Motivation
- The advent of the SDGs underpins the importance of DRM.
- The tax/GDP is determined by structural factors (determinants of the tax base, to which the tax rate is applied).
- Revenue performance is low in most developing countries.

Motivation (2)
- Due to the constraints on DRM aid is pivotal.
- The impact of aid on taxes is a revenue choice depending on political economy factors, based on the political costs of aid and tax (accountability, autonomy and bureaucratic costs of administration).
- Donors influence the choice through:
  (i) Technical support (transfer of knowledge)
  (ii) Conditionality (e.g. revenue conditionality in IMF programs).
  (iii) Supporting reform to improve efficiency and administration.

Motivation (3)
- Aid/GDP and tax/GDP ratios are typically nonstationary
- Pervasive heterogeneity in fiscal effects across developing countries
- Long run and short-run dynamics between aid and taxes.
- Simultaneity and endogeneity.

Research Questions
- Does a long-run equilibrium relationship between the aid/GDP and tax/GDP ratios exist?
- Does aid’s composition matter for tax performance?
- Does revenue conditionality in donor programs improve revenue performance?

Data
- Annual time series data on 84 developing countries from 1980 to 2013.
- Net aid disbursements (OECD DAC dataset).
- Tax/GDP data from the ICTD GRD (2016) dataset.

Methods
- Common factor models.
- Dynamic Error Correction Model (ECM) estimated using the CCEMG estimator.
- Cross section averages and lags of cross-section averages.

Results
- Co-integration (equilibrium) relationship between the aid/GDP and tax/GDP ratios.
- Long-run positive relationship between aid and taxes.
- Political costs of aid are larger than those of taxes.

Results (con’d)
- Revenue conditionality in IMF-supported programs is very important (LR and SR positive effects).
- Quantitative (SR effect) and structural (LR and SR effects) conditionality

Weak Exogeneity
- Aid is weakly exogenous. There is no ‘donor disbursement rule’.
- When conditionality is incorporated, aid is still weakly exogenous (this allays worries about endogeneity of donor-supported conditionality).
- Taxes are endogenous for the equilibrium so long-run causality is uni-directional (from aid to taxes).

Conclusion
- Tax/GDP ratios are sustained by foreign aid.
- Political costs of aid are greater than those of taxes.
- Aid and its components are weakly exogenous.