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Conditionality in Development Aid Policy

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Conditionality in Development Aid Policy

Development aid conditionality, defined as tying forms of support to the implementation of reform programs dictated by the donors, has come under fire from critics who argue that, as an instrument of development cooperation, conditionality has not led to the desired results and it has only contributed to a limited degree to economic and social development and to improved governance in the recipient countries. There is now a consensus that successful reform policies cannot be imposed, rather it is necessary that recipients be willing to take responsibility for formulating reform programs and to be equally responsible for implementing them with the financial and technical support of donors. Under the motto "Ownership, not Donorship," recipients—now called "partners"—are expected to control their own development.

This new paradigm represents a great challenge for both sides. The recipients are supposed to take responsibility for their development, but they don't really have the freedom to choose, and both sides know that. For the donors, the call towards partnership implies having to relinquish control, which, in view of their fiduciary responsibility, they cannot afford to do. After all, the precepts of administrative efficiency, transparency, and accountability are central elements of good governance in the donor countries as well. In addition, the question arises whether donors really wish to relinquish control, for it is clear that underdevelopment and its symptoms are not least the result of bad governance. And this is, of course, one of the things to which development aid tries to respond.

The continuing debate over redesigning conditionality signals an effort to translate contradictory demands and goals into consistent policy programs, which are above all efficient in aiding development. This study offers orientation in this debate by identifying the options for applying conditionality and reviews them in terms of their performance.

In doing so, I will introduce the discursive and instrumental innovations associated with the new paradigm, and I will explain those aspects that are typically masked over in the programmatic literature of donor agencies. The central dilemma of reformed conditionality is the indeterminate nature of the term "ownership," a concept that has become the key

to effective development policy. If a country wants to follow the imperative of efficiency without relinquishing control—something no donor really wants to do—then the concept needs to be narrowly defined and, consequently, the circle of recipients severely limited. This, however, contradicts the objective of reducing poverty worldwide, which development policy is committed to, and the related demand to increase official development assistance.

The alternative to a selective strategy with hard conditions is to take into consideration the long-term and contextual nature of reform processes and, using dialogue and technology transfer, to convince recipients to take ownership of the reforms. This implies a conditionality that is oriented towards processes and results and has a long-term focus. This also means forgoing immediate proof of effectiveness, which then makes it possible for "difficult" partners to be included.

The dilemmas and conflicting aims of both strategies are exemplified by the conditionality of the Millennium Challenge Account (MCA) and the development aid of the European Union (EU). It is clear that a selective strategy is not an option for the majority of donors, including Germany. First, it would require defining adequate general, yet at the same time tailor-made criteria for political and institutional framework conditions in developing countries that are conducive to economic growth. This is obviously beyond the donors' prognostic capabilities. Second, the donors would have to select recipients particularly worthy of support based on these criteria. And third, this decision would have to be consistently implemented, that is to say without the influence of special interests. A strategy of selectivity thus places demands on the coherence and convergence of the donors' interests and objectives that they cannot meet. But this strategy not only places high demands on the donors. The recipients need to make considerable adjustments in order to be considered "partners" and to be accepted in the club of the beneficiaries. Yet development policy committed to reducing poverty on a global scale cannot treat recipients differently without losing credibility.

In contrast, the example of the EU programs demonstrates that when conditionality is framed as development partnership, it is a powerful instrument of political influence. The technical language and the euphemistic style of development policy literature tends to hide the fact that it is definitely not the "partners" who determine the direction of reforms. Indeed, the new financial instruments intervene much more deeply in the internal structures of the recipient states than the conditionality of past decades. At the same time, the associated risks have been transferred to the recipient, from whom it is expected that they take ownership, and hence responsibility, for the reform programs. In view of the dilemma confronting development policy, namely that the effects of reforms are not predictable, the choice of the "right" measures is difficult, and the sources of errors are countless, the development policy community would be well advised to heed two simple, but crucial recommendations: to lower their expectations of their capacity to effect change, and to behave modestly towards the recipients.

Forms, Goals and Effects of Conditionality

The paradigm of modernization theory, to which the concept of development is ultimately tied, is based on the belief that economic and social progress in the countries of the Third World requires the modernization of social institutions. Consequently, development aid conditionality is used as a lever to push through reform programs that take the Western political and economic model as their role model and that are intended to lead the recipients to the path of "catch-up" development. Both the thrust and the modalities of conditionality have changed over time. Economic conditionality, which was dominant into the eighties, was supplemented in the nineties by conditions that sought to bring about political reforms in the countries affected. In both phases, development aid conditionality was based on a logic of incentive inspired by the model of *homo oeconomicus*: the prospect of receiving favorable loan terms and other forms of support should motivate recipients to implement certain policies defined by the donors. This form of conditionality is generally referred to as "ex-ante conditionality." Basically this is a form of bribery, whereby money is given in exchange for compliance with the desired policies.[1] Continuing criticism of the conditions, particularly those of the Bretton Woods institutions (i.e. the International Monetary Fund [IMF] and the World Bank), provided the impetus at the end of the nineties for a new conception of the relationship between donors and recipients of development aid and consequently also a reformulation of conditionality. The following section traces the development of this new "conditionality of partnership," which substantially informs the current discourse on development policy.

Economic Conditionality and Structural Adjustment Programs

Structural adjustment programs (SAP) were a political reaction to the economic and debt crises of the eighties that were created by the excessive granting of credit during the years of the oil boom. In order to bring economic stability to heavily indebted Third World countries, particularly in Latin America and in sub-Saharan Africa, and to re-establish their credit-worthiness, international financial institutions prescribed a bundle of macroeconomic measures that massively encroached on the political economies of developing countries. These measures, which were also subsumed under the term "Washington Consensus," referred to budget, fiscal, trade, and labor market policies and were based on neo-liberal models of development. The core elements included: budget discipline, liberalization of interest rates and the introduction of realistic exchange rates through the devaluation of national currencies, import liberalization and liberalization of foreign direct investment, tax reform and reductions in public expenditures, protection of property, dismantling state intervention in the market, economic privatization, and general deregulation of the economy. Corresponding measures became prerequisites for debt rescheduling measures and for the granting of structural adjustment credits from the IMF and the World Bank.[2] These credits were offered at exceptionally favorable conditions and were in many cases the most important source of capital for state budgets in the recipient countries. Regional development banks and bilateral donors also began to only provide credit to developing countries if they had concluded structural adjustment pacts with the International Financial Institutions (IFIs).[3]

At the same time, during the debt crisis changes occurred in the traditional division of labor between the IMF and the World Bank, which were originally established as complementary institutions. It was the IMF's responsibility to monitor currency and exchange

1 Paul Mosley, *Conditionality As Bargaining Process: Structural Adjustment Lending 1980–1986*, Essays in International Finance No. 168, (Princeton, October 1987), 6.

2 Ibid. On the "Washington Consensus," see John Williamson, "What Washington Means By Policy Reform," in John Williamson (ed.), *Latin American Adjustment: How Much Has Happened?*, (Washington, D.C.: Institute for International Economics, 1990), available at www.iie.com/publications/papers/paper.cfm?ResearchID=486 (accessed: May 4, 2006).

3 Peter P. Waller and Wolfgang Zehender, *Erfolgsfaktoren für Strukturanpassung in westafrikanischen Ländern*, (Berlin: Deutsches Institut für Entwicklungspolitik [DIE], 1989), 4.

rate stability and to provide temporary financial assistance to countries to help ease balance of payments adjustment. The World Bank, on the other hand, was charged with stimulating long-term economic growth through financing infrastructure and public sector projects in developing countries. After the outbreak of the debt crisis, however, this division of labor proved to be counterproductive. The IMF's prescription for stabilization in many cases led to economic recession, which hindered the development investments supported by the World Bank. As a result, during the period of structural adjustment the cooperation between the two financial institutions was stepped up and coordination was increased. For the borrowers, this created a problem of double conditionality: financing from either of the two institutions was only available if the conditions of both were fulfilled.[4]

In addition, the IMF and World Bank continuously increased the number of conditions needing to be fulfilled during the period of structural adjustment. For example, while there were an average of 34 conditions to be met for a World Bank structural adjustment program from 1980 to 1982, that number rose to 56 from 1987 to 1990.[5] On the one hand, this rise was in response to the increasing demand for loans from these programs and the expansion of loan provision. On the other hand, it was a response to pressure from World Bank creditors, who demanded security for their capital and therefore wanted to assert their varying policy perspectives.[6] The rise in conditions can also be interpreted as a reaction to the increasing criticism of the World Bank's structural adjustment programs and the resulting changes made to the allocations policy, from macroeconomic to sectoral adjustment loans. It is well known that the World Bank is a hybrid organization. As a multinational development agency, for whom the fight against poverty has had a prominent position in its agenda since the seventies, it cannot shut itself off from external criticism and the resulting demands made upon it. On the other hand, as a bank, it has no interest in withholding the monies it has at its disposal. Lending money is its *modus operandi*.[7] The greater the number of conditions that have been fulfilled, the easier it is for the Bank to justify to critics that funds still be disbursed, even if not all the conditions have been met. By increasing the number of conditions, the World Bank was able to respond to the demands of its critics without having to forgo disbursing funds.

The conditionality associated with structural adjustment programs largely came under fire because their implementation had severe social consequences, while the desired economic growth failed to materialize and it was naturally uncertain whether this would change in the future. Between 1972 and 1990 the number of Least Developed Countries (LDC) nearly doubled.[8] Even where the growth indicators were positive, social indicators had taken a turn for the worse in the course of structural adjustment. The call to clean up state budgets usually took place at the expense of cutting back on public services and government assistance programs, and the dismantling of subventions in many cases led to abrupt price increases. This especially hit vulnerable groups, who frequently articulated their anger in social unrest. Consequently, the conditions attached to structural adjustment programs were often unwillingly implemented or not stuck to, so that the disbursement of funds had to be postponed.[9] But structural adjustment programs not only encountered resistance in the recipient countries. The donors too could not close their eyes to the obvious: macroeconomic reforms alone were not sufficient to overcome the structural deficits in the national economies of developing countries. As a result, the political dimension of development policy intervention increasingly moved to the forefront.

Political Conditionality

The lack of success of structural adjustment programs put pressure on development agencies to justify their aid policies and unleashed an intense discussion among bilateral and multilateral donors about the policy of conditionality. It became increasingly clear

4 Rainer Tetzlaff, "Strukturanpassung—das kontroverse entwicklungspolitische Paradigma in den Nord-Süd-Beziehungen," in Dieter Nohlen and Franz Nuscheler (eds.), *Handbuch der Dritten Welt, Vol. 1: Grundprobleme, Theorien, Strategien*, (Bonn, 1993), 420–445 (432).
5 Axel Dreher, "A Public Choice Perspective of IMF and World Bank Lending and Conditionality," *Public Choice*, No. 119 (2004): 445–464 (445f).
6 Ibid., 449–452.

7 The fact that a majority of the capital is allocated in the form of grants is immaterial since these are largely financed by interest loans and loan repayments.
8 Tetzlaff, 439.
9 Ibid., 434f; Mosley, 9–12.

that social and political variables have a decisive influence on economic performance. Consequently, the willingness to undergo political reforms became a component of the donors' set of conditions.

The increased political focus on development aid since the beginning of the nineties is also related to the end of the bipolar international system in the wake of the dissolution of the Soviet Union and the increasing strength of democratic movements in Africa and Latin America. While development aid was also aimed at transferring Western political norms and values in earlier decades, foreign policy was driven primarily by the geo-strategic and national security interests of the super powers.[10] It was not until the end of the Cold War and following the disappointing results of structural adjustment, with its singular focus on economics, that the promotion of democracy and the rule of law and respect for human and civil rights became important components of development aid programs. This usually took the form of a more or less explicit incentive conditionality, which tied the amount of capital to be allocated to political reforms in the recipient countries. This also allowed for the provision of special financing for appropriate measures.[11] The Federal Republic of Germany introduced five new criteria in 1991, which serve as the basis for determining the amount, the nature and extent, and the instruments of cooperation with a partner country. These criteria, known as "determining factors" and which are still in force, are:

- Respect for human rights
- The rule of law and legal certainty
- Popular participation in the political process
- Creating a market-friendly, socially oriented economic system
- The development orientation of state action.[12]

The European Union for a long time had formally kept political aspects out of its regional development programs. But on 28 November 1991, the Council of Ministers of the European Community declared in a resolution on "Human Rights, Democracy and Development" that the promotion of democratic principles was a top priority in development cooperation.[13] And in the revised version of the Lomé Convention from 1995 they codified respect for human rights and democratic principles and the rule of law as "essential elements" of cooperation with African, Caribbean, and Pacific (ACP) states.[14] Because these elements are legally binding, breaching them can lead to a suspension of cooperation, which in fact has happened in many cases.[15]

The growing importance of the political dimension of development confronted the International Financial Institutions with a dilemma. In contrast to bilateral donors, who could tie development aid to political conditions, the mandate of the Bretton Woods institutions bars political conditionality as a matter of principle. The IMF and World Bank are required to make their decisions regarding allocations strictly on the basis of economic criteria. In fact, their statues expressly forbid the World Bank from making its actions dependent on political considerations.[16] The concept of "good governance" offered a way out of this dilemma. The concept was introduced in a World Bank report on the situation in Africa[17] and has since taken a prominent place in the discourse on development issues. It has been above all the World Bank that has systematically tried to operationalize the concept of good governance. Basically, the idea refers to the manner in which power is exercised in the manage-

10 Olav Stokke, "Aid and Political Conditionality: Core Issues and State of the Art," in Olav Stokke (ed.), *Aid and Political Conditionality*, (London, 1995), 1–87 (9f).

11 Ibid., 22f, and the contributions in: Peter Burnell (ed.), *Democracy Assistance. International Co-operation for Democratization*, (London, 2000).

12 Federal Ministry for Economic Cooperation and Development [Bundesministerium für wirtschaftliche Zusammenarbeit und Entwicklung (BMZ)], *Hohe Ansprüche an alle Beteiligten – die Bestimmungsfaktoren*, available at: www.bmz.de/de/ziele/regeln/bestimmungsfaktoren/index.html. English site available at: http://www.bmz.de/en/principles/rules/determiningFactors/index.html (accessed: May 4, 2006). Whether or to what extent a partner country meets these requirements is determined on the basis of a detailed catalog of indicators.

13 *Resolution of the Council and of the Member States Meeting* in the *Council on Human Rights, Democracy and Development*, November 28, 1991, Doc. No. 10107/91, available at: http://europa.eu.int/comm/external_relations/human_rights/doc/cr28_11_91_en.htm (accessed: May 4, 2006).

14 Gordon Crawford, "European Union Development Co-operation and the Promotion of Democracy," in Burnell, 90–127.

15 This was the case in cooperation with Niger (1996 and 1999), Haiti (2001) and Fiji (2000). See Carlos Santiso, "Promoting Democracy by Conditioning Aid? Towards a More Effective EU Development Assistance," *Internationale Politik und Gesellschaft*, No. 3 (2002): 107–133 (121–126).

16 Articles of Agreement, Article IV, Section 10, available at: http://web.worldbank.org/WBSITE/EXTERNAL/EXTABOUTUS/0,,contentMDK:20049603~pagePK:43912~piPK:36602,00.html#I11 (accessed: May 4, 2006).

17 World Bank, *Sub-Saharan Africa: From Crisis to Sustainable Growth*, (Washington, D.C., 1989).

ment of a country's economic and social resources for development. In this sense, "good governance" means a government administration that is efficient, predictable, and transparent and it presupposes a functioning public bookkeeping and accounting system as well as a binding legal framework that enables private economic competition.

Although the World Bank successively expanded its concept of good governance over the course of the nineties[18], at its core it has maintained a technical-administrative understanding of governance that is equivalent to sound development management. At the same time, the concept made it possible to include the economic purists within the World Bank in the discussion without having to broach political issues in the narrow sense.[19] The crucial aspects of governance for the World Bank can be deduced from the Country Policy and Institutional Assessments (CPIA) which are conducted annually by the World Bank. The results of the CPIA determine the allocation of concessionary loans disbursed by the International Development Association (IDA), a subsidiary of the World Bank, to eligible developing countries. Among the key criteria that the CPIA uses for assessing the governance of a country are: protection of property rights, the quality of budgetary and financial management and public administration, efficiency of revenue mobilization, and transparency and accountability in the public sector. Other criteria that provide information about the quality of governance are those that also aid in evaluating the social policy of a country, for example, government expenditure on education and health and the quality of government policies in the area of social protection and labor market regulation.[20]

Over the course of the nineties, bilateral donors from the Organization for Economic Co-operation and Development (OECD) and the EU adopted the concept of good governance.[21] However, they defined the concept more broadly and included aspects that referred to decision-making procedures, state behavior governed by the rule of law, and economic policy. The key factors here are democratic and participatory development, respect for human rights, and market orientation. Despite various donors weighing these factors differently and the general opacity of the concept notwithstanding, good governance became a generic term for "favorable policy frameworks"[22] and it became a benchmark concept for political conditionality.

Political conditionality is problematic in two respects. On the one hand, the narrow, technocratic understanding of governance is too limited in that it ignores the central issue of power relations. In the authoritarian or semi-authoritarian regimes with which development aid is generally involved, power is concentrated in such a way that an effective system of checks and balances is blocked. Under such conditions, exogenously induced reforms of the public sector have only a superficial impact on the problem of bad governance.[23] Often, autocratic and clientele structures are actually reinforced This is because state structures are the primary distributors of development aid, a situation that requires that a passably functioning state apparatus is in place. As a result, the donors have to rely on the cooperation of the political elite, whose position tends to be strengthened by such cooperation. Conditions aimed at bringing about institutional and administrative reforms may be accepted in these circumstances, but they don't resolve the key problem at the heart of bad governance, namely the monopolization of public resources by the ruling elites.

On the other hand, while political conditionality that is limited to administrative and regulatory aspects leads to selective blindness, a broad conception of political conditionality faces a normative dilemma in two respects. First, external demands for systemic reforms that affect the political, legal and administrative systems are often rejected by the governments of non-democratic states as a violation of the internationally recognized principle of non-

18 World Bank, *Governance: The World Bank's Experience*, (Washington, D.C., 1994).

19 Stokke, 26f.

20 Worldbank, *Country Policy and Institutional Assessments. 2004 Assessment Questionnaire*, Operations Policy and Country Services, December 6, 2004, available at: http://siteresources.worldbank.org/IDA/Resources/CPIA2004questionnaire.pdf (accessed: May 4, 2006).

21 Daniel Beck and Thomas Conzelmann, "Zwischen Sanktionierung und Dialog. Die Durchsetzung von Good Governance in der Entwicklungspartnerschaft von EU und AKP," in Franz Urban Pappi et al. (eds.), *Die Institutionalisierung internationaler Verhandlungen*, (Frankfurt a.M./New York 2004): 321–352.

22 This is part of the BMZ's definition of good governance: BMZ, Good Governance, June 2002: 8, available at www.bmz.de/de/service/infothek/fach/spezial/spezial044/a90.pdf (accessed: May 4, 2006).

23 Stokke, 27, and (in terms of World Bank analysis of corruption) Jeffrey A. Winters, "Criminal Debt," in Jonathan R. Pincus and Jeffrey A. Winters (eds.), *Reinventing the World Bank*, (Ithaca/London 2002): 101–130 (103).

intervention in the internal affairs of sovereign states. It is then up to the discretion of the donors whether they want to reduce the cooperation or cancel it altogether, but such a decision is usually only made in exceptional cases. Thus, the principle vehicle for cooperation between the EU and ACP states, the Cotonou Agreement– signed in 2000 as the follow-up to the Lomé Convention and revised in 2005—calls for the suspension of cooperation as a last resort, after consultation fails to produce results. However, this sort of negative conditionality should only be used in "cases of special urgency."[24] This condition remains necessarily vague and leaves a lot of room for interpretation and its implementation.

Second, the allocation of development aid is determined largely by institutional self-interest, foreign and trade policy considerations, and strategic interests.[25] This creates a credibility problem: while political conditionality invokes universal norms and values, they are discredited by its inconsistent application. This also undermines the position of the donors as the advocate of these norms and values and promotes a policy of double standards on both sides.

The Impact and Effectiveness of Conditionality

The expansion of the agenda of development policy to include political and institutional reforms was accompanied by a continuous debate about the effectiveness of development aid. The debate was motivated by two factors. First, due to persistent economic stagnation and widescale poverty, especially in sub-Saharan Africa, the pressure on donors increased to reconsider their development aid strategies. Second, the pressure to reform that this caused was increased by the continuous decline in Official Development Assistance (ODA) in the course of the nineties.

A recurrent theme in the debate over the effectiveness of development aid was the question whether ex-ante conditionality was an appropriate instrument to motivate recipients to undertake economic and institutional reforms and thereby to create the conditions necessary for sustainable economic growth and an effective fight against poverty. Numerous studies, some of which were commissioned by the International Financial Institutions, have come to the conclusion that there is only a weak correlation between conditionality and the desired effects.[26] According to these studies, financial incentives and negative conditionality—the threat of withdrawing funds or sanctions in the case of non-compliance—are equally ineffective in stimulating sustainable reforms. While conditionality can lead to short-term policy change, especially in cases of extreme dependency on donors, this does not necessarily result in a qualitative transformation of politics, especially given the volatility and reversibility of reform processes. Because of the structural asymmetry in the donor-recipient relationship, the conditions are typically seen as the result of external pressure, even when the recipients agree to the donors' conditions. This dominance by the donors in turn has a negative impact on the acceptance of reform programs and reduces the incentive to imple-

24 Article 96 b) and c) of the agreement, which can be read at http://europa.eu.int/comm/development/body/cotonou/pdf/agr01_en.pdf#zoom=100 (accessed: May 4, 2006).

25 Alberto Alesina and David Dollar, "Who Gives Foreign Aid to Whom and Why?" *Journal of Economic Growth*, Vol. 5, No. 1 (March 2000): 33–63; Gustavo Canavire et al., *Assessing the Allocation of Aid: Developmental Concerns and the Self-Interest of Donors*, Kiel Working Paper No. 1253, (Kiel: Kiel Institute of Economics, June 2005), available at: www.uni-kiel.de/ifw/pub/kap/2005/kap1253.pdf (accessed: May 4, 2006); Richard Youngs, "European Approaches to Democracy Assistance: Learning the Right Lessons?," *Third World Quarterly*, Vol. 24, No. 1 (2003): 127–138 (134–137); William Easterly, "The Cartel of Good Intentions: The Problem of Bureaucracy in Foreign Aid," *Journal of Policy Reform*, Vol. 5, No. 4 (2002): 223–250, and the case studies in: Stokke, 46–55.

26 On this issue see: Karl R. Pedersen, "Aid, Investment and Incentives," *Scandinavian Journal of Economics*, Vol. 98, No. 3 (1996): 423–438; Paul Collier et al., "Redesigning Conditionality," *World Development*, Vol. 25, No. 9 (1997): 1399–1407; Tony Killick (with Ramani Gunatilaka and Ana Marr), *Aid and the Political Economy of Policy Change*, (London/New York, 1998); Paul Collier, "The Failure of Conditionality," in Catherine Gwin and Joan M. Nelson (eds.), *Perspectives on Aid and Development*, (Washington, D.C. 1997): 51–77; David Dollar and Jakob Svensson, "What Explains the Success or Failure of Structural Adjustment Programmes?" *The Economic Journal*, Vol. 110 (2000): 894–917; Mosley, *Conditionality as Bargaining Process*, and Stokke, "Aid and Political Conditionality", passim.
A series of studies came to a different, namely positive, conclusion in terms of the correlation between development aid and economic growth. These works, however, have only marginally influenced the discourse on development policy, mostly likely because the claim of a positive correlation between development aid and growth is not immediately convincing. See, for example, Henrik Hansen and Finn Tarp, "Policy Arena. Aid Effectiveness Disputed," *Journal of International Development*, Vol. 12, No. 3 (2000): 375–398; Oliver Morrissey, "Conditionality and Aid Effectiveness Re-evaluated," *The World Economy*, Vol. 27, No. 2 (2004): 153–171.

ment the conditions or leads to the agreements being broken. A further reason for the failure of conditionality is the frequently weak empirical basis of the donors' priorities, which also neglect to sufficiently take into consideration a country's specific situation.

Above all, the studies reveal that conditionality often has unintended consequences. On the one hand, it undermines the recipients efforts at self-help and solidifies their dependence on the donors. On the other hand, the conventional system of incentives motivates the recipients to develop strategies to manipulate the flow of funds. Conditionality is especially counterproductive when it affects a government that is already reform-oriented. In such cases, the reform process could be stalled by the insistence on meeting conditions set by the donors, which, furthermore, are often simply impossible to fulfill due to a lack of capacity. And not least, the donors themselves are often not focused enough on efficiency criteria. The International Financial Institutions are under political pressure from their corporative stakeholders to lend even when conditions are not met. Finally, conditionality becomes a complete farce when the disbursement of new funds is solely for the purpose of aiding the recipient to repay outstanding loans ("defensive lending")—regardless of whether reform programs are implemented or not. This lack of coherence in applying conditionality erodes the logic of incentive, as does the variety and number of conditions and the absence of precise criteria for the evaluation of the fulfillment of the conditions.

The majority of studies come to the conclusion that reforms cannot be induced or forced externally, rather they must come from the recipients themselves. A successful reform process therefore requires, first of all, the voluntary commitment of the recipient. Second, effective development aid requires a reform-oriented environment, ideally characterized by an open trade system, low inflation, a small budget deficit, protection of private property and an efficient public administration. In other words, a sound economic policy and functioning public institutions. Under such conditions, development aid can produce the desired effect by promoting economic growth and contributing to poverty reduction.[27]

Thus, "good policies," the good political framework conditions which development aid aims to create, became a precondition for a successful reform process.

27 Craig Burnside and David Dollar, *Aid, Policies and Growth*, Washington, D.C.: World Bank, Development Research Group, 1997 (Policy Research Working Paper 1777) (reprinted in: *American Economic Review*, Vol. 90, No. 4 [2000]: 847–868); World Bank, *Assessing Aid. What Works, What Doesn't, and Why. A World Bank Policy Research Report*, (Oxford, 1998).

"Partnership" Conditionality

The new foreign aid paradigm which took shape in the course of the debate over the effectiveness of development aid, was officially embraced at the UN Conference on Financing for Development in Monterrey in March 2002. In order to achieve the Millennium goals set out by the UN General Assembly in September 2001, the resolution from Monterrey declared that it was necessary to establish a "new partnership" between donors and recipients.[28] The overarching goal of this partnership needs to be the fight against poverty, and it needs to be recognized that developing countries want to take responsibility for their own development plans—and that the donors want them to, as well.[29]

Ownership, understood as control of the reform process by the recipients—now elevated to the status of "partners"—thus became a precondition for a more effective development policy. This means that donors now need to abide by two imperatives that cannot easily be reconciled: efficiency and partnership. This forces the donors to constantly adjust their set of conditions. The International Financial Institutions have taken the lead in this process, foremost among them the World Bank, which sets the tone in the discourse on development policy and has been successful at maintaining its intellectual monopoly in this policy field. The following sections looks at the key discursive and instrumental innovations.

"Ownership" as a Leitmotif

The new leitmotif of development policy discourse is far more than just a buzzword. The concept of ownership is part of a semantic field that includes key concepts such as partnership, participation, empowerment of the poor, poverty reduction, and sustainability. This vocabulary evokes a new development policy consensus that makes a claim to normative validity and tends to apoliticize the debate.[30] Moreover, the ubiquity of these concepts in the programmatic literature of the donor agencies suggests a "new" approach to the problems to which development policy intervention reacts. In this context, ownership acts as a magic word that lends rationality and legitimacy to development operations, and with the causal assumption it entails, offers solutions to the problems created by these assumptions.

Thus, Joseph Stiglitz, a former chief economist of the World Bank, answered the question of whether conditionality is an effective means for bringing about political change with the dictum, "Good policies cannot be bought." Instead, the partner countries should be encouraged to arrive at a national consensus to define their own development strategies.[31] Former World Bank President James Wolfensohn described the new paradigm in a similar manner in a much quoted speech: Effective development aid requires a partnership in which the developing countries, and not the donors, are in the driver's seat and determine the direction.[32] This provides the outline of the principal meaning of ownership: the control of the reform process by the recipients. The donors undertake a supporting role, not the leadership. But this presupposes that the reform agenda and goals of both partners are

28 *Monterrey Consensus of the International Conference on Financing for Development*, Resolution, March 18–22, 2002 (Chapter I.4.), published as a supplement to the *Report of the International Conference on Financing for Development*, VN-Doc. A/Conf.198/11, March 18–22, 2002.

29 "Effective partnerships among donors and recipients are based on the recognition of national leadership and ownership of development plans" (*Monterrey Consensus of the International Conference on Financing for Development*, Resolution, Chapter II.D.40).

30 Andrea Cornwall and Karen Brock, "What Do Buzzwords Do for Development? A Critical Look at 'Participation,' 'Empowerment' and 'Poverty Reduction'", *Third World Quarterly*, Vol. 26, No. 7 (2005): 1043–1060.

31 Alan Beattie, "Stiglitz Hits at World Bank Policy," *Financial Times*, November 29, 1999, 9.

32 "Partnership [...] must rest on four pillars. First and foremost, the government and the people of developing countries must be in the driver's seat—exercising choice and setting their own objectives for themselves. Development [...] *cannot* [sic!] be donor-driven." (James D. Wolfensohn, *The Challenge of Inclusion*. Annual Meetings Address, Hong Kong, Special Administrative Region, China, September 23, 1997, available at www.worldbank.org/html/extdr/am97/jdw_sp/jwsp97e.htm [accessed: May 4, 2006]).

largely in agreement. Therefore, donors tend to stress another dimension of the concept of ownership, namely the recipients' commitment to and responsibility for aid-supported reforms.[33] As such, ownership itself becomes a precondition for a successful reform process, and if there is a lack of ownership, it needs to be encouraged.[34]

A first step towards resolving these demands was the introduction of Poverty Reduction Strategies (PRS) by the IFIs in 1999. The poorest developing countries are now required to present a corresponding strategy paper, updated every three years, in order to receive debt relief and concessionary loans and grants from multilateral and bilateral donors. A PRS explains the macroeconomic, structural, and sociopolitical programs that a government plans to undertake in the coming years in order to stimulate growth and reduce poverty. The donors place a lot of emphasis on the "participatory" creation of a PRS. That is to say, civil society and the private sector should participate in the drafting of a PRS, and they should be aimed at benefiting the poor. A PRS is also expected to be based on "a long-term perspective for poverty reduction" and to take "the multidimensional nature of poverty" into consideration.[35]

If a strategy paper is accepted by the decision-making bodies of the IMF and the World Bank, a country can receive structural adjustment loans from both institutions. In the case of the IMF, the relevant credit program is called Poverty Reduction and Growth Facility (PRGF), which replaced the earlier Enhanced Structural Adjustment Facility (ESAF) and, like its predecessor, is meant to support macroeconomic reforms. These reforms, however, are now aimed not only at stimulating economic growth, but are also expected to reduce poverty.[36] At the same time, the World Bank offers Poverty Reductions Support Credits (PRSC) or Development Policy Loans within the framework of its Development Policy Lending (DPL), as World Bank structural adjustment financing is now called. These funds are designed to finance the implementation of a PRS, and they are associated with clearly defined goals, progress indicators, and policy measures. In contrast to earlier structural adjustment programs, loans and credit tranches are not disbursed upfront, rather they are released only after certain previously agreed to conditions are met.[37] These conditions are oriented towards the recipient's PRS, which is expected to align macroeconomic, structural, and social policies. Nearly 60 developing countries have now presented a PRS.

A further innovation introduced by the World Bank in 1991 designed to strengthen the ownership of the recipients for their own development plans and to reinforce the PRS process was the conceptional expansion of the Country Assistance Strategy (CAS) into the Comprehensive Development Framework (CDF). Together with the IMF's "seal of approval," CAS, and now CDF, form the basis for the donor community's involvement in a country and they represent the overarching framework for the cooperation between the World Bank group and the recipient country.[38] According to the relevant websites of the World Bank, country-specific development goals should be set in conjunction with a "balanced and well-sequenced set of policy measures" to form a coherent development strategy. These should, analogous to the PRS, be driven by a "long-term, holistic vision" and be based on the principles of "country ownership," "results focus," and "country-led partnership."[39]

"Country Ownership"

According to the provisions of the World Bank, country ownership requires that a country's government have the support of all relevant stakeholders in the country and be able to mobilize sufficient political

33 For example, see Stefan Koeberle, "Conditionality: Under What Conditions?," in Stefan Koeberle et al. (eds.), Conditionality Revisited. Concepts, Experiences, and Lessons, (Washington, D.C.: World Bank, 2005): 57–83 (67): "ownership—that is, commitment to aid-supported reforms …"

34 For example, see the contributions to *The Role of Conditionality in Policy-Based Lending*. International Policy Workshop, InWEnt Development Policy Forum, Berlin, April 6–7, 2005.

35 Poverty Reduction Strategy Papers, available at: www.imf.org/external/np/exr/facts/prsp.htm, and the PovertyNet-Website of the World Bank, available at: www.worldbank.org/poverty.

36 *The Poverty Reduction and Growth Facility*, available at: www.imf.org/external/np/exr/facts/prgf.htm.

37 See World Bank, *Review of World Bank Conditionality*. Operations Policy and Country Services, World Bank, September 2005: 4ff, available at: http://siteresources.worldbank.org/PROJECTS/Resources/40940-1114615847489/webConditionalitysept05.pdf, (accessed: May 4, 2006).

38 Cord Jakobeit, "Das Konzept der Weltbank für die Länderplanung. Von der Projektpolitik zur umfassend koordinierten Armutsbekämpfung," *Entwicklung und Zusammenarbeit*, No. 9 (September 2000): 242–244.

39 See the Comprehensive Development Framework website of the World Bank, available at: www.worldbank.org/cdf.

support in order to implement the development strategy even if some interests groups oppose it. Political debate over fundamental issues related to national development strategies should not be prevented, but if there is broad agreement on realistic and long-term goals and the general direction and its economic soundness have been determined, this could help to limit internal discussions to matters of detail.[40] Essentially ownership here means nothing other than the voluntary acceptance of conditions based on the consent of the country's "relevant" stakeholders. These, however, act in close cooperation with the IFIs, who are not only heavily involved in the drafting of the development strategies presented by the governments of the recipient countries: the IMF and the World Bank also determine the parameters of the strategies and decide which reforms are "right" for the development of a country.[41]

In contrast to the eighties, when fiscal structural reforms along with those geared towards increasing investment and production were the focus of development programs, since the mid-nineties they are increasingly aimed at areas of governance, i.e. institutional reforms that are designed to improve public administration and state social services (see above, p. 9). But these are extremely complex reforms that cut deep into the established network of relationships and are associated with redistribution conflicts. As such, they are more difficult to push through and to implement than the structural reforms of earlier years. The balancing of interests and consensus building between the relevant parties that country ownership requires is, under such circumstances, often laborious, tedious, contentious. In states characterized by poor governance, however, that have no access to commercial capital markets and are therefore to a great degree dependent on concessionary loans, there is danger that this sort of balancing of interests will get short shrift and the government will push through reform measures against the will of relevant stakeholders. This in turn hinders the implementation of the reforms and can lead to domestic conflict or even to an end to the reform process.[42]

The new conditionality, which declares ownership as a prerequisite and a goal of reform processes and commits the recipients for many years, means two things for the recipients. First, they must fulfill more preconditions for access to loans and grants. Second, the demand for country ownership in the case of complex reforms increases the risk of unintended domestic consequences. Moreover, the technocratic consensus of the donors which makes institutional reforms dependent on the implementation of a few "key measures" overlooks that in the case of complex reforms, ownership also involves changes in behavior and consequently a transformation of norms and values. This requires a longer time horizon than the prescribed loan periods and program timelines.[43]

Results Focus

Long-term changes of this sort are hard to diagnose, let alone measure. This fact is not changed by another reorientation that is part of the new conditionality and that is intended to strengthen the responsibility of the recipients, namely the focus on results. That is, ex-ante conditionality and the associated concentration on the implementation of concrete measures (inputs) and on short-term quantitative results (outputs) should largely take a back seat to performance dependant ex-post conditionality. This means that the donors and the recipient governments agree on goals that are to be reached in the mid-term and to the appropriate indicators for measuring progress towards achieving those goals. In this way, the distribution of funds and the modalities of distribution are to be dependent on verifiable results and performance, rather than on promises. In this spirit, the World Bank is increasingly making use of floating tranches. Their distribution is tied to reform measures the timing of which is determined by the recipients themselves. The recipient government is thereby afforded greater flexibility and freedom in the choice of appropriate measures. At the same time this provides recipient governments with an incentive to shift attention to the monitoring and evaluation of programs and

40 The passages reduced here to their core statements can be found at www.worldbank.org/cdf, under the headings "Country Ownership" and "Long-term Holistic Vision."
41 Daniel Morrow, "Adjusting Conditionality: Prescriptions for Policy-Based Lending," in Koeberle et al. (eds.), 197–223; Nicolas van de Walle, *Overcoming Stagnation in Aid-Dependent Countries*, (Washington, D.C.: Center for Global Development, 2005): 51ff.
42 Morrow, 203; see also the contributions in: Jeremy Gould (ed.), *The New Conditionality. The Politics of Poverty Reduction Strategies*, (London 2005).
43 Morrow, 203f, 210f; Killick, 92ff.

policies and—with the support of the donors—to build their capacity to do so.[44]

The logic of such a reorientation is immediately apparent, but it is only of limited practicality in the majority of cases. First, reliable measurement of results stands or falls on the quality of the available data, and, second, the results can usually only be broadly assessed if the programs are implemented systematically over a long period of time. This in turns requires a certain degree of political stability that is often lacking in countries receiving development assistance. Third, the impact of donor-supported programs depends not only on the implementation of certain policies, it is also influenced by exogenous and internal factors that governments can only control to a limited degree. Consequently, it is difficult to determine whether political changes, whether desired or undesired, are the result of development policy measures.[45]

"Country-led Partnership"

The new conditionality, developed under the leadership of the IFIs, also provides the cornerstones for bilateral donors. Thus, the principle of "country-led partnership" aims at strengthening the harmonization and coordination of donor programs and aligning them to the development strategies of the partners. This is intended to counteract the fragmentation and duplication of donor activities within the same country, a situation that goes against the principle of country ownership. The divergent conditions and procedures associated with differing donor programs produce unnecessary transaction costs and absorb the institutional capacity of recipient governments. Improved coordination among the donors on the one hand and with partner governments on the other hand, who are expected to take on a coordinating role, are intended to reduce donor conditionality and make it more consistent, unleash synergies, and increase the efficiency of the use of funds.[46]

In this connection, new financing instruments that allow the use of the recipients' budget systems and procedures and are oriented towards their priorities play an important role.[47] Accordingly, traditional project financing is expected to be gradually replaced by joint program and budget financing, in which several donors co-finance ventures concerned with a specific issue or sector, or they contribute to an account that the recipient government has budget control over. (known as budget financing). The funds are either reserved for certain sectoral programs that take priority within the framework of a PRS (sectoral budget aid) or they are used at the discretion of the partner governments (General Budget Support), which provides them a maximum of flexibility and is supposed to increase their responsibility.

The use of such financial instruments, especially budget aid, places considerable demands on the quality of public budget management and good governance in general. Above all, the national Poverty Reduction Strategy must be translated into appropriate policy programs that span sectors and it must be incorporated into the mid-term budget plans of the recipient government so that program and budget aid operations can be carried out. This represents several challenges for the administration of developing countries that they are hard pressed to meet. Hence, there is often little or no connection between the PRS and a state's budget. This, however, is not necessarily due to a lack of political will on the part of those responsible, but rather to a lack of planning capacity and inadequate budget systems in the developing countries. As a result, there is often a great discrepancy between the funds estimated in the budget plan and the actual amount spent. Misuse of public funds are usually not only caused by problems within the administration. It is often the result of a lack of transparency and accountability in the public sector, because many partner countries lack effective budget control through a higher-ranking administrative body, a central auditing authority, the parliament, or even civil society.[48]

Not least because of the fiduciary risks associated with program and budget aid, there is a widespread

44 See the overview in the World Bank website entitled *Comprehensive Development Framework* available at: www.worldbank.org/cdf, under the heading "Results Focus," and in greater detail in Koeberle, 69ff.
45 Koeberle, 70f.
46 See the relevant program paper of the Development Assistance Committee (DAC) of the OECD from March 2005, the *Paris Declaration on Aid Effectiveness*, available at: www. oecd.org/dataoecd/11/41/34428351.pdf (accessed: May 4, 2006).

47 Stephan Klingebiel, Stefan Leiderer and Petra Schmidt, "Programmfinanzierung und öffentliche Budgets. Neue Instrumente und Ansatzpunkte der Entwicklungspolitik," in Dirk Messner and Imme Scholz (eds.), *Zukunftsfragen der Entwicklungspolitik*, (Deutsches Institut für Entwicklungspolitik [DIE], Baden-Baden 2005): 73–87.
48 Ibid., 78ff.

consensus among the donors that these financial instruments should only be used when there is sufficient ownership on the part of the partner. That includes, above all, the willingness to improve public budget management and reporting structures, allowing the donors to inspect the institutions and the processes of state budgeting, and permitting periodic audits, for example in the form of Public Expenditure Reviews which are conducted by the international financial institutions.[49]

In conclusion, the appeal to development partnership and the associated trend toward increased donor coordination and harmonization under the aegis of the IFIs requires increased multilateral coordination in the allocation of funds. This in turn means that donors must move away from unilaterally setting their own focus and the associated conditions and instruments of control. While this tends to reduce the number and variety of conditions and potentially increases the effectiveness of development aid, this is only possible if the recipients take ownership of their development programs. This creates the problem for the donors of having to determine the presence or absence of ownership.

Problems of Measurement

The development policy consensus that declares ownership as the *sine qua non* for successful reform policies confronts the donors with problem of measuring ownership. While the World Bank developed diverse concepts for the evaluation of ownership over the course of the nineties, their explanatory power is limited.[50] On the one hand, the analyses are only based on a limited time period, and, on the other hand, the complex and fluctuating constellation of stakeholders that needs to be looked at when evaluating ownership can scarcely be captured by surveys and game theory models. At best, such analyses can provide approximate values, but they cannot provide robust indicators of ownership.

The same is true for the Poverty Reduction Strategies. Nearly all partner countries that benefit from concessionary loans from the International Development Association and are required to present a PRS have drafted such strategy papers; about half of them have already presented progress reports. Even countries whose willingness to reform is quite questionable, such as the Central African Republic, the Republic of Congo, and Uzbekistan, have created so-called Interim PRS—a fact that reveals the self-propelling dynamic that the PRS has set into motion. Given this, there is only relative value in using a PRS as a criterion for ownership. In the end, the concept is as indeterminate as "good policies," which in the relevant literature are considered proof of ownership. There are no objective criteria for differentiating between countries with "good" and those with "bad" policies. The majority of developing countries fall somewhere between these two ideal-type poles and are characterized by a mixed record.[51]

The decisions about the necessary preconditions for and the conditions at which the limited resources for public development aid should be distributed are therefore largely matters of discretion. As such, the risk of making mistakes is high, which places the donors under constant pressure to reform and justify their conditionality rules.

49 Ibid., 82ff.
50 See, for example, Luke Haggarty and Yasuhiko Matsuda, *Assessing Clients' Commitment to Sectoral Reforms: A Reform Readiness Analysis* (undated [created: June 10, 2001]), available at: http://www1.worldbank.org/ education/ globaleducationreform/pdf/haggarty.pdf (accessed: May 4, 2006); Barbara Nunberg and Amanda Green, "Operationalizing Political Analysis: The Expected Utility Stakeholder Model and Governance Reforms," November 2004 (PREM Notes, No. 95), available at: http://www1.worldbank.org/ prem/PREMNotes/premnote95.pdf (accessed: May 4, 2006), and the overview by Daniel Morrow, "Assessing Borrower Ownership Using Reform Readiness Analysis," June 1999 (PREM Notes, No. 25), available at: http://www1. worldbank.org/prem/PREMNotes/premnote25.pdf (accessed: May 4, 2006). The issue of the measurability of ownership is dealt in detail in Killick, 86ff, 178.
51 Koeberle, 69.

Donor Policies

In the debate over the application of conditionality that is expected to comply with both the precepts of efficiency and partnership, we can differentiate between two approaches that each imply their own divergent development policy strategies. First, an exclusive approach that prescribes increased selectivity in the choice of recipients and operates with clearly defined criteria for ownership. The donors determine upfront which framework conditions must exist and what must be accomplished in order for a country to receive development aid. The bulk of funds are expected to go to countries with convincing political framework conditions and are to be used there to stimulate economic growth. This is intended to send a clear signal to the recipients that good governance is being rewarded. In addition, it is assumed that this can also have spill-over effects by creating incentives in neighboring countries to improve their governance.[52]

This strategy of selectivity stands in contrast to an inclusive approach that takes the precept of partnership literally, understands development cooperation as a process of dialogue, and calls for reducing conditionality to a minimum. In this sense, development cooperation is conceived as a mutual learning process during which both sides agree to common goals. In order to give even unproductive countries a realistic chance at improving their performance record, the political dialogue must be carried out in a spirit allowing for open-ended results and with the aim of supporting the recipients in identifying policy options. While conditionality is not superfluous under such circumstances, it is largely limited to systematic monitoring of how development aid funds are used and whether they are being used to implement the policy measures agreed upon.[53]

The two concepts are based on differing causal assumptions from which they derive specific preferences. While the strategy of selectivity focuses on the efficient use of funds through the "right" incentives, the dialogue model depends on learning and negotiating processes as prerequisites for effective development aid. In the following section, the actual practice of both strategies will be highlighted and examined in terms of their performance. Thereafter, the dilemmas and conflicting aims associated with these strategies will be explained.

"The Winner Takes All": The Conditionality of the Millennium Challenge Account

In the ongoing discussion about development conditionality, the Millennium Challenge Account (MCA) is often presented as a model for a strategy of selectivity. The initiative was launched by President Bush in March 2002, right before the UN conference in Monterrey. It can be interpreted as an attempt by the US administration to demonstrate to its coalition partners in the war on terrorism that the US is also prepared to take a leading global role in non-military areas. At the same time, the establishment of the MCA, which according to the president's announcement was to be quickly built-up over a three-year period, resulting in a budget of $5 billion by fiscal year 2006, is a reaction to the widespread criticism of American development aid, which is accused of being too limited and not efficient enough in fighting poverty.[54]

52 See, for example, Collier, "The Failure of Conditionality;" Burnside and Dollar; David Dollar and Victoria Levin, *The Increasing Selectivity of Foreign Aid, 1984–2002*, Washington, D.C., May 2004 (World Bank Policy Research Paper 3299), available at: http://www-wds.worldbank.org/servlet/WDSContentServer/WDSP/IB/2004/06/15/000009486_20040615151147/Rendered/PDF/wps3299SELECTIVITY.pdf (accessed: May 4, 2006); Peter Nunnenkamp, "Mehr Entwicklungshilfe ist nicht genug. Zielgerichtete Unterstützung armer afrikanischer Länder mit guter Regierungsführung?" *Afrika Spectrum*, Vol. 40, No. 3 (2005): 445–470; Paul Kevenhörster, "Wer hilft wem? Die schwierige Auswahl der Empfängerländer öffentlicher Entwicklungshilfe," *Auslandsinformationen der Konrad-Adenauer-Stiftung*, Vol. 21, No. 7 (2005): 4–21.

53 See, for example, Morrissey, "Conditionality and Aid Effectiveness Re-evaluated," Oliver Morrissey, "Alternatives to Conditionality in Policy-Based Lending," in Koeberle et al. (eds.), 237–247; Patrick Watt, "Partnerships in Policy-Based Lending," in ibid., 249–252.

54 Nicolas van de Walle, *A Comment on the MCA Proposals*, Washington, D.C.: Center for Global Development, January 9, 2002, 1, available at: www.cgdev.org/doc/commentary/vandewalle_20030109.pdf (accessed: May 4, 2006); Steven

Foreign aid has been a central element of US foreign and security policy since the end of World War II and served primarily to create strategic alliances in the fight against communism. In the late seventies, this foreign policy focus was supplemented by involvement in the Middle East peace process, with Israel and Egypt being the primary beneficiaries in terms of support provided. Indeed, these two countries continue to receive the most foreign aid of all recipient states. With the end of the Cold War however, foreign aid largely lost the basis of its legitimacy in the US, and as a result, the amount of aid sank continuously over the course of the nineties.

The new conception of American foreign and security policy in the aftermath of September 11, 2001, and the following war on terrorism was accompanied by a strategic revaluation of "soft" policy instruments, as manifested by, among others, the establishment of the MCA. At the same time, the MCA initiative is evidence of the Bush administration's effort to consistently tie the disbursement of funds and development conditionality to efficiency criteria.

The rationality behind the MCA is to provide targeted support for a relatively small number of developing countries whose "good policies" are verifiable.[55] The program is administered by a newly created body that answers to the State Department, called the Millennium Challenge Corporation (MCC). The focus is on programs that contribute to sustainable economic growth and are aimed at effective poverty reduction through investment in relevant areas such as infrastructure, agriculture, and education as well as in the private sector. In doing so, there is a consistent focus on ownership, and the responsibility for the conception, goal setting and implementation of a program therefore lies with the recipients. This is intended to provide them wide-ranging freedom in shaping programs. In return, the standards for participation and reporting are high. First off, it must be clear from the applications for support that all relevant stakeholders in a country, in particular civil society and the private sector, participated in the conception of programs. Second, the applications must contain clear and quantitatively measurable objectives so that the costs and benefits of investment can be analyzed.[56] An obligatory component of applications is therefore a convincing plan for monitoring and evaluation. If the agreed upon results are not achieved, the recipients must expect that the support will be discontinued.

But there is a long path that includes diverse hurdles that need to be overcome before support is forthcoming. The idea is to primarily support Low Income Countries (LIC), defined as countries with an average annual per capita income below $1575.[57] Since 2006 Lower-Middle Income Countries (LMIC) with an annual per capita income between $1576-$3255 are also eligible for consideration. The selection of potential candidates takes place annually on the basis of 16 quantitative indicators that are used to determine how a country performs in terms of "ruling justly," "investing in people," and "economic freedom." The scores for "ruling justly" and "economic freedom" are based on six indicators each, while "investing in people" is based on four indicators (overview, p. 20).[58]

In order to qualify for support, a country must score above the median in half of the indicators for each of the three categories. Scoring above the median in the corruption indicator is mandatory. The medians are determined by the scores for all candidates and are adjusted annually. The inflation indicator in the "economic freedom" category is an exception; an inflation rate below 15 percent is a prerequisite for qualification.

If a country passes the indicator test, the MCC Board of Directors then decides whether it is to be included in the shortlist of countries invited to submit an application for support from the MCA. The scores for each of the indicators are looked at more closely and compared with those of the other candidates. In

Radelet, "Bush and Foreign Aid," *Foreign Affairs*, Vol. 82, No. 5 (2003): 104–117.

55 See on the issue the website of the *Millennium Challenge Corporation* available at: www.mcc.gov.

56 A difference is made between objective indicators, outcome indicators, and output indicators. For example, the objective indicator of a program to revive regional infrastructure might be "financial uses that grow out of investment in infrastructure projects," an outcome indicator could be "an increase in the volume of traffic (in %)," and an output indicator "the number of completed individual projects." See the *Millennium Challenge Compact* with Georgia (Annex III), available at www.mcc.gov. On the significance of cost-benefit analysis in project design, see James W. Fox and Lex Rieffel, *The Millennium Challenge Account: Moving towards Smarter Aid*, Washington, D.C.: The Brookings Institution, July 14, 2005: 15, available at www.brook.edu/views/papers/20050714 rieffel.pdf (accessed: May 4, 2006).

57 This is equivalent to the "historical" upper limit for access to concessionary loans from the World Bank subsidiary IDA.

58 *MCC Selection Policy Indicators: Short Descriptions*, available at: www.mcc.gov/countries/selection/short_descriptions.shtml (accessed: May 4, 2006), and *Selection Process Fact Sheet*, available at: www.mcc.gov/public_affairs/fact_sheets/selection_ process_fact_sheet.shtml (accessed: May 4, 2006).

Overview
Determining Indicators for MCA Support

	Indicators	Source
I.	**Ruling Justly**	
1.	Civil Liberties	Freedom House
2.	Political Rights	Freedom House
3.	Voice and Accountability	World Bank
4.	Government Effectiveness	World Bank
5.	Rule of Law	World Bank
6.	Control of Corruption	World Bank
II.	Investing in People	
1.	Public Expenditure on Health	National sources
2.	Immunization Rate (DPT3*, measles)	World Health Organization (WHO)
3.	Public Expenditure on Primary Education	National sources
4.	Girls' Primary Education Completion Rate	World Bank, UNESCO
III.	Economic Freedom	
1.	Costs of Starting a Business	World Bank
2.	Inflation Rate	IMF and other sources
3.	Fiscal Policy	National sources, IMF
4.	Days to Start a Business	World Bank
5.	Trade Policy	The Heritage Foundation
6.	Regulatory Quality	World Bank

* diphtheria, whooping cough, tetanus.

addition, it is within the board's discretion to request additional information that supplements the quantitative data. For example, other aspects considered when reviewing the shortlisted candidates include whether a country is undertaking special efforts at combating corruption or is committed to democratic governance. An agreement, called an MCA Compact, is then negotiated with those countries that are eligible for support and that have submitted an application that has been approved by the MCC. While the compacts are typically valid for five years, the partner countries must re-qualify on an annual basis. Candidates that fail to qualify, but that have demonstrated that they have taken effort to improve their scores in the areas where they performed poorly, are eligible for support within the framework of a threshold program.

Since the first selection round in May 2004, 34 countries have passed the indicator test, eight of which are from the LMIC group that became eligible in fiscal year 2006. 23 of the 34 were deemed worthy of support, four of which did not qualify until November 2005 and three other candidates (El Salvador, Cape Verde, and Namibia) are from the LMIC group. But compacts were not concluded until 2005 and up to date only with those from the LIC group, namely Madagascar, Honduras, Nicaragua, Georgia the Cape Verde, which, however, advanced to the LMIC group in 2005. Three additional agreements—with Armenia, Vanuatu and Benin—were concluded in the first quarter of 2006. The emphasis of the agreements is on infrastructure projects and rural development programs.[59] This raises two critical points about the MCA program that undermine its intended impact of more effective foreign aid through support of ownership and rewarding good policies: first, the conventional approach of the project, and second, the selection process.

First of all, the MCA is a bilateral program that was established just as other donors were moving towards greater use of multilateral instruments in development financing (see above, pp. 16f). This transformation is associated with the finding that the large number of uncoordinated individual projects from many different donors and the associated differences in the rules for procurement, monitoring, and evaluation overtaxes the administration of the recipient

59 See the *Compacts* and the *Fact Sheet* available on the MCC website at: www.mcc.gov/.

countries and serves more to hinder than support the impact of aid. Whether or not the outcome of the projects financed by the MCA justify the high administrative costs associated with the process is questionable. There is also some doubt in terms of sustainability, in particular of the classic infrastructure projects. While these have the advantage of presenting concrete, visible results—that is why donors are reluctant to let go of their “own” projects despite the trend to multilateralism—numerous development ruins are evidence of the fact that these projects often only have a short life span. The measures financed by the MCA can be tackled quickly thanks to the unusually rapid disbursement of funds. In addition, due to the hard, results-oriented conditionality of the MCA, initial results can be expected in a relatively short time. But the sustainability of the measures is just as uncertain as traditional project aid, especially since a Millennium Challenge Compact is concluded for a maximum period of five years. Against this background, observers see the MCA program in danger of drifting toward “more of the same” and not being able to fully tap its innovative potential.[60]

Critical observers of American development policy also complain that the MCC administration have undue influence during the contract negotiations and have pushed through their own priorities in the programs’ conception. For example, in some cases the contract partner was allegedly talked into concentrating on infrastructure projects or the financial sector instead of on education and healthcare. This would contradict the original intention of the MCA and undermine the principle of ownership.[61]

Second, the methodology of the MCA qualification process is in principle designed to establish a maximum degree of transparency and to avoid political instrumentalization of the selection process. In several cases, however, the selections by the MCC board were difficult to comprehend and hence appear arbitrary.[62] For example, Guyana passed the indicator test in 2004 but did not make the shortlist. Instead, Nicaragua and Sri Lanka were given preference, although their performance was worse. Decisions in favor of Mozambique and Georgia were also met with surprise. Mozambique was found wanting in all the indicators for the “Investing in People” category and was below average in the indicator for corruption, but was nevertheless deemed worthy of support in principle. The rationale for this decision was that Mozambique was able to show clear progress in these areas and had a relatively low score in the corruption index of Transparency International, which the board can use for purposes of comparison. But the selection of Georgia, which concluded a MCA Compact in 2005, was met with even greater disbelief. In the category “Ruling Justly,” Georgia only made the grade in two of the three indicators and scored well below the median in the indicator for corruption. Observers believe that the MCC board used the decision to demonstrate support for the political transition process following the “Rose Revolution” in Georgia and for the recently elected President Saakashvili. While this may be legitimate from a foreign policy standpoint, it is a misuse of the MCA, as there are other sources of funding for supporting transitional governments. The use of the MCA as a reserve in case other sources of financing have been exhausted goes against the spirit of the program, which is aimed at countries with a verifiable development orientation, and it undermines the credibility of the program.[63]

The treatment of non-democratic countries or candidates whose commitment to democracy and the rule of law lacks credibility also appears inconsistent. Although the selection decisions testify to the fact that the board places considerable stock in this criterion, its importance is not expressed in the indicators. As a result, a whole series of non-democratic states—including China, Bhutan, Vietnam and Morocco—have passed the test. Although these states were determined to be unworthy of support, in similar cases exceptions were in fact made. For example, a Compact with Armenia was approved, despite the fact that its scores on the democracy-related indicators (“Political

60 Fox and Rieffel.
61 Steven Radelet, The Millennium Challenge Account: Making the Vision a Reality. Testimony for the House Committee on International Relations, Washington, D.C.: Center for Global Development, April 27, 2005: 6, www.cgdev.org/doc/mca%20monitor/MCA%20Testimony1.pdf (accessed: May 4, 2006); Fox and Rieffel, 15 and 22.
62 On this issue, see Steve Radelet et al., New Global Governance Indicators and the Possible Impact on MCA Qualification, Washington, D.C.: Center for Global Development, May 17, 2005, available at: www.cgdev.org/doc/commentary/opinion/MCA%20ProjectionsFY06_upd.pdf (accessed: May 4, 2006), and Sarah Lucas and Steve Radelet, An MCA Scorecard: Who Qualified, Who Did Not, and the MCC Board’s Use of Discretion, Washington, D.C.: Center for Global Development, May 2004, available at: www.cgdev.org/doc/commentary/MCAScorecard_0528.pdf (accessed: May 4, 2006).
63 See, for example, Elizabeth Spiro Clark, “The Millennium Challenge Account: Spur to Democracy?” *Foreign Service Journal*, (April 2005): 31–35 (34).

Rights" and "Voice and Accountability") had dropped sharply. Such decisions do in fact send signals that run counter to the intention of the MCA. Instead of incentives for creating good political framework conditions, states have been given the impression that their evaluation is negotiable.[64]

The concern that there would be a backdoor political instrumentalization of the MCA was supported by the acceptance of the LMIC group in the selection process. The expansion of support to this group of countries beginning in 2006 was viewed critically from the outset. Despite high rates of poverty, some countries in this group have access to commercial capital markets, have high savings rates, and post high tax revenues. To this extent, they are not reliant on grants to finance their poverty reduction efforts. The decision to include the LMIC group was made at a time when it was still believed that the MCA would reach its maximum volume of $5 billion in 2006. It had already become apparent in the years prior that this goal would not be met due to the cost of the Iraq war. The MCA program has also been allocated considerably less funds for fiscal year 2006 than originally planned. Congress only approved $1.8 billion of the $3 billion President Bush had requested.[65] Although the inclusion of the LMIC group in the MCA program has not been made at the expense of low-income countries, the fear that this might happen is not unfounded given the realignment of American foreign policy towards one that is increasingly focused on strategic alliances with emerging powers under the framework of "transformational diplomacy."[66]

64 Ibid., 35; Lucas and Radelet; Steve Radelet et al., *Round Three of the MCA: Which Countries Are Most Likely to Qualify in FY 2006?*, Washington, D.C.: Center for Global Development, October 27, 2005, available at: www.cgdev.org/doc/mca%20monitor/round3/Round3ofMCA_Revised.pdf (accessed: May 4, 2006).
65 "2005 Legislative Summary: Foreign Operations Appropriations," *Congressional Quarterly Weekly*, December 30, 2005.
66 U.S. Department of State, *Realizing the Goals of Transformational Diplomacy*, Secretary Condoleeza Rice, Testimony Before the Senate Foreign Relations Committee, February 15, 2006, Washington, D.C. (State Department Documents and Publications), available at: www.state.gov/secretary/rm/2006/61209.htm (accessed: May 4, 2006).

Dialogue in the Shadow of Sanctions: The Conditionality of EU Programs

The development cooperation of the European Union is considered a prime example of a policy approach with aspirations of global reach and effectiveness. It combines development policy intervention with conditionality that is the product of dialogue and is focused on results.

In 2004, Official Development Assistance amounted to $79.5 billion worldwide, with 65% of that sum coming from the EU and its member states.[67] The quantitative importance of EU development aid stands in marked contrast to its chronic bad reputation. The key points of criticism[68]—fragmentated and confusing processes, a lack of strategic coherence and focus, insufficient coordination between the EU and its member states, lack of credibility, and inefficiency—were confirmed in a series of evaluations conducted for the European Commission at the end of the nineties. As a result, the EU began to realign its development aid policy. The reforms that have been introduced since 2000 are aimed at greater efficiency and transparency of EU aid by improving project and program quality, changing the modalities of disbursement, and increased coordination and coherence of the measures. The reforms focus on six areas of action whose overarching aim is to reduce poverty.[69]

At the core is a move away from the conventional project-focused approach, which it is generally believed contributed too little to building up administrative and institutional capacities in the partner countries and instead created donor-dominated parallel structures. The new approach is intended to heed the finding that effective development aid should be focused on the ownership of reforms. Aid is there-

67 OECD, *Development Cooperation Report 2005*, Vol. 7, No. 1, (Paris: OECD, 2006), Statistical Annex, 158.
68 See, for example, Stefan Brühne, *Europas Außenbeziehungen und die Zukunft der Entwicklungspolitik*. Otto von Freising-Vorlesungen der Katholischen Universität Eichstätt-Ingolstadt, (Wiesbaden, 2005), 35, 37f.
69 The seminal documents are: Council of the European Union, *Declaration by the Council and the Commission on the European Community's Development Policy*, Brussels, November 16, 2000, available at http://register.consilium.eu.int/pdf/en/00/st13/13458en0.pdf (accessed: May 4, 2006), and Commission of the European Communities, *Communication to the Commission on the Reform of the Management of External Assistance*, Brussels, May 16, 2000, available at http://ec.europa.eu/comm/external_relations/reform/document/communication_en.pdf (accessed at: May 4, 2006).

fore to be oriented toward the priorities and systems of the partner countries and should make better use of the locally available structures. As such, the EU is increasingly taking a program-oriented approach.[70]

The frame of reference that serves as the foundation upon which the EU conceives of its country strategies is drawn from the partners' development strategies, which generally refers to their PRS. Complementing this, joint mechanisms are increasingly being used in the allocation of funds, as already outlined above (pp. 16f): the funds allocated by several bilateral and multilateral donors are deposited in a common pool or basket. The use of these pools is managed by either the donors, the recipients or both. Sector-related or direct budget aid are considered particularly effective. The latter is used above all in cooperation with ACP states and is intended to support macroeconomic policies connected to poverty reduction strategies.

The legal prerequisites for the allocation of budget aid are set out in the framework agreements with the partner countries. For the 77 ACP states this is the Cotonou Agreement that was signed in 2000 and which also prescribes the conditions for the allocation of budget aid.[71] These conditions are initially oriented towards the conditionality of the International Financial Institutions see above, pp. 14f). In order to receive budget aid from the EU, the recipient countries need to implement a macroeconomic reform program that is supported by the IMF or has met the approval of the IMF and World Bank as well as to implement a national strategy to reduce poverty (generally, a PRS). The number of conditions that need to be met remains high.[72] The central characteristic of the reformed EU budget aid, which is administered by the EU Commission, is a greater emphasis on results and impact. The budget aid programs are generally for a three-year term and they are divided into fixed and variable tranches. The disbursement of the variable tranches is based on performance-based ex-post conditionality that is ideally aligned with the PRS. The Commission uses a typology that differentiates between four levels of impact and four types of indicators in order to measure the impact:[73]

- Input conditions and indicators concerning the resources and activities that are to be put into the development process (e.g. training seminars),
- Output conditions and indicators concerning the goods or services that were provided with the help of the inputs (e.g. the number of schools built),
- Outcome conditions and indicators—also known as "results/performance indicators"—which focus on the use by the target group of the goods and services produced (e.g. rate of school enrollment),
- Impact indicators which describe the overall goal of the intervention and can only be measured over the long term (e.g. raising literacy rates).

While conditions in the first two categories, which are related to macroeconomic reform programs, are still dominant in the fixed tranches, the Commission is increasingly oriented towards outcome-focused indicators for the disbursement of the variable tranches. Above all, they are used to measure changes in social services (education and healthcare) that can be evaluated by the users. At the same time the results-oriented conditions grant the recipients greater leeway in how to run the programs. It is hoped that this will help increase their ownership of the programs and their sense of responsibility for the target groups who are meant to benefit from them.

A central component of reformed EU conditionality is a gradual system of funds allocation that sets the rules for the disbursement of variable tranches. If conditions are not met or performance is poor, the funds will not be withheld, but rather reduced.[74] This is intended to provide targeted incentives and at the same time raise the planning security of the recipients. The EU Commission makes decisions in conjunction with the partner governments about whether specified goals were reached and how to evaluate an indicator. In doing so, they heed the principle that all factors that can influence goal achievement should be taken into consideration in the evaluation process if the conditions are to be realistic, yet ambitious.

The provision of budget aid is fundamentally a risky venture and is thus viewed with skepticism by some donors, including Germany. However, the use of this financing instrument according to the Cotonou Agreement requires the recipient to demonstrate transparent and efficient budget management and hence a minimum degree of good governance. But,

70 On this and the following, see Petra Schmidt, *Budgethilfe in der Entwicklungszusammenarbeit der EU*, Deutsches Institut für Entwicklungspolitik Studies, No. 10, (Bonn, 2005), 18ff.

71 Article 61 (2) and 67 of the agreement.

72 Koeberle, 64ff.

73 Schmidt, 75ff. On the difficulty of identifying indicators and measuring performance, see Christopher Adam et al., "Performance-Based Conditionality: A European Perspective," *World Development*, Vol. 32, No. 6 (2004): 1059–1070; see also above, p. 15.

74 For details, see Schmidt, 81f.

in contrast with respect for democratic principles, human rights and the rule of law, good governance does not count as one of the "essential elements" in cooperation with ACP states. Unlike these elements, which have the status of fully mandatory norms, good governance is simply a "voluntary obligation." If it is not observed, it does not result in a formal consultation process and as such does not set a formal mechanism of sanctions in motion, though several cases of corruption represent an exception.[75]

Like "good policies" and "ownership," "good governance" is an imprecise concept whose concrete realization can only be roughly comprehended due to the lack of precise measurement criteria. Irrespective of this, the often enormous deficits in the functioning of governments and administrations of the recipients cannot be ignored. The EU elegantly walks its way around this problem in its development cooperation by making good governance, like ownership, a condition and a goal. For example, weaknesses in public budget management are not grounds for denying budget aid, but are rather framed as a challenge. In such a case, providing budget aid is viewed as an appropriate means for improving the budget process. Thus, the Cotonou Agreement calls for a continuous assessment of the recipients' governmental and administrative behavior within the framework of periodic political dialogues that are firmly established as a general condition of the budget aid program.[76]

In this process, the particular meaning of good governance is not unilaterally determined by the donors, rather it is arrived at consensually. At the same time, in connection with the political dialogue, good governance becomes a mandatory subject at the negotiations stage.[77] Moreover, the importance of the principle of good governance is enhanced by the fact that the Contonou Agreement mandates that the allocation of funds is generally dependant on the performance in governance-related areas.[78] For example, the indicators relevant to the variable tranche of budget aid are almost always related to the quality of the public budget system.[79] In this way, poor performance in the area of governance can be penalized through the reduction of the funds allocated and incentives for improvement can be offered. In the EU's development aid cooperation, conditionality thus takes the form of agreements that rely on a continuous process of interpretation. In addition, it combines a requirement to negotiate with a "soft," and as such not apparent at first glance, sanctions mechanism.[80]

Although this doesn't do away with the fiduciary risks associated with budget aid, the EU's "soft" conditionality, with its reliance on negotiation instead of rewards and punishment, does not prohibit effective control of how funds are used. The institutionalized dialogue and its associated reporting requirements, in combination with systematic results monitoring, make it possible to exert considerable influence on the budget structures and processes of the recipients and as such also on central elements of good governance. It remains to be seen, however, whether such "talks in the shadow of possible sanctions"[81] are appropriate for convincing the recipients of the centrality of good governance and for strengthening ownership of the reforms that are deemed necessary. This will depend not least on the extent to which standard policy recommendations can be avoided and a broad spectrum of stakeholders are included in the political dialogue. In other words, it will depend on the quality of the dialogue itself.

Dilemmas and Conflicting Goals

In contrast to the Millennium Challenge Account (MCA), which places high demands on potential treaty partners, the EU's choice of partners is less discriminating. Even major deficits in the area of the recipient's governmental and administrative behavior are not considered knock-out criteria by the EU. Rather, they are seen as challenges that need to be dealt with in a spirit of partnership. In contrast to the MCA, responsibility lies not only with the recipients. In fact, the principle of "equal partnership," to which the EU's development cooperation is committed, also places high demands on the donors. As a representative of the European Commission put it, the donors "have to accept a difference of views on policy action needs and timing" and political choices should be respected even when they are different from the

75 Article 9 Paragraphs 2 and 3 and Article 96 Paragraph 2 and Article 97 of the Cotonou Agreement as well as Beck and Conzelmann.
76 Schmidt, 41
77 Beck and Conzelmann, 329.
78 Article 3 Annex IV of the agreement.
79 Schmidt, 44.
80 Beck and Conzelmann, 339.
81 Ibid., 342.

beliefs of the donors.[82] It is an open question how realistic such a demand is given the imbalance of power in the relationship between partners. It is also unclear whether the development bureaucracies can live up to the associated demands this places on their own capabilities to learn and engage in dialogue. Technical assistance is generally based on the assumption that reform deficits are above all the result of deficits in knowledge and that it is the donors who have the "right" knowledge.[83] But conditionality conceived as a dialogue demands from the donors that they lower their standards in terms of the efficiency of development aid, at least in the short run, and that they consciously accept the risk of misuse.[84]

The record of the Millennium Challenge Account to date shows that a strategy of selectivity leads to conflicting aims. The strict application of criteria for selecting recipients results in fewer funds being made available for a few high-performing recipients. These recipients are thus flooded with money that they may not even be able to absorb, as they are also preferred partners of other donors.[85] In addition, the focus of allocating funds to a small number of qualified countries contributes little to combating global poverty and inequities in distribution. This is evident when we take a closer look at the contract partners of the Millennium Challenge Corporation (MCC) to date. The poorest countries usually have especially high populations, but the situation is just the opposite in countries supported by the MCA. Moreover, the number of inhabitants stands in inverse proportion to the per-capita support from the MCA. For example, the volume of the compact with Cape Verde, with a population of just a half a million people, is proportionally the highest. The support to the tune of $110 million is the same amount that was allocated to Madagascar, the most populous of the countries supported by the MCA thus far, with 16.4 million inhabitants.[86] The imperative to use funds efficiently thus conflicts with the global objective of reducing poverty and with the call for raising ODA. In order to answer this call, selection standards would have to be lowered.

Another conflict of aims connected with the strategy of selectivity has to do with the dubious objecttivity in the final selection of recipients. The high standards of objectivity and transparency are thwarted by the tendency towards political instrumentalization of the selection process. This lowers the credibility of the program and opens the MCC up to the accusation that they use double standards in their evaluation of the applicants. The EU avoids the conflict between foreign policy interests and global objectives by using soft conditionality. This enables the EU to preserve the foreign and trade policy preferences of the community and its member states while at the same time including difficult partners in the cooperation. In particular, this is true of those states where the conditions for reforms are inhospitable but the need to reduce poverty and social misery is especially high. At the same time, the intervention in the regulatory systems of the recipient states associated with the program-based approach, combined with the institutionalized political dialogue, makes it possible to have long-term influence on the political decision-making process in the partner countries. Given the difficulty of dealing with the problem of bad governance, it is uncertain the extent to which the EU can make use of this situation in order to also promote the democratization of the decision-making process.

82 Gilles Hervio, "Towards Multiyear Outcome-Based Conditionality," Koeberle et al. (eds.), 183–185 (183); see also Article 2 of the Cotonou Convention.
83 Watt, 251f; Morrow, "Adjusting Conditionality," 208f.
84 Schmidt, 63, 89ff.
85 van de Walle, 2; Fox and Rieffel, 18.
86 Fox and Rieffel, 13.

Conclusions and Future Outlook

The disappointing results of development aid intervention have discredited traditional incentive-based conditionality and have unleashed a debate on the effectiveness of development that has been going on since the mid-nineties. It is now generally recognized that sustainable reforms aimed at effectively fighting poverty cannot be imposed, rather they have to be developed and implemented in partnership. This requires a reform-friendly environment and the willingness of the recipient to take responsibility for adopting the donor-supported reforms.

A reformulation of conditionality accompanies the new paradigm of development partnership, which propagates ownership as simultaneously a prerequisite and a goal of effective development aid. The conditions tied to the support provided by donors now aims at increasing the recipients' sense of responsibility for and commitment to reform measures. An innovation of the new conditionality is the introduction of performance-based ex-post conditionality, which makes the allocation of funds dependant on outcomes and not on the implementation of particular measures, and which relies on increased results monitoring. The move away from the traditional project-based approach in favor of program and budget financing is also intended to increase the recipients' ownership and give them more leeway in shaping their reform policies. In exchange, they must be willing to adapt their budget system and allow it to be continuously monitored.

The precept of partnership and the associated emphasis on ownership are basically in tension with the precept of efficiency. Ownership is difficult to measure and is, as such, a relative concept. The complex reforms that the donors' commitment aims at require patience. The effects of the reform measures, which are deeply intrusive in the internal structures of the partner countries, often aren't apparent for many years and the prospects for success are uncertain. The ongoing debate about development aid conditionality is thus not least a reaction to the development policy dilemma of trying to follow two imperatives simultaneously: that of partnership, which serves to provide the recipients self-control over reforms, and that of efficiency, which implies stronger control and regulation by the donor.

In this debate, we can distinguish between two options in the use of conditionality. First, an exclusive approach, which is primarily committed to the efficiency criterion, calls for stricter selectivity in the choice of partners, and focuses the disbursement of funds on demonstrably reform-oriented countries. Second, an inclusive approach, which emphasizes the precept of partnership and conceives of conditionality as knowledge transfer and a learning process. These competing approaches imply different beliefs about social behavior. The strategy of selectivity assumes that actors will make choices in the desired direction when presented with clearly defined, targeted incentives. In contrast, the strategy of dialogue relies on actors whose preferences are not predetermined, but rather gradually crystallize during a process of policy consultation and negotiation. Accordingly, conditionality framed as dialogue aims to win over the recipients for the reform program in a process akin to socialization. In doing so, it hopes to create the conditions that enable the program to be effectively implemented.

A comparison of the policy requirements of the MCA and the EU on the basis of their performance capabilities shows that a strategy of selectivity can hardly be justified in development policy terms and is also not very promising in terms of the efficient use of resources. This is because it is tailored towards exceptional cases, namely to countries with high poverty rates that are also marked by good governance. But it is precisely the poorest developing countries that are largely the bad performers who are caught in a vicious cycle of economic stagnation and poor governance.[87] Overcoming these deficits is in no way simply a matter of the political will of governments, as the strategy of selectivity implies, rather it requires that numerous stakeholders and conditions be taken into consideration that can only be influenced by the governments to a certain degree.

In addition, such a strategy cannot be implemented consistently. In the case of the International Financial

87 van de Walle, 41ff.

Institutions, alone the strong incentive to disburse money stands in opposition to strict selectivity in the choice of recipients.[88] The disbursement practices of bilateral donors is also characterized by established routines and multi-layered interests.[89] Accordingly, the majority of them, including Germany, use "soft" conditionality corresponding to the EU model. A strategy of selectivity would demand from the donors a high degree of transparency and objectivity in the selection of recipients. The prerequisite for that would be a high degree of institutional coherence and extensive substantive convergence of policy areas. But as soon as political considerations in a broad sense or particular interests become part of the decision-making process—which is clearly unavoidable—a strategy of selectivity that aims at effectively reducing poverty looses its credibility.

In contrast, closer observation of EU program conditionality shows that conditionality reformed under the banner of "partnership" does not mean that the donors have to relinquish control. While the interaction between donors and recipients is conceived as a joint problem-solving exercise, the policy dialogue itself is deemed a condition of cooperation and is tied to performance-based allocation of funds and thus subject to sanction. At the same time, the dialogue-based conditionality of the EU avoids discriminating between recipients. As such, it proves to be an elastic model that enables inclusion in two directions by involving difficult neighbors in the cooperation while also being able to integrate the heterogeneous interests of the EU member states. However, for this high risks in the use of funds have to be accepted and standards of efficiency and effectiveness of aid need to be lowered, at least for the short to mid-term.

Contrary to what the donors themselves suggest, the reformed development conditionality does not guarantee that development aid will be more "effective." It is, however, an intelligent procedure for gaining commitment for reform programs that increases the responsibility of the recipients and intervenes deeply in their internal structures. At same time, the responsibility for the impact and the consequences of reform measures tends to be delegated to the recipients.

88 See, for example, Easterly. Also see above, p. 8.
89 Alesina and Dollar; Canavire et al.

Acronyms

ACP	African, Caribbean and Pacific States
BMZ	German Federal Ministry for Economic Cooperation and Development (Bundesministerium für wirtschaftliche Zusammenarbeit und Entwicklung)
CAS	Country Assistance Strategy (World Bank)
CDF	Comprehensive Development Framework (World Bank)
CPIA	Country Policy and Institutional Assessment
DAC	Development Assistance Committee
DIE	German Development Institute (Deutsches Institut für Entwicklungspolitik)
DPL	Development Policy Lending (World Bank)
ESAF	Enhanced Structural Adjustment Facility (IMF)
EU	European Union
IDA	International Development Association
IFIs	International Financial Institutions
IMF	International Monetary Fund
LDC	Least Developed Country
LIC	Low Income Country
LMIC	Lower-Middle Income Country
MCA	Millennium Challenge Account
MCC	Millennium Challenge Corporation
ODA	Official Development Assistance
OECD	Organization for Economic Co-operation and Development
PREM	Poverty Reduction and Economic Management
PRGF	Poverty Reduction and Growth Facility (IMF)
PRS	Poverty Reduction Strategy
PRSC	Poverty Reduction Support Credit (World Bank)
SAP	Structural Adjustment Program
UN	United Nations
UNESCO	United Nations Educational, Scientific and Cultural Organization