

II. THE COUNTRY-BASED DEVELOPMENT MODEL IN A CHANGING AID LANDSCAPE

A. THE COUNTRY-BASED DEVELOPMENT MODEL

7. **There is broad agreement that the country-based development model is the most effective approach for achieving results in terms of sustained economic growth and poverty reduction in developing countries.**⁴ The country-based model consists of three main strands: (i) nationally-owned development strategies; (ii) donor alignment around country-driven goals, with increased use of country systems wherever feasible and efforts to increase aid predictability; and (iii) mechanisms of mutual accountability encompassing both donors and governments in recipient countries.⁵ Accordingly, the interplay of these three strands strengthens domestic policies and systems in recipient countries, unites donors around clear development goals, and sets out a mutual accountability framework for all stakeholders. Therefore, aid effectiveness can be enhanced to the extent that development assistance is channeled through a country-based development model.⁶

8. **The introduction of the Poverty Reduction Strategy (PRS) approach in 1999 was an important step in the evolution of the country-based model, putting recipient country governments in the driver's seat and increasing the focus on results.** It brought a clearer focus on poverty reduction, an emphasis on national ownership of the development effort, and a clearer accountability for development results. Over the past six years, many low-income countries have made substantial progress in articulating and implementing national poverty reduction strategies. At present, 51 low-income countries are implementing their poverty reduction strategies; ten have completed their second PRS. As noted in the 2005 joint Bank-Fund review of poverty reduction strategies, “(...) *the core principles that underpin the PRS approach (...) provide the foundation on which results at the country level are achieved*”.⁷ Going forward, to ensure that strategies provide a solid framework for utilizing a significant increase in development resources, it is critical to continue to focus efforts to progressively strengthen content and implementation, as well as the links with the national budgets.

⁴ At the global level, this agreement was affirmed in the Paris Declaration on Aid Effectiveness.

⁵ World Bank (2007). “The Country-Based Development Model and Scaling Up”. PREM Poverty Reduction Group, Number 2. The mechanisms of mutual accountability are meant to “ensure that both national governments and donors are responsible for meeting their commitments to country-based development.” (Ibid., p. 1).

⁶ See also OECD/DAC: “there is broad agreement that development assistance should be channeled through a country-based development model”. See OECD/DAC (2006). *Using the Country-Based Model to Scale up for Results: An Agenda for Action*. DCD/RD(2006)2/RD2. June, paragraph 6.

⁷ World Bank and IMF (2005). *2005 Review of the PRS Approach: Balancing Accountabilities and Scaling Up Results*. September, p. 2 (emphasis added).

Box 1. Some key elements of robust poverty reduction strategies

Content. Poverty reduction strategies should specify clear priorities for public action, that are appropriate and feasible in light of the diagnostics, capacity, and resources. Some core elements include:

- Prioritized and poverty focused structural and sectoral policies and programs that are consistent with available diagnostics.
- A suitable macroeconomic framework, fiscal choices consistent with poverty reduction and growth objectives, and a credible financing plan with due attention to domestic resource mobilization.
- Results framework, with medium- and long-term goals, indicators of progress, and annual and medium-term targets (framed against the backdrop of the MDGs) – all of which take into account country conditions and are consistent with policy choices in the strategy.

Implementation and monitoring modalities. Poverty reduction strategies should be linked to domestic decision-making processes and implementation should be through strong country systems. Three important aspects include:

- A link between the national strategies and annual and multi-annual budget processes combined with well functioning financial management systems.
- Institutional arrangements that sustain adequate monitoring and evaluation of implementation—including data collection and analysis, feedback into the policy processes, and transparency.
- Sound governance arrangements and service delivery mechanisms, as well as transparency and accountability of public institutions and services vis-à-vis the needs of citizens in general and the poor in particular.

Absorptive capacity. Strategies need to be feasible to implement. In addition to consistency with the financing envelope, this requires a country-specific understanding of constraints to absorptive capacity at the sectoral and cross-sectoral levels. This requires:

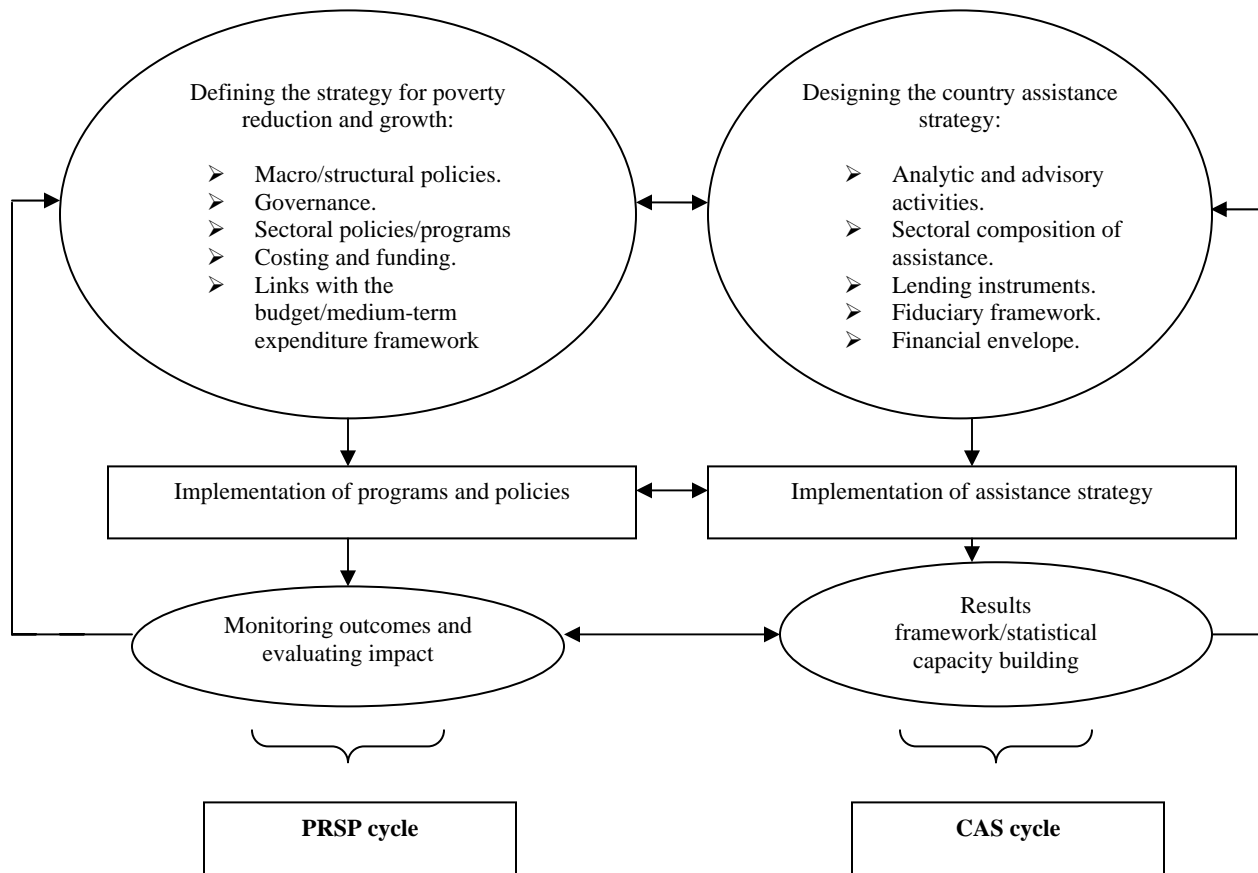
- A country-specific consideration of constraints to absorptive capacity. These could be related to the macroeconomic framework (*e.g.*, debt sustainability issues), human and physical capital, institutional and policy environments, or donor behaviors.
- A sequenced set of interventions to address identified constraints so as to pave the way to absorb effectively significantly scaled-up aid (see paragraphs 11-14).

Source: OECD (2006), *op. cit.*

9. **The country-based model has a number of implications for the delivery of development assistance.** It demands flexibility from development partners to support country priorities and to support the examination of a wider range of policy options. It also requires aid delivery mechanisms that facilitate country ownership of development policies, align and integrate aid into domestic processes, make use of government systems instead of donor specific systems, and focus on results at the project, sector, and country levels.

10. **IDA's delivery of development assistance has traditionally been grounded in detailed analysis of the recipient countries' development needs and challenges.** In response to the expanding range of services and products offered by IDA and the need to ensure consistency with a country's development agenda, IDA adopted the Country Assistance Strategy approach. Figure 1 illustrates how the design, implementation and monitoring of country assistance strategies are aligned with the PRSP process.

Figure 1. Aligning the CAS with the PRSP: The Country-Based Model at Work⁸



11. **The effectiveness of the PRSP process is directly related to how active client country governments are in two respects:** (i) in coordinating donor inputs; and (ii) in bringing different stakeholders – civil society, NGOs, academia, etc – into the PRSP approach and building broader ownership. Ultimately, governments should continue to take the lead in coordinating the aid delivery process at the country level.

12. **As countries are gaining experience with the design and implementation of PRSPs, a number of important challenges have been encountered and are being addressed.** These include:

- Many first-generation PRSPs had a strong focus on the delivery of social services to the poor, without sufficient focus on economic growth. The second generation of PRSPs typically has a much greater focus on private-sector-led economic growth (see

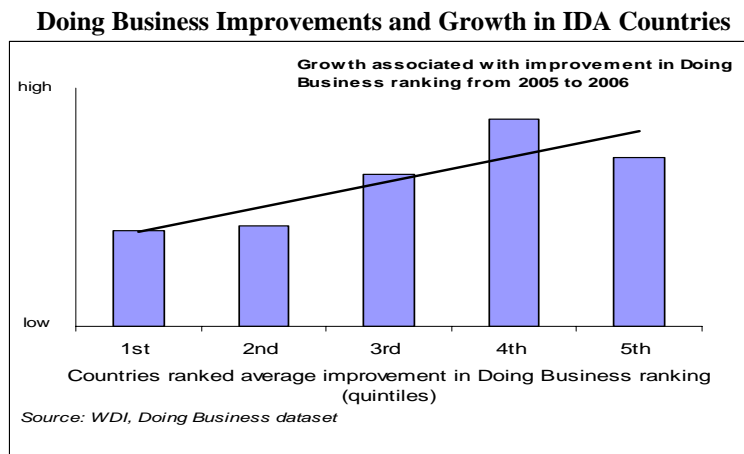
⁸ This Figure is adapted from World Bank (1999). *PRSP Sourcebook*, Figure 1, p. 3.

Box 2), recognizing that it is critical for the sustainability of enhanced access to social services as well as for reducing income poverty.⁹

Box 2. The Pivotal Role of Private-Sector-Led Growth

Policies for sustained, broad-based economic growth are a central ingredient for a sound poverty reduction strategy. Without growth, poverty reduction gains brought about through attempts to reduce inequality alone are bound to be insufficient and unsustainable. Economic growth helps to reduce poverty by raising income levels and creating employment opportunities. In turn, growth can only be sustained in the long run if it is underpinned by a vigorous, thriving private sector: “Without the dynamic force of private initiative, disciplined by competitive markets, poor people will stay poor.”¹⁰

Entrepreneurial activity thrives in environments with a solid institutional foundation and clear rules of the game. Therefore, a healthy investment climate is a crucial element in any strategy focusing on promoting sustained growth and poverty reduction. Government policies and behaviors play a key role in fostering a sound investment climate, as they can decisively influence “the security of property rights, approaches to regulation and taxation (both at and within the border), the provision of infrastructure, the functioning of finance and labor markets, and broader governance features such as corruption. Improving government policies and behaviors that shape the investment climate drives growth and reduces poverty.”¹¹ A healthier business environment does have a tangible impact on countries’ ability to unleash private-sector-led growth, as indicated in the Figure below, which related growth outcomes (vertical axis) with improvements in *Doing Business* rankings between 2005 and 2006 (horizontal axis):¹²



IDA plays a key role in supporting private-sector-led growth through its financial assistance – including funding for infrastructure, discussed in detail in Section V, as well as development policy operations that support policy reforms – and non-lending activities. The main focus is on helping governments in client countries promote a sound business environment, where private initiative and competitive markets can flourish, and private investment can be attracted and retained. IDA’s work on private sector development is complemented and enhanced through IFC’s and MIGA’s private sector investment activities.

⁹ According to the 2005 joint Bank-Fund review of poverty reduction strategies, “in line with increased attention on the productive sectors, countries are increasingly making growth a central element of their poverty reduction strategies (...).” See World Bank and IMF (2005), *op. cit.*, p. 55.

¹⁰ See *IDA at Work* note “IDA, Entrepreneurship, Job Creation, and Growth”. January 2007, p. 1.

¹¹ World Bank (2004). *World Development Report 2005. A Better Investment Climate for Everyone*. September, p. 1.

¹² *IDA at Work* note “IDA, Entrepreneurship, Job Creation, and Growth”. January 2007, p. 4.

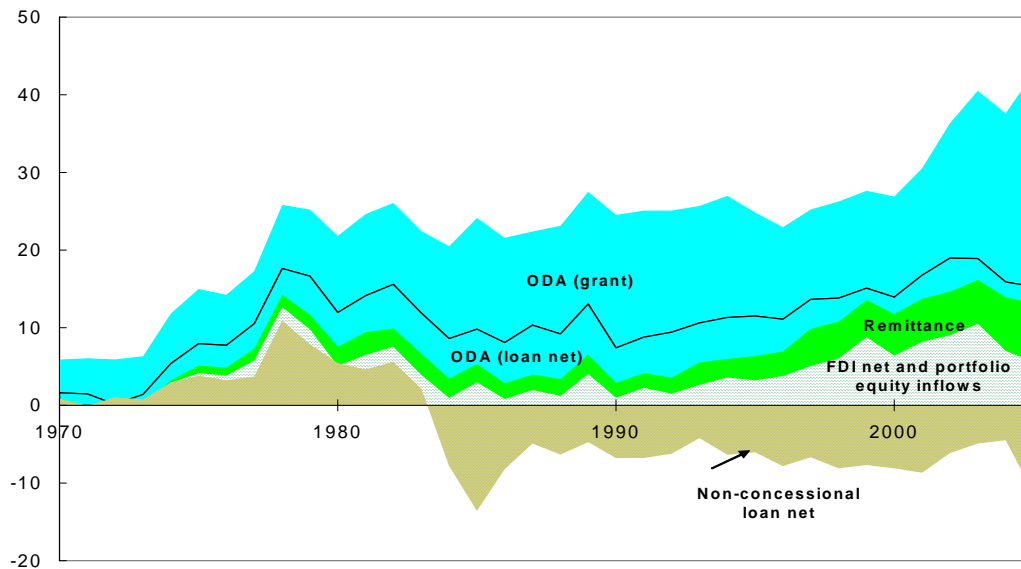
- Initially, PRSs were often developed in parallel to existing national planning, budgeting, and monitoring processes, which created difficulties in their implementation. Several countries are now undertaking efforts to mainstream the PRS approach into existing processes to ensure that there is a single national instrument for priority setting and indicative resource allocation over a multi-year period.
- Ambitious poverty reduction objectives articulated in many PRSs and related resource requirements exceeded available resources for implementation. This resulted often in tensions between countries' desire to mobilize additional resources to implement ambitious strategies and development partners seeking improved prioritization.
- Many low-income countries – particularly in Africa – are small and cannot absorb substantial aid without anchoring them in sub-regional frameworks for infrastructure and other projects. Hence, multi-country coordination and assistance as well as the spill-over of capacity from larger neighboring countries will increasingly become important extensions to the single country framework.

B. THE RECENT EVOLUTION OF THE GLOBAL AID ARCHITECTURE

13. **Official Development Assistance (ODA) continues to represent a key source of net financial flows to low-income countries, particularly in Sub-Saharan Africa.** While private financial flows have become the dominant form of resource transfers for the more prosperous among developing countries, they are still dwarfed by ODA in most IDA-recipient countries, particularly in Africa. “While equity and foreign investments have grown significantly since the mid-1990s, they are highly concentrated in a small number of countries. For most [low-income] countries, official development assistance (ODA) is still the largest single source of capital inflows, contributing nearly half of all net capital flows.”¹³ In general, FDI inflows to Africa have been concentrated in either resource rich countries (e.g., Angola, Côte d’Ivoire, Nigeria and Sudan) or better performing countries (e.g., Senegal, Tanzania, and Uganda). Over the 2001-2005 period, IDA itself provided on average 15.5 percent of the total net ODA for IDA-eligible countries. Figure 2 shows that ODA (including debt relief) accounted for the lion’s share in the total net resource flows to IDA countries in Africa over the last three decades.

¹³ Sundberg, M. and A. Gelb (2006). “Making Aid Work”. *Finance and Development*, Volume 43, Number 4, p. 2.

Figure 2. Net resource flows to IDA countries in Africa (US\$ bn., 2005 Prices)^{1/2/3/}



Source: OECD DAC for ODA data; World Bank Global Development Finance 2007 for the other data.

^{1/} The sample limits to current IDA countries in Africa (39 countries).

^{2/} Net inflows of non-concessional loans is total debt disbursement minus concessional loan disbursement minus total debt service paid.

^{3/} Net flows for non-concessional loans are negative from the early 80s onwards.

14. Some recent trends in ODA flows and in the evolution of the international aid architecture are potentially at odds with the country-based development model. The recent emphasis on social sectors – to the detriment of infrastructure – as a destination for ODA flows may reflect global rather than recipients’ needs and priorities as reflected in national development strategies. Furthermore, the proliferation of donor channels, the fragmentation of ODA, and the mounting degree of “verticalization” and earmarking of aid increases the transaction costs and could reduce the overall effectiveness of aid.¹⁴ These trends are summarized in subsections B.1 and B.2 below. Section B.3 briefly discusses the significance of these trends for the country-based model.

B.1. ODA Trends at the Sectoral Level

15. The last two decades have seen a significant shift in the sectoral composition of ODA flows. The share of social sectors¹⁵ in total sector allocable ODA to low-income countries increased from less than 30 percent in the early 90s to more than 52 percent in 2000-2004. In the case of Sub-Saharan Africa, the social sector share reached 60 percent in 2000-2004, up from about 33 percent in the first half of the 90s. In parallel, the share of infrastructure in total sector allocable ODA declined from 33 percent to 26 percent over the same period in low-income

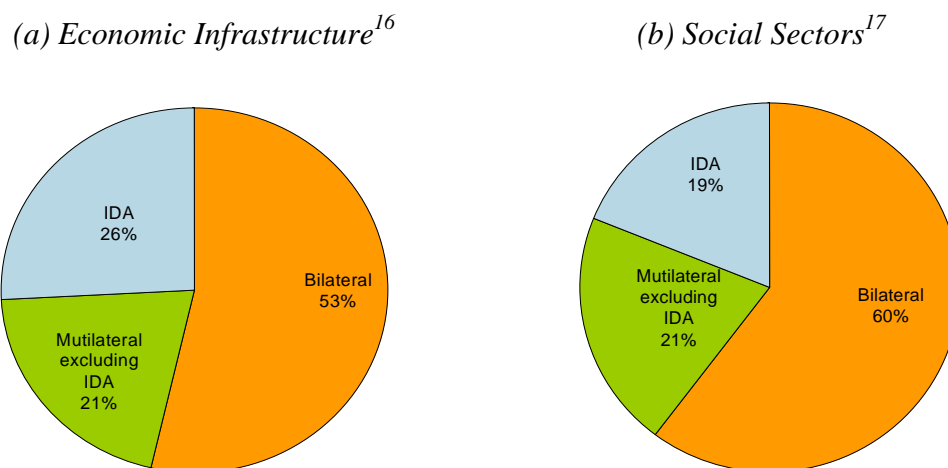
¹⁴ See IDA (2007). *Aid Architecture: An Overview of the Main Trends in Official Development Assistance Flows*. Paper presented at the first meeting of the IDA15 Replenishment negotiations, Paris, March 5-6.

¹⁵ Social sectors, in the OECD/DAC classification, include education; health and population; water and sanitation; government and civil society; and conflict, peace and security. Most of the recent growth in ODA for the social sectors is due to increased aid for health and population as well as for government and civil society.

countries. For Sub-Saharan Africa, the relative decline in infrastructure was even more marked: from 29 percent in 1990-1994 to 19 percent in 2000-2004.

16. **IDA has been a major provider of ODA for infrastructure and social sectors in low-income countries.** Using the DAC classification of sectors, IDA's share in total sector allocable ODA for economic infrastructure in IDA-eligible countries over the 2000-2005 period is around 26 percent (see Figure 3a). IDA's share in social sector ODA over the same period for IDA-eligible countries is about 19 percent (Figure 3b).

Figure 3. Donor composition of sector allocable ODA commitments to IDA Countries (2000-2005)



Source: CRS.

B.2. An Increasingly Complex Aid Architecture

17. **The aid architecture landscape has changed significantly in the last few years in light of the recent increase in the number of vertical funds as well as the growing importance of non-DAC, “emerging” donors.** These new sources of aid bring more resources for poor countries to reach their MDGs. At the same time, the increasing complexity of the aid architecture has increased transaction costs for both donors and recipients, potentially reducing the effectiveness of aid.

18. **The growing complexity of the global aid architecture can be illustrated through three distinct, but often inter-related, phenomena: proliferation, fragmentation, and “verticalization”.** Aid proliferation refers to the increasing number of donor *channels* providing ODA. Fragmentation refers to the increasing number of donor-funded *activities* with decreasing financial size. “Verticalization” is taken to mean an increasingly specialized focus of ODA

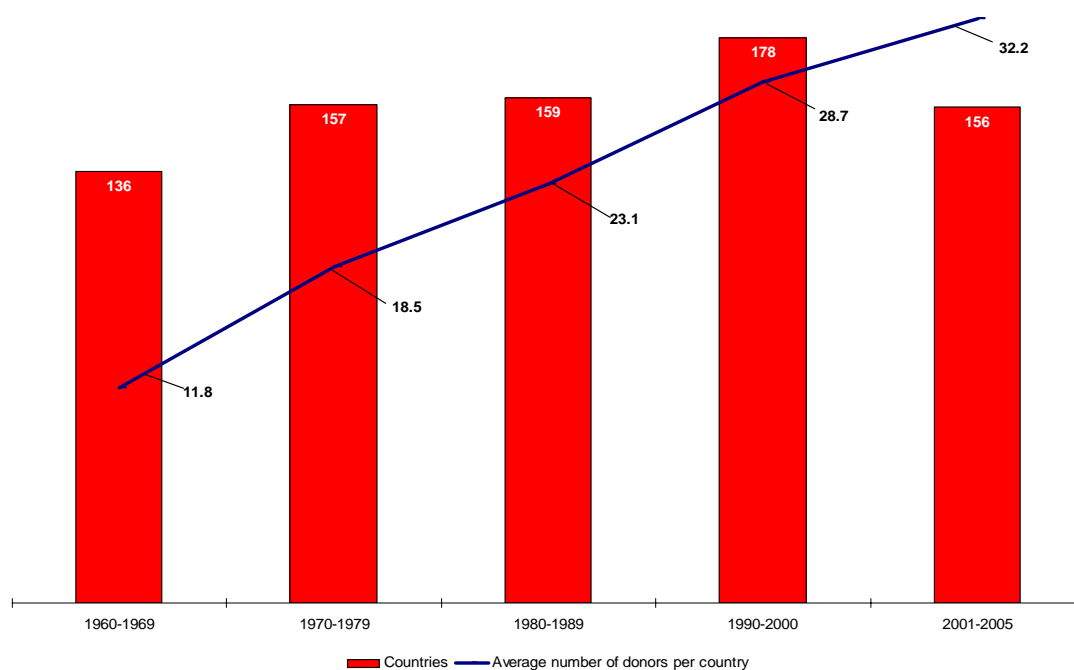
¹⁶ Under the DAC classification, it covers transport and storage, communications, energy, banking and financial services, and business and other services.

¹⁷ Classified by DAC under social infrastructure and services. See footnote 15.

providers on narrowly-defined issues or themes (e.g., HIV/AIDS), often accompanied by earmarking of donor funds.

19. **While new sources of aid bring with them much needed resources to help low-income countries reach their MDGs, the accompanying fragmentation and proliferation trends increase transaction costs¹⁸ and create new challenges for alignment and harmonization.** Figure 4 shows proliferation trends: The average number of donors per country grew from about 12 in the 1960s to more than 30 in 2001-2005. Figure 5 shows fragmentation trends: By 2004, the average number of donor activities per year had grown to 60,000 (from about 20,000 in the late 90s) and their average financial size had declined to US\$1.5 million (from around US\$2.5 million in the late 90s).

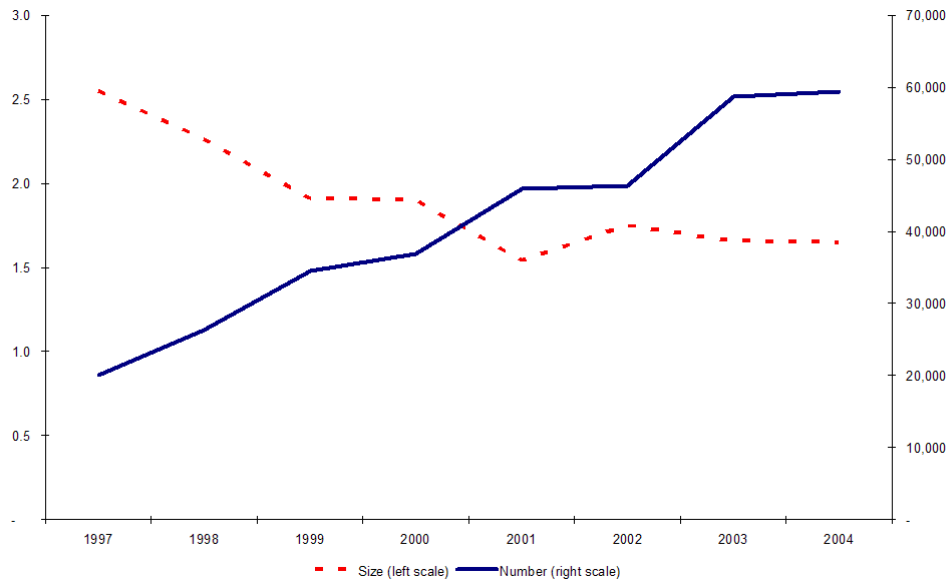
Figure 4. Donor Proliferation in Low-Income Countries



Source: CRS

¹⁸ See also World Bank (2007). “Opportunities to Scale Up: Delivering on Commitments”. PREM Poverty Reduction Group, Number 1, p. 2: “Donor support for development translates worldwide into over 60,000 ongoing projects, with some partner countries having over 1,000 donor-funded activities, hosting over 1,000 missions each year, and preparing as many as 2,400 progress reports annually. While some countries can manage these requirements more readily than others, everywhere they burden and erode administrative capacities, weaken country accountability, reduce the attention to strengthening countries’ own policies and systems, and divert financial and human resources away from addressing real development goals.”

Figure 5: Aid Fragmentation Trends in Low-Income Countries



Source: CRS online

20. **Some of the characteristics of vertical or “earmarked” approaches tend to complement the country-based model, while others tend to weaken it:** On the one hand, vertical approaches help address urgent financing needs for specific development issues (e.g., HIV-AIDS) and achieve economies of scale through a narrower focus. On the other, they may also be associated with problems of increased transaction costs, intra- and inter-sectoral distortions in resource allocations, and displacement of qualified (and often scarce) human resources in recipient countries and, in the long run, sustainability of financing. Therefore, it is critical that *renewed efforts be applied towards achieving balance and complementarity at the country level between vertical and horizontal approaches to aid delivery.*

C. IMPLICATIONS FOR DEVELOPMENT ASSISTANCE

21. **The recent trends in the global aid architecture highlight the need for a renewed emphasis on the country-based model.** Indeed, the risks and costs associated with donor proliferation and aid fragmentation “reinforce the importance of firmly anchoring aid modalities in a strong country development model”.¹⁹

22. **While the different aid delivery mechanisms and approaches add to the complexity of the global aid architecture, they are not inherently incompatible with each other, or with the country-based model.** A country-driven approach provides a platform upon which different ways of delivering aid – traditional bilateral ODA, emerging donors, and vertical funds – can work together in an integrated fashion to the benefit of recipient countries. As long as such mechanisms and approaches are framed in the context of country-owned national development

¹⁹ Hoftijzer, M. and L. Cord (2007). “The Country Development Model and IDA”. World Bank, PREM Poverty Group, processed.

strategies, their goals would be mutually reinforcing – therefore making it possible to achieve much needed balance and complementarity.

23. The Paris Declaration is a significant step forward towards addressing the complexities of the existing aid architecture and restating the centrality of the country-based approach to development aid. In this context, the following additional efforts would be required from both recipient and donor countries, based on the Paris Declaration principles:

- **Strengthening national development strategies.** Governments in recipient countries would need to continue to focus their attention in a number of areas with respect to their national development strategies, including PRSs: (i) ensuring that goals and targets are clear, sufficiently prioritized, and associated with specific policy actions; (ii) deepening the integration of national development strategies with domestic planning, budgeting, and monitoring processes; and (iii) strengthening governmental accountability to both domestic constituents and donors.
- **Improving the quality of aid.** A number of actions would also be required from the donor community: (i) strengthening donor harmonization and alignment around the PRS; (ii) expanding the use of national systems where it is appropriate; (iii) “where use of country systems is not feasible, establish additional safeguards and measures in ways that strengthen rather than undermine country systems and procedures”.²⁰

24. Strengthening recipient countries’ ability to make effective use of potentially scaled-up aid, particularly program-based ODA, is an important step to the implementation of the Paris Declaration on Aid Effectiveness. Data for 23 HIPCs (all of them IDA countries) indicates gradual progress in terms of their public financial management (PFM) systems, with a 10 percent improvement in the 15 HIPC indicators between 2002 and 2004. Working together with other development partners, the World Bank has developed a comprehensive indicator-based framework (PEFA) that tracks progress over time. The PEFA framework has 28 indicators and has been applied in 34 countries so far, with a further 50 (mostly IDA) countries planned to be covered by end 2007.

25. In this context, IDA’s role in supporting the country-based model has become even more important in light of the growing complexity of the global aid architecture. By drawing on its strengths, IDA can support a sound country-based platform upon which other forms of aid can effectively operate and work together towards the achievement of the MDGs. In so doing, IDA can help address the adverse effects of aid fragmentation through its ability to provide large-scale financing, sound analytical work, convening power, and its role in fostering alignment and harmonization at the country level. IDA’s strengths and its role in supporting the country-based model will be discussed in detail in Section III.

²⁰ See *Paris Declaration on Aid Effectiveness. Ownership, Harmonisation, Alignment, Results and Mutual Accountability*, p. 4.