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EXPLORING THE EMERGENCE OF A NEW AID REGIME: SELECTIVITY, KNOWLEDGE AND THE WORLD BANK

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Abstract

This thesis focuses on the redefinition of conditionality away from finance for the promise of policy reform to disbursement of funds conditional on what has already been achieved, 'selectivity'. This has dovetailed with a self-assigned knowledge role for the donor community, especially the World Bank. These shifts are set in the political, economic and financial realities bearing upon aid in general, and around the World Bank in particular, and against the backdrop of a projected move away from the Washington Consensus towards a more 'holistic' approach to development associated with the post-Washington Consensus and the Comprehensive Development Framework.

The study closely examines how aid, development and knowledge are understood in the economic propositions drawn upon to support the new aid paradigm. The implications for the realities of development – particularly in those countries that remain dependent on aid for their access to external finance – are explored. Special attention is given to the World Bank's assessment tool at the core of its aid allocation mechanism, the Country Policy and Institutional Assessment (CPIA), and how this sits within the evolving understanding of development projected by the World Bank. This reveals the persistence of the Washington Consensus agenda at the core of World Bank practices, often at variance with its rhetoric. Recent shifts in the CPIA indicate how these imperatives have become more entrenched and less visible in World Bank practices, veiling the contradictions resulting from the conjunction of its discursive shifts and the persistence of a set of economic and financial imperatives. Through both CPIA-steered selectivity and the exercise of the World Bank's knowledge role, a much tighter, yet less visible web of control has been spun over policymaking in low income countries despite the oft-reiterated commitment to 'ownership' and 'partnership' principles.

In the memory of my father, Luc Van Waeyenberge.

But, for Jawad

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This thesis was embarked upon in the wake of the sudden loss of my father, Luc. The mourning process became laced within the work, often preventing swifter progress. The thesis has now finally been completed and with it a page has been turned. It is in the memory of my father that my thesis was written, but I dedicate it to Jawad, in tribute to his resilience.

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List of Abbreviations

AA Assessing Aid
AAA Analytical and Advisory Activities
AARIA Aid and Reform in Africa
ABCDE Annual Bank Conference on Development Economics
ABR Administrative Barrier Report
ADF Asian Development Fund
AfDF African Development Fund
ARPP Annual Report on Portfolio Performance
BCP Basle Core Principles
bn billions
BW Bretton Woods
CAS Country Assistance Strategy
CDF Comprehensive Development Framework
CEM Country Economic Memorandum
CFAA Country Financial Accountability Assessment
CPAR Country Procurement Assessment Review
CPIA Country Policy and Institutional Assessment
DAC Development Assistance Committee
DEC Development Economics Vice-Presidency of the World Bank
DfID Department for International Development
DGF Development Grant Facility
DPL Development Policy Lending
DPR Development Policy Review
DRC Democratic Republic Congo
DSF Debt Sustainability Framework
EC European Community
EDI Economic Development Institute
ESAF Enhanced Structural Adjustment Facility
ESW Economic and Sector Work
FDI Foreign Direct Investment
FI Financial Institutions
FIAS Foreign Investment Advisory Service
FY Fiscal Year
GCF Gross Capital Formation
GDP Gross Domestic Product
GDLN Global Development Learning Network
GDN Global Development Network
GDG Global Development Gateway
GE General Equilibrium
GMM Generalised Method of Moments
GNI Gross National Income
HD Harrod-Domar
HFI Heritage Foundation Index
HIPC Highly Indebted Poor Country
IBRD International Bank for Reconstruction and Development
ICA Investment Climate Assessment
ICT Information and Communication Technology
IDA International Development Association
IFC International Finance Corporation
IFI International Financial Institution

IPG International Public Good
IMF International Monetary Fund
JICA Japan International Cooperation Agency
LDC Least Developed Country
LIC Low Income Country
LICUS Low Income Country under Stress
LMIC Lower Middle Income Country
MCA Millennium Challenge Account
MDB Multilateral Development Bank
MDG Millennium Development Goal
MDRI Multilateral Debt Relief Initiative
MIC Middle Income Country
MIGA Multilateral Investment Guarantee Agency
mn millions
NGO Non-Governmental Organisation
NIFA New International Financial Architecture
OBA Output Based Aid
ODA Official Development Assistance
OECD Organisation for Economic Cooperation and Development
OECF Overseas Economic Cooperation Fund
OED Operations Evaluation Department
OLIC Other Low Income Country
OLS Ordinary Least Squares
PA Poverty Assessment
PBA Performance Based Allocation
PER Public Expenditure Review
PCPI Post-Conflict Progress Indicators
PFM Public Financial Management
PRGF Poverty Reduction and Growth Facility
PREM Poverty Reduction and Economic Management network
PR Performance Rating
PRS Poverty Reduction Strategy
PRSC Poverty Reduction Strategy Credit
PRSP Poverty Reduction Strategy Paper
PSD Private Sector Development
PSIA Poverty and Social Impact Analysis
PWC post-Washington Consensus
RAD Researchers' Alliance for Development
RDB Regional Development Bank
RER Real Exchange Rate
RHS Right-Hand Side
ROSC Reports on the Observance of Standards and Codes
SAF Structural Adjustment Facility
SAL Structural Adjustment Loan
SAP Structural Adjustment Programme
SDR Special Drawing Right
SECAL Sectoral Adjustment Loan
SME Small and Medium Enterprise
SSA Sub-Saharan Africa
TA Technical Assistance
TC Technical Co-operation
UMIC Upper Middle Income Country

UN United Nations
US United States (of America)
WC Washington Consensus
WDR World Development Report
WB World Bank
WBG World Bank Group
WBI World Bank Institute
WTO World Trade Organisation
2SLS Two-Stage Least Square

Introduction. Realities of aid at the start of the millennium

The 1990s saw dramatic changes in development finance. Aid flows fell rapidly during the 1990s, after having reached a peak at the start of the decade. The aid effort, measured as a share of donors' national income, reached an all-time low in 2000. Further, while official flows accounted for over half of total net long-term flows to developing countries at the start of the 1990s, this fell to just over a third at the turn of the millennium.

Since 2002, however, there seems to have been a renewal of official interest in aid. The United Nations (UN) Millennium Summit in 2000 put forward a set of minimum targets, the Millennium Development Goals (MDGs), to be achieved by 2015 in poverty, education, health, child and maternal mortality, gender and the environment. In March 2002, a follow-up UN conference in Monterrey addressed the challenges of financing the development priorities embodied in the MDGs. It was recognised that donors needed to set more ambitious targets for aid, and members of the OECD's Development Assistance Committee (DAC) announced plans to expand Official Development Assistance (ODA). Aid subsequently increased by 16 percent in real terms between 2001 and 2004 (OECD 2006b).

Yet, as illustrated in the first chapter of this dissertation, the recent increases in aid have been steered predominantly by donors' special interests, and donors' commitment to the public financing of development has in effect consistently weakened since the early 1990s. A belief in, and a commitment to, the potential of private flows to finance development – now projected as a superior substitute for aid – has come to prevail in the donor community. The essential purpose of development cooperation has become to foster the emergence of 'competent societies' (OECD 1998, p. 18). Aid is to fill *institutional* rather than *financial* gaps as it is to be *primarily* used to improve domestic investment climates in developing countries and to be targeted both at building institutional and human capacity and liberalisation (DAC 2002, p. 2). ODA has become key in leveraging private finance for the major investments needed in infrastructure, health and education; and mechanisms such as public-private partnerships are to be instrumental in pooling the necessary (often foreign) resources for such investments. The *1997 Development Cooperation Report* (OECD 1998, pp. 43-6) argued as follows:[1]

[1] It can be noted that although this report was published in the immediate aftermath of the East Asian financial crisis, it contained almost no reference to the risks involved in financial market integration, indeed including much to the contrary. On these risks, see, among others: Furman and Stiglitz (1998);

> Building robust and versatile financial systems which can effectively mobilise and invest rising domestic savings and private capital inflows is essential to poverty reducing economic growth and must now be a central priority for capacity building cooperation in all developing countries, including the poorest ... A new phase of international system building has been inaugurated in the financial area, designed to provide the basis for all countries to integrate effectively into a well-functioning global financial market ... As this programme is carried through, it will enable developing countries to shift further to a pattern of development financing reflecting a private-sector-based economy. Concessional aid will continue to have an important role in strengthening the development process in contexts of greatly improved developing-country policy environments, but high levels of aid dependence should progressively come down, with aid finding its proper place as a strategic complement to, rather than a substitute for, domestic resource mobilisation and private capital inflows.

The Report continued (p. 48):

> the understanding of what successful development involves has changed, and together with the shift to market-based economic strategies and the extended reach of international financial markets, filling 'financial gaps' is no longer seen as the starting point for determining the role of aid. Rather development is seen to depend on a sound policy framework, strong investment in human capital, the fostering of effective institutions in the state and the private sectors and an active civil society. The role of aid is to invest in these fundamental determinants of development wherever this can be effective.

Significantly, the Monterrey Consensus (UN 2002) embedded the premise that financing for development is increasingly to be extracted from international capital markets. It prescribed how, in order to overcome high levels of poverty, developing countries must be in a position to attract private international capital flows by attempting to achieve a transparent, stable and predictable investment climate with special attention to property rights and business-friendly macroeconomic policies and institutions. A mainly residual and auxiliary role for aid emerges as part and parcel of the rapid expansion of private financial flows, with an emphasis on its role in

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Rodrik and Velasco (2000); Stiglitz (2000c); Demirgüç-Kunt and Detragiache (2001); Eichengreen (2002). For a brief systemic account of the various implications of financial market integration for growth and development in the South, see Wade (2006).

'capacity' or 'institution' building, promoting an enabling environment for private investment, both domestic and foreign.

Nevertheless, while donors increasingly see the role of aid as residual in the context of private finance, their ambitions to intervene in the economics (and politics) of less developed countries and, in particular, of those countries most dependent on aid for their access to external finance, have not been concomitantly downscaled. On the contrary, aid discourse and practices have become increasingly concerned with engineering recipient countries' domestic policies and institutions – within and beyond the traditional realm of economics.

We perceive this as particularly emblematic with the shift in conditionality that has characterised aid relations – away from a traditional conditionality, based on finance in return for the promise of policy reform, towards a conditionality where the disbursement of funds becomes conditional on what has already been achieved in terms of policy and institutional reform ('selectivity'); and in the combination of this shift with a self-assigned knowledge role for the donor community, and for the World Bank (WB) as a lead institution in particular. A new aid regime is taking form which appears to mark a shift away from coercion as a mechanism to impose a set of reforms towards more subtle means of influence.[2]

The aim of this dissertation is to examine critically this redefinition of aid engagement. Such an endeavour raises a set of issues. What is the relationship between the current and preceding approaches to aid? How does the shift sit with underlying changes in political, economic and financial circumstances? How does it accommodate various contradictory pressures bearing upon aid and the WB? How does it relate to the alleged move forward from the Washington Consensus (WC) as projected by the donor community, and again the WB in particular? What are the analytical foundations of the new approach? What are the implications of the latter for the study of aid? And what are the implications for the realities of development? The dissertation, then, straddles issues of rhetoric, analysis and practice as different dimensions of a particular aid moment or paradigm. Scrutinising the relationships and contradictions between these allows teasing out certain fundamental imperatives driving aid. These have a bearing, in particular, on the poorer countries that remain dependent on aid for their access to external finance and in which aid tends to

[2] We follow Gibbon (1993) who uses the term 'aid regime' following Bonne (1989, pp. 38-44) to refer to the system of principles, norms, rules and decision-making procedures governing the regulation of ODA.

account for a large share of domestic capital formation (and government expenditure).

At its core, the dissertation exposes the persistence of a particularly pernicious policy agenda promoted through aid and draws attention to the less visible, more embedded, yet relentless, manner in which this now affects a set of countries. Growing opposition faced by the Bank over its core neo-liberal agenda during the 1990s, and the growing legitimacy crisis of the neo-liberal agenda more generally, seem to have produced a transformation of the mechanisms through which a core agenda – pursued at the behest of leading WB donors – is transmitted. A less broad-swaying and more customised approach, in which the ideational role of the Bank moves centre stage, serves to take the implementation of the neo-liberal order further – while seeking to accommodate the political and financial constraints bearing upon the Bank (and upon aid more generally). A rationing approach to aid further reinforces this ideational role.

Following a close examination of how aid, development and knowledge are understood in the economic propositions drawn upon to support the new aid paradigm, this dissertation denounces the persistent failings to accommodate the defining features of these particular phenomena, and the opportunistic use to which analytical propositions have easily been put. The analytical deconstruction of the paradigm shift benefits from a set of insights, both specific to the aid literature and pertaining more generally to the critical commentary on mainstream economics. These include Joel Samoff's (1992) notion of the financial-intellectual complex which refers to repercussions for both research and development stemming from the conjunction of funding and research. Research undertaken under such an aegis is often relatively narrow and easily takes the 'existing patterns of economic, political and social organisation as givens' (p. 60). The process of knowledge creation is often obscured and the power relations embedded in the research and the programmes it supports mystified. Particular understandings are privileged and attention is often diverted away from alternative understandings or perspectives.[3] Further, Ben Fine's (1997, 2001a, 2002a) work on economics imperialism provided a particularly valuable guiding principle in the assessment of the mainstream attempts to deal with the analytics of development, aid, conditionality and knowledge.

[3] More recently, see the various observations in Mehta (2006) for a denunciation of the pervasiveness of the aid industry for determining the directions within research on development; and Mosse (2006) for an account of the hazards confronted by an anthropologist who drew on his experience in the pay of a bilateral donor agency (here the British aid agency) to author a book critical of international development policies and practices.

Additionally, an important proviso is crucial at the outset regarding the scope of the research. This dissertation aims to scrutinise shifts in the prevailing aid paradigm and examine the broad implications thereof for the understanding of aid and for the realities of development (in a set of countries). However, it only explores the latter at a *general* and *external* level, in that it considers how aid *seeks* to impose a particular policy agenda and the changes in the mechanisms through which influence is exercised. Such an analysis does not allow for inference regarding the ultimate reality of policies in developing countries, which depend on a host of additional factors. As put most recently by Castel-Branco (2007, p. 23), following Wuyts (1991):

> [The] partner of aid dependence is not only built from outside but is also the result of domestic crisis, context, conflict and established interests reacting to the local crisis and its international context.

It is repeatedly argued in this dissertation that policy outcomes at the domestic level are the result of complex dynamics, including those related to international and domestic actors, as well as specific socio-economic and historical factors. The implications for actual policy outcomes need case-by-case and specific investigation.

The research for this dissertation was done on the basis of extensive consultation of manifold documents produced by the donor community, with a focus on the WB. As part of its bid towards greater transparency, the Bank has increased the remit of documents that are publicly available, mainly through its external website. A unique opportunity to have a closer insight into shifts in Bank operational realities on the basis of text-based analysis, furthermore, arose when the Bank decided, in 2000, to disclose a set of documents relating to the method through which it allocates its aid flows. This was particularly opportune in the context of the current research endeavour as it now became possible to explore the meaning of the selectivity and knowledge paradigm through a closer look at the Bank's core operational tool for allocating aid, the Country Policy and Institutional Assessment (CPIA). As such, the disclosure potentially provided scope to confront the prevailing constraint on the use of text-based analysis when studying the WB, and particularly changes in its operational practices (see Stone 2007, p. 15).

The predominantly text-based analysis was complemented as follows. At the early stages of the research, I had the opportunity to be a non-participant observer at a High Level joint WB/DfID Technical Workshop in London entitled *Enhancing the*

Country Performance Assessments and taking place under the broader theme of *Aligning Aid Strategies to Performance in Low-Income Countries* (March 1999). The main purpose of the workshop was to familiarise a broad array of donor agencies with the Bank's selectivity method and its core tool, the CPIA.[4] It indicated a clear desire on behalf of the Bank to start actively promoting its approach across the broader donor community and provided me with a good initial opportunity to observe how the Bank understood selectivity as a way to allocate aid flows, and to gain insight into the Bank's aid allocation mechanism – centred on the CPIA – which was not yet in the public domain.

As the research for this thesis drew to a close two opportunities were provided which, in a way, allowed me to put to a test the various ideas that had been formed along its trajectory. First, in September 2006, I participated in a workshop on the WB which was part of a series of events seeking to provide 'early career researchers' with an opportunity 'to interact with peers working on related topics as well as a chance to get some feed-back from Bank staff' (Stone 2007, p. 15). This workshop was convened at the National University of Singapore, funded through an 'impacts grant' of the UK Economic and Social Research Council, and organised by the Centre for the Study of Globalisation and Regionalisation (University of Warwick) – *yet* with the assistance of the Researchers' Alliance for Development (RAD), a Bank 'knowledge initiative' that had been informally initiated, in 2004, by the Bank's External Affairs department (Paris office). The occasion hence served a two-fold purpose for me: it provided a platform to share my research results with peers and Bank staff; but it also provided an opportunity to have a closer encounter with an instance of the Bank's rapidly expanding engagement in knowledge activities, of which the RAD is but one.

Secondly, in April 2007, I was given the opportunity to participate in a workshop led by Ravi Kanbur and hosted by the Initiative for Policy Dialogue, which was devoted to the CPIA. At the instigation of Joe Stiglitz, himself a former WB Chief Economist, a broad spectrum of people who had an interest in the CPIA were brought together. This included a significant WB contingent; ex-Bank staff who, like Ravi Kanbur, had been closely involved with the CPIA while employed at the Bank; and a host of people from other multilateral organisations, NGOs and

[4] The following bilateral and multilateral donors were present: Canada, Denmark, Sweden, USA, Netherlands, Switzerland, France, Germany, UK; African Development Bank, Asian Development Bank, DG-VIII of the European Commission, and the UNDP. Developing country representatives from Bangladesh, Nepal, Uganda, Zambia as well as a few NGO representatives also attended.

academia. Informal conversations with Bank staff, as well as various exchanges during the workshop provided a valuable final feedback mechanism as I was tying together my research conclusions.[5]

The dissertation proceeds as follows. Chapter one documents the transformations that have characterised the nature of net long-term flows to developing countries over the last fifteen years. It highlights how high-income countries' commitment to concessional flows has waned significantly since the early 1990s – notwithstanding a recent apparent upturn – and how, at the same time, private flows have expanded rapidly. These trends are set against the persistent importance of aid as a source of external finance for the bulk of low income countries (LICs). The chapter goes on to argue that as the donor community's willingness to pay declined, their interventionist ambitions increased and the disciplinary power of ODA in the poorer aid recipients was tightened. This is understood to transpire from a set of practices, most notably performance-based aid allocations (or 'selectivity'), but also from the emphasis on capacity-building and, if seemingly paradoxically, on partnership and ownership. Selectivity is situated amongst these shifts in aid practices bearing upon the sectoral allocation of aid, the composition of aid, and the processes that seek to institutionalise 'participation'.

Chapter two explores the repercussions for the WB – as a lead institution – of the particular trends in development finance documented in chapter one. The Bank has aspired to a leadership role in both the intellectual and policy realms of economic development since the McNamara Presidency (1968-1981). The 1980s saw a conjunction of events that promoted such a role for the Bank and, by the early 1990s, it attained leadership in an 'aid regime' structured around its identified priorities. Attention is then drawn to the Bank's celebration of 'knowledge as aid' in the late 1990s, which originated in the Bank's response to a set of contradictory developments, and which rapidly acquired resonance in the broader donor community. The vastly expanding knowledge exercise of the Bank is elaborately documented and we point, in particular, to the large knowledge endeavour originating in the Bank's operational departments as well as to the various 'global

[5] Informal telephone and email conversations with Bank staff were also occasionally undertaken, when certain operational issues remained thoroughly unclear from the various documents consulted. These were not always successful, as on one occasion I received an email reply from a Bank employee stating that: 'Unfortunately we are not staffed to furnish information to PhD students' (email communication 6/12/2006).

knowledge initiatives'. This is accompanied by a critical deconstruction of the Bank's own understanding of its self-declared knowledge mission denouncing the ahistorical, asocial and apolitical character of its conception and exposing a set of parameters persistently bearing upon the Bank's knowledge exercise.

Chapter three goes on to explore the particular attempts projected by the Bank to re-engage with the complexities of development that accompanied the knowledge celebration. By the late 1990s, official representations from the Bank sought to infuse its development discourse with a recognition of the inadequacy of the previous approach to development that had come to be summed up as the WC. Following the latter, development was reduced, in essence, to some alleged restoration of price incentives and macro-economic balance. With the Comprehensive Development Framework (CDF) and the post-Washington Consensus (PWC), an attempt was made to propel the analysis of development forward – beyond a stabilisation and price bias – to include such phenomena as persistent market failures and non-market (non-state) institutions; and to portray development as a transformation of society requiring a broad-based approach. While serving to bestow the self-declared knowledge role with a better semblance of legitimacy than would have been purveyed by the WC, the new propositions suffered from the persistent inadequacies resulting from the underlying method. The social still comes about as a result of optimisation exercises under a set of constraints, and the analytical focus remains confined to the realm of exchange to the detriment of the realm of production.

Chapter four delves into the analytical propositions that accompanied the aid policies and practices preceding the selectivity and knowledge paradigm. Within this 'old economics of aid', a distinction is made between the literatures on fungibility and conditionality. It is argued that, despite various attempts at bringing new explanatory variables into the analysis, the old economics persistently fails to account for the essential and defining features of aid, conditionality, development, and their interaction. As a result, after almost four decades of research, the conclusions of the literature remain ambiguous, and the extent to which the various dimensions and institutions of aid have managed to restructure the recipient/debtor economies ill-recognised.

Chapter five illustrates how the shortcomings identified in chapter four were aggravated by the latest innovations in aid effectiveness research. The late 1990s saw a new surge of theorising about aid effectiveness. Its main impetus had been a renewed aid effectiveness research programme at the Bank which sought to put forward a set of formal arguments as to why aid should be allocated selectively to 'good' performers with an emphasis on the 'ideational' dimension of aid for other countries. The contribution by Burnside and Dollar (1997, 2000a) stood out, with the flagship report *Assessing Aid: What Works, What Doesn't and Why* (WB 1998a) being built around its central premise of conditional aid effectiveness. A critical literature emerged in response to the Bank-promoted arguments, revealing how the latter were based on a biased research effort, poor theoretical and econometric practice, and failed to reflect the broader findings regarding aid impact. It is argued, however, that this preoccupation within the aid effectiveness literature with the Bank's stance inadvertently anchored the latest theorising about aid in the conceptual framework implied by its premise, to the detriment of further insights into the dynamics of aid. The hazards of an aid allocation process based on the selectivity principle are further explored.

Chapter six ties the various observations made through chapters two to five together in an exploration of the assessment tool that sits at the core of the Bank's selective allocation mechanisms, the Country Policy and Institutional Assessment (CPIA). The CPIA emerges as a crystal through which the essence of the selectivity and knowledge paradigm can be observed. Although a formal link between staff assessments of prospective aid recipients' policies was initiated at the Bank in the late 1970s, the instrument has undergone dramatic changes over the last decade, both in scope and in how it relates to the Bank's aid allocation mechanism. Furthermore, since 2000, the Bank has sought to promote its assessment tool across the broader donor community, where it is rapidly becoming a benchmark. A brief overview of the CPIA is provided, which is followed by a detailed deconstruction of the policy matrix embedded in the tool. This gives rise to two main observations. First, the CPIA imposes an ahistorical policy and institutional straightjacket on LICs that remains informed by the WC, now augmented with apparent social and governance concerns. Secondly, recent changes in the CPIA indicate how some of these imperatives have become less visible, possibly in an attempt by the Bank to contain contradictions resulting from the conjunction of certain discursive shifts, as for instance through the post-WC, and the persistence of a set of economic (and financial) imperatives. This, again, draws attention to the importance of the Bank's analytical work in steering its interaction with clients and links back to the Bank's knowledge effort, extensively documented in chapter two.

The dissertation concludes with a brief overview of the main arguments put forward regarding the way in which aid interaction has been redefined over the last decade. It teases out implications for the critical study of aid realities and points to a set of possible future directions for research.

Chapter 1. The changing face of development finance

1.1 Introduction

The donor community's commitment to the aid enterprise has steadily eroded over the last fifteen years. Notwithstanding an apparent recent reinvigoration of aid, it has become increasingly marginalised amidst the fast, if not vast, expansion of private flows. While at the start of the 1990s official flows accounted for over half of total net long term flows to developing countries, by the turn of the millennium the share of official flows in net long-term flows to developing countries had fallen to just over a third. This reflects both a dramatic fall in aid effort and a rapid increase in private financial flows, with the latter mainly the result of specific policies enacted by major donor countries (or donor-controlled institutions). The surge in private flows has, nevertheless, bypassed a large of group of LICs.

This chapter seeks to document how the declining willingness to finance the aid enterprise has been accompanied by an attempt to increase its leverage, especially in those countries that remain dependent on aid. As indicated in the introduction, we see this as particularly emblematic with the redefinition of conditionality away from finance for the promise of policy reform, to the disbursement of funds conditional on what has already been achieved, or 'selectivity'; and the combination of this with a celebration of the knowledge of the donor community. These emphases sit together with a redefinition of the purpose of aid towards 'capacity building' and, if somewhat paradoxically, an insistence on 'ownership' and 'participation', most typically with the Poverty Reduction Strategy Paper (PRSP) initiative.

The chapter, first, provides a brief appraisal of changes that have characterised development finance since the early 1990s. Secondly, these changes are put against the backdrop of the persistent importance of concessional financial flows to the bulk of LICs. These countries set the scene for our investigation into the changing modalities of aid and we describe, thirdly, how something akin to a common framework, sometimes referred to as the 'new partnership model' (IDA 2007b, p. 1), is being created for aid-dependent countries, which can be seen as trying to enhance donor leverage. Its main features are, on the one hand, a greater exercise of selectivity in the allocation of aid flows on the basis of a set of predetermined policy and institutional norms, and, on the other, compulsory collaboration in 'participatory' initiatives. Meanwhile, a redefinition of the purpose of aid as auxiliary to the expansion of private flows has implied a pre-occupation with capacity-building, with specific repercussions for the sectoral composition and the preferred instruments of aid. The different aspects of this redefinition of aid engagement are explored in turn.

1.2 The demise of aid

The term 'development finance' is most commonly used to designate long-term financial flows to middle and LICs, with the destination of the flows rather than their projected purpose serving to categorise them. Within the composite term of development finance, distinctions are traditionally made between flows that originate in the public or private sector (official versus private flows), between those whose projected purpose is related to development (development versus other flows), and over the financial terms on which the flows are provided (concessional versus non-concessional flows). Several categories therefore emerge. These have been typically defined by the DAC, the principal body through which the OECD countries (which historically account for the bulk of flows to developing countries) seek to align their funding and technical assistance (TA) activities.

According to the DAC, ODA, or what is most commonly referred to as 'aid', designates those flows to developing countries (and multilateral agencies) which satisfy the following three criteria:[6] they are provided by the official sector; their main projected objective is the promotion of economic development and the welfare of the recipient country; and, they are provided at concessional financial terms. The last implies that for a loan to qualify as ODA it should carry a grant element of at least 25 percent, which is calculated on the basis of a 10 percent discount rate. In addition to financial flows, technical co-operation (TC) is included in aid. Grants, loans and credits for military purposes are excluded, and so are export credits.[7] [8]

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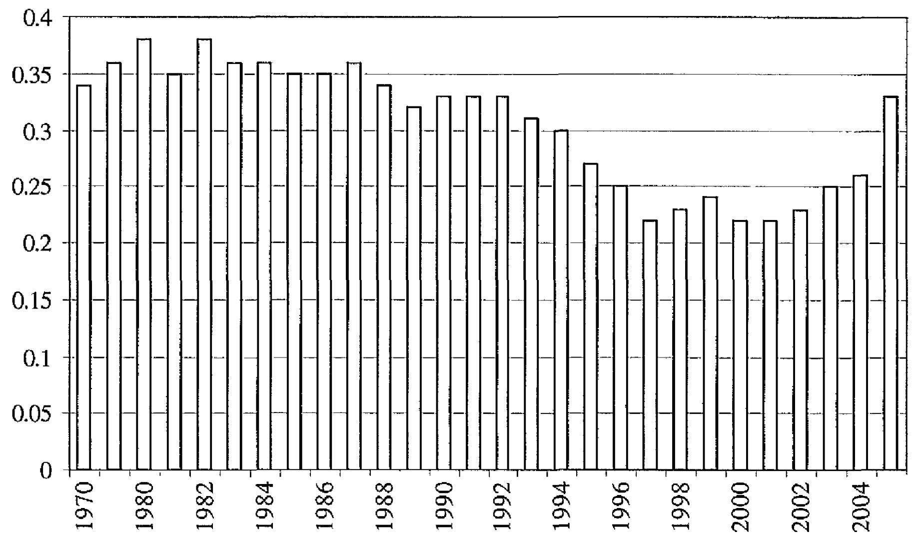
[6] To be precise, the DAC deploys two different designations – ODA and Official Aid – for flows that meet these specific criteria, depending on which countries are concerned. The DAC list of aid recipients distinguishes between Part I and Part II countries. The latter are referred to as 'countries in transition'. These include more advanced central and eastern European countries and the newly independent states of the former Soviet Union, as well as more advanced developing countries. The former group, Part I countries, comprise Least Developed Countries (LDCs); Other Low Income Countries (OLICs); Lower Middle Income Countries (LMICs); and Upper Middle Income Countries (UMICs) (OECD 1998).

[7] The WB's Global Development Finance refers to concessional flows rather than ODA and these exclude TC grants, which are included in the DAC's definition of ODA. The WB, further, compiles its information on the basis of data provided by debtor countries through the WB Debtor Reporting System, while the DAC compiles data on official development finance on the basis of information provided by donors to the DAC and through the Creditor Reporting System. For other differences between the DAC and the WB measures of official flows, see WB (1999f, pp. 78-90). For an assessment of the method used by the DAC to measure ODA, see Renard and Cassimon (2001).

[8] Since its inception, there have been a set of changes in the interpretation of the definition of ODA, some of which have tended to broaden the scope of the concept. The most noteworthy have been: the

For the last ten years, the aid effort has been low by historical standards. Figure 1.1 charts ODA as percentage of donor Gross National Income (GNI), between 1970 and 2005. The ODA/GNI ratio hovered around 0.35 percent between the early 1970s and the mid-1980s, and declined slightly during the late 1980s and early 1990s, when it still accounted for an average of 0.33 percent. However, it fell rapidly from the mid-1990s onwards and reached an all-time low of 0.22 percent in 2000. Only from 2002 do we see an improvement in the aid effort of DAC countries. The ODA/GNI ratio reached 0.26 percent in 2004, and provisional figures for 2005 indicate a further increase to 0.33 percent.

Figure 1.1: ODA from DAC donors as percentage of donor GNI, 1970-2005 (weighted average)



Source: OECD (various).

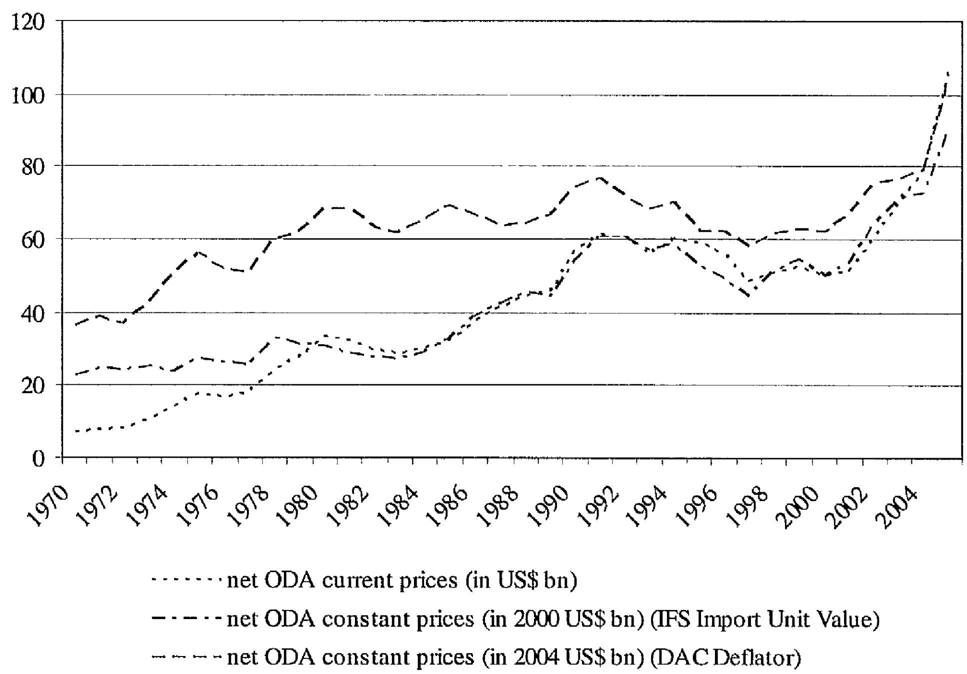
Various reasons have been put forward in the literature to account for the decline in aid effort during the 1990s. These mainly feature: the decline of political (geo-strategic) reasons for providing aid since the end of the Cold War; persistent tendencies to fiscal stringency in major OECD countries; growing concerns over the effectiveness of the aid endeavour; the re-definition of a global security agenda marked by concerns about the environment, refugees, organised crime and terrorism

recording of administrative costs as ODA since 1979; the imputation, as ODA, of the share of subsidies to educational systems representing the costs of educating students from aid recipient countries since 1984; and the inclusion of assistance provided by donor countries in the first year after the arrival of a refugee from an aid recipient country (eligible to be reported since the early 1980s, but widely used only since 1991) (OECD 1998).

threatening the case for long-term development assistance; and a general trend in major OECD countries to privatise various publicly undertaken activities implying a need for greater justification for a system whereby development in poor countries is assisted by large inflows of international public spending (see Hewitt 1994; OECD 1995; Raffer and Singer 1996; Ryrie 1995; Stokke 1996; Burnell 1997; Killick 1998; White 2002).

The decline in aid effort translated into absolute declines in aid. Figure 1.2 draws total net ODA between 1970 and 2005. Three series are charted: net ODA in current prices; net ODA deflated by a unit value index of imports for developing countries; and net ODA deflated by the DAC GNI deflator.[9]

Figure 1.2: Trends in net ODA to developing countries, 1970-2005, US$ billions



Source: OECD/DAC on-line database; IMF IFS on-line database.

The figure illustrates how total ODA expanded steadily between 1970 and the early 1990s to reach a high of US$ 60.9 billions (bn) in 1991. ODA subsequently fell rapidly between 1992 and 1997 to just over US$ 48 bn, a fall of over 25 percent in

[9] To present aid flows in real terms, the DAC uses a GNI-weighted average of all DAC donor currency-specific GNI deflators. The latter make adjustments for both inflation and changes in the exchange rate between the currency concerned and the US dollar. Alternatively, one can use an import unit price deflator for developing countries. The choice of deflator depends on whether one is interested in the value of aid from the point of view of developed or developing countries.

real terms. ODA started to recover at the turn of the millennium, and by 2004, it had been restored to its (real) 1991 level. Recent figures indicate a further increase in 2005 to US$ 106.4 bn. The trend in ODA has mainly been driven by bilateral ODA, with multilateral aid being more stable.[10]

Closer inspection of the recent recovery in ODA reveals the unfortunate persistence of the steady erosion of donors' commitment to the aid enterprise, donor posturing aside. First, much of the recent increase in aid has been steered by what are called 'special purpose grants', rather than by more flexible forms of funding for developing countries, and the bulk of the most recent increase can be accounted for almost entirely in terms of debt relief for Iraq (US$ 14 bn) and Nigeria (US$ 5 bn), and tsunami aid (US$ 2 bn) (WB 2006b).

Table 1.1 illustrates how special purpose grants, which comprise TC, debt relief, emergency relief, and administrative costs, have come to account, in 2005, for almost three-quarters of bilateral aid. Aid in the form of debt relief more than tripled between 2004 and 2005, and its share in total bilateral aid reached an exceptional high of one third in 2005. Emergency aid has also grown at a very fast pace since 1990 and now accounts, on average, for 10 percent of bilateral ODA. This is up from less than 3 percent in 1990. TC maintains a substantial and steady share in bilateral ODA, averaging a third over the last five years. Table 1.1 further indicates how, in absolute (real) terms, ODA net of purpose grants is still lower than it was in 1990. Moreover, relative to national income (of DAC member countries), ODA net of special purpose grants has declined over the past ten years, averaging 0.13 percent since the beginning of the millennium and remaining well below the 0.25 percent attained in the early 1990s.

[10] Although bilateral aid accounts for the bulk of ODA, the share of multilateral aid has steadily increased from a low of 10 percent at the beginning of the 1970s to approximately 20 percent at the beginning of the 1980s, 25 percent at the start of the 1990s, and has averaged 28 percent during the first half of the first decade of the millennium (see OECD 2006b).

Table 1.1: Net ODA and special purpose grants 1990-2005, US$ billions and percentages

	1990		1995		2000		2001		2002		2003		2004		2005	
	$bn	*(%)*	*$bn*	*(%)*	*$bn*	*(%)*	*$bn*	*(%)*	*$bn*	*(%)*	*$bn*	*(%)*	*$bn*	*(%)*	*$bn*	*(%)*
Total net ODA	57.0		59.0		49.8		51.6		60.2		70.4		79.0		106.4	
Bilateral ODA	38.5	67.5	40.5	68.6	36.1	72.5	35.1	68.1	40.8	67.7	49.8	70.7	54.3	68.8	82.1	77.2
Of which:																
- Debt relief	2.2	5.7	2.1	5.3	2.0	5.7	2.5	7.2	5.3	13.1	8.4	17.0	7.1	13.1	25.0	30.4
- TC	11.2	29.1	14.2	35.2	12.7	35.1	13.6	38.7	15.5	37.9	18.4	36.9	18.7	34.4	21.0	25.5
- Emergency assistance	1.1	2.8	2.9	7.1	3.4	9.4	3.3	9.3	3.9	9.5	6.2	12.5	7.3	13.5	8.7	10.6
- Administrative costs	2.0	5.1	2.9	7.1	3.1	8.5	3.0	8.4	3.0	7.4	3.5	7.1	4.0	7.4	4.1	4.9
Special purpose grants	16.4	42.6	22.2	54.8	21.2	58.8	22.4	63.7	27.7	67.9	36.5	73.4	37.1	68.4	58.7	71.5
Total ODA less special purpose grants	**40.6**		**36.8**		**28.6**		**29.2**		**32.6**		**33.8**		**41.8**		**47.7**	
Total ODA less special purpose grants (2004 US$) (index numbers, 1990 = 100)	**100**		**73.8**		**67.4**		**72.0**		**76.9**		**70.1**		**79.4**		**88.9**	
Total ODA less special purpose grants as a percentage of DAC GNI		**0.25**		**0.16**		**0.12**		**0.12**		**0.13**		**0.12**		**0.14**		**0.15**

Source: OECD/DAC on-line database.
Note: the DAC deflator (constant 2004 US$) was used to estimate total ODA less special purpose grants in real terms.

Second, since September 11, 2001, strategic considerations have played an important role in determining the changing landscape of official aid flows, with the 'war on terror' and the conflict in Iraq significantly affecting aid allocations. It is documented in table 1.2 how aid to Afghanistan and neighbouring countries – Pakistan, Tajikistan, Turkmenistan, Uzbekistan – has risen sharply from US$ 1.1 bn in 2000 to almost US$ 5 bn in 2005.

Table 1.2: Net ODA to Afghanistan and neighbouring countries, all donors, 2000-05, US$ millions

	2000	**2001**	**2002**	**2003**	**2004**	**2005**
Afghanistan	141	408	1305	1595	2190	2775
Pakistan	703	1948	2138	1066	1421	1666
Tajikistan	125	170	168	147	241	241
Turkmenistan	32	72	41	27	37	28
Uzbekistan	186	153	189	195	246	172
Total	1182	2751	3841	3030	4135	4882

Source: OECD/DAC on-line database.

Table 1.3 documents the dramatic increase in net ODA to Iraq since the occupation of the country by a US-led international coalition. At an international donors' conference for the reconstruction of Iraq (Madrid, October 2003) more than US$ 33 bn, in the form of loans, grants and export credits, was pledged, for the period 2004 to 2007.[11]

Table 1.3: Net ODA to Iraq, all donors, 2000-05, US$ millions

	2000	**2001**	**2002**	**2003**	**2004**	**2005**
Iraq	101	122	116	2265	4658	21653

Source: OECD/DAC on-line database.

Woods (2005) points to the risk that is associated with a rapid increase in aid being channelled to meet new security imperatives for development assistance which, at

[11] The largest pledges were from the US ($ 20.3 bn), Japan (up to $ 5 bn), the WB ($ 3-5 bn), and the IMF ($ 2.5-4.5 bn) (WB 2005h).

least at the rhetorical level, seeks the achievement of human development goals (see also WB 2005h, pp. 103-4).[12]

This draws attention, third, to a recent shift in donor discourse characterised by a pre-occupation with a set of issues broadly subsumed under the newly proposed category of International (or global) Public Goods (IPGs). A host of definitions of IPGs prevail, with the following issues most commonly identified as key: eradicating contagious diseases; creating and disseminating knowledge; protecting the environment; safeguarding peace; and maintaining financial stability (WB 2001l, p. 109).[13] Te Velde et al. (2002) show that the share of aid allocated to financing IPGs has doubled in the past two decades and estimate that, by the late 1990s, donors allocated at least 10 percent of aid to IPGs.[14] They point to a possible threat to development aid if an expanding mandate to finance public goods diverts resources away from development budgets.

Fourth, the aid figures should be seen in the context of annual spending by industrial countries to subsidise domestic agriculture, which amounts to more than US$ 300 bn (WB 2005h, p. 104). This has been estimated to reduce rural incomes in low and middle-income countries by over US$ 60 bn annually (see Beghin et al. 2002).

Fifth, aid remains well below the levels necessary to meet the MDGs. These have been estimated to require an annual increase in aid of US$ 50 bn (UN 2001). The meagre donor performance in funding the MDGs has prompted the search for new sources of development finance which, even though it has generated a set of interesting propositions, has not yet created new realities on the ground and is unlikely to do so as long as there is US opposition to propositions that draw on certain forms of international taxation or which imply increased UN power in allocating these resources (Addison et al. 2005, p. 12).[15]

[12] Woods (2005, p. 406) refers to the intention of the DAC, announced in April 2004, to broaden the definition of ODA to include expenditures related to preventing the recruitment of child soldiers, enhancing civil society's role in the security system, and promoting civilian oversight and democratic control of the management of security expenditures.

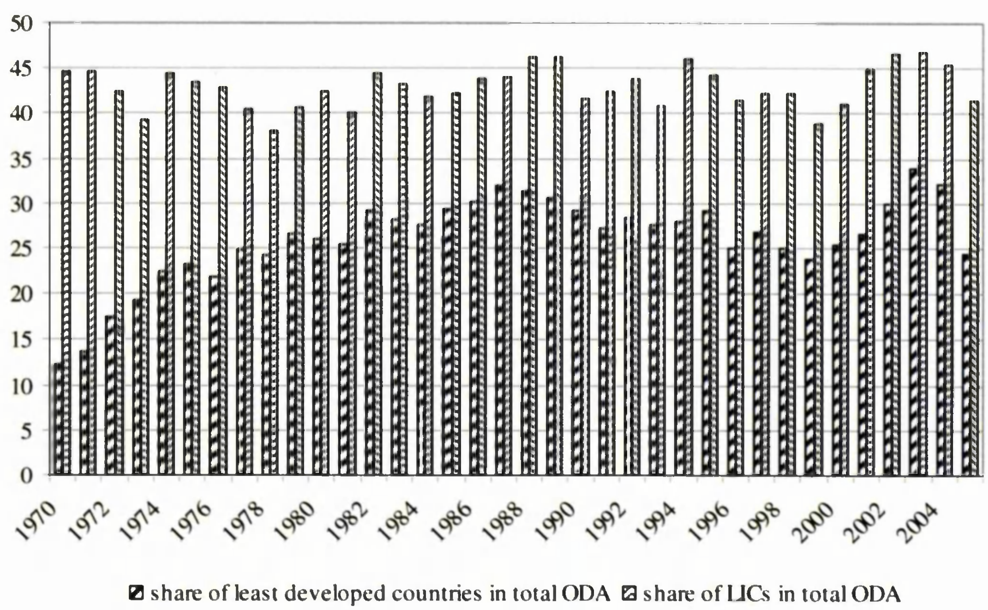
[13] See Kaul et al. (1999) and follow-up study Kaul et al. (2003) for a collection of papers touching upon various aspects of IPGs. See also Hewitt and te Velde (2006) most recently.

[14] See also Reisen et al. (2004) for alternative estimates.

[15] See Atkinson (2005) for a collection of essays discussing a set of alternative propositions. These include tax-based propositions such as the Tobin tax (Nissanke 2005) and a global environmental tax (Sandmo 2005), and other mechanisms relying variously on: international capital markets – through the International Finance Facility (Mavrotas 2005); development-focused Special Drawing Rights (Aryeetey 2005); remittances (Solimano 2005); private and corporate donations (Micklewright and Wright 2005); and a global lottery and global premium savings bond (Addisson and Chowdhury 2005).

Sixth, in a more positive vein, it can be noted that the share of grants in ODA has increased over the years, indicating a rising level of concessionality of ODA (see WB 2006b, p. 82).[16] Recently, donors have also reallocated aid to the poorest countries, particularly those in Africa (WB 2006b, p. 8). This follows a sustained fall in the share of aid flows going to SSA during the 1990s (see White 2002). Figure 1.3 illustrates how the share of aid going to LDCs rapidly recovered between 2000 and 2003 after a sustained fall since the late 1980s which had resulted, in 1999, in its lowest level (23.8 percent) over the last two decades.[17] In 2003, the share of aid going to LDCs reached a high of almost 34 percent. It has, nevertheless, declined again since, and accounted for just under 25 percent in 2005. The share of ODA going to all LICs has been more stable hovering approximately between 40 and 45 percent of total ODA.[18]

Figure 1.3: Share of ODA going to LICs and LDCs, 1970-2005, percentages



Source: OECD/DAC on-line database.

[16] On some ambiguous repercussions of increased use of grants, see chapter two. See also Odedokun (2004) for an overview of the issues pertaining to the 'grants versus loans' debate.
[17] Since 1971, the UN classifies as LDCs 'low income states that are deemed structurally disadvantaged in their development process, and facing more than other countries the risk of failing to come out of poverty' (UNCTAD 2005, p. 6). The LDCs are defined according to the following three criteria: low income (three-year average per capita income under $750 for addition to the list and above $900 for graduation of the list); weak human assets (as measured through a composite Human Asset Index); and economic vulnerability (as measured through a composite Economic Vulnerability Index). In 2006, 50 countries were classified as LDC. These accounted for 11.3 percent of the world population. For the list of LDCs, see http://www.unctad.org/Templates/Page.asp?intItemID=3641&lang=1.
[18] In the OECD (2006a) database, LICs are countries that had a GNI per capita below $825 in 2004.

Seventh, the 2005 average aid/GNI ratio of 0.33 percent remains significantly below the UN target of 0.7, to which all DAC members apart from the US and Switzerland are formally committed.

Eighth, the haphazard and protracted trajectory of how the international donor (or creditor) community has dealt with the issue of poor countries' debt illustrates further the general decline in donor commitment to finance development in the poorest countries.[19] In 1996, the Highly Indebted Poor Country Initiative (HIPC I) was launched by the WB and the International Monetary Fund (IMF) in an attempt to cut back debt to more sustainable levels. It was followed by the Enhanced HIPC Initiative (HIPC II) in 1999, and was complemented, in 2005, by the Multilateral Debt Relief Initiative (MDRI).

The HIPC initiative has, however, been denounced as a very partial response to the real and long-standing systemic problems of the poorest countries (see Strange 1998, pp. 106-9; UNCTAD 2000a, pp. 135-70; Raffer 2001; Gunter 2002; Callaghy 2003; Nissanke and Ferrarini 2004; Oddone 2005). Significantly, the real incremental benefits from debt relief afforded under HIPC tend to be low, since much of the debt being forgiven was in any case not being serviced (Serieux 2001). As a result, HIPC has been a relatively costless gesture by creditors towards the poorest countries (Culpeper 2001). Apparent increased generosity in the terms of debt relief awarded along the trajectory from HIPC I to HIPC II to, most recently, the MDRI has, furthermore, been accompanied by increased creditor control over the domestic policies of debtor economies, most visibly through the Poverty Reduction Strategy (PRS) initiative, the preparation of which now constitutes a condition to qualify for debt relief (see IDA/IMF 2004; see also below).

Ninth, the donor effort appears particularly miserly when put against the dramatic growth in workers' remittances to developing countries. Table 1.4 documents the trends in workers' remittances to developing countries between 1990 and 2004. These have quadrupled over the period and have grown even more rapidly for LICs. It should be noted that these data are officially recorded remittance flows

[19] See also the discourse on the New International Financial Architecture (NIFA), which seeks to address financial market transparency and surveillance with a focus on better data collection and reporting systems for a more efficient working of the international capital markets – rather than being concerned with the imperative of reconstructing the international financial architecture to the benefit of the poorest debtors (see e.g. Eichengreen 1999; Griffith-Jones 2003). See Best (2003) and Soederberg (2004a) for accounts of the NIFA as a re-imposition of neo-liberal domination in emerging economies.

and, as such, underestimate actual remittance flows, with remittance flows through unofficial channels probably being much larger.

Table 1.4: Workers' remittances to developing countries, 1990-2004, US$ billions

	1990	1995	2000	2001	2002	2003	2004e
Developing countries	31.3	56.7	76.8	84.6	99.0	116.0	125.8
Lower MIC	17.5	34.8	41.9	44.1	49.1	54.8	55.6
Upper MIC	5.7	8.6	13.1	16.8	18.7	24.4	26.8
LIC	8.1	13.3	21.7	23.8	31.2	36.7	43.4

Source: WB (2005h, Table 1A.1).

Table 1.5 puts the remittance receipts in developing countries in perspective. In 2001, remittances accounted for more than double the size of official flows to all developing countries. For LICs, remittances are now larger than the receipt of official flows.

Table 1.5: Remittances received and paid by developing countries in 2001

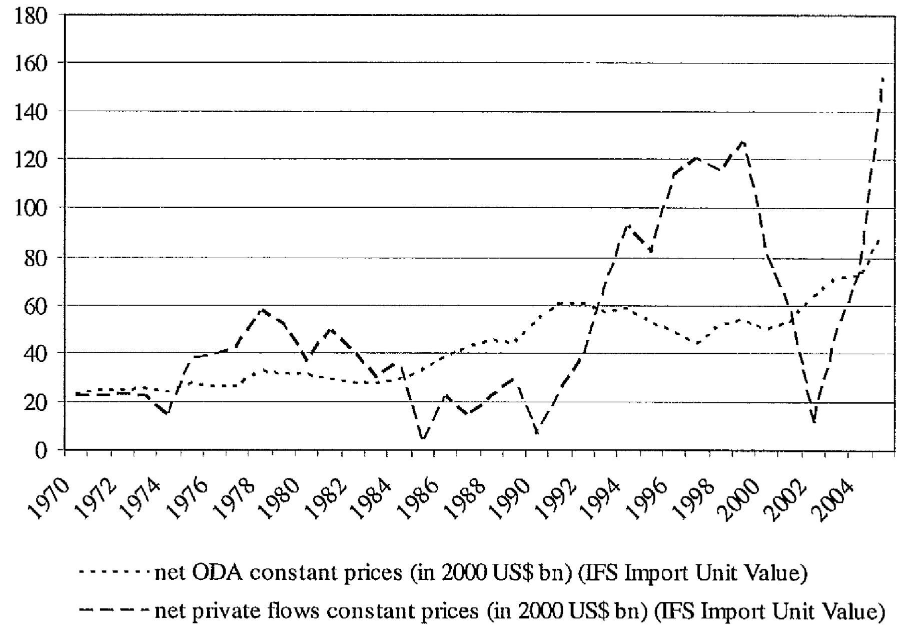
	All developing countries	LIC	Lower MIC	Upper MIC
Total remittance receipts (US$ billions)	72.3	19.2	35.9	17.3
As % of GNI	1.3	1.9	1.4	0.8
As % of Imports	3.9	6.2	5.1	2.7
As % of domestic investment	5.7	9.6	5.0	4.9
As % of FDI Inflows*	42.4	213.5	43.7	21.7
As % of total private capital inflows	42.9	666.1	44.9	20.2
As % of official flows	260.1	120.6	361.7	867.9

Source: WB (2003l, table 7.1); * Foreign Direct Investment (FDI).

Tenth, grants from non-governmental organisations (NGOs) have also come to play a growing role in funding development programmes. The private-sector component of NGO grants to all developing countries, i.e. that part of NGO activity not financed by official donors, has increased from US$ 5 bn in 1990 to US$ 10 bn in 2003, and now constitutes about 15 percent of total ODA (WB 2005h, p. 94; see also table 1.6).

Eleventh, the trends in aid documented above are in stark contrast to the rapid expansion of private financial flows since the early 1990s. This has come about as a result, amongst other things, of rapid changes in the regulation of international finance which have been actively promoted by some of the core players in the donor community (mainly the US and the IMF) (see Helleiner, E. 1994). Figure 1.4 compares (real) trends in ODA and private flows from DAC countries to all developing countries between 1970 and 2005. This illustrates that while, during the 1990s, aid flows stagnated, private flows increased very rapidly. After a significant plunge following the outbreak of a series of international financial crises (East-Asia 1997-98; Russia 1998; Brazil 1999), private flows quickly picked up again after 2002 and, in 2005, stood at more than six times the (real) level that they had attained in 1991 (after they had reached a second all-time low in 1990).

Figure 1.4: Trends in ODA and private flows to developing countries, 1970-2005, 2000 US$ billions



Source: OECD/DAC on-line database; IMF IFS on-line database.

Table 1.6 documents the absolute magnitudes of official and private flows as well as their relative shares in total net resource flows to developing countries. At the beginning of the 1990s, official flows exceeded private flows and accounted for more than half of total net flows. This changed during the ensuing decade and, by 2005, private flows accounted for nearly two-thirds of total net flows from DAC countries to developing countries.

Table 1.6: Total net flows from DAC countries to developing countries, 1990-2005

	Av. 1990-5	Av. 1996-9	2000	2001	2002	2003	2004	2005
		In US$ billions						
ODA	58.4	52.1	49.8	51.6	60.2	70.4	79.0	106.4
Other Official Flows	13.8	20.5	3.8	7.1	-2.4	-6.8	-8.8	2.8
Private Flows	54.0	124.0	81.3	55.4	9.8	47.3	82.3	182.0
Grants from NGOs	5.7	5.8	7.0	7.3	8.8	10.3	11.4	14.9
Total	132.4	202.5	141.8	121.4	76.5	121.1	163.8	306.0
		Percentages						
ODA	44.1	25.7	35.1	42.5	78.7	58.1	48.2	34.8
Other Official Flows	10.4	10.1	2.7	5.9	-3.1	-5.6	-5.4	0.9
Private Flows	40.8	61.3	57.3	45.6	12.8	39.0	50.2	59.5
Grants from NGOs	4.3	2.9	4.9	6.0	11.5	8.5	6.9	4.9
Total	100	100	100	100	100	100	100	100

Source: OECD/DAC on-line database.

Finally, it needs to be mentioned that during the past decade, a set of developing countries have become a significant source of FDI, bank lending and aid (see WB 2006b, pp. 106-36). Brazil, China, India, South Africa, and Thailand are among the developing countries that now also provide aid to other developing countries. Data are not readily available to capture the magnitude of South-South development assistance, but the resources involved, while growing, remain small compared to total ODA (p. 109).[20]

1.3 The unfortunate reality of persistent needs

While aid has come to represent a declining share of total net resource flows to developing countries, it remains a crucial source of external finance for a large number of poor countries as the worldwide expansion of private capital flows during the 1990s has largely bypassed the poorer countries (see Gabriele et al. 2000; WB 2005h, pp. 89-112). The share of LICs in total private flows from North to South averaged just over 7 percent between 2000 and 2005, and this falls to 2.6 percent once India is excluded (OECD 2006a).

Table 1.7 provides an overview of the relative importance of official and private flows in net disbursements to LDCs and OLICs. The table reveals how the

[20] Figures on non-DAC ODA in the OECD database understate the true volume of resources flowing from developing countries as they do not include potentially important donors such as Brazil, China, India and South Africa (WB 2006b, p. 109). See Oya (2006) for a speculative foray into the possibilities that could emerge from an increased importance of China as a provider of FDI and aid to Sub-Saharan Africa (SSA).

poorest countries remain overwhelmingly dependent on aid for their access to external finance and how the share of ODA in total net flows has increased most recently for both LDCs and OLICs. This compares to an average share of aid in total net resource flows for MICs of less than a third over the last decade (OECD 2006a), and points to an increasing bifurcation in the countries of the South, where MICs and a small set of LICs (including India and Pakistan) tend to have access to a broad range of sources of external finance, while a large group of LICs remains heavily dependent on aid.

Table 1.7: Relative importance of official and private flows in total net resource flows to LDCs and OLICs, 1970-2005, percentages

	Av 1970-9	**Av 1980-9**	**Av 1990-9**	**Av 2000-5**
		LDCs		
ODA	74.0	90.5	93.9	95.8
Private flows as share of total	18.7	2.5	4.7	4.3
Other official flows	7.2	7.0	1.3	-0.1
Total	100	100	100	100
		OLICs		
ODA	78.5	60.4	73.3	84.9
Other official flows	5.4	20.2	15.2	-11.9
Private flows	16.1	19.4	11.5	27.0
Total	100	100	100	100

Source: OECD/DAC on-line database.

Table 1.8 further documents the persistent importance of aid to LDCs in terms of GNI, Gross Capital Formation (GCF), and total government expenditure (GXP). In 2004, thirty LDCs had ODA/GNI ratios that exceed 10 percent, while for 29 LDCs ODA as a share of domestic investment exceeded 50 percent. This compares to an unweighted average ODA/GNI ratio of 1.26 for all developing countries or of 1.61 for OLICs (OECD 2007). Further, ODA accounts for large shares of government expenditure in the bulk of LDCs.

Table 1.8: Aid intensity indicators for the LDCs, 2004, percentages in brackets

ODA as share of GNI	**Country**
> 50%	Burundi (54,3), Liberia (52,8), Sao Tome and Principe (61,9), Solomon Islands (47,1)
20% < 50%	Afghanistan (36,7), Democratic Rep. Congo (29,1), Eritrea (28,4), Malawi (25,6), Madagascar (26,8), Guinea-Bissau (29,4), Mozambique (22,0), Rwanda (26,0), Sierra Leone (34,6), Timor Leste (31,7), Zambia (21,6)
10% < 20%	Bhutan (10,9), Burkina Faso (12,7), Cambodia (10,3), Cape Verde (14,7), Ethiopia (18,9), Mauritania (11,1), Mali (12,1), Lao PDR (11,3), Kiribati (12,7), Gambia (16,5), Niger (17,6), Senegal (14,1), Tanzania (15,5), Uganda (17,3), Vanuatu (12,4)
5% <10%	Angola (6,6), Benin (9,4), CAR (8,0), Chad (8,8), Comoros (6,7), Haiti (6,3), Guinea (7,5), Nepal (6,4), Samoa (8,6)
< 5%	Maldives (3,7), Sudan (4,4), Togo (3,0), Yemen (2,1)
ODA as share of GCF	
> 100%	Burundi (386,6), Comoros (217,8), Eritrea (122,7), Malawi (163,9), Madagascar (116,9), Liberia (346,8), Guinea Bissau (213,9), Mozambique (100,6), Niger (111,16), Rwanda (124,5), Sao Tome and Principe (169,5), Sierra Leone (318,0), Solomon Islands (134,1), Timor Leste (158,6)
50% < 100%	Angola (63,5), Benin (51,2), Burkina Faso (66,2), Cape Verde (72,3), Ethiopia (88,2), Mauritania (54,5), Mali (61,1), Lao PDR (62,3), Guinea (68,6), Gambia (55,8), Senegal (59,0), Tanzania (83,9), Uganda (75,5), Zambia (76,8)
10% < 50%	Bhutan (17,5), Cambodia (37,9), Chad (29,7), CAR (45,6), Maldives (10,3), Nepal (24,0), Sudan (18,2), Togo (16,6), Yemen (11,5)
ODA as a share of GXP	
> 100%	Democratic Rep. Congo (592), Guinea Bissau (170), Sierra Leone (128).
50% < 100%	Burundi (88), Cambodia (67), Chad (64), Eritrea (53), Ethiopia (79), Gambia (54), Haiti (56), Lao PDR (85), Malawi (71), Mozambique (88), Niger (91), Rwanda (78), Sao Tome and Principe (74), Solomon Islands (61), Tanzania (77), Uganda (64)
< 50%	Angola (10), Benin (40), Bhutan (29), Burkina Faso (49), CAR (34), Comoros (39), Guinea (44), Madagascar (46), Nepal (36), Togo (16), Yemen (6), Zambia (48)

Source: WDI on-line (2006 edition) for ODA as share of GNI and GCF; Moss and Subramaniam (2005) for ODA as share of GXP.

Meanwhile, the human development indicators in the LDCs remain ghastly and the domestic sources of finance limited. The latest UNCTAD LDC Report (2006a, pp. 34-8) sums up trends in human development indicators in LDCs. The Report further documents the state of domestic resource mobilisation in LDCs, where domestic savings rates remain half of the savings rate in other developing countries (for the period 1999-2003 for those LDCs for which data are available). Domestic savings rates in the African LDCs have been particularly low, amounting to 10.6 percent of national income during that same period (p. 105). The Report (UNCTAD 2006a, p. 105) observes that:

> With such a low domestic savings rate it is impossible to achieve the investment rates required for economic growth and poverty reduction

> without resort to external finance ... Indeed, without external resource inflows, the average domestic savings rate for the LDCs as a group is actually insufficient for economic growth to take place at all ... Without access to external savings, the real GDP per capita of the LDCs as a group would have declined by 0.66 percent per annum during 1999-2003 even if all domestic savings had been efficiently invested.

Low domestic savings rates in LDCs coexist with low government revenue. For seventeen LDCs for which recent data on public finances are available, there are only three in which tax revenue exceeds 15 percent of GDP, and tax revenue is below 10 percent of GDP in seven countries (p. 106). This compares unfavourably with an average of tax revenue as a share of GPD in developing countries of 19 percent and 38 percent in developed countries. In these circumstances (p. 112):

> external finance can play an important catalytic role in kick-starting and supporting a virtuous cycle of domestic resource mobilisation in which expanding investment opportunities generate increased savings and increased savings in turn finance increased investment.

The conditions under which such outcomes materialise are manifold and context-specific – an issue to which we return in chapters four and five when examining the existing analyses of the effectiveness of aid and conditionality. Nevertheless, both the scale *and* the modalities under which aid is received take on crucial significance for the possibilities regarding aid's catalytic role in supporting a virtuous cycle of domestic resource mobilisation. We consider the latter aspect of the current reality of aid next.

1.4 A new paradigm for residual aid flows: selective partnerships in capacity-building

Aid discourse and practices have become increasingly concerned with engineering poor countries' domestic policies and institutions, both within and beyond the traditionally economic realm.[21] This can be seen as manifesting itself in

[21] Although a certain degree of diversity persists between the agenda of different donors as aid policy is driven by concerns that take their particular character from donors' individual circumstances, the policy agenda of major donors has shown increasing convergence. This convergence has accelerated recently with the explicit attempts by the donor community to achieve better co-ordination and harmonisation of operational policies, procedures and practices. See the Rome (2003) and Paris (2005) Declarations on aid effectiveness, respectively at: http://www.aidharmonization.org/ah-wh/secondary-pages/why-RomeDeclaration and http://www1.worldbank.org/harmonization/Paris/FINALPARISDECLARATION.pdf. See also Hall and de la Motte (2004) who refer to 'globalised aid' in the context of privatisation.

aid practices in three different ways: first, through more stringent modalities of access to aid through selective allocations of aid flows for LICs; secondly, through particular shifts in the sectoral allocation and composition of aid; thirdly, through the particular way in which the participatory principle has been institutionalised. This section documents each of these and, as such, situates selectivity amongst the broader shifts in aid practices.

1.4.1 Selectivity

Under a performance-based allocation (PBA) of aid or 'selectivity', the conditionality accompanying (or now preceding) aid no longer reflects the flow of reforms, but the state of the policy and institutional environment. When aid flows are allocated 'selectively', donors set conditions that identify environments judged beneficial for growth and development, and aid is allocated accordingly. Conditions relate to past rather than future actions (policy-level versus policy-change conditionality). Selectivity seeks to reward countries that reform 'on their own', in supposed contrast to structural adjustment which sought to impose reforms on countries (Easterly 2003, p. 37). Soederberg (2004b, p. 281) refers to a shift to 'pre-emptive development', where funds are withheld until demands made by the donors are met.

The idea of making loans conditional on what is already achieved in terms of policy/institutional reform has combined with an emphasis on a more advisory role for donors. A country not yet characterised by an 'appropriate' environment is to be a recipient of 'aid skills' or advice rather than of 'aid money'. The WB's flagship report on aid *Assessing Aid* (WB 1998a, p. 4) elucidates:

> Aid can nurture reform in the even most distorted environments – but it requires patience and a focus on ideas, not money.

Aid's two dimensions ('financial' versus 'ideational') become distinct and separate, as it assumes a dual role. Selectivity means channelling lending to countries with 'appropriate' policy environments and using non-lending services more strategically to support the emergence of sound policies and good governance. It is deemed crucial to build better development synergy between advisory, analytical and lending services. Collier (2000, p. 307), a staunch advocate of the selectivity proposition, further explains:

> By abandoning the notion of aid as a 'reward' for policy improvement, donors move to a model of partnership. However with those governments

> which adopt really poor policies, partnerships are not beneficial. Engagement with those governments and with their societies in the battle of ideas is the means by which donors can best hope to influence policy.

The 'pedagogical' role of the donor community, and of the WB in particular, receives a special emphasis. This tallies well with the emerging knowledge paradigm, documented in chapter two.

Of course, other criteria – apart from policy performance – play an important role in guiding aid flows. Birdsall et al. (2004), for instance, find that the build-up of debt-stock to multilateral creditors hinders the targeting of aid flows to countries with 'better' policy and institutional environments (the CPIA measure), particularly so for bilateral donors. They recommend debt service reduction (as for instance under HIPC) as a way through which the donor community can increase its policy selectiveness.[22]

Birdsall et al. (2004) join a well-established literature on the often implicit (non-developmental) motives for aid giving. Classic contributions to this literature include Maizels and Nissanke (1984) and various contributions by McKinlay and Little (1977, 1978a, 1978b, 1979). These traditionally try to ascertain the 'balance of motivations as between the needs of development and the interests of donor governments' (Maizels and Nissanke 1984, p. 880). They find that bilateral aid tends to be allocated largely in support of donors' perceived foreign economic, political and security interests; while multilateral aid is allocated essentially in accordance with recipient need.

Yet in a comprehensive review of this literature, McGillivray and White (1993) point, amongst other issues, to the possibility of a specification error in the separation of the 'recipient need' (RN) and 'donor interest' (DI) variables in the RN/DI models. The authors estimate a hybrid model and find that recipient need cannot always be rejected as a criterion for bilateral aid allocations. More recent studies include Alessina and Dollar (2000), Alessina and Weder (2002), Berthelemy and Tichit (2002), and Feeny and McGillivray (2003). These find that donor non-developmental motives steer aid allocations in significant ways, but also report a negative (and statistically significant) relationship between aid and recipient country income per capita as a proxy for need. In general, it can then be asserted that, although the extent to which donor agencies have taken development criteria into

[22] See, however, Nissanke and Ferrarini (2004, p. 47), who guard against such a role for the HIPC initiative.

account might have been underestimated in the previous literature, non-developmental interests/reasons (political, strategic, commercial) significantly steer aid allocations (aid practice) beyond what can be inferred from declared intentions (aid rhetoric).

Returning to the prevalence of selectivity as a donor practice, it appears, nevertheless, that while non-developmental criteria, such as trade promotion or debt, remain a priority for many (mainly bilateral) donors, selectivity has taken root in donor practices as it becomes increasingly popular to allocate aid flows (and grant debt relief) on the basis of a priori assessments of the policy and institutional environment (see IDA 2002a; Hout 2002; Dyer et al. 2003, p. 11; Hout 2004; Dollar and Levin 2004; Rogerson et al. 2004, pp. 10-4; Jones et al. 2005, pp. 18-20; McGillivray 2003b, 2005).

The WB has been the main sponsor of this shift towards selectivity in the allocation of aid flows and has successfully promulgated its practice in the broader donor community. The core of the WB's PBA system, which applies to the distribution of its concessional resources, is the Country Policy and Institutional Assessment (CPIA).[23] The latter measures a country's performance on a set of macroeconomic, structural and governance criteria and then feeds into an allocation formula for the IDA's resources that is sixteen times more sensitive to changes in policy/institutional variables than to changes in income per capita (as a proxy for poverty).[24] [25]

Recently, the WB has placed the CPIA in the public domain. It has sought to promote its instrument and, concomitantly, the CPIA is rapidly becoming a standard in the broader donor community. Both the African Development Fund (AfDF) and the Asian Development Fund (ADF) use a very similar, but independently estimated CPIA (ADB 2001b; AfDB 2004),[26] and the allocation processes of Dutch and British

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[23] The WB provides finance to developing countries on near-market terms through the so-called 'hard window' of the International Bank of Reconstruction and Development (IBRD) and on concessional terms through the 'soft window' of the International Development Association (IDA) (see also chapter two).

[24] The CPIA is elaborately deconstructed in chapter six.

[25] Nunnenkamp (2002) refutes the claim that Bank resources are being allocated in an increasingly selective manner. The paper is, however, based on a confusion between the allocation of IBRD resources versus IDA flows; a misunderstanding of the actual allocation formula used by the IDA; and a failure to use available information on the CPIA (drawing on second-hand data from Collier and Dollar 2002). Furthermore, in a footnote, Nunnenkamp effectively confirms the process of selectivity at work for IDA allocations (p. 9). The mistakes are repeated in Nunnenkamp et al. (2004), where an investigation into the reality of selectivity is tentatively extended to bilateral donors.

[26] The only divergence between the CPIA questionnaire of the WB and that of the Asian Development Fund is that in the latter a regional integration dimension is added to the trade and environment criteria.

aid formally draw on the WB's CPIA scores (see Hout 2002; Jones et al. 2005, pp. 18-9; Hout 2004). Although not strictly based on the CPIA, the USA's Millennium Challenge Account (MCA) also selects countries for assistance on the basis of their demonstrated commitment to a set of policies and institutions.[27] In addition, the Debt Sustainability Framework (DSF), the framework newly formulated by the International Financial Institutions (IFIs) and which will also be used by other creditors and fora such as the Paris Club, has the CPIA at its core in determining debt distress thresholds (see Oddone 2005; see also Collier 2006b).

1.4.2 Capacity-building

The new approach of selectivity has been accompanied by an emphasis on 'capacity-building' in donor practices. The WB's Strategic Framework for the beginning of the current decade asserts, WB (2001e, p. 5):

> Even in countries where lending is not appropriate given the policy environment, we will continue to offer non-lending and, especially, capacity building support – to help poor performers become good performers. This is one of our most important roles.

'Capacity development' or 'capacity-building' has most broadly been described as, DAC (2006a, p. 9):

> the process whereby people, organisations and society as a whole unleash, strengthen, create, adapt and maintain capacity over time.

While capacity-building has always been an aspect of aid (see Panday 2002; Whyte 2004; King 2004; DAC 2006a), it has recently become elevated to aid's main purpose (see OECD 1998, p. 18).[28] This pre-occupation with capacity-building raises a set of issues. First, different agencies seek to convey different emphases in their support for capacity-building.[29] Some use a narrow definition focused on strengthening specific organisations and skills, while others use a much broader one

[27] These consist of sixteen criteria grouped under the headings 'ruling justly', 'investing in people', and 'encouraging economic freedom'. 'Ruling justly' includes: control of corruption; rule of law; voice and accountability; government effectiveness; civil liberties; and political rights. 'Investing in people' includes: immunisation rate (DPT and measles); primary education completion rate; public primary education spending/GDP; public expenditure on health/GDP. 'Encouraging economic freedom' includes: country credit rating; inflation; regulatory quality; budget deficit/GDP; trade policy; days to start a business (see Radelet 2006).

[28] In a study of current donor practices, Gould and Ojanen (2005, p. 45) suggest that capacity-building has replaced growth as the operational goal of external interventions. And a former Director of the WB's Evaluation Department explained that *all* WB operations are increasingly designed as vehicles for capacity development and policy learning (Picciotto 2002, p. 8).

[29] See IMF (2002); Fukuda-Parr et al. (2002) for the UNDP; EuropeAid (2005); OED (2005) for the WB; and DAC (2006a).

that encompasses various 'levels of capacity' from the individual to the whole of society (see Whyte 2004). As a result, 'capacity development' defies a shared definition of what it means in practice (see Moore 1995; Harrow 2001; Browne 2002; OED 2005, p. 7; DAC 2006a, p. 3), and it has been observed in the academic literature how the term could include almost everything and, by the same token, becomes in effect practically and analytically useless (see Moore 1995).

Second, a distinctive feature of the notion, nonetheless, is its emphasis on what are perceived to be 'software' elements of the development process to do with human resources and institutions across various sectors, rather than on 'hardware' such as physical infrastructure or equipment.

Third, capacity development has taken on a different character from its practices in the past. King (2004, p. 6) highlights how the logic of the new style of capacity-building is centrally concerned with exercising a particular leverage on governments in line with the legacies of the Berg Report (WB 1981) and the 1989 WB Report on SSA (WB 1989). For King (2004, p. 6), the new donor-led capacity-building is:

> about securing local analytical support for the other new paradigm of the late 80s and early 90s – policy-based lending, and about producing a cadre of local technocratic, experts who would assist with the macro-economic reforms and adjustment packages.

As a result, the new donor interest in 'capacity for policy analysis' focuses on the very policies which had already been developed externally by the donors (see also Fraser 2006, p. 43). This is in contrast to earlier capacity-building, which had been, according to Puryear (1979, p. 5 as quoted in King 2004, p. 6), more inclined:

> to create and strengthen institutions which could endure after our eventual withdrawal and would set their own research and development agenda.

Capacity-building through technical and financial assistance has become, DAC (2002, p. 2):

> crucial to supporting developing countries' efforts to implement sound policies and practices that help stimulate private finance and investment as well as to helping build the required institutional and human capacity.

Moreover, and fourth, the character of capacity-building has altered from an exclusive emphasis on re-organising government units and building state institutions to assisting civil society organisations in an attempt to stimulate 'public demand for policy improvements' (WB 2005d, p. 34). Donor funding is made available to build and regulate the relationship between the state and civil society and seeks to enhance the capacity of the latter to participate in consultations, policy advocacy and other political processes, rather than that it merely focuses on building the technocratic cadre able to assist with policy and institutional reforms (see Gould and Ojanen 2005, pp. 45-7). The WB (2005m, p. 3) explains:

> Support to public sector governance reforms has evolved considerably in the last 10 years ... shifting from supply-side reforms and technical advice to governments, toward broader efforts to enhance domestic ownership and demand for reform.

Finally, this emphasis on, and re-interpretation of, capacity-building has coincided with broad qualitative re-orientations of aid flows. We single out four specific features: first, a shift in the sectoral composition of aid away from productive sectors towards the social sectors, and in particular, towards the category of 'government and civil society'; secondly, the persistently high share of TC in total aid and the change of the nature of TC; thirdly, a shift away from project support towards budget support and programme aid; and, fourthly, a redefinition of the purpose of project aid.

First, table 1.9 illustrates the shift in the sectoral composition of aid over the last decade for bilateral aid and the main multilateral aid providers (the EC; the regional development banks, RDBs; and the WB's aid window, the IDA). The rapid increase in the share of aid going to 'government and civil society' in the last ten years across all major aid providers stands out. The aid allocation to what was previously known as 'planning and public administration' has grown, in only 10 years, from one of the smallest single sectoral aid allocation to one of the largest ones, particularly for bilateral and European aid, for which it accounts for the largest share in the sectoral allocation of aid in 2005. More generally, table 1.9 indicates how aid has become increasingly devoted to human and institutional development, at the expense of economic infrastructure and productive activity with, as was highlighted above, the expectation that remaining capital requirements come from domestic and foreign investors.

Table 1.9: Aid by major purpose (commitments), 1995 and 2005, percentages

Sector	DAC bilateral		EC		RDBs		IDA	
	1995	2005	1995	2005	1995	2005	1995	2005
SOCIAL INFRASTRUCTURE AND SERVICES	30.5	30.5	26.5	40.1	24.5	27.7	33.9	42.2
Education	11.2	6.1	2	6.6	9.5	3.1	8.2	9.2
Health	5.6	5.4	5.4	5.4	1.7	2.9	5.3	3.9
Water Supply and Sanitation	5.6	4.8	2.2	6.1	5.6	3.4	8.9	3.8
Government and Civil Society*	3.2	9.7	1.8	16.0	0.1	8.9	3.7	11.3
Other	4.8	3.7	15.1	5.6	7.6	8.7	7.7	8.1
ECONOMIC INFRASTRUCTURE	23.7	10.6	16.8	17.1	42.2	35.6	40.8	20.6
Transport and Communications	11.6	5.6	14.7	10.8	15	24.8	11.5	6.8
Energy	10.1	3.1	1.5	3.2	12.3	5.3	10.7	3.8
Other	2	2.0	0.7	3.0	14.8	5.5	18.6	10.0
PRODUCTION SECTORS	10.6	5.2	17.3	6.2	5.5	17.8	12.2	12.3
Agriculture, Forestry, and Fishing	7.4	3.3	7.4	1.9	4.2	5.0	9.3	8.0
Industry, Mining and Construction	1.6	1.3	6.4	2.9	1.2	10.0	2.9	4.1
Trade and Tourism	1.5	0.5	3.5	1.4	-	2.8	-	0.1
MULTISECTOR	5	6.5	6.9	5.6	6.1	13.7	7.6	6.7
OTHERS								
o/w: Programme Assistance	5.8	2.5	28.4	14.0	2.5	4.0	3.5	3.8
Debt relief	7.3	27.5	-	-	-	0.4	0.4	0.3
Emergency Aid	5.2	10.0	3.9	11.1	-	0.7	0.5	14.1
Administrative Expenses	4.8	4.0	-	5.4	-	-	-	-
Unspecified	7.1	3.2	0.1	0.4	19.3	-	1	-

Source: OECD (various); * previously planning and public administration.

These trends are equally striking when we consider the changing sectoral composition of aid to the LDCs (see UNCTAD 2006a, p. 20). The share of ODA for economic infrastructure and productive sectors in total aid to LDCs has been halved from 37 percent in 1992-4 to 18 percent in 2002-2004, while the share of social infrastructure and services increased from 21 percent to 32 percent. The share of action related to debt and emergency assistance grew rapidly over the same period (from 8.3 to 17.8 percent and from 5.1 to 12.2 percent, respectively). Together, social sectors, emergency assistance and action relating to debt absorbed 62.1 percent of total ODA commitments to the LDCs in 2002-2004, compared with 34.6 percent in 1992-1994 (p. 18).

Secondly, the share of TC in total aid remains substantial and, most recently, between 2000 and 2004, it has averaged over a third of net bilateral ODA (see above). In addition, here has been a relative shift in the orientation of TC. Rather than being associated with the development or implementation of investment projects, providing feasibility and engineering studies, project management or other professional services, TC is now focused on the provision of training and 'experts' (often foreign consultants) for 'institutional development'.[30] The 1997 WB *Annual Report* explains, WB (1997b, p. 126):

> Bank-supported TA in the early years, and through the 1970s and much of the 1980s focused on engineering – assistance designing bridges, dams, highways, and telecommunications systems – which involves working with identifiable products that are based on well-established technology that can be transplanted or modified relatively easily. In recent years, however, TA increasingly has been directed at capacity building which entails a more complex process of creating and disseminating knowledge for development purposes at all levels of society.

TA for capacity-building is largely concerned with making markets work better (Ridker 1994, p. 77; see also McMahon 1997, p. 9) and, more specifically, involves advice and training on economic policies, judicial reform, private sector development (PSD), financial sector reform, etc. A UNDP (2002b, p. 183) study of TC and capacity-building in Uganda, for instance, documents how:[31]

> WB Technical Assistance Loans (TALs) have been instrumental in institutional development for economic policy design, implementation and management, particularly in the Ministry of Finance, Planning and Economic Development ... The Economic Policy Research Centre at Makerere University was established with TC from the WB through the African Capacity Building Foundation. Technical cooperation has also been instrumental in developing a number of reform processes. These include liberalising the domestic goods and services markets; dismantling the Marketing Boards; privatising many government enterprises; floating the exchange rate; legalising Forex bureaux; restructuring and opening the

[30] Foreign aid sustains a large consultancy industry in OECD countries which has been estimated at US$ 4 bn a year for SSA, or 30 percent of aid to the continent (WB 2004f, p. 216). See also WB (2000e, p. 244):

> In some countries technical assistance accounts for 40 percent of aid ... with large numbers of technical experts from donor countries in Africa – estimated by some at 100,000 – a lot of technical assistance is ... effectively tied, flowing back to donor countries with less long-run impact on the development of recipients' economies.

[31] See also Brown (2001) on how the presence of TA made it more likely for local governments in transition economies (here the Ukraine) to engage in contracting out public services; and Ciurlizza (2000) on the nature of judicial reform promoted by legal TA in Latin America.

budget process; easing government licensing procedures; and decentralisation.

Gupta et al. (2006, p. 14) further examine the relative shifts in the sectoral allocation of TC. They find that the share of TC allocated to social infrastructure (including health, education, and government and civil society) has increased since the 1990s, whereas that for economic infrastructure, agriculture, and industry has declined. This re-orientation and expansion of TC has happened notwithstanding Berg's (1993) classic and powerful critique of institutional development via TC.[32]

Thirdly, there has been a shift away from more traditional project support towards general budget support. Although general budget support currently accounts for only a small, yet fast-growing share of total DAC (bilateral) aid, it takes on significant proportions for poor aid-dependent countries (OECD 2006b, p. 20; De Renzio 2006, p. 4; Lister and Carter 2006). For Booth and Lawson (2004, p. 17), the general budget support approach marks:

> a radical departure from previous aid arrangements, which have relied either on project-based aid or on forms of programme aid linked directly to the achievement of *ex ante* conditionalities.

'New' budget support seeks to distinguish itself from previous programmatic approaches in its projected move away from policy conditionality towards a more 'partnership-based' approach in the provision of macroeconomic support, particularly in the context of the PRS initiative discussed below (Lawson and Booth 2004, pp. 26-7).[33] Yet, the approach often allows for further intrusion in how the debtor/recipient state organises its public finances as it serves as a vehicle for conditions touching upon budgetary procedures, public financial management and fiscal policy (see Lister and Carter 2006).[34]

The shift towards programme aid has been particularly important for WB lending. The combined share of adjustment lending in total WB lending (IBRD and IDA) has exceeded one-third since fiscal year 1998 (FY98). Figure 1.5 illustrates how adjustment lending as a share of WB lending reached 53 percent in FY99,

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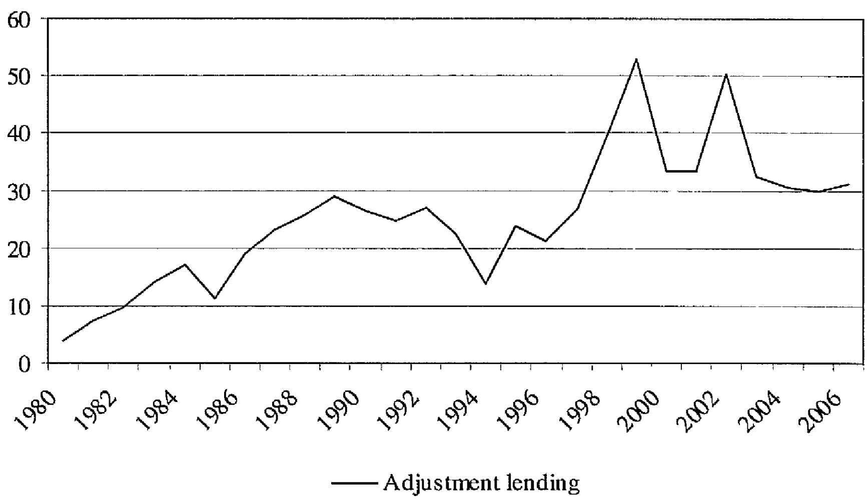
[32] See also Brewster and Yeboah (1994, p. 157); Berg (2002); Mkandawire (2002); Helleiner (2002, p. 258); Godfrey et al. (2002); UNDP (2002b, pp. 20-35); Danielson et al. (2002); WB (2000e, p. 244); OED (2005, p. 44); and White (2005, p. 11.)

[33] See also de Renzio (2005). In a donor-commissioned evaluation of general budget support, Lister and Carter (2006, S3), however, observe how the change from structural adjustment programmes to general budget support 'has tended to be gradual, to be present as an intention before it is realised in practice, and to be more significant in the eyes of the donors than in those of partner governments'. See also Unwin (2004, pp. 1509-11).

[34] The 2005 *Development Cooperation Report* acknowledges this persistent underlying tension, see OECD (2006b, p. 30).

peaked again in FY02 (the crisis in Turkey) and dropped back to 33 percent in mid-FY04.

Figure 1.5: Share of adjustment lending in total WB lending (IBRD + IDA), FY80-06 (commitments)



Source: ALCID (2007).

For the IDA, the share of adjustment lending has been in the range of 15-27 percent since FY98 (WB 2004b, p. 14) and, in 2004, amounted to just under 30 percent (WB 2005i).[35] For the Africa region, quick-disbursing support averaged 35 percent of new annual commitments over the period FY92-02, and had reached, between FY98-00, a peak of approximately 50 percent of annual commitments (WB 2004e, p. 14). These trends imply that the operational guidelines regarding WB lending have been exceeded. According to the latter, the share of adjustment lending should normally remain below 25 percent of total WB commitments (averaged over three years).

Most recently, programme lending has been renamed 'development policy lending' (DPL) and WB management expects DPL to remain at around one-third of the WB's portfolio (WB 2004b, p. 15).[36] This is high for an instrument that was originally designed as a crisis-response and was introduced under a 'special

[35] The share for IBRD alone exceeded 37 percent from FY98 onwards – reaching 63 percent in FY99, and receded to 33 percent in mid-FY04.

[36] The term DPL will substitute for each of the following adjustment lending instruments: Structural Adjustment Loans (SALs), Sectoral Adjustment Loans (SECALs), Special Structural Adjustment Loan, Rehabilitation Loan, Subnational Adjustment Loan, Programmatic Adjustment Loan. Although governed by the same operational rules as development policy lending, development policy support to an IDA country with a PRS Paper (PRSP) will still be termed a Poverty Reduction Strategy Credit (PRSC) (WB 2004b, p. 12).

circumstance' provision of the WB's Articles.[37] It is also much higher than at any point during the official 'structural adjustment' era (see figure 1.5). The recent change in nomenclature, from adjustment lending to DPL, then seems to indicate a shift from a focus on short-term reforms to medium and long-term programmes, where DPL now explicitly aims, WB (2005g, p. 7):

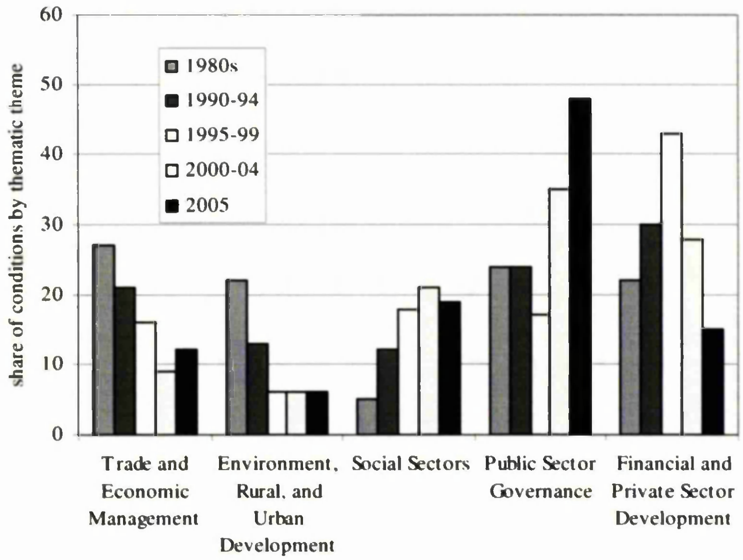
> at supporting a country's programme of policy and institutional actions to promote growth and achieve sustainable reductions in poverty reduction.

The increased importance of policy-based lending in WB lending has been accompanied by a shift in the thematic distribution of the conditions attached to this lending. WB programmes have become more focused on public sector governance and social sector issues, and less on economic management, trade and rural and agricultural issues. In FY97, close to 60 percent of the approved loans had conditions in public sector governance.[38] By FY04, 93 percent of loans approved included such conditions, and in FY05 all loans had public sector governance conditions (WB 2005n, p. 10). This development is also reflected in the share of conditions going to the category 'public sector governance and the rule of law'. Figure 1.6 indicates how the latter increased from around 25 percent of loan conditions during the 1980s and 1990s to 35 percent in the early 2000s, and stands at close to 50 percent in FY05. Within this category, 'public expenditure, financial management and procurement' account for the largest share (WB 2005n, p. 10).

[37] Under the 'special circumstance provision', programme lending was to cater for a situation when a country experienced an acute balance of payments need and when external resources to finance this gap could not be mobilised through more conventional forms of financing (WB 2004b, p. 11). The new guidelines issued as part of the new framework of DPL have dispensed with a numerical limit on the share of DPL in the Bank's aggregate portfolio (WB 2004b).

[38] The categories classified by the Bank under 'public sector governance' include: public expenditure, financial management and procurement; tax policy and administration; administrative and civil service reform; other public sector governance (including parastatal reform); anti-corruption measures; de-centralisation; and debt management.

Figure 1.6: Trends in the share of WB conditions by thematic area, FY80-05



Source: WB (2005g, p.11).

The explicit shift in the focus of conditionality, however, does not necessarily imply that other concerns have disappeared from the WB agenda. Indeed, a background paper to the WB's latest conditionality review observes that although reforms in the private and financial sectors are not necessarily covered by policy-based lending and its conditions, they continue to be important areas of WB engagement (WB 2005n, p. 11). Officially only 15 percent of conditions in FY05 loans were recorded as related to financial sector and PSD, down from 28 percent in FY00-04 on average, and from 37 percent during the 1990s (see figure 1.6). However, the WB points out, and this is further explored across this dissertation, other mechanisms and tools are increasingly used to address policy weaknesses in these areas. These mechanisms include the CPIA, deconstructed in chapter six, and a host of diagnostic and advisory services, documented in chapter two. The use of these tends to imply that particular WB priorities remain entrenched in operational realities, yet become less observable.

Finally, in the context of the emphasis on capacity-building, the criteria of success of project finance have been redefined. The latter is no longer solely assessed on the basis of economic rates of return, but equally in terms of its influence on the prevailing ideas regarding apt management of economic resources in the particular sectors concerned. Project finance becomes a vehicle for 'policy learning'.[39] The WB's flagship report on aid (WB 1998a, pp. 90-1) explains:

> The design of projects needs to adjust to the reality that money or capital stock is less important than good institutions or better ideas. The point of an education project is not to increase funding for the sector (this can be done without projects) but to help reformers change the ideas, institutions, and policies in the sector. A truly effective project is a bundle of activities that does not just build schools, but, more important, helps to change how schools are run to provide high-quality education ... An important corollary of this is that the success rate of financed projects is not particularly relevant – if success is narrowly defined ... Failed projects can often teach as much (or more than) successful ones.

It now seems that the more development co-operation fails, the more it succeeds, as the failures apparently hold important learning potential and increase the aptitude of a capacity-building role for the donor community.

1.4.3 Partnership and ownership

The current attempt of donors to increase their grip over recipients' policy formation processes, both through performance-based aid allocations and particular shifts in the instruments and sectoral destination of aid, has coincided with the promotion of more 'consultative' and 'country-driven' approaches. An emphasis on 'partnership' and 'ownership' seeks to cast the donor-recipient relationship in a new light. In the partnership framework, development co-operation does not try to do things *for* developing countries and their people, but *with* them. Development co-operation becomes a 'collaborative effort to help them increase their capacities to do things for themselves' (OECD 1996a, p. 13). In addition, while earlier aid efforts involved working almost exclusively with governments, now partnerships are sought also outside government.

This emphasis on ownership and partnership has been most clearly seen with the PRS initiative, introduced by the WB and the IMF in 1999.[40] The PRSP projects to provide a 'country-owned' policy framework for poverty reduction and to facilitate co-ordination between various donors. Drafting a PRSP, however, pre-

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[39] See also Gilbert et al. (1999, p. 621).

[40] See Jones (2000) and Foster (2000) on sector-wide approaches (SWAPs) as another attempt to bring donor support (here to a particular sector) within a common management and planning framework, with a particular emphasis on participation of local stakeholders (including government, local beneficiaries, private sector representatives) in the design of the sector programme.

conditions access to the concessionary resources of the IMF through its Poverty Reduction and Growth Facility (PRGF) and to the IDA programme of the WB, as well as eligibility for the Enhanced HIPC Initiative.[41] Once completed, the PRSP is reviewed jointly by WB and IMF staff, who advise their respective Boards on whether the PRSP is a sufficient basis for concessional lending and/or debt relief.[42] The process of producing a PRSP is to be repeated every three years and PRSPs are currently on the agenda of just over sixty LICs.[43]

The PRS initiative seeks to mark an advance on previous aid-delivery mechanisms in the following respects. First, the PRS process is to be based on 'country ownership' and 'participation' from 'all major groups in society'. Secondly, the PRSP offers a new vehicle for coordination and harmonisation among donors, reducing costs of donor fragmentation. Thirdly, the PRS process supports a move away from project-centred assistance setting development assistance in an explicit 'policy-consistent framework'. It is to embody a long-term perspective, with the need for medium-term commitments accompanied by consideration of appropriate timing, performance criteria and monitoring arrangements. Fourthly, through its emphasis on 'country ownership' and budget support, the PRSP seeks to support a move away from excessive conditionality. With aid more focused on 'willing reformers', donors would attempt to lighten conditionality and mainly support measures the country 'itself' included in its PRSP. Fifthly, the thinking underlying the PRSP is to be 'comprehensive', recognising the 'multidimensional' nature of poverty and the scope of action necessary to effectively reduce poverty (Wolfensohn and Bourguignon 2004, p.10).[44]

'Participation' is often projected as the crucial dimensions differentiating the PRSP from previous generations of aid instruments. Defined in the PRPS sourcebook as, Klugman (2002, p. 237):

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[41] The PRGF was created by the IMF in 1999 as follow-up instrument to the Enhanced Structural Adjustment Facility (ESAF), with an ambition to highlight explicitly the new anti-poverty imperative. The PRGF would try to induce policies that would focus both on economic growth and poverty reduction and that would, as a result of better national ownership, be implemented more consistently. The Bank added its own programmatic lending instrument, the PRSC, in 2001. Countries that borrow from both the IDA and the IBRD, commonly referred to as 'blend' countries, and that do not seek PRGF arrangements do not have to produce a PRSP in order to have access to IDA resources.

[42] More precisely, the Boards endorse each of the required documents of the PRS process – Interim PRSP, PRSP, Annual Progress Report, and PRSP Preparation Status Report – on the basis of a Joint Staff Assessment (JSA), recently renamed Joint Staff Assessment Note (JSAn).

[43] For the full list see http://siteresources.worldbank.org/INTPRS1/Resources/boardlist.pdf.

[44] See also the Rome and Paris Declarations of aid effectiveness on how, under the new guidelines of aid harmonisation referred to above, these principles have been adopted to steer donor assistance in general.

> the process by which stakeholders influence and share control over priority setting, policymaking, resource allocations, and/or program implementation,

it seeks to provide guarantees for national ownership of policies to improve commitment to and hence sustainability of reform and, as a result, aid effectiveness (WB 1998a). Stakeholders are identified as: the general public, particularly the poor and vulnerable groups (such as youth, women's groups, and the disabled); the government, which includes civil servants and elected representatives in central ministries, line ministries, local government bodies, parliament, cabinet and general assemblies; civil society organisations, including networks, NGOs, community-based organisations, trade unions and guilds, academic institutions, and research groups; the private sector (umbrella groups representing groups within the private sector, professional associations); and donors who are expected to participate in the PRS process to co-ordinate efforts, share costs, gain joint ownership over the PRSP and create synergies between differing donor perspectives and skills (Klugman 2002, p. 250).[45]

From the point of view of the IFIs, PRS participation aims for both better design of poverty reduction strategies as a result of improved diagnostics, a richer policy debate, and improved policy implementation resulting from enhanced accountability and ownership. Assessments of the PRSP exercise, however, converge on a broad consensus denouncing the insufficient depth and breadth of the participatory process in the PRS initiative, with particular implications for the quality of the effected ownership. The main issues raised in the literature can be summed up as follows.

First, it has been observed how participation in PRSPs is characterised by the disproportionate engagement of NGOs, often with strong links to international NGOs, and donor agencies, to the detriment of poor people and organisations representing their interests (ActionAid 2002; Brock et al. 2002; Booth 2005; Fraser 2005; Gould 2005).

Second, the divide between consultative and constitutional representative processes has been repeatedly pointed out, and the danger looms of the substitution of conventional institutions of representative democracy by ad hoc mechanisms involving particular segments of civil society where those that are excluded have no

[45] An IMF evaluation (IEO 2004, p. 28) adds that although 'empowerment of disadvantaged groups' receives a lot of emphasis as an objective of participation in external commentaries, it is not included among the explicit objectives of the PRS initiative.

legal right to demand representation (see Brock et al. 2002; UNCTAD 2002; Brown 2003; Whitfield 2005; Gould and Ojanen 2005; Fraser 2005; Driscoll and Evans 2005). For Dijkstra (2005, p. 452), the neglect of the role of parliament appears as a 'conscious decision' rather than an 'unfortunate omission'. This follows Hearn's (2001, p. 52) observation that parliaments are more likely to offer more leverage to exert autonomy than civil society precisely because they are not dependent on foreign donors.[46]

Third, not all topics touching upon economic and social policy are up for discussion in the participatory exercises of the PRS process. Consultative spaces tend to steer away from debates on macroeconomic policies or structural policies touching upon privatisation, land reform, labour market reform, trade liberalisation, etc. (Bertelsen and Jensen 2002; Nyamugasari and Rowden 2002; McGee et al. 2002, p. 13; Brock et al. 2002, p. 48; Alexander 2004; Dijkstra 2005; WDM 2005; Gould and Ojanen 2005, p. 29). Indeed, an IMF evaluation notes that, IEO (2004, p. 29):

> there is little evidence of a substantive impact of participatory processes on the macroeconomic and related structural policy choices embedded in PRSPs. In a number of cases, some important but controversial structural policy issues did not surface in the broader debate around the PRSP.

The 'economic' is treated as separate from the 'social' with greater room for consultation in issues pertaining to the latter, with the resultant PRSP often emerging as a social strategy separate from economic policy.

Fourth, the language used in economic matters may erect barriers of 'technicality' and groups disagreeing with the neo-liberal point of departure and issuing alternatives to this, run the risk of being excluded from the debate on the ground that they do not comprehend economics.

Fifth, those leading the participation exercise are frequently of the opinion that work needs to be done to make domestic organisations or constituencies understand the necessity of certain policies, such as for instance privatisation, rather than to use the PRS process as a way to establish whether or not these are to be implemented. In a WB-sponsored assessment of the international experience in 'citizen's' participation in macroeconomic policy, Brinkerhoff and Goldsmith (2003, p. 685) explain:

[46] It should be noted that to the extent that the neglect of the role of parliament is being recognised by the IFIs (see e.g. IDA/IMF 2002, p.14), they have been prompt to devise a set of special training programmes with a particular focus on providing parliamentarians with the necessary capacity to appreciate what are 'appropriate' policies (see also chapter two).

> Most aid recipient governments have agreed to orthodox macroeconomic programs, but they seldom have 'owned' the reforms and often have reverted to unbalanced public budgets and inflationary monetary policies. ... Recognising these problems, the international community now wishes aid recipients to do more to build broad public consensus for sound macroeconomic policies ... Civic involvement is expected to deepen the commitment to macroeconomic reforms, with fewer policy reversals and more impact on poverty.

Sixth, it is often unclear how the outcomes of the consultation exercises are incorporated in the actual PRSP document. Although the PRSP implies 'process conditionality' of consultations, it does not strictly require that contributions made in this process are taken into account in policy-making. The final drafting of the document is considered exclusively the domain of national governments often assisted by WB/IMF-appointed consultants (ActionAid 2002; Brock et al. 2002; Bertelsen and Jensen 2002; Booth 2003; Brown 2003; Alexander 2004; SIDA 2005; Dijkstra 2005; Driscoll and Evans 2005; Booth 2005).[47] Furthermore, the bulk of the drafting of the PRSP is often done in English, with only final outputs translated in local languages (IEO 2004, p. 24).

As a consequence, and seventh, the nature of the participatory exercise in PRSPs seems to resemble more a consultative than a participatory approach, which runs the risk of bestowing a false 'ownership' legitimacy to an essentially predetermined framework (McGee et al. 2002; Gould and Ojanen 2005; UNCTAD 2002, p. 6).[48] In this context, Brock et al. (2002, p. 43) document that certain civil society organisations in Uganda have started to advocate a disengagement from the PRSP process, on the grounds that the participation allowed to them was:

> a legitimating device wielded by governments and IFIs, rather than an opportunity to transform either the status quo or the neoliberal orthodoxy of poverty reduction policies.

Eighth, as a result of the often circumscribed quality of the ownership of PRSP processes, the content of various PRSPs has tended to be relatively similar

[47] This often takes place in technical units located in the Ministry of Finance or under the Presidency which are dependent on external financing (see e.g. Bertelsen and Jensen 2002; Driscoll and Evans 2005).

[48] Following McGee and Norton (2000) there are several typologies or 'ladders' of participation. 'Consultation' is understood to involve a relatively low-intensity form in which participants may express views without any commitment from those inviting participation that these views will be taken into account. A more intensive form, where such a commitment would exist, is often referred to as 'joint decision making' (see also McGee et al. 2002, p. 7).

across countries.[49] The macroeconomic and structural policies proposed in PRSPs fail to show a significant departure from the policies that were being promoted under the WC. Gottschalk (2005) looks, in particular, at the macro content of 15 PRSPs, and finds that their fiscal and monetary policies are narrowly focused on fiscal balance and price stability. The author adds that, although most of the PRSP countries in his sample have already achieved price stability – often with inflation at very low levels, this is not reflected in a broadening of the focus of monetary policy to encompass additionally growth and employment objectives.

Nevertheless, and ninth, PRSP countries have experienced slightly more autonomy in designing safety-nets, and policies for the social sector (mainly in terms of public expenditures on health and education).[50] The links between macroeconomic and structural policies and poverty reduction have, however, remained weakly understood in PRSPs, with Poverty and Social Impact Analysis (PSIA) only lately starting to try to fill the gap (UNCTAD 2002, p. 21; OED 2004, p. 43; IEO 2004, p. 63).[51] In essence, the PRSP then seems to be an exercise in which the recipient country facilitates a policy framework developed according to WB/IMF priorities that ties certain aspects of social policy formation to the well-known macroeconomic and institutional framework as embodied in the conditions upon which aid is allocated (under the PBA system).

Tenth, closer scrutiny of the role of the PRSP in the aid architecture further reveals how the PRSP does not function as an effective vehicle to affect the conditions under which a LIC has access to funds, notwithstanding its proclaimed ambition. A recent WB evaluation concludes that, OED (2004, p. 18):[52]

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[49] See ActionAid (2002) (Haiti; Kenya; Malawi; Nepal; Rwanda; Uganda; and Vietnam); UNCTAD (2002) (Sub-Saharan Africa); WDM (2005) (42 PRSPs); IEO (2004) (23 PRSPs); Bertelsen and Jensen (2002) (Nicaragua and Honduras); Kubalasa (2003) (Malawi); Kar (2003) (Sri Lanka); Dijkstra (2005) (Bolivia; Nicaragua; and Honduras); Seshamani (2005) (Zambia); Stewart and Wang (2003) (27 PRSPs).

[50] See, however, UNCTAD (2002, pp. 42-50) on how PRSPs have incorporated an emphasis on the provision of universal primary education and health care and, at the same time, sought to promote market-based mechanisms in secondary and tertiary education as well as in curative health care (see also Kar 2003).

[51] Note that PSIAs are specifically aimed at the assessment of well-defined reforms rather than broad strategies (IMF/WB 2005b, p. 52). This is notwithstanding the repeated call by HIPC ministers to 'shift the focus of attention from the extensive effort to diagnose poverty and "count the poor" to analysis of causes of poverty and its links to macroeconomic policies' (Debt Relief International 2001, p. 6).

[52] See also IMF/WB (2005b, p. 10). See WB (2004b, p. 45) and Wood (2005) more specifically on the relationship between the PRSP and the PRSC; and IDA (2002b, p. 42), IDA/IMF (2002, p. 31), and WB (2004k, p. 22) on the relationship between the PRSP and the WB's Country Assistance Strategies. See Killick (2002), Stewart and Wang (2003), and IEO (2004) on the PRSP and the PRGF. The PRGF, like its predecessor the ESAF, acts as a validation for access to flows of other agencies, *irrespective* of progress regarding a PRSP.

neither the donors nor the Bank have defined specifically whether or how they should change the content of their programs to reflect PRSPs … Overall, there is still little evidence that donors have coordinated and selected the majority of their programs in response to PRSPs.

Wood (2004, p. 41) adds:

> PRSPs are often just a starting point for negotiation between the governments and the IFIs … PRSPs are often vague in their policy details … when policies are better elaborated in PRSP documents these typically draw on the conditions and policy matrices defined in pre-existing IFI and other donor programmes and projects. Thus, rather than the policies and reforms defined in the PRSP forming the basis for IFI conditions, the reverse is more typical.

Yet, and finally, while the PRSP might fail operationally, it plays an important ideological role through its function in regulating domestic understandings of policy options in accordance with IFI-identified priorities. The PRS project implies a far-reaching and widespread 'capacity-building' enterprise that targets various segments of society, including the executive branch of government, parliament, regional and municipal governments, and civil society organisations, and in which the IFIs assume an important role (see IDA/IMF 2002, p. 22). To this end, the IFIs deploy a host of tools, including a PRSP Sourcebook drafted jointly by WB/IMF staff;[53] workshops; conferences; a learning programme of the WB Institute in support of the PRS process ('Attacking Poverty'); training; guidelines; and so on. In addition, the WB and Fund staffs present the country authorities with a common country-specific perspective on the 'key' impediments to faster growth and poverty reduction. This draws attention to the newly proclaimed knowledge role for the WB, which is further explored in chapter two.

The PRS initiative then appears as a valuable mechanism through which IFI imperatives can be internalised by various segments of society in LICs. Booth and Lucas (2002, p. 3) candidly observe:

> no one should be under the illusion that the coming of PRSPs implies the end of old-style conditionality and performance benchmarks. It would be a mistake even to assume that it guarantees a reduction in the number and complexity of such conditions. But the role of PRSP processes in the

[53] See http://web.worldbank.org/WBSITE/EXTERNAL/TOPICS/EXTPOVERTY/EXTPRS/0,,contentMDK:20175742~pagePK:210058~piPK:210062~theSitePK:384201,00.html.

> Enhanced HIPC decision and completion procedures, and in the broader panorama of IDA and IMF activities, does bring something new into the incentive structure facing policy makers in countries of the region. It implies a leavening of traditional conditionalities with a new form focused on in-country *processes*.

Such an understanding of the process resonates in the most recent joint WB-IMF review of the PRS initiative, where an appraisal of the role of the PRSP in streamlining ideas on development and 'apt' routes to poverty reduction takes prevalence over its role in organising or influencing the terms on which a country receives aid (IMF/WB 2005b, p. 3). The WB's Strategic Framework for Africa (WB 2004e, p. 78) further highlights:

> As IDA works within this [partnership] framework, how IDA's effectiveness is measured also needs to change. Until now, IDA's impact has largely been measured through the *projects and programs* it has financed. Current measurement systems internal to the Bank ... have primarily focused on judging the success of project-based lending. Yet, two other areas for results also become critical in this model: policy dialogue and partnership. *Policy dialogue* includes both the analytical work done by the IDA, as well as other means of advising clients: informal policy notes, policy discussions, and workshops. As IDA moves toward supporting a country's PRSP, there needs to be an increased focus on how IDA is supporting the PRSP process, including the underlying analysis of development issues and solutions.

In a last instance, these observations need to be tied back to the literature largely drawn upon above. The literature critically assessing the PRS initiative has been growing rapidly. Its contributions have, however, often been undertaken or commissioned by agents with a particular interest in the initiative (donor agencies or NGOs with a commitment to the participatory approach as an alleged route to 'empowerment').[54] These easily tend to have a technocratic bent, identifying 'problems' and 'solutions' within a context of broad acceptance of the PRSP framework, and tend to defend the assumption that the PRSP approach must be preserved (see also Fraser 2005, p. 235; Dijkstra 2005, p. 462). The intricate relationship of authors to important sponsors of the initiative can produce dubious

[54] There are important exceptions, see, among other, Brown (2003); Weber (2004a); Fraser (2005); Dijkstra (2005); Whitfield (2005); Tan (2005); Gould and Ojanen (2005).

premises. Booth's (2003, p. 155) projected understanding of ownership in his introduction to the acclaimed review of the PRS experience in seven African countries commissioned by the Strategic Partnership with Africa, serves as an indication:

> Morrissey … maintains … it does not fatally compromise the prospects of a policy being effectively implemented that it has been taken 'off the shelf', for example, from a donor or international agency source. We have no trouble going along with this. It implies, among other things, that the fact that the PRSP process is an external initiative, from the point of view of all the study countries, is not a major problem for the assessment of ownership.

While the 'constructively critical' PRSP literature (Booth 2003, p. 132) deplores, as highlighted above, the failures of participation to produce real national ownership of the policy space, its contributions, nevertheless, easily fail to provide insights on how these failures emerge as both effect of and conduit for IFI imperatives. The way in which the structural features of the reality within which the PRS initiative is embedded precondition and limit the latter's possible outcomes has been ill-appreciated. The 'constructively critical' literature often proposes to remedy the current unsatisfactory state of affairs by doing more of the same, i.e. to increase the participatory exercise. By focusing on what are perceived to be capacity problems, however, this tends to reinforce the IFI agenda of 'capacity-building' for policy-making, and fails to identify the structuring role the PRS process plays in debtor-creditor relations (see also Tan 2005).

1.5 Conclusion

It was argued in this chapter that, despite a declining willingness to pay on behalf of the donor community, there has been a concerted attempt to scale up interventionist ambitions and increase the disciplinary power of ODA in the poorer aid recipient countries. We illustrated how this transpires from a set of aid practices including performance-based aid allocations (or 'selectivity'). In this manner, donors try to increase their leverage to make aid recipients behave according to a set of predetermined norms. These norms are summed up in the CPIA, the formal set of criteria the WB deploys to allocate its aid flows and which have been heavily promoted across the broader donor community.

The attempted increase in donor control over recipient policy also appears in a broad qualitative re-orientation of aid flows, both in terms of sectors targeted and instruments used – under the 'capacity-building' emphasis. Selectivity, further, combines with the 'ownership' discourse through the PRS initiative. We argued, however, that the latter mainly effects the streamlining of purported poverty-reduction strategies across LICs, with a particular role for the donor community and the WB in particular, rather than providing a genuinely country-owned operational framework for aid. Even though the PRSP emblematically seeks to project the idea that domestic processes of 'participation' and the consequent 'ownership' of policies steer a country's poverty reduction strategy it, in effect, provides another attempt to 'teach' the Southern constituencies, governments and civil society alike, what 'apt' development and poverty reduction strategies look like. Hence, we posit, even if the PRS initiative fails operationally in terms of bringing about genuine ownership of poverty reduction strategies, it fulfils an important ideological role.

In the rest of this dissertation, we focus on selectivity and its particular combination with the emphasis on a knowledge role for the donor community, and for the WB as a lead player, in particular. This brings us to the next chapter.

Chapter 2. Knowledge as aid

2.1 Introduction

The WB has played a distinct role in the re-definition of the aid engagement documented in the chapter above. Whether it has been through the promotion of selectivity, the definition of particular criteria upon which selectivity can be exercised, the design of the PRSP approach (in collaboration with its Bretton Woods twin) or the clear move towards an approach to development assistance that favours programme aid, the Bank has charted the way for other participants in the donor community. The Bank has been a leader in the development community since a conjunction of events in the 1980s, not least its engagement in what were designated 'structural adjustment' activities. Attempts at increased coordination across the donor community have tended to enhance this role.

The trends in development finance documented in the first section of chapter one, however, have had particular repercussions for the Bank, and raise significant questions about its mission. The financial intermediation role of the so-called 'hard window' of the Bank, the IBRD, which provides finance at near-market terms to the official sector of MICs and credit-worthy poorer countries, has waned considerably in the context of the rapid development of private international flows. Concurrently, the replenishments of the Bank's 'soft' or aid window, the IDA have been more difficult to obtain as the aid effort has shrunk. Yet, at the same time, the two other, albeit smaller, affiliates of the World Bank Group (WBG), the International Finance Corporation (IFC) and the Multilateral Investment Guarantee Agency (MIGA), which engage directly with the private sector, have seen unprecedented expansion.

Against this backdrop, the Bank has made various changes. These have included, amongst other things, an attempted re-definition of its approach to development, a re-invigoration of its business with middle-income clients and a re-emphasis on the centrality of poverty to its mission ('our dream is a world free of poverty'). Notably, the Bank has specifically drawn attention to its role as a knowledge provider. This was most emblematic with the formal Knowledge Bank declaration by former Bank President, James Wolfensohn (1996a, p. 7). And, even though the 'knowledge' mission can hardly repair the disconnection between the Bank's projected purpose, to be a public IFI seeking to promote development and combat poverty, and the reality implied by the underlying shifts between the official and private arms of the Bank, it might serve to draw attention away from the Bank's financial role by emphasising its supposedly unique ability to share decades of learning about economic development with clients around the world. Furthermore, the knowledge idea found rapid resonance across the broader donor community, as it brought to the fore the implicit emphasis on policy learning that prevails across the aid practices highlighted in chapter one.

This chapter locates and explores the emergence of the 'knowledge paradigm'. It does so first by looking at how new financial, economic and political realities have brought a set of contradictory pressures to bear upon the Bank, from where the idea originated. Secondly, the chapter goes on to explore more closely the knowledge emphasis in the Bank's ensuing renewal exercise. Although the Bank has aspired to a leadership role in the intellectual and policy realm of development since at least the McNamara era (1968-1981), a formal emphasis on knowledge gained primary significance under the Presidency of James Wolfensohn (1995-2005). Moreover, while the knowledge paradigm originally focused on the organisational aspects of the institution, it rapidly broadened to accommodate a wide-ranging definition of a knowledge mission for the Bank. We proceed to document how the knowledge idea rapidly caught on in the broader donor community. 'Knowledge' propagation has, of course, always been a dimension of aid, as aid is given with the proclaimed intention of promoting development and so logically brings to bear a whole set of ideas regarding what development is and how it is best achieved. Now, however, knowledge is placed at the centre of the aid discourse. The idea accommodates the decreasing willingness of the donor community to finance the aid enterprise and, further, tallies well with the new emphases regarding aid that have been emerging.

Thirdly, we critically dissect the way in which the Bank understands its own knowledge role. Such an exercise reveals a set of pervasive biases that have tended to characterise Bank knowledge activities. This is followed, fourthly, by an extensive mapping of the Bank's knowledge exercise in practice. Special attention is drawn to the importance of development knowledge generated in the Bank's operational departments and to the recent extension of the Bank's knowledge exercise beyond the institution – through a host of 'global' knowledge initiatives.

2.2 The World Bank: between a rock and a hard place?

The Bank has been subject to a set of contradictory tendencies. In the context of increased private flows and the rapid decline of its financial intermediation activities, the case for its existence as a public finance institution has come to depend increasingly on its capacity to provide concessional flows as a development agency. The main donors, however, have tended to make fewer resources available for the Bank's aid window, the IDA, with the exception of the last replenishment. They have furthermore tended to use the IDA increasingly as a conduit to impose their own priorities on Bank activities, thus undermining the Bank's projected multilateral character. At the same time, the WBG's main effort has become sharply focused on PSD and private firms have increased as a proportion of the WBG's clients. Such use of the Bank's financial resources, at subsidised rates, to support corporate investment, sits uneasily with the Bank's supposed mission, as a public IFI, to promote development and combat poverty.

2.2.1 The World Bank in a changing world

The Bank refers to the two institutions within the WBG, the IBRD and the IDA, whose clients traditionally belong to the official sector. The IBRD provides loans at near-market rates to MICs and better-off LICs, the Bank's so-called 'hard window'. The IDA, the Bank's 'soft window', was added to the WBG in 1960 and provides concessional finance to the poorest countries. The two 'windows' share the same staff and management structure.

The IBRD obtains its funds from the international financial markets where it enjoys a triple-A rating. Voting rights are distributed in accordance with paid-in capital. At present, the main shareholders of the IBRD are: USA (16.39 percent), Japan (7.86 percent), Germany (4.49 percent), France (4.30 percent) and the UK (4.30 percent) (WB 2005j). After the General Capital Increase of 1988, the constitutional majority for changing the Articles was raised from 80 to 85 percent to preserve the US veto (Kapur et al. 1997a, p. 1205). Although the combined share of the OECD members fell during the 1980s and 1990s, it still represents a comfortable majority, in excess of 60 per cent.

The IDA obtains the bulk of its resources through tri-annual replenishments by donors, represented by the 'IDA Deputies', who set the IDA agenda through the replenishment procedures. Currently, the main IDA donors (and their relative voting powers) are: USA (11.61 percent), Japan (8.92 percent), Germany (5.71 percent), United Kingdom (4.72 percent) and France (3.68 percent) (IDA 2005, p. 72).

The WBG also consists of two other institutions or affiliates which directly engage with the private sector. The IFC was created in 1956 to finance, facilitate and insure corporate investment in poor countries. It does this by providing loans, taking equity positions, offering risk management products, and providing technical advice to the private sector (or enterprises that are majority-owned by the private sector) (see IFC 1996, pp. 9-18). The IFC shares its Board of Governors, Directors and President with the WB, but has its own mandate, operations, Articles of Agreement and funding. It currently has 175 members and the voting share of each member is determined by the share of capital paid in, with, at present, the US providing the main share of IFC funds (23.95 percent). The IFC raises funds through international capital markets and, like the WB, benefits from a triple-A credit rating.

Finally, in 1988, the MIGA was added to the WBG with the objective of providing political risk guarantees to new foreign private equity and debt investments.[55] MIGA instruments consist of guarantees to foreign investors (international political risk insurance) against losses caused by non-commercial risks such as expropriation, currency inconvertibility and transfer restrictions, war and civil disturbance, or breach of contract (WB 2002g, p. 9). The MIGA has its own Board of Governors, Directors, constitution, budget and chairman. The President of the WB is Chairman of the MIGA's Board of Directors, and they nominate the head of the Agency (its Executive Vice-President). The MIGA has 162 members, divided between capital-exporting states seeking political risk insurance and capital-importing states primarily seeking TA in increasing foreign investment. All members subscribe to the MIGA's capital stock, which provides the Agency with its underwriting capacity.

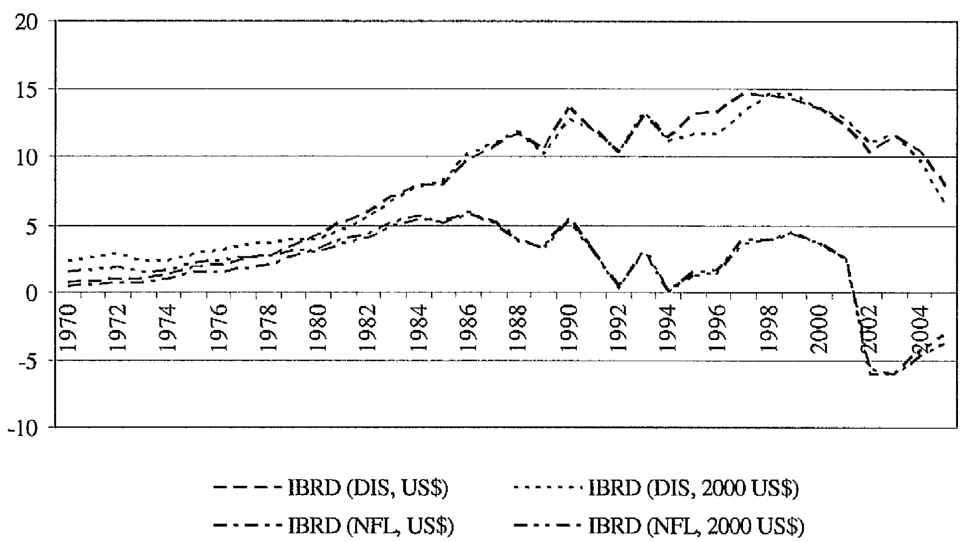
The trends in development finance documented in chapter one have had important implications for the WBG. Before the late 1980s, only the IBRD and the IDA operated on a significant scale within the WBG. Since then, the private sector windows of the WBG have grown at a very fast pace. IFC investments increased four and a half times in real terms between fiscal years 1980 and 2000, and the combined share of the IFC and MIGA in total WBG financial products increased more than seven times, from 3.3 percent to 25 percent, in the same period (WB 2002h, p. 23).

The rapid expansion of the private sector windows of the Bank has been accompanied by an increased difficulty in maintaining the traditional mainstays of the Bank's activities. The operations of the IBRD have stagnated and declined, while donors have become increasingly reluctant to finance the replenishments of the IDA.

[55] The World Bank Group additionally comprises the International Centre for Settlement of Investment Disputes (ICSID), which seeks to encourage foreign investment by providing international facilities for conciliation and arbitration of investment disputes.

Figure 2.1 charts annual IBRD gross (DIS) and net (NFL) disbursements between 1970 and 2004 and shows how net disbursements have been characterised by a downward trend since the mid-1980s and have been negative since 2002.[56] Gross disbursements have equally declined dramatically over more recent years, from nominal levels of just over US$ 13 bn in 1996 to less than US$ 10 bn in 2005. While the IBRD's statutory limitation on its gearing ratio is 100 percent (i.e. outstanding loans can be no greater than equity and callable capital), outstanding loans and guarantees represented only 47 percent of the latter in 2005.

Figure 2.1: IBRD disbursements, gross (DIS) and net (NFL), 1970-2004



Source: GDF Online. The IFS Import Unit Value was used to estimate real values.

The downward trend in gross and net IBRD disbursements has been mirrored, since 1987, by negative net borrowings by the IBRD in the financial markets. Since 1987, IBRD's debt retirement has been larger than its gross borrowings and, by the early 1990s, loan repayments became as big a source of the institution's cash flow as

[56] The net transfers of the IBRD (net lending minus interest received) have been negative since 1987, with the exception of 1998 and 1999 (see Ohlin 1995; Mohammed 2004). Naim (1995), however, observes that for those defending the IBRD as a bank rather than primarily a 'transfer-agent', negative transfers go hand in hand with attempts to maintain top credit ratings in financial markets. A Bank official quoted in Naim (1995, pp. 297-8) asserts:

> I think it perfectly normal that, after a period of strong growth, the Bank has now reached a period of maturity. The Bank's exposure cannot be increased without significant dangers for the rating of the institution by financial markets. It would be dangerous to define any net transfer target, since it would mean that the bank would constantly increase its exposure and, in practice, refinance its own interest charges. I would insist on strengthening the balance sheet, both on the asset side, improving the quality of the portfolio, and on the liability side, building a stronger capital base through larger provisions for losses and more reserves.

market borrowings (Kapur et al. 1997a, p. 1114). The financial intermediation role of the IBRD waned and the ranking of the IBRD amongst global banks fell from 27th place in 1984 to 68th (34th if IDA is included) in the mid-1990s (Kapur 2002a, p. 71).

A set of factors has been invoked to account for the observed fall in IBRD financial preponderance. These mainly concern: the decline in spread banking (the principal form of financial intermediation by the IBRD); the structural shift within private flows with a greater reliance on equity finance relative to debt finance; and the decline in public sector sovereign borrowing (Ryrie 1995; Kapur et al. 1997a; Woodward 1998). However, above all, the cause of the low demand for IBRD financial products has been attributed to the sharp rise in conditionality that accompanies Bank loans which, since the late 1980s, has broadened to include issues relating to the environment, governance and poverty. The resultant rising transaction costs, over and above the financial costs of IBRD loans, have strongly discouraged potential borrowers (Ohlin 1995; Kapur 1997; Gilbert et al. 1999; Einhorn 2001).

In this context, critics of the Bank (and of other multilateral development banks) have called, most famously in the Report of the International Financial Institution Advisory Commission to the US Congress (also known as the Meltzer Report; IFIAC 2000), for the closure of the lending operations of the multilateral development banks (MDBs).[57] The Bank itself has sought to revitalise its IBRD business with a particular emphasis on WBG synergies. It is seeking to draw increasingly on collaborations between the IBRD and the WBG's private sector affiliates, the IFC and MIGA (see Wolfensohn 1996a; WB 2001k). For those MICs where IBRD financing is not in high demand, the Bank has additionally sought to unbundle its lending and knowledge activities and to foster a demand for its 'knowledge' (consultancy) services against payment (WB 2000d, p. 10; 2003f, p. 24; 2006d, pp. 23-6; King and McGrath 2004, p. 76).

While IBRD lending is financed through the sale of bonds on international financial markets, backed by the member governments' capital subscriptions (callable capital), the IDA historically depends on donor contributions for its replenishments. However, in the context of the decreasing willingness of the donor community to finance the aid project in general, donor contributions to the Bank's soft window have fallen over the last decade, with the exception of the last

[57] See Einhorn (2006) for a most recent expression of this argument.

replenishment. Table 2.1 shows the composition of the five last replenishments of the IDA, both in absolute and relative terms.[58]

Table 2.1: Sources of IDA replenishments, IDA-10 to IDA-14.

	IDA-10 (94-96)		**IDA -11 (97-99)**		**IDA -12 (00-02)**		**IDA- 13 (03-05)**		**IDA -14 (06-08)**	
	$ bn	*(%)*	*$ bn*	*(%)*	*$ bn*	*(%)*	*$ bn*	*(%)*	*$ bn*	*(%)*
Donor resources	15.0	75.0	12.7	57.0	11.6	56.9	12.7	55.7	20.7	59.3
IBRD net income contribution	0.9	4.5	1.2	5.4	0.9	4.4	0.9	3.9	1.5	4.3
IDA's own resources	4.1	20.5	8.4	37.6	7.9	38.7	9.2	40.4	12.7	36.4
Total	20	100	22.3	100	20.4	100	22.8	100	34.9	100
Non-donor contributions as a share of the total		25.0		43.1		43.1		44.3		40.7

Source: WB Annual Report (various).

The Bank has increasingly come to depend on its own resources to finance its aid activities. These include: net income transfers from the IBRD; IDA reflows; and investment income from IDA liquidity positions. Donor contributions represented on average over 90 percent of IDA replenishments until the late 1970s, falling only slightly during the 1980s to reach 86.5 percent for IDA-9, the first replenishment of the 1990s (1991-93) (Kapur et al. 1997a, p. 1137). Their share then declined sharply subsequently to only three-quarters for the IDA-10 replenishment, and fell more dramatically to just over half for the succeeding four replenishments.[59]

The last replenishment has, nevertheless, seen a remarkable increase in donor contributions, reversing the downward trend of donor contributions to the IDA. This follows the insistence by the major IDA donor, the USA, to increase the proportion of grants in IDA's disbursements (see Taylor 2002), now set to increase from 19 percent of disbursements under IDA-13 to an estimated 30 percent over the IDA-14 period (WB 2005h, p. 23), and a commitment by donors to compensate the IDA for lost repayments as a result of HIPC debt cancellations.[60] Yet the increase of grants in IDA's portfolio has particular implications for the control over its resources as grants

[58] See also IDA (2001b) for a brief history of IDA replenishments.
[59] This trend has instigated a search for alternative methods to finance IDA. See Sanford (1997) for a discussion.
[60] See Sanford (2004) for a detailed account of the implications of the grant proposition and HIPC debt cancellation for the future of IDA resources.

do not generate reflows and hence guarantee the dependence of the IDA on its donor contributions (see Salazar 2002; Kapur 2003, p. 4).[61]

The success with which IDA Deputies have imposed the grant proposition – together with the broader PSD agenda (see below) – reflects a more general trend which has seen IDA donors increasingly interfering with the IDA's policies (and by extension the policies of the WB). Kapur (2003) refers to the 'aidisation' of the Bank. This results from both the periodicity and the burden-sharing procedures that characterise IDA replenishments, and which have rendered the IDA susceptible to the whims of major shareholders (see also Naim 1995).[62] He documents that while initially the Bank managed to secure inceases in the IDA *and* maintain a certain degree of operational autonomy, this started to change from the early 1980s and was definitely eroded with the end of the Cold War (see also Gwin 1994; Kapur et al. 1997a, chapter 17). Moreover, in any burden-sharing scheme, as Kapur (2003, p. 3) states:[63]

> the most powerful member sets the tone. From the late 1960s onwards, as the United States began a long process of reducing its financial share, other donors began to link their contributions to that of the United States – which paradoxically increased the bargaining power of the United States even as its contributions declined.

In this context, Gwin (1994) and Kapur et al. (1997) document how major European donors, as well as Japan, have started focusing on institutions in which they exercise greater control such as, respectively, the EC's Development Fund and the Asian Development Bank. As a result, even though DAC contributions to multilateral institutions have remained fairly constant over the last ten years, there has been a shift away from the IDA, with the IDA receiving 5.6 percent of total ODA contributions in 2002 as against 9.2 percent in 1995 (IDA 2004e). During 1994-2005, the IDA was the third largest recipient of cumulative funding for multilateral ODA, after the EC and the UN agencies.[64] In addition, when donors are left with additional resources for the IDA but no IDA to absorb it, the level of the IDA replenishment

[61] See Sanford (2002) for a discussion of the various official views on the debate regarding IDA grants versus loans.

[62] Kapur (1997, p. 131) observes that although this interference is initially meant to apply to IDA policies, it easily spills over to IBRD as some of the Bank Group's largest borrowers (such as India, Indonesia and Pakistan) borrow from both the IDA and the IBRD (IDA-blend countries) and that, as a consequence, strict boundaries are difficult to maintain.

[63] See also Eccles and Gwin (1999) and Woods (2000).

[64] The IDA is, however, the second largest provider of multilateral ODA for developing countries after the EC (see IDA 2007a).

being set by the US contribution, they have created separate trust funds. These trust funds are administered by the Bank in the same way as regular IDA funds, but for two exceptions: first, the US is excluded from voting on the use of these funds and, secondly, US firms are not permitted to compete for contracts funded through the trust fund (Eccles and Gwin 1999).[65]

Finally, decisions regarding the allocation of IBRD net income to the IBRD's reserves, to the IDA and other activities with particular foreign policy benefits to non-borrowing shareholders (such as HIPC), have come to reflect historical control rights (i.e. the control of non-borrowing shareholders) rather than changing patterns of burden-sharing at the Bank. Today, retained earnings out of income, rather than paid in capital, dominate Bank equity. The former are, however, generated by interest payments by borrowing members (see Kapur 2002b; Mohammed 2004).

2.2.2 Private Sector Development and the Bank

The shifts documented above have been accompanied by a fast-growing commitment to the agenda of PSD at the Bank. Despite the private sector being at the centre of the Bank's activities since its creation, the last two decades have seen a strengthening of the Bank's mandate in this area.[66] This culminated in the endorsement by the Board in early 2002 of a PSD Strategy (WB 2002h) as the Bank's corporate blueprint.[67]

The Bank's PSD Strategy is based on the central idea that a 'vibrant and competitive' private sector is key to growth and poverty reduction. It is asserted that private activity reduces poverty in two ways. First, private markets are perceived as the engine of productivity growth, providing avenues for higher incomes, economic growth and employment generation. Secondly, private initiative is seen as complementing government efforts by providing basic services that 'empower' the poor through improved infrastructure, health and education. Consequently, the strategy projects two broad objectives: to extend the reach of markets through investment climate reform with a special focus on measures that help micro, small

[65] See (WB 2006i) on the various trust funds administered by the WBG.

[66] For a brief historical overview of the role of PSD activities at the Bank see WB (2002h); see also Miller-Adams (1999).

[67] It should be noted, in the light of the comments just made above, that it was upon a request from the IDA Deputies at the occasion of the IDA-12 replenishment negotiations that the PSD Strategy was prepared. IDA-13 replenishment priorities were subsequently characterised by strong support for the strategy (see IDA 2002b, p.16), and PSD became a 'special theme' to be given in-depth treatment during the IDA-14 replenishment process (see IDA 2004c). See again Taylor (2002) for the US position.

and medium enterprises ('opportunity'); and to improve access to basic infrastructure and social services through private participation ('empowerment').

At the operational level, the broad claim of the strategy is to shift performance risks from domestic taxpayers in developing countries to private parties, where these are deemed better able to bear or manage risk through an expansion of IFC, rather than IBRD/IDA, activities. It is also to facilitate a transparent targeting of subsidies embedded in WBG products to intended beneficiaries and purposes – for example through a mechanism such as output-based aid (OBA) (see WB 2002h, 2001h).[68]

The Bank's aid window, the IDA, assumes an important role in the WBG's PSD Strategy, with the following priorities assigned to it: to support improvements in the investment climate and regulatory environment in client countries – for instance through diagnostic work such as the Doing Business Reports and the Investment Climate Assessments; to support Small and Medium Enterprise (SME) development – for instance through the provision of business development services, financial intermediation for SMEs, and the establishment of an 'enabling' environment for SMEs; to contribute to the development of public-private partnership especially with respect to provision of infrastructure (the importance of OBA); and to strengthen the relationship between the IDA, IFC and MIGA (IDA 2004c; see also IDA 2001a). Real IDA lending for PSD in LICs doubled between FY80-00 (WB 2002h, p. 23), and PSD has constituted the largest thematic share of IDA commitments for the last decade (since IDA-11) (WB 2003d, p. 85).[69]

At the level of the WBG, financial support for PSD has increased at a faster rate in recent years than total lending and guarantees. As a result, the share of total lending and guarantees going in support of PSD almost doubled between FY95 and FY00, from 16 percent to 30 percent (WB 2002h, p. 23).[70] This has been accompanied by a fast-growing host of non-lending services focused on the investment climate. The latter consist of both analytical services (Investment Climate

[68] See Bayliss and Hall (2001) for a comprehensive critique.

[69] In contrast to the increase in PSD operations in LICs over the last twenty years, PSD operations in MICs (IBRD borrowers) have declined significantly to, in FY00, one third of their (real) FY80 level (see WB 2002 h, p. 23). This fall in PSD lending to IBRD borrowers is particularly notable in infrastructure, industry and telecommunications portfolios which have often been transferred to the IFC after, or concomitant with, privatisation.

[70] The Bank offers two types of guarantee instruments. One is the partial risk guarantee which provides a guarantee for lenders to private investment projects against debt service defaults that result from non-performance of government obligations. The other is the partial credit guarantee, which covers all events of non-payment for a specified part of any financing. See Alexander and Kessler (2003) on how the Bank's issue of guarantees can constitute an important conflict of interest, and on how guarantees shift fiscal burdens onto governments.

Assessments, Doing Business Reports, Reports on the Observance of Standards and Codes) and TA (for example, the Public-Private Infrastructure Advisory Facility).

The PSD agenda has had crucial implications for the expansion of the IFC. In IDA-only countries, the role of the IFC expanded dramatically and, in FY03, the IFC provided over US$ 4 bn in direct finance to the private sector in IDA countries (IDA 2004c, p. 10).[71] This compares with the IDA's own commitments of US$ 7.3 bn in the same year.[72] In the search for complementarities between IDA and IFC, the IDA has been encouraged to focus increasingly on supporting institution- and capacity-building including through targeted subsidies and guarantees, while the IFC focuses on mobilising private finance.[73] This has the alleged benefit, already referred to above, of not exposing the domestic taxpayer to credit risk. The latest strategic directions for the IFC indicate plans for a further ambitious up-scaling of its activities, which will seek, amongst other aims, to address constraints to private sector growth in infrastructure, health and education (IFC 2006).

OBA schemes appear particularly suited to this complementary approach in which IDA support takes the form of credits or grants to finance the provision of public financial support, and the IFC complements the IDA by providing financing for private sector providers (see WB 2002h).[74] According to a WB estimate, one-third to one-half of the resources allocated for basic services could be implemented through OBA approaches (IDA 2001a, p. 6). Since 2000, when OBA was officially launched, some 30 projects (mostly WB) have been developed that include an OBA-type component.[75] These have been applied in water, sanitation, power, transport, telecommunications and health, and are used in countries and sectors where it has

[71] IFC investments in IDA countries are concentrated in three sectors: finance and insurance; infrastructure; and extractive industries together accounting for just under half the total IFC investments in IDA countries in FY03 (IDA 2004c, p. 23).
[72] The IDA figure includes allocations for blend countries while the figure on IFC to IDA countries does not. Comparing the two figures thus gives an underestimation of the importance of the IFC in IDA-only countries.
[73] Figures 8 and 9 of the Bank's PSD Strategy (WB 2002h, p. 22) document how the composition of Bank (IBRD/IDA) loans in both the telecommunications and power sector between 1980s and 2000 changed from being dominated by the construction of facilities to a main concern with policy reform, privatisation and private entry.
[74] While traditional project aid focuses on financing inputs ('input-based aid'), OBA draws on contracts that shift the responsibilities for construction, operation and/or maintenance of a facility to investors (for-profit and not-for-profit) and seek to reap benefits from performance-based incentive structures as funds are disbursed against achievement of contractually agreed outputs. As such, in contrast to traditional approaches of channelling support to inputs used by public sector providers, OBA delegates service delivery to third parties under contracts that tie payment to the outputs or results actually delivered (see Brook and Smith 2001). This financial support can complement or substitute for contributions from users (with subsidies in particular for low-income users).
[75] http://www.gpoba.org/docs/OBApproachesWhatisOBA.pdf. For a description of a set of OBA projects, see IDA (2004c, Annex 3).

generally been difficult to attract private investment (IDA 2004c, p. 14; see also Alexander and Kessler 2003).

2.2.3 Corporate welfare or aid?

As a multilateral development institution, the Bank has thus been subject to a set of contradictory tendencies. In the context of increased private flows and the rapid decline in its financial intermediation activities, the case for the Bank's existence as a public finance institution comes to depend increasingly on its capacity to provide concessional flows as a development agency. The IDA Deputies have, however, tended to make fewer resources available for the IDA, while they increasingly use the IDA as a conduit to impose their priorities on Bank activities, thus further eroding the Bank's projected multilateral character. Yet, as Woods (2000, p. 137) reminds us:

> In order to be effective, the Bank needs to be perceived by all its member countries as a legitimate multilateral organisation, pursuing predominantly developmental objectives in a rule-based way ... In order to enjoy this legitimacy, the Bank also needs a visible degree of political independence from interference by its most powerful members.

Adding to these trends, the WBG's main focus has turned onto PSD. As a result, private firms have grown as a proportion of the WBG's clients through the fast expanding activities of the IFC and MIGA as well as the attempt to use more of the Bank's lending capital for guarantee provisioning of private investments (see WB 2005k).[76] This highlights the use of the Bank's financial resources, at subsidised rates, to support corporate investment, as against its supposed mission, as a public IFI, to promote development and combat poverty.[77] Rich (2002, p. 53) comments:

> The World Bank's *raison d' être*, in its own words, is environmentally sustainable poverty alleviation; it is really the only reason why taxpayers in the industrialized world, already faced with a shrinking domestic social safety net, should support such an institution ... Meanwhile ... the institution mutates into an entity for which public support becomes harder

[76] The Executive Board Work Program for FY07 also indicates that the IDA is exploring the issue of whether it could, in the future, lend directly to the private sector without the standard sovereign counter guarantee (WB 2006e, p. 14).

[77] Mohammed (2004) further points to the Bank's large liquidity positions which, with a portfolio currently exceeding US$ 28 bn, are more than 50 percent in excess of the Bank's own prudential minimum requirement of US$ 18 bn (WB 2005j, p. 16). This raises the question of how suitable this role of financial arbitrageur is for an institution like the Bank.

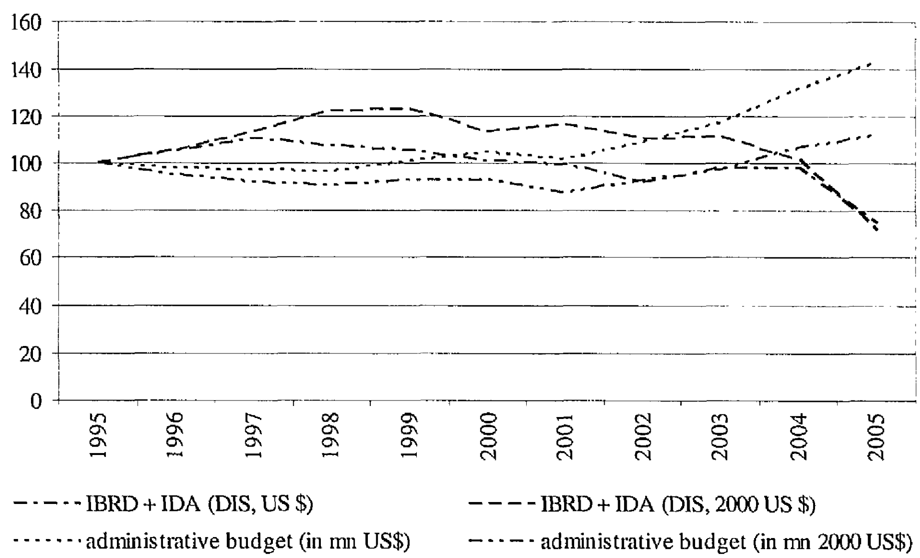
and harder to justify: a merchant bank, but one that is government subsidized and completely insulated from the financial, political, and moral consequences of its actions.

In similar terms Bayliss and Hall (2001, pp. 23-4) point to the danger of the WBG becoming:

a large, multiple-state backed venture capital scheme, with IDA money to be handed out as targeted subsidies to help the very poor pay their contribution towards the contractually guaranteed income of multinationals.

Finally, while the Bank's core business has declined, the administrative budget of the Bank has not shrunk accordingly. On the contrary, figure 2.2 charts the trend in joint IBRD and IDA gross disbursements as compared to the trend in administrative expenses, and illustrates how falling Bank lending has been accompanied by fast-increasing administrative expenses.[78] It appears that as the Bank engages less in traditional lending activities, it has, at the same time, become more expensive to operate.[79]

Figure 2.2: Total IBRD/IDA lending (gross disbursements) and administrative expenses, index numbers (1995 = 100)



[78] It should be noted that the trend in administrative expenditures depicted here does not include the trust funds that augment the resources available to the Bank. For FY05, trust funds amounted to almost US$ 1 bn and were added *onto* a Bank budget of just below US$ 2 bn (WB 2007, p. 96).

[79] Kapur and Wade (1998) add how, in 1998, the administrative budget was almost five times higher per dollar of outstanding loans than for the European Investment Bank.

Source: GDF online; WB (2006f, p. 34).
Notes: a) The IFS Import Unit Value was used to transform disbursements into real values.
b) The US CPI was used to transform administrative expenses into real values.

2.3 Banking on knowledge[80]

In response to the contradictory trends illustrated above, the Bank's management took action. It attempted to reassert the Bank's central role as a development institution seeking to fight poverty ('our dream is a world free of poverty'). It sought to reinvigorate client demand for its IBRD products (both financial and non-financial). To that purpose, new more flexible instruments were introduced (such as the adaptable programme loan and the learning and innovation loan); the cost of IBRD loans was cut; and the maximum amount it would lend to a single country was increased (by US$ 1 bn to US$ 14.5 bn) (WB 2005l).[81] Furthermore, synergies with the IFC and MIGA were actively promoted.

The Bank also projected to improve the development effectiveness of its programmes, significantly through such mechanisms as PBA, the emphasis on 'ownership', and by paying special attention to capacity building (see chapter one). This was accompanied by an attempt to move towards a more 'comprehensive' approach to development, which is documented in chapter three. The Bank further decentralised activities by relocating Bank staff to regional and national field offices. It discerned a new and leading role for the Bank in the context of IPGs. *And* it repeatedly sought to combine these various initiatives with an explicit emphasis on its unique position as a knowledge-gatherer and disseminator (see Wolfensohn 1996a, p. 7; WB 1997d, 2000d, 2001c, 2001d, 2001e; Wolfensohn 1999; Wolfensohn and Bourguignon 2004).

This section explores the 'knowledge' idea more closely. It situates the notion of a Knowledge Bank in a brief historical perspective and, in particular, draws attention to the origins of a 'knowledge' ambition for the Bank during Robert McNamara's Presidency. The Bank's capacity to exercise a leadership role in the intellectual and policy realms of economic development has, however, varied with the broader environment in which it operates. The 1980s saw a conjunction of events

[80] This is also the title of a book edited by Stone (2000) which brings together a collection of papers touching on issues related to one particular application of the current knowledge initiative, the Global Development Network (see below).

[81] The recent emphasis by the Bank on infrastructure lending can also be perceived as an attempt to rekindle its business with middle-income clients. The move to disband the Environmentally and Socially Sustainable Development network and merge it with the Bank's infrastructure department, to create a new department called Sustainable Development, can be understood as seeking to create an environment within the Bank more conducive to such a change.

that promoted such a role for the Bank and, by the early 1990s, it had attained leadership in an aid regime structured around its identified priorities. With the arrival of James Wolfensohn as President in 1995, the knowledge idea was put squarely at the centre of his renewal programme for the Bank. Wolfensohn sought to raise the knowledge profile, in particular through a rapidly expanding programme of non-lending services. Finally, the knowledge idea caught on with the broader donor community, easily accommodating the constraints and emphases that were documented in chapter one.

2.3.1 The Knowledge Bank

As part of his vision of the Bank as a leading development institution, Robert McNamara insisted on an explicit knowledge role for the institution (Mason and Asher 1973; Stern and Ferreira 1997). His office records, as reproduced in Kapur et al. (1997a, p. 476), report:

> Mr McNamara ... disagreed with the view that the Bank obtained its major impact through its project and technical assistance work. Although this work ... was essential, it did not influence ... donor policies. The development community was influenced by soundly based ideas and it was an essential part of the work of the Development Policy Staff to find such ideas and turn them into strategies for development.

So under McNamara's tenure, a set of measures aiming to strengthen the Bank's research functions were undertaken. This involved a significant increase in the research staff of the Bank. The staff, mainly economists, belonged to two different groups. There was a research staff dedicated 'somewhat like a university faculty' to the 'development of new knowledge'. These researchers were meant, following Kapur et al. (1997a, p. 1181):

> to have spill-over effects on Bank operation, but in addition to truth-seeking for its own sake, their primary mission was to enhance the Bank's image outside the institution.

In addition, and in bigger numbers, there were the 'practising' economists in the various regional sections of the Bank engaged in Economic and Sector Work (ESW). Furthermore, a Vice-Presidency for research was created, held by Hollis Chenery through most of the McNamara era and, in 1978, McNamara initiated the World Development Report (WDR) – a publication that was to attain the largest circulation of any international economic report.

These changes had important implications for the stature and position of the WB in development. Its ensuing dominance, however, was only to unfold in the subsequent decade. The 1970s were characterised by a relative abundance of resources available to developing countries and this diminished somewhat the extent to which the Bank could impose its ideas on others. Under McNamara, the Bank had dramatically expanded its lending programme, with a fourfold increase during his term. Relatively low-cost alternatives to Bank loans were available as a result of the oil shock and the subsequent recycling of petro-dollars. And some developing countries experienced commodity booms. Reflecting the breakdown of the Bretton Woods regime, the first oil shock, and the consequent very fast expansion of commercial, bilateral and multilateral lending, the principal characteristic of the aid regime of the 1970s was, as observed by Gibbon (1995, p. 119), its almost entirely laissez-faire and uncoordinated nature – with virtually no leadership role exercised by any specific institution.

The end of that decade, however, saw a set of events that dramatically affected the development scene and the role of the Bank within it. A second oil shock provoked another oil price hike, interest rates followed suit (the Volcker shock), and right-wing administrations came to power in the major OECD countries. The latter development implied political hostility to aid in general and to a multilateral institution like the Bank in particular, while both former events resulted in a dramatic increase in the financial needs of developing countries. Inside the Bank there was, furthermore, mounting concern regarding the limited influence of project lending over policy.

In response to these events, the Bank launched its lending for 'structural adjustment' in 1980. Under this programme, finance was provided over a period of several years in direct support of specific policy reforms. Where the Bank's funds were originally tied to a particular investment project, it was now obtained for 'untied' balance-of-payments support (non-project assistance). This, however, came at the cost of a conditionality, which severely impaired the borrower's capacity to set its own development agenda.[82] Policy-based lending, nevertheless, was not new,

[82] Although the introduction of structural adjustment loans (SAL) and the systematic practice of policy-conditionality, represented a real departure from Bank practice, certain features of preceding Bank practice had prepared the way. These include the conditionality that traditionally accompanied Bank loans (e.g. pricing schemes for particular Bank-financed investment projects) and the earlier experience with programme lending (mainly to India in the mid-1960s but also to a set of East African countries between 1973-1975, and Turkey in 1978). For a comprehensive overview, see Mosley et al. (1995, pp. 27-55).

arising out of the constitution of the IMF, and the advent of SAL at the Bank implied an overlap between the two institutions. The institutions sought to deal with this through increased co-operation and collaboration, with the standard practice of making a SAL agreement conditional on an IMF stabilisation programme (see also chapter three).

Policy-lending easily lent itself to ideological affiliation with the right-wing leadership of core Bank shareholders (mainly the US) and tempered the initial hostility towards development co-operation as its substantive content became coloured in by a new discourse on development that sought to celebrate the power of the market (see chapter three). Furthermore, in the context of the debt crisis of 1982, the instrument proved itself most useful in allowing money to be moved swiftly, and the IFIs came to play a special role (Perreira 1995; Gwin 1997). The Baker Plan of 1985, in particular, sought to draw the MDBs into the debt strategy with a special focus on expanding the Bank's fast-disbursing lending (see Kapur et al. 1997a, p. 628). In the Brady Plan of 1989, debt rescheduling and new lending for most developing countries through the London and Paris Clubs became dependent on the IFIs' seal of approval of the debtor country's economic policies. Furthermore, the Berg Report (WB 1981) had indicated a new role for a recipient country's consultative group of bilateral donors, which now only convened after agreements on policy reform programmes had been struck between recipients and the Bank (see Gibbon 1995, p. 123).

As a result of these various developments it became virtually impossible, by the end of the 1980s, for the weaker developing country to 'obtain funding, credit, debt rescheduling or debt relief from any western source, public or private, without approval of the Bank' (Gibbon 1995, p. 124). The Bank had come to occupy 'the conductor's role within the development support orchestra' (Ranis 1997, p. 75; see also Stern and Ferreira 1997).

This increasing dominance was clearly related to the Bank's financial muscle. But it also sprang from the Bank's growing influence in the realm of ideas, as envisioned by McNamara. The Bank's 'knowledge' activities had taken on significant dimensions and, by the early 1990s, the Bank employed around 800 professional economists and had a research budget of around US$ 25 millions (mn) per year (Stern and Ferreira 1997). These resources 'dwarfed' any university department or research institution working on development economics and the Bank could not be seen as 'just one of a number of fairly equal actors in the world of development economics' (Stern and Ferreira 1997, p. 524).

Apart from the quantitative dimension, there was a qualitative aspect to the significance of the Bank's knowledge role. Even though the research undertaken by the Bank spanned a range of topics, it was dominated by economics. Economics' predilection for quantitative analysis and formal modelling (on the basis of the central precepts of optimisation, equilibrium and efficiency) bestowed the discipline with a semblance of scientific rigour,[83] with powerful implications for the standing of Bank research. For Kapur (2002a, p. 65):

> in the social sciences in general, the greater use of numerical data is considered a sign of quality. The Bretton Woods institutions possess the holy trinity of social science research – data, financial resources, and human resources – and as a consequence offer probably the largest single environment for comparative work on LDCs [less developed countries].

For the Bank, the preference for economics served a twofold purpose: it invests propositions generated or endorsed by the Bank with the necessary 'technical' authority, and it meets the Bank's constitutional obligation of 'political impartiality' (Swedberg 1986, p. 388; Nelson 1995, p. 115; Wade 1996; Boas and McNeill 2004, p. 215). Very early on then-Bank President E. Black asserted, as quoted in Swedberg (1986, p. 388):

> We ask a lot of questions and attach a lot of conditions to our loans. I need hardly say that we would never get away with this if we did not bend every effort to render the language of economics as morally antiseptic as the language the weather forecaster uses in giving tomorrow's prediction. We look on ourselves as technicians and artisans.

The Bank's knowledge dimension came to be fervently feted under James Wolfensohn's Presidency. The Strategic Compact, the renewal exercise of the Bank initiated by Wolfensohn in 1996, explicitly asserted that one of its key objectives was to make the Bank's knowledge base a world standard, WB (1997d, p. 20):

> Collection, synthesis, and dissemination of knowledge is one of the major goals of the renewal programme … The knowledge management system will provide a corporate memory of information, lessons learned from experience, and best practices … It will interconnect with universities, foundations, and other world-class sources of knowledge.

[83] See Lazear (2000) for a recent statement and Fine (2002b) for a critique.

The Bank wanted to become, in effect, a Knowledge Bank (Wolfensohn 1996a, p. 7). Although, originally, Wolfensohn's emphasis on knowledge drew on the corporate practice of knowledge management and aimed at organisational aspects of the institution with the purpose of improving internal learning and efficiency (see King and McGrath 2004; King 2004), the paradigm rapidly broadened to encompass a wide-ranging definition of a knowledge mission for the Bank (and subsequently for the wider donor community). In this way, the Bank's strategy for knowledge sharing quickly expanded with the objective of making its know-how and experience accessible not only internally to Bank staff, but also externally to clients, 'partners' and 'stakeholders' around the world. In the process, the Bank sought to reach those who as yet did not have or had little access to the organisation's expertise (see Denning 2000). The *1997 Annual Report* (WB 1997b, p. 7) explained that:

> The Bank is made up of an unmatched repository of experience and understanding about development issues, which too often has been underused ... To meet client needs more effectively and better equip Bank staff, work began on developing a knowledge management system in fiscal 1997 to disseminate and apply lessons of experience among staff and clients. Through this system, complex information is distilled into usable formats for delivery to those who need it: policymakers, parliamentarians, NGOs and journalists, in ways that build vital understandings in member countries.

This reflected an awareness that the Bank's financial weight might, if anything, have declined. With the Bank now formally identified as the development agency undertaking the most country-specific analytical work and research on economic development, and hence a source of 'global knowledge', it would seek to strengthen the knowledge base for all development partners (IDA 2004e, p. 9). For Mehta (2001, p. 189):

> The emergence of the Knowledge Bank needs to be interpreted as a conscious attempt on the part of the Bank to carve a new niche for itself in international development.

For supporters of a knowledge turn, the Bank's 'knowledge base' became a sufficient reason to safeguard the institution's continued existence, Gilbert and Vines (2000, p. 29, my emphasis):

> The Bank's knowledge and cumulated experience of the development process provides the *justification* for a continuing role for the WB in an era

where international capital markets appear overliquid rather than underliquid.

In such an account, the Bank would concentrate on being the world's premier development institution, forging a common agenda on major issues and being in the 'forefront of development as a learning exercise' (Bergesen et al. 1999, p. 190).[84]

Accordingly, the Strategic Compact allocated the second biggest pocket in its resource envelope to the 'knowledge' dimension of WB operations (WB 2001c, p. 41). It envisaged significant investments in ESW, the Bank's applied research programme; stabilised a longer-term decline in funding for research in the Bank's research department; and sought to ensure that knowledge was more effectively shared, particularly through the World Bank Institute's (WBI) client learning programmes, as well as through sustained support for new 'knowledge-promoting' initiatives (see further below).

By the early 2000s, the Bank issued another set of documents which reaffirmed a strategic vision with knowledge at the centre (WB 2001c, 2001e, 2001d, 2003m). The Compact's knowledge vision was described as even more relevant than it was in 1997, and the Strategic Directions for FY02-04 pledged to increase further the delivery of knowledge-related services and capacity-building (WB 2001d, p. ii). This translated into the largest allocation for 'knowledge-based services' (mainly ESW and research) in the Bank management's proposition for additional administrative budgetary resources for FY02-04, and Bank expenditures on Analytical and Advisory Activities (AAA) more than doubled between 1996 and 2005, from US$ 106.6 mn 1996 (WB 2002i, p. 48) to over US$ 230 mn (WB 2007, p. 96).[85] In addition, knowledge sharing became an indicator in staff Overall Performance Evaluations; sectoral policy reports became impregnated with the 'knowledge vision'; and the 1998/9 WDR (WB 1998c) was dedicated to the theme of knowledge and development. At the 13th replenishment of the IDA, the IDA Deputies re-asserted how the IDA's comparative advantage was now understood to lie (IDA 2002b, p. 5, my emphasis):[86]

[84] See also Gavin and Rodrik (1995); Ryrie (1995); Krueger (1998); Gilbert et al. (1999); and Squire (2000).
[85] AAA consist of Donor and Aid Coordination; ESW; Impact Evaluation; External Knowledge Management; Internal Knowledge Management; Policy Framework Paper; Research; Non-Lending TA; and the WDR. These figures do not include Trust Funds. In FY05, total expenditure on AAA, including Trust Funds, exceeded US$ 350 mn (WB 2007).
[86] This was reiterated in the document accompanying the IDA-14 replenishment, see IDA (2005, pp. 19-20).

at the strategic level – in helping countries to improve their economic management and to implement economy-wide and sector-wide structural reforms, and in analysing policy options and sharing knowledge through Economic Sector Work (ESW). Critical components of this approach are IDA's ... further efforts to make capacity building a core dimension of IDA's work. IDA can play a key role in providing financing for poverty reduction strategies *and* in supporting the research and analytical work needed to identify the actions required for poor men and women to benefit from the gains of overall economic growth.

Therefore, while the transfer of knowledge had always been a dimension of the Bank's role, the knowledge initiative sought to 'broaden the scope and raise the profile of this function' (WB 2003f, p. viii), creating a 'world-class knowledge management system' and 'improving and expanding the sharing of knowledge with its clients and partners (p. xi). Furthermore, it conveniently combined with the increased emphases on PBA of aid, ownership and capacity building documented in chapter one, which had, if not necessarily explicitly, certainly effectively put 'policy learning' at the centre of aid practices.

2.3.2 Knowledge as aid

The knowledge idea rapidly caught on with other funding and TA agencies. Of course, 'knowledge' propagation had always been part and parcel of aid as, even before the widespread prevalence of policy-based lending, aid involved an important degree of policy interference. The nature of this interference was shaped by the particular form of aid or particular sector targeted and in that the acceptance of an aid-financed investment usually entailed recipient funding of recurrent costs with repercussions for budgetary allocations, or affected domestic policy through the imposition of a particular pricing scheme concomitant to the provision of project finance (Hirschmann 1967). However, with knowledge placed at the centre of the aid-development paradigm, the creation, management and transfer of knowledge became 'the primary axis or locus for international co-operation on development' (Stone, D. 2003, p. 49).

The UK 1997 White Paper on development (DfID 1997, p. 48) emphasised that:

The principle of shared knowledge is an important component of the partnerships which are essential to development. The Government sees the continued investment in knowledge generation as a key element in achieving its aims and objectives for international development.

The German development agency (GTZ) elevated knowledge to a core theme of its development co-operation:[87]

> GTZ is highlighting the importance of effective and efficient knowledge transfer for the success of its daily work. As an international knowledge broker, one of GTZ's primary tasks is to make any required (specialist) knowledge available to its partners on the ground while improving the dissemination of (general) knowledge in the target regions.

For the Swiss development agency (SDC), knowledge became one of four crucial processes in its new strategy:[88]

> The countries and SDC partners in the South and East require knowledge to ensure their independent development. The SDC's aim is to assist them by providing its knowledge and experience as a targeted contribution. Knowledge management and a culture of learning are thus understood as instruments to enhance the quality and effectiveness of international cooperation.

And the Asian Development Bank argued as follows:[89]

> As a regional development institution in Asia and the Pacific, ADB has always stressed knowledge exchange as a critical product. The principal objectives of ADB's non-lending services in the form of economic, sector, and thematic work have been to create new insights and make these widely known. Knowledge transfer is also an important component of ADB's lending operations. Embodied in investment projects that ADB finances are the best available knowledge and practices. These are complemented by extensive support for capacity development to enhance DMC's [Developing Member Countries] ability to develop, capture and apply knowledge. ... To achieve the MDGs, the DMCs will need to acquire and apply relevant knowledge to accelerate poverty reduction and to effectively mobilise and use the necessary financial resources. To remain relevant in responding to the varying and complex poverty reduction needs in the region, ADB must become more effective in sharing knowledge and more

[87] http://www.gtz.de/en/13459.htm.

[88] http://www.sdc.admin.ch/index.php?navID=21408&langID=1&userhash=4131e35109196ada324811ab2dff0899. See also CIDA (2001); ADB (2001a).

[89] http://www.adb.org/Documents/Policies/Knowledge-Management/km0200.asp.

> proactive in supporting learning … [W]ith its extensive development knowledge of the region, ADB is well positioned to capture relevant good practices and lessons learned from the rest of the world, and not only transfer them to the DMCs but also help DMCs adapt them to their particular circumstances. To remain relevant to the needs of a rapidly changing region, ADB must now expand its role in catalysing knowledge for innovation and development.

In an exposition of a knowledge vision for the Japan International Cooperation Agency (JICA), Okuda (2002) explicitly links the knowledge emphasis to an approach to development financing that puts foreign private enterprise at its centre and, in the context of Japanese aid, a move a way from the Far East Asian-type development paradigm which had been characterised by a specific role for the government in selecting and supporting strategic industries and infrastructure.

Throughout these statements, development agencies perceive themselves to have a distinct advantage in gathering information and producing knowledge about successful development practices and policies. Again, the idea initially focused on formal issues of knowledge management that sought to transform the agencies into 'learning environments' and drew on a literature and practice of corporate knowledge management which allowed agencies to look at internal patterns of knowledge use in an attempt to improve their effectiveness (see OECD 1998, pp. 6-28).[90] However, this easily spilled over into wider arguments regarding the centrality of knowledge to economic success and the connective power of information and communications technologies (ICTs).[91]

2.4 The Bank and knowledge: a closer look

2.4.1 Knowledge for development

Wolfensohn's knowledge declaration originally found inspiration in the corporate discourse and practices of knowledge management, which seek to improve organisational efficiency and effectiveness (see King and McGrath 2004, pp. 35-7). It rapidly mutated, however, into a more general emphasis on the importance of knowledge in development, and the role for the Bank therein. A set of quasi-analytical propositions emerged to support an increasingly formal discourse on such

[90] See also the collection of papers in Carlsson and Wohlgemuth (2000).
[91] See King and McGrath (2004) for a detailed account of the meaning of the knowledge emphasis at the level of discourse and practice in DfID, Sida, and JICA.

a role for the Bank. These were scattered across a few contributions (Stigtliz 1999a, 1999b, 2000b; Squire 2000, 2001; Gilbert and Vines 2000) and acquired some overarching framework in the chapter dealing with the role for international institutions in the 1998/9 WDR *Knowledge for Development* (WB 1998c, chapter 9). They mainly touch upon an understanding of the Bank's knowledge as a public good (both for the client country and the development community), the Bank's role in client capacity building and client learning, and its contribution to consensus-building in client countries. They further straddle notions of knowledge as 'codified' or explicit, 'tacit' or embedded, 'global' and 'local' borrowed from the new economics of science (see e.g. Cowan et al. 2000; Ancori et al. 2000).

The 1998/9 WDR pursues issues around what it perceives as two types of critical knowledge problems facing developing countries. It identifies, on the one hand, gaps in 'knowledge about development' – broadly understood as related to technology and institutional arrangements – and, on the other, incomplete 'knowledge about attributes' – such as the quality of a product or the effort of a worker ('information problems').

National governments have a role in addressing both 'knowledge' and 'information' gaps. The former necessitate the creation of knowledge locally and policies that enhance the acquisition and adaptation of global knowledge – through an open trade regime, technology licensing, migration, and FDI. It implies a need for investment both in human capital (tertiary education) and in technologies that facilitate the acquisition and absorption of knowledge. In that context, ICTs play an important role, with a concomitant repeated emphasis in the Report on the need for liberalisation of the telecommunications markets. This is in addition to a heavy presence of the familiar emphasis on liberalisation and privatisation running through the entire Report. In the context of information problems, the emphasis for domestic action is on devising institutional arrangements (such as product standards, training certificates and credit reports) that temper the market failures these cause.

For international organisations the Report discerns a threefold role, mainly focused on reducing 'knowledge' rather than 'information' gaps. First, international institutions can assist in knowledge creation, and as such provide IPGs. This includes international support for basic research such as in agricultural knowledge; engaging the private sector through market incentives such as offering 'contingency loans' for privately developed new products like an AIDS vaccine; or fostering collective action in such areas as the environment. Secondly, they can act as intermediaries in the transfer of knowledge. They can help in the exchange and adaptation of knowledge through the promotion of innovation and adaptation at the project level. They can help to disseminate and adapt results of policy research, for instance, by analysing and codifying policy reforms around the world so that the information can be used worldwide, and assist in the building of local capacity for policy analysis. Thirdly, development agencies can facilitate the management of the rapidly growing body of knowledge about development (see WB 1998c, pp. 130-43).

Across these propositions, the Bank emerges 'as a disseminator of development knowledge and policy lessons as well as an arbiter of "best practices" and "international standards" ' (Stone and Wright 2007, p. 14). A text box on knowledge management at the Bank in the 1998/9 WDR, in particular, conveys a vision of the Bank as a clearinghouse for knowledge about development, a corporate 'memory bank' of best practices, and a collector and disseminator of the best development knowledge from outside organisations (p. 140). 'Knowledge about development' is understood as an extra factor of production, with poor countries differing from rich ones 'not only because they have less capital, but because they have less knowledge' (p. 1). The creation and dissemination of knowledge appear as an IPG (Stigtliz 1999a; Squire 2000). Joe Stiglitz (1999a, pp. 310-1), former Chief Economist and Vice-President of the Bank explains that:

> Most knowledge is a global public good: a mathematical theorem is as true in Russia as in the US ... The problems that economics deals with, such as scarcity, are ubiquitous, and accordingly the laws of economics are universally applicable even if idiosyncratic institutions exist within each country.

He continues (p. 318):

> Much of the knowledge that is required for successful development is not patentable, it is not the knowledge that underlies new products or processes. Rather, it is equally fundamental knowledge: how to organise firms, how to organise societies, how to live healthier lives in ways that support the environment. It involves knowledge that affects fertility and knowledge about the design of economic policies that promote economic growth.

The supply of such a public good will be deficient without active public support, and this gives rise to a crucial role for the Bank (Stiglitz 1999b; Squire 2000; Gilbert, et al. 1999; WB 1998a, 1998c). Stiglitz (1999b, p. 590, my emphasis) further elucidates:

> The accumulation, processing, and dissemination of knowledge in development, as well as working more broadly to close the knowledge gap, is the *special* responsibility of the World Bank. The two activities of the Bank are complementary. Knowledge, particularly knowledge about the institutions and policies that make market economies work better, leads to higher returns and better allocation of capital ... The World Bank has a role to play in providing such advice that extends beyond the public-good nature of knowledge. It is, and is widely perceived to be, an honest broker.

This applies both to the knowledge created in the Bank's research department and the much broader knowledge exercise in its operational departments (see also Stern and Ferreira 1997). In the context of the PRSP process, for instance, the Bank has drawn attention to its unique knowledge role through the various analytical and advisory services (ESW) originating in its operational departments (see also chapter one). IDA (2004e, p. 24) emphasises:

> With regard to the PRSPs IDA is the largest provider of supporting Country Analytic Work (CAW) which is so necessary to the process. Drawing on its multi-sector country knowledge, IDA is strongly positioned to strengthen the underpinnings of PRSP. For example, CEM [Country Economic Memorandum], DPR [Development Policy Review], ICAs [Investment Climate Assessment] and PAs [Poverty Assessment] are key to this task. Likewise, its contributions to improving PFM [Public Financial Management] through PERs [Public Expenditure Review], CFAA [Country Financial Accountability Assessment] and CPIA form the cornerstone of aligning PRSP with the budget and improving the management of the public finances. A great deal of the Bank's analytical work, which in several cases is carried out jointly with other development partners, can be regarded as a 'public good' for both the client country and the development community.

In such an account, the Bank is characterised by economies of scale and scope in policy or development knowledge and, concomitantly, has a unique capacity to analyse, codify and disseminate development experience around the world (Wolfensohn 1996b; Stern and Ferreira 1997; Gilbert et al. 1999; Squire 2000;

Piccioto 2002).[92] This combines with an argument regarding the difficulties of structuring incentives in order for outside research institutes to deliver the kind of research the WB seeks to promote. Squire (2000, p. 109) asserts that:

> without an in-house capacity, integrating the results of research into the World Bank's everyday operations and making those results available to policy-makers in developing countries does not happen. This usually requires an in-house champion, and the best champion is almost always the researcher. This then supplies the primary rationale for an in-house research capacity at the World Bank.

And, while for Squire (2000), the influence of research on operations provides the basis for the argument in favour of in-house research at the Bank, Gilbert and Vines (2000, p. 29), two staunch supporters of the knowledge vision, emphasise the alleged neutral and professional character of Bank research:

> The Bank is in a position to give advice which is more disinterested than that provided by professional consultants, more professional than that provided by academics and more comprehensive than that provided by NGOs.

Further, the proponents of a Knowledge Bank vision add that for knowledge to be useful it also needs to be grounded in local experience apart from global 'best practice' (see WB 1998c, p. 140). Stiglitz (2000b, p. 31) explains:

> Prudent counsel is to scan globally for best practice but to test them locally, since local adaptation often amounts to reinventing the 'best practice' in the new context.

He emphasises how knowledge must be made applicable locally and that this adaptation must be done by the local development practitioners ('doers of development'):

> It is by local selection, assimilation and adaptation of knowledge that local doers 'make it their own'. Even by taking a machine or device apart and putting it back together again, one can 'make it one's own' even if there is little adaptation or redesign.

As a result of such 'adaptation', local policymakers see a set of policy reforms no longer as a foreign imposition but as a local product which they can sponsor and which addresses local needs (p. 33). The Bank's various knowledge activities,

[92] See also, most recently, Deaton et al. (2006, pp. 14-8) for a set of features which are somewhat idealistically ascribed to the Bank's research exercise and which, for the authors, account for the Bank's research advantage.

further, can potentially enhance the capacity of local actors to 'select, assimilate and adapt the external knowledge' (Stiglitz 2000b, p. 32). For Squire (2000 p. 120):

> It is often most efficient for development institutions to transfer internationally available knowledge to well trained government officials or other local residents, who can then merge that knowledge with local knowledge to devise locally appropriate policies or projects. For this reason, donors often help create domestic capacity for policy analysis and devise mechanisms that allow a strong civil society to engage government in a dialogue on policy.

Such an understanding implied the fast expansion of a set of Bank knowledge initiatives – documented further below – seeking to affect local understanding of development.

2.4.2 Bank knowledge: a public good?

The above account of a formal and explicit knowledge role for the Bank understood as strictly beneficial for development is prone to a set of serious misgivings. First, the discourse around the Knowledge Bank reinforces the projection of Bank knowledge as objective and value-neutral which had previously prevailed in Bank arguments. This implies a dramatic disregard for the socio-historical, political and economic context within which knowledge – including Bank knowledge – is produced as well as for the socio-political or economic functions knowledge might fulfil. Mehta (1999, p. 153), however, reminds us that:[93]

> knowledge is plural, perspectival and largely socially constructed … knowledge is created in and contingent on specific socio-historical political and economic contexts, the study of which is almost as important as the study of knowledge itself.

Garnett (1999, p. 2) draws attention, more generally, to the fact that discussions of the broader dimensions of knowledge and expertise have scarcely begun in economics, while these have been underway for some time in other disciplines. For Mehta (2001, p. 194) the Bank's knowledge agenda then appears as 'yet another attempt by mainstream economics to colonise an area of enquiry that has been developed largely by other social sciences'.

[93] See also Caddell (1999); Nustad and Sending (2000); Standing (2000); Samoff and Stromquist (2001); Torres (2001); and Stone, D. (2003).

Second, comments on the political economy of the Bank's knowledge nevertheless abound. These have drawn attention to the following: the shareholder realities of the Bank and, in particular, the role of the US; the implications of the embedded relationship of the Bank to the financial markets; and the prevalence of economics as the Bank's 'high scholarly discipline' (see Gwin 1994; Wade 1996; Kapur et al. 1997a; Mehta 1999, 2001; Standing 2000; Fine 2001a; Samoff and Stromquist 2001; Wade 2002; Kapur 2002a; Peet 2003).

Third, these broad governance features have a set of concrete implications. In a recent account, Broad (2006, p. 397) identifies what she describes as a form of 'soft law', unstated and sometimes at the expense of formal procedures, which establishes 'a de facto series of incentives that make it clear – all along the DEC hierarchy – what kind of research is being encouraged'. Through a closer look at the particular hiring and promotion practices, the selective enforcement of rules, the specific ways in which dissonant discourse is discouraged, data are manipulated, and the way in which research findings are projected outside of the Bank, the mechanisms of 'paradigm maintenance' operating in the Bank's Development Economics Vice-Presidency (DEC) are uncovered. Through these, individuals and work 'resonating' with neo-liberal ideology are privileged.

This of course does not imply that research staff at the Bank are characterised by universally shared understandings on all aspects of development, but that 'dissonant discourse', if tolerated, is not encouraged nor promoted (see also Samoff 1992, p. 65). In addition, the External Affairs department of the Bank, whose stature grew rapidly during the Wolfensohn Presidency, plays a special role in the amplification of a particular discourse within and beyond the Bank (see Ellerman 2001a; Broad 2006; Deaton et al. 2006, p. 127).

Fourth, and as a result, Bank research tends to be characterised by a set of shortcomings. Fine (2001a, p. 205) sums these up as follows:[94]

> poor quality, poor engagement with alternatives (Americanisation), excessive dissemination at the expense of independent research capacity building (ditto), poor coherence and integration in how research is used in choice, design, monitoring and assessment of activities, overgeneralisation in order to rationalise loans and leave room for discretion despite need for county and issue specificity, and limited engagement in self-criticism and assessment even when there are sea-changes in approach.

[94] See also Ranis (2003) and Deaton et al. (2006).

These weaknesses are not confined to the knowledge produced in the Bank's research department (DEC), but equally tend to characterise the more applied knowledge emerging from the operational departments.[95] Critical appraisals of the Bank's knowledge role, however, often tend to remain confined to an examination of research taking place in DEC, excluding what James Wolfensohn referred to as the Bank's larger source of 'development knowledge'.[96]

Fifth, the bias in favour of economics in the Bank's research and analysis and the resulting reductionist character of Bank knowledge persist, notwithstanding an increase in the appointment of non-economist social scientists as research staff in the Bank (albeit *outside* its research department) (see Bebbington et al. 2002). The staff at the Bank's research department (DEC) is dominated by economists who are mainly the product of the graduate economics departments of English-speaking but, especially, US universities (Kapur et al. 1997a; Stern and Ferreira 1997). A former programme director for Knowledge Management at the Bank, Denning (2001, p. 143) notes:

> There is still only one sociologist on the entire research staff, with significant risks to the distortion of knowledge generated, which is obviously multidisciplinary in nature. One can imagine what would happen to a piece of research showing that the problems of development are non-economic in origin and that a wider array of disciplines are needed. It is barely conceivable that such a piece of work would be proposed (who would propose it?), or carried out (who would do it?), or if carried out, that it would be regarded seriously by economists whose careers are linked to preserving the economic orientation of the research department.

Recent communication with DEC reveals that apart from that one sociologist, the only non-economist researchers in DEC are statisticians.[97]

Nevertheless, as the intellectual contribution of the Bank is not confined to its research department, the particular skill mix of the operational departments and the

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[95] See Hanmer et al. (1999) on Poverty Assessments. See King (1991), Samoff (1992), Samoff and Bidemi (2003) in the context of education. See Wilks and Lefrançois (2002), more broadly, on various country reports. And see chapter six on the particular bias in the Bank's analytical and advisory reports dealing with the investment climate, trade and the financial sector.

[96] See, most recently, Deaton et al. (2006).

[97] It is noteworthy that in response to my email query as to how many non-economists were employed in DEC, J. Dethier of DEC's research support unit referred to a set of social scientists employed in DEC who, according to him, do not have economics backgrounds. Closer scrutiny of the biographical details of these ten individuals, however, revealed that all but one held a PhD in economics. The confusion for J. Dethier probably originated in the fact that these individuals have research interests in traditionally non-economic fields (such as the impact of political and social institutions on development, governance, the environment, or culture).

changes therein could have bearing on the nature of the knowledge produced by the Bank. Yet non-economists employed within the Bank have tended to leave core economic issues unchallenged, trying to peg their own concerns onto an otherwise undisturbed economic agenda (see Fine 2001a). Leiterlitz and Weaver (2005, p. 382) observe:

> The quantitative shift in the staff skills mix towards the new 'priority' sectors may have countered the physical dominance of economists in the Bank and may eventually lead to meaningful transformation in how 'the Bank' as a collective set of actors 'think' about development, but this has not spontaneously disrupted the economics orthodoxy within the Bank's development approach. Several interviews with Bank staff confirm that non-economic social scientists within the organisation feel compelled to adapt their ideas to the theoretical and methodological language of the prevailing economic theory, whether it is neoclassical economics prominent in the 1980s or the current fashion of institutional economics, in order to influence conceptual and operational reality in the Bank. The observation by M. Cernea that non-economic social scientists (especially sociologists and anthropologists) hired in the mid-1990s 'did not land in an intellectual vacuum' but rather 'landed onto an in-house culture unfamiliar and resistant to this new socio-cultural knowledge and expertise' is echoed in many commentaries on the fate of new development ideas within the Bank.

Stone (2007) further notes how the Bank's tendency towards 'disciplinary monopoly' permeates the various knowledge networks that have emerged from the Bank (see below).

Sixth, within the confines of a framework of knowledge creation as an IPG, how to prioritise between different types of knowledge remains an unaddressed issue. The point has been made, in particular, with respect to social science research versus crop or vaccine research (see Kanbur 2001b; Kapur 2003, 2006). Kapur (2006, p. 160) ponders:

> If the Bank were to cut its AAA expenditures … shifting its focus from the social sciences to funding research in the health sciences, would the global welfare of the poor increase or decline?

Kapur (2006) also draws attention to the relatively expensive nature of in-house Bank research – even when compared to universities in the US, let alone in developing countries – and argues that the Bank's research activities should be more like a National Science Foundation funding activity than an in-house research one (see also Kanbur 2002, p. 22).

Seventh, in counterpoint to the observation by Gilbert and Vines (2000, p. 29) in the section above regarding the 'disinterested' nature of Bank advice, Kapur (2003, p. 13) emphasises how Bank research is undermined by 'its lack of independence, real or perceived, and without this independence the Bank's research will always be found wanting as a global public good'. Ravi Kanbur (2002, p. 22), who resigned from his position as director of the 2000 WDR (WB 2001f), insists that:[98]

> the Bank as a whole cannot possibly be viewed as an independent arbiter of social science research. It is owned by the rich countries, and it has operational policies that need to be defended. These features mean that social science research done by the Bank itself cannot fully lay claim to the mantle of an IPG.

A conflict of interest clearly underlies the Bank's joint role as an analyst and lender (see also Wade 2002; Debt Relief International 2002). The potential problems of combining the provision of funds whilst engaging in authoritative claims about development as well as of the institutionalisation of a funding agency as a provider of development advisory services are manifold. Samoff and Bidemi (2003, p. 32) observe that:

> what is deemed valid and legitimate information ('knowledge') will become increasingly centralised in the North; information that is collected in the South will be shaped and framed by its interpreters ... That powerful role in determining what is and what is not knowledge will be obscured by the mystique of science and scientific method. The centralisation of the determination of what is knowledge entrenches the role of the elite education and research institutions in the world, nearly all located in the most affluent countries. What is deemed to be the important knowledge is likely to become more technical and less humanistic and critical ... Overall, information databases created and maintained by authoritative institutions in the North with substantial economic leverage and

[98] See Wade (2002) for a reconstruction of the events that led up to Ravi Kanbur's resignation. See Kanbur (2001a) for his own account of the nature of the disagreements between what he calls the 'finance' versus the 'civil society' camp.

ideological influence are most likely to reinforce existing power relations, both within and across countries.

Finally, the Bank's knowledge emphasis and the various initiatives it engendered need to be seen in the light of the realities of knowledge creation in developing countries, where a set of factors have severely affected domestic capacity for policy analysis. First, there has been a sustained erosion and undermining of state capacity for policy analysis in developing countries that have been engaged in far-reaching structural adjustment exercises (see Bangura 2000; Mkandawire 2002). This has been the result of a number of factors, including fiscal stringency imposed upon states, a heavy reliance on expatriate technical staff by donor agencies, and the particular way in which 'ownership' has been understood by donors, where in the words of Mkandawire (2002, p. 155), 'capacity-building' exercises have more the character of cloning than the production of people with critical analytical skills (see also chapter one).

This has been compounded, secondly, by a sustained erosion of the university sector as a centre of knowledge in many LICs (see King 2001a). A complex set of factors have contributed to such a state of affairs, some of which relate to donor policies.[99] In the context of the latter, the 1980s and most of the 1990s were marked by an emphasis on support for primary education and away from higher education. Such a shift was inspired by rates of return analysis on education, mainly advocated by World Bank economists, which promoted the idea that the highest private and social rates of return to education were at the primary level. In addition, the notion prevailed that subsidisation of higher education did not benefit the poor. The effect of the shift away from higher education was particularly severe in SSA, where Bank support for higher education plunged dramatically in the 1980s (see Bangura 2000; Samoff and Bidemi 2003). This effect was compounded by donors' support for a consultancy culture, where think tanks rather than universities tended to be favoured as sites of policy analysis (Vaa 2003; Samoff and Bidemi 2003).

The knowledge discourse has, nevertheless, led to the re-emergence of higher education on the donor agenda (see Mundy 2002; King and McGrath 2004). However, and thirdly, this has happened against the backdrop of the rapid privatisation and internationalisation of the market in education and policy services – developments in which the Bank has played an important role, and which are

[99] On the various reasons for the decline of higher education and research institutions in crisis-struck countries, see Rasheed (1994); Mkandawire (1997); Bangura (2000) ; Mkandawire (2000); Samoff and Bidemi (2003); Vaa (2003).

reflected in a rapid increase in IFC involvement in the education sector (IFC 2001; Salmi 2002).[100] For King (2001b, p. 18):

> The new preoccupation with Knowledge Management in the North must be situated in the context of the brave new world of the internationalisation of the trade in educational services. It must also take account of the aggressive internationalisation of higher education in the North and the continuing challenges to the sustainability of research knowledge in the South.

The internationalisation of higher education has significant implications for the development of higher education in developing and transition countries. National institutions are likely to be faced with increasingly intense competition from foreign providers which, without appropriate protective measures by the institutions themselves or by governments could seriously affect their status and survival in the medium to long term (Bennell and Pearce 1998, p. 24; King 2001a).

2.5 The Knowledge Bank in action

Finally, the Bank engages in a massive knowledge exercise, the scale of which is mapped in this section. The Bank's knowledge activities take place both in-house – encompassing the more general policy-oriented research that seeks to produce propositions with wide applicability across countries or sectors ('research') and the vast complementary applied research effort that takes place across operations for a specific country or sector context (ESW) – and beyond the Bank, through a set of recently initiated knowledge networks and a vastly expanded training programme. We document the various dimensions of this knowledge effort, and draw attention, in particular, to the fast expansion of certain aspects thereof and the way in which the Bank has increasingly sought to draw in broader participants. This acquires particular significance in the context of an aid paradigm seeking to promote its ideational role.

2.5.1 Research at the Bank

What is commonly referred to as Bank research – distinct from the more country- or sector- specific ESW – is mainly undertaken in the DEC Vice-Presidency under the supervision of the Chief Economist, who is also a senior Vice-President of the Bank. A smaller proportion of research takes place across the regional and

[100] For critical commentary on this trend, see Norrag News (1998); Norrag News (2000); Coraggio (2001); King (2001a); Scherrer (2005).

network departments of the Bank.[101] DEC is structured into various units, the most significant ones being the DEC Research Group (DECRG) – the main research unit – and the DEC Data Group (DECDG).[102]

Table 2.2 indicates how the Bank's research programme has, on average, drawn on a budget of around US$ 25 mn a year, and how the resources available for the Bank's research programme have slowly increased from 2001 onwards, standing at US$ 29 mn in 2005 (WB 2007).[103] The budget available to DEC, nevertheless, exceeds the expenditures on research and has increased markedly in recent times, from just over US$ 39 mn in FY 2000 to US$ 51 mn in FY 2005 (WB 2003j, p. 36; WB 2004j, p. 32).[104] DEC currently employs 142 researchers (Dethier 2006a, p. 1).

Table 2.2: Expenditures on research, 1996 - 2005, in US$ millions

	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
Expenditures on Bank research	24	23.3	20.9	23.5	22.3	23.9	26.6	29.9	29.1	29.1

Sources: WB (2002i, p. 48) for 1996-2001; and WB (2007, p. 96) for 2002-2005.

Following the official Bank line, there are important two-way interactions between Bank research and Bank policy. 'Knowledge' is projected as an essential input into Bank operations, and operational experience feeds into new learning – the Learning Lending Knowledge circle (WB 2007, p. 48). More critically, Fine (2001a, pp. 200-1) points to two opposing stereotypical views regarding the relationship between Bank research and operations. At one extreme, Bank research is seen as irrelevant with research and operations functioning in separate worlds. This is explained in either of the following ways: operational departments obey their own logic, driven by the imperative of a continuous flow of new lending (see Ranis 1997, p. 76); or, policy is understood to be determined by external economic and political conditions, with research performing at most a rationalising function. At the other end, research is perceived to be highly influential in setting policy agenda, with a

[101] On the organisation of research at the Bank, see Dethier (2006b).
[102] DECDG engages in data collection and dissemination, and in statistical capacity building. Important outputs of DECDG include the World Development Indicators, the World Bank Atlas, and a large array of databases on areas such as education, gender, health, nutrition and population and poverty.
[103] This includes trust funds, which in FY05 accounted for just over US$ 8 millions (WB 2007, p. 96).
[104] Information regarding the allocation of the Bank's administrative budget across its various departments and programmes is not in the public domain prior to 2000, and could not be made available by the Bank.

decisive ultimate effect on internal operations. Traditionally, the reality has probably been somewhere in between and has varied from issue to issue (Fine 2001a).

Recently, a set of developments may have strengthened the links between the two spheres. First, the analytical work undertaken in the operational departments (ESW), which tends to draw on DEC research output, has rapidly expanded (see below).[105] In addition, the Bank has sought to improve the formal structures affecting interactions between the research and policy departments. Researchers now need to spend 30 percent of their time on support to operations (Dethier 2006a). In this context, Broad (2006, pp. 402-3) observes how the 'marketability' of a DEC researcher to Bank operational departments tends to hinge on the degree to which the researcher's work 'resonates' with neo-liberal ideology embedded in operational imperatives.

Furthermore, as part of the knowledge initiative, the Bank has developed a matrix management structure which seeks to combine local country knowledge, located in operations, with the expertise of the research department. Five thematic networks have been established and are situated between the research, policy and operational units. These are: Environmentally and Socially Sustainable Development (ESSD); Financial Sector Development (FSD); Human Development (HD); Poverty Reduction and Economic Management (PREM); and PSD.[106] The thematic networks are supplemented by hundreds of 'communities of practice', which seek to connect practitioners with other practitioners in their field and provide the organisational basis to collate relevant knowledge and display it on the internet (see Denning 2001). Still, Denning (2001, p. 147) doubts whether operational realities will be much affected by these knowledge-sharing efforts, observing that:

> The explosion of knowledge sharing that occurred within the communities of practice at the World Bank has not always inseminated and enlightened the lending operations of the World Bank, which often continued within the framework, of the existing paradigms. The paradigms themselves were not modified by new knowledge that might put in question their validity, in part because the paradigms were not fundamentally knowledge-based in origin.

[105] A Bank investigation into the impact of research on Bank operations found that 71 percent of ESW draws on Bank research and that, on average, there were eight citations of Bank research per ESW report (WB 2007, p. 47).
[106] As already observed above, the ESSD has recently been dismantled.

Finally, Bank research is widely disseminated beyond the Bank. First, Bank research benefits from a range of official outlets, including books published by the Bank, the Bank's two economic journals (World Bank Economic Review and World Bank Research Observer), WB Discussion Papers, Technical Papers, Policy Research Working Papers, and the WDR. There are also non-Bank outlets, including non-Bank professional journals carrying Bank research.[107] A recent assessment commissioned by DEC of the use of publications carrying Bank-wide research found that Bank research publications are frequently used by Bank staff and clients (see WB 2004i, p. 1). Citation rates are also often referred to as an indication of the popularity of Bank research (Squire 2000; Broad 2006; Dethier 2006a; Deaton et al. 2006; WB 2007, pp. 103-7). These, however, suffer from the flaw that they inevitably include the critical literature on Bank propositions which, evidently, does not seek to emulate or promote Bank ideas. Secondly, the Bank's website offers immediate access to topic-specific data and Bank reports and publications (www.worldbank.org). It has 700,000 users (WB 2003f, p. 20) and 5.5 mn hits per month (Wilks 2002).[108] Thirdly, Bank research receives prestigious press coverage. Fourthly, Bank research is spread internationally through the Bank's learning arm, the WBI, and through a set of knowledge initiatives (such as the Development Gateway or the GDN) (see below). Fifthly, there are the flagship Annual Bank Conferences on Development Economics (ABCDE), initiated in 1988. Initially held in Washington, DC, the conferences now take place in cities across the world and, since 2003, take place bi-annually, one conference being global (this taking place in a developed country) and one regional (which takes place in a developing or transition country).

2.5.2 Economic and Sector Work (ESW)

A much larger source of what James Wolfensohn termed 'development knowledge' (King and McGrath 2004, p. 57) derives from what the Bank calls ESW.

[107] The annual publication *The World Bank Research Programme. Abstracts of Current Studies* yearly provides a full list of Bank research outputs across these various outlets.

[108] The users of the Bank's external websites include Bank staff, development specialists and the general international development community. Bank staff account for only 2 percent of all users, but account for 16.5 percent of material requested (WB 2003f, p. 20). Although developing country use has grown by as much as 300 percent over 2000-02, residents from all developing countries combined account for only 10 to 20 percent of total usage, while those from the USA account for about 25 percent. It is recognised by the Bank that these usage numbers are a reminder of the continuing 'digital divide', undermining the effectiveness of the web as a means of reaching developing country audiences. This raises questions regarding the potential effectiveness of such web-based knowledge initiatives as the GDN or the Gateway discussed further below (WB 2003f, p. 20).

'Research' and ESW each fulfil different but complementary functions: 'research' seeks to provide general policy directions, while ESW operationalises these for a specific country or sector context. ESW refers to activities that involve analytical effort with the intent of influencing client countries' policies and programmes (WB 2003m). It has traditionally underpinned lending and investment operations, i.e. it happens upstream of lending, but is not linked to the preparation or supervision of specific loans or projects. It is carried out in operational departments of the Bank and, for LICs, increasingly in co-operation with DEC (see IDA 2003d, p. 3). ESW frequently draws on consultants, who tend to be financed through consultant trust funds provided by bilateral donors rather than through the Bank's budget and, depending on the particular report or activity, can be undertaken in some form of consultation with various government departments of a country, and sometimes with other stakeholders such as the private sector, trade unions, and civil society organisations.

Originally justified as necessary to ensure that Bank resources are put to proper use, the purpose of ESW has broadened recently and ESW outputs have come to span a wide range of policy issues, much beyond what can strictly be considered fiduciary concerns (see also below). ESW is categorised in core reports, which are undertaken for all countries in which the Bank is active and which include a Poverty Assessment (PA), a Country Economic Memorandum (CEM) or a Development Policy Review (DPR), a Public Expenditure Review (PER), a Country Financial Accountability Assessment (CFAA), and a Country Procurement Assessment Review (CPAR);[109] as well as a host of sector or issue reports – including Investment Climate Assessments (ICAs), Corporate Governance Assessments (ROSCs), Education Sector Reviews, Financial Sector Assessments (FSAs), Health sector Reviews, Energy-Environment Assessments, Risk and Vulnerability Assessments, Rural Development Assessments, and Institutional and Governance Reviews (IGRs) – which are undertaken depending on the perceived needs of a country. Appendix 1 provides a brief overview of the remit of the core reports. Appendix 2 provides a summary of all the non-lending services scheduled over a three-year period for a typical low-income Bank client – Ghana. These amount to a total of over 40 reports

[109] An Integrative Fiduciary Assessment (IFA) integrates the work normally carried out through a PER, CPAR and CFAA, and may substitute for them (IDA 2006a, p. 1).

and it is not unusual to find a total of over 30 ESW outputs over a three-year period for a LIC.[110]

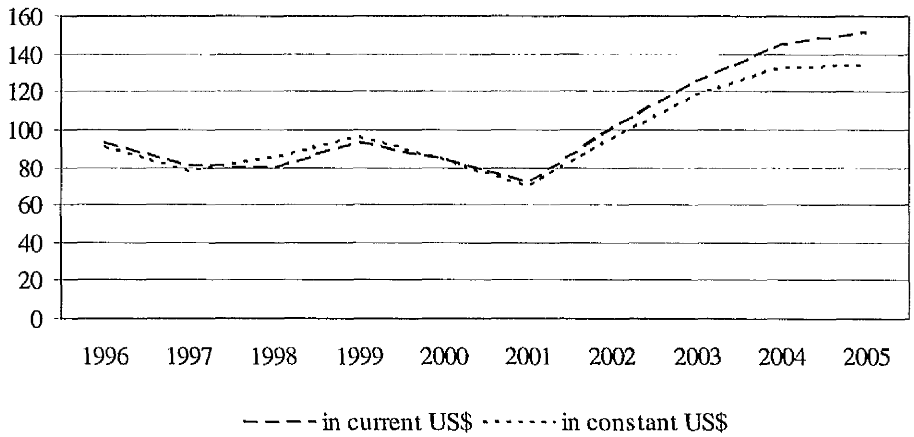
ESW also includes less formal outputs, such as policy notes, which are relatively smaller and more narrowly focused think-pieces that provide advice to borrowers, but which are not formally released as a report, and 'educational' services such as workshops, conferences, seminars and study tours. Since FY01, the Bank's annual review of the performance of its portfolio treats ESW on an equal footing with lending operations.

Five different possible objectives are attributed to ESW by the Bank. These include in order of imputed importance (IDA 2006a, pp. 19-20): to inform government policy; to inform lending; to inform and stimulate public debate; to build client analytic capacity; and to influence the development community. When the Bank measures the extent to which these objectives have been attained, a set of result indicators are assigned to each objective. These are instructive. For the first objective, it is assessed if the particular country to which the specific ESW pertains has adopted new legislation, if a government decree has been issued, or if a new government strategy has been adopted. For the second objective, the result indicators are straightforward: has a lending programme been agreed or is a new loan under preparation or implementation? For the third objective, results are reflected in whether the media in the relevant country widely reports Bank analysis, and whether major local stakeholders and academic publications give Bank views due attention. For the fourth objective, results are measured on the basis of whether the client makes a major analytic contribution to the ESW, and whether the client is learning to produce output independently. For the last objective, an assessment is made of whether additional resources were mobilised as a result of the ESW and whether there was a shift in donor policy or priorities (IDA 2006a).

Four trends can be discerned as having characterised recent ESW activity. First, as illustrated in figure 2.3, there has been a sharp increase in expenditure on ESW since 2002, and total expenditure on ESW, including trust funds, reached just over US$ 150 mn in 2005. This follows a decline and stagnation of resources allocated to ESW (IDA 2002b, p. 23).

[110] Each Country Assistance Strategy (CAS) includes a list of all non-lending services underway and planned for a particular country over a three-year period.

Figure 2.3: Expenditures on ESW, 1996-2005, in US$ millions.



Sources: WB (2002i, p. 48) for 1996-2000; WB (2004k, p. 29) for 2001; WB (2007, p. 96) for 2002-2005; WDI online for the US CPI (2000 = 100).
Note: The US CPI was used to transform nominal into real values.

ESW commands on average more than two times the resources available to the Bank's research department, and with such an amount of combined resources (lately standing at US$ 180 mn) the Bank is certainly the largest single source of analysis for the developing world. It could additionally be noted that the analytical quality of some of this ESW is increasingly similar to DEC research products, with the latest *Report on the World Bank Research Program* creating a category of 'ESW assimilated to Research' (WB 2007, p. 37).

For the WB (2002e, p. 25) the increased attention for ESW reflects 'the growing appreciation of an appropriate policy regime to overall development effectiveness'. It sees the products and dialogue generated by an ESW programme as a 'strategic contribution to policy development'. For then Managing Director, Shengman Zhang (2002, p. 1), increases in ESW are directly linked to the Bank's knowledge turn, the PRSP and the attempts to effect greater ownership and participation:

> Economic and Sector Work ... is coming to play an increasingly critical role in the Bank's tool-kit. The PRSP/CDF, the emergence of the Knowledge Bank, the growing sensitivity to ownership and participation, all point to the critical role of good policy and sound analysis.

In effect, for countries engaged in a PRSP process, the output and scope of ESW have increased significantly (see OED 2004, p. 42; WB 2004e, p. 16; WB 2004k, p. 42).[111]

Secondly, ESW has been characterised by attempts to bring about greater client participation (see WB 2002f; OED 2002, pp. 55-6; WB 2003f, p. 25). The Bank sees ESW as an important instrument for building institutional capacity, ownership and consensus for reform efforts. To that purpose it increasingly seeks 'partnerships' with local partners (IDA 2005, pp. 19-20).[112] A past note from the ESSD Network urged Bank staff to seek the active participation of 'stakeholders' in the preparation of ESW (WB 1995). It argued that as a result of collaboration in ESW the communication between Bank and governments would be improved, the Bank would gain better knowledge of and sensitivity to a client's circumstances, and a greater transparency in the Bank's work would increase the Bank's credibility within countries and among stakeholders (p. 1):

> P-CESW [Participatory Country ESW] leads to speedier acceptance of recommendations by Bank and borrower. Participation not only yields richer diagnoses of problems but also inspires and mobilises the actors to follow through on the consensus that has been built up.

The Bank then understands the purpose of participatory ESW as an important means of transmitting information and building consensus (WB 2002b, p. 19; IDA 2005, p. 20), as the key to the effective internalisation of the policy advice embodied in its analytical work, and as a way to create a constituency for policy innovation – rather than as a means through which it could incorporate a locally anchored or informed understanding of a particular policy context (WB 2002e; WB 2002f, p. 17). Indeed, an operational constraint on the way in which participation could possibly affect the content of ESW looms, reflecting a clear sense that ESW is owned by the Bank rather than by the specific country 'consulted' (see also Wilks and Lefrançois 2002, p. 16).[113]

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[111] See Brock et al. (2002, p. 34) and OED (2004, p. 43) on how the Bank's PAs, in particular, have been a significant basis for poverty profiles in many PRSP countries.

[112] See WB (2003f, pp. 25-6) for recommendations on how staff can effect such partnerships. These include: study tours; partnerships with local institutes; peer-to-peer knowledge sharing; translation of reports in local languages; and press conferences on reports.

[113] See, for instance, Bank management's response to an independent evaluation of IDA activities, OED (2002, p. 98):

> while the country must 'own' its vision and program, IDA must 'own' and be accountable to shareholders for its diagnosis and the programs it supports. In most cases, the country's vision, priorities and analysis and the Bank's diagnosis are mutually interactive, supporting and complementing each other. ESW, prepared and shared with clients and

Thirdly, ESW has become much more broadly disseminated through the Bank's website, through government offices, and through workshops and conferences, and the Bank's External Affairs department has become increasingly involved in this effort (IDA 2006a). Samoff and Bidemi (2003, p. 40) observe that:

> Formerly, many of the World Bank's documents remained confidential, available only to its staff and a small circle of others. More recently, more of its publications are broadly circulated, many now instantly accessible on its massive website ... Even resource starved African university libraries and bare shelf bookshops may have an ample supply of World Bank publications.

The authors point to the dual edge of such a proliferation. On the one hand, it is indeed desirable that Bank analysis is widely available, as it allows the tracing of its thinking. On the other, however, the profusion of documents and their authoritative character makes the Bank:

> the centre and focus of discussion and often the term-setter, manager, and arbiter of the discussion itself. The World Bank is not, however, a neutral discussion organiser but rather an institution with a strong agenda. Notwithstanding the plethora of publications, those mixed roles do not assure transparency or accountability or even equitable access to a debate in which issues are fully aired and critics have effective time at the microphone.

Finally, the Bank has encouraged greater collaboration with other development agencies in undertaking analytical work, in an attempt to pool knowledge and harmonise approaches across donors. These efforts are reflected in a growing body of joint ESW products delivered mainly to IDA clients, including those focused on poverty, financial management, PSD and the environment (IDA 2003d, pp. 3-4).[114] These 'partnerships' with other donor agencies enable the Bank to leverage its effort and to have greater impact, as other aid agencies increasingly use the Bank's diagnostic results and findings in their own country programmes (IMF/WB 2004, p. 6).

In sum, while ESW was originally justified on the basis of fiduciary concerns, it has increasingly assumed an 'advocacy' role. Tan (2006, p. 15) observes how:

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partners, provides key inputs and an analytic basis that the country can use in developing its vision and its own diagnosis.

[114] See www.countryanalyticwork.net , a joint donor website which compiles country analytic work by various organisations.

> The World Bank's Operational Policy (OP) 8.60 on 'Development Policy Lending' indicates that pre-financing assessments are critical to meeting the Bank's fiduciary obligations. In particular, the guidelines state that the Bank should focus on the 'the borrowers' overall use of foreign exchange and budget resources' through an assessment of the borrower's Central Bank 'control environment' in conjunction with the IMF staff ... and a review of the country's 'public financial management and procurement arrangements' for budget resources.

Yet, with the fast expansion of the various ESW outputs, their increasingly vast remit, and the set of additional functions that have been assigned to ESW (including consensus building and capacity building), it has become increasingly difficult to separate strict fiduciary concerns from other (more ideologically-driven) imperatives. Tan continues:

> The Bank's range of diagnostic instruments to conduct these 'expenditure reviews' and 'fiduciary assessments' has grown considerably in scope and complexity with the increasing focus on institutional policy over the years.

Most recently, the Bank views ESW as 'global public goods', to be used to 'motivate reforms through cross-country comparisons and benchmarking' (WB 2005d, p. 30). The implications of such an understanding of ESW are further pursued in chapter six.

2.5.3 The WBI and other knowledge initiatives

As the WB revitalised its approach to development, placing a greater emphasis on knowledge as a catalyst of reform, the WBI also came to play an increasingly important role (see also Thomas 1999). The WBI is the main training and educational unit of the Bank.[115] It aspires to be a centre of global learning and dissemination of knowledge about development (WBI 2005). It designs and delivers courses (traditional and long-distance), seminars, and policy advice, and seeks to provide 'a forum for the exchange and dissemination of practical knowledge gathered on the basis of the extensive research and operational experience of the Bank' (WBI 1999).

[115] The WBI was formed in 1999 by the merger of the Economic Development Institute (EDI), concerned with 'client learning', and the Learning and Leadership Centre, focused on Bank staff learning. For a brief historical overview of the EDI, see Stern and Ferreira (1997) and WBI (2005).

The WBI's activities have dramatically increased and table 2.3 documents how, in 2005, the institute trained 110,000 people, up from a mere 7,000 in 1996.[116]

Table 2.3: Number of participants in WBI client training

	1956	1973	1982	1991	1996	1997	1999	2002	2004	2005
Number of participants	20	496	1,700	2,900	7,000	20,000	28,000	48,000	79,000	110,000

Sources: WBI (2005); WB (2001c, p. 26) for 1996.

Further, whereas the WBI traditionally focused on government cadres or local policymakers, it now reaches beyond the apparatus of the state and increasingly seeks to train parliamentarians, journalists, opinion leaders, and representatives from the private and non-governmental sectors (see WBI 2005). In that context, it has set up a special programme that targets parliamentarians (WBI's Parliamentary Strengthening Programme) and, over the last decade, around 4,000 parliamentarians have attended workshops and seminars organised by the WBI (WB 2005a, p. 81).[117]

In addition to the WBI, the Bank has sponsored a host of knowledge initiatives and provides non-lending TA, with expenditure on the latter amounting to over US$ 100 mn in 2005 (WB 2007, p. 96).[118] The most remarkable of these knowledge initiatives are the Global Development Gateway (GDG), the Global Development Network (GDN) and, most recently, the Researchers Alliance for Development (RAD).[119]

[116] In addition, the WB supports other training activities such as, for instance, through the Joint Africa Institute in Abidjan, which was established in 1999 in a concerted effort by the WB, the AfDB and the IMF. Through this Institute, 4,000 participants are trained each year in courses ranging from macroeconomic management, to governance and social issues (WB 1999g).

[117] See WB (2005a, pp. 81-4) for a list of the various WBI activities that target parliamentarians. In 2000, a group of parliamentarians set up a parliamentary network on the World Bank website (www.pnowb.org) which, as of January 2006, claims to function independently from the Bank. The network, however, continues to work closely with the Bank, and many of its activities, including its Annual Conference and the Field Visit programme, are undertaken in collaboration with the Bank. In addition, its secretariat remains located at the External Affairs office of the Bank's Europe office in Paris.

[118] This is inclusive of trust funds (which accounted for almost US$ 70 mn). Non-lending TA includes such programmes as the Public-Private Infrastructure Advisory Facility. See WB (2004k, p. 30) for an enumeration of other such tasks.

[119] Others include: the Information for Development programme (*Info*Dev), launched in September 1995. It provides grants and TA to encourage policies that increase connectivity and support the innovative use of ICTs for development at global, regional, national and local levels (WB 2003f, p. 32). The Global Knowledge Partnership (GKP) (www.globalknowledge.org) supports programmes geared towards putting new information and communications resources into the hands of disadvantaged communities in North and South (Thomas 1999, p. 14). Originally co-ordinated by a secretariat located in the WBI, the initiative moved out of the Bank in 2001.

First, the GDG (http://home.developmentgateway.org) seeks to provide, on a single website, a common platform for shared material, dialogue and problem solving that is easier to access than the current wealth of information on the internet (King and McGrath 2004, p. 78). Compared to the Bank's existing external website, the ambition of the Gateway is to provide not just information and/or documentation, but judgement and analysis about best practice, along with scope for interactivity and matchmaking (p. 79). The site aims to meet the information and knowledge needs of a wide range of clients, from a local NGO looking for funding possibilities or an investor looking for joint venture partners to a donor wishing to know the latest on aid flows; as well as to provide global state-of-the-art knowledge and country-specific data. By June 30 2003, there were 24,000 users, with the site receiving about 94,000 visitors monthly (WB 2003f, p. 31). The Gateway offers four portal-based knowledge services: Knowledge/Topics; DgMarketplace; Aida; and Country Gateways. Knowledge/Topics assembles and publishes web content on some thirty development issues. Content is contributed by around 130 organisations and content editors from inside and outside the Bank manage each topic area (WB 2003f, p. 31). The DgMarketplace offers procurement listings from the Bank and other development agencies. AiDA publishes a directory of data on the Bank, other multilateral projects and all OECD-member bilateral projects. The Country Gateway is a centralised service that provides advisory services, technical support and help in mobilising funds for the establishments of country-based portals.

The Bank provided a total of US$ 15.5 mn for the start-up of the GDG. Following the creation of the independent not-for-profit Development Gateway Foundation in 2001, the Bank, as a member of the board of the Foundation, agreed to provide an additional US$ 5 mn over the next three years through its Development Grant Facility (DGF).[120] The Bank operates the GDG through a service agreement costing the foundation US$ 6 mn (none of which can come from the funds provided to the foundation from the DGF), and the Bank controls the positions of President and Treasurer of the Foundation, as well as three seats on the 18-member board (WB 2003f, p. 32).[121]

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[120] In FY01-02, the Bank also provided US$ 3.5 mn in grants for the Country Gateway Programme through *info*Dev. The Foundation attracted more than US$ 70 mn in additional funding (WB 2003f, p. 32).

[121] At the time, these arrangements prompted accusations of fraud and corruption by civil society organisations (see BWProject 2001). See also Marres (2004) on the Bank consultations on the Gateway with NGOs, and on how the modification of the Gateway's formal institutional status prompted by these consultations was limited to cosmetic interventions and failed to produce a governance structure for the Gateway that could assure its independence from the Bank.

Although the Gateway is formally established externally to the Bank, the Bank sees it as an important vehicle for its knowledge strategy (WB 2001c, p. 28; see also Wilks 2001). The Foundation's business plan (WB 2001b, paragraph 39) clarified that:

> While maintaining an arm's length relationship with respect to governance, it is expected that the Foundation will choose to align itself on a programmatic basis with key initiatives in the WB's knowledge strategy by building upon existing projects wherever possible. Key relationships envisaged thus far include those between the Foundation and the Information for Development Program (infoDev), the GDN and the GDLN.

This raised concerns that the GDG might strengthen the Bank's 'knowledge' position and crowd out existing sites of knowledge sharing (Wilks 2001). A study commissioned by the Bretton Woods Project four years after the initiation of the GDG found that it remained closely linked to the WB at the operational and strategic levels, that its information is predominantly from Northern sources, that its operations are not transparent or accountable to civil society, and that there is no clear identification of who the beneficiaries are and how they might benefit (Wilks 2004; Jha et al. 2004).

Secondly, in 1999 the World Bank launched the GDN, with a stated mission, WB (1999b, p. 3):

> to strengthen the capacity of developing country research institutions to perform policy-relevant research, to help them establish themselves as effective spokespersons on behalf of civil society, and to support their efforts to introduce the results of research into the policy debate.

The GDN is explicitly intended to be a forum for Southern knowledge-sharing through the organisation of conferences, collaborative research, research awards, etc, and more than 1,000 research and policy institutes throughout the developing world participate in GDN activities. The initiative for the GDN originated in DEC at the instigation of then Vice-President, Joe Stiglitz, and in partnership with the WBI. Today the GDN prides itself on its formal independence with headquarters in New Delhi, notwithstanding continuing budgetary dependence of more than sixty percent on the WB (GDN 2005, p. 31). Since its inception, the GDN Secretariat has also been headed by a former Bank official.[122]

For Stiglitz (2000b), the Knowledge Bank 'scans globally' for best practice and the GDN partners 'reinvent locally'. Local policy and research institutions are to adapt and prepare a 'transplanted policy initiative' to 'better survive and perhaps thrive in the local environment' (see also Squire 2001). As such, and more so when viewed against the backdrop of a persistent decline in national institutes of research in developing countries over the last two decades, the GDN can potentially play an important role in structuring the supply of development knowledge within developing countries, strengthening the advocacy and agenda-setting capacities of certain think-tanks and amplifying one discourse of a particular (economic) knowledge in preference to alternative voices (see also Kapur 2003, p. 14).[123] Certain policy approaches are reinforced by the multiplication of organisations at a domestic level and, although alternative perspectives on development and grass-roots knowledge are not necessarily excluded by either the Bank or the GDN, with the GDN in particular explicitly embracing 'multi-disciplinarity', their influence is more tenuous given the particular status (and state) of the discipline of economics (see also chapter three).[124]

Finally, in 2005, the Bank's External Affairs department initiated the RAD. The RAD is an informal network of researchers and academics that currently comprises more than 500 representatives of academic institutions and research centres, as well as research units in NGOs, bilateral agencies, the private sector and trade unions.[125] While the GDN seeks to promote the development of research capacity and research networks in developing countries, with potentially significant

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[122] See Johnson and Stone (2000) on the genesis of the GDN.
[123] On the role of think tanks in the GDN, see Stone (2000, pp. 167-71).
[124] Most recently, Stiglitz (2007, paragraph 17) has had to acknowledge the possibility of such a dynamic:

> I agree that one of the ways in which the Bank promotes development is to encourage better research around the world, and in particular in developing countries. That was why I instituted guidelines for encouraging joint research with those in developing countries and worked to create the Global Development Network. But given the dominant role that the Bank has in development research, there is a real need for care. There is a risk that the Bank uses its financial resources to divert research towards the agenda which it is pushing, and away from concerns of those in the country; or that it pushes the current development fads in the developed world. It can lead to a strengthening of an Orthodoxy. Some of these fears are surfacing in the context of Bank supported research in Africa … The GDN Africa Growth Project had put forth a set of views on the constraints or influences on growth in Africa which was strongly challenged, especially by African participants not associated with the Growth Project. Special efforts to maintain diverse perspectives will be required.

[125] For a list of member institutions, see http://siteresources.worldbank.org/INTRAD/Resources/RADmemberinstitutionsJuly2006.pdf.

implications for the nature of the ideas thus reinforced, the RAD seeks to foster relations between the Bank and outside academic and research expertise. Its stated objectives are as follows: to strengthen the voice of the academic and research community within the Bank and the international development community; to increase the flow of ideas between academics, policy makers, the Bank and other development agencies; to serve as a bridge between research bodies (individuals, institutes and networks), regional networks and other affiliates of the Bank; and to inform RAD members of the latest opportunities offered by the Bank (grants, calls for papers, research projects) (RAD 2005, p. 2). The RAD Secretariat is located at the Bank's Paris office and is co-ordinated by the Bank's Development Policy Dialogue Team (External Affairs, Europe). Its steering committee is made up of academics and researchers.

Since its recent inception, the RAD has engaged in the following activities. It offers 'Compact Seminars' on development to universities around the world. A 'Compact Seminar' is a two- to three-day series of workshops and presentations, RAD (2006, p. 6):

> aimed to raise awareness on development-related issues and policies among graduate students of various fields of study, young professionals and representatives of civil society organisations.

The seminars are prepared and carried out by the Bank (External Affairs, Europe) in partnership with the host institution and local Bank offices. The seminars are offered by the Bank free of charge, with running costs of the seminar usually split between the host institution and the Bank (with exceptions for institutions in developing countries). Since 2004, Compact Seminars have been organised in the following institutions: Jadavpur University, India;[126] Cairo University, Egypt;[127] Warsaw School of Economics, Poland;[128] Kiev Mohyla Business School, Ukraine;[129] Sorbonne Pantheon University, Paris.[130] From the respective programmes of these seminars, it seems that their main aim is to promote the activities of the WBG, with a particular emphasis on its private sector activities ('what role for the WBG in a

[126] For the programme, see http://siteresources.worldbank.org/INTRAD/Resources/ProgramJadavpurUniversity.pdf.
[127] For the programme, see http://siteresources.worldbank.org/INTRAD/Resources/CairoUniversity.pdf.
[128] For the programme, see http://siteresources.worldbank.org/INTRAD/Resources/WarsawSchoolofEconomics.pdf.
[129] For the programme, see http://siteresources.worldbank.org/INTRAD/Resources/CSKMBSDraftAgenda.pdf.
[130] For the programme, see http://siteresources.worldbank.org/INTRAD/Resources/CSagenda.pdf.

changing world?'; 'the WBG and its operational tools'; 'opportunities to work with the WBG').[131]

Apart from this 'roaming' seminar format, the Bank provides an in-house 'Global Issues Seminar Series' in which it offers semester-long series of weekly lectures by Bank staff (or staff from other international organisations) and delivers these simultaneously using video-conferencing technology to students of 5 to 7 universities in different parts of the world.[132] The RAD further participates in the organisation of conferences and workshops on the Bank and the study of development (ABCDE; 'workshop on the World Bank'); invites students from universities around the world to share their papers on the Bank through its website;[133] provides opportunities for students to present their work at Bank offices; and seeks to establish links between the Bank and academic networks (such as the Coimbra Group, the International Association of University Presidents, and the Association of Commonwealth Universities).

From its current activities, it then seems that the RAD is concerned more with promoting the operations and analytical propositions of the Bank across the broader academic community, with a particular emphasis on younger participants (students or recent graduates), rather than with exposing the Bank to outside expertise – in accordance with its officially ascribed mission (see also Stone 2007). The raises the issue whether RAD merely seeks to bestow the Bank's knowledge mission with further legitimacy (see also Van Waeyenberge 2006b, p. 25).

2.6 Conclusion

This chapter has sought to illustrate how, in response to a set of contradictions, the Bank has emphasised its allegedly unique capacity to act as a 'knowledge-broker' in development. While the Bank had come to exercise a leadership role in development during the 1980s, the renewal effort instigated by James Wolfensohn in the late 1990s sought to accentuate this role. This conveniently accommodated a set of changes in the economic, financial and political environment bearing upon the Bank. The emphasis on knowledge equally found rapid resonance across the broader donor community, tallying well with the pervasive pressures on aid and the changing emphases in aid practices documented in chapter one.

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[131] The content of the first four seminars was very similar, with minor variations. The last seminar, in Paris, incorporated the Bank's latest emphasis on infrastructure and development.
[132] The seminar series is designed and directed by External Affairs in Washington. See the RAD website for the topics and reading lists.
[133] See http://wbln0018.worldbank.org/exteu/SharePapers.nsf/pages/Homeen.

The Bank's knowledge enterprise has vastly expanded and has sought, in particular, to draw in local participants through initiatives such as training programmes, participation in applied Bank analysis and a host of Bank sponsored knowledge networks. In the Knowledge Bank discourse, the Bank sees itself as a 'clearing-house' for knowledge about development and understands its own knowledge as objective and value-neutral – assigning itself a special responsibility in the provision of knowledge regarding development, now understood as a global public good. The socio-historical, political and economic context in which its knowledge comes about and is put to use is dramatically disregarded – with a particular failure to account for the way in which features of the Bank's own political economy might affect norms of 'scientific' acceptability.

We document in chapter three how the explicit celebration by the Bank of a knowledge mission has happened in the context of an attempted re-engagement, at the Bank, with the complexities of development. Further, a closer investigation, in chapter six, of shifts in the CPIA – the instrument at the core of Bank engagement with its low-income clients – allows to illustrate further the importance of the knowledge role in the regulation of the Bank's relationship with these countries.

Chapter 3. Comprehensive development: a knowledge role legitimised?

3.1 Introduction

The assertion of a knowledge advantage for the Bank, and the donor community more generally, has been accompanied by a recognition of the inadequacy of the previous understanding of development promoted through development assistance. Development is again understood to be a complex process, requiring a 'comprehensive' approach. This contrasts with the reductionist conceptualisation of development promoted through the WC, most typically as the imperative of macroeconomic balance combined with the 'restoration' of price incentives.

A set of innovations in development economics provided the backdrop to this new discourse, often referred to as the PWC. These more easily accommodate a restatement of development economics as a sub-discipline, in contrast with the 'mono-economics' of the WC. The new development paradigm seems to bestow the self-proclaimed knowledge role of the donor community with a degree of legitimacy as the underlying analysis presents itself as 'scientific', devoid of ideological considerations and 'integrated' (bridging gaps with other disciplines). As put by the Canadian Development Agency (2001, p. 28):

> An organisation capable of implementing a comprehensive approach to development is one that intervenes at a strategic level and uses its portfolio of projects to support programme-level interventions, which are integrated into a country's national development plans or poverty-reduction strategy. This approach puts a premium on the knowledge base of a development agency. Increasingly, the true value-added of aid agencies today is their expertise in development – knowledge of the country, of its development situation and needs, of the desired solutions and how to achieve them, and of the resources, both physical and intellectual, that can be brought to bear on development challenges.

This chapter sits as an interlude between the previous two chapters and the subsequent three chapters. It serves a two-fold purpose. It sketches the changing understanding of development that has been promoted by the Bank and which provides the (rhetorical) context in which the redefinition of the aid regime documented in chapters one and two took place; and it acts as a (scholarly) background against which the analysis of the current understanding of aid and its translation in Bank operational realities, pursued in chapters four, five and six, can proceed.

First, the chapter makes a brief foray into the analytical foundations of the WC and sums up the latter's commonly acknowledged shortcomings. Secondly, it summarises empirical findings regarding the economic and social repercussions of WC-inspired programmes. Thirdly, it documents how, in the wake of the poor performance of its programmes and growing criticism, the Bank expanded the reach of its agenda. This culminated in the proclamation of a CDF by former President James Wolfensohn and a call for a PWC by former Chief Economist and Vice-President, Joe Stiglitz. Subjecting the particular propositions embodied in the latter to closer examination, however, reveals the limited extent to which they allow for better insights into the dynamics of development.

3.2 The Washington Consensus and development

A neo-liberal perspective on development came to dominate the agenda of many international development actors during the 1980s. It displaced a brief focus on poverty reduction which had emerged during the 1970s and had combined with a general appraisal of the need for the state to intervene to correct market imperfections (see Van Waeyenberge 2006a).

The new discourse was first articulated in a clear form in the Berg Report (WB 1981). In essence, the Report argued for a 'restoration' of the 'superior' allocative role of the price system and a 're-establishment' of the incentives allegedly deriving from private ownership – the mainstay of the subsequent structural adjustment agenda.[134] It indicated the rise of 'monoeconomics' in development, applicable across time and space, with which development economics ceased to exist as a sub-discipline (Hirschman 1981). 'Economic rationality' characterised agents in the less- and more-developed countries, and the universality of neoclassical economics, with its postulates of rationality and principles of maximisation, came to have general applicability (Meier 1999). This was clearly articulated by Anne Krueger (1986, p. 62), whose appointment as successor of Hollis Chenery, Vice-President for Research, had explicitly confirmed the neo-liberal turn at the Bank:[135]

[134] For comprehensive critiques of the Berg Report, see Sender and Smith (1984) and Gibbon et al. (1993).
[135] See also Williamson (1990, p. 19) on how the WC implied a dismissal of the development literature 'as a diversion from the harsh realities of the dismal science', with none of the ideas

Once it is recognised that individuals respond to incentives, and that 'market failure' is the result of inappropriate incentives rather than of non-responsiveness, the separateness of development economics as a field largely disappears.

What came to be referred to as the WC (Williamson 1990) aimed at economic policy reform with the purpose of eliminating all obstacles to a 'perfect market' as the presumed optimal path to growth. It proposed (or rather imposed) a stabilisation of the economy through control of the money supply (macro), and enhancing growth through a set of supply-side measures aimed at boosting private sector activity (micro). More specifically, the WC gave recommendations regarding ten policy instruments. First, budget deficits need to be kept under strict control (budget deficits cause inflation and capital flight) ('fiscal discipline'). Second, government subsidies need curtailing and government expenditures need to be redirected towards education, health, infrastructure ('public expenditure redirection'). Third, the tax base needs to be broadened and marginal tax rates cut ('tax reform'). Fourth, interest rates should be market-determined ('interest rate liberalisation'). Fifth, exchange rates are to be 'competitive', stimulating exports ('exchange rate management'). Sixth, tariffs are to replace quotas, and to be reduced as fast as possible ('trade liberalisation'). Seventh, FDI is to be encouraged by dismantling barriers to entry ('liberalisation of FDI'). Eighth, state-owned enterprises are to be privatised ('privatisation'). Ninth, the economy should be deregulated, i.e. regulations that impede the entry of new firms or restrict competition are to be abolished ('deregulation'). And tenth, property rights must be established and enforced ('secure property rights').

The WC inspired the policy reform programmes of the IFIs and, by the mid-1980s, the ideas about economic management underlying their structural adjustment and stabilisation programmes had become readily accepted orthodoxy across the official donor community. The Bank's Structural Adjustment Programmes (SAPs) were originally designed to act on the supply side. They were concerned with the long run (growth), the micro and real side of the economy. The IMF, through its stabilisation programmes, focused on the demand side, the short run (equilibrium), the macro and financial.

spawned by the development literature – such as the big push, balanced or unbalanced growth, surplus labour, the two-gap model – playing any role in it.

This initial division of labour implied different working areas for both institutions. The IMF focused on the money supply, budget deficits and the exchange rate (for the purpose of deflationary policies). The Bank focused on (internal and external) liberalisation of the economy to overcome market distortions and stimulate growth. By the end of the 1980s, however, the WB increasingly incorporated performance conditions with regard to inflation and the balance of payments in its adjustment programmes. Specific instruments of WB programmes were given new objectives more akin to demand management (stabilisation) than economic growth (see Mosley, Subasat and Weeks 1995). Fiscal policy's main concern became to reduce inflation, the real exchange rate's to improve the current account, and monetary policy became preoccupied with the external balance in terms of foreign exchange reserves (WB 1992a, p. 2).[136] Later on, the IMF expanded the scope of its conditionality to encompass changes in the trade regime, pricing and marketing policy, public sector management, public safety nets, restructuring and privatisation of public enterprises, the agricultural sector, the energy sector, the financial sector, and governance (see Buira 2002; Babb and Buira 2004). As such, the sharp distinction between the purposes of the programmes of the respective institutions gradually eroded with each encroaching on the original terrain of the other.[137]

While the stabilisation programmes, as designed by the IMF, relied on a specific analytical framework (the Polak model), no such analogue existed for the WB's adjustment programmes.[138] The latter's theoretical foundations consisted of a compilation of elements rather than one specific model. These were mainly: a belief in the gains that result from removal of market distortions based on general equilibrium (GE) theory (perfect markets); a presumption of investment bottlenecks as the main (or only) impediment to growth in accordance with Harrod-Domar (HD) growth theory; and a set of assumptions regarding government anchored in what has been called the 'new political economy'.

In the Arrow-Debreu theory of GE, the competitive market yields welfare maximising (Pareto-efficient) outcomes in the absence of externalities, public goods and natural monopolies, when there is a complete set of markets, and for given

[136] See also WB (1994a) and Branson et al. (1995) where policy performance is measured by fiscal, monetary and exchange rate policy, rather than by investment in physical or human capital.
[137] Even though the two institutions attempted to deal with the problems this overlap created through increased collaboration, see Mosley et al. (1995, pp. 51-5) and Ahluwalia (1999) for lurking issues of consistency. See Polak (1997) for a traditional account of the changing relationship between the IMF and the WB.
[138] See Tarp (1993) and Fine (2006c) for critiques of the Polak model.

preferences, initial endowments and technology (the first welfare theorem). Further, every Pareto-efficient allocation can be attained through the market (the second welfare theorem), implying a distributionally-neutral market mechanism. Equilibrium, which implies full employment as long as there is no interference with the workings of the market mechanisms, yields a complete set of relative prices incorporating all the available information; and the amount of money circulating in the economy does not affect this (real) outcome. Inflation is caused by excessive monetary growth and needs to be combated by decreasing the money supply. Within this framework, government activity is limited to lump sum redistributions and the correction of a well-defined set of market failures. Government should allow prices to be 'right' (reflecting scarcity and preferences) and individual economic agents to allocate resources efficiently in response to price signals.

Within the remit of mainstream economic theory, a set of issues can be raised revealing the limitations of the above for an understanding of developing economies.[139] First, GE theory is inadequate for the analysis of developing economies often characterised by missing markets and imperfect information (Stiglitz 1986, 1989).

Second, the implications of the theory of the second best (Lipsey and Lancaster 1957) are pervasive. In an economy characterised by many market imperfections, the removal of any such imperfection does not necessarily improve matters (taking the economy closer to its production possibility frontier) unless all imperfections are removed simultaneously (Mosley 1991; Falvey and Dong 1992; Mosley and Weeks 1993).

Third, in GE theory, removing distortions results in static efficiency gains, but has no implications for the rate of growth (movements towards rather than of the production possibility frontier). Static allocative gains are, however, easily confused with requirements for growth (see Husain 1994, p. 151).

Fourth, seeking these static allocative efficiency gains through extensive market liberalisation potentially jeopardises the development of a dynamic economy. Historical analysis of successful capitalist development points to the prevalence of dynamic over static concerns in the allocation of resources (see Chang 2002; Amsden 2004; Wade 2004a).

[139] Beyond the confines of mainstream theory, there are fundamental methodological and conceptual issues confronting neoclassical theory. These include: methodological individualism; rational choice; optimisation; the role of equilibrium; and its tendency for axiomatic deductive reasoning. For a summary of the way in which these undermine meaningful social theory, see Fine (1981).

Fifth, the causes of inflation are both real and monetary. The structuralist school has long emphasised the inevitability of inflation in an economy that is attempting to grow rapidly while characterised by structural bottlenecks. The latter typically relate to the distribution of income across social groups, the distribution of productive resources between public and private sectors or the particular foreign exchange needs of a developing economy – each possibly contributing to low elasticities in agricultural supplies, persistent balance of payment or fiscal problems, with potentially inflationary consequences. Monetary contraction is also likely to have high costs, causing falls in real output and adversely affecting prospects for long-term growth through its negative impact on investment (Kay 1989).

Sixth, the constraints on growth are ill-understood in the Bank's Revised Minimum Standard Model (RMSM), which is anchored on the HD equation.[140] In the latter, capital appears as the main constraint on growth. The growth process is modelled as a steady-state balanced process. There is an underlying presumption that the availability of investible resources implies their investment (full employment). And the economy is modelled in aggregate single sector terms. However, in practice, growth is typically characterised by structural transformations, implying changes in the rates of accumulation, changes in capital-output ratios (e.g. as shifts in the sectoral composition of economic activity take place), changes in population growth, changes in income distribution, or changes in consumption patterns, all of which are assumed away in a growth framework in which all variables (savings rate, capital output ratio and population growth rate) grow at a same and constant rate along a steady state balanced growth path (see Syrquin 1998; Fine 2003).

The focus on capital scarcity as the main constraint on growth also misrepresents the conditions affecting growth prospects in developing countries. Cassen and Nissanke (1991, p. 30), for instance, draw attention to the fragmented state of domestic resource mobilisation in developing countries as a constraint on the intermediation between savings and investment; furthermore, high risk covariance in mono-cultural economies strongly affects the investment climate. Weeks (1992) points to the importance of factors complementary to capital that are likely to be in short supply (e.g. skilled labour), and draws attention to the issue of demand constraints with repercussions for capacity utilisation and hence investment levels. In this vein, Bacha (1984) attempts to reappraise the two-gap model, emphasising the

[140] For an elaborate deconstruction of the RMSM, see Tarp (1993). For a recent defence of the use by the Bank of the RMSM, see Ranaweera (2004).

restrictions of the full-capacity assumption in the gap models and underlining the need to distinguish between potential and actual output. Finally, the HD framework assumes technological change to be exogenously determined, and its one-sector representation of the economy cannot easily be extrapolated to provide inference for multi-sector economies as demonstrated with the Cambridge Controversy (see Fine 2003).

Seventh, in addition to the erroneous presumptions regarding states, markets, private sector, money and growth, implicit in the frameworks underlying structural adjustment and stabilisation, there are inconsistencies between the tools used for stabilisation or adjustment and long-term development with particularly damaging implications for investment levels (see Stein 1992).

Eighth, an attempt to 'marry' the Bank's growth model (the RMSM) to the IMF's Polak model in a merged model (Khan and Montiel 1989) heavily restricts the growth projections of the model (Tarp 1993; Fine and Hailu 2002). Finally, the theory of perfectly working markets has been supplemented with a set of strongly biased normative presumptions regarding the public sector (Streeten 1993). Essentially, in the 'new political economy', governments consist of self-serving bureaucrats who pursue their own interests at the expense of the common good. Furthermore, public sector investment 'crowds out' private activity. The state emerges, Chang (2003, p. 48) comments, as:

> an agent which serves the interests of politically influential groups inside and outside the state apparatus (politicians, bureaucrats, interest groups), which means that state intervention is likely to create allocative inefficiencies, organisational slacks ... and rent-seeking 'wastes', rather than correct for 'market failures'.

In consequence, withdrawal of the state becomes necessary 'to prevent the corrupting influence of politics on the management of the economy' (p. 50).[141]

These premises have been elaborately criticised in the literature. Critical deconstruction of IFI-sponsored policies, however, has often implied a re-emphasis on the need for state intervention for successful development (see e.g. UNECA 1989b; Streeten 1993; Weeks 1998; Mkandawire and Soludo 1999). This re-connects to a large literature that has demonstrated the successful and pervasive role of the

[141] For a comprehensive overview of the various theories that constitute the new political economy, see Chang (1996). For a collection of critiques in the context of structural adjustment, see Gibbon et al. (1992) and Olukoshi (2003). For a reappraisal of public enterprise performance in developing countries, see Chang and Singh (1992).

state in promoting economic development. Yet such a premise has tended to perpetuate an underlying analytical dichotomy of market versus state, to the neglect of an investigation of the political-economic dynamics steering both state and market outcomes (see Fine and Stoneman 1996; Fine 2006a). An analysis along the latter lines implies particular attention to socio-economic structures and processes, how these change in the wake of structural adjustment, and the concomitant implications for accumulation and economic development (see for instance Ruccio 1991; Chachage 1992; Sachihonye 1992; Gibbon et al. 1993; Bangura 1994; Wuyts 1994; Gibbon 1996; Olukoshi 1996; Cramer 2001). Rather than replacing the set of general (normative) presumptions regarding the market by another set of equally abstract (and normative) presumptions regarding the state, the importance of an analysis of the dynamics of development that is strongly anchored in the empirical and varied realities of developing countries transpires.

3.3 The Washington Consensus confronts reality

The analytical shortcomings exposed above have been compounded by the experience of structural adjustment and stabilisation during the 1980s and early 1990s. We briefly sum up the main features of this experience.[142] This summary draws on the impact literature of the IFI programmes which is, however, hampered by a set of shortcomings related both to measurement methods and data problems.[143]

First, the effect of structural adjustment and stabilisation on investment has been unambiguously negative (see Taylor 1988; WB 1990a; Cornia 1991; Elbadawi 1992; Elbadawi et al. 1992; Jespersen 1992; Stewart 1994; Mosley et al. 1995). This has often been the result of sharp drops in public sector investment and an inadequate private sector investment response. In SSA, investment declined on average by 0.5 per cent per annum between 1980 and 1994, and the share of investment in GDP, which had averaged around 26 percent in the 1970s, fell to below 20 percent in the 1980s and to 16 percent in the first half of the 1990s (UNCTAD 1998, p. 123). The Bank, however, has often downplayed these dramatic falls in investment rates as intermediate steps towards greater investment efficiency (see WB 1992a, 1994a).

[142] For more elaborate documentation, see van der geest (1994); de valk (1994); White (1996b); Mkandawire and Soludo (1999); and more recently SAPRI (2002). The Structural Adjustment Participatory Review Initiative (SAPRI) was originally instigated by James Wolfensohn, and set out to be a collaborative enterprise between a vast network of civil society organisations and the Bank. As the country investigations began to yield draft findings, however, the Bank tried to downscale its involvement and ultimately withdrew from the exercise (see SAPRI 2002, pp. 23-6).

[143] For a comprehensive summary of the various evaluation methods and their respective shortcomings, see Soludo (2003, pp. 34-48).

Second, while the effect on the external account was initially positive (Mosley et al. 1995), controversy remains about whether this was due to improvements in export performance (Elbadawi 1992; Elbadawi et al. 1992; Husain 1994; Killick et al. 1998) or occurred as a result of import compression (Ndulu 1991; Jespersen 1992). By the end of the 1990s, however, negative trade balances had sharply increased. For the nine countries in the SAPRI studies (Bangladesh, Ecuador, Ghana, Hungary, Mexico, the Philippines, Zimbabwe, El Salvador, Uganda) these had settled at about 5 to 6 percent of GDP, more than double the level of the 1960s. As a result, the total external debt of these countries doubled between 1984 and 1999 (SAPRI 2002). Furthermore, there are strong concerns that export growth has been limited to primary products with limited implications for growth of export earnings in the context of deteriorating barter terms of trade. Husain (1994) observes that while the volume of exports of nine major export commodities in adjusting countries in SSA increased by 75 percent for the period 1985-90 compared with the 1977-9 averages, the export earnings from these exports fell by 40 percent over the same period (see also Cornia 1991; Helleiner, G. 1994; Stewart 1994).

Third, the catalysing effect on other financial flows did not materialise (Husain 1994; Bird 1997). Bird and Rowlands (2000, p. 965) observe:

> it seems that empirical estimations cast considerable doubt on the proposition that IMF or World Bank conditionality transmits a positive signal to private capital markets. Private sources tend to react negatively, if at all, to these arrangements, and the negative reaction tends to be more pronounced for the higher conditionality agreements.

Fourth, although debt overhang plays an important role in affecting the economic performance of the recipient countries (Helleiner 1992; Martin 1997), the external debt stock of SSA has increased dramatically since the beginning of the adjustment enterprise and this has not been accompanied by the necessary acceleration in growth to sustain future debt servicing (WB 1997a, p. 19). The countries classified by the Bank as 'poorest' compliers, which incidentally as a group originally had the lowest debt to GDP ratio as compared to the countries categorised as 'weak' and 'strong' compliers, have seen their debt to GDP ratio increase by 127 percent (from 87 percent pre-adjustment to 197.5 percent in 1994).

Fifth, the social repercussions of adjustment have been particularly damaging, with adverse movements in both the distribution of real income through the market (declining real wages and falling levels of formal sector employment) and public provisioning by the state (Cornia et al. 1987; Cornia et al. 1992; pp. 20-6; Stewart 1992; Bangura 1994; Pio 1994; Seshamani 1994; Mkandawire and Soludo 1999, pp. 69-75; van der Geest and Wignaraja 1999). SAPRI (2002, p. 86) documents how the Mexican minimum wage lost 69 percent of its purchasing power since the beginning of adjustment in 1982, and the number of people living in extreme poverty (those unable to obtain the basic food basket) rose from 6 million to 30 million between 1994 and 2000. Across its country studies it found that real wages had systematically deteriorated under adjustment/stabilisation and income distribution was less equitable than before adjustment policies were implemented. The lowest-income groups tended to experience the largest increase in unemployment and the greatest deterioration in their wages. Furthermore, the SAPRI findings point to the systematic weakening of workers' rights under structural adjustments as their rights to organise and bargain collectively were severely curtailed (p. 89).

In addition, the structural reforms in the social sectors have been targeted not only at the immediate objectives of curbing government deficits and increasing its revenue, but have also aimed to achieve large-scale changes in the role of the state in social provisioning. This has implied a radical shift away from the role of the state as one of provider and guarantor of universally accessible social services to one of providing essential services in a targeted manner only to those on the margins, while the role of the market and the private sector in the provision of social services (mainly health and education) has been strongly promoted (McKintosh 1995; SAPRI 2002).[144] SAPRI (2002, p. 169) illustrates how, in the face of low wages and high unemployment levels, the imposition of user fees and the rising cost of services to local populations have increased hardships on the poor, and the targeting of state subsidies to those in extreme poverty has not only failed to be an effective policy instrument for addressing poverty but has perpetuated inequality.

Nevertheless, a few authors have persistently demonstrated how adjustment policies have had strongly positive distributional implications.[145] A WB assessment of the social dimensions of adjustment boasts of a decline in poverty in 15 of their sample of 23 adjusting countries (Branson et al. 1995). Upon closer inspection, however, these declines in poverty were very small: less than 1 percentage point in six cases, between and 1 and 2 percentage points in five cases, and more than 2

[144] See also the observations in chapter two regarding, more recently, the rapid expansion of IFC activities, including in the social sectors, and the role of OBA therein.

[145] See in particular Sahn and Sarris (1991), and Sahn (1992, 1994). For a critical deconstruction of various Bank-sponsored accounts of adjustment and poverty, see Ali (2003).

percentage points in only four cases. Furthermore, while poverty 'declined' in more than half of the sample, inequality increased in 14 out of the 23 countries (p. 9). A 1997 Bank Report on its adjustment operations in SSA found that poverty alleviation (or the absence of an increase in the absolute number of people living in poverty) was achieved only in 10 countries out of 35 surveyed (WB 1997a, p. 15).

Finally, the output response in agriculture and industry to price-based policies has been elusive, and the implications of liberalisation and privatisation policies on industrial capacity have been predominantly negative (Mkandawire 1988; Pack 1988; Stein 1992; Gibbon et al. 1993; de Valk 1994; Lall 1995; Bennell 1995).

3.4 From Washington to post-Washington Consensus: comprehensive or illusive development?

By the early 1990s, the Bank could no longer simply ignore the various critiques of its adjustment programmes. It confronted mounting criticism, however, by opportunistically expanding its agenda, to include institutions, participation, governance, poverty, and social capital, while safeguarding the underlying economic agenda, as clearly re-affirmed in the 1991 WDR *The Challenge of Development* (WB 1991) (see Gibbon 1993). In practice, the expansion of the agenda gave birth to successive generations of SAPs, pegging 'social concerns' (expenditure reviews, social safety nets, compensatory programmes) and 'participatory measures' ('transparency', 'ownership', role of 'social partners') to the core policies of stabilisation, liberalisation, and privatisation (see van der Geest and van der Hoeven 1999).

An important moment came when Japan, the Bank's second most important shareholder, attempted to challenge the Bank's (core) economic orthodoxy. In what a Japanese aid official was to describe as the 'intellectual awakening of a sleeping partner' at the Bank (Goto 1998), the Overseas Economic Cooperation Fund – the main Japanese aid agency – began to question the Bank's stance on structural adjustment (OECF 1991). The issues raised touched upon: first, the sustainability of growth in the context of structural adjustment, and the possible need for additional investment promotion measures; secondly, the possible need for protection of certain industries in order for some viable export industry to develop (instead of the blanket liberalisation policies); thirdly, doubts regarding the (exclusive) reliance on market mechanisms for the mobilisation of development finance (accompanied by a proposal for subsidised lending under certain circumstances); and, fourthly, the conditions under which privatisation was being carried out.

Subsequently, Japan commissioned the WB to undertake a study of the East Asian development experience. The consequent *East Asian Miracle: Economic Growth and Public Policy* (EAM) (WB 1993a) explored 'the contribution of fundamental and interventionist policies to East-Asia's remarkable growth' (p. 26). The Report argued that East Asia's economic success had been largely achieved by 'getting the basics right'. A stable macroeconomic environment had provided the 'essential framework for private investment'; policies had raised financial savings; successful education policies had been pursued; and a bias against the agricultural sector had been avoided. Furthermore, price distortions had been kept within reasonable bounds, the economies had been open to foreign ideas and technology (p. 5), and the 'necessary' levels of flexibility had been maintained in labour markets (p. 19).

The Report continued, however, that these 'fundamentals' did not tell the entire story. In most of these economies 'the government intervened ... to foster development, and in some cases the development of specific industries'. Assessing whether these interventions were successful or not in contributing to growth then became the 'most difficult question' the Report tried to answer (p. 24). It drew the conclusion that (p. 6):

> in a few economies, mainly in Northeast Asia, in some instances, government interventions resulted in higher and more equal growth than otherwise would have occurred.

However, the 'prerequisites for success' had been so demanding that policymakers seeking to follow similar paths in other developing economies would meet with failure. This touched upon issues of the external environment (the particulars of the trading regime) and whether the countries concerned had high quality bureaucracies.

The final and unsurprising conclusion was that although the sheer diversity of these policies precluded drawing any simple lessons, 'pragmatic adherence' to the fundamentals (the market-oriented aspects of East-Asia's experience) could be recommended with few reservations (p. 26). Thus, Chang (1999) observes, in the same Report, the WB managed: first, to admit a theoretical case for industrial policy; secondly, to refute its empirical importance for industrial performance in East Asia;

and thirdly, to offer practical objections on why the policy was not transferable to other countries.[146]

However, even though, to the consternation of its initiators, the EAM Report endorsed a continuing 'market-friendly' approach in a neoclassical framework, it also somewhat facilitated, according to Goto (1998, p. 59):

> a shift from the simple dichotomy of government or market towards the seeking of a cooperative relationship between the two – government as well as market.

Next, the Bank was to find a way to move beyond structural adjustment and the EAM, i.e. to move on from neoclassical economics, a question 'at the frontier of development economics' (Goto 1997, p. 7). Joe Stiglitz, who had been appointed Bank Vice-President and Chief Economist in 1997, was to take up the challenge, one that became more compelling with the scant fruits of IFI-led transitions in the eastern European countries (see Florio 2002), and the outbreak of a series of international financial crises (Mexico 1994; East-Asia 1997-8; Russia 1998; Brazil 1999).

In the 1998 WIDER lecture, Stiglitz (1998a) strongly argued for a reconsideration of the WC. For him, the latter had advocated the use of a small set of instruments (including macroeconomic stability, liberalised trade and privatisation) to achieve 'a relatively narrow goal (economic growth)' (p. 13). Furthermore, while the WC may not have been sufficient for development, certain successful performers 'paid little heed to it'. In its core area (the economic realm), the WC had been 'at best incomplete and at worst misguided' (p. 3). A focus on inflation, for Stiglitz, had led to macroeconomic policies that were not the most conducive to long-term growth and had detracted attention from other sources of macroeconomic instability such as weak financial sectors. More generally, a focus on trade liberalisation, deregulation and privatisation had been to the detriment of other important conditions ('ingredients') for stability and long-term development. These comprised: robust financial systems which necessitate a strong legal framework as well as regulatory and oversight institutions; regulation for the privatised industries; competition policy; investments in human capital; technology policies. In all these areas, government was, according to Stiglitz, to complement the market.

Furthermore, the new approach sought 'broader' goals. Development was no longer the 'mere interplay of economic variables', but a 'holistic' process, a

[146] For an elaborate account of the EAM as an exercise in the Bank's art of paradigm maintenance, see Wade (1996).

transformation of society (Stiglitz 1998b). Most previous development strategies had only focused on 'pieces of that transformation', often 'failing miserably' (p. 5). Their most important failure had been a narrow focus on economics, conceiving development as a 'technical problem requiring technical solutions' (p. 6). The CDF, put forward by the WB President in 1999, endorsed the 'holistic broad-based approach to development'. Constraints on development were now 'structural' and 'social', not remediable solely through economic stabilisation or structural adjustment (Wolfensohn 1999).

The new agenda therefore tried, at least in principle, to move beyond the reductionist conception of the development process, which was characterised by a macroeconomic bias towards stabilisation, a microeconomic bias towards price incentives, and a focus on physical capital as predominant constraint on growth. It, further, sought to project a different view of state-society interactions. Following the 1997 WDR (WB 1997c), development became an 'inter-sectoral cooperation process'. The projected antagonism between state and society/market gave way to a notion of 'partnership': the private and public sector were now understood to be intimately 'entwined' (Stiglitz 1998a).

In this approach, the persistence of market failure and missing markets was increasingly recognised. Such failures, however, no longer implied 'old-style' government intervention where the state 'supplanted' the market. Now, 'modern' ways were to be deployed. Furthermore, with different sources and degrees of market failure (and states with varying levels of 'capability'), the implications for the role of the state could differ significantly between countries (WB 1997c, p. 26). The quest then became for an institutional set-up comprising a 'partnership' between state and society, involving both private profit and non-profit sectors, that would maximise 'benefits to society'. Crucially, the state was to make sure that market failures were overcome without imposing 'unnecessary' costs on society. Hence, when characterised by low 'capability', the state was to rely, as much as possible, on the relative strengths of the private sector, the community, the family and the individual ('citizen') (Stiglitz 1998b).

The new agenda reflected a set of propositions that had become increasingly popular in development economics. These drew on a collection of mainstream innovations, rejecting an implicit framework of GE and exogenous growth. More particularly, assumptions regarding market structure (imperfect competition), attributes of the economic agent (imperfect information and/or bounded rationality), production characteristics (increasing returns to scale), and/or presence of a complete set of markets were challenged with a set of theoretical innovations, each of which had important implications for the workings of the price system. Meanwhile, growth theory had moved from an exogenous description to new conceptualisations of growth, endogenising the technology variable and/or incorporating increasing returns. Further, either through these theoretical innovations or through the extension of the old orthodoxy into new analytical terrain, traditionally non-economic issues became increasingly addressed within the discipline (see Fine 1997).

In sum, two trends were at work. On the one hand, there was a re-statement of mainstream economic theory, which incorporated economic features recognised as increasingly important in the 'real' world (economies of scale, imperfect information, missing markets). On the other, through both this type of innovation and 'Becker-type endeavours' (Fine 1997), the economic analysis moved to address features beyond the traditionally 'economic' (institutions, family, social networks). And these innovations allowed, in particular, to accommodate the context of development. Bardhan (1993, p. 139, my emphasis) argued that:

> as economic theory has turned more toward the study of information-based market failures, coordination failures, multiple roles of prices and the general idea of the potential complexity of market interactions, it has *inevitably* turned to questions that have long exercised development economics.

Moreover, with this endeavour, it was claimed that not only were the 'old debates' of development economics, with their particular emphasis on economies of scale, being revisited (see Murphy et al. 1989; Coricelli et al. 1998; Krugman 1999; Ros 2000), but they, in addition, acquired 'scientific legitimacy'. Krugman (1999, p. 12) candidly observed:[147]

> Good ideas were left to gather dust in the economics attic for more than a generation; great minds retreated to the intellectual periphery. ... The truth is, I fear, that there is not much that can be done about the kind of intellectual waste that took place during the fall and rise of development economics. A temporary evolution of ignorance may be the price of progress, an inevitable part of what happens when we try to make sense of the world's complexity.

[147] See also Bardhan (1993, p. 131).

Finally, these theoretical 'advances' took place in the context of the end of the Cold War and this, according to the OECD (1995, p. 3), implied the 'liberation' of thinking about development issues:

> Although the end of the cold war did not produce a windfall of resources for development cooperation, it has liberated thinking about development issues from the constraints of competing ideologies and world views. A greater convergence of views between industrialised and developing countries about issues is evident. The new paradigm for sustainable development is emerging as an integrated process of political and economic stability, good governance, popular participation, investing in people, reliance on market forces, concern for the environment, and a vigorous private sector.

If there had not been a convergence of income, at least there seemed to be 'convergence' of ideas, with those derived from the erstwhile socialist bloc disturbing thinking much as the state had been seen as distorting policy, as for Stiglitz (1998b, p. 8):

> the end of the Cold War has brought an end to the ideological debate on whether development should be market or government (plan) led.

And putting this in the broader historical context of the experience of colonialism and decolonisation, Stiglitz (2000a, p. 4) added:

> fifty years after the supposed beginning of the end of colonialism, it appears that many vestiges of the colonial mentality have remained. For their part, nations in the developing world have had to struggle with overcoming their colonial heritage; it is not necessarily the case that everything that the colonists left behind – including their economic theories – was flawed; and it is not necessarily the case that the economic theories of those that supported the struggle for independence were sound. This was brought home forcefully by the collapse of the Soviet empire, which made those countries which had not yet become disillusioned by the failure of socialist development strategies re-examine their approach to development.

After the temporary retreat of development from economics during the reign of the WC, a resurgence of development economics, hence, seemed to take place, with the new framework purportedly incorporating issues whose neglect had rendered the preceding analysis incomplete and claiming to revisit important matters touched upon in earlier debates on development. Moreover, the new approach allegedly anchors the economic analysis of development in its broader 'social reality' and has become devoid of 'ideological interference'. The approach to development is again 'comprehensive', capturing its 'broader' aspects beyond the preceding technocratic bias along which development had been reduced to a mere interplay of economic variables, and which had been prone to an excessive macro-bias towards stabilisation and a restricted micro-agenda of price incentives.

However, it remains questionable whether the PWC, and the paradigm of 'comprehensive' development that has been attached to it, provides us with projected improvements in insights and recommendations regarding the processes of development, particularly given its alleged capacity to accommodate both the 'economic' and 'non-economic' and to theorise 'beyond the market'. Unsurprisingly, the verdict is disappointing. First, the restatement of an analysis of development proposed by Stiglitz and others, essentially proceeds on the same principles of optimisation and choice as its predecessor, its distinctiveness lying mainly in changes in the assumptions regarding the attributes of the economic agents and the environments in which these optimise (imperfect information, bounded rationality, increasing returns, missing markets, imperfect competition).[148] A 'softening' of the assumptions strengthens social theory on the basis of methodological individualism. The latter, however, is well-known for its limitations to address the 'economic' or the 'social', as it first takes the social out, only to re-introduce and re-construct it afterwards.[149]

Second, the extension of the analysis into the traditionally non-economic (institutions, knowledge, innovation) has been at the expense of substantive content and analytical power.[150] The analysis remains hampered by its ahistorical, asocial, and reductionist method. Individual choice and optimisation provide the ultimate explanation for any economic or social phenomenon. Third, the dynamics of production remain ill-understood. The understanding of the latter is constrained by a representation of production as a combination of factors of production under differing technologies, with now, admittedly, attention for organisational factors (institutions) in addition to the merely technical.

[148] This continuity has implied significant neglect in the PWC of the various critiques that had been directed at the WC (see Standing 2000; Fine 2001b).
[149] See Fine (2002a) for an examination of the innovations in economics as a Kuhnian paradigm shift.
[150] See Fine (2001a) for an elaborate illustration of this in the context of 'social capital'.

Yet, and fourth, development remains a matter of position of the production function, where, according to Stiglitz (2003, p. 123):

> gaps in knowledge and organisation, both between more and less developed countries and within developed countries account for much of the difference in income.

The PWC is inadequately equipped to deal with issues such as technological progress and general productivity growth, as for Stiglitz (2005) the general argument regarding imperfect information causing markets to fail – which implies the need for a 'market efficiency-enhancing' role for government – merely becomes more compelling when dealing with innovation.[151] Following a simple transposition, Stiglitz (2005, p. 25):

> knowledge can be thought of as a particular form of *information*, and, as a such, the results of the economics of information apply to the realm of the economics of innovation.

Knowledge has attributes of a public good and innovation generates externalities. Missing markets (such as the absence of insurance markets) worsen the uncertainties associated with innovations. 'Modern' industrial policy, then, focuses on (p. 27):

> attempting to identify areas in which interventions to correct market failures are likely to be most successful. For instance, it looks for areas in which *coordination* failures may loom large, or where there are large spillovers, or significant problems of appropriability.

A role for government emerges in finance, research, education and infrastructure. 'Modern' industrial policy also attempts, so far as possible, to employ 'market-like' mechanisms in implementation (p. 28) and government performs a 'catalytic' rather than controlling role (p. 29). As such, Stiglitz (2005, p. 31) concludes, in alleged contraposition to the WC, that:

> a more balanced approach recognizes the vital role that government can, and must, play, and that includes *both* regulation and the provision of public services, like education.

Clearly, substance and meaning are found wanting in Stiglitz's foray into the dynamics of innovation, technological progress, and productivity growth, as innovation is reduced to 'knowledge', 'knowledge' to 'information', and the process of industrial upgrading to the tackling of informational imperfections. The economy

[151] Stiglitz (2005) brings together the set of ideas on industrial policy previously articulated in Stiglitz (1996, 1997, 1998a).

remains understood through the prism of exchange with little understanding of the institutional arrangements affecting value creation (Lo 2001). Derangiyagala (2001, pp. 90-4) highlights, in particular, how: the approach is based on an inadequate understanding of firm behaviour and, in particular, of the ways in which firms generate and acquire knowledge; it is based on an inadequate understanding of the process of technology development – with insufficient attention for what actually happens inside the technological 'black box'; and how, as a result, successful industrialisation is, in essence, reduced to a removal of market failures and a move towards well-functioning markets. This ignores that market failures are often intrinsic to the process of production, and, as Amsden (1997, 2004) emphasises, that successful industrialisation frequently involves the creation of market failures and distortions in resource allocations not their correction, as deliberate attempts are made to 'get the prices wrong' in order to make manufacturing activity profitable (Amsden 2004, p. 10).

A recent UNCTAD (2006a, p. 288) Report on the LDCs, then, restates the persisting case for a new paradigm, beyond *both* WC and PWC, which:

> places the development of productive capacities at the heart of national and international policies to promote economic growth and poverty reduction in the LDCs. In this approach, policies should focus on promoting capital accumulation, technological progress and structural change in LDCs. They should seek to sustain a virtuous circle in which development of productive capacities and the growth of demand mutually reinforce each other. This should be done in a way in which productive employment opportunities expand.

Such an approach would draw on the historical experience of development as highlighted in the well-known studies of the fast-growing 'latecomers' (Amsden 2004) with their attention for the broad-based nature of discretionary government intervention through the use of manifold instruments including: trade tariffs, import substitution, export promotion, the extensive use of performance requirements on both domestic and foreign investment, selective promotion of industries, and massive investment in skill creation, infrastructure and support institutions (see Amsden 1989; Wade 1990; Amsden 2004; Chang 2004; Lall 2005). In the context of the LDCs, UNCTAD (2006a, p. 291), further, draws attention to the importance of a twin strategy of investing in dynamically growing sectors while at the same time building capacity in sectors where the majority of labour is employed and of deepening linkages between the latter and former sectors.

A 'developmental paradigm' would emphasise the importance of strengthening the capacity of late developers' governments to mobilise financial resources for investment and growth through both tax and ('off-budget') non-tax avenues – including deposits in government-owned banks, post office savings accounts and pension funds, and pricing policies in state-owned enterprises (see Amsden 1997; Krieckhaus 2002). And macroeconomic policy tools would be reattributed with growth and employment objectives (see Bradford 2005). Crucially, the approach would emphasise the importance of leaving the 'policy space' for developing countries *open* to a wide range of interventions. This would, however, not be at the expense of the recognition of the local historical-political and social conditions that steer the way in which such policies come about and can be implemented, and the specificities of the external environment in which catch-up development would occur. A prescriptive approach would, therefore, need to be anchored in a careful examination of domestic and external socio-economic, political and historical specificities.

Although Stiglitz's PWC needs to be credited for its strong critique of the stabilisation bias that characterises the WC,[152] it offers little prospect as a 'paradigm' for development, with its particular failures to provide insights into the crucial dynamics of production and accumulation. The departure of the PWC from the WC is limited, and so are the insights it provides into development. Also, in the context of its propositions regarding the role of the state, it is true that compared to the 'rolling back of the state' precept of the WC, some progress seems to have been made with the greater recognition of the importance of the state for the sound working of the economy in the PWC.[153] While the WC was built on a theoretical body of 'perfect markets', with a concomitant need for a retreat of the state, the innovations introduce a notion of 'imperfect markets', requiring more systematic intervention. The PWC further draws attention to non-market (non-state) ways of co-

[152] Joe Stiglitz was forced to resign from his position at the WB following his increasingly vociferous attacks on the IMF's handling of the financial crises of the late 1990s, in particular its high interest rate policy. He was joined by Ravi Kanbur who left his position of director of the 2000 WDR on poverty over disagreements on the implications for the poor of trade liberalisation, financial liberalisation and privatisation during the drafting of the report. See Wade (2002) for an elaborate account of these two resignations. See Fine and Van Waeyenberge (2006) on the legacy of Stiglitz at the Bank and beyond.

[153] On the relationship between the ideas of the PWC on the state and the long-established developmental state literature, see Fine (2006a).

ordinating economic/social activity arising out of optimising behaviour. As such, the economy becomes conceived of beyond the market.

The 'modern' theory of market failure, however, asserts that government interventions 'may not actually improve matters' (Stiglitz 1996, p. 156), and a set of specific ideas (on both market and non-market institutions) is put forward regarding the form intervention should take.[154] In essence, the role of the state remains confined to improving the institutional environment under which private agents (beyond the profit-seeking sector) steer their interaction in socially desirable directions, now in response to a broader spectrum of incentives than just prices, including voice (through decentralisation and participation) and social capital (through collective action). The abiding legacy of the new political economy, with its normative presumptions regarding the public sector, implies a persistent (underlying) bias against direct management of economic resources by the state – the market (or now the non-market non-state) remains superior. In addition, the benefits ascribed to the broader set of incentive mechanisms (beyond prices) that are to steer optimisation in both market and non-market contexts remain ill-examined. Even in comparison with the pre-WC McNamara era, the PWC appears as a 'regression' contrasting with the former's tolerance (and support) for state-controlled development enterprises (Fine 2001b, p. 15). As such, although under the PWC the antagonism of the WC between state and market has given way to a preference for some kind of 'synergism', Fine (2001b, p. 14) reminds us again that:

> the relationship between market and state, or between market and non-market, should not be taken as an analytical starting point. Rather, the relationship between state and market, as well as their respective roles and interactions, is the consequence of underlying economic and political realities that condition and are, in turn, conditioned by socio-economic structures. These need to be identified both theoretically and in specific country or other contexts, and are not reducible to the optimising behaviour attached to market, state and informational imperfections.

3.5 Conclusion

What has been referred to as the PWC seeks to provide an underlying formal foundation to a vastly expanded development agenda. It does so by re-establishing

[154] A hesitant admission of the potential success of certain elements of industrial policy was made in the 1997 WDR, to be qualified immediately in terms of excessive institutional requirements, rarely present in developing country contexts (WB 1997c, chapter 4).

the need for the recognition of development as a distinct phenomenon in economic analysis, and through claiming a capacity to account for social phenomena beyond the traditionally economic. It sits apart from its predecessor, the WC, through its emphasis on dimensions of development beyond stabilisation and prices. Nevertheless, it perpetuates the inadequacies of the underlying method, being rooted in mainstream economics with well-known inadequacies to conceptualise social or economic realities. The social comes about as a result of optimisation exercises under a set of constraints, and the analytical focus remains confined to the realm of exchange. Development, with its complex and uneven processes of social and economic structural change through technological progress, general productivity growth, industrialisation, urbanisation, the spread of markets and the various conflicts and struggles these engender, is ill-served by such an analytical prism. The legacy of the new political economy, further, implies a persistent prejudice against the state, with the role of government mainly understood as a way to enhance market efficiency.

While failing to provide clearer insights in the dynamics of development, both economic and beyond, the PWC does, however, serve to bestow a sense of legitimacy to the set of donor practices described in chapters one and two. Furthermore, chapter six illustrates how attempts to contain the contradictions emerging from the conjunction of the discursive shifts, as through the CDF and PWC, and the persistence, at the core of Bank practices, of WC financial and economic imperatives (including privatisation and trade and financial openness), could possibly account for a shift in the manner in which these imperatives are pursued, with a particular role for the Bank's knowledge exercise. First, however, we examine, in the next two chapters, the analytical propositions that have accompanied the changing perception of the purpose of aid, against the backdrop of the changes in the understanding of development documented here.

Chapter 4. The old economics of aid

4.1 Introduction

The current chapter surveys the literature on aid and conditionality preceding the selectivity proposition. It explores what we refer to as the old economics of aid, anchored in the old theories of growth, orthodox GE theory, and game-theoretic accounts of the donor-recipient relationship. It is structured in two parts: around those propositions that have sought to examine whether aid flows increase the resources available to the economy and whether these were used for the purposes intended (fungibility); and those propositions that have been concerned with the capacity of aid to alter the domestic policy processes in recipient or debtor economies (conditionality).

The chapter exposes how the literature on fungibility has been constrained by deficient accounts of economic mechanisms, an inadequate understanding of what aid is, and a futile attempt to overcome these shortcomings by recourse to econometric 'proof'. The overall conclusions of this literature remain ambiguous, with particular assertions easily countered by manipulation of models or data. A resultant sense of agnosticism about aid and the macro-economy prevails after four decades of research. Assessments of the effectiveness of conditionality have been additionally hampered by an incentive-based rational choice approach (game theory) and a failure to appreciate the qualitative importance of the conditionality exercise beyond quantitative assessments of compliance, which often project relatively low levels of donor influence over recipient/debtor policy formation processes.

Generally, the old economics of aid is characterised by a persistent incapacity to take the specific and defining features of aid, conditionality and development in particular country settings into account. Little consideration is given to the reality that the causes and outcomes of aid are complex, uncertain and vary across different donor-recipient situations, rendering a general theory essentially inappropriate. In this context, the extent to which the various dimensions and institutions of aid have managed to restructure the recipient/debtor economies has easily been downplayed and the role of aid in the broader political-economic-financial setting misunderstood. These shortcomings have been aggravated with the emergence of the recent propositions of selectivity and knowledge as aid, as we demonstrate in chapter five.

We recognise a strong ideological dimension to these shortcomings. This touches on the analytical habit of mainstream economics to consider what is perceived to be the politics of aid – touching upon who gives aid, why and to whom

– as distinct from the economics of aid. It can alternatively be gauged through the lens of what Samoff (1992) refers to as the financial-intellectual complex, where the conjunction of development assistance and research conditions the scope and nature of the research effort, both directly through funding the research and indirectly through setting the terms of the debate. In the context of the research on aid, which according to Doucougliagos and Paldam (2006, p. 12) depends financially for more than a third on aid budgets, this has implied a restricted conceptualisation of what constitutes the analytical realm, being predicated on a common acceptance of the donor-projected purposes of aid to the neglect of the broader international political, economic and financial context within which aid phenomena take form.

This chapter first illustrates how the shortcomings of one of the early contributions to the macro aid effectiveness literature, the two-gap model (Chenery and Strout 1966), were tentatively remedied through successive attempts at bringing more explanatory variables into the analysis of the macroeconomic effects of aid. Departing from the latter, various fungibility theories evolved trying, on the one hand, to endogenise a set of additional variables over and above imports or investment, which had constituted the only endogenous variables in the two-gap model and, on the other, to improve the portrayal of the economic relationship between aid and growth. In the context of aid and the savings gap, the distinct effect of aid on domestic savings (aggregate and public) receives specific attention. In the context of aid and the trade gap, the fungibility literature concentrates on the relationship between aid and export performance in a variation on the Dutch disease proposition.

It is documented, however, how these various alternative propositions remain characterised by: a lack of specification of economic mechanisms (the savings debate); normative presumptions regarding the behaviour of government (the fiscal response literature); inadequate understanding of the constraints on growth (HD growth theory); and erroneous presumptions embedded in a GE framework (the Dutch disease idea). These shortcomings are exacerbated by a persistent attempt to provide econometric 'resolution' of theoretically weak arguments, itself characterised by manifold flaws.

The chapter moves on to discuss the way in which the conditionality relationship was also brought into the analysis. We focus on the principal analytical contributions that have inspired a game-theoretic understanding of the conditionality relationship and consider how these have been filled in by a host of presumptions regarding the understanding of each player's objective function. A persistent failure to appreciate the structural features underlying both the conditionality relationship and domestic policy processes is revealed, mainly as a result of the straightjacket of rational choice frameworks being forced onto a vastly extended area of applicability, and attention is drawn to qualitative aspects of the creditor-debtor relationship not captured by a focus on the formal conditionality relationship.

4.2 Fungibility

4.2.1 The two-gap model

The contributions to the fungibility literature can be understood as anchored onto one of the early models of aid effectiveness, the two-gap model. Extending the analysis proposed by Rosenstein-Rodan (1961), the two-gap model asserts that the target rate of investment, necessary to achieve a target rate of growth, is constrained by limited domestic savings capacity and/or by a limited import capacity. The former is a corollary of low levels of development (the 'savings gap'). The latter emerges when there is limited substitutability between domestically and foreign produced capital goods (i.e. fixed import requirements in production), and the opportunities for rapid export growth are restricted (the 'trade gap').[155]

Aid fills the larger of the two gaps. *Ex post*, both gaps are equal and 'filled by aid' with the nature of the impact of aid depending on the particular regime faced by the economy (i.e. which constraint is binding). Four possible regimes are discerned. These depend first, on whether growth is constrained by an absorptive capacity constraint on investment (e.g. a limited supply of skills or organisational elements – referred to by Chenery and Strout (1966) as a 'skill limit'), or by the level of investment necessary for the target rate of growth; and, secondly, on which of the gaps is larger (the 'trade' or 'savings' gap).

Irrespective of whether investment is limited by absorptive capacity, or set by the target rate of growth, aid will be more productive under a 'trade' constraint than when the savings gap is binding. A binding trade gap leads to domestic resources that remain unused so long as the required complementary (imported) inputs are

[155] Cassen and Nissanke (1991) point out that if one seeks to capture a constraint on import capacity, the latter represents a foreign exchange constraint rather than a trade constraint, a distinction that acquires significance in the context of foreign exchange 'leakages' through e.g. debt service payments or capital flight.

unavailable. Relaxation of the gap then both contributes imported inputs and brings domestic resources into production (Chenery and Strout 1966).[156]

Thus, in the two-gap model, aid causes at least a one-for-one increment in investment, producing a target rate of growth in accordance with a HD understanding, in which capital acts as the predominant constraint. The provision of foreign exchange through foreign capital inflows (aid) closes the gaps, allowing investment to materialise. No other constraints interfere with this mechanism.

A large body of empirical work emerged to test for the positive relationship between aid and growth as projected by this model. This often implied the estimation of a single equation linear relationship with growth as the dependent and aid as one among a set of independent variables (income per capita, population, savings, foreign investment, other inflows, tax ratio, government spending, openness, financial repression, exports, export growth, etc.).[157] Such estimations of the aid-growth relationship are, however, prone to each of the following econometric problems.

First, many factors affect growth and to the extent that aid is correlated with any of these omitted variables, the equation will be subject to specification error and the aid coefficient therefore biased. Snyder (1993) demonstrates how estimates of the impact of aid on growth are highly sensitive to the specification of the equation. He regresses growth on domestic saving, aid, other foreign capital inflows, export growth and GDP (representing country size) for a sample of developing countries, using OLS. He finds that when country size is excluded the coefficient on aid turns small and statistically insignificant, whereas when the variable is included the aid coefficient becomes positive and significant. Another variable often omitted and likely to be correlated with aid is military expenditure.

Secondly, there will be multicollinearity if aid flows are related to other variables on the right hand side of the equation (e.g. exports). Thirdly, single equation estimation is inappropriate if any of the regressors form part of a simultaneous system with either aid or the dependent variable. Endogeneity of aid, for example, is likely when aid is allocated to those countries that have a worse growth performance. Fourthly, aid may contribute to growth, but the extent to which it does so, and the period over which this happens, are likely to be different for

[156] It can be noted how, in this account, aid is presumed to be demand-determined and not supply-constrained. The model does not allow for any adjustments necessary in the wake of a resource inflow that is lower than is required. In the context of aid flows being supply-constrained rather than demand-determined, adjustments will be necessary, with the growth rate being the endogenous adjustment variable (Cassen and Nissanke 1991).

[157] For a comprehensive review of this empirical literature, see Hansen and Tarp (2000).

different types of aid and depend on the sectors to which aid is allocated. With the channels through which aid affects growth likely to vary as the composition of aid changes across sector and across time, the impact of aid on growth cannot be expected to be constant either across time or across countries (the instability of the aid coefficient). Fifthly, few studies take into account that lags may characterise the aid-growth relationship. Sixthly, a lot of these studies are based on time-series prior to the habitual testing for stationarity. Finally, econometric assessments of aid face difficulties of how to measure aid adequately (see Riddell 1987, p. 109; Renard and Cassimon 2001). These various problems render inference on the basis of these aid-growth regressions precarious, to the extent that White and Luttik (1994, p. 29) conclude that no reliance can be put on any of these results.

4.2.2 Endogenising savings

The savings debate emerged in a first attempt to broaden the scope of the two-gap model.[158] It focuses on the repercussions of an aid inflow for the level of savings in the recipient economy. In the two-gap model, the aid inflow simply supplements domestic savings and allows the targeted level of investment to be attained. But the savings debate examines whether aid (or foreign finance in general) could displace domestic savings, potentially widening the initial gap and lowering the actual level of national investment.

Griffin (1970) argues it is reasonable to assume that consumption is a positive function of total available resources (domestic income plus aid) and infers that some aid will be used to increase consumption. As a result, a different chain of events occurs: the aid inflow no longer produces a one-to-one increment in total savings (domestic savings fall in response to the aid flow); investment rises by less than the value of aid; and a lower than targeted rate of growth materialises (in HD fashion). Apart from the short-run effect of aid on domestic savings, there is, equally, a long-run concern. For if aid reduces domestic savings in the long run, one of the conditions for the achievement of graduation from aid is violated and foreign aid could engender aid dependency.

In a more radical vein, aid displaces domestic savings and no increase in investment is associated with the aid inflow (Griffin and Enos 1970). This proposition combines with an assertion regarding the effect of aid on the capital-

[158] For an elaborate categorisation of the various fungibility theories with reference to a national accounting framework, see White (1998).

output ratio, where it is suggested that aid causes the incremental capital output ratio (ICOR) to increase, further undermining its beneficial impact on growth (Griffin 1970). Such a positive relationship between aid and the ICOR is attributed to the monumental character of aid-financed investment (as donors strive for visibility) or a general (aid) bias against directly productive activities undertaken by government which produces a pattern of investment in favour of social overhead capital and economic infrastructure.

While these contributions clearly seek to endogenise additional variables (the savings rate and the ICOR), their specification of economic mechanisms remains inadequate: multiplier effects are ignored (Eshag 1971); no insights are provided in the way national expenditure patterns are formed and possibly change in the wake of an aid inflow (White 1992a; and below); and commitment to a HD framework imposes undue restrictions on the understanding of growth.

Nevertheless, the debate was propelled forward along econometric lines (see Rahman 1968; Gupta 1970; Weisskopf 1972; Papanek 1972; Gupta 1975; Gupta and Islam 1983; Singh 1985; Snyder 1990). These exercises are often characterised by the shortcomings previously pointed out. First, the regression equations are often mis-specified (Papanek 1972). Secondly, the aid coefficient is likely to be unstable (both in cross-section and time-series analysis). Thirdly, time-series analysis is likely to suffer from non-stationarity. Fourthly, a single-equation regression of aid on savings may be prone to simultaneity bias, stemming from the possible endogeneity of aid (Stewart 1971).[159] Fifthly, problems arise from the measurement of aid and the aggregation of various forms of aid (and in the early contributions to the savings debate of aid and non-aid flows) (see White 1992a). Finally, no clear-cut conclusion emerges from these various studies regarding the aid-savings relationship, and Cassen (1989, p. 5 quoted in Cassen and Nissanke 1991, p. 14) observes that:

> the factual evidence from multi-country studies (on aid and savings) is inconclusive. Studies of individual countries suggest that there is not necessarily a negative connection between aid and savings.

Alternative 'fungibility' propositions evolved out of the savings debate. One trend shifts the focus from national to public savings. This tries to incorporate information regarding the formation of government expenditure patterns – as a major aid recipient – and analyses how aid might interact with these (the fiscal response literature). Another trend considers the implications of the spending effect generated

[159] See White (1992a, pp. 186-8) for more on the problem of simultaneity in the savings literature.

by aid through changes in relative prices, and examines the resultant re-allocation of resources across sectors (in particular the tradable versus non-tradable sector), abandoning a growth perspective in favour of a GE framework (the Dutch disease literature). Further, in the context of new developments in growth theory, the link between aid and growth is recast (see chapter five). And as policy-based lending became increasingly important, the debate became preoccupied with issues of agency and policy reform in the context of conditionality.

4.2.3 From national to public savings

Shifting the analysis to government fiscal behaviour, Heller (1975) proposes a model in which recipient governments maximise a utility function comprising five choice variables: government investment; government expenditure on socio-economic (developmental) and other civil (non-developmental) purposes; taxation; and borrowing from the local capital market. Maximisation is subject to a budget constraint according to which governments do not finance recurrent expenditure out of borrowing (dual budget constraint). Seeking to make inference regarding the interactions among various categories of public expenditure and domestic and foreign revenue, Heller (1975) tests his model for a set of eleven African countries. His findings suggest that aid increases investment but simultaneously facilitates a reduction in the level of domestic taxes and borrowing. Hence total expenditure does not increase by the full amount of aid. However, the magnitude of these effects and the precise response of public consumption to aid vary according to the financial terms of aid. Grants have a stronger pro-consumption bias, whereas loans are more pro-investment (Heller 1975, p. 430).[160]

The specific building blocks of Heller-type models have been subject to criticism.[161] Again, the lack of consideration of economic mechanisms stands out, and White (1993) demonstrates how supplementing the Heller-specification of government behaviour with a simple Keynesian macroeconomic model allows a scenario to be generated in which aid increases current income as well as potentially, through feedback effects, taxes, thereby producing an increase in government expenditure in excess of the value of the aid inflow. The impact of aid on these variables (income, taxes, government expenditure) is shown to depend crucially on

[160] Grant aid was, however, often initially intended to be used for government consumption. This literature, further, fails to acknowledge that expenditures traditionally categorised as government consumption such as teacher salaries are a form of investment.

[161] For a critique of the specification of the government utility function, see Binh and McGillivray (1993). For a critique of the use of a dual budget constraint, see White (1994).

the relationship between aid and private investment. If aid crowds out private investment, the possibility that aid reduces taxes, and possibly national income, increases (White 1993, p. 311).[162] Thus, in a static macroeconomic framework aid can, through the aid multiplier, increase current income and a fall in taxes need not happen even in the period of the aid inflow.

Following Heller (1975), the literature on government fiscal behaviour developed along two main lines.[163] One strand focused on issues of categorical fungibility, investigating the extent to which aid is used for (sectoral) purposes other than those for which it is intended (Cashel-Craig and Cordo 1990; Pack and Pack 1990, 1993; Khilji and Zampelli 1991; Khilji and Zampelli 1994; Feyziogly et al. 1998; Devarajan et al. 1999; Swaroop et al. 2000). A common problem across these studies is the (frequent) implicit assumption that government consumption retards growth. The evidence is, however, at most mixed, and for LICs tends to confirm a positive effect of government consumption spending on growth (see Devarajan et al. 1996). Furthermore, these studies do not deal with the more comprehensive issue of 'fiscal response', as they fail to incorporate – in the tradition of Heller's original model – that governments are concerned with *both* expenditure and revenue.

Other contributions attempted to project a more comprehensive approach aiming to model the response to aid of full public sector fiscal behaviour. They seek to analyse simultaneously interactions between aid, taxation and expenditure decisions (Mosley et al. 1987; Gang and Khan 1991; Khan and Hoshino 1992; Iqbal 1997). Recently, attempts have been also made to endogenise aid in the public sector response analysis (Franco-Rodriguez et al. 1998). Making aid endogenous does not require that recipients have control over the aid they are allocated by donors. Instead it requires that they have effective control over the amount that is actually spent. Endogenous treatment of aid hence tries to incorporate the notion that, while aid commitments might be supply-determined, the actual aid disbursements are influenced by recipient behaviour (McGillivray and Morrissey 2001, p. 23).

Most of the debate regarding fiscal response to aid has again been conducted in empirical terms and has often suffered similar flaws as identified in the context of

[162] It could be noted that White (1993) incorporates a crucial mis-formulation of the aid recipient economy as he builds on a definition of national income that corresponds to the description of a closed economy ($Y = C + I + G$), with an aid-receiving economy obviously not 'closed'. This was recognised in White (1998). The possibility of such a flaw in theorising the impact of aid, where the representation of the aid recipient economy is gravely incongruous with the reality of aid receipt, is noteworthy (see further below).

[163] See McGillivray and Morrissey (2001) for a comprehensive review.

the savings debate (see McGillivray and Morrissey 2001). Once more, the literature tends to be inconclusive. A few general observations, however, transpire (McGillivray and Morrissey 2001). In general, aid tends to increase total spending by more than its amount, but this does not necessarily imply that aid increases the expenditure categories towards which it was targeted by its (full) amount. However, even if aid stimulates expenditures not targeted by donors, these may still be growth enhancing. Additionally, aid seems to have significant effects on tax effort and borrowing, though the direction of this impact differs across countries. Furthermore, there may be inconsistencies between assessments of aid effectiveness on the basis of fiscal response versus those based on conditionality compliance. Typically, programme aid will be conditional on a trade liberalisation exercise with potentially adverse implications for tax revenue (tariff reductions). This contradiction is rarely recognised in the literature.

The 'fiscal response' literature attempted to provide an improvement over the savings debate by incorporating information regarding changes in government budget behaviour in response to aid. The particular specification of government behaviour in these models reveals a presumption of government as a planning entity. Utility of the planner government is maximised when a set of target values is reached, where the latter are defined in terms of development achievements (target rate of investment, target rate of taxation; target rate of socio-economic expenditures; and target borrowing rate). Clearly, with the increasing popularity of public choice ideas regarding driving motives of government behaviour, such a 'naïve' representation of the government objective function was bound to come under assault and a set of models developed aiming to integrate the analyses of aid and public choice.

Landau (1990) provides one of the first such contributions. He asserts, following a public choice perspective, that public sector decision makers will act in the general interest only if the constraints and incentives on their behaviour render serving the general interest equally in their own interest (p. 559). More specifically, it is assumed that government officials have two major objectives: staying in power, and securing maximum possible income consistent with staying in power. Staying in power involves getting and strengthening support from voters and/or the military (varying across countries). Potential supporters of the government are divided into two groups: the general public versus receivers of transfers or government-created rents (including private individuals, firms, elected government officials and bureaucrats). Government actions are categorised as follows: those that enhance general welfare, including the promotion of growth, versus those that produce transfers or create rents for blocks of supporters or members of the government. The government faces a variety of constraints, such as those relating to revenue and/or administrative capabilities, and these constraints imply an opportunity cost for government activities of either type. The benefits to the government from either type of activity, furthermore, decline when any activity is further engaged in, and the government expends resources on each of the two activities until marginal net benefits are equalised. The provision of aid then changes the equilibrium level of the mix of the two activities and, under the assumption that donors fund activities that increase welfare, the marginal political benefit to the government from (self-enacted) activities enhancing general welfare is reduced. In the wake of an aid inflow, the government thus reallocates its resources in favour of rent-creating activities. This description of government behaviour is combined with the assumption that government activities producing rents slow down economic growth, hence reducing aid's intended growth effect.

Svensson (1998) develops a similar argument, embedding it in a game-theoretic framework. In his model, social groups compete over common-pool resources. The common resources can be either invested in public goods, or be appropriated for private consumption. The latter can happen either by means of direct appropriation (through the seizure of power) or by the manipulation of bureaucrats and politicians to implement favourable transfers, regulation, or other distribution policies. The author shows that an increase in government revenues can lower the provision of public goods. This seems to provide an explanation for why large disbursements of aid do not necessarily lead to increased welfare. The author's model also suggests that the mere expectation of aid may increase rent dissipation and reduce the expected number of periods in which efficient policies can be sustained. The empirical prediction of the model is that discretionary aid (as other windfalls) in countries with divided policy control will on average be associated with higher rent-seeking activities. This is tested on the basis of a simultaneous equation system, for a sample of 66 countries (three 5-year observations since 1980), confirming the prediction that aid is associated with higher corruption ('rent-seeking') in countries suffering from a divided policy process (as proxied by a measure of ethnic and linguistic fractionalisation).[164]

Conceptually, Heller-type and public choice models of aid impact suffer from a shared shortcoming even if that manifests itself in an almost directly opposite way. Both base their description of government behaviour on a normative presumption regarding government and rent-seeking groups, while a more successful attempt to account for the outcomes of government behaviour in response to an aid flow ought to start from the particular politico-economic circumstances within which that behaviour takes place.[165] The way in which aid possibly creates opportunities for rent-seeking and the spectrum of outcomes associated with such a process need to be investigated rather than presumed.[166] And the same applies to those giving aid (see below).

4.2.4 Aid impact as Dutch disease

In as far as the above understandings of aid impact are anchored in HD theory, they suffer from its inadequacies for the understanding of growth, pointed out in chapter three. Seeking to move beyond these, the analysis of aid shifted towards a GE framework.[167] This focuses on issues that arise in the context of the assumption in the original two-gap model regarding the relationship between aid and the trade gap.

As soon as the two-gap model of aid impact had appeared, attention had been drawn to its particular and, for some, excessively restrictive assumptions regarding the recipient economy. In the two-gap model, the possibility for import substitution is eliminated by the assumption of technologically fixed import coefficients; the expansion of export restricted through the assumption of an exogenously given maximum export revenue; and a constant capital output ratio eliminates substitution in the production process (Joshi 1970; Findlay 1973). Further, the model is

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164 Adam and O'Connell (1999) use a similar framework.

165 For a concise critique of the various normative presumptions that have steered analysis of government behaviour, see Chang (1996).

166 For a political economy approach to rent-seeking in which differences in political, economic and organisational abilities and powers of various groups explain different types of rent capture with varying economic and social implications, see Khan and Jomo (2000). See also Amsden (1989) on how South Korea's chaebols arose out of the rent-seeking and business opportunities surrounding American foreign aid allocation in the 1950s.

167 Bhaduri and Skarstein (1996) put forward another, more singular, attempt to move away from the constraints imposed by a HD understanding of growth. They propose a model in which the implications of aid for the *level* of effective demand can be explored. This contrasts with the preoccupation in Dutch disease analysis, anchored in a GE framework, with the impact of aid on the *composition* of aggregate demand.

embedded in a single sector growth framework, precluding inspection of intersectoral issues and relative prices (Findlay 1973).

Although these issues were raised in the early 1970s, it was not until the 1980s, in line with the increased emphasis on prices in development theory more broadly, for the focus on relative prices to be further explored in the context of aid. A Dutch disease analysis of aid impact was proposed, exploring, within a GE framework, the relationship between aid and exports through the implications of aid flows for the relative price of tradables to non-tradables (as measured by the real exchange rate).

The Dutch disease phenomenon is concerned with the detrimental implications for the non-boom (originally non-oil/gas) traded sector resultant upon a real exchange rate (RER) appreciation, the latter caused by a temporary boom in a foreign exchange earning ('boom') sector. The phenomenon is considered particularly harmful for development as the non-boom traded sector (traditionally manufacturing) is presumed to be characterised by faster technological progress than the non-traded sector (van Wijnbergen 1984). In the simplest static model, a resource boom (here aid) affects the economy in two ways. The first is the 'spending effect': higher domestic incomes as a result of the boom lead to extra expenditure on both traded and non-traded goods. The price of traded goods is determined by international market conditions and so does not rise despite the extra domestic spending; by contrast, the price of non-traded goods is set in the domestic market and does rise. The higher relative price of non-traded goods makes domestic production of traded goods less attractive, and so their output declines. A second effect emerges if, in addition, the booming sector shares domestic factors of production with other sectors, so that its expansion tends to bid up the prices of these factors. The resulting 'resource-movement effect' reinforces the tendencies towards appreciation of the RER (i.e. a rise in the relative price of non-traded goods) and a squeeze on the tradable goods sector, predictions which are common to most Dutch disease models (Neary and van Wijnbergen 1986).

In the current context, aid causes a 'spending effect', which leads to an appreciation of the RER and the ensuing reallocation of production away from tradables ('resource movement effect') (Michaely 1981). This change in the composition of output to the detriment of exports undermines the recipient's capacity to generate its own foreign exchange, and as such delays its graduation from aid. Younger (1992) proposes a Dutch disease argument for the Ghanaian economy, after it became a recipient of large amounts of aid following the SAPs it embarked upon after 1983.[168] White and Wignaraja (1992) illustrate how increased aid inflows to Sri Lanka during the 1980s prevented the authorities from producing the RER depreciation that was intended under the liberalisation programme of the late 1970s. Paus (1995) identifies Dutch disease driven by aid as one of the key obstacles to the development of a competitive and dynamic export sector in El Salvador. And Elbadawi (1999) argues that unsustainable aid flows caused substantial RER over-valuation, a problem perceived to be particularly severe in highly aid-dependent African countries.[169]

The Dutch disease analysis of aid abandons a growth perspective. Yet, even if for White (1992a) a GE framework is to be preferred over a deficient growth framework and notwithstanding the improvement of an analysis moving beyond an aggregate single-sector approach, the approach is plagued by problems. Cassen and Nissanke (1991, pp. 20-2) provide a concise overview. The authors point out the inadequacy, especially for the context of developing countries, of the (GE) assumptions of initial full employment equilibrium, the assumption of fixed labour supply, the 'law of one price', and of a free flow of traded goods and flexible prices. Within the model, the economies of developing countries could equally be characterised by points inside the production possibility frontier with substantial underemployment or disguised unemployment in both urban and rural areas (see also Nkusu 2004). If aid is used productively, the presence of unemployed resources would ensure a positive wealth effect as the immediate effect of the aid transfer, initiating a move from the underemployed equilibrium towards a point on the production possibility frontier (Cassen and Nissanke 1991, p. 20; see also UNCTAD 2000a, p. 182). Cassen and Nissanke (1991, p. 21) further note that:

> the finally attainable production mix at the full employment level, and a transition path to this level will be determined by structural characteristics of the economies and by the economic policies pursued in the transition period, including macroeconomic, trade, industry and pricing policies.

The 'disease' is by no means inevitable:

> intelligent execution of macro adjustment policies, coupled with effective management of international financial flows and exchange rates, can abate

[168] See also Opoku-Afari et al. (2004) more recently.
[169] See also chapter five on the recent revival of the Dutch disease argument in the context of aid.

> shocks associated with such events and attenuate market forces, thus limiting overshooting and Dutch Disease effects.

In a similar vein, Rattso and Torvik (1999) demonstrate how the occurrence of the Dutch disease as a result of aid inflows depends on the import policy regime of a country. The authors argue that when foreign aid is allocated to rationed import intermediaries, the economy experiences a supply induced boom with real depreciation and higher exports as otherwise idle capacity is brought into use (see also Adam 2005, p. 14). Allen (2005) points to RER depreciation for five countries (Mozambique, Uganda, Ethiopia, Ghana and Tanzania) for the period from 1999 to 2003 (see also Nyoni 1998; Sackey 2001). He asserts how such a depreciation in the face of surging aid inflows may indicate any of the following: first, structural features of the economy such as a rapid supply response to aid expenditures or high import propensities; secondly, a fiscal and monetary policy stance leaning against real appreciation; or, thirdly, other exogenous events, notably a negative terms of trade shock. In an overview of theoretical and empirical arguments on Dutch disease, Adam (2005, p. 6) observes that:

> once appropriate consideration is taken of the supply-side there is no presumption as to whether, over the medium term, aid inflows will be associated with an appreciation or depreciation of the RER, or, indeed, with an expansion or contraction in the tradable goods sector of the economy.

Adam fails to find a convincing case for the prevalence of Dutch disease in the literature and, in particular, argues that aid flows do not occur in isolation and that their impact is intimately linked to the fiscal response to aid (how revenue mobilisation, public expenditure and the overall fiscal stance respond to aid), as well as to monetary and exchange rate policy responses (p. 14). He notes how (p. 22):

> rather obviously, the actual evolution of the economy will depend crucially on the form of [aid-financed] public investment, how powerfully (and how quickly) it feeds back into private production capabilities, and the costs of any short-run contraction of the export sector. Importantly, though, export and growth may be benefited as much, if not more, by public investment geared towards improving the productivity of domestic non-tradable goods production rather than directly towards improving productivity in the export sector itself.

Finally, Torvik (2001) argues that when learning-by-doing externalities characterise the non-tradable sector, the long-run adverse impact on productivity growth (the Dutch disease) will be limited, even if the RER appreciates in the short term.

4.2.5 From the two-gap model to Dutch disease: to what effect?

In the two-gap model, domestic savings and/or foreign exchange act as the main constraints on investment and hence on growth. Provision of foreign exchange through aid allows to alleviate these constraints and for investment and growth to materialise. No other constraints interfere. The supply of resources implies their investment, and hence growth.

The two-gap model is typically characterised by three main failures in its attempt to model the dynamics of aid. First, the aid phenomenon is thoroughly misunderstood. The two-gap model was initially developed in the context of the search by USAID for a practical tool to calculate aid requirements. This set the debate on a particular analytical and ideological footing as the dynamics of aid were predominantly to be understood within the constraints of a (teleological) development paradigm. Aid was perceived as another set of resources, another 'factor of production' to add to the productive capacity of the economy (Chenery and Strout 1966, p. 679), without consideration for the international context within which its transfer took place beyond that defined by the projected purpose of the aid transfer.

Secondly, the conceptualisation of the economic interaction between aid and the recipient economy is flawed. A gap-model understanding of the effect of aid fails to provide insight into the economic mechanisms by which aid affects the economy. Aid acts upon the variables that are singled out in the model in a fully additive way (investment, imports, or government revenue). The possible interaction between aid and other variables in the economy (such as savings, public or private, exports, the ICOR) is not considered. With constant parameters, the structural features of the model are unaffected by the aid inflow: the economy is the same before and after the aid flow, apart from the incidence of a one-to-one increase in the particular variable targeted by the aid. This is compounded by a HD understanding of growth, the shortcomings of which were summarised in chapter three. Thirdly, estimations of the aid-growth relationship are prone to a host of econometric problems.

Stated differently, the shortcomings of the two-gap model can be understood as follows (following Fine 2006b, p. xx). Economic performance (or growth) without aid is complex; the impact of aid is complex; and, as a result, the interaction of both these phenomena will be at least as complex as either phenomenon. The two-gap model, however, implies an oversimplified (and inadequate) view of growth, of aid, and of their interaction at the conceptual, theoretical and empirical level. As a result, the model implies a theoretical and empirical reductionism, with a capacity, however, to tease out whatever results are wanted from the econometric exercises that seek to fill the analytical gaps, themselves consisting, at best, of ill-founded multiple regressions.

It was documented above how a set of alternative propositions regarding aid impact, which try to address some of these shortcomings, developed.[170] This proceeded mainly along two lines. The aid-import/investment relationship was recast through the endogenisation of additional variables: aid widens the original gap(s) – either the savings or trade gap – and the 'intended' aid-growth link fails to materialise. And attempts were made to reconsider the presumed link between the gaps and growth (beyond a HD framework). Along the former reasoning, the conceptualisation of constraints on the recipient economy and the concomitant role for aid as proposed by the two-gap model is accepted, while the exogeneity of particular macroeconomic variables to the aid flow and thus the presumed constraint-relieving effect of aid are contested. Along the latter line of argument, the conceptualisation of the growth process as embodied in the two-gap model is challenged. In that case, the asserted absence of an aid-growth relationship does not necessarily stem from a widening of the gaps aid was originally presumed to fill, but from an initial misconception of aid's potential contribution to growth (see also chapter five). In the conditionality literature reviewed below the focus shifts to issues of aid and policy reform.

As such, in an attempt to remedy the failures resulting from the over-simplistic approach to aid and growth embodied in the two-gap model, a set of additional variables, mechanisms, or institutions, are brought into the analysis. This proceeds, however, without challenging the underlying approach. As a result, the three fundamental failures of the original aid impact model identified above are perpetuated. A patchy understanding of what is aid persists; its interactions with the domestic economy remain misunderstood; and this combines with an erroneous

[170] We focused on landmark publications of the literature on macroeconomic effects of aid. More comprehensive reviews abound (see Cassen and Nissanke 1991; White 1992a, 1992b; Hjertholm et al. 2000; Thorbecke 2000).

commitment to econometric testing. We elaborate on each of these continuing failings.

First, aid remains misunderstood as a phenomenon. Much in line with the analytical habit of mainstream economics, what is perceived as the 'politics' of aid, touching upon the issues of who gives aid, why, how and in what form, often remains separate from the analysis of the 'economics' of aid, with a perception that incidence of the former has no repercussions for the understanding of the latter.[171] To the extent that there is a literature on the 'politics' of aid giving, it remains separate from the literature on the impact of aid (the 'economics' of aid) (see also McGillivray 2003b, p. 2).

The motives for aid beyond those projected by donors are rarely considered in the analysis of aid effectiveness (see also Petras and Veltmeyer 2002, p. 281). The prevalence of donor motives beyond recipient need (political, strategic, commercial), together with the politico-economic, commercial and financial relations between donor/lender and recipient/borrower beyond the aid relation – typically involving trade, debt, foreign investment, migration, military 'aid' – are easily ignored. These, nevertheless, have a significant effect in determining the impact of aid (in terms of access to aid, the form aid takes, the continuity of aid flows, command over the aid flows).[172]

Such an analysis, ignorant of essential features of the aid phenomenon falls prone to a particular fetishism, where certain outcomes are attributed to the aid resources (or the aid-imposed policy reforms) rather than to the particular relationships (both international and domestic) within which these resources (or reforms) are located. This 'fetishism' is tainted by the recurrent failure to distinguish between stated and actual objectives of aid, and the attendant asymmetric normative presumptions regarding intentions of donors versus those of recipients (see White 1974; Riddell 1996b, p. 26). Success (i.e. a positive relationship between aid and the projected objectives) is then often accounted for in terms of the 'inherent' characteristics of the aid flow, while failure raises the spectre of 'local dynamics' and of the latter's possible 'interference' with aid's 'inherently good' features ('recipient bad behaviour'). The premise of a benevolent donor versus a corrupt or rent-seeking recipient/debtor government prevails and combines with an assumption of full

[171] See White (1974) for an early and comprehensive critique of this artificial separation in the conceptualisation of aid effectiveness.
[172] The flaw in White (1993) pointed out above, where an analysis of aid impact is modelled in a closed economy manner, is a good example of the way in which the analysis of aid impact has managed to abstract away from the defining features of the aid phenomenon.

control by the latter over aid funds. Recipient behaviour that diverges from donor intentions ('fungibility') is perceived as detrimental to development. McGillivray and Morrissey (2000, p. 419) object, affirming that:

> There is nothing inherently wrong or inappropriate about fungibility; all it indicates is that donors and recipients have differing views about how expenditures should be allocated.

As an analytical void is thus filled with a normative bias, with the notion of aid (and its conditions) as inherently 'good' for development permeating much of the mainstream aid literature, the features of aid that possibly undermine its projected beneficial effect and that originate in the systems and institutions of aid are easily ignored. These include the fact that aid is part of the debt-system, that aid is the product of a fragmented and uncoordinated set of donors with their own interests, or that there are negative externalities to aid caused by brain drain or tied aid practices (see Doriye and Wuyts 1992; Wuyts 1994, 1996; UNCTAD 2000a; see also chapter five).

Secondly, throughout this literature, there is a persistent failure to examine how certain constraints on growth/development come about and may interact with aid.[173] Most generally this reflects the limited consideration of the particular domestic and international socio-economic-political relations within which aid is located, and an associated failure to recognise diversity of conditions across recipient economies. In this vein, Stoneman (1975) argues that mainstream theory fails to distinguish between a payments effect (the direct balance of payments effect on national income enabling higher investment and/or consumption) and a structural effect (differential stimulus to various sectors, export promotion, change in the ICOR, change in income distribution) resulting from FDI, as it fails to take account of economic relations (past and present) that cause certain development outcomes, condition the form these take, and affect the outcomes associated with foreign capital inflows (see also Kalecki 1976, chapter 5). To the extent that aid analysis is anchored in mainstream accounts of growth, it will fail to appreciate the underlying processes

[173] See Joshi (1970) for an early critique of how mainstream aid analysis fails to capture dynamics around aid through its failure to explore how certain constraints may have arisen and possibly interfere with intended aid outcomes. Joshi argues how a saving constraint may have its origins in the unwillingness of certain social groups to finance investment – a structural constraint which will not be relieved by aid inflows and that might prevent the surplus imports that aid generates to be allocated to the designated investment sectors causing it instead to be dissipated in additional consumption of, for instance, luxury goods.

(domestic and international) associated with accumulation, and the way the resources, policies and institutions attached to aid interact with these.

Thirdly, the literature reviewed above attempts to remedy its conceptual and theoretical shortcomings by recourse to excessive econometrics. A specific conclusion regarding aid effectiveness is easily countered by the manipulation of models and data, and the respective sides of the debate are reproduced under the various formats new trends in mainstream theory and econometric practice seek to promote. For Rajan and Subramanian (2005, p. 5):

> The literature has sometimes followed a cycle in which one paper finds a result, and is followed by another paper with a twist, either overturning or qualifying the previous result, followed by another and so on. This has had some undesirable effect on policy with advocates selectively using results to bolster their preferred view on aid.

Thus, certain biases exist within the original (two-gap) framework, but removing these or introducing additional variables does not correct the underlying problems. All along, the underlying realities steering the actual aid relationship, which were ignored ab initio, remain concealed and ill-understood in ad hoc attempts to bring enhanced explanatory power to an approach that, in its initial understanding as to what aid and development are, has abstracted away from the defining features of the phenomena.

In general, then, the old economics of aid presumes a set of conditions which aid is set out to influence, with ideas about constraints in the recipient/debtor economy nurtured not by a thorough investigation of the state of the recipient/debtor economy or the relationship between the donor/creditor and recipient/debtor, but by a specific fashionable paradigm, normative presumptions regarding aid, and varying institutional imperatives (see also Riddell 1996b; Thorbecke 2000; Pronk 2001). The features of the recipient economy are modelled exogenously, except for those related to the constraint aid is supposed to affect. This produces a fragmentary aid impact analysis which falls short of examining how linkages, feedback effects and new constraints emerge in the context of aid, and which is characterised by general propositions that do not easily accommodate the fact that the causes and outcomes of aid are complex, uncertain and vary across different donor-recipient situations. In-depth qualitative studies of the longer-term development process in each country including all relevant factors and their mutual relationships, have better prospects of providing insights in the dynamics of aid than attempts to find a measurable effect of an isolated factor such as aid (see Pronk 2001, p. 615).

In this light, it should come as no surprise that the old aid economics has been incapable of providing conclusive arguments regarding the relationship between aid and key macroeconomic indicators. The sense of agnosticism has been candidly conceded by main contributors to the debate. White (1992a), for instance, concludes his review of the literature by stating that 'we know surprisingly little about aid's macroeconomic impact'. Lele and Nabi (1991, p. 4) acknowledge how the literature on aid effectiveness:

> failed to provide either a systematic evaluation of the specific conditions in which aid has worked or failed, or a synthesis of the lessons of past experience for future donor and recipient policies with regard to development aid.

And Carlsson et al. (1994, p. 1) observe that:

> although there seems to be a serious interest in knowing the effects of aid … the knowledge we have on the economic impact of aid is at best ambiguous, or, more commonly, non-existent.

The next section illustrates how these failures of the aid effectiveness literature persist as the analysis shifts to focus on issues of conditionality and policy reform.

4.3 Conditionality

As indicated in the chapters above, the 1980s saw a shift in the relative importance of the various aid instruments. Whereas traditionally project aid had constituted the bulk of aid disbursements, policy-based or programme lending now saw its share in aid allocations increase significantly. Chapter three highlighted how the relative shift towards policy-based lending was associated with the elaboration of a new discourse on development. While the era of project lending had been characterised by a recognition of the importance of the role of the state in development, as a result of which, by the late 1970s, government-owned development finance companies and state-owned industrial enterprises had become important beneficiaries of WB lending (WB 1980, p. 6), the conditions set by the WB and IMF now sought to eliminate what were swiftly perceived to be various obstacles to a 'perfect market' identified as originating in state intervention.

Chapter three also exposed the analytical shortcomings of the WC and documented the persistent negative empirical findings of stabilisation and structural adjustment. All in all, the growth and poverty reduction performance under the structural adjustment or stabilisation regimes had been very poor. Per capita income in SSA at the end of the 1990s was 10 percent lower than in the 1980s, and the gap was even larger when compared to the level of per capita income of three decades earlier (see UNCTAD 1998; Mkandawire and Soludo 1999; UNCTAD 2001). In addition, the performance of the Bank's portfolio had worsened, with the percentage of satisfactory adjustment lending operations in the Bank's own evaluations reaching a low of 60 percent during the 1980s.[174]

Still, the IFIs were not willing to admit to fundamental failures of their programmes as catalysts for growth and poverty reduction. On the contrary, after more than 15 years of experience with adjustment lending and much debate, a consensus emerged within the institutions that adjustment (and stabilisation) had promoted sound policies, but had produced weak results in terms of growth and reduction of poverty. The IFIs turned their own failure into the failure of clients, with 'failures to adjust' rather than 'failures of adjustment' dominating their understanding of the economic performance of clients. It was added that if adjustment or stabilisation produced weak results in terms of growth and poverty reduction, this was due to a lack of selectivity in lending and a poor design of operations with insufficient attention to borrower ownership of policy reform (WB 1994a, 1997a, 1998b). An update report on adjustment lending in SSA (WB 1997a, p. 5) argued that:

> Increased selectivity is required, to stop financing delays in the adoption of needed reforms. The poor results from the past show that lack of selectivity resulted in financing too many cases of low growth and increased indebtedness. This was an unanticipated effect of excessive willingness to support weak programs and/or reluctant reformers.

The assertions of the 1994 WB Report *Adjustment in Africa* (WB 1994a), which held that adjustment policies had positive effects on growth and more rather than less adjustment was necessary, acquired common currency.[175] 'Adjustment' was

[174] This improved slightly to 68 percent for the first half of the 1990s (FY90-94).
[175] This happened despite extensive criticism of: the method used to classify the 'adjusting' countries (Mosley, Subasat and Weeks 1995) in WB (1994a); the sensitivity of the results to certain observations (White and Luttik 1994, p. 19); the inconsistency of the results with other findings (Hadjimichael et al. 1994); and the reduced understanding of adjustment projected in the WB (1994a), which was more akin to stabilisation (demand deflation) than supply stimulation (Mosley, Subasat and

now an essential step to getting SSA on a poverty-reducing growth path, and while there had been some progress, government still had a long way to go (p. 219). This included accelerating their commitment to macro-economic reforms, completing trade and agricultural sector reforms, restructuring public finances, and providing an environment conducive to private production and the provision of goods and services. In response to the question 'Is adjustment paying off in SSA?', the Report declared (p. 131):

> The answer is a qualified yes. Adjustment programs may not have raised all countries' GDP growth, exports, savings, and investment ratios to those of adjusting countries in other regions. But the stronger reformers in Africa have turned around the decline in economic performance and are growing for the first time in many years.

WB (1994a) further explored the notion of 'ownership' for programme success. The ownership concept had been initially put forward in the context of the Bank's evaluations of adjustment lending (WB 1990a, 1992) and was elaborated upon by Johnson and Wasty (1993) in a WB discussion paper. Increasing the way in which government-Bank interaction affects borrower 'ownership' was to become the new challenge for the Bank (and the broader donor community), with ownership understood as domestic support for the IFI-promoted reform programme.

Rather than questioning the general presumptions regarding market efficiency contained in its programmes, or reflecting upon the somewhat restricted nature of the presumed 'growth' benefits associated with free market interaction, the advocates of adjustment and stabilisation programmes thus shifted the analysis towards mechanisms of implementation. This was supported by a growing literature on the 'political economy' of reform in developing countries. Concerns with the effectiveness of the advocated policies were now a 'distraction' from the debate which was no longer about whether countries ought to adjust but, following Abbott (1994, p. 23 quoted in Mkandawire and Soludo 2003, p. 32), about 'operational details such as design, implementation, monitoring procedures and the pace and sequencing of reforms'.

4.3.1 The analytics of conditionality and policy reform

Against the background of these developments, the analytical issues around aid moved from an initial concern with fungibility to the problem of conditionality.

Weeks 1995; Adam 1995). See Mkandawire and Soludo (1999) and White (1996b) for reviews of the critical commentary on WB (1994a).

This sought to introduce into the analysis notions of agency behaviour in response to conditionalities. The main issue became whether the aid relationship could alter the domestic policy processes in the recipient/debtor country in favour of IFI-imposed reform.

The literature on conditionality and policy reform has been dominated by case studies and has tended to be prescriptive rather than positive. Analytical accounts have been sparse. Mosley et al. (1995) and Killick et al. (1998) constitute the most significant contributions. The relationship between the donor and recipient and the behaviour of both participants are endogenised through recourse to a game-theoretic framework, following fashions in mainstream theory. This is complemented by a host of considerations from the public choice literature regarding the 'preferences' of the participants in the game, where issues pertaining to the political are incorporated into the analysis at leisure, with rational choice acting as a conduit for the rapid expansion of economic analysis onto traditionally non-economic analytical terrain.

The 'preferences' of the recipient/borrower often arise as the result of an interest-group dynamic, set within particular economic and/or institutional constraints. The donor/lender's objectives are inferred mainly on the basis of ideas relating to 'bureaucratic bias' and defensive lending. Upon this, conditionality confronts two main challenges: it needs to overcome the sources of 'inefficiency' located within the donor/creditor institutions; and it needs to deal with issues of 'institutional' order in the recipient/debtor countries and ensure the emergence of a sufficiently strong alliance in support of the advocated reform. In the frameworks reviewed below, the traditional form of *ex ante* conditionality does not fare well in either regard.

Conditionality as a game

In Mosley (1987b, 1992) and Mosley et al. (1995) the relationship between the Bank and the recipient or debtor economy is presented as a bargaining game, in which lender and borrower (initially as unitary actors) have conflicting interests concerning the implementation of conditions and a common interest in spending the donor's budget. This is the result of the recipient/borrower seeking to maximise the inflow of finance to support its balance-of-payments, but at the same time trying to resist at least some of the conditionality,[176] and the donor/lender seeking to extract as

[176] Following Mosley (1992, p. 131), even if there are gainers from the reform measures as imposed through conditionality, these gains tend to accrue to the politically weak rather than the strong (small farmers or unlicensed importers), and to accrue over a long rather than short period.

much policy reform from the recipient/borrower as possible but being constrained by its own objectives of budget spending and the protection of its financial position (the 'disbursement dilemma').

The game takes place in three contingent stages: the negotiation process; the implementation process; and, finally, the donor's response to a possible request by the recipient for refinance. Each party's expectation of the other's behaviour at these various stages is of fundamental importance to the strategy chosen by each participant, and hence to the outcome of the game (Mosley et al. 1995, p. 75). It is asserted that the tightness of the deal done at the beginning of the negotiation process will be influenced by the shape of the donor's and recipient's preference functions (affected by such factors as 'taste' for reform of the debtor, economic vulnerability of the debtor, size of donor's lending programme in borrowing country, extent of donor's geopolitical interest in the country); the probability and extent of expected slippage; and the nature of the expected punishment in the event of slippage, the severity of which is likely to be affected by the recipient's debt-service ratio (Mosley 1992, p. 139). Mosley et al. (1995, p. 74) assert that:

> the less the donor needs the recipient – either as outlet for funds or as political ally – and the more the recipient needs the donor – because of the gravity of its debt or foreign exchange position, or because it does not believe that it can borrow from any other source – the greater the loss for the recipient if there is a breakdown of negotiations, and the less room for manoeuvre the recipient has in those negotiations. However, the extent of room for manoeuvre does not, on its own, determine the outcome of the game.

In the implementation stage, the recipient's decision concerning the level of slippage will reflect its assessment of the risks of, and disutilities attached to, future punishment of such slippage in the last stage when refinance might be needed. If the avoided costs of coercion under slippage exceed the costs associated with the risk of losing refinance, there are gains from slippage (Mosley 1992, p. 140). Mosley et al. (1995) infer from the inspection of their cases that either a clear underlying commitment to implementation exists or it is absent. They add that attempts at measuring compliance in statistical terms merely serve to blur the sharpness of this polarisation (p. 151; see also below).

The authors continue by examining the political factors which influence the existence or otherwise of this commitment. They consider how any of the four following factors relate to policy reform efforts: type of political regime; incumbent versus new government; past history; competitive struggle between interest groups. They favour an explanation based on the latter (p. 159). The relevant issues regarding the struggle between interest groups then become: organisation of gainers; importance of compensation (p. 166); and the existence of a dedicated and competent local technocracy (p. 167). However, these are 'internal' explanations of government compliance, and the 'external' influence of the recipient bargaining relationship vis-à-vis the Bank needs to be added to the picture. To gauge this, Mosley et al. (1995) test the hypothesis that the extent to which recipients renege on their conditions depends on the financial state of the recipient economy rather than the political structures or administrative competence (the 'economistic hypothesis').

The authors find, for their sample, that on average low-slippage countries had more serious balance-of-payments problems than high-slippage countries, but that the difference is not statistically significant. Furthermore, the level of a country's financial dependence on the Bank appears to have no influence on slippage at all. A number of countries whose dependence on the Bank was very high, such as Kenya, Malawi and the Philippines, perpetrated serious slippage, and others with ample access to alternative sources slipped little. For the authors, the 'economistic' hypothesis performs poorly (p. 171).

With regard to the last stage of the game, the authors observe that the WB never refused follow-on finance to countries whose slippage levels fell below 50 percent, with the likely inference by borrowing countries that they will get away with any slippage up to this level. If donors wish to discourage such an assumption, they need to punish slippage randomly – punishing some recipients characterised by slippage below this level (Mosley 1992, p. 141).

Overall, the authors conclude that, first, slippage on conditionality is substantial even in cases where the recipient is financially weak and has little apparent bargaining power. Secondly, such slippage is frequently pardoned. Thirdly, this tendency corresponds to a compelling financial rationale for the lender, which tightens as the borrower's financial position deteriorates. Mosley et al. (1995) then propose, to the benefit of the lender, to draw up shorter lists of 'key conditions' tailored to cases of 'genuine' distortion only (see also WB 1988); and to pursue strategies such as randomly punishing slippage if it seeks to keep slippage rates lower. To the benefit of the recipient/debtor, it is proposed to reconsider the appropriateness of the policies embodied in SAPs, particularly in the poorer countries; to introduce policy changes on an experimental basis (implementing them in one province before applying them to the entire country) in order for recipients to see that a given policy change produces the projected merits; and to have a better information policy that includes local sources of knowledge and shares information more systematically. Finally, budgeting for compensation schemes for the losers from a programme is likely to improve its successful implementation (see also Mosley and Hudson 1996).

Killick (1996, 1997) and Killick et al. (1998) seek to account for the 'paradox' that the IFIs experience considerable difficulties in ensuring the timely implementation of their policy stipulations, while these policies, according to the authors, are known to result in improved economic performance. A framework is proposed, in which the BWIs are the principals which seek to induce recipient/borrowing governments, as the agents, to undertake certain actions in return for access to international capital through the 'co-operative' activity of policy (or institutional) reform (Killick 1996, p. 217).

The main problem is how the principal can design contracts that embody a structure of rewards and penalties (the 'incentive structure') that make it in the interest of the agent to further the principal's objectives. In the context of adjustment conditionality, the donor/lender's ability to do so will be determined by the recipient/borrower's assessment of its own interests, in which the costs of executing an outside policy agenda are set against its benefits (the 'participation constraint'). The key variables, therefore, are both the extent of government aversion to these particular policy measures (the participation constraint), and the rewards attached to implementing them – mainly the size of the credits and the potential catalytic effect of the reform programme (the incentive structure) (Killick 1997, p. 488). An important dimension of the reward system is the credibility of threatened punishment for non-compliance with donor stipulations (withdrawal of access to donor support), which varies inversely with donors' own internal reasons for continuing to lend (if known by the recipient), and is also negatively affected by competition between donors and other possible sources of finance (Killick 1996, 1997).

Applying this framework to a sample of developing country case studies, Killick et al. (1998) find that the agency approach describes the conditionality relationship with its alleged poor implementation record relatively well. They find evidence of frequent substantial participation constraints for recipient governments (mainly as a result of substantial distributional and transactions costs – see Killick et al. 1998, pp. 110-23), and the common inadequacy of donor-imposed incentive systems to secure implementation of a reform programme characterised by such a high participation constraint.[177] The 'fatal defect' of the incentive system is the lack of credibility regarding punishment of non-compliance (non-implementation fails to be effectively punished).

Following such an account of poor performance of *ex ante* conditionality in terms of ensuring the implementation of policies, a new model is proposed for the donor-recipient relationship. In this, 'policy dialogue' is de-linked from negotiations about specific grants or loans, and the four principles of 'ownership', 'selectivity', 'support' and 'dialogue' are promoted. The BWIs are urged to recognise that their main contribution to successful adjustment in developing countries is, according to Killick (1996, p. 226):

> their influence on the contemporary intellectual climate in which policy issues are debated, and persuasion of governments and their advisers through the regular contacts that occur.

Killick (1996) highlights that whereas there has been an overstatement of what has been accomplished through SAPs, there has also been an under-acknowledgement of the BWIs' intellectual influence on the 'silent revolution' that has occurred in many governments' attitudes towards economic policy. He adds that the BWIs should seek ways to *maximise* this influence, and that the BWIs should be willing 'to say "no" to governments with weak commitment to reform, and insist that all programmes be prepared by the borrowing governments' (p. 227).

With the leverage provided by lending apparently largely illusory, the BWIs should re-allocate financial resources away from reluctant adjusters towards the more committed ones. In the mean time, however, TA may be necessary to enhance the capabilities of governments to design reform programmes.

The behaviour of the players

These propositions regarding conditionality as a game between lender/donor and borrower/recipient have been filled in with ideas, mainly from the public choice tradition, pertaining to the incentives facing both the donor/lender and the recipient/borrower. With regard to the incentives operating on the donor/lender, the donor's capacity to enforce conditionality is perceived as being compromised by a

[177] Programmes are under-funded relative to the scale of problems; catalytic effects are undependable; the political risk of programmes is too great; and/or the debtor/recipient has access to other sources of external finance (see Killick et al. 1998, chapter 6).

set of ('perverse') institutional incentives to disburse. These relate, in the case of the IFIs, to a set of factors including: external pressures from non-borrowing shareholders who have an interest in the continuation of financial flows to a particular recipient/debtor country; internal pressures to disburse when IFIs feel they must continue lending to poorly-performing countries in order to protect their past investments and avoid the danger of these countries falling into arrears or defaulting; the wish to avoid (further) economic destabilisation that might be caused by the withholding of disbursement in the event of poor compliance; a 'culture of commitment' in which staff are judged by the amount of money they move rather than by the quality and outcome of these projects/programmes; a problem of asymmetrical information between the debtor and the creditor regarding actual compliance and the costs of enforcing compliance in such a context (see Mosley et al. 1995; Killick et al. 1998; Easterly 2001a; Martens et al. 2002).

The recipient/borrower government's 'propensity to reform' is mostly understood as the outcome of a competitive struggle between different interest groups.[178] Political agents or groups are assumed to be rational and forward-looking. Behavioural rules derive from solving optimisation problems with well-defined objective functions. Adjustment or reform implies gainers and losers depending on the types of commodities individuals produce and consume, and the nature of factor mobility between different sectors of the economy.

Initially impregnated with the notion of urban bias, the domestic politics of adjustment are depicted as depending on the strength of urban coalitions seeking to protect their interests (rents) as threatened by the various liberalisation measures imposed through adjustment/stabilisation programmes (Waterbury 1989; Bienen 1990). Alternatively, without necessarily reproducing the normative bias implied in the urban bias proposition, the possibilities of reform depend on a host of political, institutional and economic factors:[179] the cohesiveness of the pro-reform interest groups; the nature of the compensation to losers (Nelson 1984); the government's prior commitment to reform (Kahler 1989; Rodrik 1989; Ranis and Mahmood 1992; Casella and Eichengreen 1996); the relative capacity of regime type (democratic versus authoritarian) to ensure adjustment/stabilisation (Nelson 1984, 1989, 1990;

[178] See, for instance, the various contributions in Meier (1991).

[179] For overviews, see Haggard and Webb (1993) and Rodrik (1996). For a representative collection of papers exploring political and economic factors affecting adjustment/stabilisation exercises, see Nelson (1990).

Haggard and Kaufmann 1989; Toye 1992);[180] the appropriate timing and sequencing of various elements of the reform package (Nelson 1984; Sachs 1994); the need to insulate the 'technocracy' invested with the responsibility of carrying through the reform package from interest group pressures (Nelson 1992); the competence of the bureaucracy and its technical/administrative implementation capacity (Nelson 1984; Callaghy 1989); the coherence of the government's economic team (Williamson 1994); the extent to which new-comer (governments) have an advantage over incumbents regarding the capacity to implement reforms (Nelson 1992; Toye 1992); the role of economic crisis in inducing (or retarding) reform (Nelson 1990; Toye 1992; Webb and Shariff 1992; Krueger 1993; Drazen and Grilli 1993; Drazen and Easterly 2001); the significance of 'collective (economic) memory' (social learning on economic issues) (Sikkink 1990); the distribution of income (Berg and Sachs 1988); and other 'exogenous' factors such as the terms of trade (Ranis and Mahmoud 1992).

Finally, Morrissey and White (1997) provide a general framework in which the different assumptions regarding the preferences of donor/creditor and recipient/debtor in the conditionality-as-a-bargaining-process framework can be accommodated, and in which conclusions regarding the relative effectiveness of the traditional form of *ex ante* conditionality in different scenarios can be summarised. With utility functions of donor/lender and recipient/borrower government defined in terms of amounts of aid and economic policy reform, four cases arise: first, both parties favour reform and financing with both their utility maximised by having as much as possible of both; second, both want to spend the aid budget, but the recipient is averse to reform; third, the donor does not seek to maximise spending, unlike the recipient whilst their respective preferences regarding reform coincide; fourth, the donor does not seek to maximise lending (unlike the recipient), but their respective preferences regarding reform diverge (the recipient is reform-averse). Following Collier et al. (1997), a set of roles are attributed to the traditional form of *ex ante* conditionality ranging from inducement to monitoring, signalling, support, or restraint, with the relative effectiveness of any of these functions depending on the particular constellation of donor/recipient preferences.

Morrissey and White (1997) argue that in none of the four scenarios *ex ante* conditionality (where the disbursement of funds is linked to the promise of policy

[180] This is distinct from the debate on whether the reforms embodied in SAPs promote democratic values or are rather more conducive to authoritarian interventions. For the idea that SAPs promote democracy, see Diamond (1988). For a refutation of such an argument, see Beckman (1992).

reform) is likely to enhance the probability of reform. In the first scenario, where there is shared agreement between the recipient and the donor regarding reform and finance, a role for (*ex ante*) conditionality (as restraint, signalling, monitoring and support device) is conceivable. However, it does not enhance the probability of reform and might even harm it as it undermines the credibility of conditionality when donors condone slippage. In the second case, the donor's willingness to spend its budget undermines the effectiveness of *ex ante* conditionality. When, in the third scenario, both donor and recipient want reform but the donor is not seeking to maximise its funding and can thus restrict lending and tighten its demands regarding policy reform, conditionality may fail to fulfil its monitoring, signalling and/or support roles. In the last scenario, traditional conditionality plays no useful role in supporting reform, and punishing slippage tends to undermine the recipient's ability to implement reform (insofar as aid is supportive).

Morrissey and White add that the problems facing *ex ante* conditionality could be reduced by adopting *ex post* conditionality, where the latter is based on policy performance measures rather than on inputs (p. 504). Yet, the authors caution that this is not without its problems as donors might behave arbitrarily regarding what constitutes acceptable performance and recipients may miss a performance target because of external shocks or unavoidable implementation problems. In both instances, the recipient will be uncertain about the receipt of aid, which in itself undermines the sustainability of a reform programme.

The literature regarding selectivity or *ex post* conditionality in the allocation of aid flows is explored at length in chapter five. Other recommendations have called for increased flexibility in the practice of conditionality, for instance through the use of floating tranches or programmatic policy-based lending, as well as for the streamlining and refocusing of conditionality (WB 1999c; Khan and Sharma 2001).[181]

[181] Under floating tranche arrangements, tranches are disbursed when specific conditions are fulfilled rather than according to a set schedule. The approach has been used, in particular, for clearly defined discrete reform actions with uncertain timing such as privatisation (see Koeberle 2003, p. 262). Programmatic policy based lending involves a series of single-tranche operations embedded in a medium-term framework specified at the outset and with expected prior actions for subsequent operations (a set of annual single tranche credits embedded in a rolling programmatic framework). In contrast to multi-tranche adjustment credits, programmatic policy-based lending is based on *ex post* performance and implementation, not on expected policy changes. It has been promoted as a way to reconcile the debate between the traditional *ex ante* approach and the aspirations of a results-based approach to conditionality (see Koeberle 2003). PRSCs are an example of this approach.

4.3.2 Understanding conditionality beyond the game

The above accounts broadly raise issues on two fronts: first, regarding the framework within which conditionality is understood, steered by a rational choice incentive-based analysis in which the recipient/borrowing government and the donor/lender institutions meet as self-interested entities maximising a certain objective subject to constraints; and, secondly, regarding the embedded ideas of what steers the objective functions of the respective agents in this incentive-based framework. The second issue implies questions regarding institutional incentives at the level of the donor and regarding the depiction of the recipient's domestic political processes as a distributional struggle between losers and gainers steering the recipient's preference formation and hence its maximisation exercise.

We are concerned here with the first issue.[182] We expose the problematic nature of understanding conditionality as a game or bargaining process between two parties each invested with a certain amount of bargaining power, and illustrate how such an understanding has led to an underestimation of the significance of donors' leverage through the conditionality process. The comments we make echo the criticisms above of the two-gap model and the fungibility propositions, mainly in that they draw attention to the way in which the realm for analysis as delineated in the analysis of conditionality fails to incorporate the various defining features of the conditionality process, spanning from the particular political, financial and economic context in which the phenomenon expanded so rapidly to various qualitative aspects of the creditor-debtor relationship beyond the formal conditionality relationship.

In the framework of a two-party game between donor/creditor and recipient/debtor, the effectiveness of conditionality (the outcome of the game) is assessed on the basis of an assessment of conditions complied with, relative to the total number of conditions imposed. In this framework, high 'slippage', which is measured by a low implementation rate relative to the total number of conditions imposed, implies a situation in which the recipient/borrower retains a significant amount of control over its policymaking and points to relatively unsuccessful donor/lender leverage. This outcome is ascribed to a recipient/borrower's capacity to resist these reforms on the basis of its relative bargaining power. High slippage then projects agency, the exercise of choice, and represents a winning position for the recipient in the bargaining framework. Killick et al. (1998, p. 163) state that:

[182] For a good critical appraisal of the depiction of internal domestic political processes as the outcome of a struggle between interest groups in the context of structural adjustment, see Gibbon and Bangura (1992); Bangura (1995); and Mkandawire and Soludo (1999).

> The basic premise of the agency approach is that outcomes are a result of calculations by governments and their officials about whether implementation will be in their own interests or not. The results provide rather strong confirmation of the appropriateness of this. There is clear evidence in a high proportion of the twenty-one countries studied in … that the probability that agreed WB programme measures will be implemented is a function of the extent to which the government and its officials perceive this to be in their own interests.

Within this framework, the conclusion recurs that *ex ante* conditionality has tended to imply limited effective donor leverage – it has failed to provide donors/creditors with the desired control over debtors' policy making.

A number of problems arise with this depiction of donor/lender leverage versus recipient/borrower agency or control in the context of conditionality, according to which high slippage implies that a recipient/borrowing government retains control over its policy-making and chooses to implement (or not implement) certain policies in ways that fit its own objective function under a set of constraints (see also Collingwood 2004). First, the structural features preconditioning and characterising the field in which donor and recipient meet, are ill-accounted for. Through a focus on implementation and 'slippage', there is an implicit assumption that the problem lies with the incentives undermining compliance with what is perceived to be a legitimate and rational process. Mosley et al. (1995, pp. 313-4) emphasise in their conclusion that:

> Our own view is that policy-based lending as such represents an imaginative response by donor agencies to the global economic crisis of the early 1980s, and that the problems which remain are design problems susceptible to reform … rather than problems which undermine the entire original concept.

Mkandawire (2002, p. 155) highlights how in the principal-agent or game framework, the principal, the donor, wants development while the recipient simply wants material gain. Such an approach reflects the tendency to ignore the broader and underlying political economy in which the principle of conditionality rapidly proliferated and which affected both the form it took and the policies with which it was coloured in.[183] As a result, design changes to the conditionality process are

[183] It also reflects a poor appreciation of the notion of sovereignty – much in contrast to the legal critique of conditionality (see Collingwood 2003, 2004). In almost caricature fashion, Collier (2005,

recommended to deal with what are actually ill-recognised structural parameters determining the engagement between donor and recipient. Collingwood (2004, p. 18) comments that:

> By focusing on the procedural aspects of contract-making and equating outcomes with interest-satisfaction, rationalists undermine the extent to which something that is apparently fair can be an 'equal treaty' with unjust consequences.

Yet, the policy conditions attached to aid and loans are not neutral ideas, but are the product of asymmetric power relations. This is evident in various ways (Collingwood 2004, p. 14). Conditional contracts are agreed by borrowers on an individual basis, rather than bargained collectively. There is only limited scope to alter the content of the policy changes required by the IFIs (what is up for discussion and how). Borrowers apply for IFI assistance at times of severe economic weakness, and IFIs hold a virtual monopoly on international financing as they act as 'gateway' institutions to other donors and the market. If power issues are acknowledged (for example through a debtor's relative debt position), they are not theorised *ex ante* but are incorporated into the analysis *ex post* in an ad hoc attempt to make the rational choice framework, within which the conditionality relationship is understood, conform better to reality.

Attempts to understand the dynamics implied by conditionality need to place the phenomenon in the context within which it evolved. This would imply an interest in the interactions between the 1982 debt crisis, the response of the international financial-economic community, the role of the IFIs therein, and the nature of the adjustment imposed on troubled debtors which has been biased towards creditors' interests rather than debtors' – with the insistence on debt repayment rather than debt relief (see Weeks 1987; Biersteker 1993; Bienefeld 2000; Soederberg 2004a). In that context, the analysis proposed by Fafchamps (1996) which examines the effectiveness of conditionality in stimulating repayment of sovereign debt is more candid. Again, the need transpires to assess the 'success' of aid, or now of conditionality, in terms of actual rather than projected purposes. Soederberg asserts (2004a, p. 38, my emphasis):

> Washington's understanding of policy reform was aimed not at restoring development, but at increasing debt service capacities through export

p. 116) refers to the domestic policy space as creating 'rents of sovereignty' and calls for international standards and codes prescribing minimum acceptable practice. Such an idea informs the promotion of the CPIA as a standard for the allocation of aid flows (see chapters five and six).

expansion and import compression, so that the overextended US-based banks could be repaid. In this sense neoliberalism was *successful*, since it produced large sustained net resource transfers from many developing countries to the developed world.

Secondly, these issues reflect concretely in problems regarding compliance measures as indicators of control over policy-making or of the exercise of agency in a conflict between lender/donor and borrower/recipient. The Bank constructs compliance measures to assess the effectiveness of its programmes. These emerge as the (unweighted) average of subjective assessments of implementation in various reform areas. It claims impartiality for its ratings on the grounds that the staff members attributing the particular scores are located in the Bank's Operation Evaluation Department (OED). The OED is independent of the Bank's senior management and has a budget allocated to it directly by the Board of Directors to which it reports. Leaving aside who exercises this judgement and the evidence on the basis of which that happens, the issue remains of the adequate weighting of scores in different policy areas when constructing an aggregate country-wide measure of compliance.

More generally, gauging compliance from an assessment of the number of conditions complied with, out of a donor/lender-imposed total, might misrepresent the actual control the donor/lender is acquiring over recipient/borrower policymaking. Policies are not necessarily independent and implementation of one policy measure might have severe implications with regard to control over other policy instruments. As a result, compliance with particular conditions potentially implies a greater qualitative loss over domestic policy-making than quantitatively indicated.[184] Mosley et al. (1995, p. 143) raise a similar but contrary point. They indicate the possibility of countervailing action and trivial conditions with the implication of overestimating leverage as measured through compliance rates. In our understanding, however, high slippage does not necessarily signal the maintenance of control over development policy by the recipient/borrower, nor does it inevitably point to a winning position for the recipient/borrower in the conditionality game. The

[184] The Bank's own assessments single out performance on 'key conditions' (or 'critical actions'). McCleary (1991) comments that although the legal status of these key conditions is no different from that of other conditions, they appear as 'key conditions' because Bank staff designing the loan operation put particular emphasis on them as they are expected to make a significant contribution to stabilisation/adjustment. He finds that, on balance, performance on 'key conditions' was better than performance on all conditions, and that in public enterprise reform, tariff changes and industrial policy, performance on key conditions was particularly good (p. 206).

number of conditions set by the donor/Bank that have been complied with constitute an inappropriate (and to a certain extent arbitrary) benchmark against which to assess the implications of policy-based lending for donor leverage over recipient policy formation.

Thirdly, these assessments of slippage and their conclusions pertaining to agency are constrained by their own time framework. The inference that a country has not been subject to much donor leverage because its compliance score was low can reveal itself to be provisional. The case of Kenya in Mosley et al. (1995) illustrates this well. For Mosley et al. (1995), Kenya is a poor country with little access to alternative sources of finance but which successfully manages to outwit the Bank as indicated in its low implementation rate (38 percent; p. 142). Although the country had gone a long way in eliminating 'distortions' in the prices of its crops, credits and foreign exchange, it had allowed 'slippage' on the issues of land reform, decontrol of the maize trade and the rationalisation of the structure of protection (p. 150). Still, the Kenyan government is portrayed as taking the money while managing to retain significant control over an important area of its domestic policy, in the meantime securing refinance from the Bank. Nevertheless, implementation efforts by the Kenyan government rapidly accelerated after 1992, and Ikiara and Ndung'u (1999, pp. 79-83) portray a rather different picture:

> By the end of 1995, Kenya had implemented major political and economic reforms agreed upon with the multilateral and bilateral donors. The economic reforms implemented included the removal of virtually all price and foreign exchange controls, the liberalisation of domestic marketing trade, import liberalisation, reduction of the budget deficit, financial reforms, privatisation, removal of wage guidelines and other labour market reforms, and liberalisation of the exchange rate ... By July 1995, the maize market, hitherto the most resisted reform and the central focus of donors, and the petroleum/oil sector, had been completely liberalised.

In this vein, Morrissey (2002) argues that conditional lending often has had quite pronounced effects on policy reform but that these tend to become apparent slowly. In the context of exchange rate liberalisation, for instance, the author observes that while most SSA countries had fixed exchange rates in the early 1980s and few had fully liberalised by the end of the decade, by the mid-1990s most had quasi-floating exchange rate regimes. He stresses that 'compliance may not have occurred within the period of the agreement, but the direction of policy reform was established' (p. 12). As such, in a game-theoretic framework the issues arise as to when the game begins or ends as well as to how to accommodate the introduction of new players or the loss of old, which would be implied in the process of adjustment or development.

Fourthly, there are important qualitative dimensions of policy-based lending with significant repercussions for donor/creditor control over recipient/debtor's policy which are not reflected in compliance indices. In line with Killick's (1996) assessment highlighted above, there is a need to recognise the crucial role played by the IFIs in conditioning the broader discursive space on development, particularly since the rapid expansion of policy-based lending. Further, the importance of TA provided in the context of policy-based lending is easily underestimated. Branson and Jayarajah (1995), nevertheless, document how, in a sample of 99 adjustment projects, more than half were supported by (free-standing) TA, and all the African countries in the sample with adjustment programmes received TA. External assistance to Africa in the form of long-term expatriate advisers and resident consultants increased dramatically (by fifty percent) between the mid-1980s and mid-1990s, and by the mid-1990s stood at around US$ 4 bn a year, with around 100,000 expatriate technical advisers working in Africa (Husain 1995, p. 200; see also Helleiner, G. 1994, p. 10; and chapter one). While it might be tempting to focus on loan conditionalities as proof of the IFIs' influence on a country's policy agenda, the ownership of a particular reform agenda is more complex. As documented in chapter two, the 'pathways of influence' are manifold (Samoff and Bidemi 2003). These dimensions of the relationship between donor/creditor and recipient/debtor remain, however, ill-appreciated in the analytical frameworks surveyed above.

Fifthly, the literature that seeks to illustrate the relationship between aid and policy reform also suffers from the 'econometric disease'. Causation is established through correlation rather than structured regularities being discerned, refined and explained. Morrissey (2002, p. 12) highlights how country case studies on policy reform face the particular difficulty of distinguishing between a) the leverage of conditionality in encouraging attempted reform; b) other constraints on implementing reform; and c) outcome (performance) indicators that may only partly reflect reform efforts. The author argues that the latter two are easily confused with the former and that observing a poor outcome often leads to the inference that conditionality has failed. Morrissey (2002) additionally identifies a recurring 'criteria bias' in case studies on aid and policy reform when, irrespective of how much reform there may have been, a few instances of non-compliance are picked out to conclude that aid failed to affect policy reform.

In conclusion, it can then be asserted that, although the policy reform process in each country is complex and determined by its own political, economic and social parameters, the political and economic realities in developing countries have been dramatically affected by their relationship with the IFIs. In most developing countries the state's presence in the economy has been redefined (retreating from engagement in productive activity to a residual role as provider of an institutional framework); markets have been given greater prominence in the organisation of economic activity; and the economies have become more open to private foreign capital than before (see UNCTAD 1998; Mkandawire and Soludo 1999; UNCTAD 2000a; UNCTAD 2001; UNCTAD 2002; SAPRI 2002; Morrissey 2002; Singh 2002; Mkandawire and Soludo 2003). UNCTAD (2000a, p. 103) observes that in LDCs:

> extensive structural reforms have occurred in the deregulation of pricing and marketing, particularly in the important markets for agricultural products and inputs; the easing of trade barriers, particularly curtailing quantitative restrictions; reform of foreign exchange regimes; and liberalization of interest rates.

These reforms result from the rapid and extensive liberalisation, deregulation and privatisation endeavours promoted by the IFIs, whether they were formally imposed through conditions, or informally propagated through the IFIs' effect on general policy discourse, through TA or as a result of IFI involvement in analytical work. Such a conclusion contrasts with the propositions of limited leverage of aid (or of the IFIs) over recipient policy that tend to be supported by the analyses of *ex ante* conditionality surveyed above.

4.4 Conclusion

This chapter has surveyed what we identified as the old economics of aid. It was organised around a critical appraisal of those propositions that assess the extent to which aid augments the resources available to a recipient economy and whether it is used for the purpose intended – fungibility; and the analysis of the relationship between aid, conditionality and policy reform. Across these strands, we identified a persistent bias in the conceptualisation of the analytical realm, which has been heavily preconditioned both by the limits of mainstream economic theory and as a result of the dynamics of the 'financial-intellectual' complex of aid.

The old aid economics have tended to abstract away from the defining features of aid and conditionality as being anchored in particular (fundamentally asymmetric) donor-recipient relationships which stretch beyond the aid relation (the recipient economy is not just a recipient of aid, but trades, has debt, provides migrant labour, etc.), and as interacting with a socio-politico-economic environment the description of which should stretch beyond what is captured in those parameters determined by an 'aid-development' (teleological) perspective. Successive efforts to incorporate into the analysis distinguishing features of the aid and conditionality phenomena have been inadequate, as they fail to address satisfactorily the initial failures to understand the phenomena in their specific context and perpetuate a fragmentary account of the aid experience. Furthermore, changes to the analytical accounts have often been driven forward more by changes in the technical apparatus and fashions of neoclassical economics than by the realities of aid and development.

An important implication of these shortcomings has been that, although aid and its conditionalities have had pervasive implications for the recipient/debtor countries, the old aid economics has not been able to capture these, projecting at most ambiguous conclusions. In this way, it has contributed to a discourse in which the dynamics associated with aid and conditionality are under-appreciated. The extent to which the various dimensions and institutions of aid have managed to restructure the recipient/debtor economies has easily been downplayed and the role of aid in the broader political economy misunderstood. This has been aggravated with the recent focus on *ex post* conditionality or 'selectivity'.

Chapter 5. Selectivity and the new economics of aid

5.1 Introduction

Under a PBA of aid, or 'selectivity', the conditionality accompanying the aid flow no longer reflects the flow of reforms but the state of the policy and institutional environment. Together with 'ownership', selectivity seeks to imply a redefinition of conditionality where the primary challenge is no longer for a government to reach an agreement with the donor (or the Bank) on a set of reform measures, but rather that sufficient support for these reforms is established within the country and aid allocated accordingly.

The selectivity discourse became increasingly formalised in the late 1990s, abetted by the appearance of a set of analytical and empirical arguments. These came to constitute a new aid paradigm, heavily promoted by the Bank. On its basis, the Bank sought to encourage other agencies to emphasise prior actions rather than future policy promises when allocating aid flows. A paper by Burnside and Dollar (2000a) was central in providing the analytical and empirical foundations to the new practice, and the Bank flagship reports *Assessing Aid: What Works, What Doesn't and Why* (AA) (WB 1998a) and *Aid and Reform in Africa* (AARIA) (WB 2001a) were built around its core premise that aid effectiveness is conditional on a set of predetermined policy and institutional criteria.

A critical literature emerged, engaging with the building blocks of the Bank's approach. This literature has been mainly concerned with issues of model specification, econometric technique and data selection. It exposes how the Bank-promoted paradigm is based on a biased research effort, poor theoretical and econometric practice, and is not representative of the broader findings of the aid impact literature. It guards against the simplistic understanding of the aid-reform-growth process underlying the 'selectivity' proposition.

The preoccupation within the aid effectiveness literature with the Bank's stance, however, inadvertently anchors the latest theorising about aid in the conceptual framework implied by its premise. This implies a 'new' economics of aid preoccupied with formal modelling, characterised by a bias towards the use of large databases, and which explores the effect of aid within the confines of new growth theory.

The current chapter considers the extent to which these innovations provide improved insights on the economics of aid. It argues that the 'new' fails to overcome the inadequacies of the 'old' and remains constrained by those failures identified in chapter four. These include: a persistent lack of specificity in the analysis of aid; the crippling limitations of mainstream analytical frameworks for the understanding of economic phenomena such as growth; and a futile predilection for overcoming these analytical shortcomings by recourse to econometric 'proof'. None of the increased levels of sophistication in the analysis improves the understanding of the mechanisms of aid impact or allows for clear-cut conclusions. On the contrary, this seems a futile exercise in the context of inadequate analytical categories and behavioural assumptions, with any particular conclusion regarding aid effectiveness easily countered by mere manipulation of models or data. The debate has been essentially reduced to quibbles regarding the significance of a coefficient in an aid-growth regression and continues to circumvent serious reflection on first principles of theorising and model building. Furthermore, the issue of why such an undoubtedly poor research endeavour was so heavily promoted by the Bank remained open (if far from new).

This chapter proceeds as follows. It starts, first, with an extensive overview of the core arguments underpinning the main elements of the Bank-promoted aid paradigm. Burnside and Dollar's proposition has been complemented by a set of arguments, each dealing with a more specific embedded aspect of the aid-policies-growth-poverty relationship, and these are briefly summed up. This is succeeded, secondly, by a critical journey into the epistemological foundations of the Bank-celebrated aid paradigm. This implies scrutiny of the theoretical model upon which Burnside and Dollar (2000a) and similar propositions draw, of the soundness of the quantitative techniques deployed, and of the relationship of the new paradigm to the empirical reality it seeks to reflect and affect. The failures of the Bank-promoted propositions on these three counts stand out starkly, sitting uncomfortably with the Bank's recently self-declared 'knowledge' mission highlighted in chapter two. Thirdly, the analytical repercussions of a research agenda regarding aid set on Bank terms are assessed. It is documented how the 'new' economics of aid, prompted by the Bank aid research, fails to improve our understandings of the dynamics of aid and conditionality. If anything, the repercussions of the financial-intellectual complex, denounced in chapter four, have become more entrenched. Fourthly, the hazards of an aid allocation process based on the selectivity principle are explored. The proposition to allocate aid's financial resources to countries characterised by a predetermined set of policy and institutional features, as defended by the Bank-promoted research, risks increasing aid volatility and penalises countries for circumstances often beyond their control. It could jeopardise attempts in IDA-eligible countries to raise their investment rates as they are threatened with rationing of aid monies. In conclusion, we draw attention to the particular way in which the Collier-Dollar steered propositions mediate the relationship between operational imperatives, research and rhetoric at the Bank, providing a 'scientific' linkage between the Bank's rhetorical emphasis on development and poverty reduction and the protection of a core operational agenda embedded in the CPIA – which sits at the core of the selectivity proposition. This brings us to the final chapter.

5.2 Aid, policies and growth: the new paradigm

The Bank's latest stance on aid effectiveness builds on the work of a few well-known development economists who were employed in the Bank's research department (DEC). As the Director of the Bank's Development Research Group (DECRG) between April 1998 and April 2003, Paul Collier played a steering role in this research endeavour.[185] The position gave him the occasion to develop further a set of ideas regarding aid and conditionality he had started to explore previously (see Collier et al. 1997; Collier 1997a, 1997b). The other major player in the aid effectiveness research was David Dollar, a much-celebrated Bank researcher who has persistently demonstrated his faculty at providing scholarly support for the neo-liberal paradigm, most famously in Dollar and Kraay (2002), the development of the Dollar index of trade openness, and the aid effectiveness research.[186] At the time of the aid effectiveness research, David Dollar was a Research Manager in DECRG. He subsequently became Director of Development Policy within DEC and was finally promoted to Country Director for China and Mongolia, a much coveted job at the Bank.

Interestingly, William Easterly was forced out of the Bank during Dollar and Collier's heyday in DEC.[187] As senior economist in DEC, Easterly had called for a slightly more prudent reading of the Dollar-Collier results (Easterly 2003; Easterly et al. 2003), but had not otherwise fundamentally challenged the more general Bank

[185] He is currently the Director of the Centre for the Study of African Economies, from which he was seconded.
[186] For a critique of Dollar and Kraay (2002) see Weisbrot et al. (2000) and Lubker et al. (2002). For a critique of the Dollar trade index, see Rodriguez and Rodrik (2000) and Subasat (2003).
[187] For a good account of Easterly's departure, see the WBG Staff Association Newsletter (November/December 2001). It is ironic that the book at the heart of Easterly's resignation, *The Elusive Quest for Growth* (Easterly 2001b), was hailed as 'perhaps the most cited and influential of all of the Bank's research output' in Deaton et al.'s (2006, p. 50) evaluation of Bank research.

outlook regarding aid and growth (Dollar and Easterly 1999; Easterly 2002).[188] The factors leading up to Easterly's resignation are seemingly unrelated except for the important role the Bank's External Affairs department played in his departure and the well-documented convivial relationship that David Dollar entertained with External Affairs (see Broad 2006). Easterly's resignation also stands in stark contrast with Robert Wade's (2004b, p. 585) account of David Dollar becoming a standard for judging the stature of other economists in DEC.

The rest of this section reproduces the main propositions that weave together as the analytical fabric of the Bank's current aid paradigm. These were summed up in the Bank's flagship AA (WB 1998a). The cornerstone of the Bank's current aid paradigm is provided in Burnside and Dollar (2000a).[189] The latter argues that aid only affects the growth rate positively if a certain set of policies/institutions are characteristic of a country, and that aid does not affect the policy environment. Hence, aid should be (re-)allocated towards those countries characterised by a 'good' policy and institutional environment. This broadly reflects the CPIA or, more narrowly, focuses on the core macroeconomic policy stances of budget surplus, low inflation and trade openness. The key for aid effectiveness becomes located exclusively at the level of the debtor economy, to the further disregard of the structural features in which the aid phenomenon and its policies take form. Together with Dollar and Kraay (2002), the arguments lodged in Burnside and Dollar (2000a) and its various spin-offs (see below) sum up the Bank's position on aid, globalisation and poverty reduction. They were brought together in a Bank Policy Research Report *Globalisation, Growth and Poverty* (WB 2001h) written under the leadership of Paul Collier and David Dollar.

Burnside and Dollar (2000a) builds on Boone (1994, 1996), which argue that aid has no effect on investment or growth in the 'typical' poor country. Boone (1994)

[188] See, in particular, the following extract from Easterly (2002, p. 118), which is very much in line with the selectivity proposition the Dollar-Collier research sought to prop up:

> We should tie aid to past country performance, not promises, giving the country's government an incentive to pursue growth-creating policies. The better a country's policies are for creating growth, the more aid per capita it gets. We should rank all poor countries according to their policy performance and then give more aid to a country the higher it is up the list. The exact formula is not important; all that is important is that aid increases with policy performance, so that governments have an incentive to pursue good policies ... We know something about what policies are associated with growth. For now, let's say that a country that has a high black market exchange rate relative to its official exchange rate, a high inflation rate, a controlled interest rate well below the inflation rate, a high budget deficit, and widespread corruption should not be getting aid.

[189] Its findings were widely circulated as a WB working paper (Burnside and Dollar 1997) before publication in a peer-reviewed journal. See Easterly (2003) on how the paper rapidly became the most important reference on aid effectiveness.

models the impact of aid in a new growth framework, and Boone (1996) embeds the findings of Boone (1994) in a public choice framework.[190] Combined, Boone (1994, 1996) present an interpretation of the world as a set of heterogeneous countries, with varying levels of income caused by differences in policy variables, where the cross-country pattern of taxes and transfers is accounted for on the basis of a public choice framework. Aid transfers are fully consumed and do not affect steady-state income levels.

Boone (1994, 1996) have been the subject of a number of critical remarks. Theoretically, it has been pointed out that the predictions with regard to aid's impact in the context of new growth models depend on the assumptions regarding consumption/savings behaviour; on whether aid is perceived as a temporary or permanent income transfer; or on whether the country is on its steady-state balanced growth path or approaching it (see Tsikata 1998; and below).

Furthermore, Boone's empirical results have been challenged. First, his findings are at odds with a range of recent studies (equally exploring 'new' modelling and estimation techniques), which establish a positive relationship between aid and growth (see below). Secondly, it remains unclear why Boone decides to ignore the result that aid has an impact on investment when his full sample is used. The author excludes those countries for which the aid:GNP ratio exceeds 15 percent – i.e. those countries for which any recommendation with regard to aid is likely to matter – on the grounds that their inclusion would invalidate his presumption regarding the aid-investment-growth relationship (Boone 1996, p. 16). Thirdly, Feyzioglu et al. (1998) demonstrate how Boone's results are specific in terms of the sample selection method. Using annual observations rather than 10-year averaged data, the authors find a positive and statistically significant relationship between aid and total investment. Fourthly, Boone ignores the potential endogeneity of aid to growth.

Despite these problems, Burnside and Dollar (2000a) take their cue from Boone (1994) as they seek to understand the interactions of aid, economic policies and growth in a new growth framework. In their modified neoclassical growth model, poor countries tend to grow slowly due to a subsistence consumption constraint and imperfect international capital markets, despite a high marginal return to investment. Aid can accelerate growth rates in the transition to a steady state. This

[190] Boone (1994) was never published and is only available upon request from the *Centre for Economic Performance* at the London School of Economics. Nevertheless, it occupies centre stage in recent arguments of aid (in)effectiveness.

in contrast to Boone (1994), who rejects the premise of capital market imperfections as a rationale for aid and dismisses the idea that minimum subsistence needs explain low savings rates in developing countries.[191] However, institutional and policy distortions can lower the return to capital and reduce the transitional growth rates. Both the extent to which aid translates into increases in consumption rather than investment (dK/dA) (fungibility), and the extent to which resultant investment translates into growth are conditional on a set of policies.

On this reasoning, Burnside and Dollar (2000a) construct a growth equation that includes aid and aid interacted with policies. The institutional/political factors and economic policies that enter the growth equation are picked from the empirical growth literature and include: a measure of institutional quality, capturing security of property rights and efficiency of government bureaucracy (Knack and Keefer 1995);[192] a measure of 'ethnolinguistic fractionalisation' and the number of assassinations to capture civil unrest (Easterly and Levine 1997); and the ratio of money supply to GDP as a proxy for distortions in the financial system (King and Levine 1993). The latter variable is lagged one period out of concern over its endogeneity. Economic policies are captured by: a dummy variable for trade openness (Sachs and Warner 1995);[193] inflation as a measure of monetary policy (Fischer 1993); and the budget surplus as a measure of fiscal policy (Easterly and Rebelo 1993).[194] The growth equation further includes initial income to capture convergence, and regional dummies for Sub-Saharan Africa and East Asia. On the basis of this growth specification, the authors seek to establish whether aid and/or aid interacted with policies have an effect on growth. In addition, they examine the relationship between aid and policies: is aid a function of policy or policy a function of aid?

The authors draw on a new database on foreign aid developed by the WB (Chang et al. 1998). This database transforms existing figures on ODA into Effective Development Assistance (EDA) by including only the grant components of loans and

[191] Boone (1994) argues that capital markets work in allocating savings and that low savings rates in developing countries are related to the unwillingness of a wealthy elite to invest domestically.
[192] More specifically, the variable 'institutional quality' is an index based on evaluation of five different institutional indicators made by the private international investment risk service, International Country Risk Guide. The five indicators are: quality of bureaucracy, corruption in government, rule of law, expropriation risk, and repudiation of contracts by government.
[193] Closed economies have average tariffs on machinery and materials above 40 percent, or a black market premium above 20 per cent, or pervasive government control of key tradeables (Burnside and Dollar 2000a, p. 849).
[194] The budget surplus variable includes foreign grants in revenues and aid-financed projects in expenditures. Hence, there is no relationship between aid and the measure of the budget surplus.

excluding TA. Burnside and Dollar (2000a) express EDA as a share of recipient GDP by first converting EDA to constant 1985 dollars using the unit-value of imports price index from International Financial Statistics (IMF). This is divided by real GDP in constant 1985 prices provided by the Summers and Heston (1991; Penn World Tables 5.6) data set.

On the basis of an initial base growth regression (excluding aid and the aid×policy interaction term), the three policy indicators are combined into a policy index with their respective weights determined by the coefficients obtained from the results of the base regression: policy index = 1.28 + 6.85×budget surplus – 1.4×inflation + 2.16×openness (p. 855). This index is used to form the interactive aid×policy term.

For a panel of 56 countries using six four-year averages between 1970-73 and 1990-3, the authors estimate variations of the growth equation using both ordinary least squares (OLS) and two-state least squares (2SLS), with the latter method aiming to address the possible endogeneity of aid. Under both methods, they find no significant relationship between aid and growth for a growth equation that includes aid but not the interaction terms (p. 855). Tellingly, when the specification containing the controls, policy index, aid and aid×policy is run on the full data set, the interaction term aid×policy does *not* enter significantly either – whether in OLS or in 2SLS estimation with aid and aid×policy instrumented.

However, Burnside and Dollar (2000a) establish that the coefficient on the interaction term becomes significant after either of the following two possible changes. Five outliers can be excluded (which constitutes their preferred specification),[195] or a term can be added which interacts policy with aid squared. In the latter case, both the aid×policy and the aid^2×policy interaction terms are significant, the first with a positive and the second with a negative sign. This is taken as an indication of diminishing returns of aid on growth. These results are confirmed when the regressions are run for LICs only, with the same provision of excluding 'outliers' to get significant 2SLS results. The authors draw the conclusion that aid only affects growth when 'good' policies characterise the recipient country. In

[195] The five 'outliers' are Gambia 1986-1989 and 1990-1993; Guyana 1990-1993; and Nicaragua 1986-1989 and 1990-1993.

addition, aid flows are found to have no effect on policy reform (the failure of the traditional form of conditionality).[196]

The main argument of the first chapter of AA, that aid does not have an impact on growth except in a 'good' policy/institutional environment, is based on an econometric exercise very similar to the one undertaken by Burnside and Dollar (1997, 2000a). The only difference relates to the construction of the policy index, which in AA includes a measure of institutional quality in addition to the policy measures of inflation, budget surplus and trade openness. Following Knack and Keefer (1995), the measure of institutional quality is calculated on the basis of indicators on bureaucracy, corruption, the rule of law, risk of expropriation, nationalisation and contract repudiation.

Burnside and Dollar (2000a) further examine how donors allocate aid flows, and in particular whether donors have been sensitive to the quality of policy environments in aid recipients. They find that, on average, donors have not rewarded 'good' policies, that aid allocations are characterised by small country bias and reflect donor strategic interests rather than the quality of the policy environment (p. 863) (see also Alessina and Dollar 2000). In a final paragraph, Burnside and Dollar (2000a) briefly consider the extent to which aid affects government consumption in recipient countries. They find government consumption to be a strong positive function of aid, particularly for the case of bilateral aid which, for the authors, adds to the explanation of why the impact of aid on growth has not been more broadly positive (p. 864).[197] Burnside and Dollar (2000a) conclude that their results provide *strong* support for the recommendation that making aid more systematically conditional on the quality of policies would increase its impact on developing country growth, with a particular understanding of what constitutes apt policy (p. 864).

Burnside and Dollar (2004b) revisit their original premise, now with an emphasis on the implications of institutional quality for aid effectiveness. Using the index of institutional quality constructed by Kaufmann et al. (1999), the authors demonstrate, on the basis of a new cross-section data set focusing on the 1990s, how, first, countries with 'better' institutions have been 'rewarded' with significantly more

[196] In the 1997 Working Paper, the authors test whether changes in aid had any systematic effect on policies. In the 2000 published version of the argument, policy is treated as exogenous with regard to aid.
[197] The issue of aid, government consumption and poverty is further explored in Burnside and Dollar (2000b). Unsurprisingly, it is reaffirmed that in a 'poor' policy environment neither growth nor a decline in infant mortality is on average supported by aid.

aid (selectivity at work); and, secondly, how the institutions-aid interaction has strongly enhanced the impact of aid on growth.

Isham and Kaufman (1999) provide a micro statement complementing the Burnside and Dollar macro thesis. Examining the productivity of Bank-supported investment projects, the authors establish that there is a strong positive relationship between 'good' ('undistorted') policy regimes (macroeconomic, trade and pricing) and the rate of return on these public investment projects. For the authors the implications for lenders are straightforward (pp.177-8):

> They would generally fare better by staying away from settings with poor economic policies ... Thus, investors from institutions like the World Bank ... should recognize that lending in settings with poor policies are likely to result in significantly lower socio-economic returns. Thus, higher selectivity, minimizing investment loans to countries with poor economic policies, as well as increasingly shifting towards non-lending activities (particularly those geared to help improve and sustain a better policy framework) would be called for in such countries.

Collier and Dollar (1999, 2001, 2002) extend the core Burnside-Dollar results that aid has no impact on growth except in a 'good' policy environment and that aid does not affect policy reform, into a prescriptive model of what 'poverty-efficient' inter-recipient aid allocations should look like.[198] In their model, a poverty-efficient allocation of aid is one in which the marginal cost of poverty reduction is equalised across recipient countries, subject to the overall aid budget constraint. Pursuing a 'two-step' approach to aid and poverty reduction (from aid to growth and from growth to poverty reduction), the authors start by revisiting the core Burnside-Dollar result for a new data set (86 countries, 1990-6) and a broader measure of policy. Using the subjective ordinal measure for policy provided by the CPIA, they confirm the premise that the efficacy of aid for growth depends on the policy environment.[199]

To this, a finding of diminishing returns to aid is added. This is combined with a maximisation exercise, where donors are projected to maximise the objective function of reducing poverty, subject to a budget constraint imposed by available aid. The scope for aid-induced poverty reduction in a country depends on its level of

[198] The three papers (Collier and Dollar 1999, 2001, 2002) convey the same argument, but the latter two versions sought to remedy technical mistakes that had cropped up in the WB Policy Research Paper (Collier and Dollar 1999). For a good account, see Beynon (2001); see also below.
[199] Collier and Hoeffler (2002) add that the interactive effect of aid and policy on growth is enhanced when a country is recovering from civil war. And Collier and Dehn (2001) emphasise that increasing aid to countries suffering from large external trade shocks also raises growth.

poverty, the elasticity of poverty with respect to income, *and* the quality of policies (determining the marginal impact of aid on growth). The authors add that there are thresholds of policy below which even the first aid dollar would not be sufficiently productive in terms of poverty reduction.

In the light of these arguments, Collier and Dollar examine the extent to which donors already allocate aid in a 'poverty-efficient' way and estimate the 'gains' in poverty reduction that would be achieved if a 'more efficient' allocation of aid materialises. Comparing an allocation based on their principle with the existing allocation of aid, the authors find that, in reality, aid declines as policy 'improves'. Yet, for an 'efficient aid-poverty mapping', aid should be 'tapering in' with policy reform. With policy believed to be exogenous to aid, the current situation then represents a significant misallocation of aid and reveals the persistent habit of donors of using aid to induce policy change (1999, p. 20). According to their calculation (Collier and Dollar 1999), an 'efficient' re-allocation of aid would imply that an additional 27 million people per year could 'rise out of poverty'.[200] Holding the current distribution of allocations constant, a four-fold increase in the total volume of lending would, however, be necessary to achieve the same poverty reduction. These findings are reproduced in AA (WB 1998a, p. 46).

In sum, the authors conclude that increasing poverty reduction efforts does *not* require increasing aid but, more importantly, requires a change in the existing allocation of aid towards those countries with a high incidence of poverty that are characterised by 'good' policy. In addition, the diminishing returns to aid imply that once aid is allocated 'efficiently', there are no additional opportunities for 'effective' aid as long as the current state of policies remains unaltered – there is no purpose in increasing aid if policies do not alter.

Dollar and Svensson (2000) further examine the argument that aid does not affect policy reform. Their findings, originally put forward in a WB working paper (Dollar and Svensson 1998), provide the backbone of the second chapter of AA and are reproduced in appendix two of the Report. Following on from the literature on conditionality explored in chapter four, Dollar and Svensson (2000) reiterate the ideas that policy formation is entirely determined by domestic political processes and that donors exercise limited leverage. Their main innovation is an attempt to provide a quantitative re-appraisal of the relative importance of the various factors affecting a

[200] This calculation is based on holding the actual aid levels for India and China constant. If the allocation were not constrained in this manner, the amount of people no longer poor after an efficient re-allocation of aid would be 51 million.

country's policy stance. On the basis of a database of 220 reform programmes supported financially by the WB and completed during the period between 1980 and 1995, Dollar and Svensson test for two (not mutually exclusive) hypotheses: first, the success or failure of reform depends on 'political economy' factors within the country attempting reform; and, secondly, it depends on factors under the control of the WB that affect programme design and execution ('Bank effort' variables). The dependent variable is a zero-one variable reflecting failure or success of an adjustment loan as determined by the Bank's OED.[201]

The political economy factors taken into account by Dollar and Svensson include: ethnic fractionalisation (as a measure of social division); democratic election; length of tenure; number of governmental crises during the implementation of the reform programme (as a measure of political instability); and the state of the macroeconomic environment (terms-of-trade, inflation, budget surplus) prior, and for the terms of trade also during, the implementation of reform. The Bank effort variables include: resources devoted to analytical work prior to reform (measured in staff-weeks); resources devoted to preparation of a loan (staff-weeks); resources devoted to supervision of adjustment loans (staff-weeks); the number of conditions; how conditions are allocated between upfront conditionality and first, second and third tranches (sequencing); size of the loan; and expected length of the programme. Supervision and preparation efforts are found to be endogenous and are instrumented for.

On the basis of a set of cross-programme regressions, the authors find that underlying political-economic variables determine reform outcomes, while variables under the Bank's control have no influence on the success or failure of reform. Successful reform is associated with democratic government and political stability,

[201] It should be noted that the OED indicator of success captures both the extent to which reforms have been implemented *and* the extent to which these reforms have managed to reduce poverty and stimulate growth in the private sector (Dollar and Svensson 2000, p. 915). As such, it simultaneously reflects both compliance with conditionality *and* programme success. Mosley et al. (2003), however, aptly argue that this is too broad a measure and that it renders the econometric results uninterpretable and unreliable. Mosley et al. (2003) perform an exercise similar to Dollar and Svensson (2000) with a dependent variable that captures only a country's compliance with conditionality without identifying the latter with programme success. Significantly, they find that adequate funding increases the probability of compliance through softening the costs of adjustment, particularly in LICs. More generally, they find that changes in the investment ratio and the rate of economic growth during the programme constitute determinants of the decision to comply with conditionality. The authors conclude that (p. 35):

> The simple recognition that these factors are affected by the short-run impact of reforms, with obvious consequences for their sustainability and ultimate success, immediately brings the design of the reform programme and the quality of the policy advice under investigation.

while high degrees of ethnic fractionalisation are bad for policy reform and long-term incumbents are not likely candidates for reform (p. 902).

The implication is that the role of adjustment is to identify reformers, not to create them. Development agencies are to devote resources to 'understanding the political economy of different countries and to finding promising candidates to support' (p. 896). This suggests a more passive role for donor agencies in selecting 'genuine' reformers and using aid programmes as a commitment device to ensure that reformers are not derailed from their mission. The responsibility for the success or failure of aid programmes rests squarely with the recipients/debtors. In the Working Paper version, Dollar and Svensson (1998, p. 22) conclude that:

> If the World Bank would like to improve its success rate with adjustment lending, then it must become more selective and do a better job of understanding what are promising environments for reform and what are not. This change is likely to lead to fewer adjustment loans unless there is a significant exogenous change in the number of promising reformers. To become more effective at supporting policy reform the agency would have to be willing to accept that this may lead to smaller volumes of lending.

Following these various arguments, there is thus no value in providing aid finance to a country characterised by what are perceived to be 'poor' policies, even if the country commits to the conditions of a reform programme. By abandoning the notion of aid as a reward for future policy 'improvement', donors, further, apparently move to a model of 'partnership'. However, with those governments that adopt 'poor' policies, 'partnerships' are not beneficial (Collier 2000).

Traditional arguments for programme aid have, nevertheless, been based on a recognition of the costs of adjustment, where aid compensates governments and their citizens for the costs of changing certain policies and institutions. Following various contributions by Paul Collier, it is now, however, argued that such a notion of costs has been exaggerated and that most reforms lead to a rapid improvement in the economy with short-term pay-offs (Collier 1997a, 1997b, 2001) – costs of adjustment are 'largely mythical' (Collier 2001, p. 72). Moreover, even if there are 'temporary' costs of adjustment, adjustment lending should not go towards meeting these, as these costs, according to Collier (1997a), tend to be borne predominantly by the higher income groups within countries – targeting aid onto those costs is distributively regressive. Yet, Collier (1997a) concedes, conditional loans can still fulfil the following constructive functions: 'restraint' – helping a committed government to resist the temptation to deviate from 'good' policy; or 'signalling' – indicating to the private sector that a government is serious about reform and the new policy regime is likely to persist (see also WB 1998a). Ultimately, if any reform is observed during the era of policy-based aid, this is due to forces inducing policy change that coincide with conditionality rather than being caused by it (Collier 2000).[202]

Chapter three of AA reiterates the basic Burnside and Dollar stance, drawing on a set of additional references regarding the fungibility of aid. Chapter four turns to issues of government. Building on the 1997 WDR (WB 1997b), the emphasis is on matching the state's role to its capability. Aid should both focus on improving the quality of the public sector as well as tailor its instruments to the prevailing state capacity with particular attention to partnerships with various non-governmental agents (both private and non-profit seeking). More specifically, attention is drawn to the possibilities of providing public services without public providers, and the special role for aid in terms of non-financial support is reiterated (WB 1998a, p. 92).

As indicated in chapters one and two, these propositions combine with arguments in favour of a knowledge role for the donor community. In those environments where reform is perceived to be unlikely, donors can make a difference without large-scale financing. For the WB (1998a, p. 45):

> The priority of the world community in these countries is to help in the domestic political and social process of policy change: that is, in contributing knowledge rather than big finance. Of course, some financial flows provide opportunities for dialogue and knowledge transfers. But aid to these economies has to be justified more for its indirect contribution to policy change than for its direct effect on poverty reduction.

The donor community should, in these countries, concentrate on 'intangible and low-cost efforts' which could promote policy reform over the long term – by disseminating development ideas, sending students abroad, training the next generation of leaders, and stimulating policy debate in civil society through seminars, town meetings, or roundtables. (WB 1998a, p. 54). This reflects the idea that in countries with 'poor' policies there are apparently large latent constituencies for policy change, and that the process of policy reform then depends on strengthening these constituencies – 'within the bounds of appropriate conduct' (Collier 2001, p.

[202] As examples of such forces Collier (2000, p. 302) points to: the 'simple experience of economic failure'; the increasing prevalence of market-assisted growth and the collapse of the socialist model; the increase in the political costs of economic failure as democratisation spread.

79). In addition, donors are, according to Collier 'obvious conduits for information on how performance differs elsewhere, and can supply the analysis that shows the *true* effects of policy' (p. 79, my emphasis; see also WB 1998a, p. 55).

Apart from raising the effectiveness of aid where aid monies are disbursed, selectivity will thus also be more effective in inducing reform in poor policy environments. The successful record of those actually receiving aid money will incite non-recipients to adopt the necessary reforms through some kind of 'demonstration effect' (Collier 1997b), while the 'skills' of the donor community in the mean time inform policymakers, parliamentarians, and other local groups of what 'good' policies and institutions consist of. As the WB (1998a, p. 19) puts it:

> In countries with reform movements donors can try to nurture them through analytical work, training and technical assistance. Such non-financial assistance remains important as reform movements develop and consolidate reform plans.

The role of an agency like the WB, then, is not to twist the arms of governments to do what they are reluctant to do but 'to disseminate information that might influence public dialogue about policy reform – and to learn to read signals about whether the governments are serious or not' (WB 1998a, p. 59). For countries yet to embrace stronger policies, the Bank has to focus its assistance on policy dialogue and advisory services.

This premium on donors' analytical capacity is further explored in Basu et al. (1998), the findings of which are summed up in appendix five of AA. The authors try to quantify the importance of the Bank's economic analysis for the quality of Bank investment projects as measured by the OED. The authors address three specific issues. First, does ESW – as an indicator of economic analysis – improve the quality of WB loans? Secondly, does the allocation of resources to ESW reduce the flow of financial resources? And, thirdly, has the Bank over- or under-invested in ESW relative to other uses of staff resources? On the basis of a set of regressions that include, on the right-hand side (RHS), staff-weeks devoted to non-lending (analytical) services as well as the Burnside-Dollar set of policies (inflation, budget surplus, trade openness), the authors find the following. First, ESW has a significant positive impact on the quality of WB projects with a one-standard deviation increase in the amount of resources allocated to analytical services associated with an increase in the probability of higher than average project quality of about 10 percent. Second, ESW, rather than having a negative impact on commitments, is associated with an increase in the volume of lending. Third, the overall quality of the lending programme would be increased by reallocating resources from supervision (future deployment of analytical capacity) towards ESW (present deployment of analytical capacity), although the data does not permit 'precise quantification' of the trade-off involved in this result.[203]

In sum, the new paradigm, according to which aid money has the desired impact of increasing growth and reducing poverty only after countries have made substantial 'progress' in reforming their policies and institutions, builds on the following string of propositions. First, on average, aid has not had a discernible effect on the growth rate. This, however, does not imply that aid has no effect on the economy but that, and second, the effect of aid has been to raise the level of consumption (public or private) rather than the level of investment – aid is fungible. Whether such an aid outcome then alleviates poverty, another objective of aid, depends on whether aid finances private and/or public consumption, as well as on the purpose of the latter. Third, aid is, on average, dissipated in government consumption and, apart from not raising growth, nor does it alleviate poverty in a 'poor' policy environment. Fourth, in a qualification of the first point, whether aid actually raises the growth rate depends on the policy and institutional environment. This relates both to the effect of policies and institutions on the aid-investment link and of their effect on the (aid-financed) investment-growth link. The description of the 'adequate' policy/institutional environment varies, but always builds on the core elements of budget surplus, trade openness, and low inflation. Fifth, aid does not buy policy reform. Sixth, 'aid-for-reform' (*ex ante* conditionality) was based on a misunderstanding of how policies and institutions change on a sustainable basis. Government policy is determined by domestic political forces, rather than by what the WB conditions its aid upon. However, seventh, in countries with 'poor' policies there are large latent constituencies for policy change, and the process of policy reform then depends on strengthening these constituencies. Hence, eighth, in such countries, donors should concentrate on activities that might support reform in the long run. These imply the dissemination of ideas about policy and development at various levels of society. Ninth, old-style (*ex ante*) conditionality no longer fits with the 'new' understanding of development, now based on 'ownership' and 'democratic process': development as a newly discovered comprehensive transformation of

[203] These findings are recycled in the 1998/9 WDR on knowledge to add strength to the argument that development agencies have an important role in creating and disseminating knowledge regarding successful policies (see WB 1998c, pp. 136-7; and chapter two).

society can no longer be imposed as a technical matter from outside. Tenth, in the past, aid (money) has not been systematically channelled to those countries where 'good conditions' prevail, hence its poor record. And finally, eleventh, if donors wish to maximise reduction of poverty, aid should be allocated to countries that have large amounts of poverty and good policy.

These ideas have been consolidated at the Bank since WB (1998a) and have been heavily promulgated beyond the institution. They were at the core of *A Case for Aid* (WB 2002a), which summed up the Bank's position at the UN Monterrey Conference, and were re-asserted by Collier and Dollar (2004) in a special issue of the *Economic Journal*. Recent appraisals of the development effectiveness of Bank programmes undertaken by its evaluation unit have, furthermore, managed to make reference to the various critiques levelled at these propositions, which are explored in the section below, while, at the same time, safeguarding the essential policy messages embedded in AA. The 2003 *Annual Review of Development Effectiveness* (WB 2004c) is illustrative. In the first chapter, it sets out three premises upon which the Bank's strategy for poverty reduction rests. These include the by now familiar mantra that, first, aid is more effective in promoting poverty reduction and growth in 'good' policy/institutional environments; secondly, that aid is neither necessary nor sufficient for 'good' policy and cannot substitute for the crucial factor, 'ownership', although it can foster and reinforce ownership; and, thirdly, that what works well in one country may not work in another and donors have a crucial role in the dissemination of knowledge about various experiences with the reform process. The review then points to the exposed weaknesses, mainly of the Dollar-Burnside findings, and proceeds, unencumbered by the various critiques, in the subsequent chapters, with the original premise of the need to allocate aid flows selectively on the basis of the CPIA, and to foster ownership in line with the prescribed policies and institutions.

Most recently the Bank has announced a new research programme on aid effectiveness.[204] Eight years after the publication of AA, the new research project builds on the findings of the latter, but distinguishes itself in two respects. First, it seeks to give more attention to issues of an 'institutional' nature and, in particular, to those related to donor design and delivery of aid programmes. This implies greater

[204] See http://econ.worldbank.org/WBSITE/EXTERNAL/EXTDEC/EXTRESEARCH/EXTPROGRAMS/EXTPUBSERV/0,,contentMDK:21073824~pagePK:64168182~piPK:64168060~theSitePK:477916,00.html.

attention to the negative effect of aid volatility (Eifert and Gelb 2005; WB 2005h, p. 104) and of donor fragmentation (Knack and Brautigam 2004; Knack and Rahman 2004; Knack 2006). The underlying stance of conditional aid effectiveness promoted by Collier and Dollar remains, however, unscathed. This transpires from its recent restatement in a set of WB Policy Research Working Papers, including: Kraay and Radatz (2005); Kenny (2006); and Dollar and Levin's (2005a) micro translation of the original Burnside-Dollar thesis.

Secondly, in an interesting development, the research on aid effectiveness undertaken in the Bank's research department (DEC) has become supplemented by a research effort on aid effectiveness located in the IFC's research department.[205] The IFC is not a dispenser of aid, but this particular research preoccupation within the Bank's private sector affiliate mirrors the changes within aid that were documented in chapter two, with the IFC is an important conduit for the dominant PSD agenda and a close collaborator for such new approaches as OBA.

Finally, the Bank's current Chief Economist, Francois Bourguignon, has been compelled to reinstate its aid effectiveness research after a damning critique of the Burnside-Dollar-Collier research in a Bank-commissioned external evaluation of its research (Deaton et al. 2006). The research is depicted as a liability to the Bank's knowledge stature as follows (p. 53):

> much of this line of research appears to have such deep flaws that, at present, the results cannot be regarded as remotely reliable, much as one might want to believe the results. There is a deeper problem here than simply a wrong assessment of provocative new research results. The problem is that in major Bank policy speeches and publications, it proselytized the new work without appropriate caveats on its reliability. Unfortunately, as one reads the research more carefully, and as new results come in, it is becoming clear that the Bank seriously over-reached in prematurely putting its globalization, aid and poverty publications on a pedestal. Nor has it corrected itself to this day.

Bourguignon (2006, p. 7) initially simply retorted that the Bank's aid effectiveness research has been very instrumental in stimulating an important debate within academia and development agencies. In a subsequent paper, however, Bourguignon and Sundberg (2007) urge that more light be shed on the chain of causality involved

[205] See Klein and Harford (2005), an IFC publication, and the corresponding IFC website entitled 'The Future of the Aid Industry: the New Debate' at: http://rru.worldbank.org/Themes/AidEffectiveness/.

in the relationship between aid and development. While the main purpose of the authors is to highlight the need to recognise the complexity and 'noise' along links in this chain, a commitment to the policy stance of selectivity – on the basis of such criteria as implied in the CPIA – persists.

5.3 Epistemology of a new paradigm

The research supporting the Bank-promoted aid paradigm has been heralded as reflecting the 'economies of scope' that purportedly characterise the Bank's knowledge advantage (Squire 2000, p. 118). It has been described as 'comprehensive', drawing on various research skills present at the WB, 'bridging' gaps between economics and the non-economic social sciences:

> macroeconomists, public finance analysts and poverty experts worked together on different aspects of the impact of aid, and these analyses were then brought together to construct an integrated view of what works, what does not and why.

Furthermore, recent alleged improvements in the growth performance of aid have been explicitly attributed to these specific research efforts. The following lengthy quote from Dollar (2001, p. 1044) graphically illustrates this:

> It is always difficult to measure the impact of research. The fact that aid allocation has improved dramatically during the 1990s can be attributed to a number of factors, such as the end of the Cold War and the reform of aid agencies. But surely research results indicating how to make aid more effective played some role as well ... The first version of 'Aid, policies and growth' was circulated in 1996; this paper showed that aid in fact did affect growth, but that its impact depended on the quality of policies. Many of the changes in the second half of the 1990s have been consistent with the argumentation developed in aid effectiveness research. Suppose we attribute to research one percent of the credit for improved aid allocation ... The efficiency of aid improved by 200 percent over the decade, so we are basically ascribing to research a 2 percent improvement in the efficiency of aid. Was the money spent on research a good investment? Starting from the 1990 level of efficiency, a one-time 2 percent improvement in the efficiency of aid would lift an additional 120,000 people out of poverty in the first year. The WB spent about $1 million on all of its aid effectiveness research, including the publication of AA and

> worldwide dissemination. The efficiency of ODA in 1990 was about 100 people lifted out of poverty per million dollars. Thus, the return on research in the first year was 120,000 percent of the return on the typical aid dollar of 1990. And of course one of the special features of knowledge creation is that it can be used year after year with no additional knowledge generation costs. So, the productivity of research would actually be many times the rough estimate produced above.

Yet it is documented below how the 'knowledge' principle in the context of aid is supported by a remarkably poor research and knowledge exercise. First, it draws on mainstream economic literature in unsatisfactory and notably ad hoc ways. Secondly, it fails to live up to basic standards of econometric practice or to sustain its own conclusions once samples, definition of variables, or controls are altered. Thirdly, the research in no way exploits the oft-cited Bank advantage in terms of access to detailed country-specific information as it is characterised by a particularly deficient rendering of the empirical realities of aid.

The research is, nevertheless, typical of the Bank, particularly in its excessive insularity and its failure to engage with criticism, even with such criticism that remains within the remits of frameworks readily understandable by Bank researchers (see also chapter two). Morrissey (2000, p. 373) observes:

> AA does not adequately take stock of what is known and what is not known about the macroeconomic impacts of aid. Important elements of what was and is known ... are not mentioned. Sometimes this results in a tendency to reinvent the wheel, as in so called 'new' evidence on fungibility, but other times the tendency is to misrepresent the evidence, as in whether aid effectiveness is conditional on good policy. It is right that the Bank should contribute to the debate. If it is to do so, it is only reasonable to expect that its researchers keep abreast of what is being done outside Washington, and perhaps most saliently, outside of the US.

Still, as is documented in a subsequent section, the Bank-sponsored research on aid did set the terms of the latest debate on aid. This gave rise to a research project that is ill-defined around technical issues such as functional form and econometric technique and that bypassed serious reflection on first principles of theorising and model-building. As a result, a new economics of aid consolidated itself, anchored in a new growth theory framework and with a characteristic predilection for quantitative technique. This literature, however, can be typified, following Roodman

(2004), as constituting a small and unsystematic sampling of the specification space around Burnside and Dollar (2000a), which reveals itself to be generally fragile and provides few meaningful conclusions regarding aid and growth.

Furthermore, the failures of the aid impact analysis identified in the previous chapter persist. The new propositions perpetuate the characteristic inadequacy of the 'old', which had failed to capture systematically the structural features within which the aid phenomenon takes form and which determine its outcomes. Following broader changes in neoclassical economic theory – significantly the manifold extensions around a growth equation – the aid effectiveness literature simply proceeds by bringing in a further host of additional variables. Yet again, statistical significance supersedes economic understanding and theorising around aid and growth is reduced to the search for the best fit of a particular regression. Shaky results are promoted once they conform to the researcher's preferred understanding regarding aid and growth.

5.3.1 The new aid paradigm and model specification

In the two-gap model, low domestic savings and/or inadequate foreign exchange earnings constrain the level of investment. In the context of limited access to private foreign capital, aid has the role of filling 'financing gaps', allowing the target rate of growth to materialise. The original empirical work on aid and growth focused on capital accumulation, and its structural framework mainly relied on a HD growth model (see chapter four). In the 1990s, however, the emphasis shifted from investment to incentives, from capital to underlying institutions and policies (Easterly 1999). New growth theory emerged and, with it, a whole set of new possibilities for theorising about and empirically investigating the aid-growth relationship.

The exercises performed by David Dollar and associates emerge from the set of growth equations that seeks to test for conditional convergence of cross-country (per capita) growth rates. More specifically, the Burnside-Dollar specification is situated amongst those growth specifications that extend the original Solow-Swan approach by parametrising the state of technology (A) in the production function: Y= F(K, N, A), with N=HL, and N effective labour input, L the quantity of labour input, and H the stock of human capital embodied in the labour force. Commonly referred to as total factor productivity, 'A' captures that part of output change not accounted for by changes in inputs and is affected by the efficiency with which countries use capital and labour inputs, by resource endowments, and by other socio-economic or socio-political ('structural') variables such as, most recently, institutions, culture, thrust, religious affiliation, etc. In the original version of the Solow model, cross-country differences in this variable are assumed to be exogenous. The original Solow model then implies that, with free flowing capital and technology, the output per capita gap between countries will be closed ('absolute convergence'). This contention is 'tested' by regressing the growth rate of per capita income on earlier levels of per capita income, together with other Solow baseline variables (such as country-specific savings and population growth rate controls). Upon this, augmented growth regressions, known as Barro-type regressions (Barro 1991) developed, incorporating the notion that additional (independent) variables are bound to affect the growth performance across countries. These aim to 'test' for 'conditional convergence' – contingent on these additional 'controls'. Such regressions, at the same time, became perceived as providing a means for the 'quantitative measurement' of the effect of each of these supplementary and independent 'causal' factors of growth.

For Burnside and Dollar (2000a), convergence is mediated by: a set of initial conditions; an 'incentive' regime (policy); levels of aid; and regional features. The main purpose of the exercise is to measure the importance of a well-defined set of policies for the impact of aid on growth. The primary Bank reference, however, falls prone to two major biases. First, it reproduces the fundamental failings of the parent literature upon which it draws (new growth theory). Additionally, it is oblivious to the spectrum of possible outcomes – contingent on different specifications – that emerge when bringing aid into a new growth framework. We consider each in turn.

First, despite the ambition of new growth theory to provide an economic explanation for technological change or to incorporate 'real-world' economic features such as increasing returns to scale or traditionally 'non-economic' variables including institutions and culture, new growth theory, and hence an analysis of aid anchored therein, confronts a set of fundamental problems. Fine (2003) points out how new growth theory shares certain weaknesses with its predecessor and throws in a few of its own. New growth theory remains vulnerable to the Cambridge Critique and it remains organised around a SSBG description of growth, even if capable of generating multiple equilibria as well as complex paths out of equilibrium. More idiosyncratically, new growth theory has to confront the following issues: the reductionist and ahistorical character implied in its conceptualisation of the relationship between traditionally 'non-economic' variables and growth; the opportunistic manipulation of conclusions provided by other literatures on productivity change; the projected relationship between the micro and the macro; and the common, rather intractable, nature of its own models (Fine 1998). Finally, Fine's (2003) portrayal of new growth theory as reflecting a strong commitment to the power of policy as economic and social engineering, with its empirical work claiming to measure the impact of a wide range of interventions, is particularly familiar in the context of the current aid debate, where a particular policy direction (selectivity) is accounted for, even if hazardously, on the statistical significance of a coefficient in a growth equation.

In addition, Barro-type regressions suffer from a set of specific shortcomings. The equations suffer from 'open-endedness' and concomitant instability, as there is a myriad of ways in which they can be augmented,[206] and no robust mechanism has as yet been developed to determine which variables to include or not.[207] A major problem with the methods to establish robustness of a control variable, according to Durlauf and Qauh (1998, p. 31), is that 'they attempt to use mechanical statistical criteria in identifying factors whose interest and plausibility is motivated by economic (or social science) theory'.[208] For Durlauf and Quah (1998) it is, further, unclear what exercise a researcher conducts by adding a particular control variable, even when the variable is motivated by a particular economic theory. The authors observe that (p. 29):

> The basic Solow-Swan model admits an immense range of extensions through factors such as inequality, political regime, or trade openness. These are often highly correlated with one another, and are neither mutually exclusive nor prioritised as possible explanations of growth. Hence it is difficult to assign much import to the statistical significance of an arbitrarily chosen subset of possible controls.

Another problem with this kind of growth equation is the assumption of parameter homogeneity, when a cross-section data structure imposes the assumption that the parameters describing the growth experience are identical across countries. In addition, these growth accounting exercises are prone to problems of endogeneity,

[206] Durlauf and Quah (1998, table 2) provide a list of variables that have been included across various such exercises.
[207] On the shortcomings of the robustness tests proposed by Levine and Renelt (1992) and Sala-I-Martin (1997), see Brock and Durlauf (2001) and Fine (2003).
[208] On the lack of economic theory underlying various extensions to the growth equation, see also Solow (2001) and again Fine (2003).

casting doubts on the inference of causality from the independent to the dependent variables. The problem of endogeneity is often addressed through the use of instrumental variables (as is the case of Burnside and Dollar 2000a). However, Brock and Durlauf (2001, p. 238) note that the use of instrumental variables estimation does not often satisfactorily address the endogeneity problem due to the persistent problem of the open-endedness of the growth equations. The use of instrumental variables presupposes that the correlations between the instruments and all omitted growth determinants are (in total) negligible, an assumption difficult to defend when omitted growth determinants are neither specified nor evaluated. The equations also usually impose a linear structure, which rules out interactions between different determinants or even between a determinant and its own initial value. For Rodriguez (2006, p. 3):

> A systematic exploration of the theoretical foundations of the linear growth specification reveals that the set of assumptions necessary to justify fitting a linear function to the data is so restrictive as to practically make the linear specification the true theoretical curiosum.

He adds that existing methods for handling non-linearities, for instance through the addition of multiplicative and interaction terms, are inadequate when the form of the non-linearity is not known *ex ante*, and concludes on the following note (pp. 23-4):

> once we recognise the true multi-dimensionality of the growth process, existing data is clearly insufficient to allow us to understand it in a statistical sense ... (T)he cross-county empirical growth framework may not be a particularly adequate one for conducting analysis on the growth effects of policies. Attempting to use it in this way amounts to trying to make the data say more than it can.

Second, there are specific problems that emerge when analysing the economics of aid in a new growth framework. In general, the role of aid in new growth theory is not as clear-cut as in the HD framework and depends on a host of factors. First, the projected impact of aid depends on whether growth is endogenous or exogenous; and, if the former, how growth is endogenised and whether aid interacts with endogenous variables. Secondly, it depends on whether 'structural' features have been modelled to affect the growth rate and whether aid interacts with these. Thirdly, it depends on whether the economy is on a steady-state growth path or in transition to it. Fourthly, it depends on the particular description of savings/consumption behaviour of economic agents. Are savings a constant fraction of income (possibly also subject to a subsistence consumption constraint (the 'poverty trap' model)) or the result of an optimisation process on behalf of consumers? In the latter case, is this behaviour described in the context of an infinite horizon model or an overlapping generations model?[209] Fifthly, it depends on whether aid is perceived as permanent or temporary, and on whether aid (per capita) grows over time or is constant.

These various issues raise specific problems for the Bank-promoted propositions regarding aid and growth. These have been documented at length in the literature. What follows is a succinct summary with a focus on the primary Bank reference, Burnside and Dollar (2000a), from which the other propositions promoted through AA derive.[210]

First, consider the issue of open-endedness. For what their exercises are worth, Levine and Renelt (1992) and King and Levine (1993) find that only a few variables, including the investment share, secondary school enrolment rate, initial level of income and financial indicators robustly affect growth. Burnside and Dollar (2000a) omit all these variables except for initial per capita income and a measure of financial depth (M2/GDP). To the extent that any of these omitted variables is correlated with any of the included independent variables, coefficients are biased. In particular, attention has been drawn to the omission of investment in the Burnside and Dollar (2000a) specification of growth. In Burnside and Dollar (2000a), aid adds to investment (depending on policy) and policy determines the productivity of investment. As such, the aid-policy interaction term is included, while investment is excluded. Yet, the implicit growth theory has investment, not aid, as its argument. Furthermore, we know that not all aid is intended for investment and that not all investment is aid-financed. Omitting investment implies misspecification and causes the aid coefficient to be biased (downward – as a significant proportion of aid is not used for investment). Gomanee et al. (2005a) regress both aid and investment (amongst a number of other variables) on growth. Using the technique of generated regressors to address the attendant identification problem due to double counting, the authors find, for 24 countries in SSA (1970-1997), a consistent positive effect of aid on growth, mainly through aid-financed investment: on average, one percentage point increase in the aid/GNP ratio adds one third of a percentage point to the growth

[209] See Dalgaard et al. (2002, p. 4).
[210] The references drawn upon in this section are likely to be prone to the critiques of new growth theory provided above. They do, however, cast doubt on the Burnside-Dollar result 'from within' as they emerge from the same underlying framework and, as such, should have been readily understandable to Bank researchers.

rate. Durbarry et al. (1998, p. 4) further examine the growth impact of aid within a model that includes policy variables and all major sources of investment finance (foreign aid, private and other inflows, and domestic savings). With their specification, which includes aid^2 but not the aid×policy interaction term, and on the basis of both cross-section and panel regressions, they find aid to have a significantly positive effect on growth (p. 18). For the authors, inclusion of policy variables provides a more fully specified model, but the aid-growth effect does not depend on it. Akhand and Gupta (2002, p. 56) also point to the absence of such important determinants of growth as investment or savings in the Burnside-Dollar equation, and wonder about the ability of Burnside and Dollar's equation to explain any growth. The authors find no robustly significant relationship between the interaction term and growth, and suggest that the Burnside and Dollar result of a significant and positive relationship stems from the exclusion of the investment share in their growth regressions.

Secondly, take the particular issue of the inclusion of the policy variables, which are transformed into a policy index. In the first instance, the nature of the relationship between inflation, trade openness and growth is subject to debate (see chapter three), and a linear equation might constrain the behaviour of the relationship as it badly accommodates possible threshold effects that might characterise this relationship. Inflation's relationship to growth, for instance, is likely to be non-linear, with excessive levels of inflation bad for growth, but low inflation not necessarily good for growth (see Stiglitz 1998a). Additionally, two of the policy variables (inflation and budget surplus) are measures of outcomes rather than policies. Further, Lensink and White (2000b) discuss various problems regarding the measurement of the trade policy indicator in Burnside and Dollar (2000a). This includes the existence of various types of trade policy indicators, possibly uncorrelated, with results regarding the impact of 'openness' on growth depending on the particular measure used (Pritchett 1996). The Sachs-Warner trade index used by Burnside and Dollar (2000a) combines various elements of trade policy into a zero-one dummy classification. The use of a measure based on a combination of trade policy elements, however, further diminishes the capacity to gain insight into the trade-growth relationship, with different components of the trade policy index possibly having varying effects on growth (Lensink and White 2000b, p. 9).[211] Easterly (2003) uses alternative measures for trade openness (black market premium or trade to GDP

[211] See Rodriguez and Rodrik (2000) for a discussion of binary openness indices.

ratio) and finds the interactive term of aid and 'good' policy to be no longer statistically significant. Finally, Burnside and Dollar (2000a) construct their policy index on the basis of the coefficients of inflation, budget surplus and 'trade openness' from the base growth regression, in which the aid ratio is excluded, as respective weights in a linear combination. Yet, the weights are likely to differ between countries and the growth regression from which the weights are obtained suffers from omitted variable bias as it excludes a whole possible set of other determinants of growth.

This brings us, thirdly, to issues that arise from the incorporation of the aid×policy interaction term. Burnside and Dollar (2000a) introduce the policy term both independently and in interaction with aid, the purpose being to capture the effect of policies both on how aid translates into investment (or consumption) (fungibility), as well as on the impact of this investment, if any, on growth. However, Dalgaard and Hansen (2001) observe, any variable that changes the marginal productivity of capital could be included in interaction with aid. Chauvet and Guilllamont (2001) test for the performance of an interaction term that incorporates external and climatic factors (terms of trade trends, real value of exports instability, climatic shocks), and compare it to the performance of the Burnside-Dollar policy index. From a cross-section (66 countries) over two twelve year pooled periods (1970-1981 and 1982-1993), they find that aid effectiveness is strongly influenced by these exogenous external environment factors, but not by policy. In a similar vein, Mosley and Hudson (2001) recommend shifting the focus away from economic policies towards governance indicators if the purpose is to capture elements that affect aid effectiveness – a recommendation echoed in Burnside and Dollar (2004b). In addition, Dalgaard and Hansen (2001) demonstrate how, within a neoclassical growth framework, the interplay between aid and policies can be ambiguous. With aid and 'good' policies as substitutes in a growth model in which firms face a 'risk of destruction', according to which part of production can be destroyed because of social unrest and which is inversely related to consumption levels (potentially financed by aid), 'good' policies can do much to reduce the marginal impact of aid on growth (Dalgaard and Hansen 2001).

Fourthly, questions have been raised regarding the use of the aid×policy interaction term as a way of modelling non-linearities in the aid-growth relationship. In the recent aid effectiveness literature various reasons are provided for suspecting the aid-growth relationship to be non-linear. These include: Dutch disease features

(Durbarry et al. 1998); institutional destruction and inappropriate technology (Lensink and White 2001); diminishing marginal returns (Hansen and Tarp 2001); and synergy effects of, for example, economic policy on aid effectiveness as included in Burnside and Dollar (2000a). However, most of these non-linear effects have been incorporated in the regression through a second order aid term, in contrast to the inclusion of an aid-policy interaction term in Burnside and Dollar (2000a). Hansen and Tarp (2001) clarify that both aid squared and interaction terms may arise as a result of a second order approximation of a standard Solow growth model. Hence, the use of a non-linear aid-growth specification does not have to be justified on the basis of, for example, policy distortions, but may simply reflect increased precision in the approximation of the functional form (p. 550). The preferred formulation of non-linearity then becomes an empirical issue:

> Statistical significance of the synergy effect between aid and policy, on the one hand, and decreasing marginal returns to aid on the other, can – and should – be evaluated within the same regression model.

Hansen and Tarp (2000) proceed by estimating a general model encompassing the two contesting formulations (including aid^2 versus the aid$\times$policy interaction term) as special cases that can be obtained through parametric restrictions. They find both aid and aid^2 to be significant, and the interaction term (aid$\times$policy) and policy^2 to be insignificant. These results are robust to the exclusion of the outliers as well as to instrumental variable estimation (p. 398). Beynon (2001, p. 24) reports how Burnside and Dollar responded by demonstrating that adding the aid^2 and policy^2 variables to their model strengthens their own results, in that the magnitude and significance of the positive coefficient of the aid$\times$policy interaction term is increased. This is due to their inclusion of an aid$^2\times$policy variable (ignored in Hansen and Tarp 2000), which according to the authors is consistent with a model of diminishing marginal returns, and if ignored renders the model inappropriate. In a reply, Hansen and Tarp (2001) retort that the latter comment is not central to their critique and they proceed with their challenge of the original synergy result by pointing to shortcomings in Burnside and Dollar's identification of outliers and choice of instruments (see below).

Fifthly, the extension of the Burnside and Dollar aid premise into the aid-poverty realm as proposed in Collier and Dollar (2001, 2002) is problematic. In Collier and Dollar (2001, 2002), poverty reduction is solely a function of growth and aid enters the equation via its effect on growth. However, the insufficiency of a growth orientation for poverty reduction has been well established (see Healey and

Killick 2000), and there are ranges of interventions (often aid-supported) that can directly affect poverty and other welfare indicators without necessarily affecting growth (see Lensink and White 2000a; Beynon 2001; Mosley and Hudson 2001; Mosley et al. 2004; Gomanee et al. 2005b, 2005c). Gomanee et al. (2005b, 2005c) find that aid is associated with lower infant mortality when it finances public expenditures that increase welfare indicators (such as health, education, water or sanitation) (see also Mosley et al. 2004). This effect is greater in countries with lower original levels of human development indicators. Hence, irrespective of whether growth is pro-poor and of whether aid contributes to such growth, there are ways in which aid can contribute to welfare. This is in contrast to Burnside and Dollar (2000b), where it is argued that aid does not on average lower infant mortality. Gomanee et al. (2005b) further find no evidence that economic policies are necessary to ensure aid effectiveness or to contribute to human welfare.

5.3.2 The new paradigm and quantitative technique

Apart from issues around model specification, the Burnside-Dollar exercise is plagued by severe problems of quantitative technique. First, the Burnside-Dollar premise is highly sensitive to sample. Easterly et al. (2003) re-run the original Burnside and Dollar (2000a) specification, but extend the sample to include more recent observations (adding 1994-97) and additional countries. They find an insignificant coefficient on the interaction term between aid and policy.

Second, the Burnside-Dollar result depends on the exclusion of what Burnside and Dollar (2000a) refer to as 'outliers'. Questions regarding the way in which these outliers were selected, however, remain unresolved (Hansen and Tarp 2000, p. 391; Dalgaard and Hansen 2001, p. 28). Dalgaard and Hansen (2001) note how the five excluded observations are the extreme values of the aid×policy interaction regressor. However, the authors continue, such points are not considered as outliers in classical regression analysis, but are possible leverage points. For the authors (p. 32):

> Of course, they may be deleted if the information they convey is considered to be different from the rest of the observations. But this deletion rule is ad hoc and it is rather odd to limit the variation in the central regressor in this way.

Using the Burnside and Dollar dataset, Dalgaard and Hansen (2001) illustrate how excluding five alternative outliers with high influence produces a regression with a positive impact of aid on growth and an insignificant aid×policy interaction term.[212] Dollar retorts that the latter result is obtained on the basis of a different measure of aid (ODA rather than EDA), and that it is hence not comparable to the Burnside and Dollar (2000a) result (reported in Beynon 2001, p. 23). However, such a response only shifts the problem, as it indicates that the Burnside-Dollar result might not be robust to a change in the definition of aid (see below).

Third, Easterly (2003) highlights how the result is not robust to a change in the period over which the growth variable is observed. Substituting observations for real GDP growth rates over four years, by observations over eight, 12 and 24 years, the coefficient on the interaction term between aid and policy is not significant for the periods of 12 years and the cross-section of 24 years.

Fourth, the Burnside and Dollar result is sensitive to the definition of aid. Easterly (2003) replicates the Burnside and Dollar (2000a) exercise using the ODA measure of aid rather than EDA, and finds that, even though the EDA and the traditional ODA measure of aid are highly correlated,[213] the Burnside-Dollar premise fails to appear (see also Dalgaard and Hansen 2001). In addition, Clemens et al. (2004) point out that it makes little sense to measure the impact of an aggregate aid measure on growth of a relatively short (four-year) period. There are various types of aid, and the way these impact on growth as well as the time spans it takes for these effects to appear are likely to differ across categories. Clemens et al. (2004, p. 12) distinguish three broad categories: humanitarian aid, short-impact aid, and long-impact aid.[214] Once aid-growth equations focus on the types of aid that can reasonably be expected to cause growth over a four-year period ('short-impact aid'), they find a very strong, positive and robust relationship to growth, independent of the policy or institutional environment of the country.[215] Ram (2004) splits the aid

[212] Collier and Dehn (2001) claim that allowing for external trade shocks reinstates the robustness of the Burnside-Dollar result to the exclusion of outliers. However, see Roodman (2004) on the problems with the measure of external shocks used by Collier and Dehn (2001).
[213] Knack and Brautigam (2004, p. 14) find a correlation of 0.98 between both measures as a share of national income.
[214] For Clemens et al. (2004, p. 13), short-impact aid comprises budget support and project aid for investments in infrastructure, transportation, communications, energy, banking, agriculture or industry. TC and most social sector investments, including in education, health, population control and water are classified as long-impact aid. And humanitarian aid includes emergency assistance and food aid.
[215] It has been noted in chapter four that lumping different forms of aid together in one aggregate measure is likely to imply parameter instability in both cross-section and time-series regressions of aid on growth. The productivity of aid varies from to place to place, and in the same place at different points in time, as the composition of aid is different across time and place, and different forms of aid have a different impact on growth with a different lag structure (see also Lensink and White 2000b).

variable into the components coming from bilateral and multilateral donors which, again, eliminates the key Burnside-Dollar result.

Fifth, introduction of country-specific dummy variables (fixed effects) alters the conclusion on aid-policy interaction in aid-growth relationships (see Lu and Ram 2001; Hansen and Tarp 2000). Sixth, the Burnside-Dollar result is sensitive to instrumentation strategy used to tackle endogeneity (see Hansen and Tarp 2001; Roodman 2004, pp. 7-8; Rajan and Subramanian 2005).

Seventh, with regard to observations of fragility in the quantitative assessment of the aid-growth relationship, as epitomised in Burnside and Dollar (2000a), Hansen and Tarp (2001, p. 554) caution against evaluations of aid effectiveness based on the statistical significance of aid variables in regressions that do not reflect established theoretical or empirical results (see also Deaton et al. 2006). The authors note that a minimum requirement should be the ability to explain why models yield different results before wide-ranging conclusions are drawn. From that perspective, they point to a particular problem in Burnside and Dollar (2000a) in the context of the empirical growth literature. This relates to the insignificance of the log of initial level of income across their various estimations. This would mean that there is no statistically significant conditional convergence among the 56 countries in the sample. Hansen and Tarp remark how this is at odds with a large literature. However, while there might be good reasons for not finding conditional convergence among the countries in the sample, these reasons must be explored and explained before drawing any policy conclusions.[216] For Hansen and Tarp (2001, p. 554), Burnside and Dollar (2000a) then provide yet another example of 'regressions in which too much emphasis is placed on aid and too little on proper modelling'.

Eighth, there is a fundamental problem with the common implication across the Bank references that improvements in policy as measured by an increase in the policy index produce a measurable improvement in the growth effect of aid. This relates to the ordinal character of the policy index (whether constructed along the lines proposed by Burnside and Dollar or when based on CPIA scores). In AA, it is asserted that the marginal effect on growth of a one percent increase in aid is –0.3, 0, and 0.5 respectively for poor, mediocre and good policy environments.[217] Apart from the issue raised by Akhand and Gupta (2002, p. 59), that the values assigned to

[216] See also Akhand and Gupta (2002, pp. 55-6) for a similar point.

[217] For the sample in AA, the policy index has a mean 1.1 with a standard deviation of 1.6. A value equal to the mean of the index is considered to represent mediocre policy, while the mean and one standard deviation (2.7) is considered good policy; poor policy has an index of zero (WB 1998a, p. 122).

different qualities of policy, here zero, 1.1 and 2.7 are arbitrary (there is no reason why a value equal to the mean and one standard deviation should be characterised as 'good' policy) and are entirely dependent on the sample, the problem of ordinality precludes such inference.

Finally, a comment is in order regarding the understanding of good practice and academic honesty at the highest level of Bank research. Consider the empirical trajectory of the coefficient on the quadratic term in Collier and Dollar (1999, 2001, 2002), a parameter of crucial significance in Collier and Dollar's proposition as it constitutes a necessary condition for their maximisation problem to be bounded and hence for their method of determining a poverty-efficient allocation of aid across countries to be useful. Yet, in their original exercise, Collier and Dollar (1999) are faced with the rather inconvenient result of an insignificant coefficient on the quadratic term. They seek to remedy this by extracting a value for the coefficient from a different econometric exercise, namely from a regression result obtained by Burnside and Dollar (1997). It seems of no import to the authors, however, that the Burnside and Dollar result, apart from being riddled with problems of its own, is obtained for pooled regressions for different time periods and for different countries as compared to their own regression. Furthermore, the core variable, the policy index, is specified in a different way across the two exercises.

Criticism of this rather embarrassing flaw prompted the authors to find another way of establishing their much-needed result of diminishing returns (see Beynon 2001). The authors now proposed to 'retro-construct' a CPIA data-set going back as far as 1974. Their revised exercise then covers the period 1974-97, rather than just 1990-1996, which, with an increased number of observations, produces the necessary negative coefficient on the quadratic term (Collier and Dollar 2001).

Nevertheless, even though such an alternative seeks to make the coefficients internally consistent, being the result of the same dataset and regression, it is riddled with problems of its own. First, although the WB has produced annual country policy ratings for most countries since 1977, the set of criteria, the weight attached to each component, and the scoring scale, have changed dramatically over time (see chapter six). This renders any attempt at constructing a consistent time-series futile. In Dollar and Levin (2004), the CPIA-measure is abandoned when conducting 'historical' analysis as, by the authors' own admission, it is not available in a consistent format back in time (p. 13). Furthermore, in a footnote in an update report by the Bank on adjustment lending in Africa, it is observed how the performance ratings before 1995 are not comparable with later ones (WB 1998b, p. 9). These objections do not even touch on the fact that Collier and Dollar must themselves have attributed the scores for the years 1974 to 1977, as there was no CPIA-style practice at the Bank prior to 1977. Secondly, the CPIA was designed to assist in the allocation of aid flows and not as an input in econometric exercises regarding the relationship between aid and growth or poverty (see Herman 2004, p. 13; and chapter six). CPIA scores reflect subjective assessments that are likely to reflect 'contemporaneous bias', where country analysts might more easily assume that countries with rapid growth are characterised by what the Bank perceives to be 'good' policies (WB 2001i, p. 17; Dalgaard et al. 2004). Dalgaard et al. (2004, p. 210, my emphases) observe that:[218]

> If the CPIA index is Granger-caused by growth it should not be used as an exogenous variable in forecasts and policy simulations. *This rather obvious, and well-known, result* is unfortunately not discussed neither in Collier and Dollar (2001, 2002) nor in the documents by the IDA and DFID.

Thirdly, the CPIA output data had not as yet been released outside of the Bank, which made verification of the results obtained on the basis of the data-set impossible.[219] Finally, the results of Collier and Dollar (2001, 2002) are highly sensitive to sample and specification (see Beynon 2001, pp. 15-16).[220] And using Collier and Dollar's own model, Beynon (2001) finds that the greatest overall reduction in poverty is achieved by re-allocating aid on the basis of poverty rather than in accordance with policy criteria.

5.3.3 AARIA: value added through case studies?

The Bank's selectivity stance has been propped up not only by the econometric exercises commented upon above, but also by a set of case studies with a focus on the alleged ineffectiveness of conditionality. These are summed up in an edited volume, AARIA (WB 2001a). In a restatement of the Bank's ideas regarding aid and conditionality, Collier and Dollar (2004, p. 258) draw attention to the

[218] It could be noted that Gelb et al. (2004) have tried to remedy this, in somewhat belated fashion, by regressing year to year changes in the CPIA scores for the period 1996-2002 on growth rates of the previous year. They report no significant relationship, although no results are provided.

[219] This raises the issue as to how a peer-reviewed journal published the Collier and Dollar proposition, given that the underlying data were not available to anyone outside the World Bank and that, as a consequence, the results of the quantitative exercises could not be verified or challenged.

[220] Lensink and White (2000a, p. 405) find an estimate of the turning point about 3 times higher than the turning point proposed by Collier and Dollar (1999). For other estimates of the turning point that are much higher than the estimate by Collier and Dollar, see also Durbarry et al. (1998); and Hansen and Tarp (2000).

importance of case study material in support of the arguments obtained on the basis of large-scale econometric exercises, as follows:

> While the econometric studies are useful for summarising regularities in the data, they cannot have the richness of institutional and historical detail that one gets in a good case study.

Collier and Dollar add that while a risk with case studies is that clear generalisations may not easily be made, in AARIA a consensus on a range of issues seems to have readily emerged (p. 258). Collier and Dollar (2004) thereby refer to the ideas summed up in the overview (Dollar et al. 2001) that precedes the collection of cases in AARIA, and it is about the relationship between this overview and the lessons projected by the various cases that a few comments are in order (see also Tarp 2001).

AARIA brings together accounts of the experience of aid and policy reform in ten African countries. These are subdivided into 'successful reformer' (Uganda and Ghana), 'post-socialist reformer' (Ethiopia, Mali, Tanzania), 'mixed reformer' (Cote d'Ivoire, Kenya and Zambia) and 'non-reformer' (DRC and Nigeria). The case studies seek to assess three hypotheses: first, countries choose to reform or regress independent of aid; second, non-financial aid (TC, advisory services, and analytical work) has a better impact than financial aid on the generation of policy reforms in 'bad' policy environments; third, financial aid works when policy reforms and institution building are underway.[221]

Leaving aside for the moment the accounts of Nigeria and the DRC, each of the case studies confirms the importance of financial assistance for reform. With regard to the successful reformer, Ghana, we read how (p. 89):

> Ghana's experience shows that aid was an important part of the decision to reform as the government anticipated that aid would enable it to meet its economic and political objectives.

It is reported that 'it is unlikely that [the government] would have generated reforms in the absence of finance' (p. 89). Significantly, aid 'allowed Ghana to escape the potentially contractionary effects of a reduction in absorption' (p. 84). For the other successful reformer, Uganda, the case study finds that funding was needed for almost every reform and that most reforms implemented in Uganda could not have been implemented without donor support (p. 139). And, although it is conceded that non-financial assistance was important, the conditionality linked to financial support

[221] For the terms of reference of AARIA, see http://www.worldbank.org/research/aid/africa/tor.html#references.

probably had 'an even greater impact on the reform efforts' and 'many reforms were driven by the requirements of conditionality' (p. 136).[222]

Yet in Dollar et al.'s (2001, p. 20) summary of the case findings, we learn that the success of Uganda's reform programme can to a large extent be attributed to non-financial assistance. Apparently, Ghana, Uganda and *Vietnam* were able 'to engage in policy learning without a massive aid relationship' (p. 26).[223] More exactly (p. 28):

> large-scale finance has, if anything, a negative effect, reducing the need to reform; and conditionality has typically failed in the absence of a serious domestic movement for change. Technical assistance and policy dialogue, on the other hand, have helped governments and their civil societies learn about policy from neighbours and from their own experimentation.

Nevertheless, even for the countries categorised as less successful reformers, the case material provides ample evidence of the influence of financial aid on policy reform. In the case of Ethiopia, it is observed that (p. 203):

> It is fair to say that many of the structural reforms would not have been considered seriously, much less fully implemented, without the infusion of substantial policy loans and grants.

For Mali, 'the experience ... does seem to show a real influence of aid on reform, but with both successes and failures' (p. 258). From the Tanzanian study we learn how the generation of reforms has largely originated with the IFIs or donors 'the content of policy has largely been the standard structural adjustment package, with limited original input by Tanzanians' (p. 338). And more explicitly: 'aid has clearly exerted two kinds of influence in Tanzania: on the supply of external resources, and on policy formation' (p. 341). For Cote d'Ivoire it is confirmed that (p. 443):

> Until the mid-1990s at least, donors conceived, designed, financed, helped implement, and evaluated the vast majority of reforms. Certainly there were more reforms, and probably better ones, because of the aid presence.

Significantly, the authors of the latter case raise the following questions (p. 444):

> Can it be seriously argued that the government introduced, independent of aid relationships, the reforms in trade policy, in labour market operation, in

[222] See also for Ghana (p. 83):

> Notwithstanding the importance of WB economic analysis in the mid-1980s, given the financial constraints at the time, financial aid was clearly crucial and more important in sustaining the program ... While some of the technical work may have helped to persuade officials on particular issues, this would have been a hollow victory in the absence of financial resources that they could use to revive the economy.

[223] One can but wonder why Vietnam figures in an overview summarising the conclusions of case studies on aid and reform in ten African countries.

> liberalisation, and in privatisation (especially in areas of hard-core domestic opposition such as cocoa and coffee marketing and maritime transport?) Can it be doubted that such progress as was made would have been much smaller without donor ideas, pressures, and money?

Their reply, however, is surprising if not revealing: '(t)he hypothesis that aid has had no effect on reforms can perhaps be partially *resuscitated* by framing it more restrictively' (p. 444, my emphasis). While this at least candidly exposes the eagerness, within potential limits, of the authors to confirm the set of preconceived ideas held by the editors – i.e. that aid money does not buy policy reform – Tarp (2001, p. 351), in a commentary on the study, wonders whether a more appropriate reframing of the book would not simply 'resuscitate' the view that aid does affect reform, given that the book brims with evidence that aid did influence policy in a wide variety of ways, from country to country and over time.

Finally, a few comments are in order regarding the choice of 'non-reformer' states in AARIA. Nigeria and the DRC are singled out as examples of non-reformers in the context of particular aid regimes. In both countries, however, aid resources have been much less important compared to the rest of the sample, or the average African economy. This raises the issue of sample selection bias and throws a question mark on the importance of the aid-reform axis in an account of economic performance.[224] Furthermore, trying to extrapolate lessons regarding aid and reform in the context of a country subject to rapacious resource exploitation and the complete collapse of economy and state, as was the case for Zaire/DRC, borders on the cynical. Still, the account of Nigeria in AARIA provides evidence for the persistent leverage IFIs exercise on the country, now through their role in debt rescheduling (p. 650):

> The choice to adopt the Bank-Fund type of adjustment was not necessarily made because the Nigerian government and people had faith in that model's superiority over alternative ones. Rather, it was made principally because of the leverage exercised by the IFIs. That leverage stems from their ability to provide a basis for debt rescheduling, and therefore to provide the government with the direly needed fiscal space to operate.

Or again (p. 663):

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[224] For both countries, the EDA/GDP ratio is the lowest of the entire sample, with 1.88 for the DRC and 0.11 for Nigeria, compared to an average of 14 for SSA; aid (EDA) per capita is US$ 1.4 for Nigeria and US$ 4.9 for the DRC for the period 1994-97, while the average for SSA for the same period is US$ 32.2 per person (WB 2001a).

Without this kind of binding constraint (debt overhang), it is debatable whether the government would have willingly embarked upon the Bank-Fund reforms.

Clearly, Dollar et al. (2001) are committed to a particular story about aid and reform in which the importance of aid finance (and the conditionality attached to aid finance) is downplayed to the benefit of non-financial assistance, most commonly TA and 'policy dialogue'. The policy process is understood as being solely steered from within countries, with no appreciation of the implications of particular constraints operating on a country and of the leverage donors acquire in that context.[225] Adoption of 'wrong' policies is represented as a lack of knowledge and/or will on behalf of the borrowing government, and this raises issues of 'good' and 'bad' ownership. Aid monies only come into play once a country has demonstrated a particular economic track record. When aid plays a significant role in reform, this is because of 'ideas'.

Such a view implies a flagrant misunderstanding of the dynamics of reform within specific countries, as exposed in the previous chapter. It is furthermore oblivious to the specificities and differences of the aid and conditionality regimes across countries, and the broader structural realities within which aid and conditionality are located (see also Tarp 2001, p. 350). This is unfortunate given the potential ascribed to the Bank (see Brock and Durlauf 2001, p. 246) to complement the inevitable shortcomings of statistical analysis with qualitative studies of individual countries.

Yet the relationship between the overview of AARIA and its various case studies, as well as the particular quality of the latter, reveal another less obvious dynamic emanating from the Bank, which we have briefly touched upon in chapter two when discussing the Bank's knowledge endeavour. The various case studies in AARIA are in each instance either the work of a researcher based in Africa, or a collaborative effort between researchers based in the Northern hemisphere and in Africa. Although these various case studies frequently draw a picture that portrays a reality which is, at a minimum, more complex than implied in the simplistic and dichotomous phrasing of the hypotheses to be addressed in the study, the Bank's editorial team, in their overview, framed the research findings to the neglect of the specificities revealed in them. The participation of non-Bank and regionally based

[225] It is noteworthy that there is not a single reference to the literature critical of the Burnside-Collier-Dollar thesis in Dollar et al. (2001).

researchers then appears as little more than a token attempt to draw on perceived local expertise, with the revealed ultimate purpose of further bestowing legitimacy on a predetermined policy agenda. Indeed, Deaton et al. (2006, p. 71, my emphases) hail another flagship on Africa, *Can Africa Claim the 21st Century?* (WB 2000e):[226]

> *not so much for any new research findings* as, for the fact that it represented a collaboration between researchers from the Bank and from the best economic research institutes in Africa. That the report's message of growth, trade and poverty reduction could be *jointly* endorsed by this wide range of researchers is in sharp contrast to previous disagreements and marks what Fafchamps calls 'the beginning of a new era'.

In addition, the quality of the contributions in AARIA is highly disparate and this brings to mind an observation made by Samoff and Bidemi (2003, p. 43) regarding the involvement of African professionals in the context of Bank research on education:

> Recruiting African professionals also brings legitimacy to the World Bank's agenda, even when their work is formulaic, unimaginative and insubstantial … Yet, reading these papers does prove instructive. They reflect both the World Bank's willingness to accept insubstantial work from competent Third World scholars and its efforts to institutionalise a particular set of understandings and constructs in research on education. While those constructs do not significantly enrich these papers, it is their uncritical acceptance that is striking. Within the accepted terminology are embedded particular conceptualisations, conceptions, orientations, prejudices, and policy preferences. That discourse structuring terminology treats as part of the environment – what is 'given' and therefore does not require explicit justification and is not subjected to critical attention – important issues that ought to be the focus of policy discussion. As well, that terminology obscures important issues and thereby far too frequently misdirects the search for understanding. The quasi-official status of these constructs in a setting where the same agency oversees both funding and research effectively diverts attention from and often precludes consideration of alternatives that warrant serious exploration, systematic elaboration, and critical evaluation.

[226] M. Fafchamps was part of the 24-strong panel of evaluators that partook in the evaluation exercise led by Deaton et al. He is also Paul Collier's deputy at the Centre for the Study of African Economies.

In a similar manner, the various case studies in AARIA perpetuate the biases of the Bank-promoted understanding of conditionality, in particular pertaining to the type of reform needed and the Bank's 'knowledge' exercise; the potential to propose critical analyses of aid, conditionality and Bank knowledge is further crowded out.

5.4 The new paradigm: a radical break?

The spawning of a literature concerned with verifying or refuting the Burnside-Dollar premise of conditional aid effectiveness, along the lines documented above, has inadvertently contributed to the consolidation of an economics of aid around the conceptual framework implied by Burnside and Dollar (2000a). This 'new' economics of aid tends to be characterised by the anchoring of the aid analysis in a new growth framework, the modelling of the aid-growth relationship in a non-linear fashion, and a predilection for the use of large databases over large cross-sections; and has tended to be mainly concerned with establishing whether or not the Burnside-Dollar predetermined set of policies affects aid effectiveness. Yet following Roodman (2004), its various contributions can be seen to represent an unsystematic sampling of a specification space around Burnside and Dollar (2000a), which fails to produce meaningful robust conclusions.

For Roodman, the econometric debate on the effectiveness of foreign aid to developing countries has worrying hallmarks of Leamer's syndrome of whimsical inference. Leamer (1983, pp. 36-7) – quoted in Roodman (2004, p. 1) – draws attention to the inadequacy of many an econometric result as follows:

> The econometric art as it is practised at the computer terminal involves fitting many, perhaps thousands, of statistical models. One or several that the researcher finds pleasing are selected for reporting purposes. This search for a model is often well intentioned, but there can be no doubt that such a specification search invalidates the traditional theories of inference. The concepts of unbiasedness, consistency, efficiency, maximum-likelihood estimation, in fact, all the concepts of traditional theory, utterly lose their meaning by the time an applied researcher pulls from the bramble of computer output the one thorn of a model he likes best, the one he chooses to portray as a rose … This is a sad and decidedly unscientific state of affairs we find ourselves in. Hardly anyone takes data analysis seriously. Or perhaps more accurately, hardly anyone takes anyone else's data analyses seriously. Like elaborately plumed birds who have long since

lost the ability to procreate but not the desire, we preen and strut and display our t-values.

For Leamer (1983, p. 38), the fragility of inference needs to be assessed in a more systematic way than has often been common practice. Roodman takes up this challenge in the context of the recent aid effectiveness literature as he seeks to establish the extent to which the results from the various studies reveal solid underlying regularities in the data or rather are fragile artefacts of 'whimsy' (p. 3). To this purpose, Roodman selects a representative sample of studies from the new economics of aid on the basis of which a 'test suite' is constructed. The sample comprises studies that vary in type of estimator, control set, countries sampled, length of periods within the panel, overall study timeframe, definitions of aid and policy, and treatment of outliers.[227] Roodman devises his robustness tests as follows. In the first instance, one specification's 'whimsical' choice is transferred to the other; secondly, the definition of export shock is changed in the relevant paper (Collier and Dehn 2001); and, finally, the sample is modified by dropping outliers and/or expanding to new countries and periods (p. 14). So the tests applied derive from three sources of variation that appear across the papers selected. Roodman finds that the general fragility that we identified above with a focus on Burnside and Dollar (2000a) tends to recur throughout the cross-country aid effectiveness literature (see also Rajan and Subramanian 2005). The only result that Roodman finds to be more or less robust is the assertion by Dalgaard et al. (2004) that, on average, aid works well outside the tropics but not in them.[228] Nevertheless, Roodman notes, such a result is more a question than an answer, with the question, as to which causal mechanisms distance from the poles is instrumenting for, left unanswered. Still, for Roodman, these conclusions do not imply that aid is never effective in raising the investment rate or in altering domestic policies. It is suggested that, given that aid is not a fundamentally decisive factor for development and that foreign assistance is

[227] It includes: Burnside and Dollar (2000a); Collier and Dehn (2001); Hansen and Tarp (2001); Chauvet and Guillaumont (2001); Collier and Dollar (2002); Collier and Hoeffler (2002); Dalgaard et al. (2004)

[228] More specifically, Roodman (2004, pp. 52-3) classifies the results of the literature in his sample into five groups (from weakest to strongest results), depending on which robustness test the results withstood. In his findings, the weakest group consists of the results on aid×policy in the Burnside and Dollar (2000a), Collier and Dollar (2002) and Collier and Dehn (2001) regressions. Collier and Dehn's result on Δaid×negative shock belongs in the second weakest group. The Collier and Hoeffler (2002) result on post-conflict×aid×policy, the Hansen and Tarp (2001) results on aid and aid^2, and Chauvet and Guillaumont (2001) results on aid×environment are again stronger. And the GMM results of Hansen and Tarp (2001) and Dalgaard et al. (2004) are placed in the fourth and fifth categories, respectively.

rarely homogenous and some aid is poorly deployed, the statistical noise tends to drown out the signal (p. 53).

This brings us to a second issue regarding the 'new' economics of aid. The latest additions to the literature, much steered by the core WB contributions, have not been able to break away from the typical shortcomings of the aid literature identified in the previous chapter. Their claim to a 'radically' new approach essentially resides in the embedding of the aid impact analysis in the innovations that have characterised growth theory over the last fifteen years. Yet the embedding of the aid impact analysis in a new growth framework, accompanied by a fervent engagement in sophisticated econometric exercises, has not improved insights into the economics of aid. Its explanatory power remains constrained both by the inadequacies of new growth theories as descriptions of the growth/development processes – discussed above – and by the original failure of the aid impact literature to capture adequately external and internal structural features defining the aid phenomenon (see chapter four). The ad hoc extension of variables interacting with aid and growth – in search of better statistical fit – that has characterised the literature seeking to question the Burnside-Dollar-Collier premise again foregoes preliminary examination of what aid is, why is it provided and to whom, and what the various mechanisms and channels through which it could affect the complex dynamics of growth are.

As a result, the frameworks within which aid and growth are discussed today, being reduced to crude variations on the Burnside-Dollar equation, offer little appreciation of either the broader dynamic within which the aid relationship is embedded or the complexities of the relationships between the various RHS variables (political, institutional and economic variables) and growth. The imperative for qualitative studies of the longer-term development process per country, of all relevant factors playing a role in that process, and their mutual relationships remains (see chapter four).

Furthermore, as the current debate on aid effectiveness has fallen into the trap of allowing the flawed Bank research to dictate its agenda, it has failed to examine possible reasons as to why such a weak research exercise has been so heavily promoted by the Bank. Doornbos (2000, p. 103), however, aptly observes that:[229]

> the recent 'Dollar-report' … in putting forward the research finding that 'good' performers are 'best' able to absorb and utilise aid funds effectively, has come to provide a policy rationale for this new approach.

[229] See also Rogerson et al. (2004, p. 10).

> Through reference to 'scientific' evidence presented in this report, 'selectivity' can be advocated and rationalised as being the most cost effective and results-oriented donor strategy. Hence the keen interest with which this report has been taken up for discussion in various donor circuits … There have been serious criticism regarding the reliability and relevance of the way these particular findings have been construed. Yet to several donor agencies these may have appeared a lesser concern compared to the perceived operational advantages on which the report seemed to open a window.

Most recently, McGillivray et al. (2006) point to new emphases in the research on aid effectiveness that emerged out of the AA endeavour (decreasing returns to aid; aid uncertainty; and the influence of external and climatic conditions, political conditions and institutional quality on aid effectiveness). None of these, however, holds the promise of providing genuinely improved insights into the dynamics of aid as they focus on one specific aspect of the aid phenomenon and as such remain constrained by the original failures in their conceptualisation of aid, growth and the interaction between the two. They do, nevertheless, contribute to the perpetuation of a fragmentary account of the dynamics of aid. In addition, the nature of the predetermined imperatives that steered the original propositions in AA remains unexplored.

5.5 Specificities of aid and hazards of selectivity

Apart from the problems of theory, quantitative technique, and bias, the main arguments supporting the 'selectivity' paradigm are characterised by an inability to accommodate the empirical realities of aid. It was argued in chapter four that the notion of aid (and its conditions) being inherently 'good' for development has permeated the aid literature. Those particular distinctive features of aid and the broader economic (and non-economic) relationships, within which aid takes place, and which affect what is observed as the impact of aid, have easily been ignored or inadequately accounted for. There is a persistent failure to reconstruct the economy beyond the constraints upon which aid is projected to act and outcomes diverging from donor-intended ones are too easily attributed to the circumstances pertaining to the recipient economy.

This bias is prevalent in the recent Bank propositions, in which the causes of poor aid outcomes are almost exclusively located in the recipient economy. Along these lines, an UNCTAD Report (2000a, p. VIII) observes that:

> the current diagnosis for change is rooted in a perspective which locates past problems at the national level rather than in international economic relationships, and is also unbalanced in its attribution of policy mistakes and bad management between donors and recipients.

This manifests itself in Bank-sponsored contributions in the following ways. First, there is little acknowledgement of possible negative externalities associated with the various forms of aid. These range from the costs implied by tied aid (inappropriate technology), to repercussions for the skill base in the public/private national sector (danger of brain drain into aid-related activities with potentially lower rates of return), and aid-induced institutional fragmentation (see Berg 1993; Helleiner, G. 1994; Wuyts 1996; Lancaster 1999; Kanbur 2000; UNCTAD 2000a, pp. 171-207). In a recent article putting forward a pertinent and urgent argument for the doubling of aid flows, White (2005, p. 10) observes that:

> at worst, the excessive monitoring is the root cause of recipient 'incapacity' – as recipient government officials are too busy managing donors to spend time delivering government services. The harmful effects of donor proliferation have been well documented … Proliferation comes through both donors spreading their aid over too many countries so each government has to deal with a plethora of different donors … and from a reliance on aid projects rather than funding government activities, with separate reporting requirements for all of these projects.

UNCTAD (2006a, pp. 113-6), further, highlights features of the current aid regime which prevent aid from playing a catalytic role in stimulating domestic resource mobilisation and expanded domestic capital accumulation. These were documented in chapter one and include: the composition of aid – oriented away from physical capital formation and the productive sectors (bias towards the social sectors; large share of TA, debt relief and emergency assistance); the nature of the conditionality attached to or implicit in aid – further explored in chapter six; and the embedded understanding of the role of government in the economy (see also chapter three).

Secondly, it is commonly assumed that the size of aid flows relative to domestic macroeconomic variables is small. This goes as far as the exclusion of certain countries from tests regarding aid effectiveness in Boone (1994) on the premise that their aid/GDP ratio exceeds a certain threshold. Chapter one, however, illustrated the crucial importance of ODA to a set of LICs, where aid dominates investment and budgetary processes. The amount of resources available to these countries and changes in the modalities determining access to aid have real implications for the nature of the adjustment (and development) process. Allocating aid resources to those that have already done a 'minimum of stabilisation or structural adjustment' risks jeopardising attempts in poor countries to raise their investment rates. Following Bird (1997, p. 1412):

> the true trade-off is between external financing and the speed, and therefore the nature of adjustment. While external financing may be a substitute for short-term demand-deflation, it is a complement to longer-term and structurally oriented adjustment. If ... it can be argued that longer-term and supply-based adjustment is superior, because it protects economic growth, helps avoid social costs and political resistance, and therefore enhances the probability of implementation, external financing is appropriately seen as contributing positively to adjustment

UNCTAD (2006b, p. 25) adds that, while it is difficult to say with any degree of certainty how much additional assistance Africa will need by 2015, on the basis of existing estimates, it appears that, at minimum, Africa's additional aid requirements are likely to be around US$ 20 bn per annum by 2008-2010 which would increase to about US$ 25 bn per annum by 2015.[230] The Report continues that (p. 35):

> Contrary to much conventional wisdom, the weight of evidence seems to suggest that aid can work to stimulate growth. It can only do so, however, when provided on an appropriate scale and when focused on the right targets. Failures in both respects over the past two decades have meant that it provided little counterweight to various growth-reducing tendencies.

Thirdly, in an interesting development, Dollar and Levin (2005b) come up with the finding that 'poorly performing' countries tend to be *under*-aided by around 40 percent (even when controlling for their policy and institutional record). This finding sits uneasily with the Bank's earlier assertion of 'over-investment' of aid (by 34 percent) in Low Income Countries under Stress (LICUS) (WB 2002b, p. 6), obtained on the basis of Collier and Dollar (2002). Collier and Chauvet (2004, p. 9) furthermore concede that all aid (*other than* TA) significantly assists in improving a

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[230] These are calculated on the basis of an annual growth rate of 8 per cent which is considered the minimum necessary to achieve the MDGs.

country's CPIA rating and in effecting the 'turnaround' that takes a country out of LICUS status – a result which the authors find to be robust across a variation of specifications. Indeed, in one variant of their analysis, TA has significantly *adverse* effects on the chances of what they call a 'sustained turnaround' from a 'poor' policy/institutional matrix to a 'better' one. The authors comment, if somewhat reluctantly, that (p. 8):

> This is surely a surprising result, since to the extent that there was a conventional strategy for LICUS countries, it was to provide 'advice'. Our results suggest that on average such advice has not been well received.

Fourthly, Morrissey (2001, pp. 26-7) highlights that it is, on average, easier to implement pro-poor expenditures within the constraints of a particular policy environment than it is to implement an economic reform programme that would include pro-poor policies. The former are technically easier to design and establish a political commitment to. The author insists that:

> The binding constraint is resources, and donors can relax this ... If the primary objective is poverty reduction, therefore, the prior policy is pro-poor expenditures, and this is a feasible implementation objective ... eligibility for the release of resources (aid and debt relief) should be based on pro-poor expenditure criteria. This is more simple, and more transparent, than eligibility criteria based on a package of economic reforms that interact in complex ways, are often contested regarding appropriateness, and can be undermined by poor economic performance (not infrequently due to events beyond the control of governments).

Fifthly, the nature of the aid delivery system strongly affects the macroeconomic stability of countries characterised by large aid ratios. The Bank's selectivity proposition on the basis of the CPIA, which is analysed in detail in chapter six, is, however, sensitive to small changes in scores, particularly through the 'multiplicative super-weighting' of the governance variables in the allocation formula. This raises the spectre of uncertainty and volatility of aid flows with their well-known negative effects. Lensink and Morrissey (2000) illustrate how the uncertainty created by the instability of aid receipts significantly affects the relationship between aid and investment levels and efficiency, as well as a government's response to aid, where an unstable donor-recipient relationship results from the uncoordinated character of the aid delivery system, the exercise of conditionality, or counterpart (financing) requirements. Measured aid uncertainty can, however, also reflect the vulnerability of an economy to adverse shocks, with aid flows trying to soften the repercussions of these as, for instance, when emergency aid responds to natural disaster or balance-of-payments assistance follows a terms-of-trade shock. Nevertheless, evidence points to aid volatility tending to reinforce negative external shocks and worsening the economic vulnerability of developing countries rather than the other way round, as aid flows are found to be either non-covariant or sometimes even positively covariant with exports and government revenues (see Gemmel and McGillivray 1998; UNCTAD 2000a; Pallage and Robe 2001; Bulir and Hamann 2005). In this context, UNCTAD (2000a) draws attention to the importance of access and terms of access to foreign resources for LDCs, especially given the external shocks LDCs are prone to. Ironically, as observed by UNCTAD (2000a, p. 181):

> the community of donors has treated macroeconomic stability as a key component of policy reform conditionality since the early 1980s, and this may be one of the reasons as to why, as soon as measures such as overall volatility or aid uncertainty are introduced into cross-country regressions of aid effectiveness, the macro-policy index loses its significance (see Lensink and Morrissey 2000, Chauvet and Guillaumont 2001).

This has obvious repercussions for the propositions regarding aid, policy and growth in AA. Lensink and Morrissey (2000, p. 46) point out that:

> one should be careful in drawing inferences from empirical findings that aid effectiveness is reduced by poor policy. Simply reducing aid because of poor policy may exacerbate the problem. It may be the case that poor policy indicators and aid ineffectiveness are both caused by a third factor, such as uncertainty associated with vulnerability to shocks.

And Foster and Keith (2003, pp. 98-9) add that:

> the priority given to increasing the predictability of aid flows should be increased even if there is some consequent increased risk of disbursing in relatively weak policy environments ... Countries with predictable aid are better able to achieve good policy and sound macro management.

Sixthly, allocating aid flows selectively on the basis of a set of policy and institutional variables is built on the presumption that governments control these policy and institutional environments (see WB 2001i, p. 3). This implies a strong lack of acknowledgement of the various structural parameters (both domestic and international) conditioning domestic policies and institutions. A simple calculation, nevertheless, reveals that the average GNI per capita for the countries in the top quintile of the CPIA ranking is at least three times (and at times even four times) the size of the average GNI per capita for countries in the bottom quintile, which illustrates the tendency of the Bank's assessment tool to be biased in favour of better-off poor countries.[231] Allocating aid selectively on the basis of such a tool as the CPIA hence risks discriminating against poorer countries and concomitant aid rationing could severely precondition the available paths for development.

In this light, a set of alternative principles to allocate aid have been proposed. Macrae et al. (2004) present a framework that shifts the analysis from a focus on specific policy inputs to an analysis of the different processes within countries and internationally that determine domestic conditions over time. They argue that (pp. 83-4):

> governance and policy are two of several factors influencing performance: other important factors are structural constraints, starting conditions, aid volumes … international economic and political relations and the nature of state-society relations … Broadly speaking, donors' focus on policy inputs (especially in economic reform and the social sectors) and governance in their country strategies, and the emphasis on policy dialogue, needs to be tempered with appropriate actions to address other dimensions of performance and aid and international relationships.

They suggest that the group of 'poor performers' be disaggregated and the specifics of these disaggregated subgroups identified and acted upon when allocating aid flows (p. 35).

Cogneau and Naudet (2007) highlight that a country's policy and institutional environment, as captured in the Bank's CPIA, is influenced by structural disadvantages (climate, historical disruptions, structural inequality, health of the population) over which the country has little or no control, and propose a model that allocates more aid to 'poor performers' than that implied by the Collier-Dollar prescription steering the selectivity initiative.[232] Kanbur (2005) starts from the

[231] This observation is for quintile rankings since 2000, as quintile-based information on CPIA scores has only been in the public domain since then. WB (2001i, p. 17) also reports how a 1998 draft of an OED study of WB assistance to several West African countries noted that major shifts in CPIA rankings tended to follow, rather than predict, major changes in growth patterns. These findings were, however, not included in the final version of the study.

[232] Cogneau and Naudet (2007) attempt to develop an 'equal-opportunity' approach to aid allocations, following the contribution by Llavador and Roemer (2001). They seek, however, to remedy the failure of the latter in overcoming the idea that a country's macroeconomic performance (as measured

observation that variations around the estimates of average relationships like the Burnside and Dollar (2000a) equation are not simply random variations but reflect country specific factors that are complex and significant. He proposes to introduce a development outcome measure (such as poverty, extreme poverty, girls' enrolment, maternal mortality rates, or infant mortality rates) into the aid allocation formula. This would encourage countries to deviate from 'orthodox' prescriptions if home-grown approaches are able to produce better results in terms of the latter, although it does not overcome the ineptitude of the projected aid-policies-growth relationship implied in the aid allocation process (see also McGillivray 2004).

McGillivray (2003b) calls for a broader selectivity framework and proposes augmenting the Burnside-Dollar premise to include indicators of structural vulnerability, democratic regime, political stability, and post-conflict status in the allocation of aid flows. Morrissey (2005) emphasises 'policy dialogue' in apparent contradistinction to conditionality (and selectivity), as an alternative way to effect policy transfer. This is accompanied by the proposition of a mechanism through which donors monitor how aid resources are used and whether recipients attempt to implement agreed policies to achieve agreed objectives ('conditionality as monitoring'). Barder and Birdsall (2006), in line with an existing EC approach (see Hervio 2005), propose to tie aid disbursements to particular outcomes such as number of children vaccinated or those who completed primary school, rather than to a set of policy inputs.

Finally, in an attempt to move beyond an approach that attributes the main responsibility for 'poor' aid impact to recipient 'behaviour' running through most of the above, Amprou et al. (2007) insist that the defining features of LDCs, including per capita income, the level of human capital and the extent of economic vulnerability, provide sufficiently satisfactory criteria to steer aid allocations on *both* efficiency and equity grounds (see also Beynon 2001).[233] This joins a broader literature that seeks to emphasise the need to *scale-up* aid rather than merely increase its 'effectiveness' through enhancing the conditionality preceding or accompanying the aid flows (see White 2005; UNCTAD 2006b).

Recent arguments that favour the scaling-up of aid have, in turn, triggered a revisiting of the underlying premise of the selectivity discourse – which attributes

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through inflation, budget deficit and openness) reflects 'policy effort', much in line with the original Burnside and Dollar approach.

[233] A commitment to 'governance' as the fourth criteria to steer aid allocations unfortunately taints their proposition.

weakness in the aid effectiveness chain almost entirely to the recipient/borrower – now through a revival of Dutch disease arguments and concerns regarding 'absorptive capacity' (see Killick 2005; de Renzio 2005; Rajan and Subramanian 2005; Collier 2006b).[234] Collier (2006b, p. 1485) stands out with a new version of his argument that the donor-imposed modalities of aid and the associated mechanisms of scrutiny account for the positive impact of aid rather than the resources themselves:

> Why is aid more productive than oil? Recall that aid is delivered through technical assistance, projects, packages with conditions and debt relief. Each of these is so distinctive that their effects on sovereign rents and scrutinised revenues, and hence on the incentives for effective government, need to be considered separately.

For Collier (2006b, p. 1490), aid to Africa has more or less reached its appropriate scale. Nevertheless, the author continues, absorptive capacity in Africa can be improved through CPIA-style policies, which would create the option of increasing aid subsequently. Plus ça change, toujours la même chose!

5.6 Conclusion

The Bank's new aid paradigm has been reiterated and consolidated since AA. With selectivity, the Bank increases its emphasis in the allocation of aid resources on the quality of the policies and institutions of a country, relative to need-based criteria. It implies that the key to the effectiveness of aid lies entirely and solely with the recipient, to the further neglect – denounced in chapter four – of the structural relations within which donor and recipient interact and of the broader non-aid features which determine that environment.

With the apparent recognition of 'country specificity' and 'country ownership' as key ingredients for successful policy-based programmes, the selectivity paradigm – in combination with the knowledge emphasis, further, implies that the way forward is to become actively involved in the policy dialogue *within* the country. Chapter two drew attention to the expansion of the Bank's analytical and advisory work as part of the Bank's alleged shift from 'coercion to persuasion', where collaborative analytic work and a host of other 'knowledge initiatives' (including training, conferences, study tours, workshops, etc.) seek to assist in defining reforms that reflect 'ownership' *and* conform to the Bank's judgement regarding apt routes to development.

[234] See McKinley (2005) and UNCTAD (2006b) for cogent critiques; see also chapter four.

This chapter documented how the research that underpins this new aid paradigm is characterised by pervasive epistemological failures. Upon closer scrutiny, the propositions put forward by David Dollar and associates, summed up in AA, break down and the effectiveness of aid is revealed not to depend on a set of WC-style policies. More generally, it appears difficult to discern any systematic effect of aid on growth through econometric and, in particular, cross-country, exercises. Furthermore, Dollar et al.'s (2001) attempt to remedy this shortcoming through recourse to case material remains dramatically inadequate as it is characterised by a manipulation of case outcomes in the service of the pre-established propositions of conditional aid effectiveness and the ineffectiveness of conditionality.

The Burnside-Collier-Dollar research endeavour has, nevertheless, been successful for the Bank in at least two ways. First, it has been highly instrumental in justifying the selective allocation of aid flows and in acting as a conduit to promote the Bank's preferred policy stance of PBA across the broader donor community. This is put rather candidly recently by a supporter of the paradigm (Gunning 2006, p. 295):

> Performance-based aid could easily have remained a pipe dream of academics. That it was implemented owes much to the conjunction of two developments. First, the Assessing Aid report ... became extraordinarily influential, spreading the message of the failure of conditionality very widely. Second, rational choice models of government behaviour in response to aid contributed to a growing awareness that the effectiveness of aid depended crucially on the incentives for governments to use aid in desirable ways.

The operational reality of selectivity, however, threatens attempts in poor countries to raise investment rates or to protect pro-poor expenditures. It tends to exacerbate the volatility of aid flows and to discriminate against the poorest countries, with governments exercising little control over the policy measures that are at the core of the Bank's selectivity practice. Yet it has been pointed out how, using Collier and Dollar's own model, the greatest reduction in poverty can be achieved by re-allocating aid on the basis of poverty rather than in accordance with policy criteria (Beynon 2001).

Secondly, the Bank's research endeavour has successfully set the terms of the agenda of the new economics of aid, but to little analytical gain. The framework within which aid and growth is currently discussed has been reduced to variations on the Burnside-Dollar equation and offers little appreciation of the broader dynamic within which the aid relationship is embedded or the complexities of the relationships between the various RHS variables and growth. Ultimately, the characteristic shortcomings of the old aid impact literature are perpetuated, including: a lack of specificity in the analysis of the interaction of aid with the recipient economy; inadequacy of the description of economic mechanisms (here mainly the shortcomings of new growth theory); and an econometric zeal in an attempt to overcome analytical shortcomings. In addition, notwithstanding the recent efforts to posit a 'multi-faceted' approach, the recent developments are unable to overcome the incapacity of the literature to deal with socio-economic dynamics both within the recipient and between the recipient/debtor and the donor/creditor. They mainly consist of ad hoc additions to a fundamentally erroneous framework.

The Collier-Dollar steered research, finally, provides a stark example of the crude articulation that can characterise the relationship between operational imperatives, research and rhetoric at the Bank. This relates to the commitment to a particular policy reform agenda, here embedded in the tool through which the selectivity proposition is operationalised, the CPIA, which, through the mediation of the Burnside-Collier-Dollar research, is put in the service of the Bank's emphasis on growth and poverty reduction. This brings us to the next, and final, chapter.

Chapter 6. Country Policy and Institutional Assessments – opening the black box

6.1 Introduction

The application by the WB of a selective approach to the allocation of aid is based on the CPIA, a structured assessment tool. Through the CPIA rating procedure, Bank staff exercise their judgement regarding the policy and institutional environment of an aid recipient; this judgement then feeds into the Bank's aid allocation formula. The CPIA also provides the cornerstone of the IFIs' debt sustainability framework, which determines the grant eligibility of a country; and it affects the nature of the particular instruments under which Bank aid is disbursed. In addition, the Bank has recently sought to promote its assessment tool across the broader donor community, and other development agencies have started to model their own aid practices on it. Accordingly, the CPIA is rapidly becoming a benchmark.

A closer look at the CPIA reveals how it imposes an ahistorical policy and institutional straightjacket on LICs that remains steered by the WC. In addition, recent formative changes in the CPIA indicate how some of these imperatives have become more entrenched and less visible, possibly in an attempt by the Bank to contain contradictions resulting from the conjunction of certain discursive shifts, as for instance through the PWC, and the persistence of a set of economic (and financial) imperatives. This draws attention to the importance of the Bank's analytical work (or non-lending services) in steering its interaction with clients and links to the Bank's knowledge effort, extensively documented in chapter two. The CPIA provides a crystal through which the essence of the new paradigm of selectivity and knowledge can be observed.

This chapter starts with a brief overview of what constitutes the CPIA and how the purpose assigned to it has changed dramatically over the last few years.[235] This is followed by an illustration of how the CPIA steers the Bank's aid allocation process. The particular formula deployed by the Bank implies a considerable reward in terms of aid allocation for countries at the upper end of the performance scale. The

[235] The chapter draws on an inspection of the CPIA questionnaires between 1998 and 2006. The CPIA questionnaires have been in the public domain since 2000. The 1998 questionnaire was obtained during a Technical Workshop (London, 2 March 1999) jointly organised by the WB and DfID. The 1999 CPIA questionnaire was inferred from the 2000 questionnaire, as the latter gives precise indications where it digresses from its predecessor. An OED review of the IDA's PBA system (WB 2001i) also provides useful information regarding the evolution of the assessment tool.

chapter proceeds to assess the particular understanding of development that is promoted through the assessment tool. A set of traditional biases are highlighted, both regarding the economic and the projected relationship between the economic, the 'social' and 'institutional'. Special attention is drawn to what appears to be a significant change in the economic core of the latest CPIA questionnaires. And closer examination reveals how a set of more contentious policy imperatives (mainly related to the capital account and the financial sector) have become implicitly embedded in the assessment exercise instead of being explicitly discussed. Ultimately, *both* through CPIA-steered selectivity and the exercise of the WB's knowledge role, a much tighter, seamless and less visible web of control is spun over policymaking in LICs – despite the ubiquitous and oft-reiterated commitment to 'ownership' and 'partnership' principles.

6.2 The ascendancy of the CPIA

A formal link between staff assessments of the performance of IDA-eligible borrowers and IDA lending allocations was initiated at the Bank in 1977. This was called the Country Performance Rating (CPR) and originally assessed both policy inputs and economic performance indicators (including growth and savings rates) of prospective aid recipients. The assessment exercise was an internal Bank affair and involved country desk staff and Bank management. Four criteria affected the IDA's resource allocation, in the following order of priority: first, national poverty as measured through income per capita; secondly, creditworthiness; thirdly, economic performance, to be assessed in terms of macro indicators including growth and savings rates but also in terms of the quality of 'administration and economic management' together with 'the speed and direction of change'; fourthly, project readiness (Kapur et al. 1997, p. 1152).[236] Kapur et al. specifically note that the exercise did not imply any specific reference to market-oriented policy reform.

The definition of the criteria, their relative importance, and the rating and disclosure procedures regulating the CPR were subject to important changes over the years. Significantly, during the 1980s, the emphasis moved from an initial concern with *both* policy inputs and economic performance indicators (growth and savings rates), to a predominant concern with policy inputs. And, by the early 1990s, an

[236] Entitlements, of course, were not guarantees, and Kapur et al. (1997a, p. 1155) observe how the Bank mainly approximated the indicated norms in its ongoing operations. They add that nations at the extremes of the population-size range of IDA-eligible countries were treated as exceptions to the allocation norms, and that the 1989 guidelines established a normative allocation of 45 percent of the entire IDA envelope for SSA.

exclusive emphasis on policy inputs prevailed. As a result, the 1991 CPR exercise consisted of the following criteria. Under 'short-term economic management' appeared consideration of monetary, fiscal, exchange rate, and pricing policies. 'Long term management' focused on structural policies, including external and domestic trade regimes, PSD, tax and financial sector policies, governance and natural resource management. And 'poverty alleviation' included policies to promote the delivery of social services and the reduction of biases against the agricultural terms of trade and the demand for labour (WB 2001i, p. 4). The instructions to staff, as quoted in WB (2001i, p. 5), explicitly stressed the need to assess policies rather than outcomes:

> The objective is to get an assessment of how well countries are implementing good policies. Accordingly, we are de-emphasising recent performance in such indicators as real growth in output, exports, etc. Nevertheless, output indicators should be used judgmentally to assess whether policies are actually being implemented ... In assessing country performance, we are not interested in ascertaining whether a government is 'to blame' for a poor policy framework. There may sometimes be good reasons why a government is unable to address certain policy issues effectively, notwithstanding its best efforts. However, it is the actual policy framework that is to be assessed and not the intent or the effort of the government ... Since the focus is on policies actually in place, no account is to be taken of anticipated future policy reforms until they have been made effective. The platforms of incoming governments or recently published development plans are not deemed relevant to country performance until acted upon.

The 1990s saw further changes to the Bank's PBA process.[237] These included: improving the design of the rating systems (altering the criteria by merging some and/or introducing new ones, and providing and altering definitions for the various rating levels); issues of how to take country portfolio performance into account; considerations regarding how to take account of governance in the rating system; a change of the relative weights on income and the performance rating in the allocation formula, in order to strengthen the link between policy performance and allocations; issues of how to deal with countries at the bottom of the performance spectrum; and

[237] See WB (2001i) for a detailed account.

issues regarding the relationships between the performance rating, the Country Assistance Strategy (CAS), the Bank's country 'business plan' and, later, the PRSP.

The 1998 redesign was of particular importance. It set out to reconfigure the performance rating, now renamed CPIA, in a manner that sought to reflect the findings of AA with its emphasis on a set of policy and institutional environments as conditions for aid effectiveness (WB 2001i, p. 11). A separate six criteria-strong governance cluster was further added to the CPIA, and the CPIA was transposed into a country's performance rating by applying a portfolio performance factor and a governance discount (see below).

These changes mainly happened at the behest of the IDA Deputies. While, traditionally, the Bank's performance ratings and allocation procedures had been the preserve of Bank staff (and more specifically, country economists and managers), from the late 1980s onwards, IDA donors increasingly interfered in the rating procedure, pegging their own concerns onto the existing order of the PBA.[238] Bank management accommodated the requests as much as possible, but insisted on restricting the number of CPIA criteria to twenty, all with equal weight (see WB 2001i, p. 10). As a result, Herman (2004, p. 7) observes:

> Both the four clusters and the 20 individual items ... seem to reflect less an overall coherent design than the history over a quarter century of step-by-step revision and accretion of concepts that management sought to include in the CPIA. Over time, individual items in the CPIA have been added and subtracted, split and merged. The main constant seems to have been that there be 20 items, and that they be weighted equally in the CPIA average. Thus, as new items came into the CPIA index, other items had to be collapsed or dropped.

In the early 2000s, the disclosure procedures regarding the CPIA were dramatically overhauled. CPIA scores and their justifications were shared with country counterparts, and the questionnaires and scores (initially in quintile format) were made publicly available through the Bank's external website. Since 2005, the numerical scores have become fully disclosed for IDA-eligible countries.[239] This

[238] This reflected the broader shift, discussed in chapter two, in the relationship between the IDA replenishments and the policies and operations of the IDA (and the Bank more broadly) – in particular since the Ninth IDA Replenishment (see also IDA 2001b, p. 5).

[239] The CPIA exercise is conducted for both IDA-eligible and IBRD-only borrowers, but only serves as a resource-allocation device for the former. The new disclosure policy does not affect the IBRD countries. With the decision to disclose the numerical scores of IDA-eligible countries in 2005, the name of the CPIA for IDA-eligible countries was changed to the IDA Resource Allocation Index (IRAI) at the behest of powerful IBRD borrowers. This reflects the desire to sharpen the distinction

disclosure, however, does not apply to the write-ups that provide the rationale for the ratings, although Bank staff continue to share these with the respective country authorities. The purpose of the latter process is for the Bank to remain closely involved in the policy discussions of the particular country (see also Michailof 2004).[240] Gelb et al. (2004, p. 19) highlight that:

> CPIA scores can help to indicate where performance needs to be strengthened and how fast this can be done ... It is not necessary to subscribe to the letter of every specific CPIA question or to the exact weighting for the aggregate CPIA ... to recognise that it includes a wide range of what is generally accepted as important for development ... A more open CPIA process has the potential to link policy and institutional assessments, knowledge creation, resource allocation, and the monitoring of results, into a seamless whole.

These moves to disclosure, first at country level and subsequently more broadly, allowed the Bank to promote the CPIA not just as a device to allocate aid flows, but additionally, as an advocacy tool at both country level and in the broader donor community (see also Herman 2004). As such, while the official reason for disclosure of the CPIA method and, recently, also of its scores, was the Bank's aspiration to operate in a more transparent way, it was also indicative of a continuing attempt by the Bank to strengthen its function as a 'norm-setter'. Gelb et al. (2004, p. 1, my emphasis) explicitly observe that:

> As part of the process of increasing the transparency of ODA and working towards a model based on greater coordination and partnership, the Bank intends to move towards disclosure of the CPIA scores ... This trend will inevitably increase public scrutiny of the CPIA process and the ratings. It may also result in wider use of formal performance-based process by other donors ... CPIA disclosure offers a number of clear advantages ... it can

between the rating process for IDA-eligible versus IBRD borrowers and safeguard the different disclosure arrangements between the two types of Bank clients (personal communication with Frederik van Bolhuis, Lead Economist Resource Mobilisation, WB). See Herman (2004) for a convincing argument against disclosure of CPIA ratings on the basis that their methodology is too weak and unreliable for the scores to merit the attention they receive when published – although the issue remains how apt they are for any purpose (see further below).

[240] According to one senior Bank staff member, these discussions with countries regarding their scores could move the Bank towards a procedure similar to the IMF's Article IV consultations (Alan Gelb at the Initiative for Policy Dialogue Workshop on the CPIA, 5 April 2007). Through its Article IV consultations, the IMF exercises its surveillance over a member's economic policies and 'assesses these policies in regard to their ability to contribute to economic growth and macroeconomic and financial stability' (Lombardi 2005, p. 20). Typically, this monitoring is conducted on an annual basis and surveillance reports serve as a signalling device for other donors.

provide better information to enable the IDA countries to learn from each other and *to help harmonise* the aid allocations from various donors.

Finally, in 2004, a review by an external panel led by John Williamson concluded that the CPIA focused on the right set of issues and produced robust results (IDA 2004d). The panel broadly supported the CPIA practice of rating *implemented* rather than *intended* policy actions, and strongly favoured disclosure of the ratings for IDA-eligible countries. It did, however, point to unnecessary overlap in some of the criteria (see also Herman 2004), and outlined steps to address some methodological and process issues. Some CPIA criteria were subsequently deleted and others combined and streamlined. The core of the CPIA, nevertheless, remained the same. The number of criteria constituting the CPIA, now reduced to sixteen, has remained unchanged since (see WB 2004g, 2005e, 2006h).

6.3 CPIA and the allocation of Bank aid flows

The CPIA currently consists of sixteen criteria, which are rated on a scale of 1 to 6 by Bank staff. Appendix 3 reproduces the CPIA matrix. The criteria are compiled in four clusters and their average constitutes the CPIA score. Each cluster carries an equal weight, but not all clusters have an equal number of constituent criteria. Specific instructions ('narrative guidelines') are given for each rating level of each criterion.[241] Under 'economic management' are macroeconomic management, fiscal and debt policy. Under 'structural policies': trade, financial sector, and business regulatory environment. Under 'policies for social inclusion/equity' we find: gender equality; equity of public resource use; building human resources; social protection and labour; and, policies and institutions for environmental sustainability. And, finally, the categories constituting 'public sector management and institutions' are: property rights and rule-based governance; quality of budgetary and financial management; efficiency of revenue mobilisation; quality of public administration; and transparency, accountability and corruption in the public sector (WB 2006h).

The current CPIA rating process involves two phases. In the benchmarking phase a small representative sample of countries drawn from the Bank's different regional departments is rated. In the second phase, staff rate the remaining countries using benchmark countries' scores as a guide. The benchmarking phase seeks to

[241] Until the 2000 questionnaire, only the ratings '2' and '5' comprised rating guidance to staff. This changed with the 2001 questionnaire and, since then, the narrative guidelines to staff have become increasingly elaborate.

ensure that, given the criteria, the ratings are set at the right level and are consistent across countries and regions. In the second phase, the rating proposals are accompanied by a written justification. These proposals are reviewed within the respective region by the respective chief economist and are then submitted to a Bank-wide review (see Gelb et al. 2004).

The ratings are to depend on the level of performance assessed against the criteria, rather than the degree of improvement since the year before, and they are to reflect judgement of policy actions and implementation ('actual policies') rather than of promises or intentions. Each criterion also includes suggested 'guideposts', such as economic indicators, to complement the narrative guidelines in assisting country teams to determine country scores (see also below).

The CPIA is the core of the Bank's system to allocate aid flows, but not its only determinant. Two additional steps are included. First, to capture the dimension of quality of the development project and programme management, the Bank's Annual Report on Portfolio Performance (ARPP) is used and determines a score for each country's implementation performance. A weighted average is then calculated of the CPIA (80%) and the ARPP rating (20%). Secondly, the latter result is multiplied by a 'governance factor' to produce the country's IDA Performance Rating (PR). According to the latest formula, the governance factor is derived from the country's average rating for six governance criteria that are part of the PBA system.[242] These include the five criteria in the governance cluster of the CPIA, and a three-year moving average of the procurement practice score of the ARPP (IDA 2004a). The average score of these six governance criteria is divided by 3.5, the mid-point of the 1-6 scoring range, and an exponent of 1.5 is applied to this ratio. The country's overall rating is then multiplied by this factor, resulting in an increase (or decrease) of the overall PR, depending on the degree to which the country's governance rating is 'strong' (above 3.5) or 'weak' (below 3.5) (IDA 2005, p. 46).

The PR feeds into the IDA allocation norm according to the formula below.[243] In addition to their PBAs, all countries are allotted a basic allocation of SDR 3 million.

Allocation Country $_i$ (3-year) = SDR3.3 million + PBA $_i$

where:

[242] WB (2001i, pp. 31-2) provides a good account of the previous manner in which governance was incorporated into the allocation formula.
[243] See IDA (2007c, p. 9) for a comparison between the formulae used by the IDA, AfDF and AsDF.

$$PBA_i = \frac{(\text{IDA rating}_i)^2 \times \text{Population}_i \times (\text{GNI/cap}_i)^{-.125}}{\Sigma_{i=1\text{-}81}\,[(\text{IDA rating}_i)^2 \times \text{Population}_i \times (\text{GNI/cap}_i)^{-.125}]} \times \text{Envelope}$$

(i) IDA Rating Country $_i$ = (0.8 x CPIA $_i$ + 0.2 x ARPP$_i$) x Govfact$_i$

(ii) Governance Factor $_i$ = (average rating of 6 governance criteria $_i$/3.5)$^{1.5}$

(iii) Envelope = IDA three-year envelope, after deduction of the otherwise determined blend allocations as well as the allocations to eligible post-conflict countries;

(iv) the country allocation norm is subject to a maximum of US$ 20 per capita per annum.

Source: IDA (2005, p. 51).

The PBAs are subject to a set of exceptions. Blend countries receive less than their allocation norms due to their broader financing options, and post-conflict countries can be provided with additional resources in support of recovery.[244] Each replenishment document specifies the share of IDA funds that donors wish to see allocated to SSAn borrowers, subject to performance. The last replenishment (IDA 2005, p. 13) set this target at half of IDA assistance. As a result, an estimated 62 percent of IDA14 resources are allocated using the PBA formula.[245]

In addition, apart from determining the amount of IDA resources a country receives, the CPIA increasingly affects the form these take, where non-lending is favoured at the lower end of the rating spectrum to the benefit of TA and analytical and advisory services, while programmatic approaches prevail at the higher end of the rating spectrum.[246]

The Bank has strengthened the relationship between country performance and its aid allocations since the early 1990s.[247] While the ratio of aid per capita (pc) between the top and bottom performance quintiles was 2.35 in 1990 (Goldin et al.

[244] See IDA (2005, pp. 47-8) for further elaboration on the exceptions to the allocation norm.
[245] Around 20 percent of IDA14 resources go to capped blend countries (India, Indonesia and Pakistan). Around 10 percent of resources go to post-conflict countries, while another 8 percent go for special purposes agreed upon during the replenishment procedures (IDA 2007c, p. 2).
[246] See WB (2004e, pp. 80-8) for an illustration of how, in the context of aid to Africa, the choice of aid instruments can be linked to performance.
[247] See WB (2001i, pp. 28-9) for an overview of changes in the underlying allocation formula during the 1990s. See also below on how the formula became more sensitive to changes in the PR during the late 1990s.

2002, p. 33),[248] it increased to 2.8 for the FY00-02 allocation.[249] With the latest aid allocation (FY04-06), the countries in the top performance quintile receive on average five times as much IDA aid pc as the countries in the bottom quintile (subject to exception norm; IDA 2003a, p. 8).[250] The 2003 *Annual Review of Development Effectiveness* reports that, in 1999, 89.4 percent of Bank lending went to countries with a CPIA ranking of 3.0 or better, while, by 2003, the share had increased to 96.6 percent (WB 2004c, pp. 13-4).

The way in which the CPIA feeds into the Bank's PBA formula raises several issues. First, CPIA rankings produce a set of countries at the margin of what is considered suitable for 'normal engagement'. These have, in Bank parlance, become designated as LICUS, and refer to IDA-eligible countries that score 3.0 or less.[251] In FY06, 35 countries were classified as LICUS (WB 2005f, p. 1). These are home to more than 500 million people, including around 200 million living in extreme poverty. About one third of these countries are in non-accrual status and have no access to IDA financing.[252] The other LICUS are meeting their financial obligations to IDA and are receiving IDA lending in accordance with their performance ratings.[253] Accordingly, LICUS receive lower IDA allocations pcpa than other IDA-eligible countries and, over recent years, have seen their share in total IDA resources decrease (IDA 2004b, p. 8).

A Bank Task Force Report (WB 2002b), under the leadership of Paul Collier and Ngozi Okonjo-Iweala, defines the main principles for Bank operational engagement with these countries. Following the propositions set out in chapter five, the Report argues that traditional aid programmes have not worked well in these

[248] In 1990, the average per capita per annum (pcpa) allocation for a 'good' policy country was US$ 4.7; US$ 2 for a 'poor' policy country (Goldin et al. 2002, p.33).
[249] The average pcpa allocation for a 'good' policy country was US$ 9.9; US$ 3.5 for a 'poor' policy country.
[250] The average pcpa allocation for a 'good' policy country was US$ 12; US$ 2.4 for a 'poor' policy country (IDA 2003a, p. 8). This allocation applies to 63 of the 81 IDA-eligible countries. Eighteen IDA countries do not receive regular allocations. These include post-conflict countries (Afghanistan, Angola, Burundi, DRC, Congo Rep., Eritrea, Sierra Leone, and Timor Leste), blend countries for which allocations are fixed (Bolivia, India, Indonesia, Pakistan, Uzbekistan, and Yugoslavia), and inactive countries (Liberia, Myanmar, Somalia, and Sudan).
[251] Other fora, like the DAC, have adopted the terminology of 'fragile states', defined as those countries in the bottom two quintiles of the CPIA.
[252] In 2004, the Bank established the LICUS Implementation Trust Fund with an initial allocation of US$ 25 mn. Countries in non-accrual can draw small amounts from this fund (in the range of US$ 3 mn to 4 mn) to support governance improvements and social service capacity, and prepare for re-engagement with the Bank.
[253] LICUS emerging from conflict are rated on the basis of special post-conflict progress indicators (PCPI), with the PCPI replacing the CPIA within the PBA system.

countries.[254] But rather than calling for total disengagement from these countries, the Report emphasises the need for an approach that focuses on knowledge and capacity-building instruments rather than financial transfers – paying specific attention to the quality of Bank policy engagement and tailored analytical work (see also IDA 2005, p. 20). Complementary deployment of finance is envisaged, mainly to the private and nongovernmental sectors, or to local government for the delivery of basic social services such as health and education.

Secondly, a country's policy and institutional performance is clearly the dominant determinant of its allocation. The specific weights on the various components of the IDA's allocation formula reflect Bank staff discretion in interaction with IDA Deputies, rather than being informed by any particular analysis (see also Herman 2004). Half as much weight is given to population, and one sixteenth as much to the degree of poverty (using per capita income as proxy). This follows a change in the mid-1990s, operational since the IDA-11 (1997-99) allocations, under which the relative weight on GNI/capita in the allocation formula fell from $1/8^{th}$ to $1/16^{th}$, strengthening the link between policy performance and allocations. The bias in favour of policy performance in the allocation norm has since remained unaltered. In an update on the PBA system (IDA 2004b, pp. 6-7), the Bank reasserts its position as follows (my emphasis):

> There is … *broad consensus* that among low-income countries, large-scale financial aid has more of an impact in an environment of sound institutions and policies. Accordingly, IDA has made its Country Performance Rating the dominant factor in its allocation among its eligible countries … At this time, IDA is sharply focused on the poorest countries, and among these the system favours those that are better governed. Increasing the poverty weight in the allocation among the poor countries would de facto reduce the weight put on the quality of policies and institutions. Management is of the view that this would lead to less effectiveness in fighting poverty …

[254] It should be noted that the experience of the IFC in these countries yields a somewhat different picture from that projected for aid. The IFC has been active in about two-thirds of LICUS over the last decade and, on a portfolio basis, IFC investments in LICUS generally perform as well as those in other countries (WB 2002b, p. 7). This refers back to some of the trends pointed out in chapter two, touching upon the way in which the IFC increasingly seeks to expand its activities in LICs. Half a dozen countries, however, account for three-quarters of these IFC investments, both by number and by value. Furthermore, resource extraction (oil, gas, and mining) accounts for nearly two-thirds of IFC investment (by value) in LICUS. The remaining IFC projects are mainly in the social sectors and in agriculture. This composition of the IFC portfolio is distinctive as, in non-LICUS, the IFC usually has a substantial share of its portfolio in the financial and infrastructure sectors.

the PBA system is used to steer ... funds to where they are most likely to be effectively used to reduce poverty.

Concern amongst some IDA Deputies regarding the particularly low weighing of poverty in the allocation formula is thus readily dispelled by Bank management through reference to a supposed consensus based on the Burnside-Collier-Dollar research (see also IDA 2001c, p. 7) – despite the consistent findings across the literature emanating from outside the Bank that aid effectiveness is *not* contingent on the policy and institutional matrix embodied in the CPIA (see chapter five). The particular weighting has further been defended on the argument that IDA resources are in any case biased towards poor countries by virtue of the operational cut-off level (which stood at US$ 895 per capita income as of July 1, 2004) (IDA 2005, p. 46).

Thirdly, the governance elements of the CPIA, in effect, count twice. As a result, and also as a consequence of the exponential in the governance factor, the IDA allocation norm is very sensitive to changes in scores on governance criteria. Indeed, an update report by the IDA on the PBA system illustrates how a one-point drop in just one of the governance criteria results in a 15 percent drop in the country's allocation (IDA 2003c, p. 2). The Bank's evaluation department has, nevertheless, highlighted that the governance-related ratings are highly correlated with the other CPIA criteria and thus add little to the overall assessment of a country's policies or institutions, apart from potentially worsening the volatility of aid allocations – the pernicious effect of which was highlighted in chapter five.[255] IDA Deputies, however, remain committed to the centrality of governance to the IDA's allocation system and expressed this most recently at the occasion of the IDA14 Mid-Term Review in November 2006 (see IDA 2006b, p. 2).[256]

Fourthly, the issue arises as to the relationship between the CPIA, the PBA which it feeds into, and the PRSP. It was indicated in chapter one how the CPIA-steered selectivity framework was married to the recognition of country ownership of a development programme through the PRSP initiative. It was, however, also pointed out how the latter has functioned more as a tool to streamline poverty-reduction

[255] The OED notes that this close correlation may reflect inadequate knowledge about governance-related issues within the Bank and that, as a result, there may be a tendency for staff to rate countries in these areas more or less in line with their other ratings (WB 2001i, p. 20).

[256] See IDA (2007c) for a recent proposition by Bank staff that seeks to simplify the formula and possibly diminish the volatility of allocations provoked by the governance factor, without compromising the IDA Deputies' *explicit* request that a simplified option for the formula retains a weight of governance similar to the current formula (effectively at 68 percent).

programmes rather than as a way of imposing debtor countries' ideas regarding preferred paths of development on the donor community. Indeed, the PRSP seems to have emerged as an opportune conduit for the donors and, in particular, the Bank's broader knowledge agenda. The CPIA plays a particular role in this 'streamlining' exercise, conditioning the scope for alternative development and poverty reduction strategies. In effect, Bank documents indicate how the CPIA serves as a filter between a PRSP and the operational realities of Bank concessionary assistance (see WB 2004k, p. 22; WB 2005c, p. 23). In addition, it is expected that the implementation of PRSP policies reflects in a country's CPIA ratings (IDA 2002b), which reveals an implicit assumption that the former are necessarily in line with the imperatives embedded in the latter.

Finally, it should be observed that, although the CPIA constitutes the core of the Bank's resource allocation mechanism, it is not considered by the Bank to merit scrutiny under the revisions of its conditionality practice.[257]

6.4 CPIA deconstructed: variations on a well-known theme

Reflecting a set of additions on the Bank agenda during the 1990s, documented in chapter three, which culminated in the proposal for a CDF by then-president J. Wolfensohn, the CPIA has come to encompass an economic core touching upon macroeconomic and structural policies, augmented with concerns for 'governance' and social inclusion or equity.

According to WB staff, the CPIA criteria include 'a wide range of what is generally accepted as important for development' (Gelb et al. 2004, p. 19). Closer scrutiny of the CPIA below, however, reveals how the selective allocation of aid on its basis risks locking in an extensive policy agenda with ambiguous repercussions for growth in poor countries. The policies implied in the CPIA emerge as neither sufficient nor necessary for growth, persistently precluding the various types of strategic interventions deployed by the East Asian tiger economies or by the now-developed countries. The CPIA policy-institutional matrix does not correspond to the empirical reality of how development is likely to take place; it fails to accommodate diversity across poor countries; and it removes the potential for strategic discretion in

[257] See the WB's Progress Report on Good Practice Principles for the Application of Conditionality (WB 2006f). See also Koeberle's (2005, pp. 62-3) account of changes in WB conditionality, which clearly indicates how the CPIA is understood as a selection mechanism but *not* as a form of conditionality. For Koeberle (2005), and for the Bank, conditionality is that which is attached to the disbursements of funds, not that which precedes it.

the design of development policies – the necessity of which was pointed out in chapter three.

The CPIA essentially embodies a set of predetermined neo-liberal norms augmented with apparent social and governance concerns and reveals how little the core of WB aid practices has been fundamentally affected by the purported move forward from the WC. The policies upon which assistance is conditioned are anchored on what could more aptly be described as 'WC plus plus', where social and institutional concerns are added onto a pre-determined set of imperatives, leaving the latter undisturbed.

In addition, a change in the questionnaire between the 2003 and 2004 CPIA exercise has caught our particular attention. While the familiar neo-liberal bias clearly prevailed in the questionnaires steering the successive CPIA assessments between 1998 and 2003, a set of specific policy imperatives disappeared from the narrative guidelines of both the trade and the financial sector criteria in the 2004 questionnaire. This by itself was remarkable. Yet, concurrent to this particular change, the list of guideposts that accompany the narrative guidelines, which have the objective of assisting staff in their judgement of a country's policy and institutional environment, was redefined. The list of guideposts not only expanded but, more importantly, changed in character. While the guideposts in the economic clusters of the preceding questionnaires had mainly referred to PREM/DEC databases on economic indicators, the guideposts in the 2004 questionnaire came to include a host of 'diagnostic reports'.

Closer scrutiny of these reveals how the biases that disappeared from the narrative guidelines of the CPIA questionnaires have become embedded in these reports and now steer staff assessments in more surreptitious ways. This draws attention to the importance of the Bank's analytical clout, in particular through its applied country and sector work, to assure the *continued* adoption of a specific policy agenda in a specific country context, and links back to the way in which the Bank understands its self-proclaimed knowledge role – documented and critically assessed in chapter two.

We start this section with the deconstruction of the economic core of the CPIA, paying particular attention to the changes in the structural cluster of the economic core in the 2004 questionnaire.[258] This is followed by a brief account of presumptions regarding social and governance issues in the CPIA matrix. Two appendices are provided to document more extensively the scoring system within the various clusters of the CPIA. Appendix 4 focuses on the economic core, with specific attention to the changes between the 2003 and 2004 questionnaires. Appendix 5 documents the CPIA prescriptions regarding social and governance issues.

6.4.1 The economic core

The economic core of the CPIA comprises two clusters: 'economic management' and 'structural policies'. Each of these two clusters comprises three criteria. 'Economic management' includes 'macroeconomic management', 'fiscal policy' and 'debt policy'. 'Structural policies' includes: 'trade', 'financial sector' and 'business regulatory environment'.

The first criterion on macroeconomic management assesses the quality of monetary and exchange rate policy and favours aggregate demand policies that: produce low inflation; minimise internal and external balance; and ensure that public spending does not crowd out private investment. The second criterion assesses the quality of fiscal policy in terms of: macroeconomic stability; budgetary position; the debt to GDP ratio; the capacity for public expenditures and revenues to adjust to shocks; and the extent to which public goods provisioning is adequate to support medium-term growth. The latter reflects a slight change of emphasis in the fiscal policy criterion with the 2001 questionnaire (WB 2001j). Where the CPIA questionnaire had been traditionally characterised by an exclusive concern for 'fiscal balance' (WB 1998e, 2000c), the 2001 questionnaire (and its successors) re-attributed fiscal policy with a role for growth (WB 2001j, p. 4). Although the re-emergence of a growth concern assigned to macroeconomic policies moves the questionnaire beyond its original stabilisation bias, price stability remains the priority of monetary and exchange rate policies, and a strong concern that public spending might crowd out private investment persists (WB 2001j, 2002c, 2003i, 2004g, 2005e).

The last criterion of the 'economic management' cluster is concerned with debt policy. This is assessed in terms of whether a country's debt management strategy 'is conducive to minimise budgetary risks and ensure long-term debt

[258] The economic core of the 2005 and 2006 CPIA questionnaires (WB 2005e, 2006h) is exactly the same as for the 2004 questionnaire (WB 2004g). Commentary on the 2004 questionnaire hence equally applies to these more recent questionnaires.

sustainability' (WB 2004g, p. 9). It examines: whether a country is timely in servicing its debt (i.e. whether prospective fiscal balances and foreign exchange receipts are adequate to ensure that public debt, external and domestic, can be fully serviced under most foreseeable circumstances); whether a country has incurred arrears in debt service; what administrative processes exist for debt management and how debt management relates to macroeconomic policies (p. 10). Appendix 4 indicates more elaborately which policy and institutional environments merit a low and high score. It also draws attention to the kind of guideposts that are recommended to staff for consultation when attributing scores.

The cluster on structural policies encompasses three different criteria. These underwent a set of changes between the 2003 and 2004 questionnaires which deserve specific attention. To highlight these changes, we first indicate what was specified in the 2003 questionnaire and juxtapose this, subsequently, to the content of the 2004 questionnaire in the relevant areas.

In the 2003 questionnaire, the first criterion of the 'structural policies' cluster was concerned with trade policy and the foreign exchange regime. It sought to assess how well a country's policy framework fostered trade *and* capital movements. As indicated in appendix 4, the narrative guidelines touched on a whole set of issues including: tariff rates; import/export barriers; duty exemptions; trading monopolies; customs administration; current account convertibility ('IMF Article 8 status'); and *capital account convertibility*. A country was deemed to perform well, i.e. scoring 5, when WB (2003i, p. 8):

> Average tariff (weighted by global trade flows) is low (10% or less), with low dispersion and insignificant or no quantitative restrictions or export taxes. Trading monopolies absent or unimportant. Indirect taxes (e.g., sales, excise, surcharges) do not discriminate against imports or exports. Efficient and rule-bound customs administration. IMF Article 8 status. Minimal or no foreign exchange restrictions on long-term investment capital inflows.

Poor performance, i.e. a score of 2, implied:

> Average tariff (weighted by global trade flows) is high (over 30%). High and erratic import and/or export barriers, including quantitative restrictions and/or state trading monopolies. Export taxes or quantitative restrictions frequently used. Customs or political authorities make discriminatory or *ad hoc* exemptions. Valuation procedures arbitrary and artificial exchange

rates result in substantial over or under valuation of goods for customs purposes. Clearance of goods requires many approvals, arbitrary fines, frequent bribes to customs officials and involves long delays. Foreign exchange rationed or an administered foreign exchange regime with multiple exchange rates.

With regard to the financial sector, two different criteria existed in the 2003 questionnaire: 'financial stability' and 'financial sector depth, efficiency and resource mobilisation'. These were subsequently merged in the 2004 questionnaire under the composite heading of 'financial sector'. As indicated in appendix 4, the narrative guidelines for the 'financial stability' criterion in the 2003 questionnaire were concerned with: barriers to entry in the financial sector; the treatment of foreign investors; corporate governance arrangements (which touched upon issues pertaining to the protection of minority shareholders; see WB 1998e, p. 4); and with whether international best practice standards were guiding the regulatory regime. A country would be awarded a score of 5, when it had, WB (2003i, p. 9, original emphases):

> **Good competition policies** (e.g. no barriers to entry, equal treatment of foreign and domestic investors, integrated financial system, virtually complete capital account convertibility), **legal regime** (e.g. sound corporate governance arrangements are in place and effectively enforced, effective financial reorganisation/restructuring/debt foreclosure mechanisms exist allowing expeditious resolution of problem assets and exit of failed financial institutions) and **regulatory regime** (e.g. based on international best practice standards, with effectively functioning and independent regulatory agencies able to enforce compliance, well fenced against money laundering). Financial sector characterised by healthy competition, high level of stability and high depositor/investor confidence. Financial crises are rare and if they do occur, resolution is quick, transparent and cost effective.

A country was awarded a score of 2 when it was characterised by:

> **Unsatisfactory competition policies** (e.g. high barriers to entry and/or differential entry requirements for foreign and domestic financial institutions (FIs), segmented financial markets, strong capital controls), **legal regime** (e.g. weak corporate governance, insufficient legal powers for regulatory agencies, lack of orderly and transparent exit mechanisms for failed FIs, ineffective collator, bankruptcy and anti-money laundering

laws), and **regulatory regime** (e.g. regulatory agencies are not independent/subject to political interference, prudential regime for FIs is weak/not based on international best practice standards for consolidated supervision, capital adequacy and disclosure, large and connected exposures, money laundering, etc.). As a result, the financial sector is highly concentrated, undercapitalised and prone to frequent financial crises. Depositor and investor confidence is low. Crisis response is orderly/non-transparent (e.g. FI failure resolution costs hidden in the central bank)/lengthy/excessively costly.

As far as the criterion 'financial sector depth, efficiency and resource mobilisation' was concerned, a country was awarded a score of 5 when it was characterised by, WB (2003i, p. 10):

> **Good monetary and credit policies** (interest rates are market determined, credit is not directed, whatever few credit subsidy schemes remain can be justified on social grounds and are transparently funded through the budget, the PSBR is small enough to not noticeably crowd out private sector credit), **tax policies** (e.g. the tax regime for all FIs takes account of legitimate risk reducing expenses, tax treatment of different FIs and products create a level playing field for all financial sector activity), and **ownership policies** (e.g. state ownership of FIs is limited to justifiably Government-supported, arms-length and commercially run institutions such as export credit agencies). As a result, financial sector is characterised by low margins, high levels of intermediation and availability of a wide and sophisticated range of financial products and services.

A score of 2 implied:

> **Unsatisfactory monetary & credit policies** (interest rates are not market determined and/or credit ceilings are widely used, widespread occurrence of subsidized credit schemes that have severe distortionary effects, PSBR crowds out credit to the private sector), **tax policies** (e.g. banks are subject to unduly high unremunerated reserve requirements, taxes are levied on non-existing profits because loan loss provisions are not tax deductible, differential tax regimes create unequal playing field for different FIs/products), and **ownership policies** (e.g. widespread state ownership of FIs, reluctance to privatization, the State abuses FIs for social purposes or for fraudulent/corrupt activities). As a result, financial sector is

characterised by high margins, low levels of intermediation and limited range of financial products and services.

The 'structural policies' cluster also includes an assessment of the policies and institutions determining a country's business regulatory environment. This was done with two different criteria in the 2003 questionnaire, 'competitive environment for the private sector' and 'goods and factor markets', which were merged into one, 'business regulatory environment', for the 2004 (and subsequent) questionnaires. However, apart from this change in format, the content of the criteria remained the same between the 2003 and 2004 questionnaires. In both questionnaires, it is assessed to what extent the legal, regulatory and policy environment of a particular country helps or hinders private business in investing, creating jobs and becoming more productive. The narrative guidelines touch upon issues such as: licensing regimes for investment; procedures for entry and exit; the legal framework for addressing anti-competitive behaviour by firms; public sector procurement; state ownership; price controls; state administrative allocations regarding production; shareholder protection and financial disclosure; labour market regulations; barriers to land ownership and procedures to register property. Appendix 4 further highlights the kind of policies and institutions that merit a low and high score.

As such, the economic core of the CPIA has tended to be built around the following precepts: low inflation; an implicit preference for a surplus budgetary position; minimal restrictions to trade and capital flows; 'flexible' goods, labour and land markets; market-determined interest rates; prohibition of directed credit; competition policies guaranteeing equal treatment of foreign and domestic investors ('national treatment'); 'virtually' complete capital account convertibility; protection of shareholder rights ('good corporate governance'); and no restrictions on public sector procurement (WB 1998e, 2000c, 2001j, 2002c, 2003i).

It has duly perpetuated the traditional biases of the WC: a monetarist preoccupation with inflation in the context of monetary and exchange rate policy; a fiscal stance dominated by concerns of crowding out; a bias against trade intervention; a bias against interventions in the commodity and labour markets; a bias in favour of private property rights structures; imposition of Anglo-American corporate governance principles; and a preoccupation with corruption as a source of (static) welfare loss. With this the economic core of the CPIA eliminates the possibility for strategic interventions along which specific sectors of the economy can be promoted and the importance of which to the success of the now-developed countries and the East Asian 'miracle' economies has been repeatedly pointed out.[259]

Yet while most of these prescriptions persistently recurred in the questionnaires steering the successive CPIA assessments between 1998 and 2003, it seems that, with the 2004 CPIA exercise (WB 2004g), the economic core of the questionnaire, and in particular the trade and the financial sector criteria, have been characterised by what at first sight appear to be significant changes. These persist in the subsequent questionnaires (WB 2005e, 2006h).

First, whereas previous questionnaires explicitly assessed the extent to which a country's policy and institutional framework fostered capital movements, the latest versions seem more elusive in that respect. In the questionnaires until 2003, the imperative of an open capital account appeared in two different categories: 'trade policy and foreign exchange regime' and, rather ironically, 'financial stability'. In the 2004 questionnaire, however, it is no longer explicitly mentioned (see appendix 5). The narrative guidelines on the assessment of trade policy in the last CPIA questionnaires (WB 2004g, 2005e, 2006h) focus exclusively on the policy framework regarding trade in goods, without reference to the rules and regulations affecting capital flows.

Secondly, a whole set of specific policy prescriptions regarding the financial sector prevailed in the questionnaires until 2003. In the 2004 questionnaire, however, few of these recur. The preference for market-determined interest rates persists, but the explicit prohibition of directed credit and the imperative of 'national treatment' of foreign investment has disappeared from the questionnaire's narrative guidelines. Even the explicit restriction on state ownership in the financial sector has dropped off the page. Instead, we find a preoccupation with Basle Core Principles (BCPs) for effective banking supervision (WB 2004g, p. 15).[260]

These changes are remarkable. Their meaning is, however, open to at least two and possibly three interpretations. First, some will see the disappearance of the

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259 See chapter three which refers to the well-known contributions by Amsden (1989); Chang (2002) and Wade (2004a). These highlight the importance of the *scope* for discretion on behalf of a developing country government so that a strategy that seeks to move the economy away from low productivity activities and that is adapted to local circumstances can be devised.

260 The BCPs provide a set of international standards of 'best practice' defined by the Bank for International Settlements. See Cornford (2007) on how the introduction of BCPs in developing countries serves as a vehicle to overhaul existing banking supervision. Compliance with BCPs is monitored through the IMF-WB Reports on Standards and Codes (ROSCs), a set of summary assessments of the observance of selected standards relating to private and financial sector development and stability (see http://www.worldbank.org/ifa/rosc_more.html). See Soederberg (2004a, pp. 129-60) for a critique of the ROSCs; see also further below.

explicit mention of a set of policy imperatives as an indication of a certain opening-up of a developing country's policy space. In such an account, it would appear that certain lessons of the PWC, such as the hazards of capital account liberalisation and the fragility of the financial sector in developing countries, as well as issues raised by civil society organisations and academia more generally, have filtered into Bank practice.[261] The alterations to the CPIA questionnaire described above are then seen as an indication of the extent to which these recommendations have found their way into the aid allocation mechanism.

Secondly, it could be that some of these policies have already been comprehensively implemented by debtor countries and hence no longer need emphasising.[262] This observation is in line with Gottschalk's (2005) examination of the macroeconomic content of the PRSPs of fifteen countries. He applauds the relative absence of the imperative of capital account liberalisation from the economic policy prescriptions embedded in the PRSPs of his sample, only to discover that most of the countries in his sample had already fully liberalised their capital account. Moreover, he finds that hardly any PRSP discussed the possible negative implications of such a policy stance or how these could be tackled.

Finally, the question could be raised as to whether it is possible that those imperatives that have disappeared from the narrative guidelines of the CPIAs have somehow become 'embedded', and now steer the CPIA exercise in less visible, but no less pertinent ways. In this context, the guideposts, introduced in 2000 to assist staff in their judgement and which seek to provide 'objective' indicators, acquire particular importance.

It is indeed remarkable that, as the narrative guidelines in the 'structural policies' cluster of the economic core of the CPIA questionnaire changed along the lines described above, the list of guideposts to assist Bank staff in their judgement not only became markedly longer, but additionally and more interestingly, changed in character. While the guideposts in the 'structural policies' cluster of the CPIA questionnaires had previously referred mainly to specific PREM/DEC databases on

[261] For civil society critiques of the Bank's 'scorecard' system, see Eurodad (2002), Alexander (2004), and Northover (2004).

[262] See Emery et al. (2000) on how the investment laws in Ghana, Uganda, Mozambique, Tanzania and Namibia have been altered to contain clauses that guarantee foreign firms' equal treatment with national firms and guarantee foreign investors the right of profit remittance and capital repatriation. See UNCTAD (2000a, pp. 106-7) for documentation of the extent to which LDCs have liberalised their trade, financial sectors, and capital accounts. See also Ndikumana (2003, Table A.1) on the state of controls on foreign exchange and capital account transactions in a set of African countries (as of 1999).

economic indicators, the guideposts in the 2004 and subsequent questionnaires came to include a host of 'diagnostic reports' (see appendix 4).[263] These assess a country's regulatory/policy environment in specific areas and include: IMF IV Consultation Reports (for the 'macroeconomic management' and 'fiscal policy' criteria); Diagnostic Trade Integration Studies (for the 'trade' criterion); FIAS Administrative Barriers Reports (idem); WTO Trade Policy Reviews (idem); Investment Climate Assessments (idem and for the 'business regulatory environment' criterion); Financial Sector Assessments (for the 'financial sector' criterion); the Heritage Foundation's Index of Economic Freedom (for the 'business regulatory environment' criterion); and the WB Business Environment Survey (idem). So have these guideposts come to encompass the policy imperatives that are no longer explicitly mentioned in the narrative guidelines of the CPIA questionnaire?

Originally, the presence of guideposts, which initially consisted mainly of outcome indicators, had raised the issue of how these could affect the judgement of Bank staff when the staff is meant to score policy inputs. The internal Bank evaluation of the PBA system had observed how there is sometimes a built-in conflict between the use of these outcome indicators and the CPIA emphasis on policies rather than outcomes (WB 2001i, p. 12). However, the issue becomes more intractable when the guideposts become dominated by diagnostic reports carrying clear judgements regarding policy and institutional settings.

As indicated above, since the 2004 CPIA questionnaire, the narrative guidelines on the assessment of trade policy in the CPIA questionnaires have focused exclusively on the policy framework regarding trade in goods, without reference to the rules and regulations affecting capital flows. The narrative guidelines on the assessment of the financial sector, in turn, no longer make explicit reference to issues regarding foreign investors, state ownership or directed credit. Closer scrutiny, below, of the guideposts that accompany the narrative guidelines for these respective policy/institutional categories, however, reveals how these specific policy imperatives have in fact been subsumed in the 'diagnostic reports' that now serve as guideposts to staff's assessments.[264] These reports are anchored in a framework of

[263] PREM/DEC Indicators are not officially available for public access. They are, however, sometimes attached to a Country Assistance Evaluation. Appendix 6 provides an example.
[264] In an informal telephone interview, Satish Mannan of the Bank's Operational Country and Policy Services was keen to emphasise that such policies as capital account openness were 'commonly expected' and are 'implicit' in the redesigned questionnaire (27 September 2005). It should also be recalled that the recommendations on the CPIA exercise by an external panel, which steered the 2004 redesign of the CPIA questionnaire, had explicitly endorsed the general economic thrust of the

traditional welfare economics where government intervention is tolerated only in the context of static market failure, and typically embody a bias in favour of foreign investment and trade. More so, the reports translate a set of imperatives for the particular country context, and can assess and prescribe in more *specific* or *country-tailored* terms how liberalisation exercises can be taken further.

Administrative Barrier Reports (ABR) seek to assist Bank staff in scoring a country's trade environment in the CPIA exercise (WB 2004g, p. 11). They are produced by the Foreign Investment Advisory Service (FIAS), a joint service of the Bank and the IFC, and seek to identify what are considered as 'secondary' administrative and regulatory constraints to foreign investment. The reports focus on remaining regulations regarding import/export procedures, taxes, foreign exchange, immigration, and access to land (see Emery et al. 2000; Stone, A. 2003).

The first ABR was conducted for Ghana in 1995 and, since then, FIAS has worked to reduce 'administrative barriers' to investment in more than sixty countries and sub-national jurisdictions (FIAS 2006a, p. 2). Upon closer scrutiny, it appears that it is standard practice for these reports to condemn such traditional policy tools as performance requirements relating to local content, export, local population employment, or local ownership; they deplore 'regulatory barriers' in the labour market and licensing requirements at the sectoral level; and they typically promote the principle of 'national treatment' of foreign investors, full convertibility on the current account and the unbridled right of profit remittance and capital repatriation (see Emery et al. 2000; FIAS 2004, 2005, 2006b). The literature on development has, nevertheless, repeatedly drawn attention to a wide range of investment regulations that the now-developed countries have had recourse to, including those on: entry; ownership (of companies and of land); corporate governance; performance requirements (export requirements, foreign exchange balancing requirements, local content); and explicit requirements regarding technology transfers (see Chang 2004). For Chang (2004, p. 708, my emphasis):

> a strategic and flexible approach is *essential* if countries are to use foreign investment in a way that is beneficial for their long term national interests.

He continues (p. 711):

> restricting the measures of foreign investment regulation is likely to limit the development prospect of developing countries, as there is a clear limit

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questionnaire and not raised concerns regarding particular policy prescriptions – rather to the contrary, in fact (see WB 2004h).

to developing technological and organisational capabilities through 'non-autonomous' integration into global production networks organised by TNCs [Trans-National Corporations].

Embedding the liberal imperatives regarding foreign investment in the diagnostic reports steering staff assessments in the CPIA exercise further reduces the policy freedom necessary for developing countries to promote (FDI-assisted) industrial development, already constrained through various WTO agreements (see Wade 2003; Lall and Narula 2004).

Similar observations can be made regarding another, almost overlapping, diagnostic report, the ICA, which appears on the CPIA questionnaire as a guidepost to assess the trade and business regulatory environment of a country. The ICA was introduced as part of the Bank's PSD Strategy with the purpose of providing the means of tracking the performance of a country on achieving PSD targets (IEG 2006, p. 84).[265] As such, an ICA seeks to analyse conditions for private investment and enterprise growth in a particular country (and across various sectors). Underpinning every ICA is a standard core investment climate survey instrument, which benchmarks indicators of the quality of a country's investment climate in a way that seeks to facilitate cross-country comparisons as well as the monitoring of changes in individual countries over time (p. 10).

According to Ellerman (2001b), a former Bank official, ICAs tend to be biased in interpreting the investment climate in terms of foreign investors and assess foreign investors' needs in what are described as 'dangerously narrow terms' – favouring labour market flexibility over job stability and human capital investment, and stock market liquidity over long-term predictable investment flows. Scrutiny of a sample of these assessments reveals the recurrence of the following imperatives: establish a low-cost business operating environment; update the investment code to establish a 'competitive' investment environment; lower taxes on firms; ensure 'sound' financial market development in which the government does not crowd out the private sector, in which state owned banks are privatised, and where banking regulations are revised to relax barriers; privatise social sector and infrastructure services provisioning; continue trade reform; fight corruption; reduce fiscal deficits; establish clear land titles; increase labour market flexibility as well as enhance

[265] See Stone, A. (2003) on the complementarities and differences between the ICA and the ABR.

productivity of the labour force through education and training (with a facilitating rather than provision role for the government).[266]

To evaluate a country's record on policies and institutions affecting trade, the Bank staff is further guided to consult relevant Diagnostic Trade Integration Studies (DTISs). DTISs are conducted through the Integrated Framework, a multi-agency programme that seeks to assist the LDCs in expanding their participation in the global economy. They often, however, take place under the leadership of the Bank (see Powell 2002). The studies aim to evaluate 'internal and external constraints' on a country's integration into the world economy and provide yet another avenue for the Bank to pursue an 'unfinished trade liberalisation agenda' (WB 2003c, p. 5). This combines with recommendations regarding the investment climate (WB 2004a).

As such, DTISs provide specific indications regarding how to remove remaining barriers to trade in a particular country context and, in particular, regarding how to reduce protection for import-competing industries. They abound with assessments of the extent to which foreign firms need to meet specific performance goals or guidelines (WB 2004a, p. 42). And they tend to include specific assessments regarding the state of the capital account and regarding the regulation of financial services.[267] The DTIS on Burundi, for example, refers to the advanced state of liberalisation of the capital account and the internationalisation of financial services in neighbouring Uganda (measures which imply convertibility of the currency and the elimination of any discrimination against foreign suppliers of financial services and their local correspondents), urging the government to follow this model of good practice – although 'with the necessary attendant prudence'.[268]

Financial Sector Assessments (FSA) are to steer assessments of a country's financial sector policies in the CPIA exercise. They are a joint IMF-WB effort and were introduced in 1999 in response to the financial crises of the late 1990s. They aim to increase the effectiveness of efforts to promote the 'soundness' of financial systems in member countries and seek to 'assist' a country in designing its regulatory framework for the financial sector, with special attention to the aptitude of the financial system in delivering credit to the private sector, and to small- and medium-

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266 The following ICAs were consulted: Kenya (2004); Lesotho (2007); Zambia (2004); Tanzania (2004); Uganda (2004); Mozambique (2003); Senegal (2005). For a list of completed ICA reports, see http://web.worldbank.org/WBSITE/EXTERNAL/COUNTRIES/AFRICAEXT/EXTAFRSUMAFTPS/0,,contentMDK:20763282~menuPK:2059605~pagePK:51246584~piPK:51241019~theSitePK:2049987,00.html#completed While ABRs are confidential and the client controls the distribution outside the WBG/government circle, ICAs are often posted on the WB website following clearance.

267 Specific DTISs can be consulted at http://www.integratedframework.org.

268 http://www.integratedframework.org/files/dtis_burundi_5nov03.pdf, p. 44.

sized enterprises in particular. Significantly, they embed the notion that the primary role of government in the financial sector is to be limited to providing a regulatory, supervisory and legal framework that seeks to promote 'soundness' and competition in the financial system.[269]

Finally, a set of non-Bank (or IMF) reports appear as guideposts on the CPIA questionnaire. These include the Heritage Foundation Index of Economic Freedom (HFI) as a guidepost for the assessment of a country's business regulatory environment. The HFI focuses on measuring the degree of government involvement in the production, distribution or consumption of goods and services, and displays a blatant anti-interventionist bias and a particular concern for the regulatory environment affecting foreign firms. The CPIA exercise also draws on WTO Trade Policy Reviews. This may reflect the commitment to greater co-operation between the Bank and the WTO enshrined in the Declaration on the Contribution of the World Trade Organisation to Achieving Greater Coherence in Global Economic Policymaking in the Final Act of the Uruguay Round (Marrakesh, 15 April 1994, p. 387) and the various subsequent follow-up progress reports.[270] Reference to IMF reports for macro-issues (through its Article IV Consultations) further affirms the traditional recognition of the IMF's expertise in this area.

So while certain imperatives have disappeared from the explicit narrative guidelines of the CPIA questionnaires, they have become embedded in the various diagnostic and advisory reports which now feature as guideposts to staff awarding particular scores on the various CPIA criteria and perpetuate the original economic (and financial) bias. These reports are produced mainly under WB patronage and allow the pursuit of a particular agenda in more country-tailored fashion. They are part of the broader knowledge endeavour the WB engages in, elaborately documented in chapter two, and sit alongside a host of other diagnostic and advisory instruments produced by, or jointly with, other agencies, including the joint IMF-WB ROSC or the OECD's Policy Framework for Investment (OECD 2006c). These reflect socially constructed norms of 'common standards' regarding PSD corresponding to the ideas steering the Bank's PSD strategy (see chapter two).[271]

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[269] However, in the context of capital market development, parastatals are often encouraged to issue bonds and shares through public offerings as this would contribute to the development of the market. FSAs are available for consultation at http://www.imf.org/external/np/fsap/fsap.asp.
[270] Available at www.wto.org.
[271] For the ROSC, the IMF assesses practices in the area of data dissemination and fiscal transparency. Modules for the financial sector (monetary and financial policy transparency, banking supervision, securities market regulation, payment systems, deposit insurance) are mostly derived as by-products from a parallel WB-IMF Financial Sector Assessment Program (FSAP). The WB provides

In this context, the Bank has actively been seeking to define a new profile for itself – in line with the knowledge emphasis – in terms of the 'benchmarking' of business environments in developing countries, through its various diagnostic reports including the Doing Business indicators, ABRs, ICAs, IC surveys, and the ROSCs (see IMF/WB 2004, pp. 4-5).[272] A recent Bank report specifies, WB (2005d, p. 30):

> The Bank operationalises the findings and information from these tools in the CPIA, and therefore in Bank lending allocations, and through Country Assistance Strategies and programmatic lending. In addition, some of these tools serve as global public goods through cross-country comparisons and benchmarking. Almost all provide specific country level information to better analyse and design appropriate reform.

The reconfiguration of the CPIA along the lines documented above then allows the two crucial dimensions of Bank influence – the deployment of the CPIA as cornerstone to its aid allocation decision-making *and* as a conduit for its knowledge exercise – to come together in its interaction with LICs. As aptly observed by the Bank itself (IDA 2007b, p. 1):

> As a major pillar of the multilateral core of the global development architecture, IDA plays a central role in two dimensions: resources flows and policy dialogue. These two dimensions come together in the form of IDA's PBA system.

6.4.2 Beyond the economic

The economic core of the CPIA is complemented with 'equity' and 'governance' concerns. These are grouped, respectively, in the 'policies for social inclusion/equity' cluster and the 'public sector management and institutions' cluster. We briefly discuss the various criteria that are included in these two clusters. Appendix 5 specifies in more detail what merits a low and a high score for each

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assessments in three areas additionally covered by ROSCs: (1) corporate governance; (2) accounting and auditing; and (3) insolvency regimes and creditor rights'. Soederberg (2004a, p. 131) notes that while participation in the ROSC is strictly 'voluntary', refusal to submit to the practice would inevitably send negative signals to the international investment and financial communities. The Policy Framework for Investment provides a 'checklist of important policy issues for consideration by any government interested in creating an enabling environment that is attractive to all investors' (OECD 2006c, p. 7). Its core purpose is 'to encourage policymakers to ask appropriate questions about their economy, their institutions and their policy settings in order to identify their priorities to develop an effective set of policies and to evaluate progress'.

[272] The Doing Business database (http://www.doingbusiness.org/) provides measures of business regulations and their enforcement in a host of areas including: starting business; dealing with licenses; employing workers; registering property; getting credit; protecting investors; paying taxes; trading across borders; enforcing contracts; closing a business; and economic characteristics.

criterion. Unlike the economic core of the CPIA questionnaire, the clusters on 'social inclusion' and 'public sector management and institutions' have seen little substantive change between the 1998 and 2006 questionnaires.

The first criterion in the social cluster is 'gender'. This was introduced as a separate category in the 1999 questionnaire. The state of gender equality is assessed across three dimensions: human capital; access to economic and proactive resources; and status and protection under the law (WB 2006h, p. 19). The only remarkable change in the consecutive narrative guidelines for the assessment of gender issues is the disappearance of an explicit reference to ratification of the Convention on the Emancipation of All Forms of Discrimination Against Women (CEDAW) from the scoring system with the 2005 questionnaire (WB 2005e).

The subsequent criterion in the social cluster considers 'equity of public resource use'.[273] This assesses the extent to which the patterns of public expenditure and revenue collection affect the poor and are consistent with national poverty reduction priorities (p. 21). More specifically, the criterion examines: whether mechanisms exist to identify the poor and vulnerable; whether these groups are adequately assisted; and whether the composition of public expenditures is tracked systematically to give feedback into subsequent resource allocation decisions. Regarding revenue collection, it assesses whether a country's tax system is progressive or regressive, and how it aligns with poverty reduction priorities. The guideposts that are to assist staff in making their judgement include the JSAn, and some core diagnostic reports including the PER, PA and the CEM (see Appendix 1).

The next criterion is 'building human resources', also added to the CPIA questionnaire in 1999. Its narrative guidelines have been elaborated since, and today the criterion assesses national policies and public and private sector service delivery conditioning access to, and quality of, health and nutrition services, education, and the prevention and treatment of HIV/Aids, tuberculosis and malaria (p. 23).

The 'social protection and labour' criterion assesses government policies in the area of social protection and labour market regulation. It considers whether these reduce the risk of becoming poor, how well the poor are assisted 'to manage further risks', and whether a 'minimal level of welfare' is guaranteed to all people (p. 27). The staff is to examine the following: the nature of the social safety net programme, pension and old age savings programmes; protection of basic labour standards (ILO

[273] From the 2000 questionnaire onwards (WB 2000c), this criterion replaced 'pro-poor targeting of programs' in the 1998 questionnaire. Since the 2004 questionnaire, it includes the previously separate criterion of 'poverty monitoring and analysis'.

Conventions); the regulations regarding segmentation and inequity in the labour market; labour market programmes such as public works or job training; and whether 'community-driven development' is being encouraged by the government. Finally, this cluster includes a criterion assessing a country's policies and institutions relating to the environment.[274] It assesses the extent to which environmental policies foster the protection and sustainable use of natural resources and the management of pollution (p. 31).

In the governance cluster we find another five criteria. The first one, 'property rights and rule-based governance', examines the extent to which private economic activity is facilitated by an effective legal system and a rule-based governance structure in which property and contract rights are respected and enforced (p. 32). The next criterion assesses the 'quality of budgetary and financial management'. It considers whether there is a comprehensive and credible budget linked to policy priorities; whether there are effective financial management systems to ensure that incurred expenditures are consistent with the approved budget, that budget revenues are achieved and that aggregate fiscal control is maintained; and whether there is accurate fiscal reporting. Since the 2005 questionnaire (WB 2005e), the explicit link of policy priorities to poverty reduction has been removed from the guidelines for this criterion. So while the guidelines traditionally directed staff to assess whether 'policies and priorities that focus on poverty reduction are reflected in the budget' (WB 2004g, p. 36), this has now become reduced to an assessment of whether 'policies and priorities are reflected in the budget' (WB 2006h, p. 35).

'Efficiency of revenue mobilisation' is, further, assessed. Alongside this criterion, the overall pattern of revenue mobilisation (the nature of tax policy as well as the quality of the tax administration) is examined (p. 37). As can be seen from the specific guidelines reproduced in Appendix 5, revenue mobilisation on the basis of 'low-distortion' taxes such as VAT or property taxes (rather than trade taxes) is favoured, as well as a single statutory corporate tax comparable to the maximum personal income tax rate. Another governance criterion touches on the quality of public administration and assesses the extent to which the civil service can design and implement government policy and deliver services effectively (p. 39). Finally, transparency, accountability and corruption in the public sector are assessed. Can the

[274] This criterion originally belonged in the 'structural policies' cluster and was moved in the 2004 questionnaire to the social cluster. This reshuffle coincided with the disappearance from the narrative guidelines of an explicit assessment regarding the availability and financial sustainability of water and sanitation services.

executive be held accountable for its use of funds and the results of its actions by the electorate and by the legislature and judiciary? Are public employees within the executive required to account for the use of resources, administrative decisions, and results obtained? What information channels exist so that civil society can scrutinise public affairs? And, to what extent is the state captured by 'narrow vested interests' (p. 41)?

The addition of these social and governance issues to the economic core along these lines raises a set of issues. First, the 'social' and 'institutional' are added onto the 'economic' without reflection upon the social and institutional dimensions of the latter. In line with orthodox understandings of the discipline of economics, the social and/or institutional remain marginal to the economic, and are addressed *ex post* or separately through recourse to specific institutions/policies (targeting, safety nets, 'governance' measures). Yet the 'economic' agenda promoted through the CPIA is intrinsically 'social' as well as 'institutional'. This has a number of contradictory implications. The social criteria rated in the CPIA, apart from being added *ex post*, are constrained (and often negatively affected) by the economic imperatives defended in the economic (and governance) core of the CPIA questionnaire. Take, for example, the criterion that assesses a country's policy performance in the areas of social protection and labour market regulation, and which assesses whether government policies (in the area of social protection and labour market regulation), WB (2006h, p. 27):

> reduce the risk of becoming poor, assist those who are poor to better manage further risks, and ensure a minimum level of welfare to all people.

Yet labour market issues are also covered in the criterion assessing a country's business regulatory environment, where the focus is on the effects of labour market regulations on firms' employment decisions. Following the latter, a country is urged to have an employment law that provides a high degree of flexibility to hire and fire at low cost, and state intervention is to be limited to regulation and 'legislation to smooth out market imperfections' (p. 18).

In addition, the social cluster includes an assessment of the equity of public resource use which, among other things, seeks to guarantee that a country's tax system is not regressive. Yet within the governance cluster, with its much larger effective weight in the PBA exercise, a set of specific prescriptions prevail regarding the 'efficiency' of revenue mobilisation. These reflect a clear preference for indirect taxes like VAT, which are generally known to be regressive and to augment poverty (see WB 2001f, p. 70).

Furthermore, the various specifications of good policy in such areas as building human resources or social protection sit awkwardly with the stringent fiscal and monetary order embodied in the economic management cluster. The reality of the trade-offs between these different imperatives is ill-appreciated in the design of the questionnaire. In this context, it should be remembered that the social criteria effectively carry the lowest weight in the allocation norm deployed by the Bank – affecting the PBA only marginally. As mentioned above, all clusters in the CPIA carry a 25 percent weight. The economic clusters, however, each include only 3 criteria. This reduces the weight of the criteria in the social and governance cluster, except that the weight of the latter is heavily inflated in the actual allocation norm through the application of a governance factor. The social is subordinate to the economic imperatives of macroeconomic stability and private (and foreign) sector promotion, and to the preoccupation with 'governance' issues.[275] This was further accentuated with the disappearance of the emphasis on poverty reduction from the criterion that assesses the quality of budgetary and financial management (see above).

Secondly, the relationship to development or growth (and thus aid productivity) of the governance issues incorporated in the CPIA remains dramatically ill-understood (despite new growth theory). Such an examination takes on a particular importance given the effective weight the governance criteria carry in the IDA's allocation norm, with – as was documented above – the weighted average of the CPIA and ARPP being multiplied by a governance factor before feeding into the actual allocation norm.

Governance came to adorn the Bank's agenda in the late 1980s (WB 1989) and evolved into a fully-fledged agenda item over the subsequent decade (WB 1992b, 1994b, 1997c). Concerns regarding governance were incorporated into the Bank's performance assessments in the early 1990s and, with the 1998 redesign, came to constitute an entire cluster in the CPIA questionnaire. For the Bank, 'good governance' implies a 'public service that is efficient, a judicial system that is reliable, and an administration that is accountable to its public' (WB 1989, p. xii).

[275] It should also be noted that, given that the scores on the various CPIA criteria have not been normalised and that it is apparently easier to score more highly on the set of economic criteria than on the equity/social inclusion criteria (WB 2001i, p. 20), the effective weight of the former is further reduced.

Three aspects of governance are distinguished: (1) form of political regime; (2) the process by which authority is exercised in the management of a country's economic and social resources for development; and (3) the capacity of governments to design, formulate and implement policies and discharge functions (WB 1992b).

Operationally, the first aspect lies outside the Bank's mandate, which officially precludes it from letting political considerations influence its investment decisions.[276] As a result, the Bank has attempted to restrict itself to the 'economic' dimensions of governance. In practical terms, this has been interpreted as including: improving public sector management; increasing accountability; promoting transparency and information; strengthening the legal framework for development (including the establishment and protection of private property rights); promoting participation in programme and project design; and control of corruption and military expenditure (WB 1992b, 1994b).

Most of these concerns are covered in the current CPIA governance cluster as it seeks to reward the familiar order of well-defined, transparent and well-protected property and contract rights; comprehensive, consistent and balanced budgetary practices; revenue mobilisation on the basis of 'low-distortion' taxes such as VAT or property taxes (rather than trade or turnover taxes); merit-based hiring and promotion in the civil service (p. 40); and the establishment or existence of formal mechanisms (separation of powers, 'independent' media, information disclosure) to enforce high degrees of accountability and transparency, discouraging corruption or the abuse of public office for private gain (p. 42).

The Bank's promotion of these governance features rests on a particular understanding of the role of the state. Yet to the extent that the underlying model of the state is ill-suited to the context of developing countries, its derivative governance prescriptions will be misguided. The view of the role of the state with which the Bank's governance agenda tallies is comprehensively depicted in the 1997 WDR (WB 1997c). As pointed out in chapter three, the interventions ascribed to the state in this Report are, in principle, more extensive than projected under the state-market antagonism associated with the WC, with a broader appreciation of the incidence of market failure as the 'perfect markets' paradigm of the WC is replaced by an 'imperfect markets' paradigm. The 1997 WDR acknowledges that markets fail more persistently than previously recognised, and that this is especially relevant for the

[276] This is in contrast to bilateral donors, most of which have placed heavy emphasis on human rights and democracy.

context of developing economies. The state becomes a necessary element ('partner') for the adequate functioning of the market economy.

In practice, however, a set of institutional arrangements are prescribed, drawing on 'inter-sectoral partnerships' between the state, private profit and non-profit sectors, and these project a persistent bias against direct state presence or strategic interventions on behalf of the state in the economy. It was argued in chapter three that such a depiction of the state's role reveals a persistent legacy of the new political economy and, in particular, of orthodox notions of static welfare loss attributed to 'rent-seeking' (see Stiglitz 1996, p. 156).[277]

Yet, the processes that drive development can not be understood as an unfortunate deviation from a particular norm of liberal governance, but emerge as strategies of adaptation and survival in contested settings. The implications of specific governance arrangements for growth and development crucially depend on: the particular constellation of the political-economic forces both within the state and society (and the nature of the relationships between these); the state of development; the nature of the international relations of the country; etc. Both the state model and its derivative governance arrangements – embodied in the CPIA constitute a technicist and ahistorical attempt to deal with complex underlying political-economic processes.

The policy/institutional imperatives embedded in the CPIA matrix, whether touching upon the property rights regime, corruption, budgetary and financial management processes, tax regimes, quality of public administration or transparency in the public sector, further, at most describe what certain advanced economies could look like. In the context, for instance, of the emphasis on 'low-distortion' taxes, Baunsgaard and Keen (2005) document that while high-income countries have managed to offset reductions in trade tax revenues in the last 25 years by increasing their domestic tax revenues, LICs have on average recovered no more than around 30 percent of lost trade tax revenue. An UNCTAD Report (2002, p. 52) also reminds us that:

> there is considerable institutional diversity even among industrial countries today. Imposing a common institutional standard on all countries, with widely varying conditions, is likely to be counterproductive ... Experience shows that attempts to superimpose such institutions on existing economic,

[277] See, again, Chang (1996) and Khan and Jomo (2000) for a critical appraisal of 'rent-seeking' and development.

social and political structures in developing countries may not only fail, but may also put considerable strains on their financial and human resources.

As noted in chapter three, an alternative approach would recognise the potential importance of a wide range of interventions on behalf of the state in a developing country; anchor the analysis of governance (and growth) in its political-economic reality; move away from normative projections regarding governance phenomena, informed mainly by orthodox presumptions regarding market efficiency; and refrain from imposing such liberal norms as embodied in the CPIA exercise in a bid to take account of diverging conditions across developing countries.

Finally, most recently, the Bank has engaged in a set of econometric exercises trying to establish a *causal* relationship between the CPIA and growth (or development outcomes) (see Gelb et al. 2004; IDA 2007b). Hence, while we know that the CPIA has developed in an incremental manner, with certain criteria added and removed over the years mainly at the request of IDA Deputies, and that no theoretical body exists establishing a distinct relationship between the various separate criteria and growth, let alone an index, the Bank now seeks to produce 'evidence' (*ex post*) that there is a positive relationship between the CPIA and growth (or development outcomes) *and* that this relationship is causal. These exercises typically include as RHS variables: the CPIA; change in the CPIA; an Africa dummy; an indicator of the prevalence of HIV/AIDS; and the initial value of the development indicator (life expectancy, under five mortality rates or immunisation rates). They are prone to the various criticisms of cross-country growth equations (see chapter five). Particularly striking, however, is the absence of aid from the regressions. IDA (2007b, p. 24) nevertheless concludes that (my emphasis):

> these results … support the use of indicators along the lines of the CPIA … to provide an *effectiveness-based anchor* for the system of development assistance, including the potential value of such indicators in facilitating an open and inclusive dialog on development progress.

6.5 Conclusion

The practice of selectivity strengthens the link between aid disbursements and the state of a country's policy and institutional environment. The CPIA sits at the core of the Bank's selectivity mechanism and has rapidly risen to prominence in the broader donor community. Since 2000, the CPIA mechanism has provided the Bank with a structured consultative exercise with domestic counterparts, perhaps becoming akin to IMF Article IV consultations. The signalling function of the CPIA has also been enhanced with the disclosure, since 2005, of the numerical scores for IDA-eligible countries.

Closer scrutiny of the CPIA in this chapter revealed how it imposes a uniform policy matrix on LICs which is ill-suited for the realities of development. It does so both explicitly through its narrative guidelines and implicitly through reference to a set of diagnostic reports that have been incorporated as guideposts for the CPIA rating exercise. The role of these diagnostic and advisory reports draws attention to the significance of the Bank's 'knowledge' exercise for conditioning the practices of development in the LICs. This ties in with the other knowledge initiatives elaborately documented in chapter two (the training programmes of the WBI, the research activities of the GDN, the provision of information and analysis through the GDG and the fostering of links with the academic community through the RAD).

As such, Bank assistance to LICs remains conditional on a core set of neo-liberal policies, with a veneer of social and governance concerns. Yet these are now imposed through more subtle and less visible mechanisms – possibly to accommodate the contradictions between the persistence of a set of imperatives at the core of Bank practices and the rhetorical shifts it has sought to promote.

Conclusion. Tightening the web: selectivity, knowledge and the WB

We have been concerned in this thesis with a moment in the regulation of aid that succeeded the 'structural adjustment' era – when aid policies were dominated by the adjustment discourse and its related practices, including the rapid ascent of conditionality and the WC. We saw this new moment as characterised, essentially, by a decline in the donor community's willingness to finance aid, combined with an attempt to increase its leverage in the pursuit of a persistent core neo-liberal agenda – against a backdrop of increasingly popular discourses on 'ownership', 'participation' and 'partnership'.

This development was seen as anchored in a belief in, and commitment to, the potential of private flows to finance development – now projected as a superior substitute for aid – which steadily took hold in the donor community during the 1990s (see UN 2002). Following this, a mainly residual and auxiliary role for aid emerged as part of the rapid expansion of private financial flows, with an emphasis on its role in promoting an enabling environment for private (domestic and foreign) investment. Stern and Lankes (1998, p. 105) pointed to the implications for the role of the IFIs as follows:

> Since the importance of IFIs as a source of funds has decreased while the potential role of the private sector has increased, a central challenge for IFIs is to find ways of fostering development through expanding opportunities for the dynamism of the private sector. They should view the private sector as a prime vehicle for the achievement of development goals.

We posited, in chapter one, that as the donors' willingness to finance aid decreased, their ambition to interfere with recipients' affairs (both economic and beyond) persisted, if not increased. We saw this as taking effect, if somewhat paradoxically, through a shift away from coercion as a mechanism to impose a set of reforms towards more subtle means of influence. Under the projected 'new partnership model' a range of new aid emphases and mechanisms coalesced, including: the PRSP; the redefinition of the purpose of aid and of the use to which the various aid instruments are put; changes in the sectoral composition of aid; the 'selectivity' paradigm according to which aid flows are to be disbursed on the basis of past rather than future actions; and the formalisation of a knowledge role for the donor community – and for the WB in particular.

We focused on selectivity as a redefinition of conditionality, and the special role of the WB in this, with a formal and explicit emphasis on its knowledge role conveniently linked to the selectivity proposition. We documented, in chapter two, how the Bank had taken on a leadership role in the aid regime during the structural adjustment era and how a set of changes in the political, economic and financial environment in which it operates – including the evolution of its constituent public and private affiliates and the relationship of the Bank's aid window with its donors – made the redefinition of the role of aid along these lines particularly compelling for the institution.

Following Bank arguments, selectivity is meant both to direct resources to environments where they are expected to be relatively more effective as well as encourage LIC governments to 'improve' their policy performance (through some form of 'demonstration effect'). Upon the premise that aid finance affects an economy positively only after countries have made substantial 'progress' in reforming their policies and institutions, it is argued that aid should be allocated following the assessment of a country's policy and institutional environment. Further, 'successful' aid in 'difficult' environments typically involves 'intensive staff input' and small disbursements of finance. In these environments, effective assistance is more about 'ideas' than about finance. Indeed, the latter can harm the former. The knowledge of the donor community, and especially that of the Bank, acquires particular significance, and chapter two elaborately documented the various channels through which the Bank exercises this role. It drew attention, specifically, to the fast and vast expansion of ESW, the applied 'development knowledge' originating in the Bank's operational departments, and the rapid promulgation of a set of 'global' knowledge initiatives, aimed at drawing in local policy and opinion makers.

It was further observed, in chapter three, how the new directions in aid policy – with its embedded 'knowledge celebration' – were concurrent with an endeavour at the Bank, instigated by then President James Wolfensohn and led by then Vice-President Joe Stiglitz, to propose a 'new' approach to development. The latter sought to project a break with the WC, the policy paradigm that had prevailed during the adjustment era, by attempting to re-emphasise the broader scope and distinct features of development. Development was no longer a technical matter focusing on prices, but a societal process involving broad transformations which was ill-served by the neoclassical orthodoxy of perfect markets. A call was made to move towards a PWC and the Bank formalised a CDF to serve as an over-arching approach in its engagement with LICs.

These innovations were accompanied by a sense that the more ideological aspects of the development debate had been neutralised with the end of the Cold War and the advances in economics. For Stiglitz (1999c, p. 14), the grand ideological battles were over, with now 'almost universal agreement' that markets should be at the centre of any vital economy. Within this broad agreement, the continuing debates were 'over more technical matters, such as how to respond to economic crisis, how to undertake financial reform, and what is the proper sequencing of privatisation'.

Through such a prism, the Bank emerges as a 'clearing-house for knowledge about development', a corporate 'memory bank' of best practices, and an 'honest broker' of development knowledge. In the few formal arguments defending a knowledge role for the Bank, the creation and dissemination of knowledge appears as an IPG characterised by under-provision. This gives rise to a crucial role for the WB, which, as it is understood, has a comparative advantage of scale and scope in the production and dissemination of 'development knowledge'.

We pointed out in chapter two how, in such an account, the socio-historical, political and economic context in which knowledge comes about and is put to use is dramatically disregarded – with the particular failure to account for the way in which features of the WB's own political economy might affect norms of 'scientific' acceptability, exacerbated by the leading role of economics at the Bank and the particular state of the discipline. We then argued, across chapters two and three, that the pernicious implications of the specific political-economic and financial realities, within which the Bank is anchored, for projected preferred paths for development have persisted together with the limits of mainstream economics for understanding social phenomena in general, and development in particular (despite the more rounded PWC relative to the WC).

An example of these limits on the Bank's self-proclaimed knowledge advantage was provided by the research put forward by the Bank in support of its selectivity paradigm. In almost archetypal fashion, this research embodies the hazards plaguing an institution fulfilling crucial 'advocacy' roles driven by its own political-economy and operational priorities. A closer look at the operational imperatives this research was trying to defend, embodied in the CPIA, revealed a particularly crude articulation between operational imperatives, research and rhetoric at the Bank in this specific area – its core pertaining to the demarcation of a country's policy space. These issues were illustrated across three successive chapters.

Chapter four first surveyed the literature on aid and conditionality effectiveness preceding the selectivity proposition. It pointed to a failure within mainstream approaches to reveal the true dynamics affecting aid outcomes – essentially as a result of a reductionist understanding within mainstream economics of what growth is, what aid is, and how these are likely to interact. We illustrated how successive attempts to remedy the shortcomings of one of the early contributions to the aid impact literature, the two-gap model, remained constrained by their ad hoc and partial nature where the underlying realities steering the aid relationship – ignored ab initio – remain concealed and ill-understood.

The explanatory power of the old economics of aid remains limited by the tendency of mainstream economics to see the economics and the politics of a particular phenomenon, here aid, as distinct and separate, and by the prevalence of what has been termed the 'financial-intellectual complex' – where the conjunction of development assistance and research conditions the scope and nature of the research effort, here infused with particular presumptions regarding the purpose of aid. We argued that, as a result, the old economics of aid was characterised by a persistent incapacity to take the specific and defining features of aid, conditionality and development in particular country settings into account. The extent to which the various dimensions and institutions of aid manage to restructure the recipient/debtor economies has been easily downplayed and the role of aid in the broader political-economic-financial setting misunderstood.

These shortcomings were perpetuated, if not exacerbated, with the new economics of aid that emerged to support the propositions of selectivity and knowledge as aid. Close scrutiny, in chapter five, of a core set of Bank-propagated premises regarding aid and conditionality revealed dramatic epistemological failures characterising this research. Poor scholarly standards combined with the dramatic unsuitability of the policy recommendations for the reality of the LICs.

Yet the research was highly instrumental in promoting the Bank's preferred policy stance of PBA of aid across the broader donor community. The serious issues of reliability and relevance of the research findings appeared to be of lesser concern compared to the perceived operational advantages which they seemed to imply. The new paradigm of selectivity, crucially, embodies the notion that the key to the effectiveness of aid and growth lies entirely with the recipient, to the further neglect of the structural relations within which donor and recipient interact and the broader non-aid related features that determine that setting (such as terms of trade; access to markets; debt; or capital flight).

At the Bank, the selectivity practice is anchored in a particular policy matrix which is embedded in the structural assessment tool at the core of its PBA mechanism, the CPIA. The CPIA was placed in the public domain recently and has been vigorously promoted by the Bank across the broader donor community. A closer look in chapter six at the particular criteria that constitute the CPIA revealed the persistence of a set of specific imperatives at the core of Bank operational practices, often at variance with Bank rhetoric. These touch upon familiar neo-liberal norms, augmented with a set of social and governance concerns.

Apparent changes in the CPIA questionnaire most recently, moreover, indicate how there has been a shift from the explicit, albeit general, pursuit of a set of policy imperatives, to a more embedded and less visible, yet more specific, promotion of particular imperatives through increased reliance on the WB's 'diagnostic' capacity. This ties into the broader promotion of the Bank's knowledge stature – most recently through the proliferation of a set of specific knowledge initiatives documented in chapter two – and can possibly be understood as an attempt by the Bank to contain the contradictions resulting from the conjunction of its discursive shifts, as through the PWC, and the persistence of a set of economic (and financial) imperatives (including privatisation and trade and financial openness) at the heart of its operational realities.

Ultimately, we see the CPIA-knowledge framework as contributing to the establishment of a logistical aid framework that seeks to facilitate further the adoption of the Bank's reform agenda focused on a particular understanding of PSD, with now a broader reach than was originally the case under the era of structural adjustment. The new paradigm then intrinsically implies, borrowing Soederberg's (2004a) expression, 'an intricate web of surveillance and discipline' that aims to spin 'common-sense values' across and within national spaces.

What are the implications of these findings for further critical study of aid realities and practices? First, it clearly transpires from the above that development cooperation would benefit from more concerted attempts on behalf of donors to scale up aid, alter the composition of aid (in favour of the productive sectors and economic infrastructure), not marginalise the state as a partner, and reduce the various conditions that accompany aid flows, instead of the existing trend towards greater stringency in the imposition of a set of policy and institutional arrangements with dubious repercussions for growth and development that has accompanied the reluctance to finance aid. This has been repeatedly pointed out in the literature (see chapter five). A more general appreciation of the need for an integrated understanding of the dynamics of aid, taking into account the broader international and domestic economic, political and financial features impinging upon aid outcomes, would also move the debate forward.

However, given the current political-economic-financial reality within which aid policies and practices take form, the chances for a substantial re-orientation of aid policy appear slim. The aid agenda seems likely to remain dominated by the strong commitment to PSD on behalf of the main donors, with specific implications for the preferred partners for aid, the composition of aid, as well as the conditions attached to it. A recent UNDP publication, *The New Public Finance* (Kaul and Conceição 2006) is indicative, compiling a large collection of papers all of which explore the way in which issues of public finance can be taken forward wholly in line with the rapid ascent of private financial flows and donors' commitment to private finance as the main source of external finance for developing countries.

Unless new sources of development finance create a new political economy underlying aid policy-making, this direction is not likely to change fundamentally in the near future. The terms on which the broad agenda of PSD is imposed through aid, then, need further scrutiny and the relationship to the local realities of LICs to be continuously and critically assessed. This touches upon the set of macro, structural and governance conditions imposed through such mechanisms as the CPIA; the various dimensions of the donors' knowledge exercise; the proliferation of mechanisms like OBA – where aid acts as a vehicle for the expansion of private, and that is often foreign, enterprise; and, the evolving collaboration between the IDA, the Bank's aid window, and the IFC, its private sector affiliate.

With the emphasis on the ideational aspect of aid in the pursuit of this agenda, the imperative further emerges to scrutinise carefully the knowledge produced by the donor community, and the Bank in particular. Crucially, this extends beyond the knowledge emerging from the Bank's research department. The bulk of the Bank's 'development knowledge' is produced in its operational departments, and its training programme and 'global knowledge initiatives' have expanded rapidly. These remain, however, the subject of relatively little scrutiny. Such an investigation could be taken further forward by extending the analysis to include an exploration of the role of Northern institutions in economics education more broadly, as for instance through the internationalisation of education, and its implications, among other things, for the conceptualisation of the policy space in the developing world, and the important role the WB (and the IFC) are assuming in this context.

More parochially in this context, the issue arises as to how the researcher profiles her- or himself vis-à-vis the vastly expanding knowledge realm of the Bank. Will the scope for critical engagement remain limited and circumscribed and, if so, is great caution necessary in the context of an ever-expanding Bank presence through various knowledge initiatives? Or are these issues less rigid and could the world of ideas, even within the Bank, be more porous than its operational translations would lead us to believe?

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Appendix 1: Economic and Sector Work at the Bank.

Core diagnostic ESW:

The *Country Economic Memorandum* (CEM) and *Development Policy Review* (DPR) seek to provide an analysis of key aspects of a country's economic development, such as growth, fiscal reform, public administration, foreign trade, financial sector development and labour markets. They assess strengths and weaknesses of an economy and its policies, and provide a set of policy recommendations – much in line with the priorities embodied in the CPIA matrix.

The *Poverty Assessment* (PA) seeks to provide information on the causes and consequences of poverty in a country and examines how public policies, expenditures, and institutions affect poor people. It provides a profile of the poor – detailing their living conditions and describing their changing situation over time – and seeks to identify a set of challenges perceived as confronting those trying to escape poverty. PAs tend, however, to be characterised by the following shortcomings (see Hanmer et al. 1999). They over-emphasise an income measure of poverty, defined against an arbitrary poverty line (see Reddy and Pogge 2005). They are often weak in identifying the structural causes of poverty and disregard historical elements, the political context and such international dimensions as debt and commodity prices. Instead they tend to focus on aggregate and sectoral growth performance as the main explanatory factors of poverty trends. Their recommendations are usually centred on a three-pronged approach – much in line with what was set out in the *1990 World Development Report*, which focuses on: increasing the opportunities of the poor to use their most abundant asset (labour) primarily through agriculture-driven growth; augmenting their capacity to take advantage of increased opportunities (investments in 'human capital'); and guarantee social safety nets for residual poverty groups (WB 1990b) – now approached within a framework organised around the MDGs (see Hanmer et al. 1999 for a critique).

A *Public Expenditure Review* (PER) aims to analyse the equity and efficiency of public expenditure and to assess the effectiveness of public expenditure management processes in achieving 'fiscal discipline' and enabling 'cost-effective' public service provision. The PER tends to embed recommendations in line with the governance cluster of the CPIA and is anchored on an IMF diagnosis and conditions regarding public finance (including wage bill targets; inflation targets; and budgetary positions). A bias against increasing public expenditures tends to prevail, accompanied by directions to deepen structural reforms such as privatisation, marketisation and liberalisation. Furthermore, recommendations regarding public procurement put forward in a PER may serve as a conduit for opening up government procurement processes not only to internal competition but also to external competition from foreign firms (Tan 2006).

A *Country Financial Accountability Assessment* (CFAA) seeks to evaluate the overall quality of a country's public financial management system, covering budgeting, accounting, reporting and auditing, and external scrutiny of public finances (WB 2004c).

A *Country Procurement Assessment Review* (CPAR) assesses a country's public sector purchasing procedures and provides guidelines regarding a country's system for procuring goods, works and services (WB 2004c).

Appendix 2: Summary of non-lending services for Ghana (FY03-07) (as of February 9, 2004)

Recent completions	Underway	Planned
JSA/PRSP	CEM on Growth, Poverty and Budgeting	WB-Parliamentary quarterly dialogue sessions
Gender Assessment	Country Assistance Strategy (CAS)	Investment Climate Assessment (ICA)
Ghana Poverty Note	Energy Policy Note	Country Environmental Assessment
Client Survey	Public Expenditure Review (PER)	Country Portfolio Performance Review
Country Procurement Assessment Review (CPAR)	Trade Study	Telecommunications
Administrative Barriers (FIAS study)	Energy PSIA	CAS Progress Report
Microfinance Background Study	National Health Insurance Implementation	PER
	Post Financial Sector Assessment Prog. Follow-up	Benchmarking Study (MIGA)
	Promoting Foreign Investment (IFC/MIGA)	Communications Review
	Country Financial Accountability Assessment (CFAA)	Public-Private Partnerships
	Communication and Outreach, incl. Media	Urban Strategy Note
	PRSP Progress Report	Natural Resource Management
	Accounting &Auditing ROSC	Community Empowerment
	Ghana Corporate Governance Assessment	Disability in Ghana
	Poverty and Social Impact Analysis	CFAA
	Capacity Building for Sustained Sub-national regional Development Compet.	Employment and Youth Study
	HIPC Tracking Assessment and Action Plans	Poverty Assessment (PA)
	Development Dialogue Series	Country Economic Memorandum (CEM)
	HIPC Completion Point	CPAR

Source: Ghana 2004 CAS, Annex B4

Appendix 3: CPIA criteria

A. Economic Management
   1. Macroeconomic Management
   2. Fiscal Policy
   3. Debt Policy

B. Structural Policies
   4. Trade
   5. Financial Sector
   6. Business Regulatory Environment

C. Policies for Social Inclusion
   7. Gender Equality
   8. Equity of Public Resource Use
   9. Building Human Resources
   10. Social Protection and Labour
   11. Policies and Institutions for Environmental Sustainability

D. Public Sector Management and Institutions
   12. Property Rights and Rule-based Governance
   13. Quality of Budgetary and Financial Management
   14. Efficiency of Revenue Mobilisation
   15. Quality of Public Administration
   16. Transparency, Accountability and Corruption in the Public Sector

Source: WB (2006h).

Appendix 4: Changes in the economic core of the 2003 and 2004 CPIA questionnaires

A. Economic Management

1. Macroeconomic Management:

Assesses the quality of monetary and exchange rate policy and favours aggregate demand policies that produce low inflation and internal and external balance; public spending should not crowd out investment.

A country is awarded a score 5 (i.e. doing very well) when, WB (2004g, p. 7):[278]

> aggregate demand policies pursue external and internal balances. Rapid and flexible policy response mitigates the effects of external and internal shocks. Monetary/exchange rate policies clearly target price stability, and public spending does not crowd out private investment.

A poor score (score 2) is awarded when aggregate demand policies are:[279]

> inconsistent with macroeconomic stability. Monetary and exchange rate policies do not ensure price stability; and there is significant private sector investment crowding out. Policy framework is inadequate to mitigate the effects of external/internal shocks.

Guideposts 2003 (WB 2003i): PREM/DEC Indicators on Macroeconomic and Fiscal Policies; PREM/DEC Indicators on Financial Sector; PREM/DEC Indicators on Access to Capital.
2004 (WB 2004g): PREM/DEC Indicators on Macroeconomic Policies + IMF Article IV Consultation.

2. Fiscal Policy:

Assesses a) the size of the fiscal balance ('sustainability of public finance'); b) whether public expenditure/revenue can be adjusted to absorb shocks; and c) whether the provision of public goods, including infrastructure, is consistent with medium-term growth.

A country is awarded a score 5 when, WB (2004g, p. 8):

> fiscal policies are consistent with macroeconomic stability. Fiscal balance can be financed in a non-inflationary way and is consistent with adequate credit for the private sector and a sustainable path of public debt. Public expenditures and revenues are flexible to adapt to shocks, and the provision of public goods is adequate to support growth.

A country is awarded a score 2 when:

> fiscal balance will likely lead (or is already leading) to macroeconomic imbalances. The primary balance is insufficient to halt the increase of the ratio of public debt to GDP; public expenditure and revenues are rigid to adapt to shocks without jeopardising the quality and quantity of public goods procured; and the provision of public goods is insufficient to support medium-term growth.

[278] A score 6 is awarded when a country is characterised by these features for three consecutive years.
[279] Again, if a country is characterised by these features for three consecutive years, its rating automatically drops to 1.

Guideposts 2003 (WB 2003i): PREM/DEC Indicators on Macroeconomic and Fiscal Policies.

2004 (WB 2004g): idem + IMF Article IV Consultations.

3. Debt Policy:

Assesses whether the debt management strategy is conducive to minimise budgetary risks and ensure LT debt sustainability.

A country is awarded a score 5 when, (WB 2004g, p. 10):

> debt burden indicators do not signal a reasonable risk of debt servicing difficulties. Terms of new borrowing are conducive to long-term sustainability. There is good coordination between debt management and macroeconomic policies. The debt management unit is well established, supported by efficient systems, and has good analytical capacity as indicated by regular analytical work on debt. Regular, comprehensive and accurate statistics are produced. The government produces annually a strategy defining how the composition of the debt is projected to evolve over the medium term. The legal framework for public borrowing is clearly defined, and information is shared between different agencies responsible for contracting debt.

A country is awarded a score 2 when:

> debt burden indicators are high with a significant risk that arrears will emerge in the absence of debt restructuring/reduction. New external/domestic debt is contracted on terms that may worsen debt sustainability in the short/medium term. There is little coordination between debt management and other macroeconomic policies and major conflicts may exist. A debt management unit exists, but lacks adequate systems for recording and monitoring debt. Data on debt are made available on a sporadic basis and analytical capacity is weak. Financing strategies are prepared on an informal basis and are not clearly linked to the composition of debt. The legal framework for borrowing is defined, but there is little coordination between agencies responsible for contracting debt.

Guideposts 2003: PREM/DEC Indicators on Access to Capital; WB's Debt Reporting System

2004: idem.

B. Structural Policies

4. Trade

2003 Questionnaire Trade Policy and Foreign Exchange Regime	**2004 Questionnaire** Trade
Assesses how well the policy framework fosters trade ***and*** capital movements	Assesses how well the policy framework fosters **trade in goods**.
Narrative guidelines: tariff rates; import/export barriers; duty exemptions; trading monopolies; customs administration; current account convertibility ('IMF Article 8 status'); ***capital account convertibility***	Narrative guidelines: tariff rates; non-tariff barriers; internal taxation; trading monopolies; customs administration.
Guideposts: PREM/DEC Indicators on Trade Policies and Competitiveness	Guideposts: Simple average tariff rates and NTB indexes from IMF trade restrictiveness index tables; Tariff dispersion from tariff schedules in WITS (WB database); **Diagnostic Trade Integration Studies**

	(DTIS); Investment Climate Assessment (ICA); FIAS Administrative Barriers Report (ABR); WTO Trade Policy Review

5. Financial Sector

2003 Questionnaire Two separate criteria: Financial Stability and Financial Sector Depth, Efficiency and Resource Mobilisation		**2004 Questionnaire** Financial Sector
Financial Stability: assesses structure of the financial sector and policies and regulations affecting it	Fin Sector Depth, Efficiency and Resource Mobilisation: assesses to what extent policies and regulations affecting FIs foster mobilisation of savings and efficient financial intermediation	Assesses structure of the financial sector and policies and regulations that affect it; three dimensions: a) financial stability; b) sector's efficiency, depth and resource mobilisation strength; c) access to financial services.
Narrative guidelines: competition policies in the sector (barriers to entry, ***national treatment of foreign and domestic investors***, ***capital account convertibility***); legal regime (including corporate governance arrangements); regulatory regime (international best practice standards)	Narrative guidelines: monetary and credit policies (market determined interest rates, ***no directed credit***, small PSBR); tax policies (level playing field for all financial sector activity); ownership policies (***state ownership of FI limited to export credit agencies***)	Narrative guidelines: vulnerability to shock of the banking sector; share of non-performing loans and level of capital at risk; Basel Core Principles for banking supervision; quality of risk management in FI; size and reach of financial markets; interest rate spread; efficiency of microfinance; development of payment and clearance, and credit reporting systems; access of SMEs to finance; legal and regulatory framework
Guideposts: none	Guideposts: PREM/DEC Indicators on the Financial Sector	Guideposts: WDIs; **World Business Environment Surveys (WB)**; IMF Financial Statistics; WB Data on Credit Reporting from Financial Sector Network and PSD; Micro finance Data from the Consultative Group to Assist the Poorest and the Microfinance Bulletin; Available FSAP data, including data from Basel Core Principle reviews

6. Business Regulatory Environment

2003 Questionnaire Two separate criteria: Competitive Environment for the Private Sector and Goods and Factor Markets	**2004 Questionnaire** Business Regulatory Environment
Assesses extent to which legal, regulatory and policy environment helps or hinders private business in investing, creating jobs, and becoming more productive	
Narrative Guidelines: licensing of investment; procedures of entry and exit; legal framework	

to address anti-competitive behaviour by firms; public sector procurement; state ownership in competitive sectors; price controls; state administrative allocations regarding production; shareholder protection and financial disclosure; labour market regulations; barriers to land ownership, procedures to register property	
Guideposts: PREM/DEC Indicators on Private Sector Framework; WB's Doing Business database	Guideposts: Doing Business Indicators; **Investment Climate Assessments (ICAs)**; **Heritage Foundation Index of Economic Freedom**; International Country Risk Guide (Investment Profile Component); WBI Governance Indicator (Regulatory Quality)

A country is awarded a score 6, when it has, WB (2004g, p. 19):

a) Almost no bans or investment licensing requirements. Regulations facilitate efficient entry and exit of business. Good legal framework to address anti-competitive conduct by firms exists, and is consistently enforced. All public sector entities are free to procure from any source.
b) Streamlined industry licensing, permits, and inspection requirements facilitate business activity. State intervention in the goods market is limited to regulation and/or legislation to smooth out market imperfections. Corporate governance laws encourage disclosure and protect shareholder rights and are enforced effectively.
c) Employment law provides a high degree of flexibility to hire and fire at low cost. Other labor market institutions facilitate doing business. State intervention in the labor and land markets is limited to regulation and/or legislation to smooth out market imperfections. Procedures to register property are simple, low cost, and fast.

A country receives a score 1, when it has (p. 18):

a) Extensive bans on, or complex licensing of, investment. Procedures to enter and exit are extremely difficult and costly. No legal framework to address anti-competitive conduct by firms in naturally-competitive markets. Public sector entities are required to purchase only from state firms.
b) Extremely burdensome operational licensing, permits, inspections, and other compliance systems, including taxes and customs. Goods markets are highly restricted, e.g. through extensive state ownership in competitive sectors, widespread price controls, or the state makes administrative allocation/decisions about production. No, or weak requirements on ownership and financial disclosure, few or no shareholder protections; those that exist are not enforced.
c) Extensive labour market controls and rigidity of labour regulation. Private land ownership is illegal or severely curtailed. Very few businesses have formal title or use rights to land. Process to register property extremely costly.

Appendix 5: Policies for Social Inclusion/Equity and Public Sector Management and Institutions in the CPIA questionnaire.

C. Policies for Social Inclusion/Equity

7. Gender Equality

Assesses the extent of gender equality in a country across three different dimensions: the human capital dimension; access to economic resources; and status and protection under the law.

A country is awarded the lowest score ('1') when, WB (2006h, p. 19):

> a. Significant differences exist in female to male primary completion rates and enrollment in secondary education. Substantial gaps exist in access to delivery care and family planning services, and the adolescent fertility rate is high. Policies and laws are obstacles to gender equality in education and do not provide access to delivery care and family planning services. There have been no recent efforts to make laws or policies more supportive of gender equality in education, to improve delivery care and access to family planning services, and to reduce adolescent fertility.
>
> b. Significant gender disparities exist in participation in the labor force, business ownership, land tenure, property ownership, and inheritance practices. Formal policies and laws are obstacles to gender equality in these areas, and there have been no recent efforts to make formal laws and policies more supportive of gender equality.
>
> c. The law gives men and women different individual and family rights (requesting a divorce, child custody, obtaining individual identity cards or a passport). Violence against women (including such practices as female genital mutilation, trafficking, or sexual harassment) is common, the law does not treat it as a crime, and there are no policies, institutions or programs aimed at decreasing violence against women. Significant gender disparities exist in political participation at the national level. Laws and policies are obstacles to women's participation in national government, and there were no recent efforts to make them more supportive of gender equality in this respect.

A country performs very well (score '6') when, WB (2006h, p. 20):

> There are no gender differences in human capital development, access to productive and economic resources, and status and protection under the law. Policies and laws that specifically address gender equality in all these areas are consistently and effectively enforced, and there are active programs or institutions to promote greater gender equality or prevent an increase in gender inequalities.

8. Equity of Public Resource Use

Assesses the extent to which the patterns of public expenditure and revenue collection affect the poor and are consistent with national poverty reduction priorities.

A country performs very poorly when, WB (2006h, p. 22):

> a. Public expenditures are not aligned with poverty reduction priorities. Poverty diagnosis, and the identification of vulnerable groups, and of groups without access to basic services are not in place. There are no strategy and interventions to explicitly assist above identified groups. There are no tracking of composition and incidence of expenditures and no feedback into allocation of resources.

b. The overall incidence of revenues is very regressive and does not reflect national poverty reduction priorities.

A country performs very well when:

a. Public expenditures are fully aligned with poverty reduction priorities. Strong poverty diagnosis is in place that very clearly identifies poor, vulnerable groups, and those lacking services. A strategy has been adopted with well-defined interventions directed at assisting identified groups. Good progress has been achieved in aligning expenditures with the strategy. Tracking of spending (program, category, region) is in place. Benefit incidence analysis is carried out for major programs. Feedback of the analysis to subsequent expenditure allocations is fully implemented.
b. There are no egregious regressive revenue sources. Revenue generation aligned with national poverty reduction priorities

9. Building Human Resources

Assesses national policies and public and private sector service delivery conditioning access to and quality of: health and nutrition services, education, and prevention and treatment of HIV/Aids, tuberculosis and malaria.

A country performs very poorly when:

a. Policies, programs and implementation are nonexistent or grossly inadequate to assure equitable access to a minimum package of basic health services, protect against the financial burdens of illness, or prevent malnutrition.
b. Policies, spending, and effectiveness are nonexistent or grossly inadequate to assure literacy, universal access to basic education, equitable access to ECD [Early Child Development] services, and adequate post-basic education and training; teacher and student learning standards are nonexistent or grossly inadequate.
c. Policies, programs and implementation for prevention and treatment of HIV/AIDS, tuberculosis, and malaria are nonexistent or grossly inadequate.

A country performs very well when:

a. Health or social insurance policies exist and have wide coverage; access to appropriate preventive and curative health services is universal and services are client-focused and good quality; national health strategy is consistent with best practice and regulation is effective; policies and resources allow prevention and treatment of all forms of malnutrition; public resources are used cost-effectively.
b. Strategic national education policies, high standards, and effective use of public and private resources support a good quality, universal basic education system, good quality, equitable ECD services, and diversified, good quality post-basic education and training systems adequate to support economic development and life-long learning; government oversight of private/NGO providers is effective; school performance and student learning outcomes are systematically tracked, with feedback to schools and parents; performance data and evaluation guide policy; at all levels of education, equity of access is protected and efficiency of resource use is high.
c. Policies for prevention, treatment, care and support of HIV/AIDS, tuberculosis, and malaria reflect strong government commitment and client-focused programs reach all who need them; national authority is able to track disease prevalence, resources, and program implementation; quality and timeliness of services is steadily improving; interventions focus on the poor; public resources are used cost-effectively.

10. Social Protection and Labour

Assesses government policies in the area of social protection and labour markets regulation.

A country performs very poorly when (p. 29):

a. Social protection programs to assist the poor and other vulnerable groups (the disabled, orphans, etc) to cope with risk and ensure adequate living standards are non-existent or severely under-funded.
b. The ILO conventions on core labour standards have not been ratified nor legislation that conforms with them passed.
c. Labour market regulations on health and safety, working conditions and hiring and firing do not exist, or are inappropriate and discourage job creation in the formal sector while not protecting most workers.
d. Government policies and programs impede development of community initiatives or local accountability mechanisms.
e. Pension and old-age savings systems are regressive, consume an unsustainable share of public resources, and do not provide adequate income security even to the few who are covered.

A country is attributed a score '6' when (p. 30):

a. Social protection programs provide income support to poor and vulnerable groups. Programs are cost-effective, well-targeted, and include monitoring and evaluation procedures. They form a balanced strategy with measures to increase poor and vulnerable groups' own incomes and their access to services and to social insurance.
b. Government has ratified international conventions on, or passed legislation that conforms with, core labour standards and is implementing these through its policies and programs. Government policy encourages civil society and local government actions to reduce child labour, including appropriate incentives for children to remain in school.
c. Labour market regulations and active labour market policies promote broad access to employment in the formal sector and reflects a balance between social protection and job creation objectives in accordance with the economic circumstances and values of the country.
d. Government policies and programs encourage and support communities' own development initiatives with systematic community involvement in planning, significant allocation of resources to the community level, and capacity building and other institutional strengthening efforts to ensure integration of communities into local government processes.
e. A diversified, well-supervised, and appropriate combination of pension and savings programs (including mandatory, voluntary, public, private, funded, pay-as-you go, contributory and non-contributory programs) provide affordable, adequate, sustainable and robust income security to most of the potentially vulnerable groups with minimal distortions in the operation of labour markets.

11. <u>Policies and Institutions for Environmental Sustainability</u>

Assesses the extent to which environmental policies foster the protection and sustainable use of natural resources and the management of pollution.

A country performs very poorly when (p. 31):

For both pollution and natural resource issues: Regulations and policies are lacking. Environmental information is not published. Environmental Assessment (EA) legislation is lacking. No data are available for priority setting. Sector ministries do not incorporate environmental concerns.

A score '6' is allocated when:

For both pollution and natural resource issues: Regulations and policies are comprehensive. Implementation is effective. No harmful subsidies exist. Public information is widely available. The public is consulted on most environmental issues. EA is effective and findings are acted upon. Priorities are adhered to and reflected in interventions. Environmental concerns are integrated in sector policies and inter-ministerial coordination is effective.

D. Public Sector Management and Institutions

12. Property Rights and Rule-based Governance

Assesses the extent to which private economic activity is facilitated by an effective legal system and a rule-based governance structure in which property and contract rights are respected and enforced.

A country performs very poorly when (p. 33):

a. Formal property rights are hardly recognized, and informal rights are seldom enforced. Formal contractual arrangements are little used. Manipulation of property and contract rights is endemic.
b. Laws and regulations are changed frequently, unpredictably and non-transparently to benefit a select few. The judiciary is an arm of the executive, and favoritism pervades the judicial system. Corruption in the judicial system is endemic. Judicial decisions are not publicly available.
c. The state is unable or unwilling to protect the lives and property of its citizens in most or all of its territory. The police are often a source of crime and violence against citizens.

A country is doing well ('5') when:

a. All property rights are transparent and well protected. Property registries are current and non-corrupt. Contracts are routinely enforced.
b. Laws and regulations affecting businesses and individuals are determined through transparent political or administrative processes, and are publicly announced. Low-cost means are available for pursuing small claims. Application of laws and regulations is impartial and predictable. Citizens can pursue claims against the state without fear of retaliation.
c. A well-functioning and accountable police force protects citizens and their property from crime and violence. When serious crimes occur, they are generally reported to the police and investigated.

A score '6' is allocated when: criteria for '5' on all four sub-ratings are fully met; when there are no warning signs of possible deterioration; and when there is widespread expectation of continued strong or improving performance.

13. Quality of Budgetary and Financial Management

Examines the quality of the budgetary processes and financial management systems.

A country performs very poorly (score '1') when (p. 35):

a. If there is a budget, it is not a meaningful instrument, nor an indicator of policies or tool for allocation of public resources. There is no forward look in the budget, nor any meaningful consultation with spending ministries. No consistent budget classification system is used. More than 50 percent of public resources from all sources do not flow through the budget.

b. Expenditures across broad budget categories have little or no relationship to the amounts budgeted. There is practically no monitoring and reporting of public expenditures. Payment arrears exceed 10% of total expenditures, or cannot be determined.

c. There is no reconciliation of cash accounts with fiscal records. No regular, in-year fiscal reports are produced. Public accounts are seldom prepared, or are more than five years out of date. The use of public resources is not on the public agenda.

A country is doing well (score '5') when (p. 36):

a. Policies and priorities are linked to the budget. Multi-year expenditure projections are integrated into the budget formulation process, and reflect explicit costing of the implications of new policy initiatives. The budget is formulated through systematic consultations with spending ministries and the legislature, adhering to a fixed budget calendar. The budget classification system is comprehensive and consistent with international standards Off-budget expenditures are minimal, and transparent.

b. The budget is implemented as planned, and actual expenditures deviate only slightly from planned levels (by less than 10 percent on most broad categories). Budget monitoring occurs throughout the year based on well functioning management information systems. Payment arrears are negligible or non-existent.

c. Reconciliation of banking and fiscal records is practiced comprehensively, properly, and in a timely way (daily or weekly). In-year fiscal reports are prepared at least quarterly, issued within 4 weeks of end of period, and provide accurate data on all budget items, with coverage of expenditures at both the commitment and payment stages. The public accounts are prepared within 6 months of the end of the fiscal year, and include full information on revenue, expenditure, and financial assets and liabilities. Accounts are audited in a timely, professional and comprehensive manner, and appropriate action is taken on budget reports and audit findings.

14. Efficiency of Revenue Mobilisation

A country performs very poorly (score '1') when (p. 38):

a. Tax base is extremely narrow with many open-ended exemptions. Most tax revenues are collected from foreign trade and other distortionary taxes. There are high, multiple, and widely ranged import tariffs, which change frequently or are applied in a highly discretionary manner. Little is collected from income taxes.

b. Tax administration is extremely weak, with very low collection rates. It is organized by type of tax and business processes have not been reviewed and reformed. Computerization is limited to very basic functions. Many taxpayers must make several or more personal visits to tax offices. Corruption is endemic among tax and customs officials.

A country performs well (score '5') when:

a. The bulk of revenues are generated by low-distortion taxes such as sales/VAT, property, etc. Import tariffs are low and relatively uniform, and export rebate or duty drawback are functional. There is a single statutory corporate tax rate comparable to the maximum personal income tax rate. Tax base for major taxes is broad and free of arbitrary exemptions.

b. Tax administration is effective, and entirely rule-based. Administrative and compliance costs are low. A taxpayer service and information program, and an efficient and effective appeals mechanism, have been established.

15. Quality of Public Administration

Assesses the extent to which the civil service can design and implement government policy and deliver services effectively.

A country performs very poorly when (p. 40):

a. Mechanisms for coordination are non-existent or ineffectual, creating bureaucratic conflict and uncertain or conflicting policies.
b. Administrative structures are highly fragmented, with vague and overlapping responsibilities. Business processes are extremely complex and convoluted, with multiple decision layers, and many signatures required to move decisions forward.
c. There are no workable rules on hiring and promotion, which are based on bribes, personal ties, or ethnic affiliation rather than merit. Most public employees, even at lower levels, lose their positions on changes in government. Bribe seeking is endemic.
d. Level of public employment has little relation to provision of public services: either employment is too low or too few employees show up for work to provide essential services, or the wage bill consumes all of current spending, leaving no funds available for essential supplies such as drugs or textbooks. Pay and benefit levels, particularly at upper levels, are a small fraction of comparable private sector levels, and bribe payments represent a large share of income for many public officials.

A country performs well when:

a. Effective coordination mechanisms ensure a high degree of policy consistency across departmental boundaries.
b. Organizational structures are along functional lines with very little duplication. Business processes are regularly reviewed to ensure efficiency of decision making and implementation.
c. Hiring and promotion are based on merit and performance, and ethical standards prevail.
d. The wage bill is sustainable and does not crowd out spending required for public services. Pay and benefit levels do not deter talented people from entering the public sector. There is flexibility (that is not abused) in paying more attractive wages in hard to fill positions (e.g. rural teachers, technical specialists).

16. <u>Transparency, Accountability and Corruption in the Public Sector</u>

Assesses the extent to which the executive can be held accountable for its use of funds and the results of its actions by the electorate and by the legislature and judiciary, and the extent to which public employees within the executive are required to account for the use or resources, administrative decisions, and results obtained.

A country performs very poorly (score '1') when (p. 42):

a. There are no checks and balances on executive power. Public officials use their positions for personal gain and take bribes openly. Seats in the legislature and positions in the civil service are often bought and sold.
b. Government decision-making is secretive. The public is prevented from participating in or learning about decisions and their implications.
c. The state has been captured by narrow interests (economic, political, ethnic, and/or military). Administrative corruption is rampant.

A country performs well (score '5') when,

a. Accountability for decisions is ensured through a strong public service ethic reinforced by audits, inspections, and adverse publicity for performance failures. The

judiciary is impartial and independent of other branches of government. Authorities monitor the prevalence of corruption and implement sanctions transparently.
b. The reasons for decisions, and their results and costs, are clear and communicated to the general public. Citizens can obtain government documents at nominal cost. Both state-owned (if any) and private media are independent of government influence and fulfil critical oversight roles.
c. Conflict of interest and ethics rules for public servants are observed and enforced. Top government officials are required to disclose income and assets, and are not immune from prosecution under the law for malfeasance.

Appendix 6: PREM/DEC Indicators, Ecuador 1999

Source: Ecuador Country Assistance Evaluation, June 4, 1999, OED, Annex B: Standard Tables; B.1: PREM Indicators

PREM/DEC INDICATORS
Methodology and Data Sources

	Indicator	Source	Benchmarks	Rating Method
	1. Institutional Quality			
1	ICRG rating: Law and Order (0-6) a/	International Country Risk Guide (ICRG)	Predicted value from regression	2
2	ICRG rating: Corruption (0-6) a/	International Country Risk Guide (ICRG)	Predicted value from regression	2
3	TI corruption rating (0-10) (Bad to Good ===> 0,1,2..........10)	Transparency International web site	Predicted value from regression	2
4	ICRG rating: Bureaucratic quality (0-4) b/	International Country Risk Guide (ICRG)	Predicted value from regression	2
	2. Macroeconomic & Fiscal Policies			
1	GDP per capita per annum growth rate, %	SIMA data base (LDB central)	Mean for all borrowers	1
2	Inflation (consumer prices) (%)	SIMA data base (LDB central)	Absolute value	4
3	Real interest rates (%)	SIMA data base (LDB central)	Absolute value	5
4	Gross National Savings (% of GNP)	SIMA data base (LDB central)	Mean for all borrowers	1
5	Current account balance (% of GNP)	SIMA data base (LDB central)	Absolute value	6
6	Fiscal balance (% of GDP)	SIMA data base (LDB central)	Mean for all borrowers	1
7	Central government expenditure (% of GDP)	SIMA data base (LDB central)	Mean for all borrowers	1
8	Tax revenue (% of GDP)	SIMA data base (LDB central)	Absolute value	7
9	Public sector debt (% of GDP)	SIMA data base (LDB central)	Mean for all borrowers	1
10	Government debt interest (% of revenue)	SIMA data base (LDB central)	Mean for all borrowers	1
11	Aid dependency (Aid as % of GNP)	SIMA data base (LDB central)	Mean for all borrowers	1
	3. Poverty & Employment			
1	Population below the national poverty line (%)	SIMA data base (LDB central)	Mean for all borrowers	1
2	Population below $1 a day (%)	SIMA data base (LDB central)	Mean for all borrowers	1
3	Population below $2 a day (%)	SIMA data base (LDB central)	Mean for all borrowers	1
4	Poverty gap (%)	SIMA data base (LDB central)	Mean for all borrowers	1
5	Gini index	SIMA data base (LDB central)	Mean for all borrowers	1
6	% Population with access to health care	SIMA data base (LDB central)	Predicted value from regression	2
7	Prevalence of child malnutrition (% of children under 5)	SIMA data base (LDB central)	Predicted value from regression	2
8	Under-5 mortality rate (per 1000)	SIMA data base (LDB central)	Predicted value from regression	2
9	Access to safe water (% of population)	SIMA data base (LDB central)	Predicted value from regression	2
10	Access to sanitation (% of population)	SIMA data base (LDB central)	Predicted value from regression	2
11	Adult illiteracy rate : Male	SIMA data base (LDB central)	Predicted value from regression	2
12	Adult illiteracy rate : Female	SIMA data base (LDB central)	Predicted value from regression	2
13	Gross primary enrollment ratio	SIMA data base (LDB central)	Predicted value from regression	2
14	% of cohort reaching grade 4 - male	SIMA data base (LDB central)	Mean for all borrowers	1
15	% of cohort reaching grade 4 - female	SIMA data base (LDB central)	Mean for all borrowers	1
16	Child labor (% of 10-14 years age group in labor force)	SIMA data base (LDB central)	Predicted value from regression	2
	4. Trade, Policies & Competitiveness			
1	WTO member	WTO	Membership	Yes/No
2	Trade (% of GDP)	SIMA data base (LDB central)	Predicted value from regression	2
3	Manufacturing exports/Merchandise exports (%)	SIMA data base (LDB central)	Mean for all borrowers	1
4	Mean tariff (%)	SIMA data base (LDB central)	Mean for all borrowers	1
5	Trade policy index (5-1) c/	The Heritage Foundation, Decembner 1998	Mean for all borrowers	1

PREM/DEC INDICATORS
Methodology and Data Sources

	Indicator	Source	Benchmarks	Rating Method
	5. Access to capital			
1	Euromoney country creditworthiness rating	SIMA data base (LDB central)	Mean for all borrowers	1
2	Moody's long-term foreign currency debt rating (Good to bad ==> Aaa, Aa1, Aa2, Aa3, A1.........Ca, C)	Moody's web site	NR	NR
3	Dun & Bradstreet risk rating (Good to bad ==> DB1, DB1a, DB1b........DB7)	Dun & Bradstreet : International Risk & Payment Review	NR	NR
4	Arrears/DOD (%)	SIMA data base (LDB central)	Mean for all borrowers	1
5	Present value, DOD/GNP (%)	SIMA data base (LDB central)	Mean for all borrowers	1
6	Short-term debt/Total debt (%)	SIMA data base (LDB central)	Mean for all borrowers	1
7	Short-term debt/Gross reserves (%)	SIMA data base (LDB central)	Mean for all borrowers	1
8	M2/(Reserves minus gold)	IMF data	NR	NR
9	Gross Reserves excl. Gold (Months of Imports)	SIMA data base (LDB central)	Mean for all borrowers	1
10	Date of last rescheduling (as of end-1998)	SIMA data base (LDB central)	NR	NR
11	Foreign investment index (5-1) c/	The Heritage Foundation, December 1998	Mean for all borrowers	1
12	Integration of private capital flows	Private Capital Flows to Developing Countries, The Road to Financial Integration, World Bank, August 1997	NR	NR
	6. Financial Sector			
1	Banking development index (LAC only)	Loayza,N.,Economic Reforms and Progress in LAC, June 1997	Mean for all borrowers	1
2	Domestic credit provided by banking sector (% of GDP)	SIMA data base (LDB central)	Mean for all borrowers	1
3	Interest rate spread (lending-deposit) (%)	SIMA data base (LDB central)	Mean for all borrowers	1
4	Lending rate spread over LIBOR (%)	SIMA data base (LDB central)	Mean for all borrowers	1
5	Banking index (5-1) c/	The Heritage Foundation, December 1998	Mean for all borrowers	1
	7. Private Sector Framework			
2	Private investment (% of GDP)	SIMA data base (LDB central)	Mean for all borrowers	1
3	Stock market capitalization (% of GDP)	SIMA data base (LDB central)	Mean for all borrowers	1
4	Government intervention index (5-1) c/	The Heritage Foundation, December 1998	Mean for all borrowers	1
5	Regulation index (5-1) c/	The Heritage Foundation, December 1998	Mean for all borrowers	1
6	Wage and price control index (5-1) c/	The Heritage Foundation, December 1998	Mean for all borrowers	1
	8. Gender			
1	Total fertility rate (births per woman)	SIMA data base (LDB central)	Mean for all borrowers	1
2	Maternal mortality ratio (per 100,000 live births)	SIMA data base (LDB central)	Predicted value from regression	2
3	Gross primary enroll. ratio gap (male-female), years	SIMA data base (LDB central)	Mean for all borrowers	1
4	Secondary school pupils - % females	SIMA data base (LDB central)	Predicted value from regression	2
5	Life expectancy at birth, Male (years)	SIMA data base (LDB central)	Predicted value from regression	2
6	Life expectancy at birth, Female (years)	SIMA data base (LDB central)	Predicted value from regression	2
7	Life expectancy at birth gap (female-male), years	SIMA data base (LDB central)	Absolute value	7
8	Females as % of labor force	SIMA data base (LDB central)	Predicted value from regression	2

NR=not rated.
a/ ICRG rating : Bad to Good ===> 0,1,2......6)
b/ ICRG rating : Bad to Good ===> 0,1,2......4)
c/ Heritage rating : Bad to Good ===> 5,4......1)

Methodology and Data Sources

	Indicator	Source	Benchmarks	Rating Method

Rating Method:

1 Comparison with mean for all borrowers
- B = +/- 0.5 standard deviation from the mean for all borrowers
- C = > 0.5 standard deviation worse than the mean for all borrowers
- A = > 0.5 standard deviation better than the mean for all borrowers

2 Regressions on GNP per capita
- B = actual value within +/- 0.5 standard deviation from the predicted value
- C = actual value > 0.5 standard deviation worse than the predicted value
- A = actual value > 0.5 standard deviation better than the predicted value

4 Inflation rates (%)
- B = 10 - 25
- C = More than 25
- A = Less than 10

5 Real interest rates (%)
- B = 2.0 - 3.5, 4.5 - 6.0
- C = Less than 2.0 or more than 6.0
- A = 3.5 - 4.5

6 Current account balance (% of GNP)
- B = -3.5 to -2.0
- C = Less than -3.50
- A = More than -2.0

7 Tax revenue (% of GDP), Life expectancy gap
- B = +/- 0.5 to 1.0 standard deviation from the mean
- C = > +/- 1.0 standard deviation from the mean
- A = upto +/- 0.5 standard deviation from the mean