Some Unpleasant ODA Arithmetic

Ranil Dissanayake, Atousa Tahmasebi

Abstract

Official development assistance is supposed to be designed to prioritise the economic development and welfare of developing countries. The OECD's Development Assistance Committee is a club of wealthy donor countries which collaborate to set rules and norms to this effect. However, digging into the official data submitted by donors to the OECD reveals some unpleasant truths. We use data on every funding line reported by donors to the OECD between 2006 and 2019 to investigate the pattern and distribution of commitments and disbursements of ODA to developing countries, and discover that ODA is targeted poorly within the group of eligible developing countries; that this group of eligible countries is gradually expanding to include more relatively wealthy places; that aggregate ODA flows are organized and structured sub-optimally; and that ODA responds more to arbitrary income classifications than it should. We suggest informational and incentive reforms in response. These findings also suggest limits to what realistic reform of ODA can achieve, and, consequently, the importance of non-aid development policy for outcomes in developing countries.

Center for Global Development
2055 L Street NW
Fifth Floor
Washington DC 20036
202-416-4000
www.cgdev.org

Center for Global Development
www.cgdev.org

CGD Policy Paper 236
October 2021

Some Unpleasant ODA Arithmetic

Ranil Dissanayake, Atousa Tahmasebi
Center for Global Development

The authors are grateful for excellent research assistance by Bernat Camps and Bhavika Chawla, and helpful comments from Euan Ritchie, Charles Kenny, Nilima Gulrajani and participants at a roundtable held on 29/09/21. All omissions and mistakes that remain are our own.

The Center for Global Development is grateful for contributions from the UK Foreign, Commonwealth & Development Office in support of this work.

Ranil Dissanayake, Atousa Tahmasebi. 2021. "Some Unpleasant ODA Arithmetic" CGD Policy Paper 236. Washington, DC: Center for Global Development. https://www.cgdev.org/publication/some-unpleasant-oda-arithmetic

Center for Global Development
2055 L Street NW
Washington, DC 20036

202.416.4000
(f) 202.416.4050

www.cgdev.org

Contents

Introduction 1

The data 2

Patterns in the use of ODA, 2006–19 4

ODA is not concentrated in the poorest places 4

ODA eligibility criteria are too broad and includes too many wealthy countries 8

ODA remains enormously fragmented, and this problem is not improving in LICs 10

However, ODA is used for different things as countries become wealthier 11

Changes in income classification exert too much influence 13

Discussion and policy recommendations 16

Information and learning channel 17

Behavioural and incentives channel 17

References 19

List of figures

Figure 1. The distribution of ODA across income categories and time....4
Figure 2. ODA per person and per person living in poverty by income group, 2006–19....5
Figure 3. Grant, loan, and equity ODA by income classification over time....5
Figure 4. The evolution of ODA eligibility over time....9
Figure 5. Project commitments in LICs, LMICs, and UMICs....11
Figure 6. Sectoral Distribution of ODA....12
Figure 7. Development outcomes against GNI per capita....13
Figure 8. Average project commitment size (millions) before and after graduation to LMIC status....14

List of tables

Table 1. Number of LICs, LMICs, and UMICs in each year covered 6

Table 2. Average tax as a percentage of GDP for each income group 12

Table 3. Instruments used for economic development spending 13

Introduction

The OECD's Development Assistance Committee (DAC) is the widely accepted arbiter of the definition of official development assistance (ODA) and has taken on the role of promoting better and more cooperative models of providing ODA. Its mandate is broad and ambitious:

> "The overarching objective of the DAC for the period 2018–2022 is to promote development co-operation and other relevant policies so as to contribute to implementation of the 2030 Agenda for Sustainable Development, including sustained, inclusive and sustainable economic growth, poverty eradication, improvement of living standards in developing countries, and to a future in which no country will depend on aid."

In pursuit of this admirable set of goals, the DAC sets the rules for what counts as ODA, operates a club of peer reviewers, and engages with non-members to promote the effectiveness of development cooperation. But even among the club that has tasked itself with making development cooperation "better," there remains much that is—at least—surprising in how ODA is given. This paper looks at the distribution and structure of ODA in the DAC and suggests an unpleasant truth: global ODA is substantially short of optimally organized, even among the DAC donors.

In December 2020, Ranil Dissanayake, Charles Kenny, and Mark Plant set out a framework for assessing the appropriate role of ODA in middle-income countries (Dissanayake et al., 2020). The paper argued that ODA should be used sparingly in middle-income countries, but where it is used, it should be aimed at

1. a major development challenge;
2. where relatively small amounts of finance can be expected to have a significant return;
3. activities consistent with the political economy of the recipient country or that are likely to induce a shift in the political economy.

If donors were acting in line with these recommendations, it argued, we would expect to see the following stylized facts:

1. in absolute terms, more ODA is being used in low-income countries (LICs);
2. the average financial commitment of ODA becomes progressively smaller as recipient GDP per capita increases;
3. the objectives of ODA funded action change as GDP per capita increases and the sectoral distribution of ODA substantially shifts with income classifications;
4. the modalities most used to deliver aid substantially change as incomes increase.

For 2018, at least, Dissanayake et al. found that none of these were clearly true.

This paper extends this analysis in two ways. First, it looks at a much longer time period, and investigates both whether 2018 was a one-off and whether the use of ODA is becoming more or less closely aligned with these expectations. And second, it includes additional analysis: investigating how the eligibility criteria for ODA have led to changes in the make-up and income levels of potential recipients, and how ODA patterns change with graduation to higher-income categories.

The data show that ODA is not only poorly structured with respect to the differentiated challenges faced by countries at different income levels, but it is also—on some dimensions at least—becoming more so. Where changes do occur, they are unduly influenced by the arbitrary line at which income classifications change, rather than responding to the gradual change in income per capita. And regardless of recipient characteristics, ODA is fragmented, administered in unduly small pots, and volatile.

This does not mean that ODA doesn't "work." A great deal of evidence suggests that aid-funded programmes can and do deliver meaningful change.[1] Thus it becomes more important to use it in the right places and in the right ways.

The paper proceeds as follows. We describe the data used to conduct the analysis; report our findings from analysing ODA use among DAC donors from 2006 to 2019; discuss the broader implications of these findings; and conclude with recommendations to shift incentives towards a distribution and use of ODA and developed-country resources more generally towards a more differentiated, higher-impact structure.

The data

We use the OECD's Creditor Reporting System (CRS) project-level data for each year from 2006 to 2019 (prior to 2006, the data was collected on a financial year basis and not strictly comparable to the years selected). The data was pruned to include only DAC donors and to exclude all flows not eligible as official development assistance, and to remove the administrative costs of donors. The data from CRS includes the donor country; the donor agency; the project title; the recipient country; various project characteristics (including its modality, the sector in which it operates, and its SDG, gender and climate focus, if any); and the project's financial information, including commitments and disbursements. All of the data we report in this paper excludes core contributions to multilateral agencies, though it does include bilateral ODA which is implemented through a multilateral partner for a specific purpose or programme (so-called multi-bi aid). For all analysis we further exclude "bilateral unspecified" ODA, which is mainly made up of ODA which is not country programmable and includes administrative costs, ODA spent on refugees in donor countries and some

[1]See, for example, the list of JPAL pilots that have been successfully evaluated and scaled up at https://www.povertyactionlab.org/evidence-to-policy/scaling-evaluated-pilot.

research costs. In other words, we restrict our analysis only to ODA which has a clearly identified recipient or beneficiary country.

Using the WDI package in the statistical package R, we then linked each project line to data on the recipient country income classification (according to the World Bank income groups) that year, its current income classification, its GNI per capita in that year, its population, and its poverty rate. We further link each observation to additional data downloaded from the WDI database directly.

Throughout our analysis, we use the World Bank income classifications, which differ from the OECD's. The World Bank's classifications are simpler, dividing countries into low-, lower-middle, upper-middle, or high-income countries. They focus only on income, rather than non-income development indicators, and by virtue of having a simpler classification criterion are somewhat less susceptible to donor preferences in determining the designation of recipient countries. We use historical data on the income classification of each country between 2006 and 2019 to link our data on the provision of ODA by DAC donors to the contemporary income classification of the recipients (by default the OECD DAC's statistics use today's income classifications for all current and historical data on ODA flows; our data give a better view of how donor flows were allocated according to the country classifications at the time the flows were committed or disbursed).

This is a rich data source. The source data are provided by donors themselves and are thus official. It allows highly disaggregated analysis at the level of individual funding commitments, as well as higher levels of aggregation: by donor, recipient, recipient group (regional, income class), and donor group, over time or pooling multiple years. Combining it with the World Bank WDI data gives it further depth and allows analysis that neither the WDI or the CRS alone allows for.

Unfortunately, it is not perfect. Especially for non-DAC donors, coverage can be patchy. Not all donors report all of the supplementary information with equal care, so there is a great deal of missing data in the climate, gender, and SDG focus markers. And while the data is complete, different donors may define line-items slightly differently. For some it may be a full project; for others it may be a budget line, which could be lower than the project level. And it unfortunately does not allow for subnational geocoding of data. Despite these limitations, this remains the most comprehensive source across multiple donors and years available.

All of the analysis was run using R. Code and data required for reproducing each of these graphs are available on request.

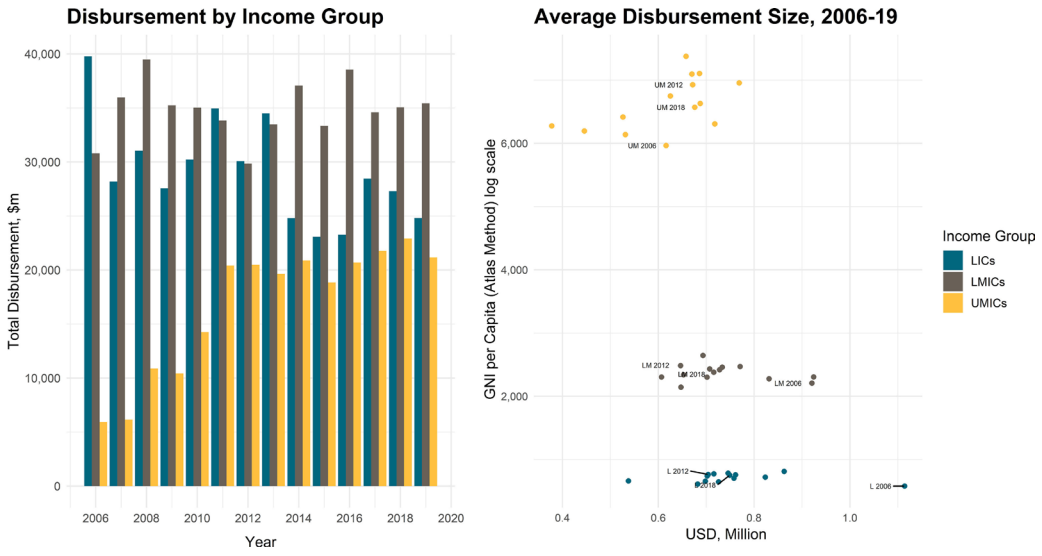
The next section uses this data to investigate trends in how ODA has been structured among DAC donors since 2006.

Patterns in the use of ODA, 2006–19

ODA is not concentrated in the poorest places

Dissanayake et al. (2020) argued that ODA should be used to get resources to the poorest countries primarily, an argument further developed and quantified in welfare terms by Kenny (2021). Nevertheless, this does not appear to be how DAC donors have used ODA in the last 15 or so years. Figure 1 demonstrates that in only three years since 2006 have the total disbursements made to low-income countries been greater than those made to lower-middle or upper middle-income countries. Panel 2 suggests that this is driven by the number of projects undertaken in different places, not their size: in low-income countries, the average disbursement size is around the same size as those in LMICs, and often substantially larger than in UMICs. The difference in total disbursements must therefore be driven by the number of engagements in different income groups.

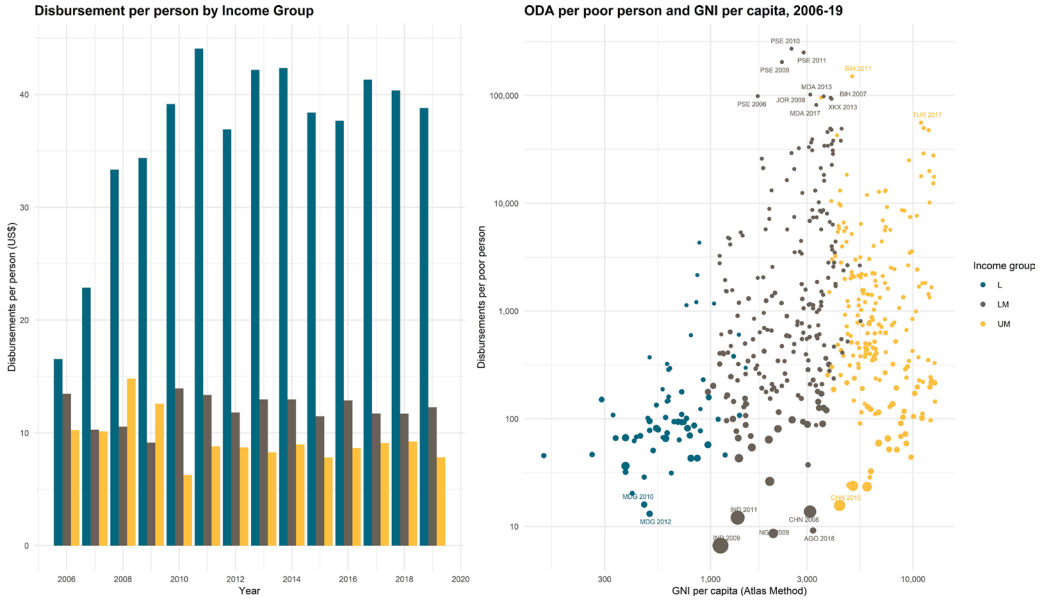
Figure 1. The distribution of ODA across income categories and time



Note: High income ODA recipients are excluded from this graph for clarity. Relatively little ODA was disbursed to HICs in this period, with the most provided in any single year being $450 million in 2014. Each point represents an income group-year.

While presenting the same information in terms of ODA provided per head of population reverses this result entirely, looking at ODA per person living in poverty restores—even emphasises—the original result. Adjusted for the number of poor people in a country, ODA allocations are regressive. Though a couple of the outliers at the top end are driven by large refugee populations (Turkey and Jordan in particular) and at the bottom end by extremely large countries (notably China and India), a regressive trend is apparent even excluding these outliers (Figure 2).

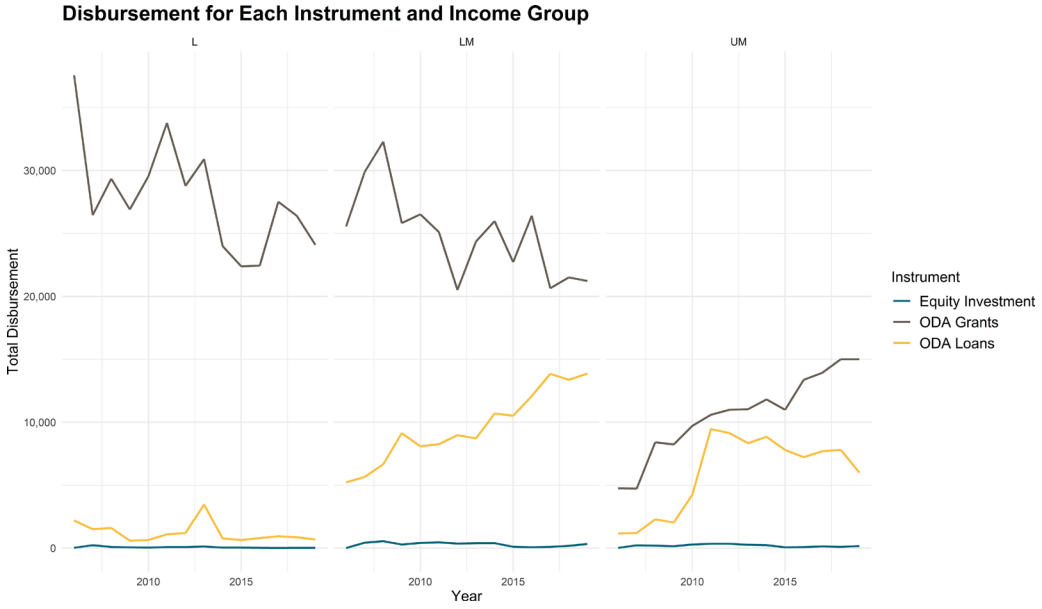
Figure 2. ODA per person and per person living in poverty by income group, 2006–19



Note: The panel on the left shows total ODA disbursements divided by the total population of countries in each income class in each year (using their contemporary classification). The panel on the right shows how much ODA was disbursed per person living in poverty as measured by the World Bank's $1.90 extreme poverty line. Each point is a country-year. The size of the point is proportional to the number of poor people living in the country in that year. It omits 47 data points for which measured poverty was 0% of the population, thus generating an infinite value for disbursements per poor person. Country-years with disbursements of over $50,000 or below $20 per poor person are labelled.

This failure to target the poorest is somewhat ameliorated when we disaggregate ODA flows by type, separating out the use grants from loans and equity support (Figure 3).

Figure 3. Grant, loan, and equity ODA by income classification over time



Since ODA diminishes both in size relative to the recipient economy (Dissanayake et al., 2020) and in its impact on global social welfare (Kenny, 2020) as recipient countries become richer, it makes sense that grants (most concessional resources available), which are most scarce, should focus on the poorest places, while the concessional loans and equity that stretch the money further but come at a cost to the recipient, should be used more in rich places (though still used where appropriate in low-income countries). The observed pattern of ODA provided by the DAC countries since 2006 is in keeping with this approach, but also has room for improvement. LMICs typically receive roughly as much grant financing as LICs over this period. That said, given the decline in the number of LICs since 2006 (Table 1), the high proportion of grant financing still allocated to them suggests that grants are increasingly being focused in fewer poor countries. While the distribution of grant ODA is thus increasingly focusing on the poorest places, the high volume of grant ODA (and the rising proportion allocated to UMICs) do not suggest a ruthless prioritization of the places that can least appeal to alternative funding sources. More likely, this pattern has been driven by the ease of implementing large-scale projects in slightly richer places with greater bureaucratic capacity and where more complementary investments are in place—an international version of the mechanism found by Briggs (2021); though of course, donor realpolitik plays a substantial role as well.

Table 1. Number of LICs, LMICs, and UMICs in each year covered

Year	LICs	LMICs	UMICs
2006	53	55	41
2007	49	54	41
2008	43	55	46
2009	40	56	48
2010	35	56	54
2011[2]	36	54	54
2012	36	48	55
2013	34	50	55
2014	31	51	53
2015	31	52	56
2016	31	53	56
2017	34	47	56
2018	31	47	60
2019	29	50	56

It is also striking that while loans and equity represent a larger share of ODA in richer countries, they do not outweigh the use of grants. This might reflect real limits to the borrowing capacity of LMICs and UMICs, but of the LMICs and UMICs, only 9 countries out of 79 were classed by the UNDP as being highly vulnerable to debt distress (Jensen, 2021). It is similarly notable that LICs receive very little loan or equity ODA. This may be

[2]The increase in number of LICs in 2011 reflects the creation of South Sudan.

sensible, if they are more at risk of debt distress, or there are fewer potentially viable equity investments available (though again, according to Jensen (2021) only 2 LICs were in the high category of debt distress). If loans and equity are not viable modalities in these countries, they should be receiving more of the available grant resources. The observed pattern suggests room for a more strictly prioritised allocation.

What is less clear is exactly *why* this pattern is observed. Gulrajani & Faure (2019) argue—in an analysis of DAC ODA to the BRICS countries—that geopolitical and, in particular, economic diplomacy concerns are privileged in allocation and use decisions. Kenny & Yang (2021) use regression analysis to suggest that while the strongest explanatory factor for how donors allocate their aid is "need" (measured by GDP per capita and population), and the next strongest is "donor ties" (that is, colonial or trading links), but that around half of the variance in allocation across countries is unexplained. So, though realpolitik and geopolitical concerns may be a major factor in deciding allocations, roughly half of the allocation is driven by other factors. DAC donors may argue that it is rational for donors not to spend in the poorest places if it is genuinely too difficult to achieve anything with the resources, though the level of effectiveness required in LMICs and UMICs over LICs to make substantial spending in them welfare-maximizing is very high (Carter et al., 2015), especially given the substantially lower poverty incidence among even LMICs compared to LICs. And if existing structures are unable to operate in LICs as effectively as in LMICs or UMICs, this suggests that existing structures may not be fit for purpose. Donors may prefer to spend in places which show signs or conditions for take-off or rapid development,[3] but it is not clearly the case that more of these are middle- than low-income countries. For the most part, both low and lower middle-income countries are making slower progress than ideal; models for how to support pockets of development on the one hand, and those left behind on the other, are needed in both.

This suggests that the case for at least exploring alternative models of ODA management and use, and encouraging greater risk tolerance among donors, to allow for greater spending in poorer places is strong. It won't affect that portion of the allocation driven by politics, but that still leaves a great deal in play. The Istanbul Programme of Action commits donors to provide 0.15–0.2 percent of their GNI in ODA to least developed countries (LDCs). Most donors have fallen well short of this, with only Denmark, Luxembourg, Norway, Sweden, and the UK meeting this benchmark in 2018–19.[4] The OECD-DAC has invested substantially in establishing principles for effective aid spending, most prominently through its four High-Level Fora for aid effectiveness starting in 2002 (Rome, Paris, Accra, and Busan), and before that through the publication of its Development Assistance Manuals and related documents dating back to at least the 1980s. However, it's notable throughout that this work has tended to focus on *how* to do aid projects well in any given country; there

[3] And indeed, when such signs are observed donors should be particularly quick and generous with their support.
[4] See table 31 ("Aid from DAC countries to least developed countries"), accessed 19/10/21 at: https://www.oecd.org/dac/financing-sustainable-development/development-finance-data/statisticsonresourceflowstodevelopingcountries.htm. Whether the UK maintains this in the wake of brutal cuts to ODA is uncertain to say the least.

are few references to which countries should receive ODA. This may not be surprising; from the outset, with the Paris Declaration, the aid effectiveness agenda focused on donor internal processes. This was followed by the move in Busan to incorporating more recipient perspectives into the agenda, leaving little space for recommendations over which countries to prioritise.

Indeed, the OECD's own list of eligible recipients is notably broad, including a number of quite well-off places. Its list of countries eligible for ODA in 2021 includes substantially more upper-middle-income countries than low- or lower-middle-income countries (DAC, 2021). If DAC donors are restricting their operations in poor places in order to spend on more reliable progress in richer places, this suggests their risk tolerance is far too low (even after accounting for the impact of donor-recipient ties on allocation), given the magnitude of potential welfare gains available in poorer places, or that the permitted list of destinations for ODA is too broad, or both.

The DAC cannot directly affect the risk tolerance of different donor countries, but it can reframe its own work on aid effectiveness by explicitly accepting that in some of the poorest places in the world there are greater delivery risks. While these should be managed as far as possible, they must also be accepted as part of the cost of supporting the poorest. Meanwhile, the DAC has direct control over the permitted list of destinations for ODA, its most direct tool for helping to focus ODA where it can do the most good. Unfortunately, the list has no such ambitions.

ODA eligibility criteria are too broad and includes too many wealthy countries

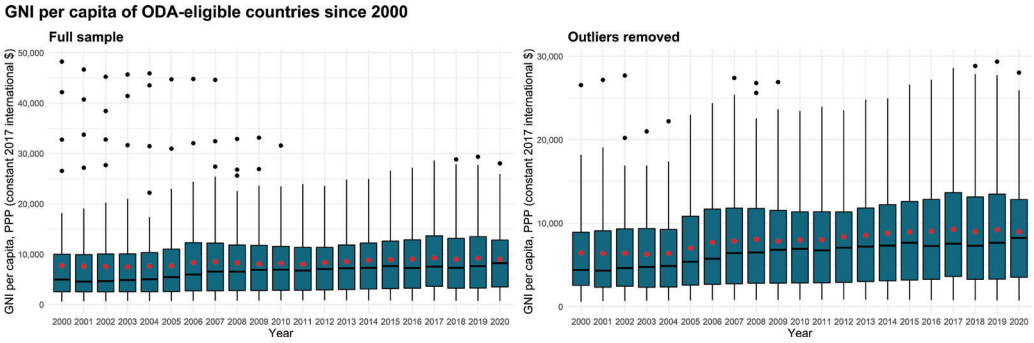
The DAC's objective in setting out a list of ODA-eligible countries is explicitly not to help prioritise or focus ODA. Indeed, it says, "The DAC List of ODA Recipients designed for statistical purposes. It helps to measure and classify aid and other resource flows originating in donor countries. It is not designed as guidance for aid or other preferential treatment."[5] This much is clear from even a cursory glance. Figure 4, below, plots the GNI per capita of every country eligible to receive ODA for each year from 2000 to 2020; the teal box represents the range from the 25th to the 75th percentile of eligible recipients (the interquartile range), the median eligible recipient is represented by the black horizontal line, the vertical black lines represent countries within 1.5 times the interquartile range and the black dots are outliers. Panel 1 includes the full data set; panel 2 excludes three outliers (Saudi Arabia, Bahrain, and Oman) which received little ODA during this period.[6]

---

[5] "History of DAC Lists of aid recipient countries," accessed on 13/09/21 at: https://www.oecd.org/development/financing-sustainable-development/development-finance-standards/historyofdaclistsofaidrecipientcountries.htm.

[6] Bahrain received no aid from DAC donors in this period. Both Saudi Arabia and Oman received small amounts, with the most in any given year amounting to $12 million to Saudi Arabia in 2007; no aid was disbursed to Saudi after this year, and none to Oman after 2010.

Figure 4. The evolution of ODA eligibility over time



Note: The teal box presents the inter-quartile range of GNI per capita (the 25th percentile to the 75th percentile); the whiskers capture observations within 1.5* the interquartile range and the black dots are outliers. In panel 2, only the most extreme outliers are removed. The red dot is the mean GNI per capita of eligible recipients; the black line is the median.

The ODA eligibility criteria are extraordinarily generous: countries with a GNI of almost $50,000 per person (in purchasing power parity terms, i.e., measuring purchasing power and accounting for price differentials across space) have been eligible at some point or another since 2000. Excluding the most egregious outliers in this period makes the picture less startling but reveals an equally worrying fact: the range of incomes of ODA-eligible countries has been growing, even as the number decline, while both the mean and median GNI per capita of recipients has been rising. While there has been little change among the poorest ODA-eligible countries (the "floor" has not risen appreciably since 2000), there has been rapid growth at the other end (again, omitting outliers). Even for a list designed purely as a statistical counting aid, this is striking. The rules it follows have allowed for a widening of the legitimate use of ODA to include relatively richer places despite the continued clustering of many countries towards the lower end of the income spectrum. At the very least, it has failed to disincentivize the use of ODA in wealthier places or to encourage a focus on poorer recipients. Instead, the rules condone the use of ODA in small but relatively wealthy places, such as Montenegro and St. Lucia—and indeed, until quite recently, Saudi Arabia. If all donors treated ODA purely as a statistical accounting category, as the DAC does, this would not matter; but given the increased use of input targets among donor countries over the last couple of decades, spending on richer places crowds out spending in poorer ones for at least some donors. An analysis of countries that graduate from eligibility suggests that most donors do not simply use the list for statistical counting purposes: those countries that received ODA in the years immediately before graduating from eligibility see a sudden cessation of ODA which is not replaced in subsequent years by other official flows. The DAC could discourage this with tighter rules on graduation from eligibility, though of course this battle would likely be messy and difficult.

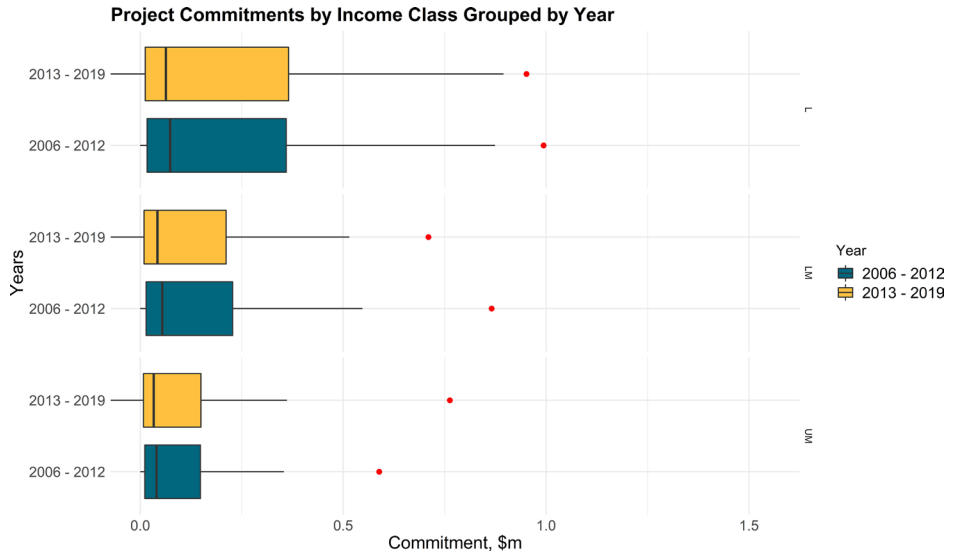
That said, since the DAC is formally silent on the allocation of ODA in its work on aid effectiveness, it is unsurprising that some DAC members give ODA to rich places. However, the performance of DAC members is hardly more encouraging even on those aspects of aid effectiveness that it does offer stronger advice on.

ODA remains enormously fragmented, and this problem is not improving in LICs

The High-Level Fora on Aid Effectiveness and even the much-earlier Development Assistance Manuals all, in various ways, argue for a reduction in the transaction costs incurred by recipient countries in receiving and using ODA.[7] This message does not appear to have been acted upon. The box-and-whiskers graphs in Figure 5 show the range of commitment sizes by project in the first and second half of the period covered for LICs, LMICs, and UMICs. It excludes all ODA without a clearly identifiable recipient or beneficiary country (i.e., all 'bilateral unspecified' ODA, and administrative costs of donors). The boxes show the interquartile range of commitment sizes (that is, the 25th to the 75th percentile of commitments). The vertical black lines show the median commitment size. The horizontal black lines show the range covered by outliers (defined as 1.5 times the interquartile range), and the red dot shows the mean commitment size. The fact that for each income group, the mean is either beyond the outliers or right to their furthest extent shows that the vast majority of the value of commitments is made up by a few huge outlier commitments. The remainder are typically very small indeed, with median commitment sizes of around $100,000 for LICs, and even smaller for LMICs and UMICs. These figures aren't wholly reliable: some donors provide commitment data at sub-project level, and not all ODA imposes a transaction cost on the recipient country government, but even if they are out by half, this suggests rather too many projects are far too small to make a serious impression in the context of even a low-income country economy. We should exercise some caution on this point: the argument is not simply that bigger is always better; rather it is that a preponderance of very small projects is unlikely to be optimal. What's more, fragmentation is not falling over time. The transactions costs of a portfolio made up disproportionately of tiny projects is likely to be very high. Donor behaviour has not kept up with rhetoric.

[7] This analysis considers transactions costs arising from fragmentation at the project level, rather than the donor level. While research on fragmentation at the donor level has been found to have mixed effects (see, for example (Gehring et al., 2017)), fragmentation at the project level can be problematic for both donor and—when it requires engagement from recipient governments—at the recipient level (for example in (Dercon, 2014) the then-DFID chief economist demonstrates in an internal DFID policy note, cited with permission, that small projects require an outsized return on investment compared to large projects to justify the time cost of management).

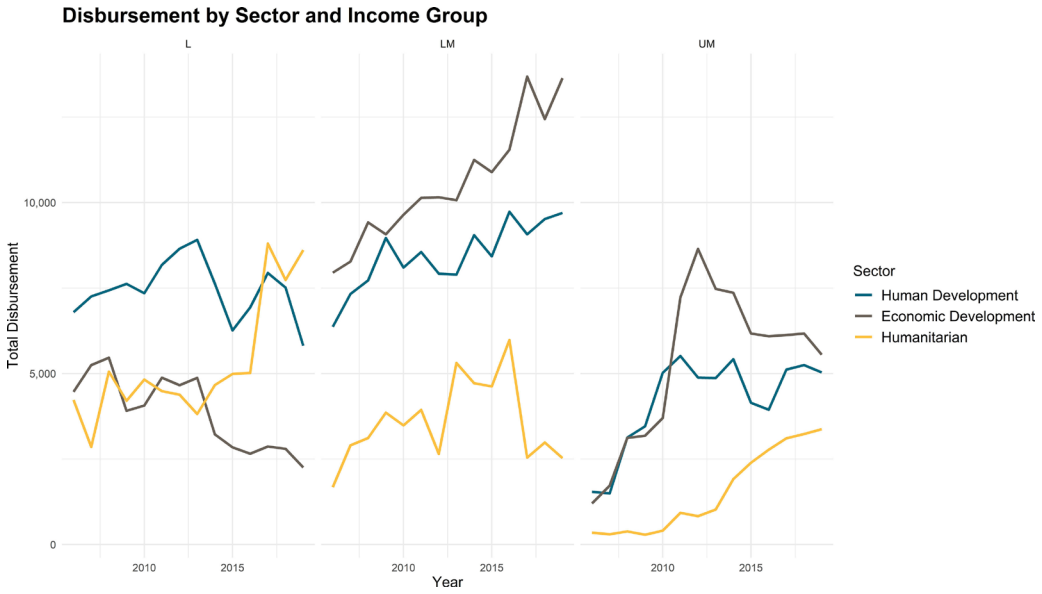
Figure 5. Project commitments in LICs, LMICs, and UMICs



However, ODA is used for different things as countries become wealthier

As Dissanayake et al. (2020) argued, the challenges for which ODA is most suited will become different as countries get richer. This is borne out in the data; we observe that countries receive aid for different things as they become wealthier. The poorest countries are—increasingly—recipients of humanitarian aid, which partly reflects that many of the countries that have remained low income since 2006 have been disproportionately likely to be fragile or conflict-affected, or prone to natural or human-caused disasters. By contrast, humanitarian spending is relatively less common among LMICs, which are more able to finance their own response to some extent (Figure 6). In recent years, there has been an increase in the proportion of humanitarian spending in UMICs, a trend driven almost entirely by spending in Iraq, Lebanon, Turkey, and Jordan, partly (in some of these countries) in response to their role in hosting refugees from the conflict in Syria.

Figure 6. Sectoral Distribution of ODA



Note: Sectors are grouped as follows: **1. Human Development includes**: "Education" (*Unspecified level, Basic Education, Secondary Education, and Post-Secondary Education*); "Health" (*General Health, Basic Health, Non-communicable diseases (NCDs), Population Policies/Programmers & Reproductive Health*); "Water Supply and Sanitation"; **2. Economic Development includes:** "Infrastructure and Energy" (*other Social Infrastructure & Services, Transport & Storage, Communications, Energy Policy, Energy generation, renewable sources, Energy generation, non-renewable sources, Hybrid energy plants, Nuclear energy plants, Energy distribution*); "Banking, Business, Financial Service"; "Industry, Mining and Construction"; "Tourism"(*Trade Policies & Regulations, Tourism*) **3. Humanitarian includes**: Refugees in donor countries, Disaster and Emergency Relief (*Emergency Response, Reconstruction Relief & Rehabilitation, Disaster Prevention & Preparedness*). We report only these sectors in this graph for clarity, so the total amount of ODA reported is less than in previous graphs.

It is surprising, however, that spending on the human development sectors in middle-income countries still account for so much ODA: as much is spent in this area in middle-income countries as in low-income countries. While supporting those left behind in LMICs may often be an appropriate area for donor support, in the first instance, such action should be self-funded, as they are much more capable of funding such spending themselves. This argument applies much less to support for refugees, especially given the uneven distribution of refugees across the globe, though this may affect the humanitarian more than the human development sectors.

Table 2. Average tax as a percentage of GDP for each income group

	2006	2011	2016	2019
LICs	11.2	11.8	13.2	12.4
LMICs	20.0	19.1	14.9	17.6
UMICs	18.9	17.7	16.6	15.4

The much higher spending on economic development in richer countries is less surprising, given that there are likely to be more opportunities for productive investment in more diverse, advanced economies, and that such spending is much more likely to be financed from

ODA loans than pure grants (though one could equally argue that the problem of economic development is most acute in low-income countries, by definition). In total, 52 percent of economic development spending was in the forms of loans, 45 percent in the form of grants, and 2 percent equity. It is reassuring, however, that the use of grants in at least this sector is much more prevalent in poorer places.

Table 3. Instruments used for economic development spending

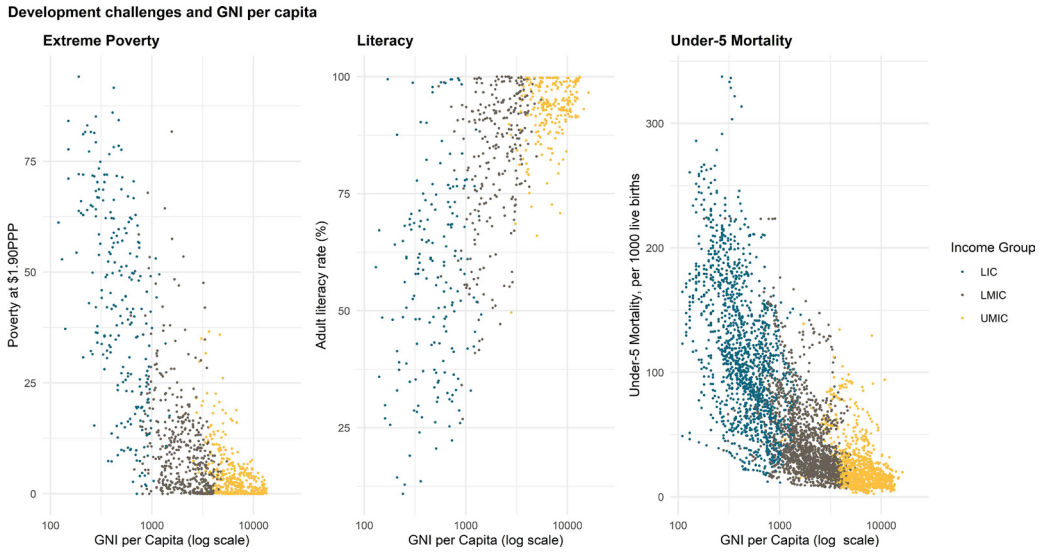
	Equity Investment	ODA Grants	ODA Loans
LIC	1%	91%	8%
LMIC	3%	37%	60%
UMIC	3%	36%	61%

These findings suggest that, though the overall distribution of resources by country is likely to be some way short of optimal, the relative focus of effort in different kinds of countries is, at least, driven by the different kinds of challenges they face.

Changes in income classification exert too much influence

Throughout this paper, we have used income classifications as a convenient shorthand for dividing countries into poorer and richer groups. This can be helpful when comparing if ODA is managed in a qualitatively different way in different kinds of countries. But the great disadvantage of using these categories is that there is relatively little difference between a country just below the LMIC income cut-off and one just above it. They fall under different income classes, but they are likely to face similar challenges with respect to poverty, child mortality, education, and the like, as figure 7 demonstrates.

Figure 7. Development outcomes against GNI per capita

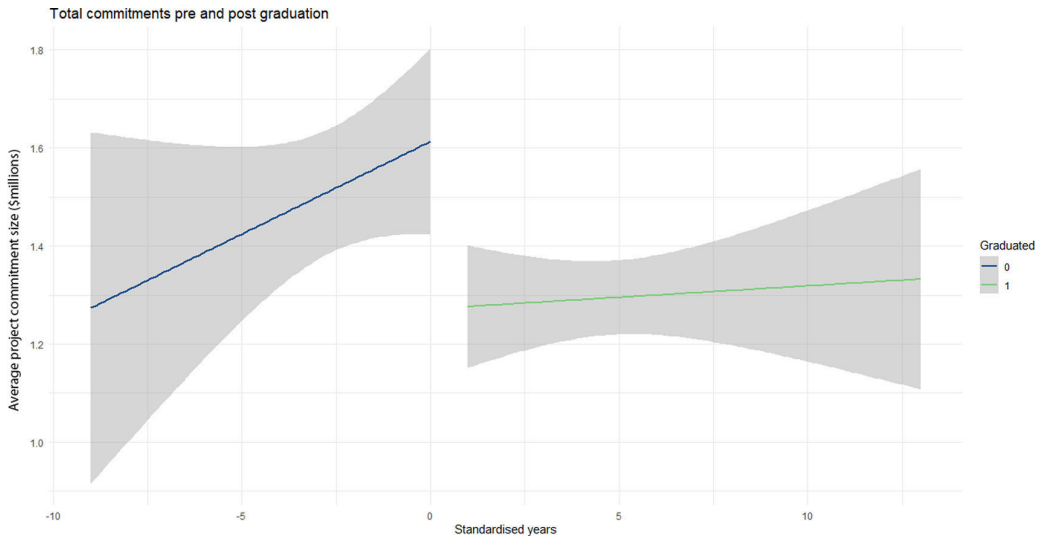


Note: Each dot is a country-year. Income classes are contemporaneous.

While comparing averages within the income categories can be helpful, dividing countries into "rich" and "poor" will always involve some arbitrary cut-off, since the income classification line itself is not particularly informative about the needs and capacities of countries just above or just below it. Accordingly, though we should expect that countries above the LMIC line will, *on average*, be treated differently than those below the line, this is because the groups above and below the line are mainly made up of countries that are not very close to it. However, this does not mean we would encourage the treatment of countries just above and just below the income cut-off to be very different, and still less would we want the act of vaulting the cut-off to materially change the way they receive ODA. In other words, as countries become richer and move into LMIC status, we should observe that the ODA-funded projects and activities donors undertake there in their last years of being a LIC and the first years of being an LMIC are rather similar.

To test whether this is the case, we construct a new dataset limited to countries that graduated from LIC to LMIC status during the period covered (29 countries), and create a new running variable that tracks, for each country, how far it is from the year in which it graduates. This means standardising the data so that the year of graduation for each country that ever crosses the LIC/LMIC boundary during the period under consideration is set to 0.[8] Years before graduation are negative and years after graduation are positive. Analysing how project support evolves as countries approach and cross the threshold to low-middle income status reveals, contrary to what we should expect, a clear discontinuity around graduation (Figure 8).

Figure 8. Average project commitment size (millions) before and after graduation to LMIC status



Donors reduce the size of new project commitments made to countries when they become LMICs. Since this data is limited to bilateral aid, this does not reflect changes to the recipients' ability to access multilateral resources—it is purely a result of bilateral donor

[8] Graduation dates can be found here.

behaviour. Project commitments increase as countries approach the LMIC threshold—suggesting that donors plan or implement slightly larger projects in countries that are growing and approaching graduation.[9] Once graduation is achieved, however, there is a drop in the average size of donor-funded activity in the country, which gradually increases again as LMIC status is consolidated.

While we perhaps shouldn't get too exercised over a relatively small drop in the average commitment size made, this is exactly the opposite of what we would hope for: little change immediately after graduation, when the conditions and problems faced by the country are unlikely to suddenly change, and then a gradual change in the pattern of ODA spent in country as they continue to grow or consolidate their middle-income status. It suggests, as does much of the foregoing analysis, that donors are responding to signals that are at least imperfectly correlated with optimal aid distribution and organization strategy. It's not entirely clear why this pattern is observed, and the data available do not offer an insight into donor motivation. It may be that the LIC/LMIC/UMIC heuristic carries undue weight with donors when setting spending priorities; or it may be that movement across boundaries tends to focus attention to the movers when budgets are set; or it may be that in the years immediately after a jump in income classification there are specific concerns around being seen as too generous (for example, if negative press stories are more common when aid is given to countries who are making clear progress). The common thread to these explanations is that the thresholds create internal incentives for sub-optimal behaviour on the part of donors.

This, together with our analysis of the increasingly expansive definition of ODA eligibility over time, in turn opens the question of how classification of developing countries for statistical and policymaking purposes happens, and how it can be improved. The World Bank's income classifications are relatively difficult to manipulate: they are based on long-established cut-offs and updated to account for inflation over time using a predetermined approach (Hamadeh et al., 2021). The OECD's are more complex, combining the UN's classification of least developed countries with World Bank income classifications, and a rather flexible rule that countries that achieve high-income status for three years in a row will graduate from ODA eligibility (the most recent list is replete with negotiated exceptions).[10] In each case, however, the cut-offs are arbitrary; a convenient shorthand that can be used in policy decisions to provide a veneer of rigour which nevertheless provides little empirical basis for those decisions (Kenny, 2014).

While eliminating discretion (and applying a more restrictive cut-off) would make the DAC's categorisation more closely focused on poorer countries, any system that depends on income classifications to determine the volume or type of assistance is likely sub-optimal due to the lack of any real discontinuity of performance on any development metric around any given cut-off. Any income-based cut-off will face this problem; a more sensible approach might be

---

[9] This could reflect that donors are more willing to "gamble" on larger individual commitments where countries are clearly on a positive path, or that it is easier to administer aid in growing or richer countries.

[10] See World Bank Country and Lending Groups at https://datahelpdesk.worldbank.org/knowledgebase/articles/906519-world-bank-country-and-lending-groups.

a kind of graduated "taper rate" for ODA counting analogous to that used for tax credits.[11] That said, what such a system gains in de-emphasising arbitrary income classifications, it may lose through its complexity and in the inevitably contested choice of taper rates.

Discussion and policy recommendations

The fact that DAC members (and indeed the DAC itself) have great scope to improve the overall allocation of and administration of ODA does not mean that it is failing in its mission to improve the quality of ODA. It is quite likely that in a counterfactual world in which the DAC, with its rule-setting and peer-reviewing function, does not exist, ODA would be even worse than we observe.[12] The DAC has an extremely difficult job, navigating competing political interests to generate a shared understanding of what ODA is and should be; it is unsurprising it cannot force commitment to perfection in how ODA is provided.

That said, the foregoing analysis should not be comfortable reading for DAC member countries. Though the political difficulties in agreeing rules make any set of reasonable restrictions an impressive achievement (Hynes & Scott, 2013), there is an uncomfortably broad scope to use ODA inefficiently within the rules that have emerged (see, for example, Ritchie, 2020, 2021). Though some of this scope would be closed with tighter, more considered rules, nothing prevents members from providing ODA more effectively than the rules mandate. The failure to efficiently and effectively pursue the maximization of global utility is down to the policy choices made by DAC members, and their willingness to trade political expediency for global good (or even just their unwillingness to implement reforms to how their donor agencies operate).

The observed pattern of ODA suggests:

1. ODA could be reallocated across countries to do more good than it currently does;
2. ODA could be restructured in any given time and place to be more efficiently administered; and
3. ODA could be better allocated over time, in particular responding more sensibly to changes in recipient country conditions.

This, in turn, suggests that while the fight to protect or increase ODA budgets is an important one (with France taking steps to improve its aid and the UK moving in the other direction), there is also substantial mileage to be gained in simply improving how what is already provided is allocated.

---

[11] For a clear, simple explainer of taper rates in the context of UK tax credits, see Lisa Stidle's 2015 blog post, "93% tax?! Effective Marginal Tax Rates Explained," at https://policyinpractice.co.uk/93-tax-effective-tax-rates-explained/.

[12] Personal experience from 10 years as a senior adviser in one DAC member agency suggests this is, indeed, extremely likely—ministerial and government preferences were often restrained by reference to DAC rules.

We make proposals below designed to improve the situation through two channels: an information and learning channel, and a behavioural/incentive channel.

Information and learning channel

- The DAC should report as standard how the current stock of commitments for each DAC member are distributed by both GNI per capita of recipients relative to other DAC donors, and relative to the distribution of eligible countries. This would be a minor amendment to the existing Development Finance dashboard,[13] but would give a sense of whether donors are focused on the richer or the poorer end of eligible DAC countries.
- This should be supplemented by annual analysis of whether the new commitments reported by each donor serve to make their portfolio more or less pro-poor.
- Alongside this, data on fragmentation of projects and the use of different modalities in different kinds of countries should form part of the "donor dashboard" generated by the routine statistics already collected by the DAC.

These suggestions are light-touch amendments to what the DAC already does well. They should also be uncontroversial. If the ODA eligibility threshold is purely a statistical counting category, a way of comparing how the distribution of each donor's aid differs from the eligible population of countries simply allows an at-a-glance view of how their ODA is allocated in practice compared to those it could be offered to. And the data on fragmentation and modalities would not be new: it has previously been reported as part of the High-Level Fora on Aid Effectiveness and by recipient countries themselves. Though it can be argued that DAC members may not welcome this additional scrutiny and will undermine attempts to implement it, it involves relatively little change to what is already presented. And, notably, such analysis is already quite possible, and can be undertaken by any research institution or think tank using the existing public information the DAC makes available.

However, both could change donor decisions and behaviour. Separate analysis (Dissanayake & Camps, 2021) suggests that many donor officials have inaccurate beliefs about the actual distribution of ODA their agency gives. In general, most donor officials believe their agency is more pro-poor than it actually is, and that it should be more pro-poor than they believe it is. Perhaps better information may help shift—at the margin—some of their spending choices.

Behavioural and incentives channel

However, it is likely that a simple information intervention will not be enough to seriously shift the practice of ODA allocation and implementation among most donors. The DAC can

---

[13] Which currently simply reports the distribution of ODA across income classifications, without any benchmarking at all. See https://public.tableau.com/views/AidAtAGlance/DACmembers?:embed=y&:display_count=no?&:showVizHome=no#1.

consider changes to its rules or processes to incentivize a shift to more targeted aid, although it may open a minefield in doing so (indeed, it invites the possibility that the fragile consensus it holds together cracks or embraces even less development-focused outcomes than those currently embodied in its counting rules). Three possible reforms are suggested, though all are likely to be difficult.

- DAC peer reviews could be supplemented or replaced by independent evaluations—or even an independent check, empowered to make judgements over how well ODA is allocated and structured, and to investigate the impact (or expected impact) of the portfolio of each donor. The expected impact will depend not only on what they do, but where they do it. The Istanbul Programme of Action provides a useful justification for at least part of this. Though effectiveness is at the heart of the DAC's mission, it is typically pursued through analysis or reform of process; an assessment of expected impact, drawing on the allocation of ODA, its programmatic structure, and the specific programmes adopted might incentivize donors to strengthen their portfolios.
- The DAC could tighten rules on ODA eligibility, or even outsource decisions to an independent committee. The existing drift of ODA eligibility to a richer subset of countries makes a focus on poorer places more difficult to maintain or advocate for. As long as ODA eligibility is broad, at the margin some allocation decisions with minimal development impact will be made.
- Given relatively little success in translating the energetic, but process-driven aid effectiveness agenda into tangible changes in how ODA is delivered, the DAC could signal a shift towards an impact-focused agenda. Switching from tackling the management and institutional arrangements around ODA to tackling the content of ODA programmes may have both more impact on final outcomes and be more tractable, given how difficult a nut the institutional arrangements governing the allocation and management of financial resources has been to crack.

These are stronger signals that the DAC could send to member states to strengthen the existing use of ODA—though it should be noted that they are not mutually exclusive of the recommendations made under the information and learning channel. Though under the current system, it's quite possible for a donor to pursue an "optimal" ODA strategy, and indeed some may approximate one, it's also easy to give aid to countries that don't need it, in ways they find hard to use, and in modalities that are not well-suited to the problem. Any close reading of ODA statistics makes these failures plain. Especially when ODA volumes are under pressure, giving with greater impact should be a policy priority.

A more radical conclusion is also possible: that after more than a decade of concerted effort from dedicated and high-quality bureaucrats at the OECD, and after much political negotiation and skilful manoeuvring, patterns of ODA haven't changed much. Perhaps the time has come to shift the focus of development discourse away from financial flows and focus much more firmly on policymaking in developed countries, at regional and international levels, and in developing countries themselves. Policymaking at these levels may not prove much more malleable, but may well have a much larger impact when it does move.

References

Briggs, R. C. (2021). Why Does Aid Not Target the Poorest? *International Studies Quarterly*. https://static1.squarespace.com/static/5acc1ee17e3c3a103525fb2b/t/60a19b4363de2f0a135743a0/1621203782570/Briggs+%282021%29+Aid+poorest.pdf

Carter, P., Postel-Vinay, F., & Temple, J. (2015). Dynamic aid allocation. *Journal of International Economics*, *95*(2). https://doi.org/10.1016/j.jinteco.2014.11.005

DAC. (2021). *DAC List of ODA Recipients Effective for reporting on 2021 flows*. https://www.oecd.org/dac/financing-sustainable-development/development-finance-standards/DAC-List-ODA-Recipients-for-reporting-2021-flows.pdf

DAC 2021. (n.d.). *DAC List of ODA Recipients Effective for reporting on 2021 flows*. Retrieved September 21, 2021, from https://www.oecd.org/dac/financing-sustainable-development/development-finance-standards/DAC-List-ODA-Recipients-for-reporting-2021-flows.pdf

Dercon, S. (2014). When small isn't beautiful. *Unpublished, Internal DFID Analysis*.

Dissanayake, R., Kenny, C., & Plant, M. (2020). What Is the Role of Aid in Middle-Income Countries? In *Center for Global Development*. https://www.cgdev.org/sites/default/files/PP201-ODA-MICs.pdf

Dissanayake, R., Camps, B. (2021). Progressive, Optimistic, and Misinformed: What Donor Officials Believe about ODA Allocations. In *Center for Global Development*. https://www.cgdev.org/publication/progressive-optimistic-and-misinformed-what-donor-officials-believe-about-oda

Gehring, K., Michaelowa, K., Dreher, A., & Spörri, F. (2017). Aid Fragmentation and Effectiveness: What Do We Really Know? *World Development*, *99*, 320–334. https://doi.org/https://doi.org/10.1016/j.worlddev.2017.05.019

Gulrajani, N., & Faure, R. (2019). Donors in transition and the future of development cooperation: What do the data from Brazil, India, China, and South Africa reveal? *Public Administration and Development*. https://doi.org/10.1002/pad.1861

Hamadeh, N., Metreau, E., & van Rompaey, C. (2021). New World Bank country classifications by income level: 2021–2022. *World Bank Blogs*. https://blogs.worldbank.org/opendata/new-world-bank-country-classifications-income-level-2021-2022

Hynes, W., & Scott, S. (2013). The Evolution of Official Development Assistance: Achievements, Criticisms and a Way Forward. *OECD Development Co-Operation Working Papers*. https://www.oecd.org/dac/financing-sustainable-development/development-finance-standards/Evolution%20of%20ODA.pdf

Jensen, L. (2021). Sovereign Debt Vulnerabilities in Developing Economies Which countries are vulnerable and how much debt is at risk? In *United Nations Development Programme*. https://www.undp.org/sites/g/files/zskgke326/files/publications/54241%20-%20UNDP%20WP%20Debt%20Vulnerability-web.pdf

Kenny, C. (2014). The Strange and Curious Grip of Country Income Status on Otherwise Smart and Decent People. *Center for Global Development*. https://www.cgdev.org/blog/strange-and-curious-grip-country-income-status-otherwise-smart-and-decent-people

Kenny, C. (2020). Official Development Assistance, Global Public Goods, and Implications for Climate Finance. In *Center for Global Development*. https://www.cgdev.org/sites/default/files/PP188-Kenny-ODA-GPGs-Full.pdf

Kenny, C. (2021). We Should Be Spending More of Available Aid in Poorer Countries, Not Less. *Center for Global Development*. https://www.cgdev.org/publication/we-should-be-spending-more-available-aid-poorer-countries-not-less

Kenny, C., & Yang, G. (2021). Why Do Some Donors Give More Aid to Poor Countries? *Center for Global Development*. https://www.cgdev.org/sites/default/files/Why-Some-Donors-Give-More-Poor-Countries.pdf

Ritchie, E. (2020). New DAC Rules on Debt Relief – A Poor Measure of Donor Effort. *Center for Global Development*. https://www.cgdev.org/sites/default/files/WP553-Ritchie-DAC-Debt.pdf

Ritchie, E. (2021). Accounting Anomalies and Arbitrary Targets are Conspiring to Hurt the Poor: SDRs, the UK Aid Ceiling, and Fiscal Trickery. *Center for Global Development*. https://www.cgdev.org/sites/default/files/SDRs-and-UK-aid.pdf