focus of complementary support, partly as a risk mitigation strategy (e.g. EU budget support that includes support to PFM systems).

Studies have highlighted the advantages of donors using government systems and the problems that arise with parallel systems. The latter include high transaction costs and low predictability and implementation rates, with an opportunity cost in terms of the quality and sustainability of outputs produced (World Bank, 2009b). Harmonising with recipient country systems has the advantage of enhancing the efficiency of domestic resource allocation and improving PFM systems and good practices (Mokoro and ODI, 2009).

The OECD notes there is no minimum threshold for the benefits of using partner country PFM systems to materialise, as long as partner governments are clearly committed to improving the quality of these. The scale of benefits from moving to using government systems depends on the share of aid using country systems, how predictable it is and the extent of any modifications required to meet special donor requirements (OECD, 2010). The study uses the example of Mozambique to explore the different degrees of use of country systems by sector project aid.

In donors' consideration of the degree to which recipient country systems are to be used, their assessment of risk and mitigation strategies is important, and should be weighed up against the potential benefits. If the rise of RBA reduces the use of GBS, then this is likely to reduce donors' engagement with government systems, particularly as it is likely to be directed towards more risky environments with weaker government systems. In this context, it will be particularly important to retain an emphasis on the capacity of government systems.

7.2 Summary: to what extent does the activity duplicate what has already been examined and usefully explore a new set of issues?

As this outcome develops an applied tool, rather than undertaking further research, the conclusion here is based on considering areas of weakness in the existing literature and on an exploration of the dominant approach to aid delivery and the political economy to see how such a tool would be received.

18 Horizontal accountability is the capacity of agencies of restraint (law courts, ombudspersons, audit offices, electoral tribunals, central banks, the media, trade unions, lawyers' guilds) to ensure other branches of government are answerable for their actions, that is, restraints imposed by institutions of equal status on each other. Vertical accountability refers to the state–citizen relationship, or the relationship between unequals, and the holding to account of public officials through actions of democracy such as elections, civil society and the media or 'making elected officials answerable to the ballot box' (O'Donnell, 1999: 61).

19 Developed in Outcome 1.

No such tool was found in the existing literature. While there is scope for developing a framework, the methods of allocating aid are influenced either directly or indirectly by politics, and there is therefore a concern that such a framework could not be fully applied.²⁰ Furthermore, the details of such a framework would be influenced directly by the conclusions emerging from the other areas of research proposed. In turn, its application by aid practitioners would be heavily dependent on support to the findings of these outcomes.

In view of this, useful preliminary work could be undertaken to examine current aid allocation methods, both globally and by modality. For instance, what factors feed into GBS allocation decisions and, in turn, how does this influence the overall aid portfolio on a country-by-country basis and overall? An example that could be explored and extended is that the case that donor agency staff have to make for GBS to be provided can depend on a balance of the likely benefits and the partnership environment; for instance, if the benefits are low, then a stronger partnership environment is required to mitigate the risk. Literature that considers aid allocation includes Clist et al. (2011), DFID (2003) and Foster and Leavy (2001).

This preliminary work could help to identify factors that should be included in the framework for designing aid modalities. Further background work could include how perceptions of risk influence the provision of aid and donor-recipient relations; the different risk management strategies donors use; and how different combinations of aid instruments produce different results according to the country context.

There is little detailed exploration of variations in delivery methods. Indeed, a portfolio approach to delivering aid should identify good practices and consider ways in which aid instruments interact to have an impact on the achievement of the principles, as discussed above. This would present a more nuanced understanding of how applying the principles in reality may produce results that are less than ideal.

Other factors that are likely to increasingly change the aid environment and should therefore be included in a forward-looking framework are the rise of new donors; new financing methods that blend aid and private finance; hydrocarbon reserves that are discovered and change the context for accountability relationships; and new policy focuses such as climate change and changes in risks as global security concerns increase. Uncertainties include a potential increasing interdependence between aid and other cross-border flows such as FDI, trade and remittances.

The increased availability of foreign aid and investment by non-OECD donors has the potential to have an impact on the response of the government to OECD donors, and therefore in turn it may have an effect on the behaviour of donors. To further examine the implications of this research for policy and the effectiveness of aid modalities, a closer comparison of the strategies of individual donors could be made.

²⁰ See the discussion in the political economy research stream.

8 Conclusion

In order to prioritise the research activities under the work stream of 'better aid modalities', ODI carried out a literature review and held a consultation with a group of experts. The conclusions from this are laid out below.

First, developing a revised and up-to-date taxonomy of aid instruments and their specific features is a useful first building block for a work stream on aid instruments. No recent taxonomies have been developed, and yet aid instruments continue to morph and hybrid types develop. Such types are often being implemented in an attempt to better manage and mitigate a range of risks facing development practitioners. Given this, developing a revised taxonomy to outline clearly the distinguishing features of different instruments will be the first activity for this work stream.

Second, improving the bulk of knowledge on recipient country views on aid instruments and how they can be most effective is crucial. This is because there is a growing consensus on the importance of delivering results and an appreciation that some aid instruments have not sufficiently addressed service delivery blockages. In addition, much of the analysis of aid instruments is often framed from a donor perspective, and it is crucial to improve the knowledge base on recipient country perspectives and that of those officials working most closely with service delivery systems in developing countries. This will be the second activity of the work stream. However, the planned research piece will vary from that described in the proposal above in two main ways. First, rather than primarily trying to find out which features of aid instruments development recipient officials prefer, the overall research question will be 'what features of aid delivery do development practitioners feel best facilitate service delivery results'. This focuses the question on features that best facilitate service delivery, which not only talks to the MDG agenda but also allows for a more manageable research scope. Second, the study will be based on a case study methodology, rather than a perceptions survey, as it is felt that the former approach would be best suited to addressing the overall research question.

Third, understanding and analysing political economy issues will be incorporated (as best as possible) in all the research pieces, as these are key factors in the effective implementation of any aid instrument. A standalone piece will be drafted, but may go beyond just budget support operations (the theme of the meeting series on budget support) and explore other aid instruments. This will be carried out in the near future.

Fourth, there appears to be a large knowledge gap regarding designing portfolios of complementary aid instruments. The taxonomy and work on recipient country views will include portfolios or at least complementary aid instruments. In addition, it would be useful to develop a conceptual piece on optimal aid portfolios, from the perspectives of recipient countries and donor organisations.

Fifth, the literature review did not explore the evidence on comparing the fiduciary risks of different aid instruments.

Finally, the ultimate objective for this work stream is to design better frameworks for aid delivery. Once the taxonomy and recipient country view pieces are completed, the findings will feed into this research area, which will then be explored in greater depth. The ultimate objective will be to provide evidence-based policy advice on options donors and recipient governments can pursue when designing and implementing aid instruments. Essentially, the framework will aim to lay out the range of aid features which should best address country specific risks, while delivering on results.

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