

Do donors practice what they preach?

The allocation of budget support by OECD-DAC donors

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Budget support increases developing countries' ownership of development programs but reduces the ability of donors to monitor and control aid flows. In this context, decisions about which countries are eligible for budget support, and how much budget support they should receive, take on particular significance. This paper examines the extent to which members of the OECD Development Assistance Committee (DAC) comply with their own policies on the allocation of budget support. Using a new quantitative data set and qualitative evidence from Zambia and Uganda, it seeks to answer two related questions. First, what factors shape bilateral donors' decisions about whether or not to provide budget support to a particular developing country? Second, what factors shape their decisions about how much budget support should be given once a country has been categorised as eligible for this type of aid? This helps to fill a gap in existing research, which to date has focused on the allocation of budget support by multilateral donors. The results indicate that bilateral donors are generally compliant with their policies on the allocation of budget support. However several additional factors influence the allocation of budget support as well, including certain characteristics of the donor. There also appears to be a substantial amount of bureaucratic inertia in budget support allocations, which are strongly influenced by allocations in the previous year. In light of doubts expressed about the effectiveness of budget support in promoting good governance, this begs the question of whether the problem is the modality, or the manner in which it is allocated by donors.

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Budget support became a prominent part of the international community's efforts to make aid more effective in the 1990s and 2000s. This form of aid is commonly defined as aid that is channelled directly to recipient countries' national treasury, becoming subject to their budgetary procedures. Although the total proportion of aid disbursed as budget support has never been overwhelming, it has become particularly important for some donors and for some aid recipients. In 2010 EU institutions disbursed around 18.4% of their official development assistance (ODA) as budget support and the UK, 11.6%, while Ghana received almost half its aid as budget support¹. The growth in budget support was driven by widely held expectations that this new aid modality would generate a range of benefits. These include increased accountability to the citizens of developing countries, greater host-country ownership of development programs and reduced fragmentation of aid flows². Yet these high hopes for budget support have been balanced against a number of risks, some of which have slowly eroded donor's enthusiasm for using budget support. Most notably, budget support gives recipient countries greater ownership of aid, but reduces the ability of donors to monitor and control how aid funds are used. Thus budget support trades off an expected increase in accountability to the citizens of developing countries, against a potential decrease in accountability to the citizens of donor countries. This has led to a recognition that budget support is a type of aid that combines high risks with (potentially) high returns³. In this context, donors' decisions about which countries are eligible for budget support, and how much of their aid should be delivered via this aid modality, take on particular significance. This has become even more true in the last few years as enthusiasm for budget support has declined and donors' use of budget support, particularly general budget support, has tended to become even more selective⁴.

In light of the importance of selecting the 'right' countries in which to employ budget support,

- 1 Calculations based on the OECD's International Development Statistics.
- 2 Stefan Koeberle and Zoran Stavreski, "Budget Support: Concepts and Issues," in *Budget Support as More Effective Aid? Recent Experiences and Emerging Lessons*, ed. Stefan Koeberle, Jan Walliser, and Zoran Stavreski (Washington D.C.: World Bank Publications, 2006), 3–26.
- 3 African Development Bank Group and World Bank, "Providing Budget Aid In Situations Of Fragility: A World Bank - African Development Bank Common Approach Paper," December 2010, <http://www.afdb.org/fileadmin/uploads/afdb/Documents/Project-and-Operations/CAP%20Budget%20Aid%20in%20Fragile%20Situations%20English.pdf>.
- 4 While many donors remain committed to using budget support on paper, donor officials interviewed in Zambia and Uganda in 2013 consistently reported declining enthusiasm for budget support and frequently observed a shift away from general budget support in favour of sectoral budget support.

donors have developed a range of policies which provide guidance on its allocation. Though not identical, these policies, particularly those of OECD-DAC members, are broadly similar. They tend to focus on good governance, particularly the quality of public financial management systems⁵, and pro-poor policies as the criteria that should guide the allocation of budget support. A case in point is Norway's aid agency, Norad, which makes the provision of budget support contingent on an assessment of the quality of recipients' national development strategies, including the government's capacity to implement them and the extent to which those strategies focus on poverty reduction and equity⁶. The Canadian International Development Agency (CIDA), now part of the Department of Foreign Affairs and International Trade, takes a similar approach. Its policy states a desire to employ program-based approaches (which include budget support) "where the basic pre-conditions and opportunities exist for their effective use."⁷ These basic preconditions include recipients' capacity and track record in implementation, and the existence of effective monitoring and reporting mechanisms. On paper, concerns about political freedoms are largely a secondary factor when it comes to policies on the allocation of budget support. The policy of the UK's Department for International Development (DFID) is illustrative, stating that in relation to budget support it "will not require partner countries to meet a minimum standard of domestic accountability; rather we will be looking for commitment to strengthen domestic accountability."⁸ Similarly, CIDA looks for "positive trends in government transparency, accountability, enforcement of the rule of law, promotion of human rights and inclusive political participation."⁹ Norad expects assessments of potential budget support recipients to address issues of human rights, and whether conditions for free and fair elections are in place. However these do not appear to be hard requirements: budget support may still be provided where the political leadership has "broad public legitimacy and there is participation in decision-making processes."¹⁰

5 See David Shand, "Managing Fiduciary Issues in Budget Support Operations," in *Budget Support as More Effective Aid? Recent Experiences and Emerging Lessons*, ed. Stefan Koeberle, Jan Walliser, and Zoran Stavreski (Washington D.C.: World Bank Publications, 2006), 27–44.

6 NORAD, "Norway's Provision of Budget Support to Developing Countries: Guidelines" (Norwegian Ministry of Foreign Affairs, 2007), 9.

7 CIDA, "Policy on Program-Based Approaches" (Government of Canada, 2009), 4.

8 DFID, "Implementing DFID's Strengthened Approach to Budget Support: Technical Note," July 8, 2011, 2, <http://www.dfid.gov.uk/Documents/Strengthened-approach-budget-support-Technical-Note.pdf>.

9 CIDA, "Policy on Program-Based Approaches," 4.

10 NORAD, "Norway's Provision of Budget Support to Developing Countries: Guidelines," 11.

This paper adds to existing research by seeking to determine the extent to which bilateral members of the OECD-DAC comply with their own policies on the allocation of budget support. It aims to answer two related questions. First, what factors shape donor decisions about whether or not to provide budget support to a particular developing country? Second, what factors shape donor decisions about how much budget support should be given? In focusing on the allocation of budget support by bilateral donors (that is, individual countries), this paper helps to fill a gap in existing research, which to date has focused on the allocation of budget support by multilateral donors such as the EU and World Bank.

In order to answer these questions, this paper employs a mixed method approach. It begins with quantitative analysis using an original data set. This data set has been built around data on budget support allocations which has only recently become available via the OECD's International Development Statistics. Given the limited nature of this data set – which at present only captures general budget support allocations in 2010 and 2011 – the results of the quantitative analysis must be interpreted with some caution. In order to reinforce the robustness of the analysis, and to unpack some of the variables which appear to be significant, this paper also draws on qualitative evidence. This evidence takes the form of semi-structured interviews conducted with donor officials based in Zambia and Uganda in the second half of 2013 and early 2014¹¹.

The results of the quantitative analysis suggest that donors are generally compliant with their policies on the allocation of budget support, though several caveats are in order. In line with donor policies, pro-poor policies and good governance appear to attract budget support. However, the results relating to these variables are dependent on model specification. Several other factors which are not generally mentioned in donor policies on budget support also appear to be influential. Poorer countries are more likely to get budget support, and tend to get

11 This paper draws on 14 'core' interviews conducted with officials at bilateral donor organizations who either currently provide budget support, or who have provided budget support in the recent past. These interviews were conducted in Zambia in October and November 2013, and in Uganda between November 2013 and February 2014. Additional interviews were conducted with multilateral donors (the World Bank, African Development Bank and EU Delegations), and with bilateral donors who do not currently provide budget support to Zambia and/or Uganda.

more of it. In addition, the nature of the relationship between donor and recipient plays an important role in donor decisions about budget support. Donors are more likely to give budget support to recipients for whom they are major donors, with whom they trade more, and with whom they have a colonial tie. This suggests that self-interest plays an important role in a donor's choice of aid modality. Perhaps more worryingly, it also appears that donors are willing to overlook a state's failure to respect civil liberties when deciding whether or not they are eligible for budget support. Finally, the quantitative analysis suggests that there is a substantial degree of bureaucratic inertia in donors' decisions about budget support. Donors' decisions about whether or not to use budget support in a particular country, and to a lesser extent their decisions about how much aid to allocate as budget support, are strongly influenced by whether budget support was provided (and how much was provided) in the previous year.

The qualitative evidence generally supports the quantitative evidence, adding weight to the conclusion that pro-poor policies and good governance tend to attract budget support. The qualitative evidence also allows us to unpack the concept of 'bureaucratic inertia.' It suggests that donors' apparent unresponsiveness to changing circumstances is not simply the product of bureaucratic red tape, but rather masks the role of several different factors. These include concerns about maintaining good relationships with recipient governments and a genuine desire to be a 'good' donor who respects its international and bilateral commitments. The qualitative evidence also reveals a number of shortcomings in the statistical models. It highlights the role of several omitted variables, including the strength of public support for development aid in donor countries, the financial position of donors and the extent to which domestic (donor) media provides coverage of events such as corruption scandals or breaches of human rights which occur in recipient countries. Interviews also suggest a substantial degree of interdependence between donors' decisions about budget support, undermining one of the assumptions that underpins the statistical techniques employed in this paper. Ideally, the statistical models would be updated to remedy these shortcomings. While the difficulty of obtaining appropriate indicators has prevented this for the purposes of this paper¹², it is

12 For example, while various public opinion surveys provide measures of public support for development aid the coverage of this data is patchy. Including these indicators in the analysis would, as a result, drastically reduce the number of observations included in the quantitative analysis.

hoped that these shortcomings can be addressed in the future.

Section 1 of this paper provides a review of existing research on aid allocation generally, and budget support in particular. In section 2, this paper sets out the design of the quantitative component of the analysis, explaining how key variables will be measured. Section 3 presents and interprets the quantitative results drawing on some of the qualitative interviews to aid in interpretation. Section 4 delves into the qualitative evidence in more depth to unpack the concert of bureaucratic inertia and identify some potential short-comings in the statistical models. Section 5 concludes by examining the implications of this paper's findings.

1 Existing research

Two related bodies of research inform this paper. The first examines the determinants of aid allocation generally, while the second focusses more specifically on the factors that influence donors' choice of aid modality, and budget support in particular. Broadly speaking, these two bodies of research suggest that a combination of interests, institutions and ideals influence donors' choices about the allocation of aid. They also reveal a divergence between the determinants of bilateral and multilateral aid allocations and raise questions about whether aid allocation has become more selective over time.

Alesina and Dollar provide the foundation of the literature on aid allocation¹³. Using an analysis of bilateral aid flows between 1970 and 1994, they argued that aid allocations are primarily the result of political and strategic considerations, rather than a response to institutional factors, such as good policies and control of corruption, that might make aid more effective. In particular, they find that past colonial ties and the similarity of a recipient's UN voting behaviour to that of the donor are associated with more substantial increases in aid allocations than measures of poverty, democracy or policy priorities in developing countries. Subsequent research has also highlighted the fact that donors do not always stand on principle when it comes to aid allocation. This is particularly true with respect to corruption, with Alesina and Weder finding no evidence that bilateral and multilateral donors systematically

13 Alberto Alesina and David Dollar, "Who Gives Foreign Aid to Whom and Why?," *Journal of Economic Growth* 5, no. 1 (2000): 33–63.

reward less corrupt governments with more aid¹⁴. In fact, they find that certain donors, most notably the United States, tend to give more aid to more corrupt governments.

The impact of democracy and human rights on aid allocation has proved difficult to pin down, particularly with respect to the decisions of bilateral donors. While concluding that political and strategic factors were the primary drivers of cross-country variation, Alesina and Dollar also reported that democracy played a role at the margins, helping to explain variation in bilateral aid allocation to a given country over time¹⁵. They observed that countries which democratise tend to receive an immediate surge in bilateral aid, stating that "the typical democratizing country gets a 50% increase in aid."¹⁶ Yet this result has not been consistently reproduced by subsequent studies. Using data on bilateral aid between 1980 and 1999, Berthélemy and Tichit find such a strong relationship between aid allocations and political rights and civil liberties that they suggest "the best way for a developing country to obtain better assistance from the donor community is to adopt democratic institutions."¹⁷ However, they note that the impact recipients' democratic credentials on aid allocations varies with the identity of the donor. Demirel-Pegg and Moskowitz would qualify this finding further¹⁸. They argue that the impact of human rights on US aid allocation is dependent both on the level of democracy, and on the level of economic development in recipient countries. Neumayer analyses the impact of human rights on the aid allocations of 21 bilateral donors between 1985 and 1997¹⁹. In contrast to Berthélemy and Tichit, he finds that while respect for civil and political rights influences donor decisions about eligibility (i.e. whether to give aid or not), it does not appear to consistently influence the amount of aid allocated once a country has passed the eligibility phase.

These inconsistent results may in part be the product of a failure to distinguish between the

14 Alberto Alesina and Beatrice Weder, "Do Corrupt Governments Receive Less Foreign Aid?," *The American Economic Review* 92, no. 4 (2002): 1126–1137.

15 Alesina and Dollar, "Who Gives Foreign Aid to Whom and Why?"

16 *Ibid.*, 34.

17 Jean-Claude Berthélemy and Ariane Tichit, "Bilateral Donors' Aid Allocation Decisions—a Three-dimensional Panel Analysis," *International Review of Economics & Finance* 13, no. 3 (2004): 263, doi:10.1016/j.iref.2003.11.004.

18 Tijen Demirel-Pegg and James Moskowitz, "US Aid Allocation: The Nexus of Human Rights, Democracy, and Development," *Journal of Peace Research* 46, no. 2 (2009): 181–198, doi:10.1177/0022343308100714.

19 Eric Neumayer, "Do Human Rights Matter in Bilateral Aid Allocation? A Quantitative Analysis of 21 Donor Countries," *Social Science Quarterly* 84, no. 3 (2003): 650–666, doi:10.1111/1540-6237.8403010.

impact of *levels* of democracy and respect for human rights on aid allocation, and the impact of *changes* in democracy and respect for human rights. As Lebovic and Voeten point out, donors are more likely to respond to large and prominent abuses of human rights²⁰. They find that the adoption of a United Nations Commission of Human Rights (UNCHR) resolution condemning human rights violations in a country leads to a significant and sizeable reduction in multilateral aid (especially World Bank aid) to that country, but no reduction in bilateral aid. Carey employs similar reasoning, criticising prior work on human rights and aid allocation for failing to take into account the possibility of bureaucratic inertia (that is, the fact that which countries have received aid in the past, and how much aid they have received, is likely to affect future aid allocations) and the possibility that changes in respect for human rights are more influential than absolute levels²¹. Drawing on data on European aid allocations between 1978 and 2003, and controlling for prior patterns of aid allocation, Carey finds that human rights issues do not consistently influence aid allocation at the bilateral level. She reports that Germany is the only country to consistently allocate less aid to more repressive countries, while only Germany and France consistently respond to improvements in human rights when deciding who is eligible for aid. In line with Lebovic and Voeten's finding that the World Bank is more responsive to human rights scandals²², Carey also finds that human rights improvements have a positive and significant influence on the European Commission's (EC) allocation of aid.

One contentious point in the literature on aid allocation is whether or not the factors which influence aid allocations have shifted over time. There is debate about whether aid has become more selective, that is, whether donors have become more responsive to good policies and good political institutions; the factors thought to make aid more effective. Berthélemy and Tichit suggest that the importance of colonial ties has faded over time²³. Comparing aid allocations in the 1980s to the 1990s, they conclude that bilateral donors have become more prone to direct aid towards important trading partners and countries with successful economic

20 James H. Lebovic and Erik Voeten, "The Cost of Shame: International Organizations and Foreign Aid in the Punishing of Human Rights Violators," *Journal of Peace Research* 46, no. 1 (2009): 79–97, doi:10.1177/0022343308098405.

21 Sabine C. Carey, "European Aid: Human Rights Versus Bureaucratic Inertia?," *Journal of Peace Research* 44, no. 4 (2007): 447–464, doi:10.1177/0022343307078938.

22 Lebovic and Voeten, "The Cost of Shame."

23 Berthélemy and Tichit, "Aid Allocations and Development Financing."

policies. Dollar and Levin also argue that aid allocation has become more selective with respect to the rule of law²⁴. Their results indicate that the rule of law had a significant but negative effect on aid allocations from 1984 to 1989, but that between 2000 and 2003 this relationship was positive. However, like both Carey²⁵ and Lebovic and Voeten²⁶, they highlight a divergence between the behaviour of multilateral donors and bilateral donors: the effect of the rule of law on aid allocation was only statistically significant with respect to multilateral donors, such as the EC and World Bank. Clist also addresses the question of whether the determinants of aid allocation have shifted over time, relying on a dataset covering 7 major bilateral donors²⁷. His results suggest that aid allocation has become more strongly influenced by poverty over time: more needy countries are now more likely to get more aid. However, Clist concludes that aid allocations have not become more selective on other grounds, and in particular, notes that bilateral donors have not become more responsive to human rights. Nunnenkamp and Thiele²⁸ as well as Easterly²⁹ also reject claims that aid allocation has become more selective.

Research examining donors' choice of aid modality has only emerged relatively recently. It reflects a realisation that "donor allocation is not a two-stage decision of who gets aid and how much but a three-stage decision that also considers what type of aid should be given."³⁰ Within this body of research, there are very few studies which specifically examine the allocation of budget support. However, there are a number of studies which examine the use of programmatic aid modalities, which include budget support. Winters provides one example³¹. He examines the choice of project-based versus programmatic modality by the

24 David Dollar and Victoria Levin, "The Increasing Selectivity of Foreign Aid, 1984–2003," *World Development* 34, no. 12 (2006): 2034–2046, doi:10.1016/j.worlddev.2006.06.002.

25 Carey, "European Aid."

26 Lebovic and Voeten, "The Cost of Shame."

27 Paul Clist, *25 Years of Aid Allocation Practice: Comparing Donors Eras*, Working Paper (University of Nottingham: CREDIT, 2009), <http://www.nottingham.ac.uk/credit/documents/papers/09-11.pdf>.

28 Peter Nunnenkamp and Rainer Thiele, "Targeting Aid to the Needy and Deserving: Nothing But Promises?," *World Economy* 29, no. 9 (2006): 1177–1201, doi:10.1111/j.1467-9701.2006.00836.x.

29 William Easterly, "Are Aid Agencies Improving?," *Economic Policy* 22, no. 52 (2007): 633–678, doi:10.1111/j.1468-0327.2007.00187.x.

30 Paul Clist, Alessia Isopi, and Oliver Morrissey, "Selectivity on Aid Modality: Determinants of Budget Support from Multilateral Donors," *The Review of International Organizations* 7, no. 3 (2012): 268, doi:10.1007/s11558-011-9137-2.

31 Matthew S. Winters, "Choosing to Target: What Types of Countries Get Different Types of World Bank Projects," *World Politics* 62, no. 3 (2010): 422–458.

World Bank's two lending arms, the International Development Association (IDA) and the International Bank for Reconstruction and Development (IBRD), between 1996 and 2002. Winters finds that well governed countries (i.e. those that score highly on the Worldwide Governance Indicators (WGI)) get less programmatic aid from the IDA, but more programmatic lending from the IBRD. He finds this ironic, as the IDA has a mandate to focus on development, but suggests that the result may reflect the IDA's greater susceptibility to bilateral donor pressure. Winters does not find any relationship between civil and political rights and the use of programmatic aid, but does find some evidence that democracy (measured using PolityIV data) has a small, but significant, positive effect on the use of programmatic aid.

Dietrich's analysis of donor's choice of delivery channel also sheds some light on the variables which may influence the allocation of budget support³². She argues that poor levels of governance in recipient countries lead donors to bypass those governments, rather than to reduce total aid allocations. They do this by using implementation channels such as non-government organizations (NGOs) and private sector partnerships, which allow projects and programs to be delivered without funds passing through the hands of developing country governments. Like Winters³³, Dietrich measures good governance using the WGIs and reports a negative and statistically significant relationship between a country's governance scores and the amount of aid which donors deliver through bypass mechanisms. While Dietrich does not address the allocation of budget support directly, but given that budget support represents the very opposite of bypassing recipient governments, her findings imply that donors are unlikely to give budget support to countries with poor records on governance.

Knack examines when donors use recipients' public financial management (PFM) systems³⁴. While this is not exactly the same as budget support, Knack refers to additional, unreported analyses, and notes that his "results in general hold for... use of direct budget support."³⁵

32 Simone Dietrich, "Bypass or Engage? Explaining Donor Delivery Tactics in Foreign Aid Allocation," *International Studies Quarterly* 57, no. 4 (2013): 698–712, doi:10.1111/isqu.12041.

33 Winters, "Choosing to Target."

34 Stephen Knack, *When Do Donors Trust Recipient Country Systems?*, Policy Research Working Paper (World Bank, 2012), <http://ideas.repec.org/p/wbk/wbrwps/6019.html>.

35 *Ibid.*, 4.

Knack argues that the use of recipients PFM systems depends on their perceived trustworthiness. This is measured using two indicators: control of corruption (from the WGIs) and Freedom House's civil liberties indicator (a supplementary indicator of trustworthiness, which Knack argues provides a measure of transparency and accountability). Both have a positive and significant effect on donors' use of recipient PFM systems. Knack also finds that multilateral donors use recipients' PFM systems more than bilateral donor; donors are more likely to use recipient PFM systems when there is popular support for aid at home; and donors are more likely to use them when they provide a greater share of aid to a particular country. In a later paper that employs a similar approach, but which uses different indicators of the quality of host country systems, Knack again finds a positive relationship between the of use host country systems and the quality of those systems³⁶.

Clist, Isopi and Morrissey provide one of the only articles to expressly focus on the allocation of budget support³⁷. They argue that multilateral donors are more likely to provide budget support to recipient countries with greater government efficiency and pro-poor policies that align with those of donors. They test this using data on EC and World Bank budget support in the period between 1997 and 2009 using a probit analysis to model eligibility for budget support and OLS to model donors' decisions about how much aid to give as budget support. Government effectiveness is measured using the relevant indicator from the WGIs. The extent to which a potential recipient has adopted pro-poor policies is measured using two variables; whether they have published a Poverty Reduction Strategy Paper (PRSP) or an interim PRSP³⁸, and the level of public spending on education as a percentage of GDP. Both the existence of a PRSP, and government effectiveness, had a positive and statistically significant effect on the probability that a developing country would be categorised as eligible to receive budget support from both the EC and the World Bank. Clist et al also found that both donors were more likely to give budget support to recipients that were more important to them (i.e. to whom they gave a greater percentage of their total aid budget), while the World Bank was

36 Stephen Knack, *Building or Bypassing Recipient Country Systems: Are Donors Defying the Paris Declaration?*, Policy Research Working Paper (Washington D.C.: World Bank, 2013), <http://papers.ssrn.com/abstract=2255888>.

37 Clist, Isopi, and Morrissey, "Selectivity on Aid Modality."

38 As noted by Clist et al., PRSPs were initially used as a criteria for eligibility for debt relief under the Highly Indebted Poor Countries initiative, but are now widely used by developing countries to set out their national development strategy.

more likely to give budget support to more aid dependent countries. In the models of donors' decisions about how much aid to give as budget support, most variables of interest (particularly the measures of PRSPs and government effectiveness) lost statistical significance. This may have been due to the much smaller sample size in this stage of the analysis, which examined only those cases in which recipients had first been deemed eligible for budget support.

Existing research on budget support suffers from a number of limitations, largely due to the dearth of reliable data on budget support allocations. While budget support emerged as an important form of aid in the late 1990s and early 2000s, data on its allocation has only been systematically reported to the OECD-DAC from 2010 onwards. As a result, researchers have focussed on the allocation of budget support by multilateral donors, such as the EC and World Bank, for whom data was easier to obtain. Yet, given that research on general aid allocations has highlighted a divergence between the factors that influence multilateral donors and the factors that influence bilateral donors (particularly with respect to human rights and democracy), we should be wary of generalising the findings of existing research on the allocation of budget support to bilateral donors. There is a need for research which examines the factors which shape bilateral donors' decisions about who should get budget support, and how much aid should be provided through this aid modality. This is the gap which this paper aims to address.

2 Quantitative research design

When it comes to the quantitative component of this paper, the first issues which arises relates to which technique is most appropriate for modelling budget support allocations. The use of budget support is relatively uncommon among bilateral donors. Since there will be many cases in which recipients will receive no budget support, a simple OLS regression would produce coefficients biased towards zero, underestimating the effect of independent variables. In order to address this problem, this paper models donors' decisions about the allocation of budget support in two stages. In the first 'eligibility' stage probit analyses are used to model donors' decisions about who should receive budget support. In the second 'proportion' stage,

OLS is used to model donors' decisions about how much budget support to give, that is, what proportion of their total aid to a given country will be provided as budget support. This approach raises the possibility of selection effects, since the second stage of analysis excludes cases in which no budget support is allocated. However, this problem can be managed by placing appropriate limitations on interpretation: findings about the proportion of aid allocated as budget support can only be applied with respect to recipients who are first determined to be eligible to receive this type of aid. While there are alternative solutions such as tobit or Heckman selection models, Clist makes a compelling argument that the two-stage combination of probit and OLS is preferable when modelling aid allocation³⁹.

This paper employs an original dataset composed of donor-recipient dyads to model the allocation of budget support in 2011. The dataset covers the 24 OECD-DAC donors and 93 developing countries who fall into the low and low-middle income categories (a full list of both is provided in Appendix A). The dataset is restricted to OECD-DAC donors partially for reasons of data availability, but also because these donors represent the universe of comparable cases: non-OECD-DAC donors tend to have different policies on aid allocation, and cannot be expected to make decisions about the provision of budget support in the same way.

Data on the dependent variable, budget support, is taken from the OECD's International Development Statistics (IDS) database⁴⁰. At the eligibility stage the *budget support* variable is a dichotomous variable, coded 1 if a donor allocates budget support to a recipient, and 0 if not. At the second stage of analysis, this variable measures the percentage of a donor's total ODA to a recipient that is provided in the form of budget support. These figures are calculated using data on aid disbursements rather than aid commitments. This ensures that the models capture the allocation of budget support in practice, rather than simply on paper. An increasing number of bilateral donors include a performance based or incentive based tranche in their budget support programs. Since performance based tranches are rarely paid out in full, relying of budget support commitments may systematically inflate the budget support

39 Paul Clist, "25 Years of Aid Allocation Practice: Whither Selectivity?," *World Development* 39, no. 10 (2011): 1726, doi:10.1016/j.worlddev.2011.04.031.

40 OECD, "International Development Statistics Online," *OECD International Development Statistics*, accessed April 6, 2010, <http://www.oecd.org/dac/stats/idsonline>.

allocations of these donors. Relying on budget support commitments is also likely to misrepresent donor behaviour because disbursements are more sensitive to changing circumstances than commitments. For example, when confronted by major corruption scandals donors tend to freeze or delay budget support disbursements, delaying decisions about their future commitments until they have had a chance to evaluate the recipient government's response. Budget support commitments may eventually be affected, but this tends to be a more drawn-out process⁴¹.

The independent variables included in the models at both stages fall into two main categories: variables that capture some aspect of the relationship between donor and recipient, and variables which capture characteristics of the recipient. The first category includes three variables: *donor share of aid*, *trade* and *colony*. *Donor share of aid* is the percentage of a recipient's total ODA provided by a given donor, and has been calculated using data on aid disbursements from the OECD's IDS database. Most of the independent variables are measured in 2010 because decisions about the disbursement of budget support in 2011 will generally be made on the basis of data from the previous year. *Donor share of aid* is an exception. It is measured in 2011 because allocations of budget support will primarily be influenced by the donor's expected share of aid in the year that budget support is to be disbursed. *Donor share of aid* is included because Knack's finding that donors are more likely to use country systems when they provide a greater share of aid to a particular country seems likely to hold true with respect to budget support⁴². In both cases donors are more likely to provide aid via these aid modalities because their larger presence in a recipient country gives them a degree of bargaining power that helps to allay concerns about removing restrictions that stipulate how and where aid money will be spent. *Trade* and *colony* are included because of past research showing that trading relationships and colonial ties influence both who gets aid, and how much they receive⁴³. Since donors' decisions are most likely to be influenced by their own trading interests (rather than that of recipients) the *trade* variable is measured using

41 Budget support commitments are generally made several years in advance and cover a multi-year period. These commitments are made as part of an agreement with the recipient government (often in the form of a Memorandum of Understanding).

42 Knack, *When Do Donors Trust Recipient Country Systems?*.

43 Alesina and Dollar, "Who Gives Foreign Aid to Whom and Why?"; Berthélemy and Tichit, "Aid Allocations and Development Financing."

the value of the donor's exports to the recipient, as a percentage of the value of the donor's total exports in 2010⁴⁴. This measure is then logged, in order to generate a more normal distribution. *Colony* is a dichotomous variable, coded 1 if the recipient has ever been a colony of the donor⁴⁵.

Three variables are included to try and capture the recipients' need for aid generally, and budget support in particular⁴⁶: *GDP per capita, PPP* (measured in current international dollars and logged), *population* (which has also been logged) and *aid dependency* (the total amount of ODA received by a country as a percentage of its GNI). While existing research has consistently shown that poorer countries get more aid, it also suggests that donors tend to give more aid (on a per capita basis) to smaller countries⁴⁷. Clist et al's results also suggest that more aid dependent countries may be more likely to be eligible for budget support, and more likely to receive a greater proportion of their aid through this aid modality⁴⁸.

Following Clist et al's finding that pro-poor policies attract budget support from the EC and World Bank⁴⁹, several variables are also included in order to capture the spending priorities of recipients. These are *education spending*, *military spending* and an interaction term which is the product of the two. The interaction term is included because it seems likely that donors are likely to determine whether a recipient has a pro-poor agenda not only by reference to levels of social spending, but by reference to how levels of social spending compare to spending on sectors, such as the military, which generate few benefits for the poor. Both spending variables are measured as a percentage of GDP. Due to the large amount of missing data on both education and military spending (a common problem in developing countries), the values used are averaged over a three year period (2008-2010) in order to reduce the number of cases that are dropped from analyses.

44 Calculations are based on data from the International Monetary Fund, "Direction of Trade Statistics," *IMF Data and Statistics*, 2013, <http://www.imf.org/external/data.htm>.

45 This data is from Thierry Mayer and Soledad Zignago, "Notes on CEPII's Distances Measures: The GeoDist Database," *CEPII*, December 2011, <http://www.cepii.fr/anglaisgraph/bdd/distances.htm>.

46 Data for each of these indicators is from Daniel Kaufmann, Aart Kraay, and Massimo Mastruzzi, "Worldwide Governance Indicators," *World Bank*, 2012, <http://info.worldbank.org/governance/wgi/index.asp>.

47 Alesina and Dollar, "Who Gives Foreign Aid to Whom and Why?"; Berthélemy and Tichit, "Aid Allocations and Development Financing"; Clist, "25 Years of Aid Allocation Practice."

48 Clist, Isopi, and Morrissey, "Selectivity on Aid Modality."

49 Ibid.

Several variables are included in order to test the impact of the political conditions in recipient countries on donors' decisions about budget support. The first is *political stability*, an index taken from the Worldwide Governance Indicators (WGI)⁵⁰. This index measures perceptions of the likelihood that the government will be destabilized or overthrown by unconstitutional or violent means, including politically-motivated violence and terrorism. The *good governance* variable combines four other indexes from the WGI: the measures of regulatory quality (which captures perceptions of the ability of the government to formulate and implement sound policies and regulations that facilitate private sector development); government effectiveness (which captures perceptions of the quality and independence of public services and the civil service, as well as the quality of policy formulation and implementation); the rule of law (which captures confidence in and compliance with the rules of society, particularly the quality of contract enforcement, property rights, the police, and the courts) and control of corruption (which captures perceptions of the extent to which public power is exercised for private gain). Initial analyses included each of these as separate variables, but struggled to produce significant results. Examination of the relationships between these four variables using the Pearson product-moment correlation coefficient (Pearson's r) suggested that this was due to a substantial degree of co-linearity between these four indicators (see Appendix B). As a result, these four indicators were combined into a single index of good governance. Both the *political stability* and *good governance* variables ranges from -2.5 to 2.5, with 2.5 representing the best score. In light of donors' policies on budget support (which emphasise the importance of these factors), Knack's findings with respect to corruption⁵¹, and Clist et al's with respect to government effectiveness⁵², both of these variables are expected to have a positive effect on the likelihood of a country being deemed eligible for budget support, and the amount of budget support which it receives.

This paper employs two alternative measures of regime type, the first focussed on political liberties and the second on the procedural safeguards commonly associated with democracy. The first is a two-part measure: the *political rights* and *civil liberties* variables produced by

50 Kaufmann, Kraay, and Mastruzzi, "Worldwide Governance Indicators."

51 Knack, *When Do Donors Trust Recipient Country Systems?*.

52 Clist, Isopi, and Morrissey, "Selectivity on Aid Modality."

Freedom House⁵³. To facilitate interpretation, these have been inverted so that 1 is poor, and 7 is high respect for political freedoms. The second measure of regime type, *democracy* is the polity2 measure from the PolityIV dataset⁵⁴. This combines two 10-point measures of democracy and autocracy into a single measure that ranges from -10 (complete autocracy) to 10 (complete democracy). A separate measure of respect for personal integrity rights, which are not fully captured in the Freedom House or PolityIV measures, is also included. The *political terror* variable relies on data taken from the political terror scale, which is calculated based on yearly country reports published by Amnesty International and the U.S. State Department⁵⁵. This variable ranges from 1 (which indicates that in a given country people are not imprisoned for their view, torture is rare or exceptional, and political murders are extremely rare) to 5 (indicating that terror has expanded to the whole population, with the leaders of a country placing no limits on the means or thoroughness with which they pursue their goals). While existing research has produced inconsistent results with respect to the impact of democracy and human rights on aid allocations, Knack's findings suggest we should expect a positive relationship between *civil liberties* and the allocation of budget support⁵⁶, while Clist et al's suggest the same with respect to *democracy*⁵⁷. This, together with donor policies, also suggests that we should expect a positive relationship between *political rights* and the allocation of budget support, and a negative relationship between *political terror* and the allocation of budget support. Given that donor policies do not present democracy and human rights as strict requirements, we should, however, expect that these variables will have a smaller or less strongly significant effect than those relating to the quality of governance.

Finally, a control for receipt of budget support in 2010 is used in some models. In the first stage this is a dichotomous variable coded 1 if a recipient received budget support from a given donor in 2010. In the second stage this variable measures the proportion of the donor's

53 Freedom House, "Freedom in the World Comparative and Historical Data," accessed May 12, 2010, <http://www.freedomhouse.org>.

54 Monty G Marshall, Keith Jagers, and Ted Robert Gurr, *Polity IV Project: Political Regime Characteristics and Transitions, 1800-2010, Dataset Users' Manual* (Severn: Center for Systemic Peace, 2010).

55 M Gibney, L Cornett, and R Wood, "Political Terror Scale 1976-2011," *Political Terror Scale*, 2012, <http://www.politicalterrorsscale.org>.

56 Knack, *When Do Donors Trust Recipient Country Systems?*.

57 Clist, Isopi, and Morrissey, "Selectivity on Aid Modality."

total ODA to a recipient that is provided in the form of budget support in 2010. This variable is included in light of Carey's argument that there is a substantial amount of bureaucratic inertia in aid allocations⁵⁸, with the expectation that it will be positively correlated with both eligibility for, and the proportion of budget support received in 2011. However, it is possible that the stability of aid allocation reflects a large degree of continuity in the factors that shape its aid allocation (i.e. most variables change little from year to year) rather than the inertia that characterises bureaucratic decision-making. Controlling for prior allocation of budget support does not allow us to distinguish which of these two alternatives is at play⁵⁹. As such, the qualitative evidence presented in section 4 provides some valuable insights regarding how the impact of this variable should be interpreted.

3 Results and analysis

Stage 1: Deciding who is eligible for budget support

Table 1, below, shows the results of a probit analysis of donors' decisions about who was eligible for budget support in 2011. It includes models with and without controls for the prior allocation of budget support, and using alternative measures of regime type. To aid in interpretation, Table 2 presents the predicted probabilities of a donor allocating budget support to a recipient in 2011 at different values of significant variables.

There is a large degree of similarity in the results for Model 1 and Model 3, indicating that these results are robust to different measures of regime type⁶⁰. Most, though not all, of the independent variables have the effects that were expected. *Donor share of aid* is very strongly significant (passing the 99.9% confidence level) in both Models 1 and 3 and has a positive, albeit somewhat small, effect on the probability that a donor will give budget support to a recipient. If a donor provides 2.5% of a recipient's total ODA, the probability that they will provide that recipient with budget support is a little over 6%⁶¹. If the donor's share of aid is

58 Carey, "European Aid."

59 It is also possible (and perhaps likely) that they are not mutually exclusive.

60 Unless otherwise noted, the predicted probabilities given in this paragraph are roughly the same for both Models 1 and 3.

61 All probabilities are calculated with other independent variables left at their observed values. For continuous

Table 1 Eligibility for budget support in 2011

	(1)	(2)	(3)	(4)
Donor share of aid	0.039*** (4.73)	-0.005 (-0.44)	0.040*** (4.85)	-0.002 (-0.22)
Trade (logged)	0.112* (2.40)	0.130* (2.03)	0.101* (2.20)	0.115† (1.85)
Colony	0.803*** (3.55)	0.583* (2.14)	0.809*** (3.58)	0.575* (2.13)
Aid dependency	-0.015† (-1.90)	-0.018 (-1.44)	-0.013† (-1.67)	-0.017 (-1.29)
GDP per capita, PPP (logged)	-0.750*** (-5.01)	-0.467* (-2.35)	-0.700*** (-4.76)	-0.409* (-2.11)
Population (logged)	0.127† (1.79)	0.007 (0.08)	0.129† (1.81)	0.015 (0.16)
Political stability	0.418** (3.11)	0.159 (0.96)	0.365** (2.68)	0.112 (0.67)
Good governance	0.555* (2.29)	0.058 (0.18)	0.396† (1.82)	-0.162 (-0.57)
Education spending	0.183* (2.46)	0.112 (1.23)	0.167* (2.25)	0.095 (1.05)
Military spending	0.289† (1.84)	0.131 (0.66)	0.239 (1.51)	0.075 (0.37)
Education x military spending	-0.076* (-2.28)	-0.042 (-1.00)	-0.069* (-2.07)	-0.035 (-0.84)
Political terror	-0.202† (-1.71)	-0.152 (-0.99)	-0.116 (-0.98)	-0.047 (-0.31)
Political rights (FH)	0.107 (1.38)	0.147 (1.45)		
Civil rights (FH)	-0.268* (-2.01)	-0.328† (-1.85)		
Democracy (PolityIV)			-0.019 (-1.42)	-0.016 (-0.94)
Budget support 2010		2.272*** (12.50)		2.259*** (12.49)
<i>N</i>	1242	1242	1218	1218
Pseudo R ²	0.225	0.523	0.217	0.516
Log likelihood	-248.421	-152.891	-249.391	-157.253
Correctly predicts receipt of budget support (% cases)	42.65	77.21	42.65	78.68

Figures in cells are probit regression coefficients. Figures in parentheses are t statistics.

† p<0.1 * p<0.05, ** p<0.01, *** p<0.001

variables, probabilities have generally been calculated at the mean for that variable, and the mean ± one standard deviation.

Table 2 Probability of receiving budget support in 2011

	(1)	(2)	(3)	(4)
<i>Donor share of aid (% ODA)</i>				
2.5 ($\approx \bar{x}$)	.064		.065	
9.5	.098		.101	
<i>Trade (logged)</i>				
-7.9	(0.0004%)	.038	.044	.041
-5.4 ($\approx \bar{x}$)	(0.005%)	.060	.062	.062
-1.9	(0.150%)	.109	.097	.106
<i>Colony</i>				
No	.064	.067	.065	.068
Yes	.195	.117	.201	.118
<i>GDP per capita, PPP (logged)</i>				
7.00	(\$1097)	.153	.096	.147
7.75 ($\approx \bar{x}$)	(\$2322)	.070	.068	.070
8.50	(\$4915)	.028	.048	.030
<i>Political stability</i>				
-1	.057		.059	
1	.183		.168	
<i>Good governance</i>				
-1	.050		.056	
1	.227		.172	
<i>Education spending (% GDP)</i>				
2.5	.044		.046	
4.5 ($\approx \bar{x}$)	.078		.078	
6.5	.129		.125	
<i>Civil liberties (FH)</i>				
1	.220			
3	.119			
5	.057			
7	.025			
<i>Budget support 2010</i>				
No		.015		.015
Yes		.471		.477

Figures in cells are the probabilities of receiving budget support when other variables are left at their observed values. Probabilities were calculated using the models from Table 1. For continuous variables probabilities have been calculated at the mean \pm one standard deviation.

increased to 9.5%, that probability rises to around 10%. *Trade* is significant at the 95% confidence level in both Models 1 and 3. When a donor's exports to a recipient represent 0.005% of its total annual exports, the probability that it will give budget support to the recipient is around 6%. If exports increase to 0.15% of a donor's total, that probability changes to almost 11%. Colonial ties have a notably larger substantive effect. Significant at the 99.9% level in both Models 1 and 3, the existence of a historical colonial tie between donor and recipient shifts the probability of a donor providing budget support from about 6% to roughly 20%. The results for *donor share of aid*, *trade* and *colony* suggest that the nature of the relationship between donor and recipient, and in particular the donor's interests with respect to the recipient, play an important role in decisions about who should receive budget support. Yet poverty also has a large effect on these decisions. The (logged) GDP per capita of the recipient, adjusted for purchasing power, is significant at the 99.9% confidence level. A recipient with GDP per capita (PPP) of \$1097 has about a 15% chance of attracting budget support from a donor, but for a recipient with GDP per capita of \$2322, this falls to 7%.

In line with donor policies, measures of the quality of governance and the policy priorities of developing countries appear to have a positive effect on eligibility for budget support. *Political stability*, significant at the 99% confidence level, has a large substantive effect. For a country with a *political stability* score of -1, the probability that a donor will provide budget support is just under 6%. If the political stability score changes to 1, that probability increases to around 18% in Model 1, or 17% in Model 3. *Good governance* has a larger substantive effect but is less robustly significant: it passes the 95% confidence level in Model 1, but falls short in Model 3⁶². In Model 1, a country with a *good governance* score of -1 has only a 5% chance of attracting budget support from a donor, while a country with a *good governance* score of 1 has almost a 23% chance. *Education spending*, significant at the 95% confidence level, has a less dramatic effect. A recipient country that increases its spending on education from 4.5% of GDP to 6.5% will shift the probability of receiving budget support from roughly 8% to almost 13%. The effect of the spending interaction term (which captures the effect of interaction between military and education spending) is also significant at the 95% confidence level, though its substantive effect is difficult to interpret. The fact that it is significant does,

62 Possible reasons for this are discussed in more detail below.

however, suggest that the ratio of education spending to military spending, rather than simply the level of education spending, plays a role in the allocation of budget support. Additional support for this is provided by the fact that omitting the interaction term from the models in Table 1 leads to *education spending* becoming insignificant (results not shown).

Aid dependency, though significant only if the confidence level is dropped to 90%, appears to have an unanticipated negative effect on eligibility for budget support. Countries that are more dependent on aid are less likely to receive budget support⁶³. While this result might fall short of normal standards of significance, it is somewhat worrying given that budget support is, in large part, designed to reduce the negative side effects of aid dependency.

Almost all of the measures of democracy and human rights fall short of statistical significance. The exception is the *civil liberties* variable in Model 1. As Tables 1 and 2 show, while none of the other measures of democracy are statistically significant, civil liberties is significant at the 95% confidence level. However, contrary to expectations, it has a negative effect on the probability that a recipient will be categorised as eligible for budget support. Holding other variables at their observed values, a country with a civil liberties score of 1 (the worst) has a 22% chance of receiving budget support from a donor. At a score of 3, this decreases to 11.9%, while at a civil liberties score of 5 a country has a 5.7% chance of a donor categorizing it as eligible for budget support. For countries with the highest possible civil liberties score (7), the probability of receiving budget support is a tiny 2.5%.

The large, unexpected negative effect of civil liberties on the probability of receiving budget support warrants closer investigation. Figure 1, below, illustrates the relationship between civil liberties and the probability of receiving budget support in Model 1. Figure 1 reveals a very large degree of uncertainty surrounding the predicted probabilities at low values of *civil liberties*. One reason for this could be a shortage of observations at low levels of civil liberties. Figure 2, below, suggests that while this might explain some of the uncertainty, it cannot account for it all. Figure 2 shows only on those observations included in Model 1, Table 1. It reveals the fact that this does not include any observations in which the recipient's

⁶³ This has been confirmed by calculating marginal probabilities, though they have not been included in Table 2 because the relationship falls short of statistical significance.

Figure 1 Civil liberties and the probability of receiving budget support

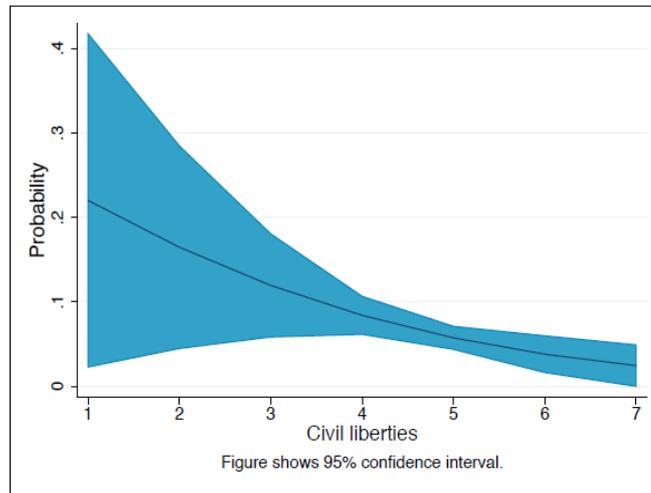
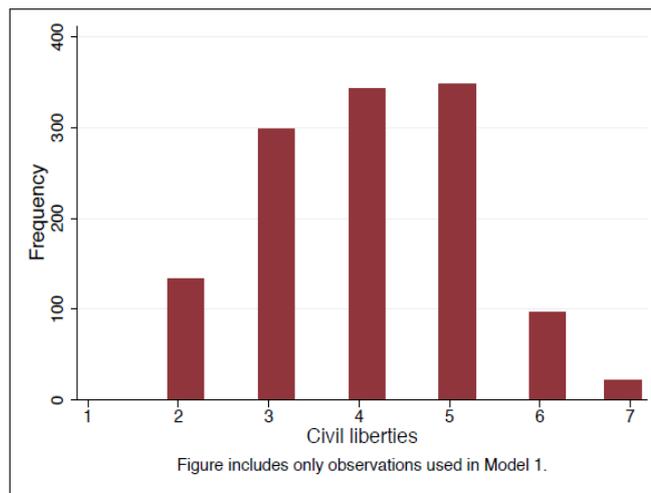


Figure 2 Variation in civil liberties



score for civil liberties is 1. Yet Figure 2 also shows that there more observations with civil liberties scores of 2 or 3, than there are with scores of 6 or 7, points at which the uncertainty surrounding predicted probabilities is much lower. This suggests that a large part of the uncertainty, perhaps most of it, is due to an omitted variable which has a particularly strong influence on donors' decisions about eligibility for budget support at low levels of civil liberties. Perhaps the most likely candidate is the existence of geopolitical or strategic considerations that lead donors to disregard a recipients' poor record on civil liberties.

The contrasts between Models 1 and 2, and Models 3 and 4, indicate that there is a substantial amount of continuity in the allocation of budget support. Adding the control for receipt of budget support in 2010 drastically reduces the significance of the other independent variables, with most becoming insignificant at the 95% confidence level. Other than that control, only trade between donor and recipient and the poverty of the recipient are significant in both Models 2 and 4. As Table 2 shows, the substantive impact of these variables on the probability of receiving budget support is also reduced. In addition, introducing the control for prior receipt of budget support more than doubles the pseudo R^2 , and dramatically increases the predictive accuracy of the models. While Models 1 and 3 correctly predict less than 43% of cases in which a recipient is categorised as eligible for budget support, Models 2 and 4 both predict over 77% of such cases correctly. The substantive effect of prior receipt of budget support is illustrated in Table 2. In both Models 2 and 4, a country which did not receive budget support in 2010 has only a 1.5% probability of receiving budget support in 2011, holding other variables at their observed values. In contrast, the same probability for a country that did receive budget support in 2010 is more than 47%. Unfortunately, exactly what this means is unclear. One possibility is that Carey⁶⁴ is right, and that aid allocations, including decisions about eligibility for budget support, are subject to a substantial amount of bureaucratic inertia. Another possibility is that the determinants of eligibility for budget support, such trade between donors and recipients, colonial ties and the quality of governance, vary very little from year to year. The control for receipt of budget support in 2010 may not be capturing bureaucratic inertia, but rather the values of all of the other independent variables in 2010. While the statistical techniques applied in this paper do not allow us to clearly determine which of these possibilities is correct, the mechanics of budget support suggest that at least some degree of bureaucratic inertia is likely. As noted above, budget support commitments are generally made for multi-year periods (most commonly 3 or 5 years) and, in line with the goal of reducing aid volatility, are intended to be relatively stable. The qualitative evidence presented in section 4 provides additional insight into how this result should be interpreted.

64 Carey, "European Aid."

As noted above, the impact of *good governance* on eligibility for budget support is substantial, but is not as robust as might have been expected given that it is generally given a central role in donors' policies on budget support. One possibility is that the variables *education spending* and *military spending* (and by extension, the relevant interaction term) are also capturing the effect of good governance: both collecting and spending revenue requires substantial government capacity. If this is the case, the significance of the *good governance* variable may be suppressed by co-linearity between it and these two variables (as well as the spending interaction term). Testing the correlations between these variables does not, however, suggest that this is the case: the Pearson's R for *good governance* and *education spending* is only 0.159, while for *good governance* and *military spending* it is just -0.083. Omitting the spending variables from the analyses presented in Table 1 does increase the significance of the *good governance* variable (see Table 1A in Appendix C). However, much of this increase appears to be due to the larger number of observations that are included in the analysis when the spending variables are dropped⁶⁵. Dropping the spending variables increases the significance of a number of other variables, not just *good governance*. In addition, if the spending variables are dropped, but the analysis is constrained to the same samples used in the models in Table 1, the increase in the significance of *good governance* is less marked (see Table 1B in Appendix C).

Curiously, even when the samples are constrained to match those of Table 1, the significance of *good governance* still increases. In contrast to Models 1 and 3 in Table 1, *good governance* is significant at the 99% confidence level in the revised of Model 1, and at the 95% level in the revised Model 3 (see Table 1B in Appendix C). Given the low correlations between *good governance* and the spending variables, the most likely explanation for this is not co-linearity, but a selection effect. As noted in Section 2, data on sectoral spending is particularly patchy for developing countries. In a significant number of cases, the information is simply not available. Moreover, it is likely that the recipients for which this information is missing, and which are therefore falling out of the analyses in Table 1, are countries in which the quality of governance is lower. As a result, these countries are probably under-represented in the samples on which those analyses rely, suppressing the significance of *good governance*.

65 As noted above, data on the spending variables (and particularly education spending) is missing for a significant number of cases.

Despite this selection effect, the models presented in Table 1 are arguably the better specification when it comes to modelling donor's decisions about who is eligible for budget support. While they may underestimate the impact of *good governance* on eligibility for budget support, they have greater predictive accuracy. Removing the spending variables from the four models presented in Table 1 reduces the predictive accuracy of all four, particularly those which do not control for prior receipt of budget support. While Models 1 and 3 in Table 1 correctly predict over 42% of the cases in which a donor provided a recipient with budget support, the models omitting the spending variables (i.e. Models 1 and 3 in Table 1A Appendix C) correctly predict only 23% and 25% of such cases, respectively. The latter models do have a slightly higher pseudo R^2 , but given the artificiality of that measure in a probit analysis⁶⁶, the predictive accuracy of the models seems the more important measure. In this case, the higher predictive accuracy of the models in Table 1 strongly suggests that the policy priorities of aid recipients, measured as sectoral spending on education and the military, play an important role in shaping donors' decisions about who should get budget support.

Stage 2: Deciding how much budget support to allocate

The second stage of the analysis models donors' decisions about how much of their aid to allocate as budget support once a recipient has been categorised as eligible for this form of aid. Table 3 strongly suggests that the variables that shape decisions about who should get budget support are not the same as those that shape decisions about how much budget support should be provided. In particular those variables which capture the nature of the donor-recipient relationship are far less influential in determining the proportion of aid which a donor allocates as budget support. *Donor share of aid*, *trade* and *colony* were all significant in the models of eligibility for budget support. Yet when it comes to the amount of aid that is given as budget support, only *trade* obtains significance at the 95% confidence level, and only when the control for prior receipt of budget support is included.

66 Timothy M. Hagle and Glenn E. Mitchell II, "Goodness-of-Fit Measures for Probit and Logit," *American Journal of Political Science* 36, no. 3 (1992): 762–784, doi:10.2307/2111590.

Table 3 Proportion of bilateral ODA provided as budget support in 2011

	(1)	(2)	(3)	(4)
	<i>Budget support in 2011 (% ODA from donor)</i>			
Donor share of aid	0.125 (0.43)	0.0365 (0.17)	0.139 (0.48)	0.039 (0.18)
Trade (logged)	0.732 (0.37)	3.224* (2.17)	0.461 (0.24)	3.018* (2.07)
Colony	-2.143 (-0.34)	-4.951 (-1.09)	-1.927 (-0.31)	-4.408 (-0.97)
Aid dependency	-1.345* (-2.26)	-1.292** (-2.97)	-1.301* (-2.22)	-1.225** (-2.85)
GDP per capita, PPP (logged)	-22.44** (-3.07)	-18.36*** (-3.44)	-21.83** (-3.12)	-16.78** (-3.25)
Population (logged)	-3.913 (-1.32)	-7.093** (-3.22)	-3.418 (-1.10)	-7.315** (-3.14)
Political stability	5.362 (1.23)	-1.216 (-0.37)	5.187 (1.15)	-2.581 (-0.75)
Good governance	17.90* (1.99)	3.749 (0.55)	15.38† (1.93)	1.836 (0.30)
Education spending	8.471* (2.51)	6.833** (2.77)	8.083* (2.50)	6.030* (2.53)
Military spending	15.80* (2.09)	11.32* (2.04)	15.23* (2.04)	10.25 (1.86)
Education x military spending	-3.775* (-2.54)	-3.137** (-2.89)	-3.584* (-2.49)	-2.933** (-2.77)
Political terror	0.137 (0.03)	-0.449 (-0.15)	0.946 (0.25)	-0.398 (-0.14)
Political rights (FH)	1.127 (0.41)	-1.793 (-0.89)		
Civil liberties (FH)	-3.064 (-0.60)	-0.284 (-0.08)		
Democracy (PolityIV)			0.009 (0.02)	-0.554 (-1.46)
Budget support 2010 (%)		0.672*** (8.20)	0.666***	0.672*** (8.17)
constant	258.2* (2.46)	276.4*** (3.61)	232.8* (2.34)	262.0*** (3.59)
N	90	90	90	90
Adjusted R ²	0.180	0.564	0.186	0.564

Figures in cells are OLS regression coefficients. Figures in parentheses are t statistics.

† p<0.1* p<0.05, ** p<0.01, *** p<0.001

Unfortunately, Table 3 also suggests that donors' decisions are somewhat incoherent when it comes to responding to the need of recipients. In line with donor behaviour at the eligibility stage, poorer countries do tend to receive a greater proportion of their aid as budget support. For example, in both Models 1 and 3 in Table 3, if the logged *GDP per capita, PPP* of a country decreases by one unit, from 8 to 7 (roughly equivalent to a decrease of GDP per capita from \$3000 to \$1100) then, holding other variables constant, the proportion of aid which a donor provides to that country as budget support will, on average, increase by about 22 percentage points. Yet more aid dependent countries, which need budget support the most, receive a smaller proportion of aid as budget support. Holding other variables constant, a one percentage point increase in *aid dependency* leads to a 1.3 percentage point decrease in the proportion of aid delivered as budget support. This apparently perverse result may be due to limits on absorptive capacity. In a highly aid dependent country, allocating 20% of aid as budget support will place far more strain on country systems than allocating the same percentage of aid as budget support in a less aid dependent country.

One very interesting aspect of the results at this stage is the effect of adding the control for prior receipt of budget support. In contrast to the first stage of analysis, where introducing this control suppressed the significance of other variables, in the second stage it tends to *increase* their significance. In addition several variables which are not significant in Models 1 and 3 of Table 3 become so. This includes *trade*, which becomes significant at the 95% confidence level in Models 2 and 4, and *population*, which becomes significant at the 99.9% confidence level. This suggests that donors' decisions about the proportion of aid that should be given as budget support are less strongly determined by prior decisions than decisions about eligibility for budget support. This lends some support to the argument that bureaucratic inertia plays an important role in the allocation of budget support. Qualitative evidence from interviews with donor staff help to explain why. Several interviewees noted that decisions about the proportion of aid to provide as budget support are likely to require approval at a much lower level of government while decisions to start, or withdraw, budget support have political implications that will often render them subject to approval at the ministerial level. In addition, the mechanics of budget support build in a degree of flexibility when it comes to the precise amount of budget support disbursed in a particular year. This is because many donors

include performance-based or incentive tranches in their budget support programs. This allows donors to vary the amount of budget support disbursed depending on performance against a set of agreed indicators. These mechanisms help to explain why bureaucratic inertia is less influential on decisions about how budget support to provide.

The results of the spending variables are once again difficult to interpret. *Education spending* is significant in all four models. In Models 1 and 3, a one percentage point increase in education spending as a proportion of GDP is associated with an increase in the proportion of aid provided as budget support of just over 8 percentage points, holding other variables constant. Yet *military spending* is also significant at the 95% confidence level (except in Model 4), and has a positive effect on the proportion of aid allocated as budget support. In both Models 1 and 3, a one percentage point increase in military spending as a proportion of GDP leads to a more than 15 percentage point increase in budget support. In contrast, the spending interaction term, also significant at (at least) the 95% confidence level in all four models, has a negative impact on how much budget support a donor allocates. This implies that if education spending remains constant, but military spending increases, part of the positive effect that the increase in military spending had on the proportion on aid allocated as budget support would be offset by the negative effect associated with an increase in the value of the interaction term. Unfortunately, the net effect of this is hard to gauge, as it would be dependent on the values of both *education spending* and *military spending*. At the least, the significance of the interaction term does seem to indicate that the relationship between education and military spending, rather than just their levels, is important in modelling donors' decisions about how much aid they will provide as budget support. This is given additional weight by the fact that the omission of the interaction term leads both *education spending* and *military spending* to become insignificant (results not shown). This is a valuable finding, as previous work (most notably that of Clist, Isopi and Morrissey⁶⁷) has relied on the level of education spending as an indicator of pro-poor policies. The failure to recognise that pro-poor policies entail not only higher education spending, but higher education spending relative to non-social spending (and military spending in particular) may explain why the measure of education spending is not reliably significant in Clist et al's models.

67 Clist, Isopi, and Morrissey, "Selectivity on Aid Modality."

Neither *political stability*, nor any of the measures of democracy and human rights, gain significance with respect to the proportion of aid allocated as budget support. *Good governance* is significant at the 95% confidence level in Model 1 of Table 3, but falls short of significance in the others. However, as in stage 1, there are signs that this may be due to a selection effect, specifically, the fact that countries with lower levels of governance are more likely to drop out of the analysis due to missing data. Table 4 shows the results that are generated once the three spending variables, the variables where missing data is greatest, are dropped from the analysis.

What is particularly remarkable about the results in Table 4 is not only that the significance of good governance is substantially increased, but that all of the other independent variables, with the exception of the control for prior levels of budget support, lose significance. Limiting the sample to observations included in the Table 3 analyses produces results more similar to Table 3 (see Table 4A, Appendix C). Together, this strongly suggests that a selection effect is at play. If this is the case then, apart from prior levels of budget support, good governance may be the most important factor influencing donors' decisions about what proportion of their aid to provide as budget support. In Model 1 of Table 4 a one unit increase in the index of good governance leads, on average, to a massive 22 percentage point increase in the proportion of aid which a donor provides as budget support, holding other variables constant. In Model 3 of Table 4 this increase is even larger, at 24 percentage points. The good governance variable loses statistical significance when the control for prior levels of budget support is introduced, though it does pass the 90% confidence threshold in Model 4 of Table 4. The qualitative evidence bolsters the conclusion that good governance plays an important role, but one which is masked by a selection effect when the spending variables are included. When asked about the factors that influence the allocation of budget support, the first response of those managing budget support almost always involves reference to good governance. Donor staff place particular stress on the quality of public financial management systems and control of corruption. However, some staff will sometimes qualify this, observing that a commitment to improving the quality of financial management may at times be more important than its absolute level.

Table 4 Proportion of bilateral ODA provided as budget support in 2011, omitting spending variables

	(1)	(2)	(3)	(4)
	<i>Budget support in 2011 (% ODA from donor)</i>			
Donor share of aid	0.041 (0.23)	0.007 (0.05)	0.079 (0.40)	0.004 (0.03)
Trade (logged)	-2.506† (-1.74)	-0.496 (-0.45)	-2.196 (-1.48)	-0.042 (-0.04)
Colony	-2.070 (-0.40)	-2.844 (-0.73)	-3.342 (-0.62)	-3.288 (-0.83)
Aid dependency	0.062 (0.21)	-0.057 (-0.26)	-0.042 (-0.15)	-0.076 (-0.36)
GDP per capita, PPP (logged)	-4.277 (-0.87)	-1.540 (-0.42)	-4.803 (-0.98)	-1.413 (-0.39)
Population (logged)	2.502 (1.14)	-0.603 (-0.36)	0.515 (0.21)	-2.500 (-1.36)
Political stability	5.240 (1.42)	0.007 (0.00)	4.070 (1.11)	-1.316 (-0.48)
Good governance	21.99** (2.93)	9.410 (1.64)	24.24*** (3.46)	9.751† (1.82)
Political terror	-0.589 (-0.20)	-1.438 (-0.67)	0.464 (0.16)	-0.127 (-0.06)
Political rights (FH)	2.881 (1.32)	1.000 (0.61)		
Civil liberties (FH)	-3.851 (-1.04)	-2.876 (-1.05)		
Democracy (PolityIV)			0.0411 (0.10)	-0.239 (-0.82)
Budget support 2010 (%)		0.655*** (9.51)		0.660*** (9.71)
constant	25.92 (0.34)	48.13 (0.86)	58.49 (0.79)	69.59 (1.27)
<i>N</i>	124	124	120	120
Adjusted R ²	0.178	0.543	0.186	0.561

Figures in cells are OLS regression coefficients. Figures in parentheses are t statistics.

† p<0.1* p<0.05, ** p<0.01, *** p<0.001

Section 4 Exploring the qualitative evidence

Unpacking bureaucratic inertia

The quantitative analysis suggested that bureaucratic inertia plays an important role in the allocation of budget support. Yet what, exactly, does 'bureaucratic inertia' entail? On the face of it the concept is somewhat pejorative, implying that allocations of budget support are stable because donors' organizational systems are inefficient and slow to respond to change. Evidence from interviews with donor staff indicates that donors' apparent unresponsiveness to changing circumstances is not simply the product of bureaucratic red tape. As noted earlier, some degree of bureaucratic inertia is created by the mechanics of budget support, with commitments generally being made for multi-year periods. In interviews, many donor staff made reference to the impact of these long-term commitments on the day to day management of budget support. A number of those interviewed stressed the quasi-contractual nature of the Memorandum of Understanding (or equivalent document) in which they committed to providing budget support. These interviewees often emphasized the fact that arbitrary, unilateral decisions to suspend budget support would represent a breach of these agreements. In Uganda, one Head of Development Cooperation commented:

You make a commitment and you sign that commitment. So, if we change the instrument, then we have to sit again around the table... You have a state of law, you have to respect your commitments⁶⁸.

Some donor staff, most commonly those working for northern European donors, also noted that decisions about the use of budget support were influenced by a desire to be a good donor, one who acts in accordance with the principles (particularly the principles of ownership and alignment) set out in the *Paris Declaration on Aid Effectiveness* of 2005 (Paris Declaration). In explaining Finland's continued use of budget support in Zambia, one embassy official observed that "Finland has been trying to be... the so-called 'good pupil' in the class," feeling bound not only to respect bilateral commitments made to the Government of Zambia, but also

68 Marc Deneer, Head of Development Cooperation, Embassy of Belgium - Uganda, interview by Susan Dodsworth, November 22, 2013.

commitments made at the international level⁶⁹. Many interviewees noted that donors are evaluated on the timeliness and predictability of their aid disbursements. They mentioned concerns that delaying or suspending budget support could lead both host governments and domestic NGOs to criticize them for a failure to live up to the principles set out in the Paris Declaration. In Uganda the Belgian Head of Development Cooperation stated:

we [Belgium] have a civil society that is relatively strong, and every year we are criticized by the NGOs who say [to the Belgium Government] you do not reach the 0.7% [of GNP target for ODA] and even the budget you have you are not able to disburse.⁷⁰

Evidence from interviews suggests that bureaucratic inertia also captures donors' desire to maintain good relationships with recipient governments. Donor staff frequently emphasized the importance of maintaining good working relationships with recipients. In particular, some observed that the past provision of budget support, and the high level political dialogues associated with it, represented an important investment that would be placed at risk if budget support were to be suspended or withdrawn. In doing so, donor officials often noted that such a risk would only be taken when there was clear evidence of an emerging problem or change in circumstances. After making such comments, donor officials stressed that while they did aim to be responsive to changing conditions, they often confronted an absence of hard evidence on which decisions could be based. This complaint was made most often with respect to changing political circumstances, with many interviewees noting the potential for grey areas and subjectivity when it came to assessments of political trends. This problem was highlighted in Zambia, where many of those interviewed mentioned concerns about a perceived narrowing of political space. Yet, as one donor official commented:

The thing is, not all donors are convinced that the human rights issue has changed. The issues might have become more visible, but we're not sure that the situation is so much worse.⁷¹

Perhaps unsurprisingly, the background of donor staff appeared to have an impact on whether

69 Ville Luukkanen, Counsellor (Economic Growth and Private Sector Development), Embassy of Finland - Zambia, interview by Susan Dodsworth, October 2, 2013.

70 Marc Deneer, Head of Development Cooperation, Embassy of Belgium - Uganda, interview.

71 Head of Cooperation, Budget Support Donor - Lusaka, interview by Susan Dodsworth, November 6, 2013.

or not these kinds of complaints would be made. Most of those tasked with management of budget support have backgrounds in economics and commonly expressed the view that 'politics' was outside of their realm of expertise. The handful of budget support managers with more politically-oriented backgrounds were notably more comfortable in discussing and making judgements about political change.

Omitted variables and potential interactions

The qualitative evidence reveals some potential shortcomings in the statistical models presented in the earlier part of this paper. Interviews suggest that they omit a number of important variables: public support for development aid in the donor country, the economic situation of the donor, and the extent of domestic media coverage of scandals and crises in the recipient country. Perhaps more importantly, the interviews also point to a substantial degree of interaction between these variables. Two examples serve to illustrate the interaction of these factors. The first is the response of bilateral donors to the corruption scandal at the Office of the Prime Minister (OPM) in Uganda, which was exposed in 2012. The second is the response of donors to corruption in the health sector in Zambia in 2009.

Uganda's OPM scandal involved the embezzlement of almost US\$13 million of basket funding⁷² which had been provided for reconstruction programs in the northern part of Uganda. The affected funds had been provided by Norway, Sweden, Denmark and Ireland. Reports of problems at the OPM first surfaced in 2011, but were not confirmed until October 2012, when the Auditor-General published a special investigation report on the matter⁷³. The report laid out the full scope of corruption, and provided an impressive level of documentation regarding how money had been diverted, and by whom. While all donors suspended budget support in the wake of this scandal, the timing of their decisions and their willingness to resume budget support varied. Ireland's response was the quickest, and the strongest. The Irish Embassy received instructions to suspend budget support within 48 hours of the Auditor-General's report being released. Ireland did not just delay any disbursement of budget support,

72 While the report from the Auditor-General refers to the affected funds as budget support, donors consistently expressed the view that these funds were more appropriately categorized as a basket fund.

73 Office of the Auditor-General, *Special Investigation Report on Allegations of Financial Impropriety at the Office of the Prime Minister* (Kampala: Government of Uganda, October 2012).

but cancelled its entire program of cooperation with the Government of Uganda⁷⁴. Officials interviewed from a number of different donor organizations consistently attributed this to the interaction of three factors: Ireland's poor economic situation in the wake of the global financial crisis, the prominence given to the OPM scandal by Irish media and, as a consequence of both of these, a significant decline in public support for development assistance in Ireland. In contrast, Belgium was slower to suspend budget support and far more willing to return once key concerns were addressed. While, unlike Ireland, Belgian funds had not been directly affected by the OPM scandal, the Head of Development Cooperation at the Belgian embassy attributed this slower, more moderate response to strong public support and mobilization around aid issues⁷⁵. He observed that a continued suspension of budget support was likely to attract substantial public criticism from Belgian NGOs.

Zambia experienced a similar corruption scandal in 2009. That case involved the misappropriation of grants from the Global Fund to Fight Aids, Tuberculosis and Malaria. However it led both Norway and Sweden, who provided substantial funding to the health sector, to suspend their development assistance. In the case of Sweden, this included first a suspension, and then a complete withdrawal from budget support. Sweden's withdrawal from budget support was notable because it was made unilaterally and, apparently, against the recommendation of staff based at the embassy in Lusaka. Prominent coverage of the scandal in Swedish media appears to have made the continuation of budget support political untenable, ultimately leading to the dismissal of the head of the Swedish International Development Agency⁷⁶. As one official from the Swedish embassy reported:

... it was a big issue in the Swedish press. And after that budget support had a really bad reputation. I think the Embassy at the time... after the 2009 scandal... we were ready to resume budget support towards the end of 2010, but our Government said no.... It was really in the media that Zambia was the face of corruption...⁷⁷

74 Economic Advisor, Budget Support Donor - Uganda, interview by Susan Dodsworth, December 5, 2013.

75 Marc Deneer, Head of Development Cooperation, Embassy of Belgium - Uganda, interview.

76 Rizza Leonzon, "Sweden Dismisses Sida Chief, Orders Agency Revamp," *Devex*, August 27, 2010, <https://www.devex.com/en/news/sweden-lets-sida-chief-go-eyes-revamp-of-agency/67501>.

77 Nina Strandberg, First Secretary, Embassy of Sweden - Zambia, interview by Susan Dodsworth, November 5, 2013.

The interviews also point to a notable degree of interdependence between donors' decisions about budget support. The interviews suggest the interdependence of donors' decisions is primarily a concern with respect to decisions about whether or not to allocate budget support. Several donor officials noted that when other donors are providing budget support, there is pressure to do likewise in order to ensure access to the high level political dialogues associated with the modality. This appears to be particularly true for smaller donors who, as several donor officials observed, have very few people on the ground and little high-level access to recipient governments outside of the forums attached to budget support. These smaller donors need budget support “to buy a seat at the table.”⁷⁸ Statements made by donor officials also indicated that the decisions of other donors are particularly important when it comes to suspensions of budget support. In such cases, there is clear recognitions that a co-ordinated response is more likely to prompt the desired reaction from recipient governments. This is particularly true for smaller donors, who are well aware that the amount of budget support they provide is generally too low for their individual decisions to have much impact on the behaviour of recipient governments. This is evidenced by the following statement, which was made in response to a query about donors' apparent preference for stable budget support disbursements:

... the main reason really is that Finland tends not to go solo anywhere. We don't see the value in making a solo stand on almost any issue, anywhere, because we feel that we are a small country. It's counterproductive and detrimental to both parties.⁷⁹

The response of budget support donors to the OPM scandal in Uganda is also illustrative. Almost all donor staff interviewed stressed that the decision to suspend budget support after the publication of the Auditor-General's report was a joint decision.⁸⁰ This attempt at coordination was driven by a desire to send a clear and unambiguous to the Ugandan Government, and a recognition that an uncoordinated response was likely to translate into a lack of impact on government behaviour. One donor official explicitly referred to the OECD-

78 Governance Advisor, Budget Support Donor - Uganda, interview by Susan Dodsworth, February 3, 2014.

79 Ville Luukkanen, Counsellor (Economic Growth and Private Sector Development), Embassy of Finland - Zambia, interview.

80 For example, Marc Deneer, Head of Development Cooperation, Embassy of Belgium - Uganda, interview.

DAC Governance Network Principles on Anti-Corruption⁸¹, noting that Uganda was the first country in which donors implemented this framework⁸².

The potential interdependence of donor decisions on the allocation of budget support represents both good and bad news. It is good news because it suggests that donors' efforts to coordinate and harmonize their ODA, and in particular their responses to corruption, are working. It is bad news because the statistical methods employed in the quantitative component of this paper assumes that allocation decisions by one donor are independent of others. As such, additional care must be taken with respect to the results of the quantitative analysis.

5 Limitations and implications

The evidence presented in this paper is subject to a number of limitation. Most notably, the quantitative component of this paper has examined the allocation of budget support at a single point in time. While a matter of debate, there are some signs in existing research that the factors that shape donors' decisions about aid have shifted over time⁸³. In the interviews that inform the qualitative component of this paper, several donor officials also observed an increasingly level of selectivity in the allocation of budget support. In light of this we should be wary of assuming that the results of this paper can be generalised to the allocation of budget support prior to 2011, or to the allocation of budget support in the future. The research presented in this paper is a first step, and one that makes the most of the very limited data that is currently available with respect to bilateral budget support. As more data becomes available, further research will be required to determine whether or not the patterns of budget support allocation identified in this paper hold over time.

On important finding to emerge from the quantitative component of this paper is that the factors that influence donor's choices about who is eligible for budget support and how much

81 Set out in OECD, *Policy Paper and Principles on Anti-Corruption: Setting and Agenda for Action*, DAC Guidelines and Reference Series (Paris: OECD, 2007).

82 Governance Advisor, Budget Support Donor - Uganda, interview.

83 Berthélemy and Tichit, "Aid Allocations and Development Financing"; Dollar and Levin, "The Increasing Selectivity of Foreign Aid, 1984–2003"; Clist, "25 Years of Aid Allocation Practice."

budget support they should receive are not exactly the same. In particular, the nature of the relationship between the donor and recipient is more important in determining eligibility than in shaping the amount of aid provided as budget support. A donor's share of aid to a developing country, the importance of its trading relationship with that country and the existence of historical colonial ties, all make a donor more likely to categorise that country as eligible to receive budget support. In contrast, they have relatively little effect on the proportion of aid that donor delivers as budget support, once it has decided that a developing country should receive this type of aid. The results presented in this paper also suggest that good governance may be particularly important at this second stage of the allocation decision. However, this conclusion rests on the assumption that the inclusion of spending variables in stage 2 of the quantitative analysis leads to a selection effect that suppresses the effect of good governance. If this assumption holds, then good governance emerges as one of the most important factors shaping donors' decisions about the proportion of aid delivered as budget support. This is a positive finding, albeit a tentative one, as it suggests that while donors are influenced by their own self interests in deciding who should get budget support, they pay more attention to good governance (and thus, their own policies) when it comes to deciding how much budget support those countries should get.

It is clear that there is substantial continuity in the allocation of budget support, both at the eligibility and proportion stages. One possible explanation for this is bureaucratic inertia in the aid allocation process, something that arguable should be expected in the case of budget support due to the mechanics of this aid modality. Yet bureaucratic inertia, a term used in previous research⁸⁴, is somewhat vague and pejorative, implying that donor agencies are inefficient and insufficiently responsive to change. Qualitative evidence gathered in interviews with donor staff helps to illuminate this issue, suggesting that the idea of bureaucratic inertia masks the interaction of a number of factors. These include the mechanics of budget support, the desire to be a good donor, a fear of undermining bilateral relationships with recipient governments and the difficulty of detecting and measuring change circumstances, particularly political changes.

84 Dietrich, "Bypass or Engage?".

On the whole, the evidence presented in this paper suggest that donors are largely compliant with their own policies on the allocation of budget support. They are more likely to give budget support to poorer countries, those with better governance and those whose spending habits reflect pro-poor policies. Donors also tend to give these countries a greater proportion of aid as budget support. Despite this, several important qualifications must be made. The first is that donors are not more likely to give budget support to more aid dependent countries, nor do they give a greater proportion of aid as budget support to aid dependent countries that pass the eligibility phase. In fact, more aid dependent countries get less budget support. On the surface this is worrying: aid dependent countries are precisely those countries where a shift towards budget support it most needed in order to reduce the corrosive effects that aid dependency has on local ownership of development, aid effectiveness and accountability to local citizens. However this result may be the product of limits on recipients ability to absorb aid flows, limits that are more likely to come into play in highly aid dependent countries.

The second qualification that must be made relates to democracy and human rights. With the exception of civil liberties, which have an unexpected and negative effect on eligibility for budget support, none of the measures of regime type or human rights were statistically significant. This does not necessarily mean that donors are ignoring these factors, or their own policies, which generally do not identify democracy and human rights as hard or strict requirements for the allocation of budget support. It may, however, be a sign that donors are more responsive to changes in these measures than to their absolute levels. This would be consistent with several donor policies which make express reference to the importance of changes or trends with respect to democracy and human rights. The importance of change in shaping the allocation of budget support warrants further research. Unfortunately, the limitations of the dataset employed in this study prevent it at present. The data on budget support is restricted to 2010 and 2011. Any attempt to analyse responses to change would generate results driven by the handful of cases where these was change in democracy and/or human rights between 2010 and 2011. Such results are unlikely to be robust.

Another qualification to be made is that the unexpected negative impact of civil liberties on donors' decisions about eligibility for budget support suggests that the models presented in

this paper omit some relevant variables. In particular, they suggest that donors may have particular strategic interests which lead them to disregard concerns about civil liberties when they decided which countries will receive budget support. This unexpected result also raises the possibility that OECD-DAC donors are using budget support as an incentive for political reform. This possibility is concerning as there is scant research on the political effects of budget support. The limited research that does exist tends to suggest that budget support is of limited utility in democracy promotion⁸⁵. If donors are using budget support to create incentives for political reform, they are likely to be disappointed with the results.

Additional qualifications and implications emerge from interviews conducted with donor agency staff. The first is that several important 'donor side' variables are missing from the quantitative models. The interviews make it clear that the level of public support for development aid, the economic situation of the donor, and the extent of media coverage of scandals and crises in the recipient country are important, and that there is a substantial degree of interaction between these three variables. Ideally, the statistical models would be revised to remedy this defect. While time and data constraints prevent that in the case of this paper, it remains an area to be addressed in future research. The second qualification to emerge from the interviews is that there is a substantial degree of interdependence between donor decisions about budget support, particularly decisions to suspend it. On one hand, this is good news as it suggests that donor efforts to improve coordination, such as attempts to implement the OECD-DAC Governance Network's Principles on Anti-Corruption, are working. On the other hand, it is bad news as the statistical methods employed in this paper assume that each allocation observed in the data-set is independent of others. This is a problem that pervades comparative politics, but which has no easy solutions⁸⁶. As such, additional caution is warranted in relying on the statistical results.

85 Development Information Services, "General Budget Support: Key Findings of Five USAID Studies," in *Budget Support as More Effective Aid? Recent Experiences and Emerging Lessons*, ed. Stefan Koeberle, Jan Walliser, and Zoran Stavreski (Washington D.C.: World Bank Publications, 2006), 105–120; Rachel Hayman, "Budget Support and Democracy: a Twist in the Conditionality Tale," *Third World Quarterly* 32, no. 4 (2011): 673–688, doi:10.1080/01436597.2011.566998.

86 Adam Przeworski, "Is the Science of Comparative Politics Possible?," in *The Oxford Handbook of Comparative Politics*, ed. Carles Boix and Susan Carol Stokes, Oxford Handbooks of Political Science (Oxford: Oxford University Press, 2009), 147–171.

Ultimately, the evidence presented in this paper indicates that donor behaviour is broadly consistent with donor policies. Yet that evidence also makes it clear that several factors not mentioned in policies have an important influence on the allocation of budget support. In some cases, these appear to be more influential than factors such as good governance, pro-poor policies, and respect for human rights. At a time when disillusionment with budget support is growing, fuelled by its disappointing returns in terms of governance and political reform, this begs the question of whether the problem is the modality, or the manner in which it is being allocated by donors.

Appendix A: Countries included in the dataset

<i>Donors</i>	<i>Recipients</i>	
Australia	Afghanistan	Malawi
Austria	Angola	Mali
Belgium	Armenia	Marshall Islands
Canada	Bangladesh	Mauritania
Denmark	Belize	Micronesia
Finland	Benin	Moldova
France	Bhutan	Mongolia
Germany	Bolivia	Morocco
Greece	Burkina Faso	Mozambique
Iceland	Burundi	Myanmar (Burma)
Ireland	Cambodia	Nepal
Italy	Cameroon	Nicaragua
Japan	Cape Verde	Niger
Korea (South)	Central African Rep.	Nigeria
Luxembourg	Chad	Pakistan
The Netherlands	Comoros	Papua New Guinea
New Zealand	Congo, Dem. Rep.	Paraguay
Norway	Congo, Rep.	Philippines
Portugal	Cote d'Ivoire	Rwanda
Spain	Djibouti	Samoa
Sweden	Egypt	Sao Tome & Principe
Switzerland	El Salvador	Senegal
United Kingdom	Equatorial Guinea	Sierra Leone
United States of America	Eritrea	Solomon Islands
	Ethiopia	Somalia
	Fiji	South Sudan
	Gambia	Sri Lanka
	Georgia	Sudan
	Ghana	Swaziland
	Guatemala	Syria
	Guinea	Tajikistan
	Guinea-Bissau	Tanzania
	Guyana	Timor-Leste
	Haiti	Togo
	Honduras	Tonga
	India	Turkmenistan
	Indonesia	Tuvalu
	Iraq	Uganda
	Kenya	Ukraine
	Kiribati	Uzbekistan
	Korea, Dem. Rep.	Vanuatu
	Kosovo	Vietnam
	Kyrgyz Republic	West Bank & Gaza Strip
	Laos	Yemen
	Lesotho	Zambia
	Liberia	Zimbabwe
	Madagascar	

Appendix B: Building an index of good governance

Table 5 Correlations between Worldwide Governance Indicators

	Political stability	Government effectiveness	Regulatory quality	Control of corruption	Rule of law
Political stability	1.000				
Government effectiveness	0.379***	1.000			
Regulatory quality	0.170***	0.756***	1.000		
Control of corruption	0.614***	0.735***	0.494***	1.000	
Rule of law	0.652***	0.769***	0.565***	0.819***	1.000

Cells contain Pearson's R. Shading identifies the indicators included in the index of good governance.
 *** p<0.001

Appendix C: The effect of dropping spending variables

Table 1A Eligibility for budget support in 2011, omitting spending variables

	(1)	(2)	(3)	(4)
Donor share of aid	0.037*** (5.82)	0.003 (0.34)	0.036*** (5.44)	0.00002 (0.00)
Trade (logged)	0.104** (2.82)	0.094† (1.87)	0.094* (2.49)	0.073 (1.48)
Colony	0.834*** (4.36)	0.827*** (3.65)	0.893*** (4.53)	0.874*** (3.77)
Aid dependency	-0.007 (-1.44)	-0.007 (-1.11)	-0.007 (-1.46)	-0.006 (-0.88)
GDP per capita, PPP (logged)	-0.656*** (-6.01)	-0.347* (-2.46)	-0.638*** (-5.85)	-0.300* (-2.16)
Population (logged)	0.144* (2.54)	0.040 (0.54)	0.145* (2.41)	0.045 (0.58)
Political stability	0.554*** (5.06)	0.340** (2.59)	0.541*** (4.90)	0.301* (2.24)
Good governance	0.631** (3.16)	0.223 (0.87)	0.623*** (3.41)	0.113 (0.49)
Political terror	-0.031 (-0.33)	0.002 (0.01)	-0.047 (-0.53)	0.020 (0.17)
Political rights (FH)	-0.048 (-0.80)	0.028 (0.36)		
Civil liberties (FH)	0.051 (0.52)	-0.090 (-0.71)		
Democracy (PolityIV)			-0.005 (-0.44)	-0.007 (-0.55)
Budget support 2010		2.239*** (14.59)		2.253*** (14.37)
<i>N</i>	1826	1826	1719	1719
Pseudo R ²	0.264	0.545	0.249	0.536
Log likelihood	-329.608	-203.712	-322.736	-199.673
Correctly predicts receipt of budget support (% cases)	22.79	72.79	25.00	73.53

Figures in cells are probit regression coefficients. Figures in parentheses are t statistics.

† p<0.1 * p<0.05, ** p<0.01, *** p<0.001

Table 1B Eligibility for budget support in 2011, omitting spending variables but retaining the same sample

	(1)	(2)	(3)	(4)
Donor share of aid	0.036*** (4.48)	-0.007 (-0.66)	0.037*** (4.62)	-0.005 (-0.44)
Trade (logged)	0.118* (2.56)	0.133* (2.10)	0.107* (2.38)	0.118† (1.91)
Colony	0.790*** (3.52)	0.572* (2.11)	0.797*** (3.56)	0.571* (2.12)
Aid dependency	-0.015* (-2.09)	-0.017 (-1.49)	-0.013† (-1.85)	-0.015 (-1.30)
GDP per capita, PPP (logged)	-0.739*** (-5.17)	-0.460* (-2.40)	-0.708*** (-5.03)	-0.419* (-2.24)
Population (logged)	0.109 (1.58)	-0.003 (-0.03)	0.117† (1.69)	0.013 (0.15)
Political stability	0.404** (3.08)	0.151 (0.94)	0.379** (2.88)	0.128 (0.79)
Good governance	0.629** (2.60)	0.103 (0.32)	0.497* (2.34)	-0.096 (-0.35)
Political terror	-0.192† (-1.71)	-0.162 (-1.12)	-0.127 (-1.15)	-0.076 (-0.54)
Political rights (FH)	0.098 (1.33)	0.149 (1.53)		
Civil liberties (FH)	-0.219† (-1.67)	-0.302† (-1.72)		
Democracy (PolityIV)			-0.012 (-1.02)	-0.009 (-0.58)
Budget support 2010		2.288*** (12.65)		2.270*** (12.65)
<i>N</i>	1242	1242	1218	1218
Pseudo R ²	0.215	0.520	0.208	0.513
Log likelihood	-251.466	-153.801	-252.187	-155.041
Correctly predicts receipt of budget support (% cases)	12.36	67.42	12.36	71.91

Figures in cells are probit regression coefficients. Figures in parentheses are t statistics.

† p<0.1 * p<0.05, ** p<0.01, *** p<0.001

Table 4A Proportion of bilateral ODA provided as budget support in 2011, omitting spending variables but retaining the same sample

	(1)	(2)	(3)	(4)
<i>Budget support in 2011 (% ODA from donor)</i>				
Donor share of aid	-0.0518 (-0.18)	-0.0993 (-0.46)	-0.0506 (-0.18)	-0.114 (-0.54)
Trade (logged)	-0.256 (-0.13)	2.206 (1.46)	-0.210 (-0.11)	2.213 (1.49)
Colony	0.682 (0.11)	-2.245 (-0.48)	0.333 (0.05)	-1.971 (-0.43)
Aid dependency	-0.680 (-1.23)	-0.716† (-1.73)	-0.684 (-1.24)	-0.694† (-1.68)
GDP per capita, PPP (logged)	-13.93* (-2.07)	-11.15* (-2.21)	-14.48* (-2.21)	-10.71* (-2.17)
Population (logged)	-0.881 (-0.31)	-4.339* (-2.02)	-0.539 (-0.19)	-4.406† (-1.97)
Political stability	4.969 (1.12)	-1.496 (-0.44)	5.665 (1.26)	-1.571 (-0.45)
Good governance	20.72* (2.31)	6.995 (1.01)	20.95** (2.77)	7.760 (1.32)
Political terror	0.595 (0.15)	0.011 (0.00)	0.704 (0.20)	-0.407 (-0.15)
Political rights (FH)	1.500 (0.54)	-1.327 (-0.63)		
Civil liberties (FH)	-0.997 (-0.19)	1.720 (0.44)		
Democracy (PolityIV)			0.333 (0.73)	-0.107 (-0.31)
Budget support 2010 (%)		0.679*** (7.93)		0.671*** (7.95)
constant	161.0 (1.61)	183.8* (2.46)	160.7 (1.69)	185.5* (2.60)
<i>N</i>	90	90	90	90
Adjusted R ²	0.135	0.518	0.145	0.522

Figures in cells are OLS regression coefficients. Figures in parentheses are t statistics.

† p<0.1* p<0.05, ** p<0.01, *** p<0.001

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