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International Coordination and the Effectiveness of Aid

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Abstract

This paper discusses and seeks to quantify the effects of improved donor coordination on aid effectiveness. Empirical estimates are first provided of the reductions in transaction costs that can be achieved by better donor coordination via concentration to fewer partner countries and a shift from project aid to programme-based approaches. Further estimates are presented showing how much could be gained in terms of poverty reduction by optimizing aid allocation across countries. The potential gains of a coordinated reallocation would be huge, but there are severe political implementation constraints. Still, the overall conclusion of the paper is that there are huge potential gains from donor coordination.

Keywords: donor coordination, Paris Agenda, aid efficiency

JEL classification: F35, F55, F59

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Acronyms

AAA	Accra Agenda for Action
CPA	country programmable aid
DAC	Development Advisory Committee
EC	European Commission
EU	European Union
GBS	general budget support
GCGD	Gothenburg Centre of Globalization and Development
GDP	gross domestic product
IFIs	international financial institutions
IDS	international development statistics online databases by OECD/DCD-DAC
NGOs	non-governmental organizations
ODA	overseas development assistance
PA	Paris Agenda
PBA	programme-based approaches
TA	technical assistance
UNICEF	United Nations Children's Fund
WDI	world development indicators (of the World Bank)
WGI	worldwide governance indicators (of the World Bank)

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1 Introduction

The concept of aid efficiency can have many different meanings. From a donor perspective, effective aid could mean aid that helps the donor achieve its own goals, which do not necessarily have to be altruistic. In this paper, however, we mean effective in terms of achieving good development outcomes (higher incomes, reduced poverty, social improvements) in the recipient countries relative to the resources spent.

Aid efficiency depends on the character of the donor–recipient relationship. This consists of resource flows, technical assistance, policy advice and conditions. One important dimension affecting aid effectiveness is the extent to which donors coordinate their aid activities. This impacts on the direct transaction costs of aid, but it also has effects on recipient governance, which affects the efficiency of aid use.

The Paris Declaration from 2005 summarized the experiences about how a good aid relationship should be structured. This was then extended in the Accra Agenda for Action (AAA) of 2008 and in the Busan Declaration of 2011. We refer to the entire set of aid efficiency declarations as the Paris Agenda. This paper discusses the implications of different dimensions of donor coordination for aid effectiveness. The discussion concentrates on government-to-government aid, but we touch upon the activities of non-government actors when needed.

2 What is the Paris Agenda?

The Paris Declaration of 2005 outlined a strategy to make aid more efficient through the rationalization of donor behaviour. This would be achieved by measures to increase recipient country ownership, to improve donor harmonization and alignment with recipient policies, to manage aid more according to results, and to enhance mutual accountability. At a subsequent high-level meeting in Accra in 2008 donors elaborated on these themes in the AAA. This added, among other things, the notion that one should seek to improve the predictability of aid flows and reduce conditionalities. On the basis of these two declarations, DAC identified a set of indicators by which they would measure progress with regard to the Paris Declaration (Table 1).

Table 1
Indicators of progress on the Paris Agenda

1. Partners have operational development strategies
2. Reliable country systems
3. Aid flows are aligned on national priorities
4. Strengthen capacity by coordinated support
5. Use of country public financial management systems and procurement systems
6. Strengthen capacity by avoiding parallel implementation structures
7. Aid is more predictable
8. Aid is untied
9. Use of common arrangements and procedures
10. Encourage shared analysis
11. Results-oriented frameworks
12. Mutual accountability

Source: OECD (2008a).

In November 2011 there was another high-level meeting in Busan, where participants agreed on the 'Busan Partnership for Effective Development Cooperation'. This document is very much a compromise, where new donors and developing countries have been more extensively involved than previously. It is an attempt to adjust the aid architecture to the new realities with a more diverse body of donors. Four shared general principles are listed in the Busan Declaration:

i) *Ownership of development priorities by developing countries*: The concept of *ownership* is thus still a central feature of the aid agenda, and it is one of the four important concepts that are focused in this paper.

ii) *Focus on results*: This principle is again the same as before and emphasizes that learning from experience is important. Under this heading one also emphasizes the importance of *alignment* of aid inflows with recipient priorities and policies, which is the second key dimension we focus on in this paper.

iii) *Inclusive development partnerships*: In the discussion on aid modalities in the Declaration, the need to reduce fragmentation is underlined, although the term 'harmonization' is not used. The Busan Declaration puts a lot of emphasis on how to incorporate new actors (South-South cooperation) and new aid modalities into processes. The new actors are expected to use the Declaration as a frame of reference on a voluntary basis. It seems as if the desire to be inclusive and open up for the new players has meant that there is less emphasis on harmonization than in previous declarations. This means that a discussion of the future of *harmonization* is more complex but it may be even more important. It is therefore the third key dimension that we focus on in this paper.

iv) *Transparency and accountability*: There is an even stronger focus in the Busan Declaration than in the earlier ones on the issues of transparency and accountability. Democratic accountability is important for governments if they are to be legitimate to their citizens, but it is also very important for donor–recipient relations. If recipient governments cannot account for the resources that have been transferred to them, both to their citizens and to the donors, the latter will not be willing to continue transferring resources to the government. Or they will at least be less willing to transfer resources in those general forms, which could enhance ownership. Since *accountability* is a goal in itself as well as a key dimension linked to the other aspects we consider, we take it as the fourth key dimension.

Our paper focuses on the behaviour of donors and its implication for aid efficiency. This theme has increasingly come into focus, and the formulation of the Paris Agenda is one result of this debate. This paper seeks to provide a discussion of how aid efficiency can be improved by donor coordination. It is thus really about donor efficiency.

The donors have set up DAC's peer review process, which monitors each donor's aid programme. This provides extensive information about donor behaviour, but it is of a rather general nature. The most interesting attempt to measure donor quality in recent years is the study by Birdsall and Kharas (2010), who benchmark countries and agencies against each other. They identify four broad dimensions of donor quality with

the help of 30 indicators: (i) maximizing efficiency; (ii) fostering institutions; (iii) reducing the burden on recipients, and (iv) transparency and learning. The first dimension, among other factors, picks up alignment. Their second dimension relates to ownership as well as alignment. Both these factors affect how well institutions work. The third dimension picks up reductions in transaction costs, i.e., cost savings from coordination, division of labour and use of cost-effective aid channels. This relates to both the alignment and harmonization dimensions. The fourth dimension measures how well the administrative and oversight processes function, and is thus related to accountability. So the set of dimensions we have chosen to focus on are well in line with those identified in this study of donor quality.

Accordingly, we focus on four key dimensions of the extended Paris Agenda. First there is harmonization, which concerns how donors coordinate with each other. Then we have the concepts of ownership and alignment, which primarily relate to the manner in which donors link up with recipients. But in this paper we look at how donor coordination affects these dimensions. Finally, we look at accountability, which concerns the transparency of the aid processes. Again, we focus on how donor coordination matters for this dimension.

3 What kind of aid is relevant for the Paris Agenda?

Analyses of the aid efficiency implications of the Paris Agenda (EC 2009; Birdsall and Kharas 2010; Bigsten et al. 2011) have generally focused on country programmable aid (CPA), i.e., the part of ODA that is subject to multi-year programming at the country level. According to DACs definition, CPA:

> represents a subset of ODA outflows. It takes as a starting point data on gross ODA disbursements by recipient but excludes spending which is: (i) inherently unpredictable (humanitarian aid and debt relief); or (ii) entails no flows to the recipient country (administration costs, student costs, development awareness and research and refugee spending in donor countries); or (iii) is usually not discussed between the main donor agency and recipient governments (food aid, aid from local governments, core funding to NGOs, aid through secondary agencies, ODA equity investments and aid which is not allocated by country); (iv) CPA does not net out loan repayments, as these are not usually factored into aid allocation decisions. CPA is therefore a gross concept.

CPA thus includes projects and programmes and technical assistance plus some smaller aid categories. Non-CPA grants that could be of importance in a PA perspective are food aid and humanitarian aid, which potentially could be improved by better donor coordination and PA-inspired reforms. Still, we agree that CPA is the most relevant part of aid in relation to the PA, and our discussion focuses on that type of aid.

Still, we note that the huge donor evaluation of the Paris Agenda (Wood et al. 2011) suggest that one should ‘work to extend the aid reform gains to all forms of cooperation’. This is certainly on the agenda, and the number of actors in the aid business is increasing rapidly. The Busan Declaration can be seen as a step in this direction. One concern here is that the agenda has become more diffuse, and thus has

less of a steering effect. It may make sense to try to coordinate better with the large new official donors, since their behaviour may otherwise undermine the activities of the classical DAC donors.

When it comes to the NGOs the need for coordination is less obvious. Since they are not involved in setting conditions for the recipients or channelling resources through the public sector, it is less critical to coordinate with them. It may even be advantageous in some cases to let them operate outside the aid coordination framework and to let them have a complementary role. They could, for example, by being part of the civil society contribute to the pressure on governments for relevant policy changes or accountability. So there are some arguments for not trying to coordinate all donor activities. The argument that Easterly (2006) makes, is that one should let aid entrepreneurs (e.g., NGOs but also others) function more freely and independently of any large coordinated plan. So it is not self-evident that NGOs should come under the Paris Agenda umbrella.

4 Four key dimensions of the Paris Agenda

Above we identified four key dimensions of the Paris Agenda, namely (i) harmonization, (ii) ownership, (iii) alignment, and (iv) accountability. We consider these dimensions when we review evidence about the role of coordination for aid efficiency in the next section, but before moving to that discussion, we make some general observations about the four aspects.

4.1 Harmonization

First, it seems obvious that harmonization should have a cost reducing effect. Aid coordination allows donor to economize on their own transaction costs, and at the same time reduce the amount of resources that recipients need to spend in the aid delivery process. Still, these cost savings results are not always self-evident. For example, Odén and Wohlgemuth (2011: 7) report that for recipients such as Zambia, Kenya and Tanzania, the general perception is that the developed dialogue structure has become too complex, overburdening the recipient administration. They also warn of an increasing tendency among donors to want to micromanage programmes in the numerous consultation bodies, which have been set up to coordinate aid interventions.

Second, there are the incentive effects of donor coordination. This issue has mostly been analysed for the case with several donors and one recipient country (Torsvik 2005; Knack and Rahman 2007). The results of the literature can be summarized as follows:

> When the recipient country's government shares the goals of the donors (it is equally averse to poverty), aid coordination is unambiguously beneficial. In the opposite case of diverging interests, however, coordination is not necessarily beneficial if contracts cannot be effectively used to align the interests of the recipient country with those of the donors (Bigsten et al. 2011: ch. 3).

So the effectiveness of coordination would depend on the congruence of goals. If the recipient is not development-oriented, it is hard to improve results by coordinating.

The literature has further discussed the mechanisms by which harmonization could reduce the risk of elite capture (Azam and Laffont 2003; Svensson 2000, 2003; Bourguignon and Platteau 2011; Gaspart and Platteau 2011). This could be achieved if donors, by reducing the number of players in a country, can limit the exit options available to the local counterparts. And if donors jointly introduce a mechanism to inform each other about fraudulent acts committed by intermediaries, elite capture could be contained (Platteau 2000; Aoki 2001).

Another dimension relates to how easily the donors can adjust their aid in response to inefficiencies or corruption. For example, Easterly (2006) points out that in a situation where there are many donors involved, it is hard to decide who is accountable. This can weaken incentives of donor organizations. It is hard to allocate responsibility, which means that it is harder to introduce corrective action.

One may also note that there are some donors, which do not want to harmonize (e.g., the US and the new donors such as China, India and Brazil) as well as the new vertical or global funds, which run their projects outside the government budget system. So it is not clear that there is in aggregate a trend towards increasing harmonization. In the case of Tanzania, for example, the number of projects is increasing again. But as we have noted, the need for coordination is strongest when resources are transferred through the recipient government's apparatus.

The huge donor evaluation of the implementation of the Paris Declaration by Wood et al. (2011: xiv) concludes that the results have been somewhat disappointing in relation to the goal of rapidly reduced burdens in managing aid. Still, they find that practices have been put in place, which at least allow a better overview of aid by both donors and recipients. The report is concerned by the fact that that donors are slow to change and generally very risk averse, while partner countries have increasingly taken on the agenda. Still, harmonization is regarded as the most successfully implemented part of the Paris Agenda.

4.2 Ownership

It is important for recipient incentives that the government can formulate its policy according to its own priorities. How this is affected by donor coordination is not self-evident, but it may well be that the recipient has a stronger incentive to formulate its position well vis-à-vis a large cohesive group of donors than against a group with many different requests. It is hard to measure how changes in conditionality affect aid effectiveness, but it seems reasonable to assume that aid coordination can allow for a more effective implementation of conditionalities.

There is a presumption in the literature that more general forms of aid make it possible for recipients to have better ownership of the policy process. By reducing the reporting burden and simplifying coordination of activities, it should be efficiency enhancing. However, Odén and Wohlgemuth (2011) report that for Tanzania, Zambia, and Mozambique, which are among the most advanced with regard to the implementation of the Paris Agenda, there are increasing problems with regard to the dialogue between the donors and the recipient governments related to the use of general budget support (GBS) modality. They voice the concern that the increased use has meant that the dialogue has become more political in nature, which may imply a reduction in

ownership. So it does not seem to be automatic that a general from of aid leads to improved ownership.

Odén and Wohlgemuth draw the conclusion from their review that there is weak willingness and capacity of the host governments in Africa to take up their leadership role in the PA process. At the same time there is also a reduced willingness by many donors (Paris fatigue) to accept delays due to increased ownership. The key recommendations of Wood et al. (2011) are that the aid process should be country led, risks should be managed more honestly, and there should be high-level political commitment to the PA process. But the rate of implementation has been disappointing. This may reflect dissatisfaction with the results, rather than a reluctance to apply the PA.

4.3 Alignment

There is a broad consensus that development depends fundamentally on policies and institutions (Hall and Jones 1999; Kaufmann, Kraay and Zoido-Lobatón 1999; Rodrik, Subramanian and Trebbi 2004). Besley and Persson (2010) point to 'state capacity' as the key determinant of whether a country can achieve development. Aid is often allocated to improve the quality of public institutions, but how should interventions be designed to help build effective institutions rather than undercut incentives for good public governance? It seems clear that aid affects growth via governance variables, and how governance is affected depends on how aid is channelled. Projects require a lot of detailed decisions and steering, which is a burden on the administrative systems. Therefore more general forms of aid or even transfers outside the state apparatus should be preferable. This would make it possible to leave more of the decisionmaking in the hands of the recipient, i.e., increase ownership.

It is likely that aid to government will have a more sustainable impact if it is integrated within the regular government system, even if it may increase the risk of misappropriation. On the basis of the large recent literature on the importance of good governance, it seems clear that one key impact of aid is the effect it has on governance structures. Therefore, even if an individual project may work better within parallel structures, one must factor in what the consequences are for the long-run functionality of the whole system of government.

4.4 Accountability

The final issue we consider is how aid coordination affects transparency in the recipient countries. It may well be that countries have a stronger incentive to report effectively to a larger group of donors than to them individually. It will, of course, also be easier to produce one comprehensive report than to produce many adjusted to each donor's individual requests. Both these factors may thus contribute to improved reporting and increased transparency.

One of Wood's et al. (2011) recommendation is to 'focus on transparency, mutual accountability, and shared risk management'. Odén and Wohlgemuth (2011) find that some donors have found it increasingly difficult to hold governments accountable for mismanagement and corrupt practices.

5 Donor coordination and aid effectiveness

The Paris Agenda has broad scope, covering both various dimensions of how donors coordinate their actions among themselves, and dimensions relating to how each donor interacts with the recipient government. Since our focus is on the first dimension, we concentrate on two dimensions which are crucial. This is, first, the issue of coordination of aid activities among the donors so as to reduce transaction costs. The second dimension relates to donor coordination of the allocation of aid resources across developing countries. Can we improve poverty reduction by better allocation of aid resources among countries? Can more be achieved by shifting resources from donor darlings to donor orphans? We complement these discussions by some comments on other dimensions of the Paris Agenda.

5.1 Transactions costs (cost saving for donors)

In this section we discuss two parts of harmonization. One can reduce aid fragmentation (having a more effective division of labour) by having fewer partner countries and by shifting from projects to programme-based approaches. We estimate how far from the optimal levels the donor community is, and we also try to measure what it costs. We do this by estimating the extra administrative costs that are due to aid not being fully harmonized.

Much of the debate about aid coordination has concerned coordination of aid to individual countries (Bigsten 2006). 'Since aid activities are often complementary, donors need to coordinate to avoid inefficient aid allocations. How difficult it is to coordinate donors depends on the degree of similarity of their preferences. Donors may have different views on what matters for development, or different national interests. Multilateralism could help reduce the influence of vested interests in the various donor countries' (Kanbur 2000, 2006).

A key question in this context is how aid efficiency is affected by reduced administration of aid interventions. Administrative controls are important in some instances—and in particular if aid is given to poorly governed and possibly corrupt countries. It is certainly not possible or appropriate to bring the level of administration to zero, and this is not envisaged here.

Although the optimal overhead is not zero, our estimates give an indication about the savings that can potentially be made on administrative costs. The focus in this section is on the short-term or transaction costs of aid on the donor side. Our approach is an extension of Bigsten et al. (2011). We try to get full coverage of all transaction costs of the donors. To do this we start with comprehensive information from donors on all their administrative costs and evaluate how much of this cost could be saved by concentrating activities. There can be concentration by country and there can be concentration to fewer activities. The challenge is to know how much can be saved by concentration. We assume that the aid budget will not shrink, which means that the remaining activities will be larger. We do not believe that they can grow in size without some increase in administrative overheads. However, there are clearly economies of scale so the increase is not proportional to the growth of the budget.

For data reasons our computations are made for all DAC country donors plus the EC.[1] This means that other multilaterals plus a few smaller donors are missing, and that we cover about three-quarters of all aid, but one could argue that we cover the most relevant part. Multilaterals like the UNICEF are not supposed to concentrate their aid on only a few countries. Still, also the multilaterals could use PBA to a larger extent, but we lack the data to estimate potential effects.

The steps in our computation of administrative savings possible for year 2009 are done as follows:

Step 1: We first scale down the administrative costs by reducing the number of partner countries. We estimate the percentage reduction in administrative costs when reducing the number of recipients, while keeping the overall aid budget constant and without changing the composition of the aid flow, i.e. the mix of projects and programmes. To be able to do this we use an estimate of the economies of scale in aid delivery, which we have derived earlier with the help of regression analysis (Bigsten et al. 2011).

Step 2: We then reduce costs further by changing the aid modality. We investigate how much money can be saved by shifting money from projects to programmes. This gives an extra cost saving on top of the effect of country concentration. So we estimate the required amount of aid that comes from bilaterals as project support that needs to be shifted to programme support to meet the 66 per cent target of the Paris Declaration. To get an estimate of how large the cost savings are, we need an estimate of the administrative cost reductions such a shift implies. One might expect that there are also efficiency consequences of a switch from projects to programmes. The administrative costs of recipients would probably tend to fall, while leakages of resources might increase. There may also be specific instances where projects should be preferred. However, we cannot be certain about the sign of the aggregate of these excluded effects, and we are not able to incorporate these potential effects in the estimations here.

It should be noted that technical assistance is not included in our computations, for two reasons. First, we can reach the 66 per cent target by only shifting from projects to programmes. Estimates in Bigsten et al. (2011) show that there is a bigger saving from shifting from projects to programmes than shifting from technical assistance (TA) to programmes based on the price tags we have derived. Second, it is less clear that it is as feasible to shift this type of aid into programmes, although there should be some scope also here that donors could exploit if there were the political will to do so.

Table 2 shows the most important aid magnitudes for 2009. The calculations of cost savings will start from the number for administrative costs of US$6113 million.

Step 1: We first estimate how much the administrative costs can be reduced if donors focus on fewer partner countries. To be able to come up with such an estimate we need an estimate of the scope for costs savings. Bigsten et al. (2011) estimate the relation between fragmentation and administrative costs controlling for aid volume and a time trend. Fragmentation was measured as the number of partner countries a donor has. This

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1 We also included those new donors which had reported data (Czech Republic, Korea, and Turkey). We have had to exclude Arab countries, Hungary, Iceland, Israel, Poland, Slovak Republic, Slovenia, Thailand, Chinese Taipei and some small donors, since they do not report administrative costs. They have a total bilateral ODA of US$4,974 million.

is measured as the number of links relating to CPA, since what we are proposing is to have fewer partner countries and not, for example, to give emergency aid, food aid, or debt relief to fewer countries.[2] Their analysis covers all donor countries and the EC (other multilaterals had to be excluded due to lack of data) for 2000-09.

The fragmentation measure was on average 100.7 and had a standard deviation of 37.1. That the average donor country has a hundred partner countries is astonishing. The Paris Declaration does not provide any target for how much this should be decreased, but following the tradition in economics, we discuss the effect of a reduction in the number of partner countries by one standard deviation. Bigsten et al. (2011) find that the effect of such a concentration is that the administrative costs would decreases by 20 per cent. See Bigsten et al. (2011).

This means that administrative costs would decrease by about 20 per cent. Applying this 20 per cent estimate on total administrative costs of US$6,113.15 million (from Table 2), we get a saving of 0.20 * 6,113.15 = US$1,223 million.

Step 2: Once donors have focused on fewer countries, they can change, as a second step, the modalities of aid. It is a challenge to get estimates of the price tags of administration for different modalities. We do not have comprehensive estimates of this, but we have information from the Swedish Aid Agency, Sida. This is a medium-sized bilateral donor, which probably can be taken to be rather typical in terms of administrative costs.[3] Sida undertook a detailed analysis of its administrative costs in 2010, which was presented in its annual report for that year (Sida 2011). Using that information, we can conclude that programme aid per dollar disbursed only costs 33.5 per cent as much as project aid in donor administration costs. Further, money transferred as TA had a transaction cost of 45.9 per cent of the costs for a project. Thus, also technical assistance is associated with relatively low administrative costs

The focus in the Paris Declaration is about shifting to programme-based approaches (PBA) from non-PBA, i.e., projects and technical assistance. What we simulate here is a shift from projects to programmes, while we leave technical assistance aside. The goal set up is to have 66 per cent of the aid through PBA, so what we look at is a reduction on the project side in favour of programmes.

After reducing the number of recipients in step 1, the administrative costs remaining in our main case is US$4,890 million. We now want to consider how much of this is affected by a shift from non-PBA (projects) to PBA. We first compute how much of these costs are related to CPA, the most relevant part of aid in this context. We find that 77 per cent of the administrative costs, that is US$3,765 million, are related to CPA. See Appendix A1.

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2 They also do an analysis of the effect of the number of links between donors and sector in countries, to check whether there is more information in the links to sectors over and above what was picked up in their first regressions. As it turns out there are no added effects of including this dimension.

3 Easterly and Pfutze (2008) collect information from donors about administrative costs. Their estimates indicate that there is a huge variation across countries and multilaterals. The average for bilaterals is 7 per cent. It is noteworthy that the share of administrative costs in their sample of 21 countries is close to our own estimate for Sida.

The target of the Paris Agenda is to increase the share of flows going through programme-based approaches to 66 per cent. This could possibly be interpreted to mean 66 per cent of total ODA, but in our estimate here we interpret this to mean that 66 per cent of CPA is to go through PBA. With the broader interpretation the estimate would of course be larger than what we get here. If we increase the proportion of CPA that constitutes PBA from the actual 2009 level of 39 per cent to 66 per cent, the CPA administrative costs related to CPA will be reduced by 24.3 per cent. See Appendix A2. The figure 24.3 per cent is based on programme aid per dollar disbursed costs only 33.5 per cent as much as project aid in donor administration costs, as Sida notes (2011). That gives a cost saving of 0.243*3765 = US$915 million.

Summing up the results of our two steps, we get a total saving on transaction costs of US$2138 million. So it seems clear that donors could save significant amounts of resources by reducing aid fragmentation, but the fact that they have not done this may be an indication that they consider the political costs of adjusting to be too high.

Table 2
Gross disbursements in 2009 at current prices (from the DAC database)
(million US$)

Donor	CPA	Administrative costs	Bilateral ODA excl. CPA and admin costs	Bilateral ODA
Australia	1,622.62	109.07	580.09	2,311.78
Austria	106.57	39.9	373.77	520.24
Belgium	514.7	94.77	1,054.25	1,663.72
Canada	1,712.07	269.62	1,200.11	3,181.8
Czech Republic	92.24	3.9	4.9	101.04
Denmark	1,342.36	161.56	437.32	1,941.24
EU Institutions	9,484.95	762.81	2,775.82	13,023.58
Finland	412.22	80.27	298.61	791.1
France	4,171.17	441.43	5,234.54	9,847.14
Germany	4,674.73	287.49	3,397.45	8,359.67
Greece	153.15	23.36	120.43	296.94
Ireland	381.5	44.85	266.85	693.2
Italy	580.96	59.43	412.55	1,052.94
Japan	10,568.53	723.77	1,692.46	12,984.76
Korea	526.24	27.76	61.31	615.31
Luxembourg	180.56	19.5	65.94	266
Netherlands	1,850.15	331.17	2,775.94	4,957.26
New Zealand	162.88	23.95	39.16	225.99
Norway	1,460.68	215.66	1,491.89	3,168.23
Portugal	240.39	18.33	53.47	312.19
Spain	2,797.12	189.57	1,886.37	4,873.06
Sweden	1,377.53	219.43	1,416.15	3,013.11
Switzerland	573.79	162.47	1,024.34	1,760.6
Turkey	614.34	51.68	-0.71	665.31
United Kingdom	3,992.8	397.05	3,474.52	7,864.37
United States	15,732.11	1,354.35	8,905.94	25,992.4
Total	65,326.36	6,113.15	39,043.47	110,482.98

Note: Due to lack of data on administrative cost, the following donors are excluded: multilateral donors excluding the European Commission, Arab countries, Hungary, Iceland, Israel; other donor countries, Poland, Slovak Republic, Slovenia, Thailand and Chinese Taipei.

Source: Based on International Development Statistics (IDS) online databases from OECD/DCD-DAC.

It should also be noted that what we have estimated here relates just to costs on the donor side, while lack of harmonization, of course, has consequences for costs also on the recipient side. Recipient costs are both administrative transaction costs and various indirect costs. In our study of European aid (Bigsten et al. 2011) we attempted to capture indirect costs of the lack of harmonization on growth, and we do find that there are such costs. Our estimates in Bigsten et al. (2011) indicate that these effects are potentially large, but the estimates are very imprecise.

5.2 Addressing the issue of aid orphans (benefits for recipients)

The reduction of costly fragmentation of aid is an essential part of donor coordination. As was pointed out in the AAA, the efficiency of aid use can be enhanced by improved allocation of resources across countries. Developing and donor countries stated in the AAA that that 'we will work to address the issue of countries that receive insufficient aid' (AAA: Point 17d).

To what extent has this issue been addressed, and how much more needs to be done? We analyse this by investigating what an 'optimal' aid allocation would look like if the aim is to achieve as large a reduction of poverty as possible. We also investigate how much greater poverty reduction could be achieved if aid were actually allocated according to our allocation rule.

In this analysis we consider country programmable aid (CPA) from the whole of DAC for the year 2009. We include CPA both from country donors and from multilateral donors, but we exclude CPA given as regional aid. This gives us a total of US$87,638 million of aid to start with. After excluding aid to some countries that could not be included due to lack of data on incomes (mainly the Palestinian Administrative Areas and Mayotte, see Appendix Table 1), we are left with US$83,958 million that donors could seek to allocate optimally. Two arguments for including both bilateral and multilateral CPA is that donor countries have influence on multilateral aid indirectly, and that even if we consider multilateral aid (the European Commission excluded) as 'exogenous', the bilateral aid plus EC aid could still be allocated so that the final total allocation is optimal. Since bilateral CPA plus CPA from the EC make up 70 per cent of the CPA included in our analysis, it is large enough to make it possible to adjust the total allocation towards the optimal allocation.

In the analysis of optimal aid allocation, it is important to discuss issues related to both the needs and the ability of recipient countries to transform increased aid volumes into poverty reduction. Therefore, when computing how much aid should to be reallocated from darlings to orphans, we develop the extension of Collier and Dollar (2002) which is presented in Bigsten et al. (2011). We need to take into account that aid has been found to have decreasing returns with regard to its share of GDP. We assume that the point at which the positive impact of aid falls to zero is when aid/GDP (PPP) = 10 per cent.[4]

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4 This level is based on the average estimate of 30 per cent for all aid in nominal dollars in the studies surveyed by Clemens and Radelet (2003). This estimate is first scaled down to 20 per cent, since we only consider CPA and not all aid. It is then scaled down further to 10 per cent, since we use PPP-figures for GDP/capita. We use PPP-adjusted figures, since we let poverty be a function of

From a theoretical perspective the quality of governance should be included in the model. But measures such as the Worldwide Governance Indicators (WGI) are largely subjective, and the estimates of the impact of quality of governance on the ability to transform aid volumes into poverty reduction are very imprecise. Therefore, any aid allocation rule that is derived from a model that takes the quality of governance into account will be quite imprecise. Thus we argue that it is preferable, first, to derive an optimal aid allocation that does not take the quality of governance into account, and instead incorporate the quality of governance in a second step when discussing this allocation and its benefits and costs.

The model

For country i we let N_i be population, y_i be GDP per capita, A_i be aid/GDP, h_i be headcount poverty, G_i be growth and α_i be the income elasticity of headcount poverty. Like Collier and Dollar, we assume that $\alpha_i = \alpha$, i.e., that the elasticity is the same in all countries. This is clearly not the case,[5] but since we only want to find the aggregate effect, the use of this simplification should be acceptable. We assume that the objective function of donors is to allocate aid among countries so as to

$$\text{Max poverty reduction } \sum_i G_i \alpha\, h_i N_i \tag{1}$$

If we consider for the moment only interior solutions, the first order conditions for a maximum are

$$\frac{dG_i}{dA_i} = \lambda \frac{y_i}{\alpha h_i}, \tag{2}$$

where λ is the shadow value of aid. Assuming (as is standard in the literature, e.g., Collier and Dollar 2002) a quadratic relationship between A and G, using 10 per cent as the saturation point, and letting g denote $\frac{dG}{dA}$ when $A = 0$ it follows that

$$\frac{dG_i}{dA_i} = g(1 - 10A_i). \tag{3}$$

Bourguignon (2000) finds an income elasticity of headcount poverty (US$1 per day line) of approximately –2. He also finds that the absolute value of the elasticity is generally smaller in poorer countries, so we use –1 as a conservative number. This may bias our results downwards somewhat. Now we can write poverty as a function of income and a constant k.

$$h_i = k y_i^{-1} \tag{4}$$

Then (2) – (4) implies

$$A_i = 0.1 - \gamma y_i^2 \tag{5}$$

GDP/capita, see expression (5.4). This simplification should be more accurate when using PPP-figures than nominal figures.

5 See, for example, Bigsten and Shimeles (2007) on variation of the elasticity across African countries.

where $\gamma = \frac{0.1\lambda}{gk\alpha}$.

Now we can derive an allocation rule. The aid allocation to country i, A_i^*, should be the aid derived in (5), but obviously aid must be non-negative, so we now also need to consider corner solutions.

This gives:

$$A_i^* = 0.1 - \gamma y_i^2 \qquad if\ 0.1 - \gamma y_i^2 > 0 \tag{6}$$

$$A_i^* = 0 \qquad if\ 0.1 - \gamma y_i^2 \leq 0$$

We cannot use this allocation rule directly, since we cannot solve for λ analytically, and we do not know the exact values of g and k. But since the budget condition is

$$\sum_i y_i A_i^* N_i = 83\ 958 \tag{7}$$

we can numerically solve for γ and then use (6) as our allocation rule. Note that there is no need to solve for λ, or to apply values for α, g, or k. It is enough to solve for γ to be able to derive the optimal allocation.

Results and discussion

We define 'aid orphan' as a country that receives less aid than our allocation rule recommends. To reduce poverty more effectively, the donor community should scale up aid to these countries. Table 3 shows data for all orphans, including the increase in aid our analysis recommends. We further define 'aid darling' as a country that gets more aid than our allocation rule recommends. The donor community should scale down aid to these countries. Table 4 shows detailed information on the most important darlings, and aggregate information for the rest of the darlings, including the decrease in aid our analysis recommends.

If we do not take aid absorption capacity into account

In Tables 3 and 4 we see that as much as US$44,609 million of aid (out of US$83,958 million) should be reallocated. The fact that more than half of the money would have to be reallocated is alarming. But one might be concerned that there are differences across countries in how effectively the money is used to reduce poverty. Therefore it is important to study the relation between the cost and the benefit of making such a re-allocation.

The benefit of this is US$44,609 million more to the orphans (that end up with US$75,534 million) and the cost is that the darlings lose US$44,609 million (ending up with US$8,424 million). This shift represents an efficiency gain in terms of poverty reduction (decrease in the number below the poverty line), since the poverty reduction effect of one dollar in the darling countries is only 16.2 per cent of the effect the same dollar would have in the orphan countries.[6] If we use the dollars optimally allocated as

6 This is calculated using Equations (3) and (4).

the norm, we can say that the cost is 0.162 * US$44,609 million = US$7,227 million. Thus, the net benefit is US$44,609 million minus US$7,227 million = US$37,382 million. So we conclude that the net gain from reallocation according to the assumptions used so far would be US$37,382 million.

Table 3
Aid orphans

			Actual aid 2009			Optimal aid				
	Popu-lation	GDP/cap PPP	/cap	/GDP	Total	/cap	GDP	Total	Recom. increase	Gov.
	million	$	$	%	million	$	%	million	Million	index
	Good orphans (Gov. index > –5.8, weighted average Gov. index is –4.48)									
Bangladesh	162	1,286	10	0.8	1,665	94	7.3	15,217	13,552	-5.4
Kenya	40	1,428	38	2.7	1,520	95	6.7	3,787	2,268	-4.6
Uganda	33	1,105	47	4.3	1,545	88	8.0	2,893	1,347	-3.7
Tanzania	44	1,237	65	5.2	2,829	93	7.5	4,056	1,227	-1.7
Madagascar	20	912	19	2.1	381	79	8.6	1,546	1,164	-3.4
Ghana	24	1,410	65	4.6	1,544	95	6.7	2,268	723	0.8
Cameroon	20	2,002	32	1.6	633	69	3.4	1,345	712	-4.9
Cambodia	15	1,739	47	2.7	701	88	5.1	1,301	600	-4.8
Niger	15	626	25	3.9	376	59	9.4	896	520	-4.4
Burkina Faso	16	1,078	63	5.9	1,000	87	8.1	1,375	375	-1.9
Malawi	15	721	45	6.2	686	66	9.1	1,007	321	-2.0
Togo	7	772	33	4.3	218	70	9.0	461	243	-5.4
Senegal	13	1,650	73	4.5	921	92	5.5	1,147	226	-2.0
Mali	13	1,077	72	6.7	932	87	8.1	1,135	202	-2.4
Benin	9	1,369	72	5.3	647	95	6.9	848	201	-1.4
Lesotho	2	1,333	66	4.9	136	95	7.1	195	59	-0.7
Mauritania	3	1,751	74	4.2	243	87	5.0	287	44	-5.2
Gambia	2	1,285	76	5.9	130	94	7.3	160	30	-2.7
Zambia	13	1,299	93	7.2	1,204	94	7.2	1,216	12	-1.9
Sum	464				17,313			41,140	23828	
	Bad orphans (Gov. index < –5.8)									
Nigeria	155	2,001	11	0.5	1,657	69	3.4	10,680	9,022	-7.0
Ethiopia	83	848	35	4.2	2,919	75	8.8	6,200	3,281	-5.9
Sudan	42	2,007	23	1.1	956	68	3.4	2,894	1,938	-9.4
Nepal	29	1,049	30	2.8	866	86	8.2	2,522	1,656	-5.8
Côte d'Ivoire	21	1,545	38	2.4	796	94	6.1	1,984	1,189	-7.4
Chad	11	1,181	23	2.0	262	91	7.7	1,021	759	-8.6
Zimbabwe	13	898	26	2.9	329	78	8.7	976	648	-10.4
Guinea	10	951	17	1.8	175	81	8.5	816	641	-8.6
Yemen	24	2,243	17	0.8	403	40	1.8	937	534	-7.5
Pakistan	170	2,369	17	0.7	2,842	19	0.8	3,291	449	-7.2
Congo, DR	66	290	25	8.8	1,680	29	9.9	1,887	207	-10.0
Tajikistan	7	1,791	57	3.2	394	85	4.8	592	198	-6.8
Eritrea	5	527	21	4.1	109	50	9.5	255	147	-8.2
CAR	4	688	41	5.9	181	63	9.2	281	100	-7.7
Comoros	1	1,074	68	6.3	45	87	8.1	57	12	-6.5
Sum	640				13,613			34,394	20,781	
All orphans	1,104				30,926			75,534	44,609	

Source: Computed by authors based on IDS online databases from OECD/DCD-DAC, WDI and WGI from the World Bank.

Table 4
Aid darlings: countries from which donors should reallocate more than US$300m are shown

	Popu-lation	GDP/cap PPP	Actual aid 2009 /cap	Actual aid 2009 /GDP	Actual aid 2009 Total	Optimal aid /cap	Optimal aid /GDP	Optimal aid Total	Recom. increase	Gov.
	million	$	$	%	million	$	%	million	Million	index
	Bad darlings (Gov. index < –2.3, weighted average Gov. index is –4.67)									
Viet Nam	87	2,682	47	1.7	4,066	0	0.0	0	4,066	-3.1
Indonesia	230	3,813	14	0.4	3,323	0	0.0	0	3,323	-2.5
Afghanistan	30	1,200	177	14.8	5,285	92	7.6	2,734	2,552	-11.1
China	1331	6,200	2	0.0	2,440	0	0.0	0	2,440	-3.1
Iraq	31	3,222	72	2.2	2,271	0	0.0	0	2,271	-9.0
Egypt	83	5,151	16	0.3	1,350	0	0.0	0	1,350	-2.6
Philippines	92	3,216	12	0.4	1,076	0	0.0	0	1,076	-2.9
Colombia	46	8,136	20	0.2	923	0	0.0	0	923	-2.3
Bolivia	10	4,013	64	1.6	634	0	0.0	0	634	-4.5
Nicaragua	6	2,398	123	5.1	705	14	0.6	81	624	-4.0
Lebanon	4	11,868	133	1.1	562	0	0.0	0	562	-4.0
Honduras	7	3,488	56	1.6	419	0	0.0	0	419	-3.4
Kazakhstan	16	10,452	20	0.2	318	0	0.0	0	318	-2.4
Guatemala	14	4,286	23	0.5	316	0	0.0	0	316	-3.5
Rest	313				7,344			3,944	3,400	
Sum	2301				31,031			6,759	24,273	
	Good darlings (Gov. index > –2.3)									
India	1155	2,993	3	0.1	3,918	0	0.0	0	3,918	-1.3
Turkey	75	11,209	22	0.2	1,653	0	0.0	0	1,653	-0.1
Morocco	32	4,081	37	0.9	1,194	0	0.0	0	1,194	-1.7
South Africa	49	9,333	20	0.2	1,007	0	0.0	0	1,007	1.7
Sri Lanka	20	4,333	49	1.1	996	0	0.0	0	996	
Jordan	6	5,082	150	3.0	894	0	0.0	0	894	0.2
Georgia	4	4,335	185	4.3	789	0	0.0	0	789	-0.7
Kosovo	2	5,969	412	6.9	744	0	0.0	0	744	-2.2
Tunisia	10	7,512	59	0.8	617	0	0.0	0	617	-0.3
Ukraine	46	5,737	13	0.2	608	0	0.0	0	608	
Serbia	7	9,967	79	0.8	582	0	0.0	0	582	-1.0
Armenia	3	4,794	180	3.8	556	0	0.0	0	556	-1.3
Peru	29	7,836	18	0.2	539	0	0.0	0	539	-1.8
Brazil	194	9,414	3	0.0	488	0	0.0	0	488	0.8
Mongolia	3	3,198	146	4.6	389	0	0.0	0	389	-2.0
Bosnia-Herz.	4	7,266	102	1.4	385	0	0.0	0	385	-2.0
Albania	3	7,449	108	1.4	340	0	0.0	0	340	-0.7
Namibia	2	5,821	153	2.6	332	0	0.0	0	332	1.9
Rest	344				5,972			1,665	43,07	
Sum	1,989				22,001			1,665	20,336	
All darlings	4,291				53,032			8,424	44,609	

Source: Computed by authors based on IDS online databases from OECD/DCD-DAC, WDI and WGI from the World Bank.

If we do take aid absorption capacity into account

However, for this gain to be realized there should not be any difference in the quality of governance between the darlings and the orphans. But there is such a difference! In the sample the weighted average of the governance index (WGI, see Kaufmann, Kraay and

Mastruzzi 2010) is lower among the orphans than among the darlings.[7] A high index indicates strong governance performance, and a low index indicates weak governance performance. The growth effect of the resources shifted to the orphans should thus on average be lower than it would have been if the orphans had had the same quality of governance as the darlings. To adjust for this we use a rather crude approach. We first separate out a re-allocation from the worst governed darlings to the best governed orphans. We want these two groups to contain as much aid money (that our allocation rule recommends to be reallocated) as possible, and at the same time we want the weighted average quality of governance index among the good orphans to be at least as high as the weighted average governance index among the bad darlings. As much as US$23,828 million of the missing aid in orphan countries is in countries with a weighted average governance index of –4.48. These are the 'good orphans'. We can also create a group of the worst darlings. We expand this group successively until it includes at least US$23,828 million. The weighted average governance index is then –4.67.

It turns out that the bad darlings (e.g., Indonesia, China, Egypt and the Philippines) contain US$24,273 million. Out of this total, US$23 828 million can be reallocated to the 'good orphans', which on average have a bit higher quality of governance index. When comparing the bad darlings to the good orphans we see that: the poverty reduction effect of a dollar in the bad darling countries is 18.2 per cent of the effect the same dollar would have in the good orphan countries. The cost is therefore 0.182 * US$23,828 million = US$4,337 million, and thus the net benefit is US$23,828 million minus US$4,337 million = US$19,491 million. So we conclude that the net gain from reallocation according to the assumptions used so far would be US$19,491 million.

For the remaining US$44,609 million minus US$23,828 million = US$20,781 million, it is hard to estimate the magnitude of the efficiency loss. US$24,273 million minus US$23,828 million = US$445 million is today the sum transferred to bad darlings. This money could probably be reallocated to some orphans. Now remains the question of the effect of reallocating money from good darlings to bad orphans. We would like to highlight that a lot of money could be transferred from the rich good darlings that do not need the money to the bad orphans that are so underfunded that they could absorb more aid money even though they have bad governance (as reported by WGI), for example Ethiopia (aid/GDP = 4.2 per cent), Nepal (2.8 per cent) or Côte d'Ivoire (2.4 per cent), or maybe the oil producing Nigeria (0.5 per cent).

Of the US$20,336 million of 'surplus money' that goes to good darlings, US$8,915 million goes to countries with over US$6,000 GDP/cap PPP (e.g., Turkey, Tunisia and Brazil, but also Malaysia and Argentina gets some money!). The cost of reallocating this money is very low, since there is not much poverty to fight in those 'rich' countries. This money should therefore be reallocated to some of the orphans. Another US$6,554 million goes to countries with GDP/cap PPP 4000-6000 (e.g., Morocco, Sri Lanka and

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[7] The Worldwide Governance Indicators (WGI) project studies six dimensions of governance. For each dimension a governance indicator is estimated. We use the sum of the six indicators as a governance index. The weighted average of the governance index within a group of partner countries is weighted using the amount of aid that should be reallocated as weights.

Ukraine), and one could, of course, also reallocate those as well as the rest. But it is hard to come up with reasonable estimates of the efficiency losses.

Thus, our crude estimates are two-fold. First, there is US$23,828 million minus US$4,337 million = US$19,491 million that we assume can be transferred without loss in growth and poverty reduction efficiency. Second, we can transfer US$8,915 million from countries with over US$6,000 GDP/cap PPP (e.g., Turkey, Mexico and Brazil) to bad orphans, but here we are uncertain about the poverty reduction efficiency. And we could continue the process of reallocation further but then with even more uncertainty about the poverty effects.

It should be noted that some of the darlings are post-conflict countries such as Iraq and Lebanon. Maybe it makes sense to give them aid, but should that not be taken from another budget than ODA? These countries have no extreme poverty. The same argument goes for the ex-communist countries. We support them for reasons other than to fight extreme poverty. So the money should not come from ODA budget.

So what we have tried to do is to measure how much could be gained if all donors were concerned only with aggregate poverty reduction and completely ignored political costs of coordination. In this experiment we consider only country programmable aid. It is clear that aid after reallocation would be concentrated in fewer countries. The reallocation would lead to a modest increase of poverty among the donor darlings and a large decline in poverty in the orphan countries. But clearly our estimates must be seen as an upper limit as to what can be achieved.

5.3 Further dimensions of the Paris Agenda and aid coordination

In the previous two sections we discussed the two key dimensions of donor coordination and aid effectiveness, but there are also other aspects of the Paris Agenda which are relevant and which we will touch upon here more briefly.

One aspect of bad donor behaviour that is addressed in the agenda is the tying of aid. This increases the cost of aid or reduces the amount of effective aid that a certain amount of budgetary resources can buy. The magnitude of this negative effect on the value of aid depends on the amount of aid that is tied and the cost increase associated with the tying.

Bigsten et al. (2011) estimate the cost of the tying of aid within the EU. Cost is equal to the reduction in the value of resources transferred due to restrictions on their use. By combining information about the extent of aid tying (only considering fully tied aid, which was 8.9 per cent of bilateral EU aid) with the EU with an estimate of the cost increase implied by tying (18 per cent is assumed to be lost), we compute a cost increase of €800 million per year. Of course, this is a very crude estimate. Partially tied aid is not included and there is certainly much more cost-increasing informal tying going on that is not reported into the DAC database (Easterly and Pfutze 2008; Knack, Rogers and Eubank 2010; Clay, Geddes and Natali 2009; Jepma 1991). One counterargument sometimes advanced against these kinds of estimates is that tying helps increase the willingness of donors to give aid, a fact which may have some validity. But it is also possible that the tying of aid has negative effects on recipient

behaviour. It may make the recipient a more passive actor, but there is little systematic evidence on this.

So what could donor coordination do here? Basically what could be done is to seek an agreement where all agree to avoid tying. It is harder to conceive of how one would coordinate tying activities to increase efficiency. This is clearly a bad thing as far as aid efficiency concerned.

Another problem for aid efficiency is the unpredictability and volatility of aid flows. This makes it much harder for recipient countries to plan and implement their policies. The hypothesis is that uncertainty makes recipient more conservative when it comes to allocating funds. They will be less inclined to invest for the long term if they are not certain that the money is forthcoming. And it may also undermine the quality of governance generally. But there are also fluctuations which are welfare-enhancing. Many poor countries are vulnerable to external shocks. Shocks were previously related mostly to trade, but they have increasingly come to be financial shocks. It is also noteworthy that financial flows to the least developed countries follow a procyclical pattern, with negative effects on growth. If a country is exposed to negative shock, it is desirable that donors increase aid to compensate for this. Therefore countercyclical aid can potentially be very important. And this is clearly an area where there is room for donor coordination. One or a few could bear the responsibility of trying to provide countercyclical aid.

Bigsten et al. (2011) undertakes calculations (using the methodology of Kharas 2008) as to how much could be gained if the volatility of country programmable EU aid was eliminated. The conservative estimate of the deadweight loss was €1500 million per year, which is a large amount.

Bigsten et al. (2011) also tries (bravely) to estimate how the choice of aid modalities affects institutions and growth. The variables tried in this context were three PD indicators, namely aid fragmentation (CPA/GDP per number of donors giving CPA), general budget support share (GBS/GDP), and tied aid share (tied aid/GDP). Only one of the indicators had a statistically significant effect on growth, and that is budget support/GDP. Still, these estimates are uncertain.

6 The political economy of implementation of the recommendations

We started this paper by identifying four key dimensions of the Paris Agenda, namely (i) harmonization, (ii) ownership, (iii) alignment, and (iv) accountability. We then present new empirical evidence on the efficiency gains of aid coordination. These were the gains from reduced fragmentation of aid and coordinated allocation across countries. And we also discussed other efficiency gains that can be realized by better coordination.

With regard to *harmonization* we find that major cost savings can be achieved if donors concentrate their aid efforts on fewer countries and focus on more general forms of aid transfers, such as general budget support. There may be political constraints on such a change, since it would mean that major donors would have to abandon certain countries, while they may feel that they have a political interest in showing presence there. To focus aid on more general forms of assistance may be politically easier, but donors are

reluctant to go for general forms of aid when they are uncertain about recipients' quality of governance. Major gains in terms of poverty reduction can also be won if donors coordinate their aid allocation across countries. But such a coordination of allocation would mean that countries would have to abandon some partner countries with which they would like to maintain links, which makes it hard to find political support in the major donors for such a move.

The two closely related dimensions of reform are *ownership* and *alignment*. Donor coordination and more general forms of aid should make alignment easier and lead to increased ownership as well. There is at least a presumption that this could lead to faster economic growth and thus more rapid poverty reduction.

We furthermore may note that *accountability* and transparency are both required if donors are to be willing to shift to more general forms of aid, which would mean a higher degree of ownership. What is required is, first and foremost, that the budget process is transparent so that the flow of funds through the government can be followed. It is clear that this is important for the effective functioning of government, but there is little evidence as to how donor coordination affects this. This would depend on how donor coordination affects the incentives on the recipient side.

Most of these conclusions are rather uncontroversial, but there has been little movement of donor choices in this direction. Why? To answer this question, we need to think about how the issue of coordination looks from the perspective of donors (see the analysis in Bigsten et al. 2011). Aid coordination efforts may reduce donor transaction costs and increase the possibilities of achieving donor objectives in recipient countries (e.g., poverty reduction), but it will also have political costs in so far as the donor loses some political control of aid transfers. So donors need to weigh the importance of political influence against poverty reduction effectiveness. Larger countries put greater weight on their political influence than smaller ones, partly because they pursue international strategies but also because they have the required clout to be able to assert their influence.

One must ask why the actual allocation is far from the 'optimal' allocation. Obviously donors have other aims apart from maximized alleviation of global poverty. They want to be present in a broader range of countries for economic and political reasons, which means that there are political constraints on the reallocation our analysis suggests. So coordination can take different forms, but in the end, the extent of coordination will depend on the political goals of the participating countries.

Donor coordination can be done in various ways. One option is that countries allocate aid resources to a common agency such as the EU or the international financial institutes (IFIs). Within the European context, one could, for example, let the European Commission (EC) manage more of European aid. How should the division of labour then be between the Commission and member countries? Either member countries could channel more of their aid through the EC, or they can accept tighter coordination of their aid by the Commission. Even if a reduction in transaction costs would be easier within one structure, it would be a radical change politically to channel all aid through the Commission. So what can be achieved in the short term is probably a strengthening of the processes of joint programming and policy coordination.

What can we say about the other dimensions of the Paris Agenda which we have touched upon? The untying of aid does not really require coordination. It is just a matter of doing it. But peer pressure, through the Commission, OECD/DAC or otherwise, could help the process.

Increased predictability is much harder to organize in a decentralized fashion, since all countries have their own political and budgetary processes. This would be more easily handled if aid were channelled through one multilateral, since there would then only be one process to stabilize. This also increases the policy influence of that agency, which might be good (or bad).

Are donors willing and able to improve the stability of aid flows? One must keep in mind that aid is the result of domestic political processes in the donor countries. Thus the first constraint relates to the politics of aid decisions. But there may also be unexpected revelations of bad governance or corruption in the partner countries, which means that the donor may want to cut aid or change its character. This might mean that they are reluctant to enter into non-changeable long-term contracts. To make it possible to use long-term contracts that make aid more predictable, one probably needs to have conditionalities specifying what should be done in case of misappropriations or breach of agreement.

Aid policymaking in donor countries is an area in which the electorate does not feel the impacts of policy directly, and the reporting of results to the electorate is generally weak. Therefore, aid policy is not fundamentally important in the policy agendas of most parties and does generally not decide political success. Thus the risk exists that policymakers choose aid policies without sufficient concern for their long-term development impact.

One popular idea is that one must have ‘corruption free aid’, but this is not without problems. If only projects are pursued, where there is no risk of corruption, it may well be that only the projects which are unrelated or insulated from to the local context are chosen. This is certainly not what the Paris Agenda argues for and it may mean that aid effects are not sustainable. The harder the donor pushes for this, the less likely it is that the Paris Agenda will be actively pursued.

It is clearly the case that donors should be willing to take some risk in the aid processes and possibly to coordinate their activities to manage these risks. It is not desirable for donors to hold back on the implementation of PA reforms because they are more risky, if one is convinced that they lead to better outcomes for the recipients in the long run. It should be possible to admit that intervention has failed, but according to the current perception, one risks undermining aid support if one admits failure. There is a need for a more serious management of risks, and it should involve recipient governments as well.

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Appendix

A1

We assume that the administrative cost of multilateral ODA is relatively small and can be ignored here. Further we assume that the administrative cost of CPA is twice as high as the administrative cost of bilateral ODA that is not included in CPA. In 2009 the size of CPA was US$65,326 million and the size of bilateral ODA (not CPA nor administrative cost): was US$39,043 million. (The numbers are from Table 2.)

Now we can calculate the proportion of the administrative cost that is related to CPA. Let x be the administrative cost percentage for CPA. Then the admin cost for rest bilateral ODA (bilateral ODA not CPA and not admin cost) is 0.5x. Total administrative cost = 65 326 x + 39 043 * 0.5x = 84 848x. We now can conclude that the proportion of the admin cost that is related to CPA is 65 326 x / 84 848 x = 77.0 per cent. (Note that x cancels out.)

A2

OECD (2011: Table B9) reports PBA as share of CPA by donor. We use these shares to construct a weighted average for the donors we study. CPA for 2009 as reported in the OECD/DAC database is used as weights. This way PBA/CPA is found to have been 39.0 per cent in 2009. The best case scenario would be that all aid was PBA. We use this as benchmark. We further know that the administrative cost for non-PBA aid is 299 per cent of the administrative cost for PBA aid (299 per cent = 1/0.335). The figure 33.5 per cent is from Sida (2011). This tells us that the administrative costs in 2009 were (0.39*100 per cent + 0.61*299 per cent =) 221.39 per cent of benchmark. If the target in Indicator 9 which states that 66 per cent of aid flows should be PBA was reached, the administrative costs would be (0.66*100 per cent + 0.34*299 per cent =) 167.66 per cent of benchmark. We now can conclude that the proportion of the administrative costs related to CPA that would be saved is 53.73 per cent of benchmark / 221.39 per cent of benchmark = 24.3 per cent. (Note that ‘benchmark’ cancels out).

Appendix Tables

Appendix Table A1
Countries not included in the analysis (due to lack of data on GDP/cap)

Country	Actual aid 2009, million US$
Palestinian Administered Areas	2204.6
Mayotte	549.11
Myanmar	180.18
Somalia	175.61
Suriname	157.1
Territory of Wallis & Futuna Islands	118.28
Cuba	79.13
Montserrat	44.13
St Vincent & Grenadines	35.25
St Helena	30.89
Korea, Dem. Rep.	25.99
Nauru	23.27
Tuvalu	17.09
States ex-Yugoslavia	10.9
Tokelau	9.72
Niue	9
Cook Islands	8.36
Anguilla	1.62
Total	**3680.23**

Source: IDS online databases from OECD/DCD-DAC.

Appendix Table A2
CPA 2009, million US$

	Countries (incl. COMM)	Multilateral (excl. COMM)	All donors
Countries	61,772	25,866.06	**87,638.06**
Regional	7,606.31	1,832.58	9,438.89
Total	69,378.31	27,698.64	97,076.95

Source: IDS online databases fom OECD/DCD-DAC.