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doi:10.1016/j.worlddev.2011.07.028

Aid Quality and Donor Rankings

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Summary. — This paper offers new measures of aid quality covering 38 bilateral and multilateral donors, as well as new insights about the robustness and usefulness of such measures. The 2005 Paris Declaration on Aid Effectiveness and the follow-up 2008 Accra Agenda for Action have focused attention on common donor practices that reduce the development impact of aid. Using 18 underlying indicators that capture these practices—derived from the OECD-DAC’s Survey for Monitoring the Paris Declaration, the new AidData database, and the DAC aid tables—the authors construct an overall aid quality index and four coherently defined sub-indexes on aid selectivity, alignment, harmonization, and specialization. Compared with earlier indicators used in donor rankings, this indicator set is more comprehensive and representative of the range of donor practices addressed in the Paris Declaration, improving the validity, reliability, and robustness of rankings. One of the innovations is to increase the validity of the aid quality indicators by adjusting for recipient characteristics, donor aid volumes, and other factors. Despite these improvements in data and methodology, the authors caution against overinterpretation of overall indexes such as these. Alternative plausible assumptions regarding weights or the inclusion of additional indicators can still produce marked shifts in the ranking of some donors, so that small differences in overall rankings are not meaningful. Moreover, because the performance of some donors varies considerably across the four sub-indexes, these sub-indexes may be more useful than the overall index in identifying donors’ relative strengths and weaknesses.

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Key words — aid effectiveness, official development assistance, aid quality, aid selectivity, donor harmonization, donor proliferation

1. INTRODUCTION

How should aid quality be evaluated and compared across donors? A number of recent papers have proposed rankings of bilateral and multilateral donors, on the assumption that donor performance can be measured and ranked globally in a meaningful and robust way (Birdsall, Kharas, & Mahgoub, 2010; Center for Global Development, 2007; Easterly & Pfutze, 2008; Mosley, 1985; Roodman, 2006 and 2009; Sinha, 2010). These public rankings are intended to inspire both bilateral and multilateral donors to improve their effort, effectiveness, and efficiency in ways that will move them up in the rankings. And there is evidence that donors do in fact pay attention to these rankings and care about public perceptions (see, e.g., Ramankutty, Berglof, Easterly, & Pfutze, 2009). A sustained and focused “peer pressure” campaign within the DAC appears to have contributed to a marked decline in the share of aid that is tied to purchases of goods and services in donor countries (OECD, 2009a).¹

Whether this approach is successful or not is likely to depend on the perceived validity and robustness of the rankings. While the ranking of aid agencies on well-defined individual components is hard to argue with, this paper investigates the robustness of these overall rankings to inclusion of new indicators and to different weightings of the components.

In assessing aid quality by donors, this paper extends and enlarges upon the methodologies of Roodman (2006 and 2009) and Easterly and Pfutze (2008) in several respects. First, it includes a more comprehensive set of performance indicators, combining existing indicators with new ones that reflect

the content of the Paris Declaration in a more comprehensive and representative way. Second, as explored in the methodological sections below, most of our aid quality indicators adjust for important factors that are not directly under the control of the donor agencies. And third, in computing indicators of sectoral fragmentation and project proliferation, we take advantage of the new AidData database produced by researchers at the College of William and Mary and Brigham Young University (Tierney *et al.*, 2011).

The results from this exercise in collecting and combining aid quality indicators are both encouraging and instructive. First, we show that it is possible to group these indicators into logical and statistically valid sub-indexes that capture key aspects of aid quality: selectivity, alignment with country systems, harmonization in country, and specialization. Donor rankings within these sub-indexes should be useful in and of

* We are grateful to the World Bank’s Knowledge for Change Program (KCP) for funding the valuable research assistance from Afroza Chowdhury and Lodewijk Smets, to Ryan Powers for clarifying technical issues regarding AidData, and to Alex Gerbrandij, David Roodman, Mark Sundberg, Adam Wagstaff, and two anonymous referees for providing very helpful comments. This paper was originally prepared for the March 2010 Oxford Conference on “Aid Transparency and Donor Finance”. The findings, interpretations, and conclusions expressed in this article are entirely those of the authors. They do not necessarily represent the views of the World Bank and its affiliated organizations, or those of the Executive Directors of the World Bank or the governments they represent. Final revision accepted: May 6, 2011.

themselves, by helping donors to identify areas of relative strength and weakness.

Second, we offer a new overall ranking of donor quality, constructed from these sub-indexes. This ranking has the advantage of incorporating more aspects of quality than other rankings, so that it is likely to be a fairer representation of overall donor quality.

Third, we show that weightings do matter to the rankings: because donor rankings vary among the different sub-indexes, the ultimate overall ranking will be sensitive to the weightings of those sub-indexes. We argue that ranking exercises need to take into account this sensitivity to weightings and should make their weighting choices explicit, to allow the reader to decide whether he or she agrees with them. In the interest of transparency, we aggregate our sub-indexes several different ways and show how the rankings change with each reweighting.

2. RANKING DONORS: CHALLENGES, MOTIVATIONS, AND METHODS

Any effort to rank donors on aid quality faces a number of challenges, some of which we cannot address satisfactorily. First, most indicators of donor performance are based on plausible but largely untested beliefs about best practices in aid management. Policy selectivity has received the most attention in the literature (Burnside & Dollar, 2000; World Bank, 1998). Nevertheless, the evidence linking the quality of policies to the effectiveness of aid has been disputed (Easterly, Levine, & Roodman, 2003; Easterly, Levine, & Roodman, 2004; Hansen & Tarp, 2000; Hansen & Tarp, 2001). In the case of other aid quality indicators, such as donor use of country systems, there is an even stronger consensus in the donor community on their importance, despite an even weaker base of empirical evidence. In selecting plausible indicators of aid quality, we follow the approach of Easterly and Pfütze (2008) in selecting our indicators based on the consensus in the donor community and academic literature—which means that “we are asking in effect if aid agencies operate the way they themselves say they should operate” (Easterly & Pfüte, 2008, p. 32).

Second, we do not know whether the relationship between aid characteristics and better outcomes is monotonic over the relevant range. In making the assumption that it is, we follow the existing ranking efforts.

Third, some of the indicators included in the rankings ignore interactions among donors, which could be important. For example, if most donors “herded” toward the poorest countries, it would improve those donors’ poverty-selectivity ratings, but would not necessarily improve outcomes at the margin, if aid’s impact on growth diminishes at higher aid levels. In that case, the marginal donor might reduce poverty more by avoiding the stampede and instead allocating its aid to countries that are slightly less poor.

In this paper we largely set those three issues aside to focus on the following question: even if we assume that the donor behaviors captured by the indicators are important for development, does it follow that one can aggregate them into a single index of donor quality that is valid and reliable? Or are the component measures sufficiently uncorrelated that any overall ranking of donors on aid quality will be sensitive to subjective judgments regarding weighting or grouping into sub-indexes?

In ranking donors, it is important to match the methodology to the purpose. Donor-ranking exercises to date have been “name and shame” exercises: their goal has been to motivate

lagging donor agencies to improve the quantity and quality of the aid they deliver by benchmarking donors against each other. Both Roodman/CGD and the Easterly and Pfüte ranking exercises have made this aim explicit: they write of hoping to cause aid agencies to become more transparent (Easterly & Pfüte, 2009) and of trying to inspire “a race to the top” (Center for Global Development, 2010), in which aid agencies change their practices to improve their rankings.

What does this “name and shame” goal imply for methodologies? To assess how well aid agencies are delivering on their mandate, we believe it is important to control econometrically for factors that are outside the agencies’ control. For example, it is pointless to castigate the EBRD for not focusing on the world’s poorest countries, given that the institution is allowed to operate only in the largely middle-income Europe and Central Asia region. By adjusting for limited mandates, we are able to ask the more relevant question for aid agency management: given its mandate, is the agency reducing poverty as effectively as possible, for example by targeting based on policy and poverty within its assigned geographic area? For other indicators, we adjust for donors’ total aid budgets; for example, larger donors will typically “proliferate” their aid across more countries and sectors, other things being equal, and should not be penalized for this. And in measuring use of country systems, we adjust for differences in risk among donors’ country portfolios, to avoid unduly penalizing donors that provide a large share of their aid to recipients that have weaker public financial management systems. All of these adjustments enter into our calculation of the core ranking below. (In one of our alternative rankings, the “allocation index”, we reverse some of the adjustments as appropriate for the different purpose: helping donor-country governments determine how best to allocate their marginal aid resources most effectively.)

3. DATA AND METHODOLOGY: CONSTRUCTING THE SUB-INDEXES

As discussed above, one of the main contributions of this paper is to base donor rankings on a more comprehensive set of indicators of aid quality than have been used in the past. This section describes how we have interpreted, adjusted, and aggregated these indicators.

In constructing our index, we identified four distinct dimensions of aid quality: selectivity, alignment, harmonization, and specialization. These emerge from the aid effectiveness literature and from international agreements on aid, but we find that they also hold up empirically. We assigned indicators to the four sub-indexes based on the OECD-DAC’s mappings (OECD, 2008) to a large degree, supplemented by theory and intuition, but we found in most cases that the intra- and inter-sub-index correlations confirmed those assignments. In Section 4, we discuss why these sub-indexes may be useful in their own right, and not just as building blocks for the overall index of aid quality.

(a) *Aid selectivity*

Aid is widely believed to have greater development impact where it is needed most—that is, where there are large numbers of poor people—and where the policy and institutional environment is favorable to growth and development. The intuition for this belief is difficult to dispute, even if the empirical results in Burnside and Dollar (2000) have not proven very robust. For this reason, both the CGD and Easterly and Pfüte rankings incorporate measures of policy and poverty selectivity in

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