



Good Governance, Aid Modalities and Poverty  
Reduction: Linkages to the Millennium Development  
Goals and Implications for Irish Aid

**Research project (RP-05-GG) of  
the Advisory Board for Irish Aid**

The Advisory Board for Irish Aid  
An Bord Comhairleach do Chúnamh Éireann



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## Working Paper 5

### Measuring Governance: What Guidance for Aid Policy?

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August 2007



### **Disclaimer and acknowledgements**

The views presented in this paper are those of the authors and do not necessarily reflect the views of the Advisory Board for Irish Aid or those of any of the organisations in the research consortium implementing the project.

The authors thank Bill Morton of the North-South Institute for comments on a previous draft, and Jo Adcock (ODI) for excellent editorial assistance. Responsibility for the content of published version remains with the authors.

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# List of Acronyms

BTI	Bertelsmann Transformation Index
CPIA	Country Policy and Institutional Assessment
DFID	UK Department for International Development
EDF	EC European Development Fund
EIU	Economist Intelligence Unit
GII	Global Integrity Index
H&A	Harmonisation and Alignment
ICS	Investment Climate Survey
IDA	International Development Association
IRAI	IDA Resource Allocation Index
KKZ	Kaufmann-Kraay-Zoibo-Lobaton Indicators
MCA	Millennium Challenge Account
MCC	Millennium Challenge Corporation
OECD-DAC	OECD Development Assistance Committee
PRS	Poverty Reduction Strategy
Sida	Swedish International Development Co-operation Agency
SWAps	Sector-wide Approaches
WBI	World Bank Institute
WGA	World Governance Assessment

# Executive summary

There is widespread agreement that governance matters – intrinsically, as well as for improvements in socio-economic outcomes and for aid effectiveness. This raises a set of broad policy questions about how best to rigorously and systematically link aid policy to governance situations in developing countries.

The paper has four main analytical sections. Section 2 provides a brief summary of the literature on the importance of governance for development and aid effectiveness. Section 3 focuses on two main sources of governance data that cover developing countries and the associated opportunities and limitations, and that are produced regularly, namely: (i) the World Bank's Country Policy and Institutional Assessment (CPIA), which focuses on development management issues; and (ii) Kaufmann and Kraay's six aggregate governance indicators which are broader in issue coverage. The section emphasises that while governance data can certainly help with management decisions, they should be used with care since they are based on perceptions and have significant margins of error. Donor judgment is important, however, and to further inform their work, donors also increasingly carry out qualitative political, governance or political-economy assessments of partner countries.

Section 4 focuses on how Irish Aid partner countries and other potential partners 'look' through different governance assessment lenses. One key issue is that categorisation depends on the donor approach to governance issues – whether the focus is limited to development management for growth or how much issues of voice, human rights and democracy also matter. The second issue is that, given the limitations of the data, only loose categorisation is possible.

Section 5 explores how donors use governance data to allocate aid, focusing on IDA allocations that use the CPIA, and the US Millennium Challenge Account that uses the aggregate governance indicators as part of their allocation and selection criteria. Many bilateral donors also consider governance issues (as part of a range of considerations) in selecting focus countries or in informing their country aid strategies. Care is needed in making judgments about how governance varies across the developing world, what the key issues for reform are and whether and when aid should be provided in large quantities. However, there is a case for donors linking governance assessments to aid policy in general, and scaling up in particular.

Section 6 concludes with some preliminary recommendations, which are tentative from the perspective of this paper, but will be complemented by those of other work packages and drawn together in the synthesis report. They consider the following issues: (i) should Irish Aid engage in qualitative governance assessments (such as those being launched by a number of other donors) in light of the limitations of quantitative governance indices? (ii) can we design general principles for the types of governance interventions to engage in? and (iii) if and how can governance indices be used to inform the selection of partner countries and the choice of aid modalities?

Key suggestions include:

- As with other diagnostic tools, governance assessments should be undertaken jointly by donors to avoid proliferation and unnecessary increases in transaction costs.
- There are already a number of existing governance indices and assessment tools that donors can draw on, for example when assessing the governance context in a partner or potential partner country. Existing tools include: DFID's Drivers of Change analysis, Sida's 'power analysis'; the World Bank's political-economy assessments, and the independent *World Governance Assessments*.<sup>1</sup> Further tools are currently being launched, such as the EU Governance Profiles and DFID Country Governance Assessments among others.
- There is debate as to how information from governance indices and assessments should be shared among donors and/or published. As a minimum, sharing should be encouraged.

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<sup>1</sup> For details, see: [www.odi.org.uk/wga\\_governance/](http://www.odi.org.uk/wga_governance/)

- The OECD-DAC GOVNET is taking the Harmonisation and Alignment (H&A) agenda surrounding governance assessments forward with a conference planned for Autumn 2007.
- Given the rising importance of governance and related assessments and diagnostic tools, donor agencies need to ensure adequate central capacity to review and digest existing governance indices and qualitative assessments (as a first priority before engaging in and carrying out assessments), and also with a view to contributing to the European and international policy debates.
- With regard to governance interventions, there should be a focus on the essential rather than the merely desirable (as stated by Grindle), and possibly on governance in priority sectors, rather than at the national level (which may be covered by larger donors, although sectoral and overall interventions should be well-linked).
- Strategically, it is important to focus on politically feasible reforms. Experience constantly reminds us that reform is a political not just a technical exercise. Political analysis can help here too. Local context will affect the approach taken; experience suggests that countries often deal with similar challenges in quite different ways.
- Available governance indices may be used when selecting additional partner countries as well as aid modalities, however donors need sufficient capacity to interpret such indices and must be knowledgeable regarding their limitations (see suggestion 5, above). Furthermore, governance indices cannot be applied mechanically: donors may deliberately choose to provide aid to a country with a difficult governance context and many poor countries have relatively poor governance. Discussion about how the choice of aid modalities may be linked to governance considerations is a relatively recent one in development policy thinking, which will be discussed further in the synthesis report.

# 1. Introduction

This paper examines governance data and categories in relation to Irish Aid's evolving programme, with particular emphasis on the implications for scaling up aid. The paper is part of a broader study on governance, aid effectiveness and poverty reduction. The overall study will result in a synthesis report which will draw on individual work packages and wider evidence to address the overarching policy questions of the relationship between governance, (the choice of) aid modalities, and poverty reduction. The focus here is therefore primarily on mapping the field of governance categories.

## ***1.1 Irish Aid context and projections***

It is worth summarising some key background information regarding Irish Aid:<sup>2</sup>

- Irish Aid (formerly DCI) is set to increase its overall aid programme to achieve the 0.7% target by 2012. This will mean an increase from €545 million in 2005 to projected spending of €1.2 billion in 2010 and €1.5 bn in the year 2012. Among European donors, Ireland was 12th in terms of absolute spending in 2005 (see Muerle, 2007);
- Irish Aid currently focuses on 8 'programme' countries: Ethiopia, Lesotho, Mozambique, Tanzania, Uganda, Zambia, Vietnam and East Timor (there are also additional programmes in Zimbabwe, South Africa, Palestine, Western Balkans and Eastern Europe);
- Irish Aid currently focuses on Education, Health and HIV, but also engages substantially with governance issues (see Table 1);
- Irish Aid currently focuses on 5 main modalities: projects, area-based programmes, SWAps, budget support and support for civil society (see DCI, 2005a).

With regard to governance we can summarise the following key issues (based on DCI, 2005b):

- Irish Aid sees governance as important for poverty reduction;
- it takes a broad view of governance involving a range of actors around the key areas of state accountability and effectiveness;
- governance issues are important considerations for country aid strategies;
- Irish Aid intervenes in a number of ways – with activities to promote democracy, human rights, rule of law, public-sector reform and civil society;
- governance now represents approximately 18% of the total Irish ODA budget. Irish Aid has been advised by the OECD-DAC to expand its work on governance.

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<sup>2</sup> <http://www.dci.gov.ie/>

**Table 1: Outline of current Irish Aid programmes in main partner countries**

Country	Spend (€ m.) 2005	Main modalities (NB: limited information)	Priority issues under overall poverty focus (and governance issues)
Tanzania	25.7	Area programme, SWAps, budget support	Health, education, agriculture, HIV/AIDS and governance (decentralisation).
Ethiopia	30	Projects, Programmes, SWAps	Education, health, HIV/AIDS, food security, water/sanitation, governance and roads (public-sector reform, supporting democracy and civil society, human rights).
Mozambique	27.2	SWAps, area programmes, budget support (€6 m.)	Health, education, agriculture, HIV/AIDS and governance (public-sector reform, human rights, judicial reform, media).
Uganda	30.5	SWAps, budget support	Health, education, governance, HIV/AIDS and NRM (decentralisation, justice, parliament, civil society, anti-corruption).
Zambia	15	Area programme, Projects, SWAps	Education, health, HIV/AIDS, water/sanitation, urban, governance and economic sector (democracy, civil society, local government).
East Timor	4.2	Grants and capacity-building	Governance, service delivery for poverty reduction and job creation (institutional capacity-building, local development, gender equality and human rights).
Lesotho	10.1	NA	Health, education, water, rural access, HIV/AIDS and governance (public-sector reform, strengthening service delivery systems, supporting democracy, accountability, human rights and civil society).
Vietnam	3.0	Area programmes (budget support €3 m. for 2006)	Governance, private sector and health (anti-corruption).

Note: Data from Uganda = 2004; Zambia = 2003.

Source: Adapted from <http://www.dci.gov.ie/>

## **1.2 Governance and aid policy**

There is widespread agreement among donors that governance matters – intrinsically, as well as for improvements in socio-economic outcomes and for aid effectiveness (Reynolds, 1983; North, 1990; Knack and Keefer, 1995; World Bank, 1997; Acemoglu et al., 2001; Kaufmann et al., 2002; Hyden et al., 2004; Moore and Putzel, 2000). This raises a set of broad policy questions about how best to rigorously and systematically link aid policy to governance situations in developing countries. It also raises challenges in terms of measuring governance and for using such measurements to inform aid policy in a sensible way.

The principle of orienting aid policy to reflect governance contexts has been accepted by the high-level reports of the UN Millennium Project (Sachs et al., 2005) and the Commission for Africa (2005).<sup>3</sup> But the major reports have provided few answers on how to operationalise this.

Using a range of measurement tools, a number of donors already consider governance issues (as part of a range of considerations) in selecting focus countries or in informing their aid allocations across countries:

<sup>3</sup> The Millennium Project report suggests a division between countries with poor governance, and those which have a political will but lack capacity (Sachs et al., 2005: 51). The report of the Africa Commission, and the G8's statement on substantially increasing aid to the poorest countries over the coming years, recognise that scaling up depends on improvements in governance in recipient countries.



- The World Bank uses the Country Policy and Institutional Assessment (CPIA), which includes governance assessments, for IDA funds.
- DFID and the Netherlands also use the CPIA as part of a model to inform their aid allocation.
- The Millennium Challenge Account of the US uses aggregate governance indicators developed by Daniel Kaufmann and his colleagues at the World Bank Institute (WBI) to help with country selection for extra funding.
- Donors have also started to support a range of approaches to political analysis. DFID's Drivers of Change analysis, Sida's 'power analysis'; World Bank political-economy assessments as well as independent assessments (such as the WGA) provide more detailed country assessments. However, the use of these in-depth qualitative assessments in the development of aid policy remains limited.

How to measure governance and what use to make of such measures remains contested (Arndt and Oman, 2006). There are questions regarding different conceptions of governance, whether governance can actually be measured accurately and the ways the measures are used to allocate aid. Systematically linking governance assessments to aid policy and country programming is a challenging enterprise.

### ***1.3 Key questions and approach***

This report addresses the following issues in the course of five sections:

- i. Governance, development and aid effectiveness: what are seen as the key governance issues that matter for development performance and aid effectiveness?
- ii. Governance data: what are the sources of governance data? Can governance issues be assessed/measured rigorously across countries and over time? What are the opportunities and constraints?
- iii. Governance categories and Irish Aid countries: can governance data be used to establish broad 'categories' of countries (with a balance of simplicity and sophistication) as a basis for informing aid policy? How do Irish Aid countries 'look' through different governance assessment lenses?
- iv. Governance and aid allocation: how are governance measures used for aid allocation mechanisms by the IDA (CPIA) and by the MCC (16 indicators measuring governance as well as development outcomes)?
- v. Implications for Irish Aid policy: what are the possible implications of this discussion for Irish Aid's evolving policies and strategies?

The findings in the paper are based on:

- A review of the literature on governance, development and effectiveness, and governance indicators;
- Interviews in Washington, DC regarding World Bank Institute and CPIA approaches to measuring governance, the utility of governance categories and the use of governance data in aid allocation (IDA and MCC).
- Some basic collation of existing governance data regarding Irish Aid partner countries from a comparative perspective.
- Synthesis of the findings and assessment of policy implications.

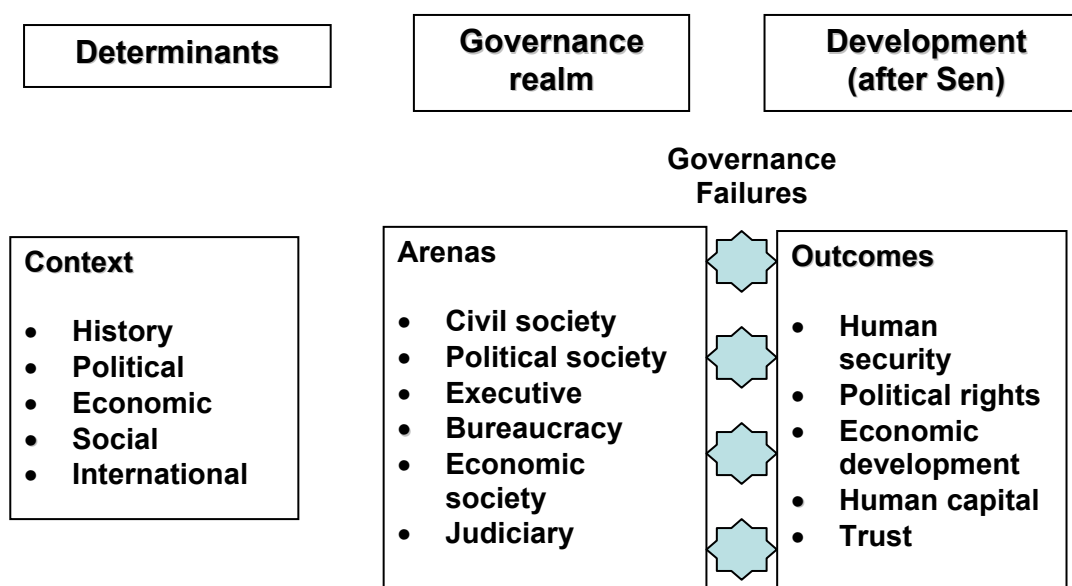
## 2. Governance, development and aid effectiveness: A brief review

This section provides a brief review of the key governance context issues that matter for development and aid effectiveness.

Governance refers to the *rules that regulate the public realm* – the space where state, economic and societal actors interact to make decisions. As such, it goes beyond a focus on government and also to the nature of relations between state and society. Governance refers to processes – how things are done, not just what is done. The relations between governance and development are difficult to tease out conceptually since there are both instrumental and intrinsic elements (Court, 2006; Kjaer, 2004). Importantly, (good) governance is a broad concept with unclear boundaries and loosely defined normative content.

One illustration of the multi-dimensional nature of governance is provided by Hyden et al. (2004) who outline six governance arenas that matter in terms of state legitimacy and effectiveness, and link them to underlying factors as well as outcomes (Figure 1).

**Figure 1: Framework for analysing governance and development**



Note: Relationships are complex and two-way.  
Source: Hyden et al. (2004).

In recent years, governance has moved to the centre of development policy debates. The importance of improving governance is set out in a number of high-level international policy statements such as the Millennium Declaration:<sup>4</sup> ‘Success in meeting these objectives [of poverty reduction] depends, *inter alia*, on good governance within each country. It also depends on good governance at the international level ...’

The 2005 EU Strategy for Africa<sup>5</sup> also put governance and peace at the top of the agenda, and the EC issued a new communication on ‘Governance in the European Consensus on Development’ in

<sup>4</sup> <http://www.un.org/millennium/declaration/ares552e.htm>

<sup>5</sup> [http://www.europe-cares.org/africa/eu\\_strategy\\_en.html](http://www.europe-cares.org/africa/eu_strategy_en.html)

August 2006.<sup>6</sup> The World Bank widely consulted on its new governance strategy in 2006, until its final adoption by the Board in March 2007,<sup>7</sup> setting out that '[g]overnance refers to the manner in which public officials and institutions acquire and exercise the authority to shape public policy and provide public goods and service'. The strategy emphasises that governance and corruption are not equivalent (although there is a strong underlying push to do more about anti-corruption).

Governance is central to DFID's 2006 White Paper, *Making Governance Work for the Poor*, while AusAid made the fostering of 'functioning and effective states' one of the four main pillars of its work in its own White Paper of 2006, declaring that existing governance work would be enhanced by: (i) 'focusing on political governance by targeting leaders from all facets of society through a Pacific leadership programme and by building demand for better governance; (ii) providing incentives through allocating additional funding (up to 10% of the aid budget over time) to those countries able to achieve agreed improvements in areas such as governance and addressing corruption; and (iii) making more selective and effective use of technical assistance to promote reform, and undertaking an integrated approach to law and justice support'.<sup>8</sup>

The UN, which prefers the term 'democratic governance' has argued that: 'Democratic governance is central to the achievement of the MDGs, as it provides the "enabling environment" for the realisation of the MDGs and, in particular, the elimination of poverty'.<sup>9</sup> According to Kemal Dervis, the head of UNDP, 'institution-building for democratic governance has become the most important part of our program, taking up 40 to 45% of our worldwide budget' (Dervis, 2006).

Importantly, donors are large bureaucratic 'machines' and the specific reforms promoted 'on the ground' under the broad banner of 'good governance' can vary substantially in content – for example in their emphasis on certain aspects, and neglect of others – and can differ from high-level policy pronouncements. This is reflected, for example, in a 2006 evaluation of the EU's support for improving governance in developing countries.<sup>10</sup>

The above policy development has been based on increasing evidence from cross-country analysis that governance matters instrumentally for development performance, however there is still considerable uncertainty about which dimensions of governance matter foremost (Rodrik, 2004; Khan, 2006; Dervis, 2006).

Generally, performance associated with the various dimensions of governance is weaker in poor countries and stronger in richer countries. Low-income countries tend to fall in the bottom half or even bottom third of most governance indices. Nonetheless, within each 'income band' (e.g. low, lower-middle and high) there is also considerable variation – thus Chile is as highly-rated within Transparency International's Corruption Perceptions Index as the US, despite the latter's substantially higher income, and Saudi Arabia falls into the bottom third of the ranking despite having a much higher per capita income than most similarly rated countries.

The 1997 *World Development Report: The State in a Changing World* highlights the importance of property rights, judicial reliability and control of corruption for investment and growth. Kaufmann et al. (1999; 2002) find that the six dimensions of governance that they measure are positively associated with per capita incomes and adult literacy and negatively associated with infant mortality. Knack and Keefer (1995) find that better governance is positively associated with improved investment and growth rates, while Mauro (1995) finds that the efficiency of the bureaucracy (among other issues) is associated with better rates of investment and growth, whereas corruption is negatively related to these. Chong and Calderón (2000) find that good governance contributes to (and also results from) strong economic performance.<sup>11</sup>

<sup>6</sup> [http://www.europe-cares.org/africa/docs/COM\(2006\)421\\_EN.pdf](http://www.europe-cares.org/africa/docs/COM(2006)421_EN.pdf)

<sup>7</sup> <http://www.worldbank.org/html/extdr/comments/governancefeedback/gacpaper-03212007.pdf>

<sup>8</sup> [http://www.ausaid.gov.au/publications/pdf/wp\\_summary.pdf](http://www.ausaid.gov.au/publications/pdf/wp_summary.pdf), p. 7.

<sup>9</sup> <http://www.undp.org/governance/mdgs.htm>

<sup>10</sup> Available at: [http://ec.europa.eu/europeaid/evaluation/document\\_index/2006/884\\_docs.htm](http://ec.europa.eu/europeaid/evaluation/document_index/2006/884_docs.htm)

<sup>11</sup> The relationship between democracy and economic growth is not as clear cut (witness the rapid growth of China and the other East Asian tigers). There is increasing evidence that democracies do perform well in developing countries (Halperin et al., 2004).

### Box 1: Some key references on institutions

- i) Adam Smith famously argued over 200 years ago that 'little else is requisite to carry a state to the highest degree of opulence from the lowest barbarism but peace, easy taxes and tolerable administration of justice' (Smith, 1776).
- ii) North (1990) on the importance of institutions for economic performance.
- iii) De Soto (2000) on the government-exacerbated challenges of running businesses in developing countries
- iv) In Reynolds' (1983) study of long-term economic growth 'the single most important explanatory variable' was 'political organisation and the administration of government'.
- v) Acemoglu et al. (2001) estimated that differences in institutions explain approximately three-quarters of the income per capita differences across former colonies.

Quantitative cross-country studies on the relationship between governance and various development outcomes should always be interpreted with some caution, due to the fact that 'measuring' governance is still a recent and inexact science (see Section 3 below), and that often only a particular dimension or aspect of governance is being measured rather than the concept as a whole. For example, the longest time-series for measuring governance are those measuring the presence or absence of a democratic regime reaching back to the 1860s (University of Maryland: Polity IV);<sup>12</sup> while other dimensions of governance have at most been measured since the mid-1980s (when the International Country Risk Guide started as one of the first comprehensive commercial risk indices).<sup>13</sup>

The available evidence and resulting conclusions are well summarised in the World Bank's 2006 *Global Monitoring Report*: 'Statistical evidence suggests that the causality between growth and governance is two-way – implying that gains in either can give momentum to a virtuous spiral of development improvement' (World Bank, 2006a: 121).

Governance issues are of intrinsic importance to development. As outlined by Sen (1999), poverty is not just a matter of being economically deprived; it is defined and sustained by a sense of helplessness, dependence and lack of opportunities, self-confidence and self-respect on the part of the poor. And these are not just academic discussions: the *Voices of the Poor* study, carried out under World Bank auspices (Narayan et al., 2000), highlights powerlessness and lack of voice as crucial components of poverty as stated by the poor themselves; and the *Gallup Millennium Survey* – the largest ever public-opinion survey – highlights the importance of human rights to ordinary people in both developed and developing countries (Sprogard and James, 2000). At the level of policy pronouncement at least, there is also overwhelming international agreement about the intrinsic value of democracy, human rights and good governance.<sup>14</sup>

A number of studies have sought to explore the links between governance and aid effectiveness. This literature will be covered in greater depth in the synthesis report, however some pertinent points serve to be addressed here.

As McGillivray et al. (2005) highlight, debates surrounding the importance of policies and/or governance for aid effectiveness are built on long-standing controversy about the effectiveness of aid (primarily in fostering growth). An important turning point in the debate came from the World Bank's *Assessing Aid: What Works, What Doesn't and Why* (1998), which argues that policies and governance (primarily framed as good macro-economic management and 'strong' institutions) are crucial for aid to have a positive impact (based on background papers by Burnside and Dollar,

<sup>12</sup> Available at <http://www.cidcm.umd.edu/polity/>

<sup>13</sup> Available at <http://www.prsgroup.com/>. The ICRG is a fee-based index.

<sup>14</sup> See UN Millennium Declaration, <http://www.un.org/millennium/declaration/ares552e.htm>

1997). Subsequent studies, however, have again disputed these findings. Some find that the quality of policies made no difference (Roodman, 2004; Easterly et al., 2004), while others find factors ranging from democratic governance to political stability, geography and climate more important in determining the effectiveness of aid (Kosack, 2003; Islam, 2002; Dalgaard et al., 2004). Two of these alternative explanations – that democratic governance or political stability matter – in fact point to governance fundamentals as being important (rather than ‘just’ good macro policies as proposed by Burnside and Dollar), while geography and climate are alternative variables to the nexus of governance, institutions and policies. Recent studies on aid effectiveness also suggest that recipient-country factors may not exclusively shape the effectiveness of aid, but also the way in which aid is being provided (i.e. the ‘diagnosis’ underlying the Paris Declaration on Aid Effectiveness); and in fact, the high fragmentation of aid may even contribute to governance problems (Knack and Rahman, 2004).

While large-N studies on governance and aid effectiveness are thus somewhat inconclusive, there is an overall sense that the quality of recipient-country institutions certainly plays a role in their overall development prospects as well as their ability to use aid well. This is also supported by evidence from a more micro-level perspective on the success of development projects:

- Isham et al. (1997) analyse the impact of the quality of governance on the performance of hundreds of World Bank projects and find that rates of return are higher in nations with greater civil liberties.
- Work at the WBI highlights a relationship between country corruption ratings (and also rule-of-law indicators) and World Bank project success – particularly for infrastructure projects (Mastruzzi, pers. comm; Kaufmann, 2005).
- The importance of governance as a factor in aid effectiveness is accepted by DFID and the Dutch governments, among others, based on the experience of practitioners.

It is also worth mentioning here the findings of the recent evaluation of General Budget Support (IDD and associates, 2006), which is based on studies in a number of Irish Aid partner countries (Mozambique, Uganda, Vietnam, and also draws on a separate study of Tanzania) and a potential partner (Malawi) which already receives some GBS. Of general relevance here, the study concludes:

- ‘Assessments of political risks ... were less explicit’ and ‘the political risks of PGBS had been underestimated’ (p. S3);
- ‘political context has tended to be less well analysed and adapted to than other elements of the context’ (p. S4);
- ‘The main threats to continuity and sustainability of PGBS are likely to be political’ (p. S9).

Overall, there is a growing consensus that governance is important to development and that governance is likely to have an impact on how well and effectively aid is being used. At the same time, it is important to acknowledge that there is less certainty about precise causal linkages, pathways of improving governance and economic growth over time, and about the dimensions of governance that would matter most. For example, Grindle (2004) and Khan (2006) both emphasise that all-out effort to generate ‘good governance’ in poor countries may be misplaced; and that the emphasis may need to be on more limited improvements (‘good enough governance’) building momentum over time, and as more resources become available.

This is the context in which donors such as Irish Aid are currently defining their policies and interventions, and governance data are playing an increasingly important role in this situation. The remainder of the paper seeks to provide an overview of key data sources and how donors may be able to make good use of them.

### 3. Governance data: Opportunities and challenges

If governance matters, it would help to have reliable and valid data on key governance processes. Better information provides a basis for understanding a context, identifying the main challenges and opportunities, identifying reform priorities and monitoring change (or not), and may also serve to inform aid policies with regard to choices about aid allocation and the modalities to be used. Do we have such governance data?

This section examines governance measures more closely. It looks at key sources of data – and their opportunities and limitations (see Sudders and Nahem, 2004; Munck and Verkuilen, 2002) – and assesses their conceptualisation of governance and the extent of methodological quality.

The lack of reliable and valid (and comparable) data on key governance issues has certainly provided a challenge to donors. Assessing governance poses challenges that are very different from other socio-economic issues. Firstly, there are few objective or ‘hard’ indicators that make sense, therefore indicators tend to be based on subjective criteria – whether these are perceptions of groups (e.g. business executives; public opinion) or assessments by individual analysts rating various aspects of governance in a certain country.

The scarcity of ‘hard facts’ is inevitable given the nature of governance issues: corruption is not included in national statistics. Furthermore, indicators – such as the Global Integrity Index – which seek to be based on hard facts have their own problems. Assessing whether countries have certain institutional and legal features, such as asset disclosure or anti-corruption agencies, is important. However, governance cannot be reduced to particular institutional arrangements and, moreover, measuring such ‘facts’ often means assessing only the ‘formal side’ of governance, and not the way in which things are actually run (see also Arndt and Oman, 2006: 30). Basing assessments on perceptions, for example of efficiency and accountability, is legitimate and can give us real insights. It does mean, however, that such data should be treated with care. Also, governance is a broad issue – specific indicators describe only certain aspects – and it is important to know what an indicator is actually measuring.

There is an increasing number of governance assessment tools and indices, many of which are summarised in the UNDP/EU 2004 handbook *Governance Indicators: A Users’ Guide*, which details 33 data sources of a certain quality (plus others that did not meet UNDP standards), and in *Uses and Abuses of Governance Indicators* by the OECD Development Centre (Arndt and Oman, 2006). As the World Bank’s 2006 *Global Monitoring Report* states, there has been a ‘growth industry’ of governance indices, and new indicators continue to be developed.

As yet there are relatively few indices that have comprehensive country coverage and the methodology of which have undergone substantial debate and refinement. The 2006 *GMR* focuses on governance and highlights 14 specific indicators that can be used given their cross-country and temporal coverage (see Table 2).<sup>15</sup>

Two key sources – together accounting for 8 of these 14 indicators – are described in greater detail in this paper, namely, the World Bank’s CPIA and the World Bank Institute’s Kaufmann-Kraay-Zoibo-Lobaton (hereafter KKZ) indicators, for which we provide a brief description and discussion of their value and limitations.<sup>16</sup>

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<sup>15</sup> These 14 indicators are drawn mainly from three indices: the CPIA, the KKZ index and the IFC’s ‘Doing Business Survey’. From each of these indices some, but not all, of their specific indicators are used.

<sup>16</sup> The three indicators related to corruption referred to by the *GMR* are discussed in greater depth in WP 3.

**Table 2: Fourteen governance monitoring indicators proposed by the 2006 GMR**

	<b>Indicators with comprehensive coverage</b>	<b>Other key indicators</b>
<b>Overall governance performance</b>	1, 2, 3. <i>Control of corruption</i> (KK, TI, ICS) 4. <i>Policy outcome</i> (CPIA cluster a-c average) 5. <i>Aggregate public institutions</i> (CPIA cluster d) 6, 7. <i>Business transactions costs</i> (DB, ICS)	
<b>Bureaucratic capability</b>	8. <i>Budget/financial management</i> (CPIA-budget) 9. <i>Public administration</i> (CPIA-admin) 'Doing Business' indicators Investment climate surveys Statistical capacity	14. <i>PEFA indicators</i> Procurement 'Actionable' public administration Service-provision-specific
<b>Checks and balances institutions</b>	10. <i>Voice and accountability</i> (KK) 11, 12. <i>Justice and rule of law</i> (KK, CPIA-rules) 13. <i>Executive constraints</i> (Polity IV)	Global Integrity Index

### 3.1 Country Policy and Institutional Assessments (CPIAs)

The World Bank's Country Policy and Institutional Assessments (CPIAs) account for 5 of the 14 governance indicators suggested for use in the *GMR*. The CPIA, initially developed in the 1970s, was used to guide allocation of International Development Association (IDA) funds. The CPIA has 16 criteria in 4 clusters, one of which is on governance issues (D: Public-sector management and institutions) with five criteria (see Box 2 for the full list and Annex 1 for the 2005 scores for IDA countries). In future, the overall country scores will be known as the IDA Resource Allocation Index (IRAI).

Until very recently, the CPIA was considered to be methodologically rather weak. A revision came in 2004 to improve the preparation of the indicators, and it is now seen to have a relatively robust process to prepare the indicators – each has guidelines to help in its preparation and there are various review processes. Regional benchmarking countries are assessed, World Bank staff then prepare ratings and finally there is a review process. Countries are scored on a 1-6 scale and these will then be made publicly available for IDA countries (2006 was the first year for 2005 scores).<sup>17</sup> But weaknesses remain. The data are prepared by World Bank staff and the independence of the indicators is questioned. The assessments only focus on 5 issues which are mostly development 'management' issues – overall governance is much broader. Also, 3 of the criteria cover more than one issue (criteria 16 covers transparency, accountability *and* corruption in the public sector). Since the country scores affect Bank allocation there is an incentive for country staff to try to manipulate them. Other problems have been identified: some indicators are not suited to an ordinal scale, there is risk of an ideological bias and margins of error can be substantial (see World Bank, 2006: 129; Nash et al., 2006).

#### Box 2: Components of the CPIA

##### A. Economic management

1. Macroeconomic management
2. Fiscal policy
3. Debt policy

##### B. Structural policies

4. Trade
5. Financial sector
6. Business regulatory environment

##### C. Policies for social inclusion/equity

7. Gender equality
8. Equity of public resource use
9. Building human resources
10. Social protection and labour
11. Policies and institutions for environmental sustainability

##### D. Public-sector management and institutions

12. Property rights and rule-based governance
13. Quality of budgetary and financial management
14. Efficiency of revenue mobilisation
15. Quality of public administration
16. Transparency, accountability and corruption in the public sector

<sup>17</sup> Only current years, not past years, are being made available.

### **3.2 Aggregate governance indicators**

The World Bank Institute generates six aggregate indicators of governance – known as KKZ indicators. Using a complex statistical technique, they *aggregate data from existing sources* into the following six composite indicators:

- Voice and accountability (V&A)
- Political stability and absence of violence (PS)
- Government effectiveness (GE)
- Regulatory quality (RQ)
- Rule of law (RoL)
- Control of corruption (CC)

These indicators are available for 1996 to 2005. Previously available for every second year, the KKZ indicators became annual from 2006. While some of the 37 data sources are not available publicly, there is ongoing effort to make all of the data public.<sup>18</sup> In particular, the *GMR* proposes to use (i) voice and accountability; (ii) rule of law; and (iii) control of corruption.

The KKZ indicators have certainly provided a helpful step forward, offering broad coverage of the governance realm. Available for 209 countries for, by now, a whole decade, they enable comparative assessments and by aggregating reduce the problems of using a single source or approach.

KKZ indicators suffer from drawbacks, however: each of the aggregate indicators is still very broad in terms of issue coverage; substantial margins of error remain, particularly for developing countries for which there are far fewer sources of data; the specific data used in the aggregations often suffer from variations in sampling, questions, mode and management, which make cross-country comparisons problematic (for a more in-depth discussion see Knack, 2006); some sources are not available to the public; some are seen as much less rigorous than others; the aggregation approach gives weighting to certain indicators; and there is concern about the fact that some sources feed off each other (especially in the sense that assessments by individual analysts draw on existing indicators).

### **3.3 The debate about governance indicators**

The increasing attention to measuring governance has resulted in a lively debate surrounding governance indicators and their use. Arndt and Oman (2006), in particular, have criticised the KKZ indicators and their use. The main issues relevant to the aid policy debate are:

1. Aid donors should not construct cut-off points from the KKZ indicators (as has been done by the Millennium Challenge Account) – since due to margins of error and measurement uncertainties, there is a certain probability that countries are unfairly excluded;
2. In particular, CPIA ratings may be influenced by outcomes (such as a country's growth performance);
3. Users should not construct one aggregate indicator based on the six dimensions identified by KKZ. Summarising very different dimensions of governance (such as voice and accountability and political stability) can lead to meaningless results.

Furthermore, while acknowledging the strengths of the KKZ, Arndt and Oman (2006) raise the following issues with respect to this index:

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<sup>18</sup> Transparency International's Corruption Perception Index is similar in its approach, also aggregating other existing indicators, and correlates closely with the KK corruption measure.



1. The likelihood of correlation of errors among the underlying sources (also noted by Knack 2006) – i.e. the fact that the underlying data sources draw on similar information, or even on each other;
2. Limits to comparability over time due to the fact that only changes beyond the ‘margins of error’ can be read as significant;
3. Sample bias in the weighting of underlying indicators (in favour of business surveys and expert assessments);
4. Insufficient transparency (still).

Arndt and Oman raise important points that users of governance indices should be more aware of. Their criticism should not be read, however, as arguments for abandoning efforts to measure governance or using such measurements to inform donors. They should be taken as reminders to be judicious in the use of indicators and also to critically assess claims about causation – since the ways in which governance is measured can have very significant impacts on the results of regression analyses and hence claims about causality (which in turn can easily be forgotten in the policy debates using such evidence).

A further key point is that it is very difficult to place countries in a meaningful governance category. Countries vary according to the governance issue – for example, voice and accountability vs. corruption – therefore categorisation depends on the issue selected. Except at a broad level, margins of error also make rigorous categorisation difficult.

### **3.4 Other governance data sources**

There are increasing sources of information on governance issues in developing countries.

Ratings for specific governance issues are most commonly generated by panels of international experts. Indices based on such expert assessments remain problematic for methodological reasons, however, as they are usually done by panels comprising only a few individuals. They also focus on a narrow set of issues (for example regime type in the case of Freedom House) and can have an ideological bias (such as the Heritage Foundation’s Index of Economic Freedom).

Similar in construction, but with a different focus, political-risk ratings generated by various organisations for the private sector (EIU and PRS) are also worth considering (for a brief assessment of such indicators and their usefulness for donors see Phillips, 2006).

More directly pertinent for donors are the data from the ‘Doing Business’ (DB) database and Investment Climate Surveys (ICS) prepared by the World Bank (IFC). The DB assessment is based on a precise set of transactions and gauges the applicable domestic rules (number of necessary tax payments per year, days needed to obtain specific business licenses, etc.). The ICSs, which are perception-based surveys of the investment climate among firms, currently cover around 60 countries, while in 2006 the DB assessment covered 155 (World Bank, 2006: 132). Both focus on the broad concept of the ‘investment climate’ rather than ‘governance’, however there is a conceptual overlap which makes the indices relevant from a governance perspective.

Similarly, there are various public-opinion surveys that include questions about general governance issues. Of particular relevance to Irish Aid, the *Afrobarometer* currently covers 18 African countries and provides a wide range of cross-country data on governance, the political regime, state effectiveness, government responsiveness, as well as trust and trend data for the 12 countries in which 3 cycles of surveys have been conducted. The *Afrobarometer* follows a similar methodology as barometers on other regions (Latino Barometer, New Europe Barometer, etc.), and hence is also useful for inter-regional comparison. A limiting factor is that it is constructed around a concern for democratisation (dominant in the 1990s), rather than being more widely concerned with governance.

At present there is only one source that conducts comprehensive country-level governance assessments in poor countries, based on an approach developed by a team co-ordinated by ODI (the World Governance Assessments).<sup>19</sup> This approach has the benefits of using a cohesive framework of governance, focuses on processes, draws on the views of a panel of experts *within* each country and generates qualitative as well as quantitative information. The approach is also independently managed. One draw-back is its limited country coverage (16 countries in 2000 and 10 in 2006), and the fact that, thus far, only two rounds of the assessment have been carried out.

A new source is the Global Integrity Index (GII), which has been generated for 40 countries in its latest round,<sup>20</sup> and is interesting in that it generates systematic data on specific governance issues and across countries, and seeks to be a mainly 'facts-based index'. The GI uses an integrity/corruption lens rather than a more general governance one (discussed further in WP 3). At present there exist questions over rigour of data collection, as the GI is based on views of only 5 experts per country.

The Bertelsmann Transformation Index (BTI) has extensive country coverage (119 countries in 2006), as well as wide coverage of issues, and a useful web portal to allow users to analyse and visualise data in various ways.<sup>21</sup> The main weakness of the BTI is similar to that of the GI, in that it is based on assessments by a small number of experts who are asked to rate a wide range of (detailed) issues.

The PEFA indicator set, developed by the Public Expenditure and Financial Accountability global programme is worth mentioning (and is also included in the 14 indicators suggested by the 2006 GMR).<sup>22</sup> The PEFA Performance Management Framework contains a set of 28 indicators focused on a range of PFM issues in country, and 3 indicators related to the quality of aid provided. Since the quality of public financial management is vital to the effective scaling up of aid, these indicators are relevant in the context of governance and aid. The ratings generated by the PEFA PMF are specific and hence are more 'action-oriented' than many other indicator sets. They are also based on intensive, in-depth assessments by consultancy teams. PEFA assessments have been carried out for around 60 developing countries thus far, however, only selected reports have been made public.

Additional sources that cover Africa include:

- The Economic Commission for Africa 28-country governance assessment, however there are concerns about quality of work in some countries and not all assessments are publicly available;
- The emerging NEPAD African Peer Review Mechanism Country Governance Assessments, most of which have only been made public with long time delays (to be covered in depth in WP 4);
- The African Development Bank's Country Governance Profiles;
- The Mo Ibrahim Foundation's African Governance Indicators to be launched in the second half of 2007.<sup>23</sup>

The UNDP has also compiled a useful list of sources dealing with governance indicators.<sup>24</sup>

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<sup>19</sup> See [http://www.odi.org.uk/wga\\_governance/Index.html](http://www.odi.org.uk/wga_governance/Index.html)

<sup>20</sup> See <http://www.globalintegrity.org/>

<sup>21</sup> See <http://www.bertelsmann-transformation-index.de/atlas.0.html?&L=1>

<sup>22</sup> See [www.pefa.org](http://www.pefa.org)

<sup>23</sup> See <http://www.moibrahimfoundation.org/>

<sup>24</sup> [http://www.undp.org/oslocentre/docs06/Bibliography\\_of\\_governance\\_and\\_democracy\\_indicators\\_resources.pdf](http://www.undp.org/oslocentre/docs06/Bibliography_of_governance_and_democracy_indicators_resources.pdf)

## 4. Governance categories and Irish Aid countries

This section looks at whether, and how, meaningful country categorisations are possible, based on discussion of how Irish Aid partner countries ‘look’ through different governance assessment lenses and also by putting them in comparative context.

We focus our data presentation on countries that are current Irish Aid programme partners (Ethiopia, Lesotho, Mozambique, Tanzania, Uganda, Zambia, East Timor, Vietnam – plus South Africa and Zimbabwe) or are under consideration (Palestine, Sierra Leone, Liberia, Malawi, Niger, Kenya, Mali).

To give an indication of CPIA overall scores and how they have been clustered (by quintiles for overall scores), the data from 2002 (IDA, 2003) are presented in Table 3. Since 2006, the World Bank has started to publish the individual scores, but only for IDA countries and for current years.

Table 4 shows the 2005 CPIA scores for our focus countries, and includes the average for the policy dimensions of the CPIA (clusters A-C) and details for the governance-related cluster D (see Annex 1 for the full set of 2005 CPIA scores). Generally, within the CPIA a rating of 3.5 or above on the 1-6 scale is considered ‘strong’, while a performance below this threshold is considered ‘weak’.

Two main issues emerge from Tables 3 and 4:

- Only 3 current and potential Irish Aid countries are strong within the governance section of the CPIA: Tanzania, Vietnam and Mali. Existing partners Lesotho and Uganda are also close to the 3.5 threshold. Uganda, in particular, has a strong overall rating, but in 2005 its performance within the policy dimensions was significantly higher than within the governance/institutional dimensions. Mozambique reaches the 3.5 threshold overall, but has a weaker performance within the governance/institutional dimension than on policy.
- There is some variation across issues – between policy and governance scores and within governance ratings (especially Ethiopia and Zimbabwe). Within the governance scores, efficiency of resource mobilisation tends to be rated rather well across the 13 countries, while (the very broad) indicator for transparency, accountability and corruption in the public sector tends to be the lowest score for most countries, followed by the quality of public administration, and property rights and rule-based government.

Furthermore, with the exception of Zimbabwe, nearly all countries are quite closely clustered around the 3-4 point range – from 3.1 to 3.9 for the overall ratings, and from 2.9 to 3.8 for the public-sector management and institutions section. Thus, the measured differences between best and worst performers are relatively small. The categorisation of countries into quintiles is therefore based on relatively small measured differences, except for the bottom quintile of ‘poor performers’ where the difference compared with the next highest quintile tends to be more substantial.

Table 5 maps the same 13 countries plus South Africa, East Timor, Liberia, and West Bank/Gaza (which are not included in the 2005 CPIA ratings) on the 2004 KKZ governance indicators. The countries are listed based on the average of the six dimensions, therefore this indicator should not be used for wider interpretation as discussed in Section 3 above.

**Table 3: Categories (quintiles) of the 2002 CPIA**

<b>First quintile</b> Average = 3.69	Bhutan, Cape Verde, Grenada, Honduras, India, Maldives, Mauritania, Samoa, Senegal, Sri Lanka, St. Lucia, St. Vincent and the Grenadines, Tanzania, Uganda, Vietnam
<b>Second quintile</b> Average = 3.48	Albania, Armenia, Bangladesh, Benin, Bolivia, Bosnia and Herzegovina, Burkina Faso, Ghana, Indonesia, Mali, Nepal, Nicaragua, Pakistan, Rwanda, Zambia
<b>Third quintile</b> Average = 3.28	Azerbaijan, Côte d'Ivoire, Dominica, Eritrea, Ethiopia, Kenya, Kyrgyz Republic, Lesotho, Madagascar, Malawi, Moldova, Mongolia, Mozambique, Republic of Yemen, Serbia, Montenegro
<b>Fourth quintile</b> Average = 3.06	Cambodia, Cameroon, Chad, Republic of Congo, Djibouti, The Gambia, Georgia, Guinea, Guyana, Kiribati, Niger, Papua New Guinea, Sierra Leone, Tonga, Vanuatu
<b>Fifth quintile</b> Average = 2.57	Angola, Burundi, Central African Republic, Comoros, Democratic Republic of Congo, Guinea-Bissau, Haiti, Lao PDR, Nigeria, São Tomé and Príncipe, Solomon Islands, Sudan, Tajikistan, Togo, Uzbekistan, Zimbabwe

Note: Countries not rated in CPIA 2002 exercise: Afghanistan, Liberia, Myanmar, Somalia and Timor-Leste.  
Source: IDA (2003).

**Table 4: 2005 IDA Resource Allocation Index ratings: Policy average, public-sector ratings and total**

Country	Policy (A-C)	D. Public-sector management and institutions						Total
		12	13	14	15	16		
	Policy average	Property rights & rule-based government	Quality of budgetary & financial management	Efficiency of revenue mobilisation	Quality of public administration	Transparency, accountability & corruption in public sector	Average	IDA Resource Allocation Index (IRAI)
Tanzania	4	3.5	4.5	4.0	3.5	3.5	3.8	3.9
Uganda	4.1	3.5	4.0	3.0	3.0	3.0	3.3	3.9
Vietnam	3.8	3.5	4.0	3.5	3.5	3.0	3.5	3.7
Mali	3.7	3.5	4.0	4.0	3.0	3.5	3.6	3.7
Kenya	3.7	3.0	3.5	4.0	3.0	3.0	3.3	3.6
Lesotho	3.5	3.5	3.0	4.0	3.0	3.5	3.4	3.5
Mozambique	3.5	3.0	3.5	3.5	3.0	3.0	3.2	3.5
Ethiopia	3.5	2.5	3.5	4.0	3.0	2.5	3.1	3.4
Malawi	3.3	3.5	3.0	4.0	3.5	3.0	3.4	3.4
Zambia	3.4	3.0	3.0	4.0	3.0	3.0	3.2	3.3
Niger	3.3	3.0	3.5	3.5	3.0	3.0	3.2	3.3
Sierra Leone	3.2	2.5	3.5	3.0	3.0	2.5	2.9	3.1
Zimbabwe	1.7	1.0	2.5	3.5	2.0	1.5	2.1	1.8

Notes: Scale: 1 = Lowest, 6 = Highest. (a) IDA countries excluded since not rated in IRAI 2005 exercise: Liberia and Timor-Leste; (b) Palestine and South Africa are not IDA countries; (c) Existing Irish Aid partner countries are highlighted.

Source: World Bank CPIA website.

**Table 5: KKZ governance indicators, 2004\***

Country	Voice and accountability	Political stability	Government effectiveness	Regulatory quality	Rule of law	Control of corruption	Average (for sorting only)
South Africa	0.86	-0.24	0.74	0.44	0.32	0.48	0.43
Lesotho	0.28	0.27	-0.33	-0.26	-0.03	-0.05	-0.02
Mali	0.35	0.07	-0.29	-0.26	-0.34	-0.52	-0.17
Mozambique	-0.13	-0.15	-0.39	-0.29	-0.6	-0.79	-0.39
Tanzania	-0.35	-0.38	-0.37	-0.55	-0.49	-0.57	-0.45
Timor, East	0.25	-0.62	-1.21	-0.43	-0.6	-0.29	-0.48
Zambia	-0.36	-0.16	-0.84	-0.49	-0.54	-0.74	-0.52
Malawi	-0.5	-0.33	-0.81	-0.57	-0.29	-0.83	-0.56
Vietnam	-1.54	0.16	-0.31	-0.57	-0.59	-0.74	-0.60
Uganda	-0.64	-1.27	-0.43	0.07	-0.79	-0.71	-0.63
Niger	-0.12	-0.56	-0.87	-0.63	-0.92	-0.87	-0.66
Kenya	-0.34	-0.96	-0.81	-0.43	-0.98	-0.89	-0.74
Sierra Leone	-0.49	-0.61	-1.32	-1.02	-1.1	-0.88	-0.90
Ethiopia	-1.11	-0.98	-0.96	-1.19	-1	-0.85	-1.02
West Bank/Gaza	-1.25	-1.33	-1.05	-1.02	-0.95	-0.6	-1.03
Zimbabwe	-1.48	-1.86	-1.2	-2.15	-1.53	-1.01	-1.54
Liberia	-1.24	-2.2	-1.86	-1.83	-1.76	-0.86	-1.63

Note: \* Point estimates, sorted by average (Scale -2.5 = low; +2.5 = high). (a) Existing Irish Aid partner countries are highlighted; (b) These figures are indicative purposes only – the margins of error are large – see Annex 2.

Source: WBI Governance website ([www.worldbank.org/wbi/governance/govdata/](http://www.worldbank.org/wbi/governance/govdata/)).

A range of issues emerge from this table and the comparative scores and charts provided in Annex 3 (for V&A, GE, RoL and CC since these are the most accepted KKZ indicators), and furthermore in Annexes 4 and 5 (comparison of individual countries over time).<sup>25</sup>

- There are few positive scores. This is not surprising in so far as most low-income countries rank poorly in global comparisons. At the same time, Irish Aid partner and potential partner countries include only three potential ‘worst performers’ as reflected in Table 5 and Annex 3 – West Bank/Gaza, Zimbabwe and Liberia.
- South Africa is a middle-income country and scores by far the best on all indicators except ‘political stability’.
- Government effectiveness and control of corruption are the relatively worst scores for the group of 17, however there are also countries which have distinct patterns – e.g. Vietnam scoring lowest on voice and accountability, but relatively well on government effectiveness.
- The three lowest performing countries of the group – Liberia, West Bank/Gaza and Zimbabwe – all score particularly low on political stability, however Uganda scores low on this as well, while performing relatively better on other indicators (in particular regulatory quality and government effectiveness).

<sup>25</sup> Annex 4 shows the scores for the 6 KKZ indicators over the 1996-2004 period for the current Irish Aid programme partners. Annex 5 does the same for potential partners (and South Africa and Zimbabwe).

- Apart from the particularly high and low scoring countries, what emerges again is a 'muddled middle' (as for the CPIA scores) – where margins of error and countries scoring differently on different indicators make categorisation difficult.
- For many indicators/countries, variation over time is too low to be counted as 'real change', as cautioned by Arndt and Oman (2006) and as discussed above. However, there are at least some instances of substantial positive or negative change (changes exceeding the margins of error), namely: Tanzania (improvements in government effectiveness and control of corruption), Uganda (improvements and renewed decline in the rule of law), Ethiopia (significant decline across all indicators).
- For some ratings (indicators/countries/time periods), margins of error are extremely wide (often due to low numbers of underlying data that KKZ is drawing on) – e.g. control of corruption in Ethiopia, or regulatory quality for East Timor. The visualisation available from the KKZ web tool for exploring the data is helpful in signaling this issue (even if, as criticised by Arndt and Oman (2006), it is still too frequently ignored by users).

It is worth mentioning some key discussion points here:

- (a) Categories and thresholds depend on the policy questions and issues that matter to the specific user/donor, and countries fall into different categories depending on the issues that are selected. For the World Bank, development management and corruption are the key issues. For DFID, concerns about democracy and human rights have also explicitly been added as key issues of political governance (DFID, 2006). The *GMR* states that 'not all good things come together' and gives the example of Bangladesh which does well in terms of economic policy framework but scores poorly in terms of corruption (2006: Chapter 5). The KKZ indicator charts (Annex 3) show how different countries rate according to different indicators; focusing on different issues does give different country rankings.
- (b) A key issue is whether donors want to include considerations of democracy/voice and accountability in their overall assessment of countries and with what intensity (relative to other dimensions of governance).
- (c) Margins of error are significant which makes the rigorous categorisation of countries difficult. Annex 2 shows a detailed example for the indicator 'control of corruption'. The range of countries which could potentially (given margins of error) fall into the top half of the sample is much broader than the range of countries actually positioned there based on their numerical scores.
- (d) Clusters are somewhat arbitrary. The CPIA quintiles and KKZ traffic-light approach are most meaningful for distinct cases at the polar ends of the spectrum. There are no known thresholds above or below which things improve for aid effectiveness; rather there is a continuum. It is fairer to say that development performance seems adversely affected (and risks to aid interventions increase) as governance performance declines.
- (e) Different governance indices can signal (very) different things about countries. For example, Tanzania scores better on the CPIA than on the KKZ indicators – both with regard to the 'average' and with regard to specific indicators (even if these are not fully comparable). Things get even more confused when we take the wider sets of governance indicators discussed in Section 3 into account. For example, Nigeria and Kenya both score 'moderate' with regard to overall integrity according to GII 2006; while both score in the lowest 25% according to KKZ's indicator 'control of corruption' (with Nigeria being one of the worst performers). As a consequence, users really need to be well-informed (or become better informed) about underlying concepts, methods and interpretation of the range of available governance indicators (some of which are more intuitive than others).
- (f) A further challenge is that the quality of governance and the perceived political commitment to better governance varies over time, which may pose challenges for adjusting aid commitments. While this is a problem for particular countries at specific times (changes of regime), in fact, the evidence suggests that governance situations in most countries change rather slowly most of the time (this implies that the 'direction of travel' argument can only be used over the longer term.) Once the initial 'noise' of regime change dissipates, there is

rarely a major shift in the governance situation. Perhaps it might be possible to track shifts over a 5-year period.<sup>26</sup>

Governance indicators certainly have a role to play in providing 'quick glance' assessments of the particular position of countries. However, they should always be read and interpreted with due caution, and a better understanding of governance indicators among development practitioners is certainly desirable. Furthermore, the distinctions among low-income countries and changes over time are often relatively small. This certainly makes it difficult to use governance indicators to put countries in distinct categories and to use these to define aid policy in a mechanistic way. Nonetheless, if indicators are used and interpreted with care, they can provide helpful guidance, and also point to issues where it may be worthwhile to 'dig deeper' in terms of qualitative analysis.

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<sup>26</sup> For both CPIA and KK indicators some recent country fluctuations are attributed to changes in the data/methodology rather than any changes on the ground.

## 5. Governance assessments and aid allocation

Two main systematic approaches to governance assessment and aid allocation are in use. The World Bank uses the CPIA to guide allocation to IDA countries (other donors also use the CPIA to various degrees), and the Millennium Challenge Corporation (MCC) uses the KKZ and a set of other indicators to guide allocations of the Millennium Challenge Account (MCA).

### 5.1 The use of the CPIA in IDA allocations and elsewhere

The aim of the IDA is to provide concessional lending to the poorest countries. Since the late 1970s, this has been done based on a performance-based allocation system that uses the CPIA to assess policies and institutions. The details of the CPIA process have been outlined above. The governance components of CPIA do have a significant influence on the overall IDA allocation (Hout, 2004).

A detailed description of the process is provided in Annex 6. The CPIA is one important determinant for IDA allocations; but it is combined with other considerations, in particular, World Bank project performance (assessed through an Annual Report on Portfolio Performance (ARPP)), population and GNI per capita. The weighting of the CPIA governance/institutional scores in the overall allocation process is rather strong.

Interestingly, the Dutch have drawn on the IDA approach as the basis for their selection of aid focus countries (ibid.). The CPIA is also included as a component of DFID aid allocations. As discussed above, the CPIA focuses on a more 'managerial' set of issues, whilst in contrast, the MCC focuses also on political issues and more strongly on corruption.

### 5.2 The Millennium Challenge Corporation and its use of governance indices

The MCC is a new institution that administers additional US aid funds (the Millennium Challenge Account) to countries that are seen to be taking 'greater responsibility for their own development'. There are three main steps: (i) identifying *candidate* countries – i.e. those with low GNI – the main category is countries below \$1,675 (for FY 2007); and a supplementary category is lower-middle-income countries (LMICs) (those with per capita incomes between \$1,675 and \$3,465);<sup>27</sup> (ii) the MCC evaluates candidate countries according to three policy areas: ruling justly, investing in people, and economic freedom. It uses 16 independent indicators to assess these, which are composed of indicators focused on governance and others focused on outcomes (see Table 6).<sup>28</sup> Countries must score above the median on half of the indicators in each of these three broad groups, and must pass the 'control of corruption' indicator (i.e. achieving the upper half for their respective income group – lower or lower-middle income); (iii) there is also an element of Board discretion, if there are data issues or other factors of country performance that are not captured adequately in the data. Countries then prepare a compact for MCA funding.<sup>29</sup> The levels of funding can be substantial – for example, Ghana agreed a compact for approximately \$547 million over a five-year period.

<sup>27</sup> LMICs may receive up to 25% of all MCC allocations in a given year.

<sup>28</sup> For details of the process and countries, see the MCC website: [www.mcc.gov](http://www.mcc.gov)

<sup>29</sup> There is also a threshold programme. This is designed for countries that have not yet qualified for MCA Compact funding but have demonstrated commitment to improve performance. The threshold programme is designed to address specific policy or institutional weaknesses.



**Table 6: Indicators used by the MCC for country selection<sup>30</sup>**

Indicator	Category	Source
Civil liberties	Ruling justly	Freedom House
Political rights	Ruling justly	Freedom House
Voice and accountability	Ruling justly	World Bank Institute
Government effectiveness	Ruling justly	World Bank Institute
Rule of law	Ruling justly	World Bank Institute
Control of corruption	Ruling justly	World Bank Institute
Immunisation rate	Investing in people	World Health Organisation
Public expenditure on health	Investing in people	World Health Organisation
Girls' primary education completion rate	Investing in people	UNESCO
Public expenditure on primary education	Investing in people	UNESCO and national sources <sup>a</sup>
Cost of starting a business	Economic freedom	International Finance Corporation
Inflation rate	Economic freedom	IMF WEO
Days to start a business	Economic freedom	International Finance Corporation
Trade policy	Economic freedom	Heritage Foundation
Regulatory quality	Economic freedom	World Bank Institute
Fiscal policy	Economic freedom	National sources, cross-checked with IMF WEO <sup>b</sup>
Natural resource management index	Supplemental information	CIESIN/Yale
Land rights and access index	Supplemental information	IFAD/IFC

Notes: a) <http://www.mcc.gov/selection/indicators/nationalsources.php>; b) <http://www.imf.org/external/pubs/ft/weo/2006/02/data/index.aspx>

Source: [www.mcc.gov](http://www.mcc.gov)

The approach is innovative in that it is systematic in linking additional aid to country performance and is transparent. It is argued that this will:

- Channel aid to where it will be used more effectively;
- Reduce risk – this is particularly important for GBS as highlighted in the recent multi-donor evaluation;
- Generate an incentive for developing countries to improve governance;
- Reassure the public that their taxes are well spent.

Kaufman and Kraay (2002), as the source of some of the key indicators used by the MCC, highlight a number of relevant issues:

- There are large margins of error so particular care needs to be taken for borderline cases.
- Measuring improvements in governance is difficult (there may be a degree of stickiness in the ratings as expert and possibly even public opinion is influenced by previously published data on corruption).
- There are time lags with the KKZ data. These are now being reduced with the annual publication of data since 2006, however the time lag between the original collection of governance data, the aggregation process, and the publication of KKZ data can still be substantial.

The scores for certain countries are seen to not reflect the latest situation on the ground (e.g. Nepal or Palestine). Also, adding new indicators to the calculation of aggregate indicators can affect country scores, even if the actual situation has not changed. The MCC has established leeway for itself to take time lags and information gaps into account: 'The Board may also consider information to address gaps, time lags, trends in the data or other weaknesses in the indicators,

<sup>30</sup> The MCC is still searching for an indicator to assess natural resource management and is using interim indicators in the meantime.

and to assist in assessing whether MCC funds might reduce poverty and promote economic growth in a country'.<sup>31</sup> While the control of corruption indicator is given special emphasis (a country that does not meet this particular indicator is excluded from eligibility), the actual threshold is relatively low, given that it is the median of all low-income candidate countries that has to be reached, not an international benchmark. Thus, a country such as Nicaragua was eligible, despite its relatively high levels of corruption, while Zambia just missed the line and only made it into the group of threshold countries. Nicaragua was rated within the 35th percentile by KKZ for 2005 or -.62 on its -2.5 to +2.5 scale; and Zambia 23.2 or -.82. Both countries received a rating of 2.6 on TI's 1-10 scale for 2006.

The MCC determined the following countries as eligible for assistance for FY06 (four are already Irish Aid partners (*in italics*) – and one is potential): Armenia, Benin, Bolivia, Burkina Faso, Cape Verde, *East Timor*, El Salvador, Georgia, Ghana, Honduras, *Lesotho*, Madagascar, Mali, Mongolia, Morocco, *Mozambique*, Namibia, Nicaragua, Senegal, Sri Lanka, *Tanzania* and Vanuatu.

To date, a total of 18 countries have been selected for the MCA threshold programme. Eight were participants from 2005: Guyana, Kenya, Malawi, Paraguay, the Philippines, São Tomé and Príncipe, *Uganda* and *Zambia*. Five were selected in 2006: Indonesia, Jordan, Kyrgyz Republic, Moldova and Ukraine; and a further five were selected in 2007: Albania, Niger, Peru, Rwanda and Yemen. Threshold countries receive smaller amounts of funding (in the range of \$10-20 million) to support improvements within specific dimensions that are measured for MCC eligibility based on plans submitted by the country (these can be focused on the corruption indicator or on others). For example, Burkina Faso received such funding in 2005 to improve girls' primary education completion rates; while Malawi received funding for an anti-corruption programme.

Radelet (2005) argues that, overall, the MCA represents a positive innovation. While acknowledging that there are problems inherent in the choice and use of the 16 indicators on which the selection of countries is based, he lauds the approach on its transparency, ability to provide a 'pull'-based approach to inducing improvements in governments (rather than the more common 'push' approach adopted by donors), and the fact that it provides significant amounts of aid in ways which are more country-driven than many other forms of aid (except GBS). Radelet also emphasises, however, that the MCA is a useful approach for the allocation of *additional* aid, not one that could be used for all aid, and advocates that donors should develop a broader range of aid tools and strategies to use in different country (governance) contexts.

A point of criticism has been that the actual selection of countries (particularly among the group that is in principle eligible by passing the indicator tests) has not been sufficiently transparent. In particular, there was an apparent, but unstated, bias against non-democratic countries (Radelet et al., 2005a). Wider challenges of the MCC relate to compact size, speed of processing countries, compact content, and monitoring and evaluation (Radelet et al., 2005b).

The MCC has a lot of anecdotal evidence – from its own experience and those who produce the governance data (e.g. World Bank) – that there is an 'incentive' effect. In order to access the MCA, potentially eligible countries are seeking information on governance indicators and reforming in order to improve their positions. This has recently been supported by research from Harvard, which finds substantial evidence that countries respond to MCC incentives (Johnson and Zajonc, 2006).<sup>32</sup> However, realistically, it is too early to tell conclusively whether the MCC (or CPIA or other donor efforts at linking aid to governance) can trigger reforms to improve governance or in which countries they would do so.

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<sup>31</sup> [http://www.mcc.gov/selection/1006\\_Fact\\_Sheet\\_Selection\\_Process.pdf](http://www.mcc.gov/selection/1006_Fact_Sheet_Selection_Process.pdf)

<sup>32</sup> Given that the MCC uses medians for selection, prospective countries need to improve at a rate faster than the average in order to increase their position (and selected countries need to continue to improve to retain their position).

### 5.3 Other donors

What do other donors do in terms of linking governance data/categories to aid policy? The EC's European Development Fund (EDF) and a minority of bilateral donors (UK/DFID, the Netherlands, and possibly France in future) use allocation formulas to guide their aid-allocation decisions.

Some indicative examples include:

- The EU has a regional approach to development policy, with its main focus on ACP (African, Caribbean, Pacific) countries, and in particular Africa. In the 10th EDF, which funds development assistance to ACP countries, the EU has earmarked €3 bn to provide additional support to countries that have 'a credible plan of concrete actions and reforms', and that are positively assessed by the EU's recently launched governance profiles.<sup>33</sup> While the approach is somewhat similar in intent and scope to the MCC (which will be able to spend up to \$5 bn in countries worldwide), it is thus far less clearly developed and less transparent.
- The UK/DFID uses the CPIA as part of a model to inform their aid allocation across countries, and is a key factor influencing the amount of aid allocated.
- The Dutch also use the CPIA, but primarily as one indicator to help identify and select their list of 36 partner countries. They look at the levels and trends for various issues, with the main criteria being: development need (defined by IDA eligibility for an indication of low income and population); governance situation (using CPIA); need for aid; Dutch value added; and foreign-policy considerations.<sup>34</sup>
- Most donors also respond reactively to governance crises – human rights abuses, democratic reversals or cases of corruption for example, but these are generally *ad hoc* reactions.

Furthermore, an increasing number of donors link (or plan to link) political and qualitative governance assessments to overall country strategy and governance interventions. DFID's Drivers of Change analysis, Sida's 'power analysis'; and the World Bank's political-economy assessments provide more detailed country assessments. The Netherlands is planning to undertake Strategic Governance and Corruption Assessments in its 35 partner countries in 2007-8. USAID has two relatively well developed assessment tools – its Democracy and Governance Assessments and Corruption Assessments. These various assessments vary in terms of rigor, thematic coverage, and the time and effort put into them. Their actual use in informing policy development remains limited, however. Relatively few have been made public thus far, and there is also some concern that with more donors undertaking such assessments there will be a duplication of efforts (which the OECD GOVNET hopes to discuss in the second half of 2007).

Overall, the bottom line is that the MCC currently remains the most comprehensive attempt to use rigorous, transparent governance assessments and systematically link these to aid allocation and country programming, however it remains controversial for the issues outlined above.

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<sup>33</sup> See [http://www.europe-cares.org/africa/governance\\_en.html](http://www.europe-cares.org/africa/governance_en.html)

<sup>34</sup> For details see 'Mutual Interests, Mutual Responsibilities: Dutch Development Co-operation en route to 2015' (<http://www.minbuza.nl/>).

## 6. Some tentative policy implications for Irish Aid

This section seeks to draw some pertinent policy implications for Irish Aid. These are preliminary conclusions, based on the limited perspective of this Work Package, and should not be read as final. Broader considerations and trade-offs between different considerations will be discussed in the synthesis report.

We have seen that there are a growing number of sources of governance indicators. The CPIA and KKZ indicators are the two that cover developing countries and are produced regularly. These can assist management decisions, and can help make aid more effective, creating an incentive effect and reassuring taxpayers.

This is clearly a challenging area, however. Existing governance indicators are useful, but have limitations. It is difficult to make clear-cut decisions based on the data alone. Many countries lie between the extremes. The measures are based on perceptions and have significant margins of error making it difficult to accurately categorise countries, and categorisation also depends on the donor approach to governance issues – some focus more on instrumental issues (which governance issues matter for economic growth?) and others on constitutive issues (are human rights and democracy also a consideration?). A further challenge is that the quality of governance and the perceived political commitment to better governance varies over time, which may pose challenges for adjusting aid commitments.

Care is needed in making judgments about how governance varies across the developing world, what are the key issues for reform and whether and when aid should be provided in large quantities. Indicators should not be used in a mechanistic manner; judgment should always have a place. Not only for governance, but also since many other issues should affect aid decisions: levels of poverty, other aspects of need (what are the main constraints?), size of population, absorptive capacity, situation of other donors, etc.

However, there is a case that donors should link governance assessments to aid policy in general, and scaling up in particular. The key is to find nuanced positions regarding aid quantity, timeframe, breadth of activity, etc. based on rigorous governance assessments.

This section highlights some implications for Irish development co-operation policy, and will try to (briefly) address what governance data/categories mean for three key policy areas: (i) country selection for scaling up; (ii) country strategies and aid modalities; and (iii) governance interventions. These are clearly major, complex issues and only a few key points are made here.

### **6.1 Qualitative governance assessments**

One reaction among donors to the growing recognition that governance matters, and to the limits of quantitative governance indices, has been the commissioning of qualitative governance assessments as discussed in the previous section. This raises the question as to whether Irish Aid wants to commission such assessments.

We believe that in the context of Paris Declaration commitments on aid harmonisation and alignment, Irish Aid should not do so on its own. However, it may want to: a) discuss access to existing governance assessments carried out by other donors. These are currently not published, but even when there are concerns about publishing them, they should be shared more widely among donors; b) consider existing joint assessments and possibly also potential partner countries; c) consider focused governance assessments of specific sectors where Irish Aid is particularly active as these can be important in generating better interventions; and d) ensure adequate capacity at HQ to interpret governance indices and governance assessments carried out by others, in order to be able to advise embassies as well as to respond to concerns about

governance and aid policies that emerge among domestic stakeholders (Parliament, audit office, the media, NGOs, general public).

## **6.2 Country governance programme**

Governance is now widely held to be crucial for development and aid effectiveness. But, what governance aspects could Irish Aid focus on?<sup>35</sup> It is not possible to provide specific guidance in this paper (this will emerge from the other Work Packages on democratisation support, anti-corruption support, public-sector reforms, NEPAD, etc.), but rather to outline some broad aspects of strategy.

The broad definition of governance and the high priority attached to it has had an unfortunate result – developing countries are showered with governance issues to consider. Grindle has made the sensible call to distinguish between the ‘essential and the merely desirable’, which has led to debates surrounding what constitutes ‘good enough governance’.

The existing context assessment tools are a useful first step to identifying key issues. As suggested previously, this might include: DFID’s Drivers of Change analysis, Sida’s ‘power analysis’; World Bank political-economy assessments, the EU’s Governance Profiles and other helpful governance assessments (such as the WGA) and domestically generated assessments.<sup>36</sup> It will be important to stay engaged with developments at DFID, the World Bank and EU in this area.

Rather than be ideologically driven, in the short term it is important to start with where a country is: (i) what is the current situation with regard to the core governance agenda? What are the main barriers and weak points? (ii) strategically, it will then be important to focus on reforms that are politically feasible. Experience constantly reminds us that reform is a political not just a technical exercise; and (iii) local context will affect the approach taken. Experience highlights that countries often deal with similar challenges in quite different ways.

It is important to work in governance areas where progress looks possible – from administrative performance to state-market relations to the rule of law. In the longer term, however, advances in civil and political society are seen as a foundation for state legitimacy. Reforms to expand civil and political freedoms do not necessarily lead to accelerated economic performance, but they are important in their own right. And poor countries across the world – from Tanzania to Mongolia to Chile – have shown that you do not need to be rich to have relatively high standards of political governance.

For a comparatively small donor such as Irish Aid, there are a few key issues to consider: a) based on Grindle’s concern to be careful with ‘adding’ specific governance demands on a country, a more useful emphasis may be to help countries think through and implement commitments to improving governance that they have made, for example, to the EU; b) it may be most useful, as with the assessments, to focus on governance issues within sectors in which Irish Aid is particularly active (e.g. improving transparency, accountability and effectiveness in the health sector of a country).

## **6.3 Governance measurements as inputs to country selection and choice of aid modalities**

As part of its effort to scale up aid, Irish Aid is considering expanding its number of partner countries, and several potential partners have already been suggested (discussed previously).

Governance indices can provide some helpful guidance in choosing additional partner countries and in deciding the use of aid modalities. Importantly, as reflected in the discussion above,

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<sup>35</sup> This section draws on Court (2006) – see: [www.odi.org.uk/wga\\_governance/](http://www.odi.org.uk/wga_governance/)

<sup>36</sup> The World Bank Institute also carries out specific institutional diagnostics (in key organisations such as tax and customs authorities) that can help set benchmarks, monitor governance situations and provide the basis for interventions to improve governance at the institutional level.

governance can be an important, but not a singular criterion. Other important criteria are need/poverty levels; existing aid flows and donors to a country; and international peace/stability (e.g. in supporting fragile and post-conflict states).

One relatively easy strategy for country selection is to focus on poor, but peaceful and well-governed countries, where aid is quite likely to be effectively used. However, relatively few countries fit this description; and those that do generally already receive quite high levels of aid. Mali quite closely approximates such a case. Nonetheless, aiding those countries that are better governed is consistent with the intention to build incentives and rewards for better governance into the international aid system – as long as this does not result in neglect of those that are relatively poorly governed.

Furthermore, from a governance perspective, the following broad assessments can be made of potential partner countries:

- Ethiopia has become more problematic – ratings have significantly worsened on all six KKZ indicators since 1998 and the country scored poorly (even before recent problems).
- Kenya is being considered by Irish Aid – it has opportunities since donor perceptions of performance tend to be worse than suggested by the data.

Countries that are currently not being considered by Irish Aid but are performing well from a governance perspective are Ghana and Madagascar. Ghana scores well on CPIA and KKZ indicators and is ‘waking up’ – it might be considered by Irish Aid. So too Madagascar, which scores relatively well on CPIA and KKZ indicators. This is an MCC compact country and might also be interesting for Irish Aid for historical and geographical reasons.

These considerations should be taken to be very indicative. If Irish Aid decides on a new partner country, it is likely to establish aid programmes for a number of years, during which various changes in the quality of governance may occur. Taking governance into account should not mean excluding countries from aid programmes, but it may be worthwhile to justify choices in the light of low governance performance explicitly – e.g. in the case of support to ‘difficult cases’ such as Zimbabwe, or to a post-conflict country such as Sierra Leone.

As donors are working in countries with good as well as relatively poor governance contexts, this raises questions of choice of aid modality and policies in terms of quantity of aid, recipient interlocutor and type of activity.

There tends to be a consensus regarding ways to orient the level and type of aid according to the specific conditions in each country. For well-governed poor countries, it makes sense to provide more aid over longer periods through direct budget support to governments, and thus for the range of development activities defined by the country. For poorly governed countries, the approach might mean the provision of limited amounts of aid for shorter periods, for humanitarian response directed through NGOs and oriented towards improving governance.

The table below provides a preliminary, generic outline of what governance assessments might mean in terms of aid modality. Capacity is used here to mean the ability of governments to deliver and use aid well (assessed by the CPIA or KKZ indicators on government effectiveness, rule of law and control of corruption), and accountability to refer to issues of political accountability and checks and balances (assessed using the KKZ indicator on voice and accountability).

We suggest that the greater capacity and accountability, the more scope there is for working with government, providing funding through government systems (GBS) and working on more complicated issues. We suggest that Irish Aid should look carefully at the voice and accountability indicators to inform decisions about where budget support is being used.

**Table 7: Who, how, what? Some preliminary suggestions of how to match intervention to context**

Context	Key partner	How (key modality)	What issues (and governance)
Adequate capacity and accountability (e.g. Lesotho or Tanzania)	Government	GBS	Complicated issues
Adequate capacity/lower accountability (e.g. Vietnam)	Government	Compacts, SWAps or GBS	Complicated interventions (accountability support)
Lower capacity/adequate accountability (e.g. East Timor)	Government	SWAps or projects	Simple interventions (capacity support)
Middle (e.g. Kenya)	Government	SWAps or projects	Simple interventions (broad governance support)
Weak (e.g. Zimbabwe)	NGOs and government	Projects	Basic state functions (basic but broad governance support)

Note: The context descriptors in this table refer to relative comparisons across poorer countries. In global comparison, poor countries understandably score less well than OECD countries.

Many countries will fall between the extremes, where perhaps identifying an appropriate aid strategy seems a little more straightforward. The key is to find nuanced positions regarding quantity, timeframe, breadth of activity and type of aid based on rigorous governance assessments.

The first step should be to draw on existing governance data (as above) and governance and political context assessments that have been conducted in Irish Aid partner countries. Assessments of the quality of public financial management systems (PEFA assessments; CFAAs) will also play an important role when deciding whether budget support is to be used.

The next step is to orient the level and type of aid according to the specific conditions in each country. This is outlined in a crude manner in the table above. It would need to be in a much more rigorous and nuanced way across Irish Aid partner countries; also taking into account what aid modalities are being used by other donors.

There are a number of other considerations:

- the findings of governance assessments and the aid-governance ‘agreement’ between Irish Aid and recipient partners should be made clearer – this could help avoid a start-stop approach to aiding more difficult contexts;
- donor support (especially in heavily-aided countries) should not diminish accountability to domestic stakeholders such as local parliaments, private sector and civil society actors;<sup>37</sup>
- donors should work together more – this improves the systemic impact of linking aid to governance issues.

A final challenge is to be realistic about the lengthy time it takes for governance constraints to be overcome. Recent arguments to dramatically increase aid seem to assume that governance can be improved *quickly*, thus enabling aid revenues to be boosted. However, if history teaches us anything, it is that there is usually no shortcut to building sound institutions in the poorest countries and that providing external assistance to such initiatives is difficult.

<sup>37</sup> We believe donors should encourage consultation and information sharing between the executive branch agencies and the legislature, opposition parties, private sector and civil society actors. At the very least, agreements must be widely publicised to facilitate monitoring.

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## Interviews

- Brian Levy, Advisor, Public-sector Governance, Poverty Reduction and Economic Management, World Bank
- Greg Kisunko, World Bank
- Steve Knack, Development Research/Public-sector Governance, World Bank
- Phil Keefer, World Bank
- Massimo Mastruzzi, WBI
- Brad Parks, MCC
- Joel Barkan, University of Iowa
- Dennis de Tray, CGD
- Others from CGD

**Annex 1: 2005 IDA Resource Allocation Index (IRAI)<sup>a</sup> (countries ranked by IRAI)**

Rank	Country	A. Economic management			B. Structural policies				C. Policies for social inclusion/equity						D. Public-sector management and institutions						IDA Resource Allocation Index (IRAI)	Policy average	
		1	2	3	4	5	6	Average	7	8	9	10	11	Average	12	13	14	15	16	Average			
		Macro. management	Fiscal policy	Debt policy	Average	Trade	Financial sector	Business regulatory environment	Average	Gender equality	Equity of public resource use	Building human resources	Social protection & labour	Pol. & instit. for environ. sustain.	Average	Property rights & rule-based govern.	Quality of budgetary & finan. mgt.	Effic. of revenue mobilisation	Quality of public Administration	Transparency, accountability & corruption in public sector	Average		
1	Armenia	5.5	5.0	5.5	5.3	4.5	3.5	4.0	4.0	4.5	4.5	4.0	4.5	3.5	4.2	3.5	4.0	4.0	4.0	3.5	3.8	4.3	4.5
2	Cape Verde	4.5	4.0	4.0	4.2	4.0	4.0	4.0	4.0	4.5	4.5	4.0	4.5	4.0	4.3	4.0	3.5	3.5	4.0	4.5	3.9	4.1	4.2
3	Samoa	4.0	3.5	4.0	3.8	4.5	4.0	4.0	4.2	4.0	4.0	4.0	3.5	4.0	3.9	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.0
4	St. Lucia	4.5	3.5	4.0	4.0	4.0	4.0	4.5	4.2	4.5	3.5	4.0	3.5	3.5	3.8	4.0	4.0	3.5	3.5	4.5	3.9	4.0	4.0
5	Tanzania	5.0	4.5	4.0	4.5	4.0	3.5	3.5	3.7	4.0	4.0	4.0	3.5	3.5	3.8	3.5	4.5	4.0	3.5	3.5	3.8	3.9	4.0
6	St. Vincent & The Grenadines	4.0	4.0	4.0	4.0	4.0	4.0	4.5	4.2	4.5	3.5	4.0	3.5	3.5	3.8	4.0	3.5	3.5	3.5	4.0	3.7	3.9	4.0
7	Honduras	4.5	4.5	4.0	4.3	4.5	3.5	4.0	4.0	4.0	4.0	4.0	4.0	3.0	3.8	3.5	4.0	4.0	3.0	3.0	3.5	3.9	4.0
8	Uganda	4.5	4.5	4.5	4.5	4.0	3.5	4.0	3.8	3.5	4.5	4.0	3.5	4.0	3.9	3.5	4.0	3.0	3.0	3.0	3.3	3.9	4.1
9	Ghana	4.0	4.5	4.0	4.2	4.0	3.5	4.0	3.8	4.0	4.0	3.5	3.5	3.5	3.7	3.5	3.5	4.5	3.5	3.5	3.7	3.9	3.9
10	Georgia	4.5	4.0	4.0	4.2	3.5	3.5	4.0	3.7	4.5	4.0	4.0	3.5	3.5	3.9	3.5	3.5	4.0	3.5	3.5	3.6	3.8	3.9
	Maldives	3.5	3.5	4.5	3.8	4.0	4.0	4.0	4.0	4.0	4.0	4.0	3.5	4.0	3.9	4.0	3.0	4.0	4.0	3.0	3.6	3.8	3.9
12	Bhutan	4.0	4.0	4.0	4.0	3.0	3.0	3.5	3.2	4.5	4.0	4.5	3.5	4.5	4.2	3.5	3.5	4.0	4.0	4.0	3.8	3.8	3.8
13	Dominica	4.0	4.0	3.0	3.7	4.0	4.0	4.5	4.2	4.5	3.5	4.0	3.5	3.0	3.7	4.0	3.0	3.5	3.5	4.0	3.6	3.8	3.8
14	India	4.5	3.0	4.5	4.0	3.5	4.0	3.5	3.7	3.5	4.0	4.0	3.5	3.5	3.7	3.5	4.0	4.0	3.5	3.5	3.7	3.8	3.8
15	Burkina Faso	4.5	4.5	4.5	4.5	4.0	3.0	3.0	3.3	3.5	4.0	3.5	3.5	3.5	3.6	3.5	4.0	3.5	3.5	3.5	3.6	3.8	3.8
16	Senegal	4.5	4.0	4.0	4.2	4.5	3.5	3.5	3.8	3.5	3.5	3.5	3.0	3.5	3.4	3.5	3.5	4.5	3.5	3.0	3.6	3.8	3.8

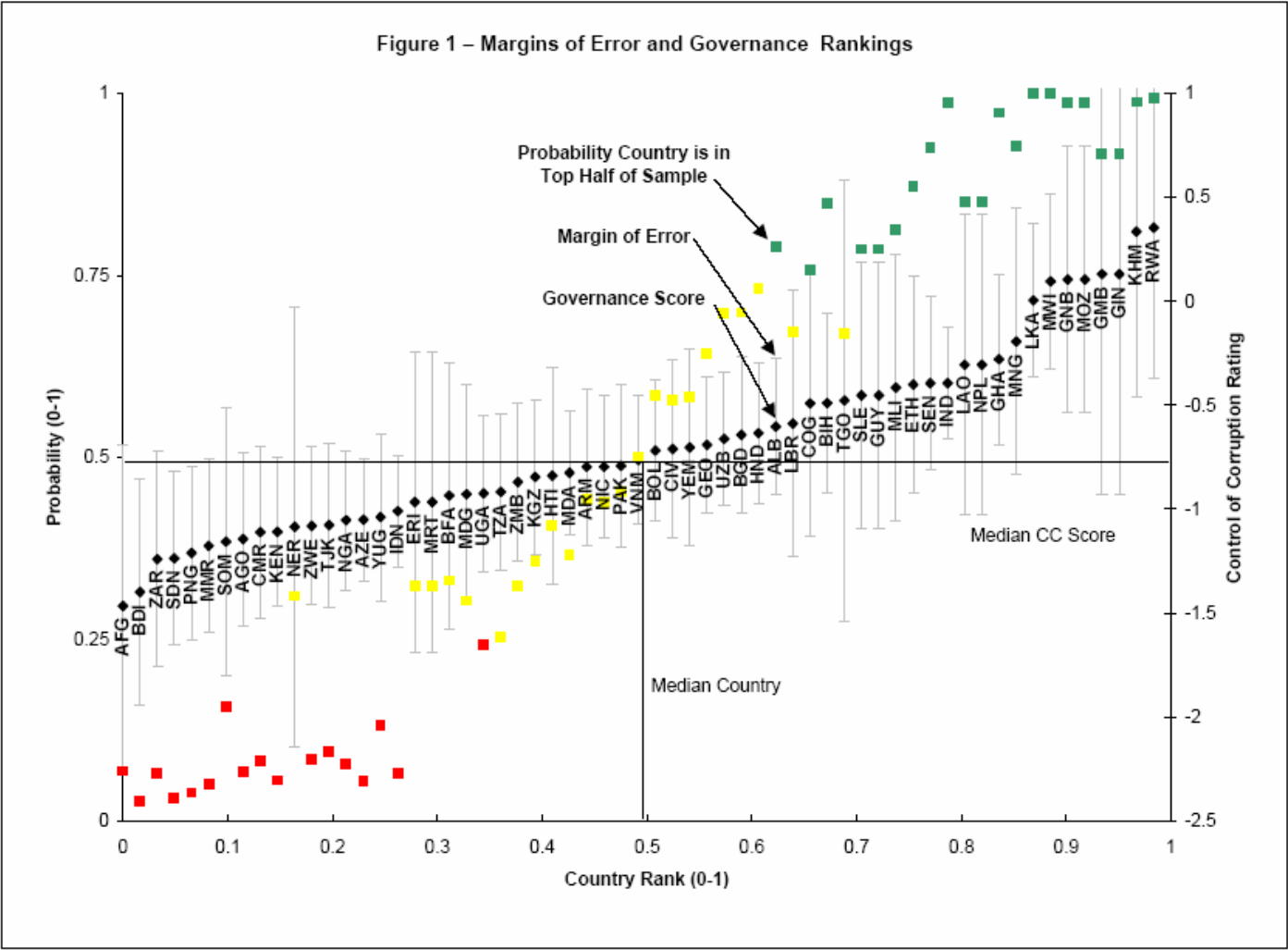
17	Vietnam	5.0	4.0	4.0	4.0	4.3	3.5	3.3	4.5	4.0	4.0	4.0	4.0	3.0	3.5	3.0	3.5	3.8	3.5	4.0	3.5	3.0	3.5	3.7	3.8
18	Nicaragua	3.5	4.0	4.5	4.0	4.0	4.5	3.5	4.0	4.5	4.0	4.0	3.5	3.0	3.5	3.5	3.5	3.7	4.0	3.5	4.0	3.5	3.5	3.7	3.8
19	Bolivia	4.0	4.0	4.0	4.0	4.0	5.0	3.0	3.5	4.0	4.0	4.0	4.0	3.5	3.0	3.5	4.0	3.7	4.0	3.5	4.0	3.0	3.3	3.7	3.8
20	Mali	4.5	4.0	4.5	4.3	4.3	4.0	3.5	3.5	3.5	3.5	3.5	3.5	3.0	3.5	3.0	4.0	3.4	3.0	4.0	3.0	3.5	3.6	3.7	3.7
21	Serbia & Montenegro	3.5	4.5	3.5	3.8	3.5	4.5	3.0	3.5	3.5	4.0	3.5	4.0	3.0	3.5	4.0	3.5	3.9	3.5	3.5	4.0	3.0	3.4	3.7	3.8
22	Grenada	4.0	3.0	2.5	3.2	3.2	4.0	3.5	4.5	4.0	3.5	4.0	3.5	3.5	4.0	3.5	4.0	3.9	3.5	3.5	4.0	3.7	3.7	3.7	3.7
23	Albania	4.5	3.5	4.0	4.0	4.0	4.5	3.5	4.0	4.5	3.5	3.0	3.0	3.5	3.0	3.5	3.0	3.4	3.0	3.5	3.0	3.0	3.3	3.7	3.8
24	Pakistan	4.5	3.5	4.5	4.2	4.2	4.0	4.5	4.0	4.5	3.5	3.5	3.5	3.0	3.5	3.0	3.5	3.1	3.5	3.5	2.5	3.2	3.7	3.7	3.8
25	Azerbaijan	4.5	4.5	4.5	4.5	4.5	4.0	3.0	3.5	3.5	3.0	3.5	3.0	3.0	3.5	3.0	3.0	3.4	3.5	3.5	2.5	3.2	3.7	3.7	3.8
	Benin	4.5	4.0	3.5	4.0	4.0	4.5	3.5	4.0	4.5	3.0	3.0	3.5	3.0	3.5	3.0	3.0	3.2	3.5	3.5	3.5	3.4	3.7	3.7	3.7
	Indonesia	4.5	4.0	4.5	4.3	4.3	4.5	3.5	3.0	3.7	4.0	3.5	3.5	2.5	3.4	2.5	3.5	3.4	3.5	3.5	3.0	3.2	3.7	3.7	3.8
28	Sri Lanka	3.5	3.0	3.5	3.3	3.3	3.5	4.0	4.0	3.8	4.0	3.5	4.5	3.5	3.5	3.5	3.5	3.8	3.5	4.0	3.5	3.5	3.6	3.7	3.7
29	Kenya	4.5	4.0	4.0	4.2	4.0	4.0	3.5	4.0	3.8	3.0	3.0	3.5	3.0	3.0	3.0	4.0	3.1	3.5	4.0	3.0	3.3	3.6	3.7	3.7
30	Bosnia & Herzegovina	4.0	3.5	4.0	3.8	4.0	4.0	4.0	3.5	3.8	4.0	3.0	3.5	3.5	3.0	3.0	4.0	3.4	3.0	3.5	3.0	3.3	3.6	3.7	3.7
31	Madagascar	3.5	3.0	3.5	3.3	3.3	4.0	3.5	4.0	3.8	3.5	3.5	3.5	3.5	4.0	3.5	3.5	3.6	3.0	3.5	3.5	3.4	3.5	3.6	3.6
32	Kyrgyz Rep.	4.5	3.5	4.0	4.0	4.0	4.5	3.5	3.5	3.8	4.0	3.5	3.5	3.5	3.0	2.5	2.5	3.5	3.0	3.0	2.7	3.5	3.5	3.8	3.8
33	Lesotho	4.0	4.0	4.0	4.0	4.0	3.5	3.5	3.5	3.3	4.0	3.0	3.5	3.0	3.0	4.0	3.5	3.3	3.0	4.0	3.0	3.4	3.5	3.5	3.5
34	Moldova	3.5	3.5	3.0	3.3	3.3	3.5	3.5	4.0	3.7	4.5	3.5	4.0	3.5	3.0	3.0	3.0	3.8	3.5	3.0	3.0	3.2	3.5	3.5	3.6
35	Rwanda	4.0	3.5	3.0	3.5	3.5	3.5	3.5	3.5	3.5	3.5	4.0	4.0	3.5	3.5	3.0	3.5	3.6	3.5	3.5	3.0	3.3	3.5	3.5	3.5
36	Mozambique	4.0	4.0	4.5	4.2	4.2	4.0	2.5	3.0	3.2	3.5	3.5	3.5	3.0	3.0	3.0	3.0	3.3	3.5	3.5	3.0	3.2	3.5	3.5	3.5
37	Mongolia	4.0	3.5	3.0	3.5	3.5	4.5	3.0	3.5	3.7	3.5	3.5	3.5	2.5	3.3	3.0	4.0	3.3	3.0	3.5	2.5	3.3	3.4	3.5	3.5
38	Bangladesh	4.0	3.5	4.5	4.0	4.0	3.0	3.0	3.5	3.2	4.0	3.5	4.0	3.5	3.0	3.0	3.0	3.6	3.0	3.0	2.5	2.9	3.4	3.6	3.6
39	Ethiopia	3.5	4.0	3.5	3.7	3.7	3.0	3.0	3.5	3.2	3.0	4.5	3.5	3.5	3.5	2.5	4.0	3.6	3.5	4.0	3.0	3.1	3.4	3.5	3.5

40	Guyana Malawi	3.5	3.5	3.5	3.0	3.5	4.0	3.5	3.0	3.5	3.0	3.0	3.5	3.5	2.5	3.0	3.1	3.4	3.4
42	Nepal Tajikistan	4.5	3.5	3.5	3.8	4.0	4.0	3.0	3.0	3.5	3.0	3.0	3.2	3.5	3.0	2.5	3.0	3.3	3.5
44	Zambia	3.5	3.5	3.0	3.3	4.0	4.0	3.0	3.0	3.5	3.0	3.5	3.4	4.0	3.0	3.0	3.2	3.3	3.4
45	Yemen, Rep.	4.0	3.0	4.5	3.8	4.5	2.5	3.0	3.0	3.3	3.5	3.0	3.1	3.0	3.0	3.0	2.9	3.3	3.4
46	Cameroon	4.0	3.5	2.5	3.3	3.5	3.0	3.5	3.5	3.3	3.0	3.5	4.0	3.0	3.0	2.5	3.1	3.3	3.4
47	Niger	3.5	3.0	3.5	3.3	4.0	3.0	3.5	3.5	3.5	3.0	3.0	3.0	3.5	3.0	3.0	3.2	3.3	3.3
48	Mauritania	2.0	2.5	4.0	2.8	4.5	2.5	3.5	3.5	3.5	3.5	3.5	3.4	4.0	3.0	2.5	2.9	3.2	3.2
49	Kiribati	2.5	2.5	5.0	3.3	3.0	3.0	3.0	3.0	3.0	2.5	3.0	3.0	3.5	3.0	3.5	3.3	3.2	3.1
50	Djibouti	3.5	3.0	3.0	3.2	4.0	3.5	3.0	3.0	3.5	3.0	3.0	3.1	2.5	2.5	2.5	2.8	3.1	3.3
	Nigeria	4.0	4.0	3.5	3.8	2.5	3.0	3.0	3.0	2.8	3.0	3.0	3.1	2.5	3.0	2.5	2.8	3.1	3.3
	Vanuatu	3.0	3.0	4.0	3.3	4.0	3.0	3.0	3.0	3.3	2.5	2.0	2.8	3.0	3.5	3.0	3.1	3.1	3.2
53	Sierra Leone	4.0	3.5	3.5	3.7	3.5	3.0	2.5	3.0	3.0	3.0	2.5	2.9	2.5	3.0	2.5	2.9	3.1	3.2
54	Papua New Guinea	4.0	3.0	3.5	3.5	4.0	3.0	3.0	3.0	3.3	2.5	3.0	1.5	2.5	3.0	3.0	3.1	3.1	3.1
55	Cambodia	4.0	3.5	3.5	3.7	3.5	2.0	3.5	3.0	3.0	3.5	2.5	3.1	2.5	2.5	2.5	2.6	3.1	3.3
56	Gambia, The	3.5	3.0	2.5	3.0	4.0	3.0	3.0	3.0	3.3	3.5	2.5	3.0	3.5	3.0	2.0	2.9	3.1	3.1
57	Guinea	2.5	3.0	2.5	2.7	4.5	3.0	3.0	3.0	3.5	3.0	3.5	3.2	2.0	3.0	2.5	2.7	3.0	3.1
58	Uzbekistan	3.0	3.5	4.0	3.5	2.5	2.5	2.5	2.5	2.5	4.0	3.5	3.6	2.0	2.5	1.5	2.4	3.0	3.2
59	Lao, Pdr	4.0	3.5	3.5	3.7	3.5	1.5	3.0	3.0	2.7	3.0	2.0	3.1	3.0	2.5	2.0	2.5	3.0	3.1
60	Sao Tome & Principe	3.0	3.0	2.5	2.8	4.0	2.5	3.0	3.0	3.2	2.5	2.5	2.8	2.5	3.0	3.5	3.1	3.0	2.9
61	Burundi	3.5	3.5	3.0	3.3	3.0	3.0	2.5	3.0	2.8	3.5	3.0	3.0	2.5	2.5	3.0	2.7	3.0	3.1
62	Tonga	3.0	2.0	3.5	2.8	3.0	3.0	3.0	3.0	3.0	2.5	4.0	3.2	3.5	2.5	2.0	2.7	2.9	3.0

63	Chad	4.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	2.5	3.0	2.8	2.0	2.4	2.9	3.0
64	Congo, Dem. Rep.	3.5	3.5	2.5	3.2	4.0	2.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	2.5	2.5	2.8	2.0	2.3	2.8	3.0
65	Solomon Islands	3.5	3.5	2.5	3.2	3.0	3.0	3.0	2.5	2.8	3.0	3.0	3.0	3.0	2.5	2.5	2.0	2.7	2.8	3.0	2.6	2.8	2.9
66	Congo, Rep	3.5	3.0	2.5	3.0	3.0	2.5	3.0	2.5	2.7	3.0	3.0	3.0	3.0	2.5	3.0	3.0	2.9	2.8	2.5	2.6	2.8	2.9
67	Haiti	3.5	3.0	2.5	3.0	4.0	3.0	3.0	2.5	3.2	3.0	2.5	2.5	2.5	2.5	2.5	2.5	2.6	2.8	2.0	2.3	2.8	2.9
68	Guinea-Bissau	2.5	2.5	2.0	2.3	3.5	2.5	3.0	2.5	3.0	3.0	3.0	2.5	2.5	2.5	3.0	3.0	2.8	2.7	2.5	2.6	2.7	2.7
69	Sudan	3.5	3.5	1.5	2.8	3.0	2.5	3.0	2.5	2.8	2.0	2.5	2.5	2.0	2.5	2.5	2.5	2.3	2.6	2.0	2.4	2.6	2.7
70	Angola	3.0	2.5	2.0	2.5	4.0	2.5	2.0	2.5	2.8	3.0	2.5	2.5	2.5	2.5	2.5	2.5	2.6	2.6	2.5	2.4	2.6	2.6
71	Eritrea	2.0	2.0	2.5	2.2	1.5	2.0	2.0	2.0	1.8	3.5	3.0	3.5	3.0	3.0	3.0	3.0	3.2	2.5	2.5	2.8	2.5	2.4
72	Côte d'Ivoire	2.5	2.0	1.5	2.0	3.5	3.0	3.0	3.0	3.2	2.5	1.5	2.0	2.5	2.5	3.0	3.0	2.3	2.0	2.0	2.5	2.5	2.5
	Togo	2.5	2.0	1.5	2.0	4.0	2.5	3.0	3.0	3.2	3.0	2.0	3.0	2.5	2.5	2.0	2.5	2.6	2.5	2.0	2.2	2.5	2.6
74	Comoros	3.0	2.5	1.5	2.3	2.0	2.5	2.5	2.5	2.3	3.0	3.0	3.0	2.5	2.0	2.5	2.5	2.7	2.5	2.5	2.3	2.4	2.5
75	Central Afr. Rep.	3.0	3.0	1.5	2.5	3.5	2.5	2.0	2.0	2.7	2.5	2.0	2.0	2.0	2.5	2.0	2.5	2.2	2.0	2.5	2.2	2.4	2.5
76	Zimbabwe	1.0	1.0	1.0	1.0	1.0	2.5	2.0	2.0	2.2	2.5	1.5	2.0	1.5	2.5	3.5	2.0	2.0	1.5	2.1	1.8	1.7	1.7

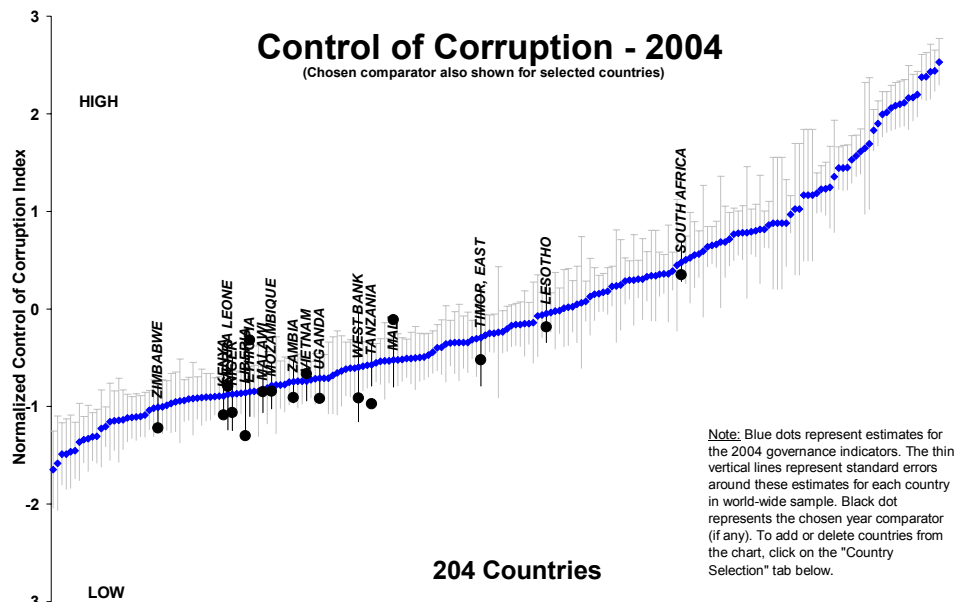
Notes: a) Five IDA countries excluded since not rated in IRAJ 2005 exercise (Afghanistan, Liberia, Myanmar, Somalia, and Timor-Leste). For calculation of the cluster averages, all criteria are equally weighted within a cluster; IRAJ is calculated as the mean of the score of four clusters. Scale: 1 = Lowest, 6 = Highest. Rankings are based on un-rounded data.  
Source: World Bank (2006b).

# Annex 2: Margins of error and corruption rankings

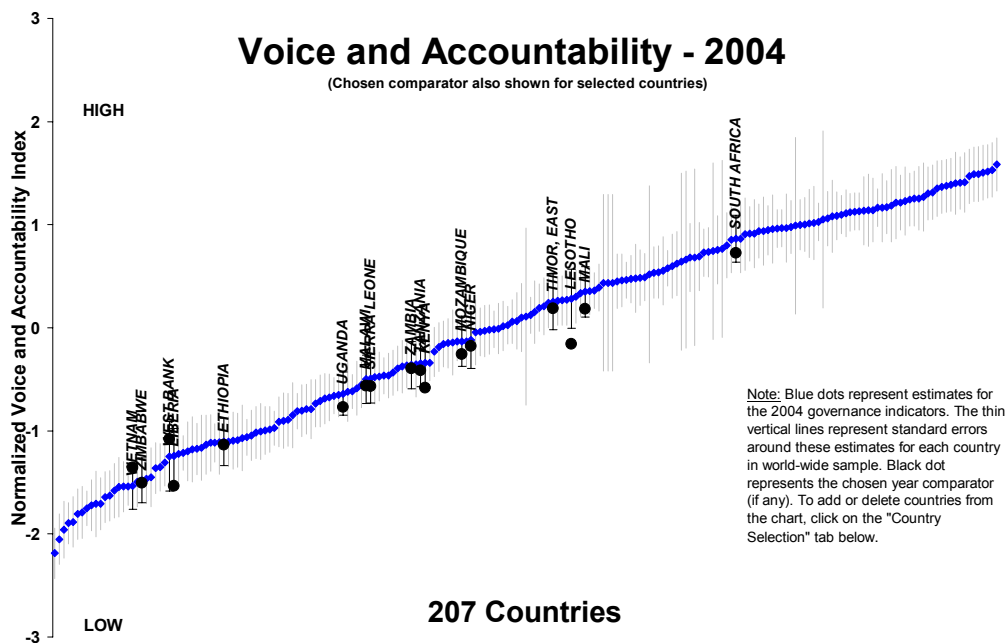


Source: Kaufmann and Kraay (2002).

# **Annex 3: KK governance indicators: Irish Aid countries in comparative perspective**

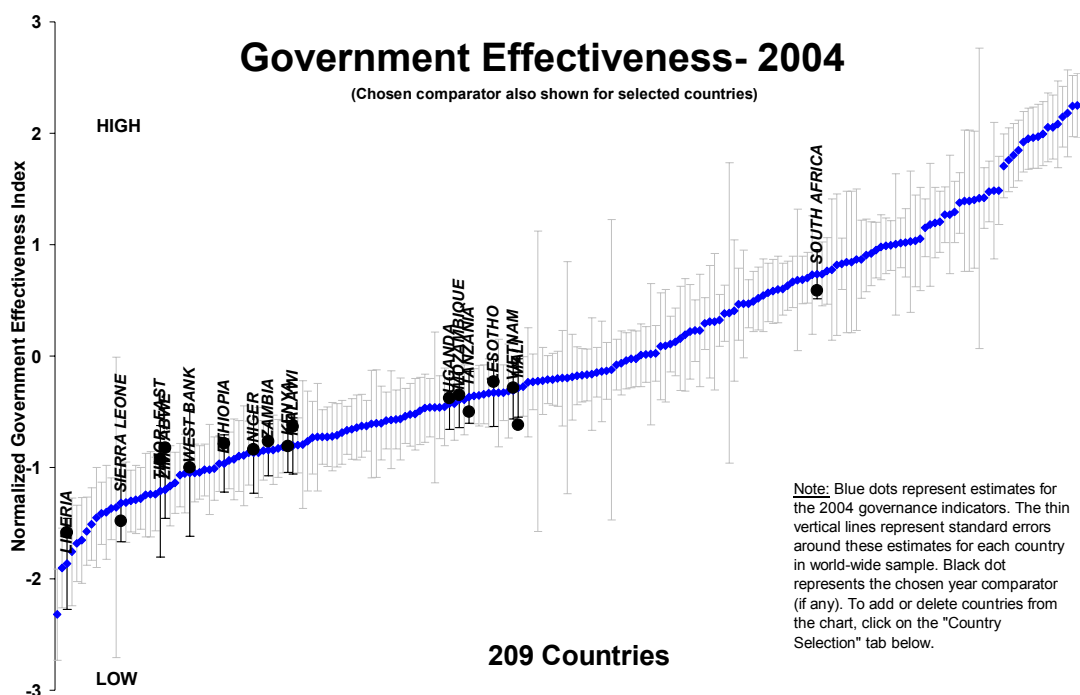


Source: "Governance Matters IV: Governance Indicators for 1996-2004" by Daniel Kaufmann, Aart Kraay and Massimo Mastruzzi, 2005.  
**Disclaimer:** The governance indicators presented here reflect the statistical compilation of responses on the quality of governance given by a large number of enterprise, citizen and expert survey respondents in industrial and developing countries, as reported by a number of survey institutes, think tanks, non-governmental organizations, and international organizations. The aggregate indicators in no way reflect the official position of the World Bank, its Executive Directors, or the countries they represent. As discussed in detail in the accompanying papers, countries' relative positions on these indicators are subject to margins of error that are clearly indicated. Consequently, precise country rankings should not be inferred from this data.



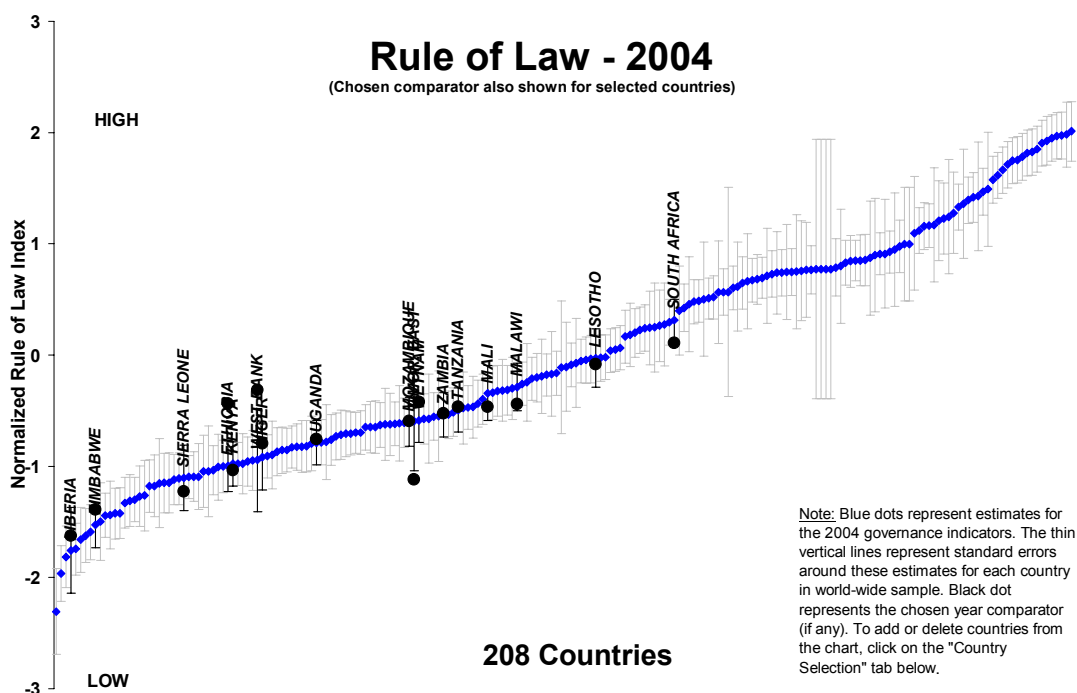
Source: "Governance Matters IV: Governance Indicators for 1996-2004" by Daniel Kaufmann, Aart Kraay and Massimo Mastruzzi, 2005.  
**Disclaimer:** The governance indicators presented here reflect the statistical compilation of responses on the quality of governance given by a large number of enterprise, citizen and expert survey respondents in industrial and developing countries, as reported by a number of survey institutes, think tanks, non-governmental organizations, and international organizations. The aggregate indicators in no way reflect the official position of the World Bank, its Executive Directors, or the countries they represent. As discussed in detail in the accompanying papers, countries' relative positions on these indicators are subject to margins of error that are clearly indicated. Consequently, precise country rankings should not be inferred from this data.





Source: "Governance Matters IV: Governance Indicators for 1996-2004 " by Daniel Kaufmann, Aart Kraay and Massimo Mastruzzi, 2005.

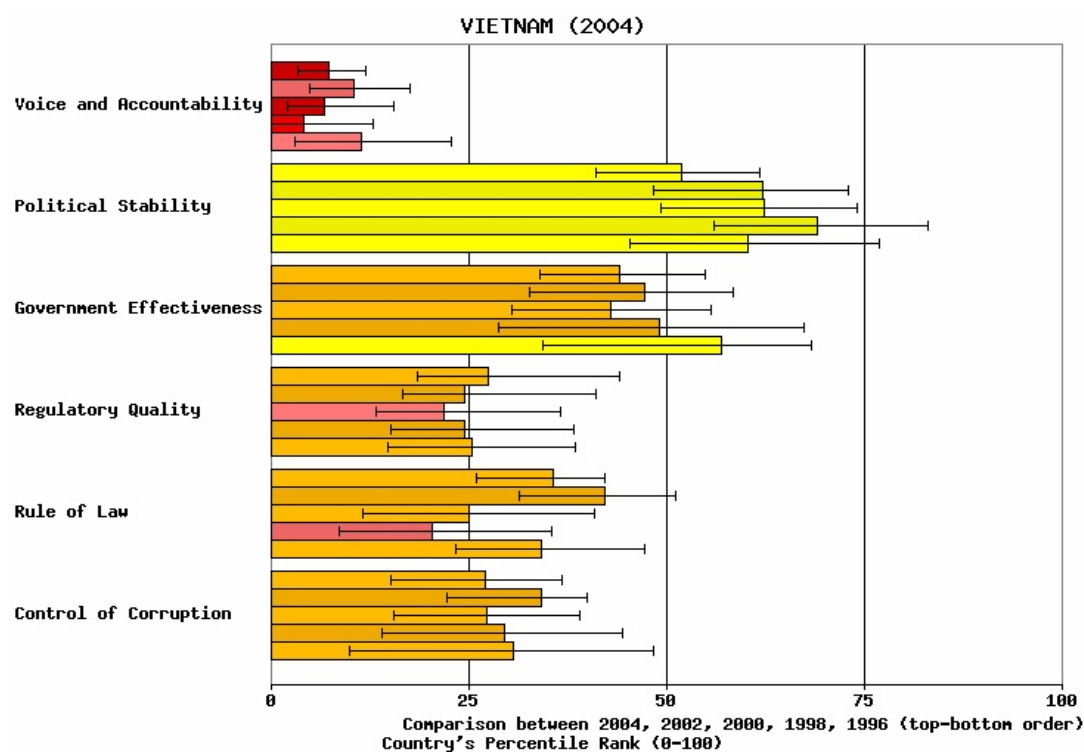
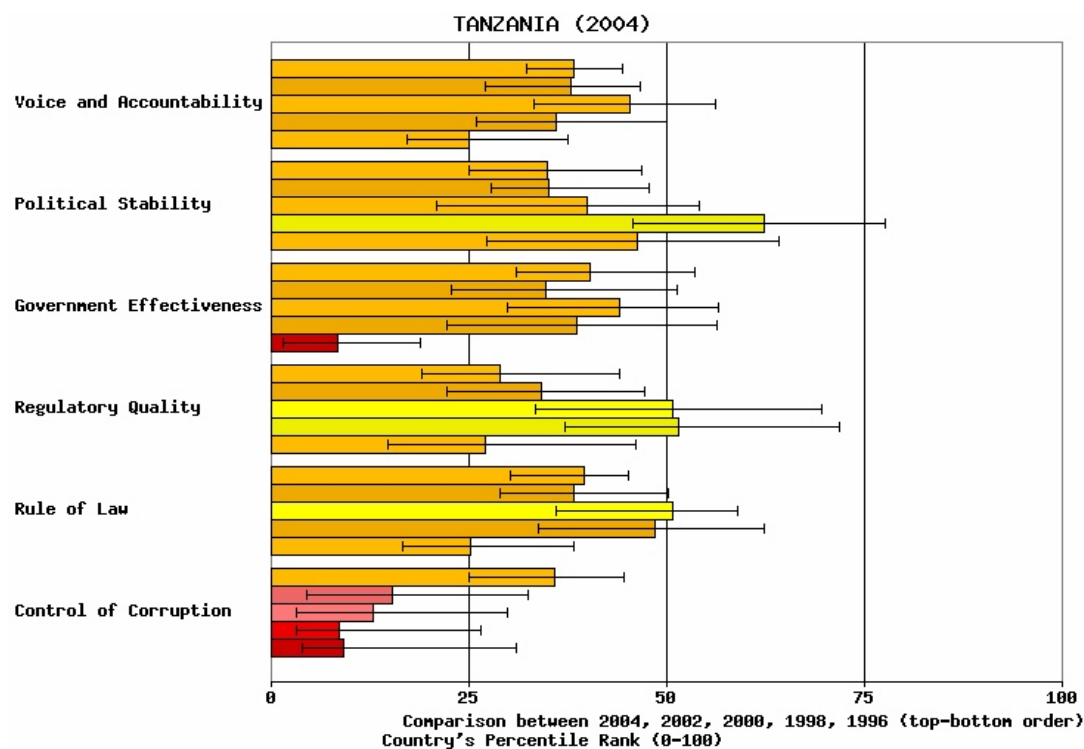
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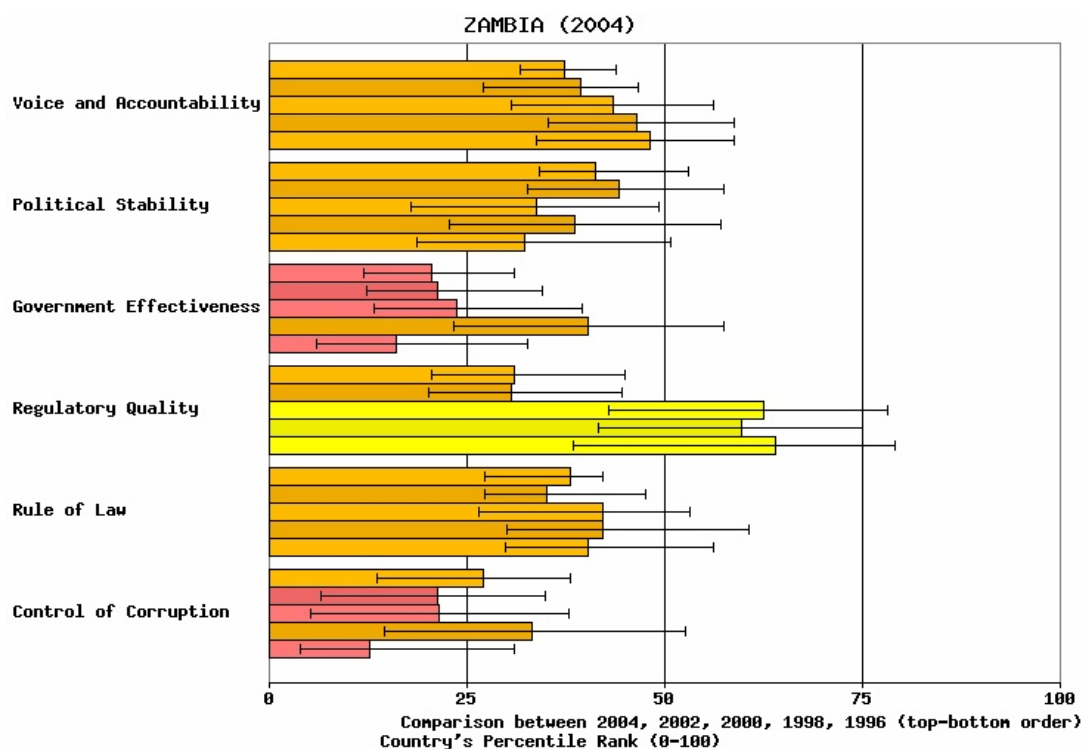
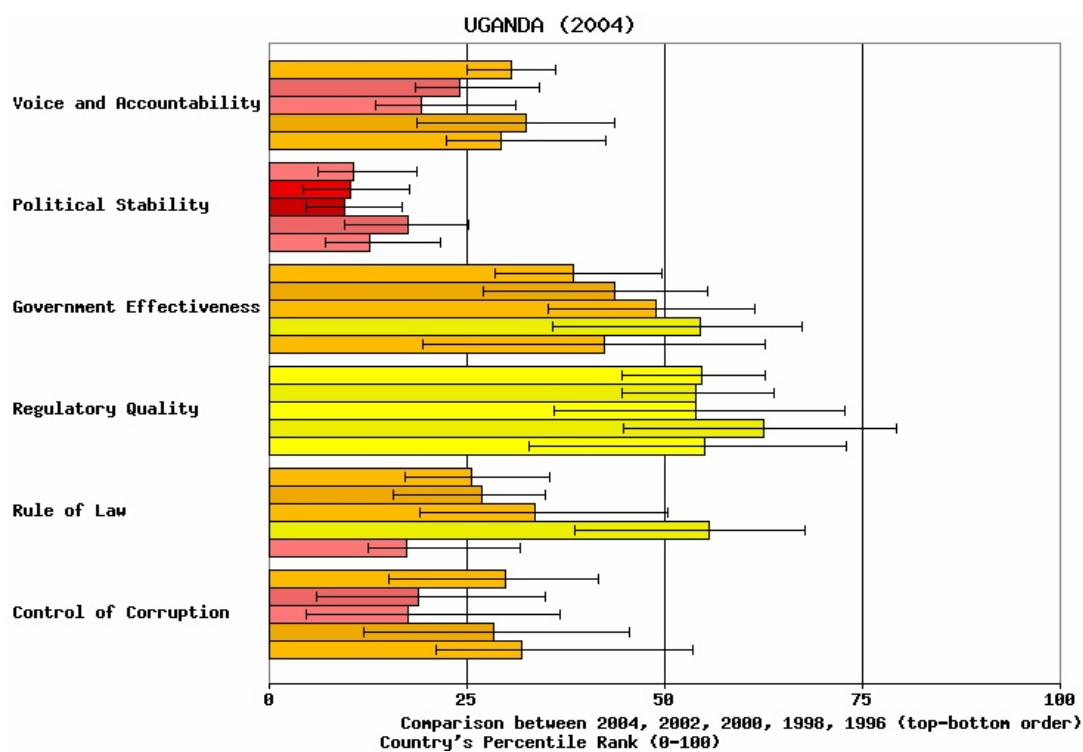


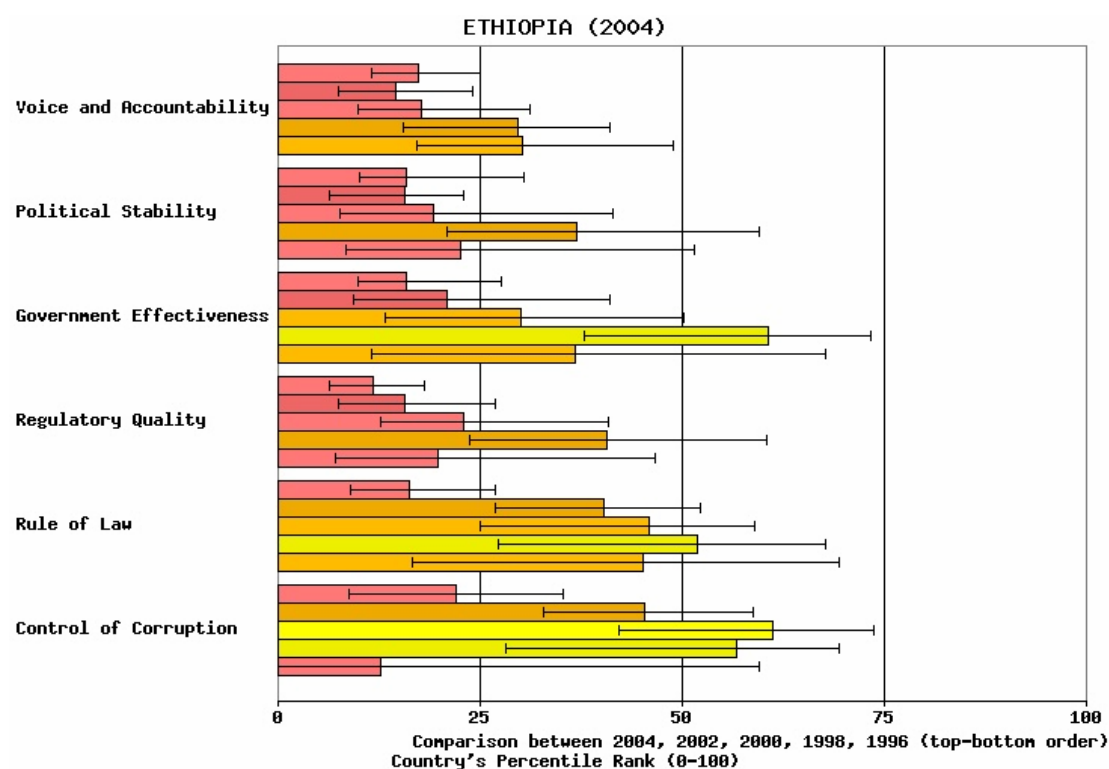
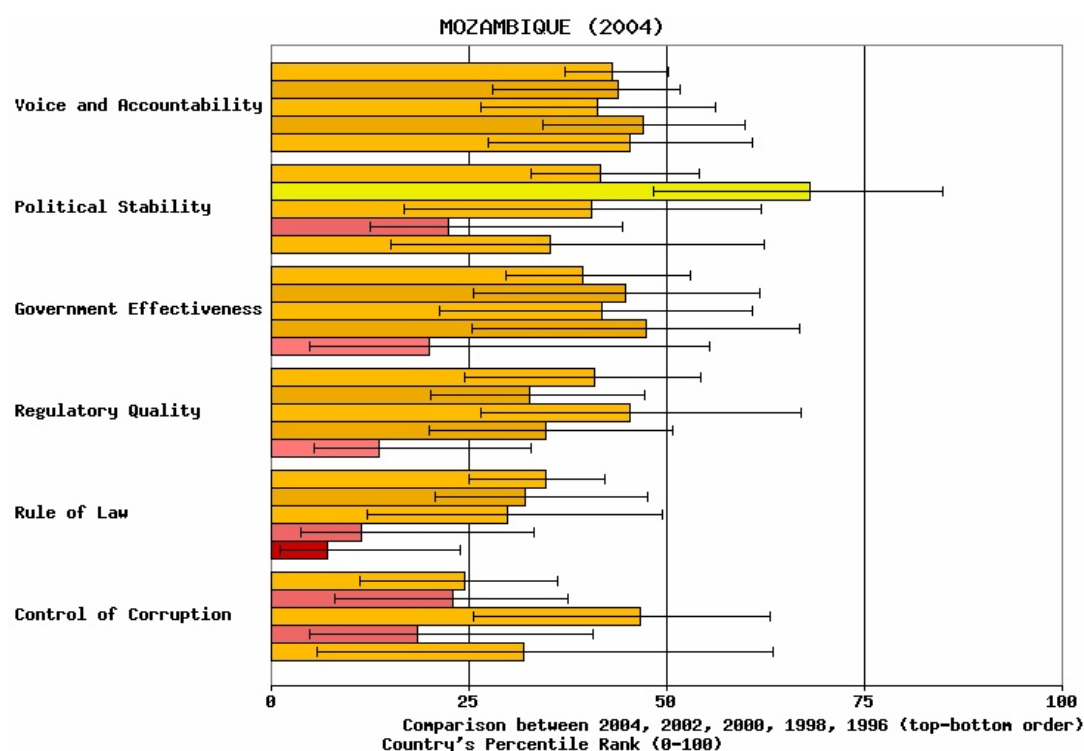
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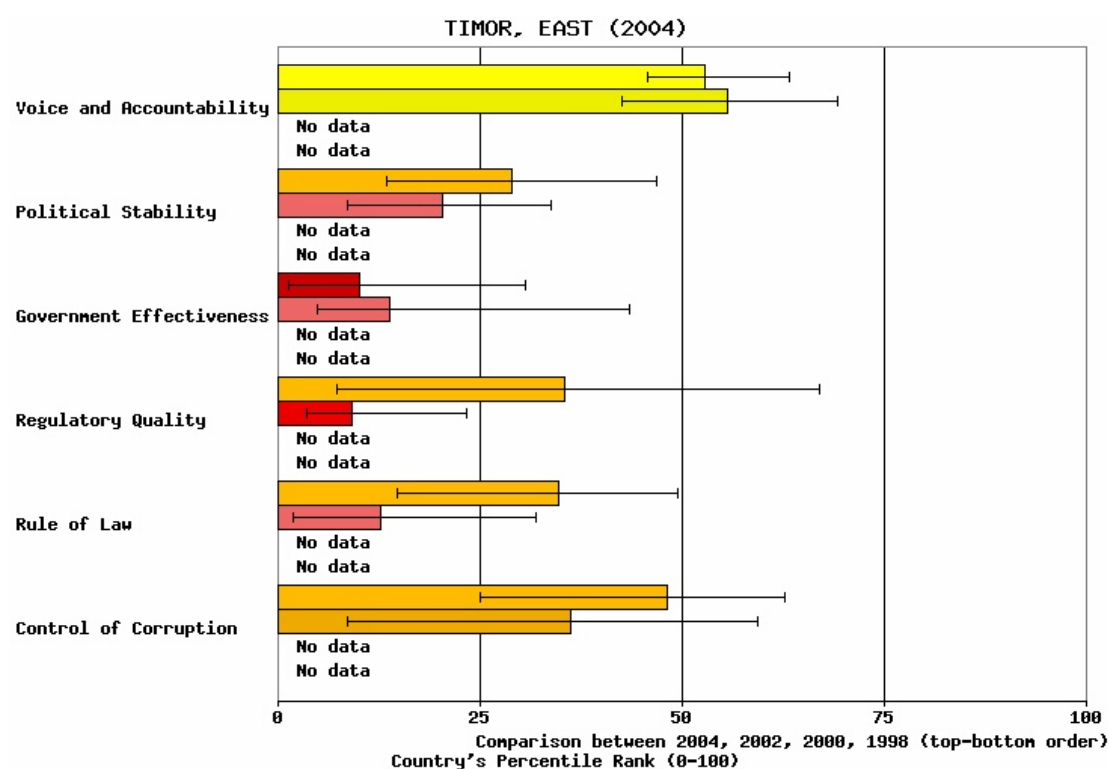
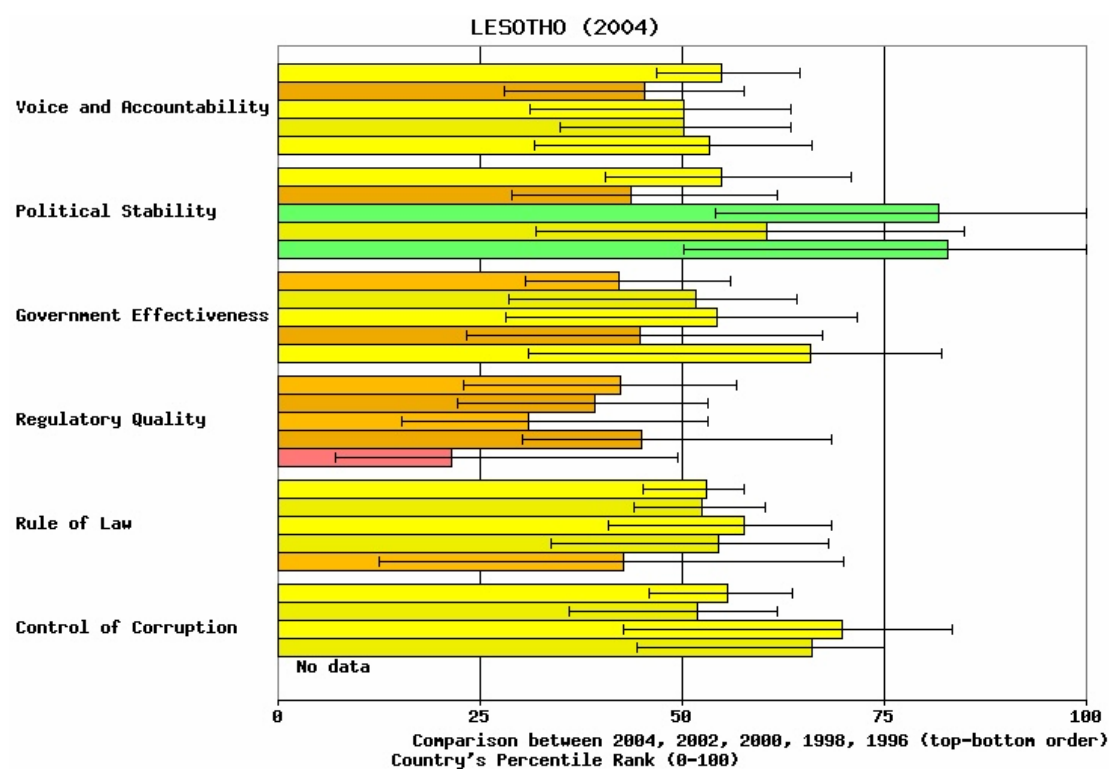
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## Annex 4: Governance indicator charts 1996-2004 for Irish Aid partner countries



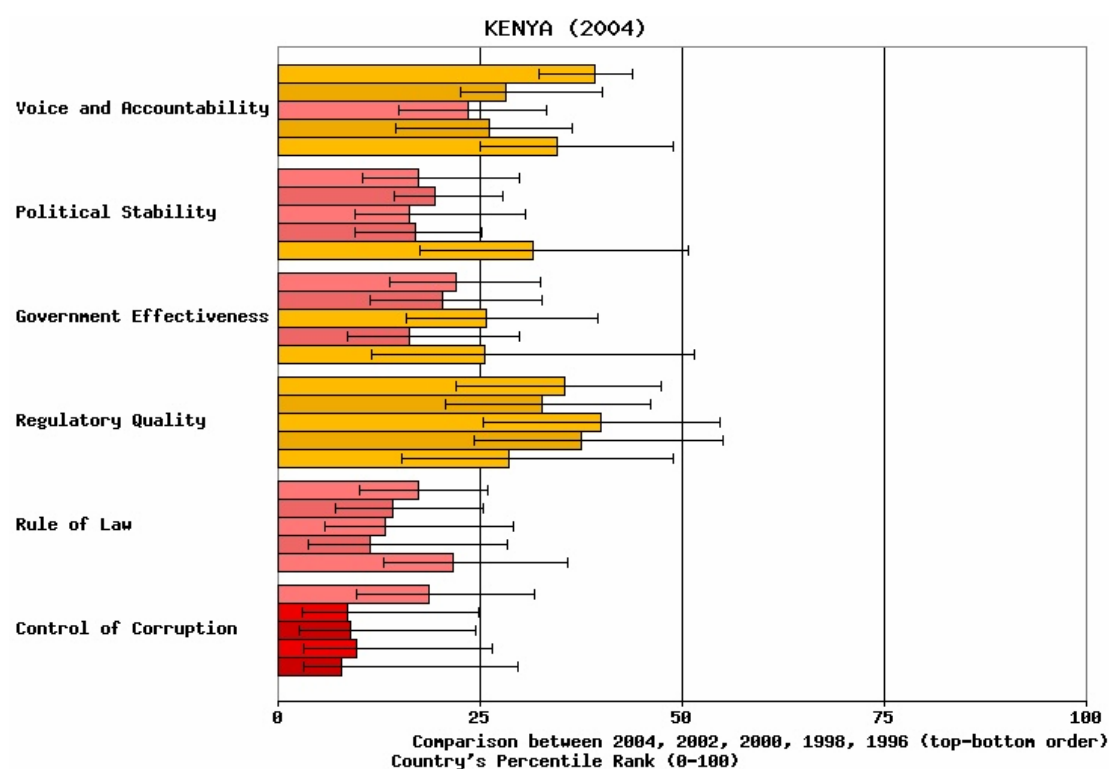
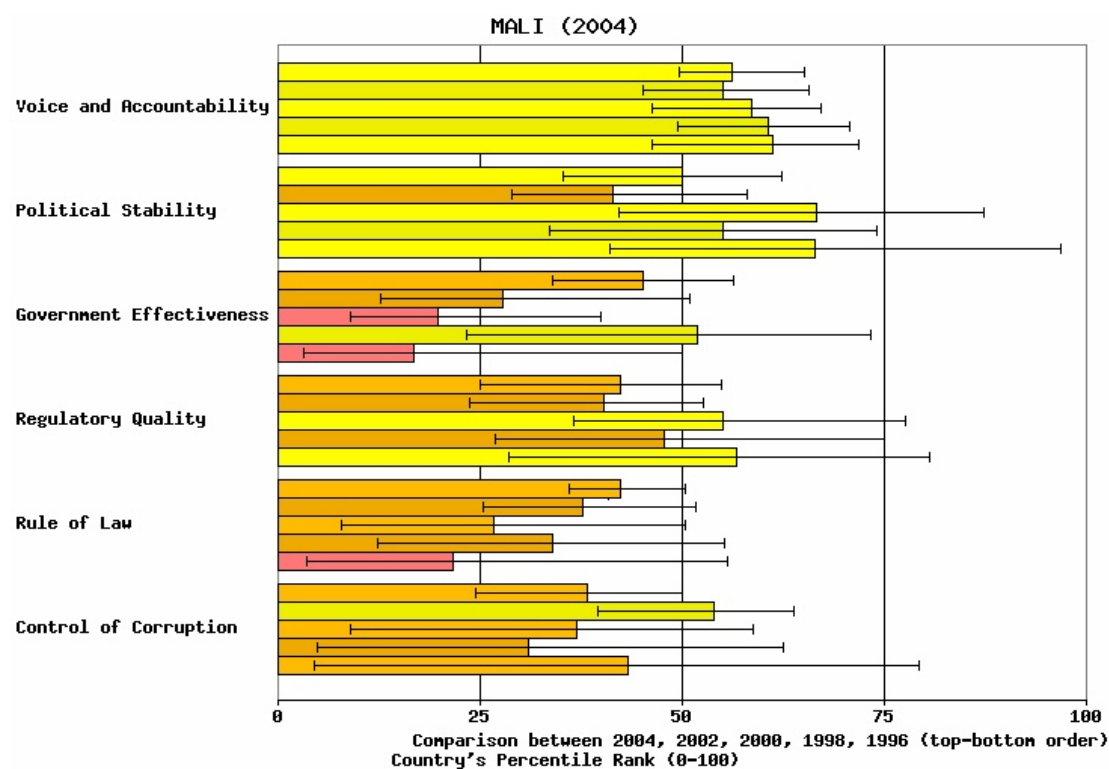


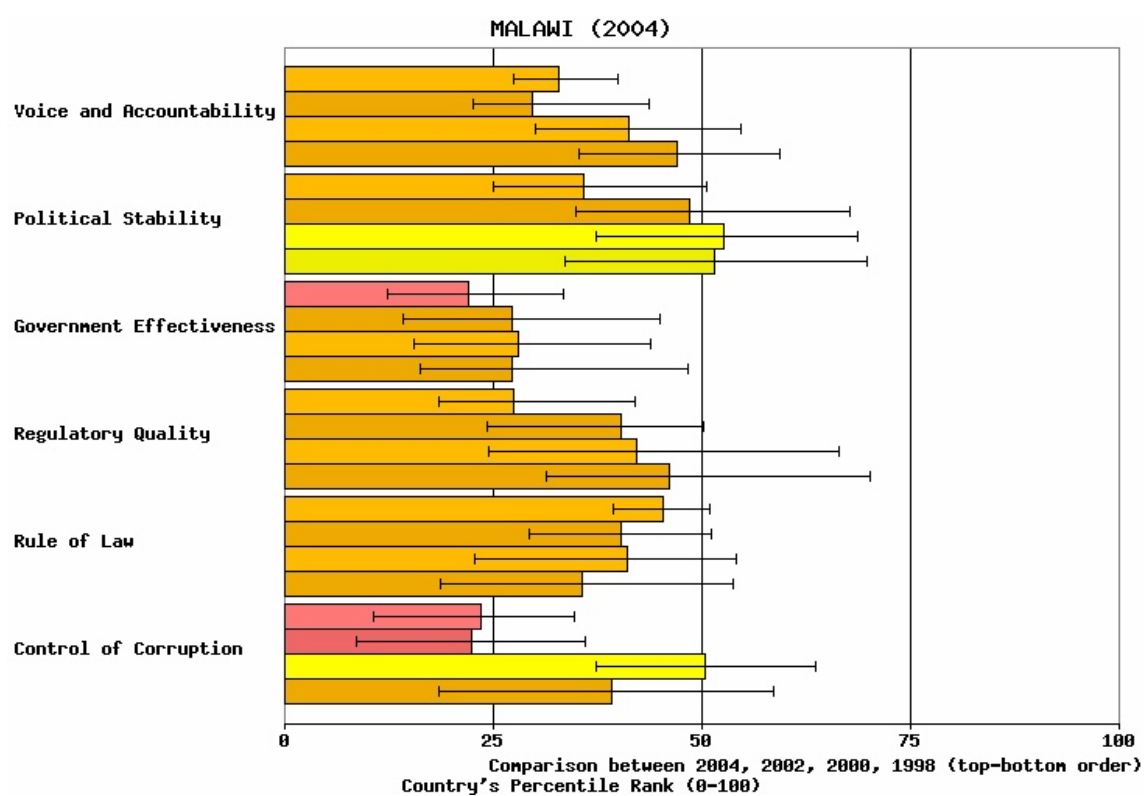
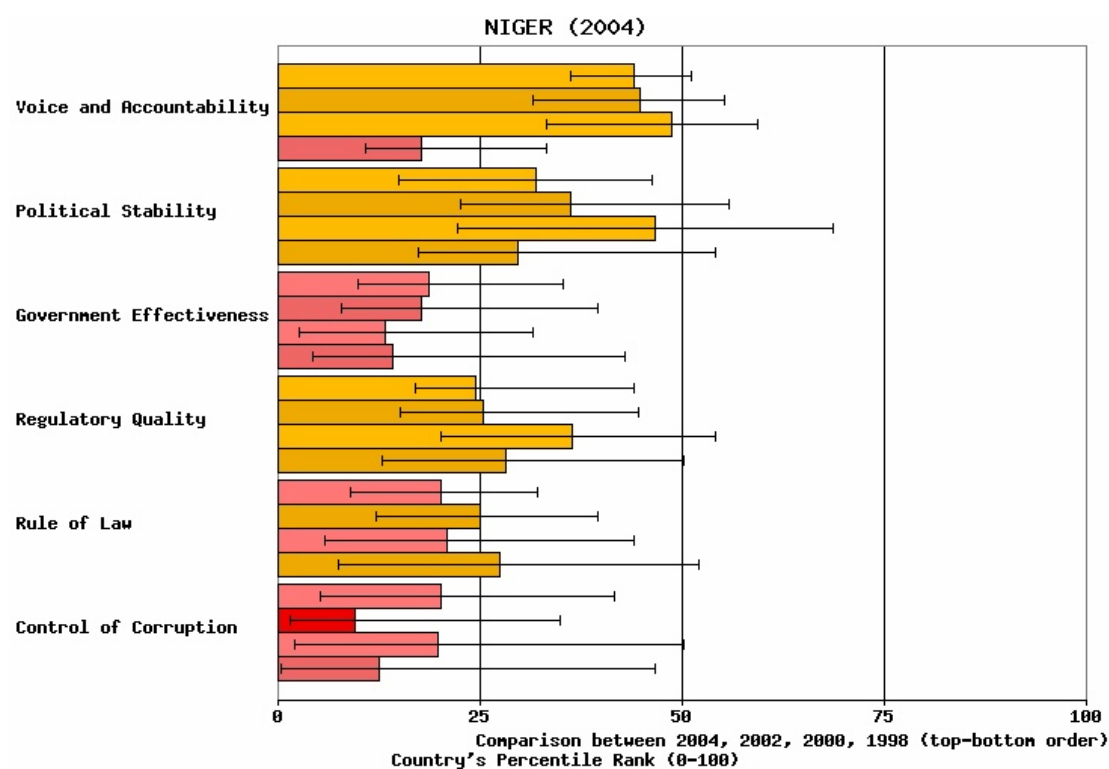


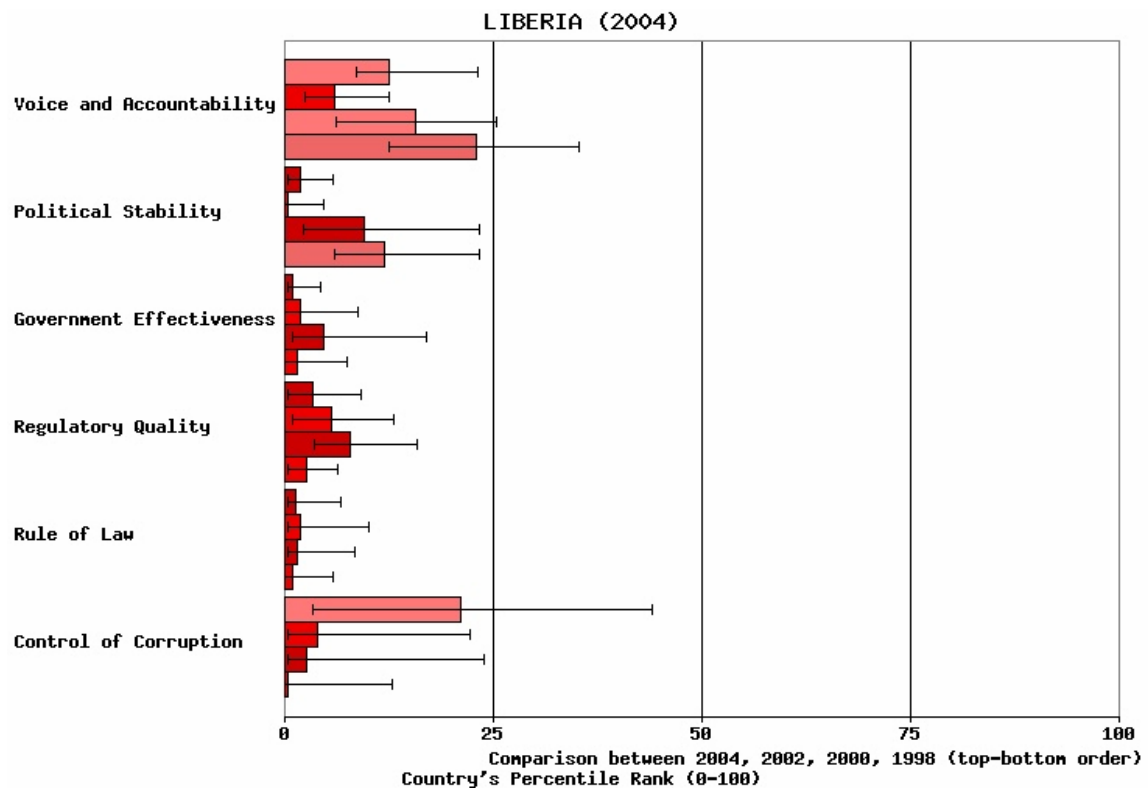
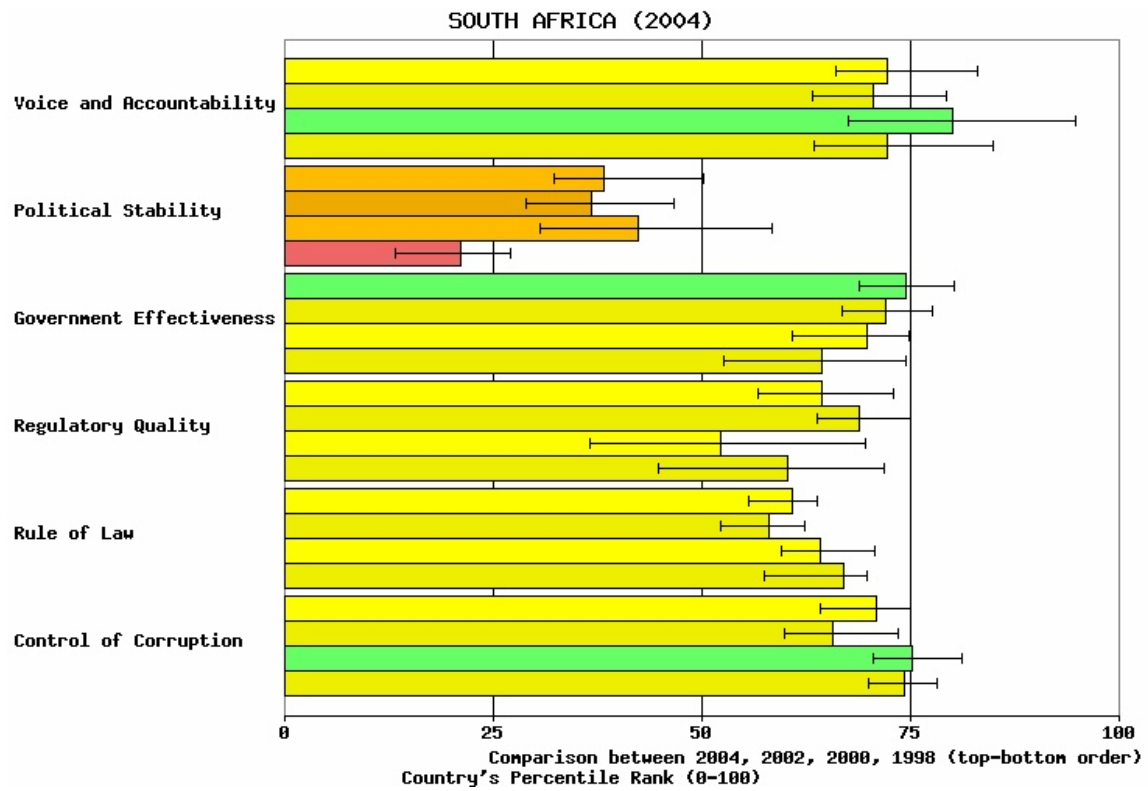


Source: World Bank Institute ([www.worldbank.org/wbi/governance/govdata/](http://www.worldbank.org/wbi/governance/govdata/)).

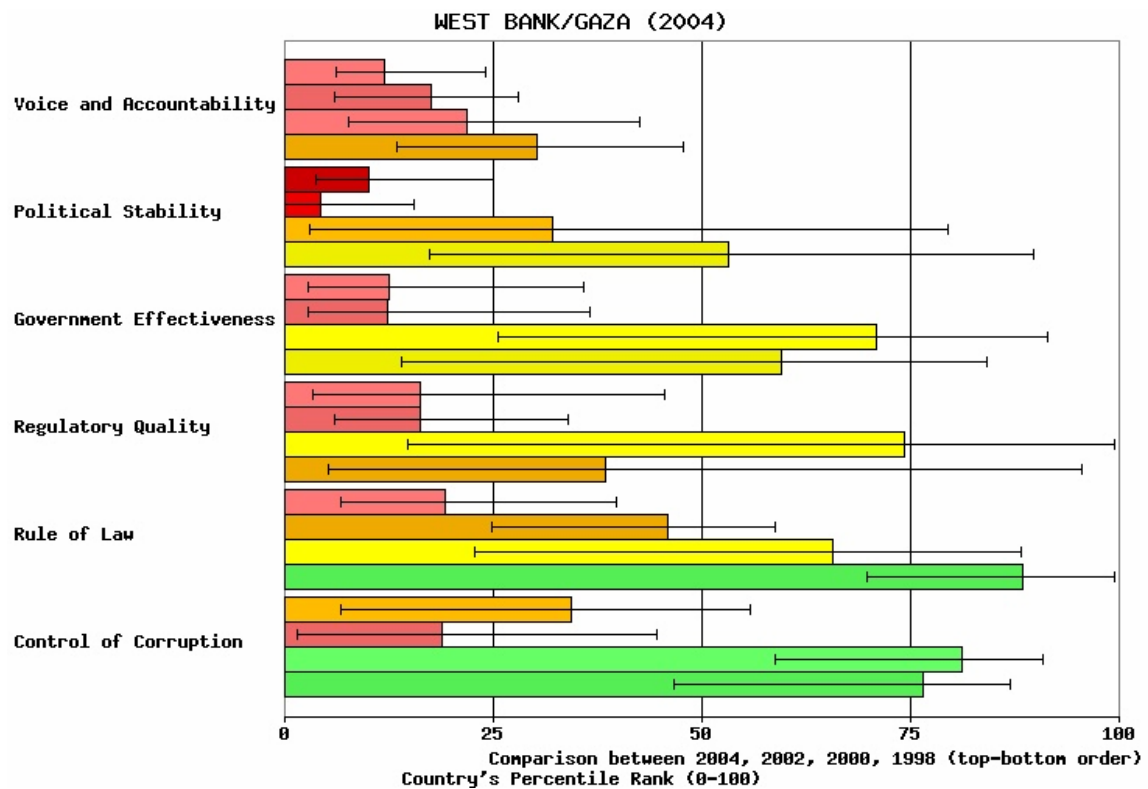
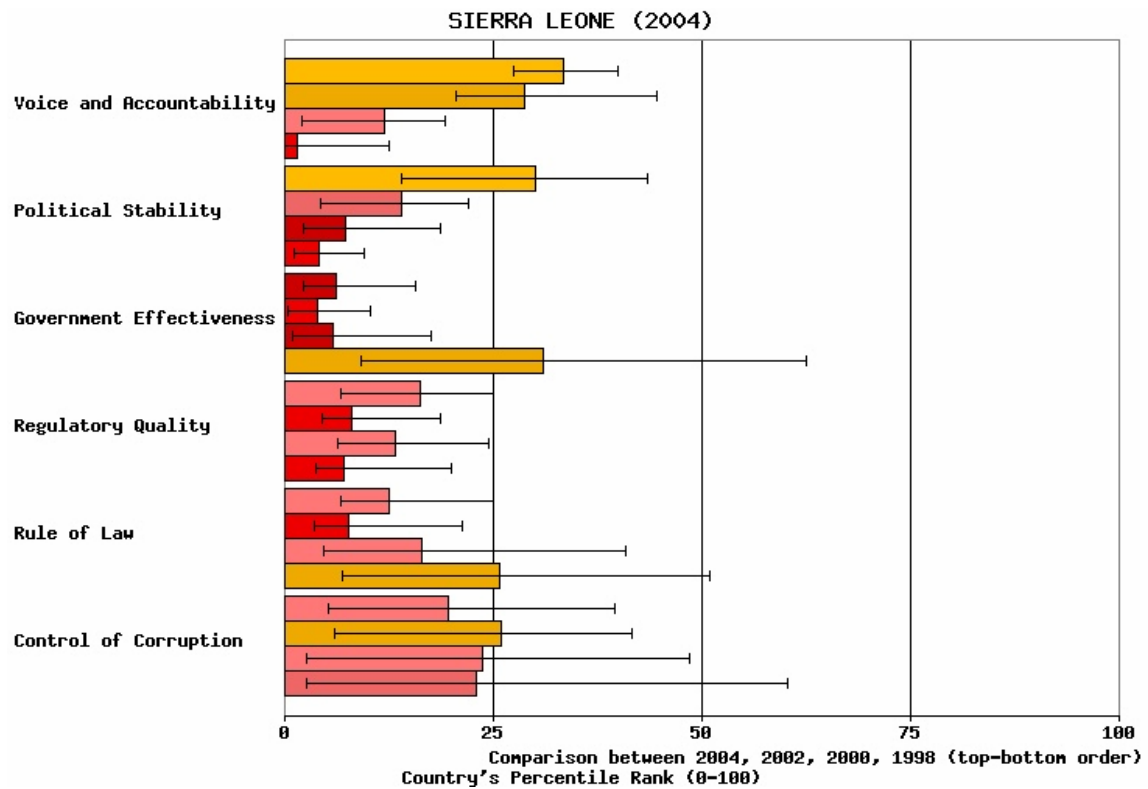
## Annex 5: Governance indicator charts 1996-2004 for Irish Aid potential countries







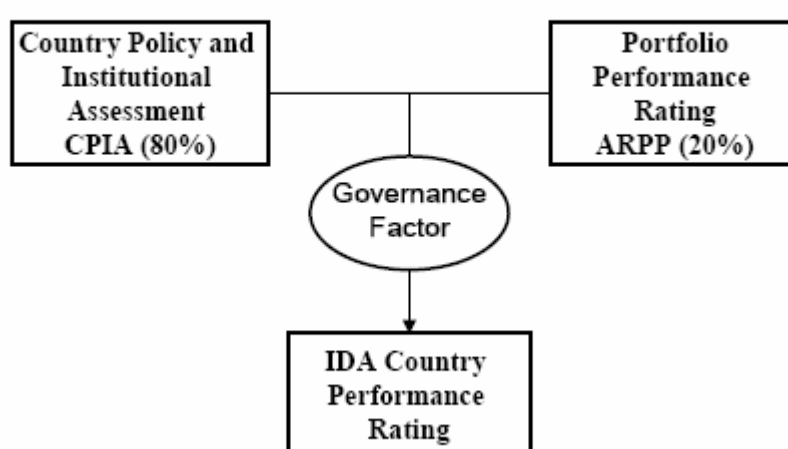




## **Annex 6: Use of the CPIA in the IDA allocation process**

'The CPIA underpins IDA's allocations but is not its only determinant. Two additional process steps are included. First, to capture the important dimension of quality of development project and program management, the Bank's Annual Report on Portfolio Performance (ARPP) is used to determine a score for each country's implementation performance. The ARPP scores are based on the percentage of IDA funded projects in the country that are considered at risk. These percentages are translated into 1-6 scores with the help of a conversion table. A weighted average rating is calculated of the CPIA (80% weight) and the ARPP measure (20% weight). In the second step, this composite rating is multiplied by the "governance factor" to produce the country's IDA CPR (chart 1).

Chart 1- IDA Country Performance Rating



'The governance factor is derived from the five criteria in the CPIA's governance – or public-sector management and institutions – cluster D, plus the three-year moving average of the procurement flag that is an element of the ARPP portfolio rating. The average score of these six governance criteria is divided by 3.5, the mid-point of the 1-6 range, and an exponential of 1.5 is applied to this ratio:

$$\text{Governance Factor} = (\text{average governance rating} / 3.5)^{1.5}$$

'The country's overall rating is then multiplied by this factor, resulting in an increase (or decrease) of the overall IDA CPR, depending on the degree to which the country's governance rating is strong – above 3.5 (or weak – below 3.5).

'IDA's resources are allocated on the basis of the IDA CPR (ensuring that good performers get a higher share of IDA's available resources), population and GNI per capita:

$$\text{IDA Country Allocation} = f(\text{CPR } 2.0, \text{Pop } 1.0, \text{GNI/Cap.} - 0.125)$$

'The formula shows that the country's policy and institutional performance is the dominant determinant (twice as high a score results in four times the allocation), while population also affects it significantly (the relationship is linear: a higher population results in a proportionally increased allocation). Finally, there is a modest bias in favor of the IDA eligible countries with a lower GNI per capita.'

Source: CPIA Technical Annex.