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Politics, Evidence and the New Aid Agenda

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Based on study of (a) the HIPC debt relief initiative, (b) the linking of aid to policy conditionality and (c) transactions-cost arguments in favour of programme aid, this article argues that major elements in the new aid agenda may not be well-based empirically. This is partly because of inadequate knowledge, but particularly because the evidence often conflicts with political preferences. As a result, it is likely that large amounts of aid resources are being misdirected. Ways are suggested of narrowing the gap between evidence-based and 'political' decision-making. In the meantime, donors should avoid diverting more aid into debt relief, should roll back their reliance on policy conditionality, and should exercise pragmatic caution in the expansion of programme assistance.

1 Introduction

This article is about the role of evidence in the choice of aid modalities. It suggests that major elements in the new aid agenda may not be well-based empirically. Part of the problem is that the evidential base is not good enough. Perhaps to some extent this is so because of time-lags. The contemporary aid environment is rather fast-changing, whereas research and evaluation are retrospective and occasional, and reflect the aid choices of the past rather than the fascinations of today. However, a probably more important part of the problem is that evidence gets in the way of the preferences of politicians (and the publics which stand behind them) and of the incentive structures to which they are responding. Such tensions are familiar enough but, it is suggested, their potential seriousness has been magnified by the trend within the new aid agenda for aid modalities to become more 'macro'-based.

The pendulum of professional opinion about effective aid modalities has swung away from an earlier concentration on project-based assistance in favour of more programmatic forms, most notably sector-wide or direct budget support and the associated modality of debt relief. Thus, a recent British policy statement on the subject (DfID, 2000: 93):

> there needs to be a real improvement in the way that assistance is delivered. That means reducing support for stand-alone projects, and increasing support for sector-wide reforms. Where governments have a strong commitment to poverty reduction and strong policies in place, it means moving towards providing financial support directly to recipient government budgets using their own systems.

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Although some donors remain wedded to the project mode, there is little doubt about the trend in favour of programme support. The successive HIPC debt relief schemes of the 1990s added further major elements of programme aid, as has the opening within the World Bank of its Poverty Reduction Support Credit (PRSC) window, and the Bank's programmatic 'policy-related' credits are now running at record levels. The potential costs of making 'wrong' decisions about aid modalities are greater when transfers are concentrated in a relatively limited number of large transfers in support of country-wide programmes, as contrasted with the smaller absolute risks attached to 'wrong' project decisions, confined by the limited scale of most projects.

This article illustrates these issues by reference to three specific topics:

- *First*, we utilise a recent study by the World Bank's Operations Evaluation Department (OED) to argue that, in terms of aid effectiveness, there is a quite severe conflict between evidence-based considerations and the politically driven use of aid resources for the provision of *debt relief* under the HIPC scheme. In this case, the evidence is there, but the question is: who's listening?
- The *second* illustration also relates to an apparent – but this time more complex – failure of decision-makers to take an evidence-based approach, this time not only because of 'politics' but also because of institutional factors and research time-lags. This refers to interactions between work on *policy conditionality* and the practices of the Bretton Woods institutions (BWIs) and other donors.
- *Third*, we start from the frequently made assertion that programme aid is superior to the project-based alternative because it lowers *transactions costs*, to raise questions about the state of our knowledge about comparative costs, and about the loose way in which this concept is used in the rhetoric of debates about aid modalities.

2 The OED's HIPC evaluation: who's listening?

The OED has recently completed an evaluation of the HIPC debt initiative (OED, 2003). This examines issues of design, implementation and (in a necessarily preliminary way) effectiveness. While it does not overtly spell out the implications of its findings for the likely developmental effectiveness of the assistance in question, the implications are barely below the surface and are negative. It can be inferred from the report that the HIPC scheme, while there are important items to put on the credit side of the ledger, has been bad news for aid effectiveness, for reasons summarised below, although we take the argument further than the OED report chooses to do.

2.1 Failure of the additionality principle

The OED report valuably draws attention to the central importance, when assessing the effects of the Enhanced Heavily Indebted Poor Country debt initiative (hereafter E-HIPC), of the notion of *additionality,* i.e. the extent to which resources provided by creditors to finance the E-HIPC scheme are additional to normal and previously planned flows of development assistance. The creditors formally agreed the principle that this money should be additional and, had it been observed, the result would have been a substantial net addition to the total volume of transfers to poor countries. However, the

OED report draws attention to the facts (a) that the E-HIPC scheme contained no specific provisions to ensure that additionality was observed and (b) that the early evidence does not suggest that it has been achieved in practice. Indeed, the introduction of the original HIPC scheme in 1995 coincided with a very sharp fall in total transfers to HIPC countries, to levels which have not since recovered.

Although additionality is an elusive concept, because of the difficulties of assessing the counter-factual, what can be said is that successive HIPC schemes have not prevented a decline in net financial transfers to debtor countries, because the financial cost of debt relief has apparently been deducted from intended aid transfers (see Gunter, 2001, for a similar finding), and that actual transfers to them have been well below projected levels. It would take a major creditor-by-creditor research effort to be able to estimate the true extent of additionality, but the presumption must be that, in the general case and over the longer term, a creditor-donor government will decide how much in total it wishes to provide as assistance and will then reduce its other aid expenditures to accommodate the budgetary cost of debt relief.

2.2 Inefficient redistribution of aid

Despite the stagnation of aid to the HIPC countries, there has nonetheless been a sharp redistribution of resources away from low-income countries which are not rated as eligible for HIPC relief. These 'non-HIPC' countries have had their aid cut particularly heavily. Comparing 2000 (latest available) with 1998 indicates the following changes in the respective shares of these two groups (% of total net resource transfers):

	1998	**2000**
HIPC	44	76
non-HIPC	56	24

Evidently, recipients of E-HIPC assistance are being treated in a privileged way, but is this consistent with aid effectiveness? The E-HIPC scheme has the reduction of poverty as one of its principal objectives, but eligibility for HIPC relief is not well correlated with the incidence of poverty. Outside Africa, China, India, Bangladesh, Pakistan and Indonesia are obvious examples of non-HIPC countries with much poverty. Within Africa, Nigeria stands out among the excluded, along with Eritrea, Namibia, South Africa, and Zimbabwe – all non-HIPC countries with large numbers living in absolute poverty. Ranis and Stewart (2001) estimated that, among low-income countries, actual and potential HIPC agreements covered only about a quarter of all people thought to be living in poverty. The distributional implications of an E-HIPC scheme without additionality are such as to raise questions about the consistency with a poverty-reduction objective of the resulting geographical pattern of resource transfers. There is a real sense in which the poor in countries outside the HIPC scheme are subsidising those who live in HIPC countries.

There are other reasons for questioning the desirability of this redistribution among recipient countries, given the failure of additionality. One flows from the erection of indebtedness as the prime criterion of eligibility for E-HIPC assistance. Hitherto, a well-established conclusion of the aid-effectiveness literature has been that aid should be allocated selectively on the basis of the quality (however defined) of prospective recipients' economic and social policies. Inserting indebtedness as an overriding criterion and giving E-HIPC debt relief a privileged status among aid modalities seriously impedes application of this selectivity. Although exogenous factors have been important too, the case studies conducted for the OED report showed that poor past fiscal policies and failures to adjust were important reasons for the emergence of unsustainable debt burdens. This confirmed earlier results by Brooks et al. (1998), and others before them, showing weak macro and adjustment policies, and lack of prudent debt management strategies, to be associated with debt difficulties among HIPCs. Indebtedness tends to be *inversely* correlated with the quality of past policies. Thus, the global redistribution of aid may be consistent neither with maximum poverty reduction nor with productive use of the assistance. It may also raise questions of moral hazard, punishing those with good records of economic management in order to rescue governments that have been less responsible or competent.

Such concerns have been compounded, as the OED report makes clear, by the processes which brought the 'enhanced' HIPC scheme into existence. As is well known, this was a political response by creditor governments under varying degrees of pressure from civil society organisations to be generous at the end of the last millennium, as a result of successful mobilisation by groups campaigning under the Jubilee 2000 banner. One consequence was that creditor governments not merely agreed to E-HIPC, introducing considerably more liberal terms than the original HIPC scheme, but also committed themselves to a target of getting at least 20 countries within the scheme (at 'Decision Point') by the end of 2000. This target was achieved (actually, 22 countries) but only as a result of what is now labelled 'the millennium rush', with 17 debtor countries being accepted as having reached their 'Decision Point' between July and December 2000. Inevitably, this could only be achieved by lowering required standards of policy performance. Thus, the OED report records for this group worse policy track records, weaker development programmes and poorer past records of using aid productively. Unsurprisingly, a substantial proportion of these 'rush' countries have subsequently failed to deliver on policy promises. The pace of new inclusions has since slowed considerably, but the report indicates that the most recent entrants into the scheme have particularly poor policy records. It appears that E-HIPC is turning out to be a mechanism for reallocating resources in favour of countries which, taken as a group (and with important exceptions), cannot be expected to make the best use of the scarce resources on offer.

2.3 Undesirable policy biases

One of the most striking aspects of the E-HIPC scheme, as the OED report points out, is its association, under pressure from NGOs, with a particular and narrow approach to the task of reducing poverty, namely, the expansion of spending on social services to the neglect of wider growth and developmental priorities. In fairness, this trend in the allocation of aid monies had already been well under way for some time, but the E-HIPC initiative took this bias to another level. The report points out that, for the 13 countries for which data were available, 65% of all resources released by E-HIPC debt relief were to be devoted to social services, with 7% on infrastructure, 4% on governance and just 1% on structural reforms. Among other things, this has been associated with a sharp rise in the share of total aid in these countries devoted to the social sectors *with an almost corresponding decline in the share of aid for production services.* Moreover, HIPC progress reports indicate that *over half* of government revenues will be earmarked for social spending in future years.

This concentration on social services raises the question, to what extent will it act on the causes of poverty? Inadequate access to education and health is certainly a powerful influence on poverty. But poverty has many other causes as well, notably the effects of past economic stagnation or decline, inadequate access of the poor to various forms of capital, large and growing inequalities, high demographic dependency rates, gender biases, and various forms of disempowerment and of state failure.[1] At least as it relates to Africa, poverty-inducing social structures and various government failures suggest themselves as the principal primary causal factors, but even if the reader disagrees with that judgement, it is harder to dispute the proposition that a multitude of factors contribute to poverty, only a few of which have much to do with any neglect of social spending induced by the necessity to service external debts. Not the least of the negative features of the E-HIPC linkage between debt relief and social service provision is that it risks diverting attention from more fundamental causes of poverty. It also pays little heed to what is universally agreed: that far more than money is needed in order to ensure that social spending will actually raise the standards of the poor, with the OED drawing attention to the pervasiveness of low efficiency, poor service quality, capacity shortfalls and low utilisation within poor countries' social services. In fact, cross-country evidence suggests that expenditure levels have little influence on educational outcomes, although comparable tests for health provide more mixed results.[2] There is also the problem of skewed access to these services. African evidence suggests that these services are overwhelmingly enjoyed by the relatively more affluent members of the population, with the poorest quintiles receiving much less than proportionate shares (Castro-Leal et al., 1999).

As already hinted, one consequence of the concentration on social spending is that it diverts attention away from the fundamental necessity to raise economic growth and remedy structural weaknesses. It is not sufficiently realised on what soft terms the HIPC countries have obtained capital in the past.[3] In 1999, for example, the average terms on which the HIPCs borrowed were at 3.5% interest, with an average maturity of over 20 years and a 43% grant element. Moreover, in the same year, they received grants equal to more than half of their total borrowings, so that the true 'average terms' were actually much softer than those just cited. The equivalent figures for sub-Saharan African countries were even more favourable. The obvious question to ask is, how could countries receiving capital on these terms possibly run into debt-servicing problems? There is no simple answer to that question and the explanation will doubtless vary from country to country. But in the general case it is likely to be found in a combination of exogenous shocks; poor past macroeconomic management worsening the already large problem of capital flight; weak domestic saving, fiscal and export performances; and low returns to past investments. In turn, low returns can be seen as reflecting often low-quality public investment decisions; deteriorating terms of trade, obstacles to market

1. For a survey of the causes of poverty in Africa see White and Killick et al. (2001: Part II).
2. The evidence is briefly surveyed in ODI (2003).
3. For an elaboration of the following argument see Killick (2002b). I am at this point going beyond the coverage of the OED report. See also Bird and Milne (2003). The source of the following debt statistics is World Bank (2001b: 260-61).

access and inflexible export structures; past and continuing policy failings, as already mentioned; and low enforceability of property rights.

Excessive indebtedness can exacerbate these disincentives, through what is known as the 'overhang' effect. In principle, the negative force of the policy biases could be mitigated if the E-HIPC scheme were to reduce the overhang problem, in which case investment and growth could be boosted. There is little controversy that in the circumstances of middle-income debtor countries, such as the Latin American debtors which dominated the debt crisis of the 1980s, the overhang could and did have such an effect. The applicability of this argument to the small, low-income economies which characterise most HIPCs and where there are so many other deterrents to investment, is less clear. The empirical evidence does not show a strong connection between debt stocks and investment levels, and the direction of causality is ambiguous. The OED report suggests that an overhang effect is speculative and has not been demonstrated convincingly.[4] It would be unwise to rely heavily on a strong positive overhang effect from E-HIPC relief.

Creditworthiness and debt sustainability, as the OED report makes clear, will best be achieved by measures which strengthen the domestic economy, and its underlying institutional bases, and which address the above causal factors. Debt difficulties are better seen as a symptom of economic weaknesses than as a cause of them. The current donor preoccupation with social spending diverts attention away from this priority and thus carries the risk that the resources devoted to debt relief will not be effectively deployed, meaning that the goal of debt sustainability may prove unattainable. Of course, the Bretton Woods institutions would deny this, asserting that Poverty Reduction Strategy Papers (PRSPs) should tackle all these weaknesses as part of the anti-poverty effort. But not everything can be done at the same time; attention bias is real. Much stress is now put on raising the quantity and quality of social service provisions and this is liable to further increase total consumption relative to saving, even though saving and investment are already too low.

2.4 Multiple and conflicting objectives

The OED report points out that the E-HIPC scheme has been burdened with multiple and potentially conflicting objectives, namely, (i) debt sustainability, (ii) the acceleration of long-term growth and (iii) the reduction of poverty. Were enough resources to be made available, and in grant form, it might be possible to reconcile these (although the theory of policy suggests that pursuing three objectives with one instrument is unlikely to be an efficient way of proceeding). But the failure of additionality means that this condition is not satisfied. Even if it were, there are also problems of design and attention bias, as already shown.

One further distortion that has been introduced in response to the tensions between these objectives and the inadequate size of the resource envelope is a strong tendency to base the debt sustainability analyses which underpin the E-HIPC packages on

4. For a recent examination of the debt-growth connection, see Pattillo et al. (2002). For a large sample of developing countries, this finds that high levels of debt are associated with lower economic growth, operating through lower factor productivities rather than through investment effects. However, they do not investigate HIPC, or low-income, countries as a sub-sample and are notably cautious in interpreting their results for that group.

unrealistically optimistic export projections. For the 24 HIPC countries analysed by the OED, the projected export growth rate was more than twice the historical average for 1990-2000, almost six times the average for 1980-2000, and almost twice as fast as the growth actually achieved in 2000-01. Not surprisingly, staffs of the Bretton Woods institutions have not been transparent about how these and other key macroeconomic forecasts were derived. No doubt they did so with their eyes open, as a politically necessary way of reconciling E-HIPC's ambitious goals with the limited resources available to support them, but the point hardly needs to be spelled out that effectiveness is bound to be a casualty if an aid scheme is based on systematically unrealistic assumptions.

2.5 Conclusion

The OED evaluation has thus drawn attention to some serious problems with current debt relief arrangements. Especially if non-additionality continues to dominate, the consistency of the E-HIPC scheme with aid effectiveness is seriously in question. In qualification, it should be acknowledged that there are some compensating gains to put on the other side of the ledger. As Birdsall and Williamson (2002) have argued, aid in the form of debt relief reduces the enormous burden of never-ending debt renegotiations on the usually small number of individuals who can deal with such matters in the public administrations of low-income countries, thus releasing them for more productive policy analysis. In effect, E-HIPC substitutes untied programme aid for tied donor projects, and this too should have beneficial effects on both transactions costs and local ownership (but see Section 4). As the OED report states, E-HIPC also embodies best practice in strengthening institutions and incentives for aid co-ordination, in seeking in the design of PRSP processes to strengthen local ownership, and in its greater concern for the social content of agreed policy programmes. Moreover, the PRSPs, around which E-HIPC relief is mobilised, have pushed poverty up recipient governments' policy agendas and also, through their emphasis on participatory approaches, have the potential to involve citizens and civil society much more in policy formation, monitoring and execution. These are genuine gains, although it is universally acknowledged by those involved that the E-HIPC linkage has seriously degraded quality by inducing governments to rush PRSP processes in order to secure the irrevocable relief that is granted on reaching Completion Point.

So there are important positives as well as negatives, and it is not the intention here to deny that. Nevertheless, the last few pages have surely been enough to demonstrate a real danger that E-HIPC is resulting in a misdirection of aid resources. At the very least, in the face of the failure of additionality, the desirability of increased debt relief should not be taken as axiomatic. Well-targeted transfers delivered as regular aid by cost-effective means would be preferable to a further absorption of these scarce resources by means of yet more liberal debt relief. The OED report does not argue this, but one does not have to read too deeply between the lines to draw that conclusion.

Moreover, the OED is not alone in pointing in these directions. Easterly (2001) had already shown the negative association between indebtedness and the quality of past policies and pointed out the dangers, therefore, of using indebtedness as the criterion for the provision of support. Ranis and Stewart (2001) and Dagdeviren and Weeks (2001: 17) have all drawn attention to the poverty-reducing limitations of HIPC.

Bird and Milne (2003) have presented a carefully argued but sceptical review of the (in)efficiency of debt relief as an aid modality.

The question for present purposes is, who's listening and learning? This partly reflects an institutional gap. With evaluations of projects and other institution-specific interventions, there are, in principle at least, established channels for lesson-learning and reasons for believing that examining the past may improve the future. This is less obviously the case with a topic like debt relief, which is 'super-macro' in orientation. Responsibility for it straddles both the Bank and the Fund, and a large number of creditor-donor governments. Despite active dissemination, therefore, it is not clear that the OED report will carry much weight, or even reach those who are influential in these matters. The Bank's own defensive, stone-walling 'Management Response' to this report is not encouraging (OED, 2003: Annex K).

More fundamentally, however, the fact that E-HIPC is highly political in its motivation lessens the prospects that evidence of the type summarised above will govern future decisions. Imagine the furore among campaigning civil society organisations in many creditor countries if their governments were seen to be rowing back from debt relief, or even loosening the link between such relief and social spending. And just think of the outrage that the Bretton Woods institutions would provoke if they too were seen as weakening their commitment. In this area, politics and institutional interests appear to stand in rather stark opposition to the most effective use of available aid resources.

3 Conditionality: another knowledge-practice gap?

Another apparent area in which there appears to be a gulf between what the known facts tell us and the continuing policies of the aid community generally and the BWIs in particular relates to the use of conditionality as a means for achieving policy change in aid-recipient countries. On the one hand, much research – and quite a lot of World Bank (but not IMF) rhetoric – emphasises the limitations of conditionality as an instrument for change. On the other, it is arguable that, at least within low-income indebted countries, governments find themselves expected to conform to an even wider array of policy stipulations than in the apparent heyday of conditionality in the earlier 1990s.

However, the issues here are complex and the evidential basis less satisfactory. They are also important, because if misplaced reliance is placed on an instrument which actually fails to deliver the safeguards it appears to offer, this can lead to the mis-application of large amounts of public money. What is suggested below is that that may well have happened because alternative modes of operation would encounter institutional and political resistances.

3.1 Doubts about conditionality[5]

There was a veritable explosion in the use of policy conditionality during the 1980s and into the 1990s, as the World Bank became increasingly involved in structural adjustment lending, as the IMF extended the range of its own conditions from a

5. The following borrows quite heavily from my own work on conditionality (Killick, 1998), but see also Collier et al. (1997), Crawford (1997), Dollar and Svensson (2000) and Mosley et al. (1995).

previously fairly narrow macroeconomic focus to a much wider range of 'structural' matters, and as various other multilateral and bilateral donors increased their own use of this instrument. While there was from the beginning much controversy about the appropriateness of the design of the BWIs' conditionality, it tended to be common ground between them and their critics that these policy stipulations were implemented, whether for good or ill.

As the 1990s proceeded and evidence accumulated, however, a body of research grew up which cast doubt on conditionality's efficacy. It had long been well-known, for example, that a high proportion of IMF programmes broke down before the end of their (relatively brief) intended currency (Killick, 1995). Similarly, casual empiricism suggested that programmes of structural adjustment were not working well, at least in many low-income countries. This writer's own work and that of others listed in footnote 5 began to show the limited impact of BWI programmes and to raise questions which went to the heart of the use of conditionality as a way of achieving policy change. This was reinforced by the perceived failings of 'structural adjustment' in African and other low-income countries. Countries which had received large numbers of successive highly conditional credits were still rated by the BWIs as having weak, sometimes deteriorating, policies, with little apparent association between programmes and policy trends. Programmes were often poorly implemented, so that it was not surprising that they produced weak results, but non-compliance with the BWIs' policy stipulations appeared rarely to be punished in any effective or consistent way. When, as was often the case, a conflict of interest was perceived locally between domestic political imperatives and BWI stipulations, it was usually domestic politics that won out. Conditionality relating to governance issues was thus particularly prone to be ineffectual (Crawford, 1997, found that in only two out of 29 cases examined was donor pressure effective in inducing political change).

The use of conditionality came to be seen as in conflict with a growing consensus about the importance for effective action of local 'ownership' of chosen reforms, and as undermining the credibility, and therefore effectiveness, of the measures that were undertaken. Governments had learned that probably no more than temporary inconvenience would be visited upon them as a result of failures to implement 'agreed' conditions (amply justified, in the case of the IMF, by research showing little association between past compliance and future credits – Bird, 2002; Dreher, 2003). The BWIs (and other donors) had strong institutional imperatives to 'keep the money moving', not least a desire to protect the servicing of past credits, and these were often reinforced by staff incentives within these institutions. By providing the appearance but not the reality of safeguarding against poor policy performance, over-reliance on conditionality was blamed for resulting in major misallocations and waste of public monies (Killick, 1998: 168). Far better, the critics argued, would be greater insistence on local ownership and more selectivity in the choice of governments to be supported.

How did the BWIs stand in relation to the emergence of this critique? The IMF, by and large, has remained in denial (although we shall see shortly that it too is beginning to show signs of acknowledging the problem), but the Bank and members of its staff contributed quite strongly to the negative evidence. In the words of one Bank report (1995: 1), 'adjustment lending has mostly promoted good policies, but got weak program results'. An important Bank study of Africa concluded flatly that 'Conditionality as an instrument to promote reform has been a failure' (Devarajan et al., 2001). Another Bank report (1998) concluded that conditionality had been ineffectual where reform lacked political support, and had been counter-productive in some cases. More examples could be cited, but the point is that the Bank appeared to acknowledge as valid the critique of conditionality and to share it.

3.2 Institutional responses

It is reasonable, then, to expect a fairly strong movement away from reliance on conditionality. For the most part, this has not occurred. Some other donors, notably the United Kingdom and the European Union, have been trying to diminish such reliance, moving instead to greater selectivity and to relationships with recipient governments based far more on dialogue, ownership and partnership. There are voices within the World Bank urging movement in the same direction, particularly in connection with its new Poverty Reduction Support Credit (PRSC) facility. It is also the case that, following a sharp rise in the number of conditions per Bank programme during the later 1980s, there was then a decline in the average number of conditions in the latter half of the 1990s (World Bank, 2001a: 80), although it is unclear what was driving this. By 1998-2000 the average stood at 36, down from a peak in 1988-92 of 58. However, the biggest reductions occurred in what the Bank calls 'non-binding' conditions (from 23 to 8), with a smaller proportionate reduction in the more serious 'legally-binding' conditions (35 to 28). In any case, the 1998-2000 average was still well above the numbers prevailing in the earlier 1980s, and even in the later period Bank staff regarded only 37% of all conditions as 'very relevant' to the attainment of loan objectives. There is, in short, ample scope for streamlining action by the Bank, comparable with what is occurring in the Fund (see below), but this does not appear to be happening. Moreover, the share of adjustment lending has grown to new record levels – 64% in 2002 – and with it the importance of conditionality (Thomas, 2002: 2). There is thus a large apparent disconnection between the Bank's own evidence on conditionality and its continuing heavy reliance upon it.

What of the Fund? Perhaps, instead of publicly expressing its anguish, it is just quietly getting on with transforming the way it does business. Things are indeed happening, in the form of a substantial 'streamlining' exercise. Introduced in 2000, this aims to reduce the number of 'structural' conditions in its programmes (which had escalated from an average of 2 per programme in 1987, to 4 in 1994 and 14 in 1997-9 – Goldstein, 2000: 82) and to focus these more on actions regarded as critical to programme success and within the Fund's own core areas of expertise. Moreover, early evidence suggests that this exercise has resulted in an appreciable decline in the average number of structural conditions, although with the extent of this varying greatly from country to country (Adam and Bevan, 2001; Killick, 2002a, Eurodad, 2003).

However, it remains unclear to what extent the streamlining exercise should be seen as a response to the weaknesses of conditionality. On one view, it is a rather narrowly conceived *efficiency* measure, as reflected in the Fund's *Annual Report* for 2001 (IMF, 2001c: 45): 'the main goal of streamlining was to make conditionality more efficient, effective and focussed ...' Others hold that streamlining should be viewed more broadly and as concerned with enhancing local ownership. Streamlining seeks to reverse the proliferation of structural conditions, calls for greater clarity in programme documents about what constitutes Fund conditionality, and seeks to ensure that, in countries where both agencies are operating, there will be a clear division of responsibility on policy matters between the Fund and the Bank. The exercise is confined exclusively to what the Fund classifies as 'structural' conditionality, with no comparable change in its traditional macroeconomic stipulations. Streamlining, in other words, is a fairly limited exercise and once we lift our eyes from the purely quantitative aspect of conditionality, it is by no means clear that it marks any real move away from reliance on conditionality *per se.*

A relatively new element in the situation, with potential for reduced reliance on conditionality, is the initiation of Poverty Reduction Strategy Papers (PRSPs) as a focus around which the BWIs and bilateral donors can harmonise their assistance (and also their debt relief under the E-HIPC scheme). In principle, PRSPs can be viewed as an attempt to get away from old ways of doing business and to substitute these by broad-based, locally owned strategies, in which policy commitments are self-defined by the responsible governments, subject only to 'endorsement' by the BWI Boards.

There is real potential here, but it is by no means clear that the move into PRSPs has actually marked a retreat from BWI-defined policy conditions. HIPC governments now have to concern themselves with further conditionality arising from the World Bank's Country Assistance Strategy papers, as well as that specific to the HIPC Completion-Point arrangements,[6] to say nothing of the stipulations of other multilateral and bilateral donors. Countries which aspire to membership of the EU also have the conditionality of that institution to worry about. HIPC conditionality alone is potentially both onerous and wide-ranging, with its content recently summarised as normally centred around macroeconomic issues, structural reforms, social sectors and 'other poverty reduction requirements', especially governance and budget management issues (SPA, 2001: 9). Not much is left out there! There are also reports of bilateral donors picking up structural conditions being dropped by the Fund as a result of streamlining (Debt Relief International, n.d., para 13) and of the Fund actually increasing its stipulations for actions in the governance area.

At least for HIPC countries, it seems that governments today are probably confronted by a wider range of policy stipulations than they were two or three years ago. Freedom of action should also be judged according to the importance of the various areas of policy action. Since IMF streamlining is about ensuring that conditionality is focused on the most critical policy areas, and with both BWIs tending to cut back most heavily in the grey area of second-order benchmark, or non-binding, conditionality, here too governments may well be in a more constrained situation, rather than an improved one. It may well prove that the E-HIPC/PRSP arrangements have provided a vehicle for further increasing conditionality, despite all the rhetoric of ownership. Here too, an institutional gap is revealed, for no one agency is responsible for maintaining an overview of the aggregation of conditions being required of a government from BWI and other sources, not to mention the internal consistency of these. Nor, indeed, are the data generated which would readily permit such an overview.

Two other considerations rather reinforce this view. One is the prospect that the more important structural conditions dropped as a result of Fund streamlining will be

6. For example, at a Commonwealth Secretariat-IMF consultation in July 2001, the Tanzanian delegate reported that his government was confronted with no less than 13 specific HIPC Completion-Point conditions, over and above those of the BWIs.

taken up in Bank credits. According to a Fund staff report on initial experiences with streamlining (IMF, 2001d:17, 34), the Bank is 'strengthening' its conditionality in areas, such as privatisation, health system reform and public sector reform, from which the Fund is scaling back. In a number of cases, the report states, 'measures no longer covered by Fund conditionality were incorporated as conditions by the Bank, but in others this was not the case'. Eurodad (2003) is more categorical:

> World Bank involvement in the areas where the IMF pulls out is seen as a prerequisite for streamlining and the findings of this paper suggest that indeed the World Bank is taking over conditions left by the IMF in an aggressive manner.

A second consideration concerns the extent of cross-conditionality between the two BWIs. There has long been a *de facto* cross-conditionality from Fund to Bank adjustment programmes, but under the arrangements between the Bank and Fund concerning their PRSC and Poverty Reduction and Growth Facility programmes the degree of cross-conditionality has been increased at the level of broad performance, although the Boards of both institutions state that cross-conditionality should *not* be applied to policy specifics within either programme, with each institution 'separately accountable for its lending decisions ...' (IMF-World Bank, 2001: 26).

In summary, what the above reveals is a major disjuncture between a rather wide perception that conditionality is a flawed instrument and the continuing reliance on this instrument by the BWIs (as well as other donor agencies). One source of difficulty, as Thomas (2002) has recently argued, may be that a good deal of the evidence on which the critique of conditionality was based relates to the 1980s and early 1990s, since when the record may have improved and with it the utility of using conditionality.

3.3 Is compliance improving?

Both BWIs can point to some evidence of improvement. In the case of the Bank, OED reviews of development effectiveness report satisfactory or better outcome scores from adjustment lending operations, rising from around 60% in the 1980s to 86% in FY1999-2000 (97% when weighted by disbursements). As regards the Fund, a recent review of the performance of conditions in 24 operations found that only 10% were not implemented at all, while 65% were fully implemented (Nestmann and Weder, 2002).

But there are other indications pointing in the opposite direction. Results reported in recent IMF Working Papers suggest that programme failure remains a large and growing problem. Mussa and Savastino (1999: Table 2) rate as failing programmes where actual disbursements are less than half of the agreed amounts and show a rising proportion of programmes failing this test over the last two decades, after an earlier period of apparently improving outcomes (percentage of programmes less than 50% disbursed):

1983-87	29%
1988-92	33%
1993-97	46%

Ivanova et al. (2003: Table 1) similarly show that in 1992-8 only a quarter of ESAF/PRGF programmes were *not* subject to some interruption and that nearly half (45%) experienced irreversible interruptions.[7] Similarly, the first report of the recently created Independent Evaluation Office (IEO) of the IMF, on the 'prolonged use' of Fund resources, shows that both absolutely and proportionately prolonged use has been on a continuously, and rather steeply, rising trend since the late 1970s, continuing at least through to 2000 (IEO, 2002). This evidence is again consistent with the view that Fund conditionality is ineffectual, perhaps increasingly so.

Econometric analysis by Ivanova et al. (2003) re-confirms the dominance of domestic political-economy factors in determining Fund programme success found by independent researchers, and also that neither heightened 'effort' by Fund staff nor even increased resort to prior actions could substitute for favourable political-economy conditions and exerted no significant influence on the likelihood of programme implementation (see Thomas, 2003). Associated with this, a Fund paper on conditionality policy issues (IMF, 2001a: 55) asserted the position, apparently with approval, that the primary role of the BWIs 'is to identify reformers, not to create them' and that 'IFIs should have no illusions that their conditionality will appreciably affect the probability of reform'. Indeed, the Fund's own Executive Board is on record as stating that 'conditionality cannot compensate for a lack of programme ownership'. These influences have led to a Board paper on the strengthening of country ownership in Fund programmes (IMF, 2001b).

3.4 Conclusion

The conclusion which suggests itself here, then, is that the politics of Fund and Bank governance, as well as internal resistances, have led to a large apparent gap between what the balance of available evidence tells us about the efficacy of conditionality as a way of securing desired policies and the continuing policies and practices of these two institutions. A large part of the problem here is that any major attempt by BWI managements to move away from the use of conditionality – even if they wished to do so – would be strongly resisted by their respective Boards. This is particularly the case with the IMF, whose Board is manned by Ministers and officials from Treasuries and Central Banks of shareholder countries, but it is also the case with the Bank. It appears that many representatives of major shareholder countries simply remain unconvinced by, or unaware of, the evidence, or unpersuaded that any alternative would produce superior results.

It is worth repeating an implication of this: that if indeed conditionality often does not provide an assurance of improved recipient policies – the substitute for borrower collateral – then continuing to use it as if it did is a recipe for a waste of large amounts of scarce aid resources. This effect is compounded by the tendency for bilateral donors to piggy-back on the conditionality of the BWIs. Just think of all the 'structural adjustment' credits and grants that were provided during the 1980s and 1990s to

7. They also show an apparently more satisfactory 73% compliance with programme conditions, but this figure is hard to interpret because the authors regard it as biased upwards. For a useful very brief review of other evidence on programme effects, see IMF (2001a: 45-6). See also Bird (2002) for corroboration of declining IMF programme completion rates.

governments in Africa and elsewhere which had no serious commitment to policy reform. Lessons have been learned, of course, but we still seem to be stuck with one of the principal instruments which led to this waste.

To be fair, the evidential base on the more recent record with conditionality is too mixed and incomplete to permit a firm judgement on whether the weaknesses identified earlier have been reduced and whether further action is necessary. The point here, then, is that a major research and evaluation effort, which should at least straddle both BWIs, could bring the evidence up to date and could provide answers to some of the many questions that remain unresolved:

- Given new developments, such as the E-HIPC initiative, the increased use of PRSPs and the IMF's streamlining exercise, what is the overall trend in the totality of policy conditionality? Do governments today have greater effective room for manoeuvre in the determination of policies? What difference is IMF streamlining making?
- Have there been decisive changes in institutional and staff incentives which gave priority to new lending over the implementation of past programmes?
- Is there evidence of more effective sanctions against non-compliance (other than that which arises from shocks) and of the application of greater selectivity in the choice of governments supported? Has the HIPC initiative made any difference in this respect, by reducing pressures for defensive lending?
- To what extent have the negotiation styles and modalities of the BWIs changed in order to foster improved relationships and greater borrower ownership of the programmes supported?

In the meantime, we appear fated to continue the present unsatisfactory mismatch between what available evidence tells us and continuing reliance by BWIs and other donors on a modality of doubtful efficacy.

4 'Transactions costs' and the choice of aid modalities

Programme aid is claimed by its growing number of advocates to be superior on a number of grounds (stronger influence on the policy environment, superior ownership properties, greater overall coherence, etc.) but many of these boil down to the oft-heard claim that a given sum of programme aid gives rise to smaller transactions costs than an equivalent amount given in the form of traditional discrete development projects. Thus, a recent report on aid relations in Tanzania (IMG, 2003: 37):

> … we see programme aid as avoiding various of the drawbacks … of project aid, especially when it takes the form of a pooling of resources and co-ordination among donors. The presumption is that, with a much smaller number of reporting points, with no necessity for a multitude of Project Implementation Units, with donors accepting common reporting procedures and standards, with tied procurement virtually eliminated and with much less necessity for enforced project-linked technical assistance activities, transactions costs per dollar of aid received will be much smaller.

That is now the conventional wisdom and it remains a *reasonable hypothesis*. Many complaints are justifiably levelled against the project approach: that it undermines local capacity development, imposes heavy procurement and reporting requirements because of the large numbers of individual projects, and reduces the value of aid through the imposition of procurement tying. However, the superiority of programme aid in this respect remains only a hypothesis because it rests on a presumption of the comparative costs of the respective aid modalities, which has not, so far as is known, been empirically established in any systematic way. In fact, a literature search revealed only one study examining aid transactions costs, in Vietnam (Brown et al., 2000).[8] We suggest that the language of transactions costs has been used too loosely, as part of the rhetoric about the relative merits of alternative aid modes, and is not sufficiently evidence-based.

4.1 Conceptual issues

One reason for taking a careful look is that there are some conceptual issues that are generally disregarded. The text-book meaning of transactions costs is clear enough: 'the costs of negotiating, monitoring and consummating a contractual arrangement'. However, there is a lack of clarity in professional usage about what the chief categories are in the case of aid-delivery contracts. There are questions too about the *distribution* of such costs, as between donors and recipients, within the structures of each party, and over time. First, categories. The following is an attempted classification of types of transactions costs.

Administrative (recipient and donor):

- *ex ante* identification, appraisal and preparation of the aided activity;
- implementation, including any special procurement requirements;
- monitoring, administrative and financial reporting, including special arrangements to safeguard against maladministration and to secure aid effectiveness;
- *ex post* evaluation, including tracker, outcome and impact studies.

(To be included in each of the above items, and some of those that follow, are the opportunity costs resulting from absorption of scarce staff time within both donor and recipient agencies, although the presumption is that the burden of such costs is disproportionately high within recipient administrations. As a special case, there are the opportunity and other costs arising from 'staff capture' as a result of donor inducements to recipient civil servants to give priority to a particular aided activity, or to move across to that activity from regular duties.)

Tying (recipient):

- costs arising for recipients from loss of coherence and national ownership as a result of the tying of aid to large numbers of individual projects;

8. In addition, see Annex 3 of an OED report on aid co-ordination (1999) which contains a brief discussion of the costs of co-ordination.

- the higher costs of imports resulting from procurement tying (the World Bank (1998) has estimated that this typically reduces the value of aid by about a quarter);
- costs arising for recipients from losses of national ownership and sovereignty as a result of policy tying (conditionality), and perceived increases in political risks resulting from any associated governmental loss of policy freedom (but see Section 3 on conditionality).

Fiscal (recipient):

- erosion of fiscal discipline by extent of off-budget allocations (associated with project approaches) and the wider consequences of that;
- fiscal management problems generated by under-funding, requirements for counterpart funding and the recurrent costs of aided activities;
- planning problems created by the volatility and unpredictability of different classes of aid, and the macroeconomic consequences of that.[9]

We shall suggest shortly that programme aid is apt to generate more transactions costs than is commonly assumed, but what is already clear from this listing is that all aid modalities are likely to give rise to a number of these different cost types. However, they do not do so equally.

Before looking at the programme aid case, we should consider how different forms of delivery distribute transactions costs differently among the various parties. Take the case of a shift from project to macro-level programme aid (budget support). Within the donor agency in question, there will be a shift in administrative and professional work away from project specialists in favour of more macroeconomically oriented staff (which is one reason why project staff so often oppose the move to programme aid and why this can be a sensitive issue in the internal politics of donor agencies). Since a lot of donor project-related administrative costs are often shifted to specially contracted consultants, whereas this may be less readily done with programme aid, a shift in favour of programme aid is apt to increase the work burdens of aid agency staff as well as concentrating more of it in agencies' 'macro' departments.

Shifts will also occur within the recipient administration. In crude terms, more resources – and the associated transactions costs – flow through the budget from 'the centre', 'the Ministry of Finance and Development'. It is this ministry which will have to bear the main brunt of donors' reporting and evaluation requirements, so that its capacity to meet these becomes a critical variable. Even line ministries may also find themselves with additional burdens, because they are now having to account, through regular budgetary processes, for items which previously were off-budget and most likely being handled semi-autonomously by Project Implementation Units and the like.

Another consideration is the way comparative transactions costs may change over time. It is suggested, for example, that some of the transactions costs associated with programme aid are essentially start-up costs, which can be expected to diminish as experience is gained and systems are developed, and that while a shift to programme aid

9. Conceptually, this might be thought of as the opportunity cost of the extra volume of reserves it would be necessary to hold in order to smooth out unexpected variations in aid receipts.

may well eventually reduce aggregate transactions costs, the initial effect may be to raise them (Lawson et al., 2002).

A final complication concerns the fact that at least some of the costs described above are intended to produce benefits. This is most obviously the case with the various administrative measures intended to safeguard against mis-use of aid. Similarly, policy conditionality is intended to improve the policy environment and hence aid effectiveness. On the one hand, it obviously does not make sense to view the costs in abstraction from whatever benefits they might generate: one needs to think in terms of *net* costs or benefits. Against this, since we are not talking here of costs and benefits which can be reduced to a common quantifiable numeraire, a large element of judgement is involved in any attempt to net them out.

It is considerations like this which help to explain why researchers and evaluators have in the past shied away from the direct study of transactions costs. As the Brown et al. (2000) paper spells out, there are numerous other difficulties to overcome. Various of the costs listed earlier cannot be directly observed. Even some of those which can be observed – for example, some of the fiscal costs – are difficult to more than describe. The totality of aid transactions in aid-dependent economies involves large numbers of agencies and individuals, with the result that the information required to get a view of the extent of transactions costs will be fragmented and dispersed. There will also be a variety of perceptions. One man's cost is another's safeguard.

All this is daunting. Evidently, no more than indicative evidence would be possible from even the most thorough investigation. At the same time, the concept of transactions costs is being used to justify really large changes in the modalities of aid delivery, which suggests that it would be well worthwhile to strip away as much as possible of the conjecture which surrounds this topic. At present, our ignorance is such that a statement like 'programme (or project) aid is preferable because it reduces transactions costs' is not much better than saying 'I like programme (or project) aid'. In particular, the empirical study of transactions costs seems worthwhile because there are grounds for not taking for granted the alleged superiority of programme aid in this regard.

4.2 Costs of programme aid

First, we should note a major type of cost which is largely unique to programme aid: what is described above as policy-tying, or conditionality. As indicated there, conditionality, *assuming it achieves its intended purpose* (but see Section 3), can be thought of as generating costs because, by requiring governments to undertake policy measures they would not otherwise have chosen – or not at such a fast pace – they are apt to generate political risks and to reduce governments' ability to manage these risks. Note that the risks are borne almost entirely by the recipient, as distinct from the BWI (or other donor) in question. There is also likely to be a perceived loss of sovereignty and, therefore, of national ownership of policies. Many policy changes also generate adjustment costs of various kinds.

It may reasonably be objected that in contemporary best practice programme aid is seen as going along with a 'partnership' approach, which has precisely been designed as an alternative to extensive policy conditionality. However, whatever may be the case on the bilateral front, we have seen in Section 3 that the BWIs have thus far not introduced any substantial reduction in reliance on conditionality. Even among bilateral donors, it is clear that far from all of them have 'bought' the partnership approach as an alternative to conditionality (for example, see Lawson et al., 2002). Although there are some that are serious about moving in that direction, it is probably true to say that most continue to pin their faith on conditionality, especially on prior actions. Of course, it could also be objected that if, as suggested in Section 3, conditionality is often ineffective, most of the costs in question do not actually occur. This may well be the case, but it is scarcely evidence of the superiority of programme aid that one of the principal ways in which it is expected to be made effective does not actually work very well.

Conditionality – whether or not it is effective – necessitates monitoring and reporting, which introduces some of the administrative transactions costs listed earlier. This is illustrated by the special monitoring arrangements being established in connection with the E-HIPC initiative. Here the essence of the task is to ensure that extra monies released through debt relief are spent on the designated priority poverty-reducing budgets, but to do so is actually a complex task, involving significant costs, as well as begging a lot of questions about the fungibility of resources. Partly in response to the latter, some bilateral donors get into the, surely ill-conceived, business of trying to track what 'their' funds are spent on through the budget, imposing substantial transactions burdens both on themselves and on recipient administrations. As White and Dijkstra (2003: 476-7) put it:

> Donor attempts to trace their funds resulted in complicated systems which were anyhow likely to be an accounting fiction. These attempts also led to systems trying to micro-manage the recipient's foreign exchange allocation system which may have been inappropriate … Some agencies may have been forced to adopt such procedures for domestic political reasons, though a better response would be to educate decision-makers on how programme aid works.

More generally, the enhanced levels of 'dialoguing' and conditionality associated with programme aid generate substantial costs for all parties, but especially for recipient administrations. Especially where there is a combination of sectoral programme aid (SWAps) and direct budget support, the tendency for the development of rather elaborate mechanisms for dialoguing, monitoring, reporting and *ex post* evaluation is apt to impose substantial burdens. This is particularly so where there is a less than perfect convergence of government and donor objectives, and less than complete trust of the former by the latter.

A further aspect of programme aid is the special extent to which it relies on co-ordination and harmonisation in order to reduce transactions costs – and the well-known difficulties of achieving these in practice. This is sufficiently well understood to need no elaboration here. Since many of the costs of co-ordination and harmonisation fall on the local representatives of donor agencies, there may be a tendency to discount these as less onerous, although they are nonetheless real. However, effective co-ordination is most likely to be achieved where the government is actively involved and 'in the driving seat', in which case quite a lot of the costs in question fall upon it. Of course, in the (more general) case where co-ordination and harmonisation are not very effective, most of the costs of these failures fall upon the recipient country.

Even on a rather narrow view of transactions costs, as equated to staff time taken, the uncertain benefits of a shift to programme support are illustrated by the conclusions of a recent evaluation of Dutch programme support to the 'local governance' sector in Uganda (Netherlands Ministry of Foreign Affairs, 2003: 71):

> In sum, *for the Netherlands*, the decrease in costs (due to pooled funding, harmonisation of procedures and less time needed in direct programme management) is outweighed by the increased time use due to co-ordination, particularly on the sectoral level. On balance, there may have been hardly any time saving in overall aid management for Dutch assistance … not least during this initial period of establishing mechanisms of operational co-ordination.
>
> *For Uganda,* the increase in time, particularly due to own programme management … and increased co-ordination time, surpasses the time savings due to pooled funding and harmonisation of procedures. Overall, increased intensity of co-ordination has led to an increase of transaction costs for Ugandan partners …

A final reason why we should not take it as axiomatic that programme aid is superior in transactions costs terms concerns the problems it creates for fiscal management. Part of the problem here is that budget support tends to be geared to the fiscal cycles of the various donors rather than of the recipient, and gives rise to patterns of commitments and disbursements which do not fit with recipients' cycles of budget preparation and execution. Thus, a 'Needs Assessment Survey' recently conducted by OECD-DAC (2003: 103) in 11 aid-recipient countries found that 'donor-driven priorities and systems' was substantially the most frequently mentioned as the most burdensome aspect of dealing with donors.

Even more serious, programme aid appears to be especially unpredictable. Part of the difficulty here, as is now acknowledged by practitioners in the field, is that programme aid is more vulnerable to ministerial 'interference'. If a donor is providing relatively large amounts of aid in support of the general programmes of a recipient government and that government does something regarded as undesirable – perhaps undermining the independence of the judiciary, or buying a Presidential jet – then many Ministers of Development Co-operation will be unable to resist the temptation to suspend their programme support, *whether or not the offending behaviour was covered by the Memorandum of Understanding agreed in connection with the aid.* Here again, we have a tension between political incentives (with ministers responding to pressure from the media and/or NGOs) and what donor agencies are seeking to achieve through the new aid agenda, which includes more predictable aid, flowing through the recipient's budget and facilitating an improved standard of public expenditure management by the recipient administration.

The large resulting uncertainties are well demonstrated in a research paper by IMF staff members (Bulir and Hamann, 2001) which investigates the volatility and predictability of aid in general and of programme versus project aid. Among their remarkable results are the following:

- aid is more volatile than domestic fiscal revenues and tends to be pro-cyclical;

- fiscal planners are highly uncertain of aid receipts and 'the information content of commitments made by donors is either very small or statistically insignificant';
- there are much larger prediction errors in programme aid than with project assistance and a stronger tendency to over-estimation. This is partly because of the application of conditionality but there are other reasons too.

(The paper just cited, incidentally, is an excellent example of how at least some aspects of transactions costs are amenable to rigorous empirical testing.)

The hypothesis that transactions costs are proportionately lower with programme aid is thus not one whose validity should be taken for granted. Indeed, one study of aid to the health sector has suggested that the truth may lie the other way round (Foster et al., 2000), a judgement with which Lawson et al. (2002) concur, at least as it relates to the shorter term.

4.3 Conclusion

Table 1 is an impressionistic attempt to pull together various of the suggestions made in the text. The identified cost types are those suggested earlier and the suggested extent of costs in each entry should be read as relative to the investment cost of the aided activity in question. One obvious conclusion to emerge from the table is that the greater part of the burden falls upon recipients rather than donors, a factor which would be multiplied manifold if it was measured relative to the resources available respectively to donor and recipient administrations.

Concentrating on the recipient side of the table, it does seem to emerge that, on a narrow view of costs which concentrates on the administrative aspects, lower transactions costs are associated with programme aid. However, this is less clear on a broader view, and one of the limitations of the table is that it treats all types of cost as of equal significance, whereas the seriousness of loss of freedom for political management or of fiscal destabilisation is evidently on a different scale from, say, project evaluation costs. In any case, the entries under programme aid challenge any idea that this modality generates only small costs.

These comments are by no means intended as an attack on programme aid. For one thing, there are other reasons for preferring it over project approaches. But what we have tried to do is to suggest that the trend in aid shares away from projects in favour of programme aid may not be as strongly based on evidence as is commonly assumed and that, to some extent, the language of transactions costs has been used as a rhetorical weapon in debates about the effectiveness of alternative modalities. It is perhaps rather telling that, in the OECD-DAC Needs Assessment Survey mentioned earlier, switching to budget support was not a frequently mentioned suggestion for lowering transactions costs, coming only ninth out of a list of 13 ways of improving donor practices (OECD-DAC, 2003: 117). Recipients, it seems, are far from seeing programme aid as a panacea.

There is, therefore, a strong case for a serious evaluative study of the whole transactions costs question. Because it would have to be a major effort, such a study would probably lie outside the capabilities and budgets of the evaluation departments of bilateral donors, which leaves the World Bank's Operations Evaluation Department as the best equipped, perhaps heading a consortium of donor evaluators.

Table 1: Hypotheses about comparative transactions costs of programme and project aid

Transaction costs	Recipient		Donor	
	Programme	**Project**	**Programme**	**Project**
Administrative costs				
Pre-investment appraisal	Moderate	Moderate	Moderate	Very large
Implementation	Low	Potentially large	Low	Moderate
Monitoring and reporting	Large	Very large	Large	Moderate
Ex-post evaluation	Low	Moderate	Large	Moderate
Tying costs				
Loss of coherence and ownership	Nil (?)	Large		
Price premium	Nil	Large ('25%')		
Political etc. costs of policy conditionality	Potentially large	Low		
Fiscal costs				
Counterpart fund and recurrent cost problems	Nil	Large		
Volatility/unpredictability, destablisation	Very large	Moderate/large	Moderate	Moderate
Erosion of budget by extra-budgetary aid	Nil	Large		

5 Conclusions

One of the characteristics of the new aid agenda is that it moves the spotlight of attention to the quality of recipients' sectoral and country-wide policies. One of the criteria for deciding whether a developing country is a candidate for a switch from project to programme aid is the extent of channels of 'dialogue' through which donors can have inputs into recipient decisions, if possible without weakening local ownership. In their contacts with governments, donor representatives are much concerned to urge that policy choices should be more evidence-based than has hitherto been the case.

What this article has shown, however, is that in major respects donors' own choices may not have been sufficiently evidence-based. In the three illustrations presented here, the conflict between political preferences and evidence-based considerations is most stark in the case of E-HIPC debt relief. It is quite stark too in the continued adherence of the BWIs and other donors to the extensive reliance on policy conditionality, although this judgement is qualified by an admission that some of the evidence here is rather out of date. The evidential base is worst, among our three illustrations, in the case of arguments about the superior merits of programme aid, where there appears a danger that neglect of evidence may have led to an over-exuberant espousal of the programme form.

Each of the aid modalities examined in this article is of large importance in the global aid scene. We have argued that the potential costs of making 'wrong' decisions in such important aspects of aid policy are larger when transfers are concentrated in a relatively limited number of large credits or grants in support of country-wide programmes, as contrasted with the smaller absolute risks attached to 'wrong' project decisions, confined by the limited scale of most projects. In all three of the topics covered by this article, large-scale actual or potential waste of resources is a real risk.

Of course, conflicts between 'rational actor' and 'political' models of decision-making are familiar enough in many areas of public policy. Moreover, it would be quite wrong to take the view, rational actor = superior, political = wrong-headed. Politicians as ministers do the best they can in the context of the goals they determine, the information they receive and the incentives they face. These incentives are much influenced by the perceptions of civil society and of public opinion, as informed and affected by the media. Without public support and political engagement there would be far fewer transfers from rich nations to poor. So the politics is important and there is little to be gained by wishing it would go away. The task, rather, is to find ways of raising ministers' willingness and ability to give more weight to what the evidence shows. Remaining within the context of the three topics covered by this article, some suggestions can be made:

Improving communication of available evidence, not just to politicians but to the media, to civil society and to the wider public. There is a whole army of evaluators within the aid industry, but they tend largely to talk to each other and, if they are lucky, to influential officials within their respective agencies. Rarely do they effectively reach a wider audience, or even seek to do so. Thus, despite quite an active programme of dissemination and potentially explosive results, the OED evaluation of the E-HIPC scheme reported above remains little known and appears fated to slip quickly into obscurity. Similarly with more academic research, much of it remains essentially oriented to the researchers' peers, with often little attempt to reach wider audiences.

Responding to institutional gaps. In different ways, each of our three topics has revealed architectural lacunae which have contributed to the problems under discussion. In the case of E-HIPC, one difficulty is that responsibility for decisions about debt relief straddles both BWIs and a large number of creditor-donor governments, so that there is no natural forum, for example, where the OED report could be considered at a suitably senior level by all major parties involved. Merely reporting to the Board of the World Bank, as is OED's remit, will not meet the need. Similarly with the conditionality issue, the subject is one which cuts across institutional boundaries. As was argued earlier, no one agency is responsible for maintaining an overview of all the conditions being required of a government from donor sources, not to mention the internal consistency of these. Not surprisingly, therefore, the data are not being generated which would readily permit such an overview. In the case of establishing the transactions costs of alternative aid modalities, the institutional issue is that it is not clear how such a major research effort might be organised, or by whom, although we suggest that the World Bank's OED might be the most appropriate lead agency here.

The point about these deficiencies, however, is that it is not hard to imagine that reasonable *ad hoc* solutions could be found in each case.

Strengthening the evidence. In two of the three subjects examined above the evidential base was found wanting. This was most obviously the case with transactions costs, where our ignorance is profound and where the plea was for a major programme of research to try to unpack as many aspects of these costs as possible, given the undoubted difficulties of researching this subject. The position is more straightforward as regards the topic of conditionality, where the key question is whether the, largely negative, results of research on the data of the 1980s and early 1990s would be validated by examination of the record of later years.

In the meantime, it would be reassuring if donor governments could avoid tying up more aid resources in further versions of the HIPC scheme, if more of an effort could be made to roll back reliance on the probably false security seemingly offered by policy conditionality, and if the more full-blooded adherents of programme aid could leaven their advocacy with more pragmatic caution.

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