Splitting the Check: Counterpart Commitments in World Bank Projects

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When an international development agency enters into a project agreement with a foreign aid-receiving country, the agreement often requires the recipient country to provide a certain level of counterpart funding from its own budget for the project. In contrast to much of the aid allocation literature, which views donors as making decisions about how much funding countries should receive, we think about donors and recipient states bargaining over the specific funding of aid projects, identifying factors that might result in more or less counterpart funding. Then we use an original dataset to look at the variation in counterpart commitments across a sample of 1,800 World Bank projects from the 2000s. Ultimately, the data reveal that more effective governments and countries that have already borrowed significant amounts from the Bank contribute more counterpart funding, whereas democracies and governments with greater ODA flows contribute less counterpart funding. Geostrategic relationships between World Bank principals and borrowing countries seem to have little influence on counterpart commitments.

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Much of the literature on foreign aid allocation places donors in a privileged position, assuming that donors make decisions about funding commitments and that aid recipients accept these decisions. In reality, aid projects are the result of negotiations between development partners and the governments in developing countries. Although there is a literature from the 1990s that explores donor-recipient bargaining over conditionality in structural adjustment programs (Mosley, Harrigan and Toye 1991; Killick 1998) and a literature that thinks very generally about contracts between donors and recipient governments (Svensson 2000, 2003; Azam and Laffont 2003), there is little research that tries to explain the design elements of specific development investment projects in terms of their being negotiated agreements.

We believe that understanding the negotiations between donors and recipients is important. First, doing so will help us to understand patterns in aid allocation in a way that current donor-centric models cannot. Second, understanding the way in which the content of specific projects is determined is essential for thinking about the outcomes of these projects and aid effectiveness in general. Having a better understanding of how particular development projects come to have the features that they do will help us better understand the contributions that foreign aid makes to poverty alleviation and economic growth in developing countries. Third, to the extent that we can identify recipient-driven projects, we can pose a challenge to the dominant donor-driven perspective underlying the study of aid allocation.

In this paper, we think about donor-recipient negotiations in the context of the counterpart funding requirements found in World Bank-sponsored investment projects. The World Bank lends money to poor and middle-income countries to help them meet their development objectives. Although much attention has been paid to World Bank structural adjustment lending,[1] the majority of

[1] Now known as development policy lending, structural adjustment lending is programmatic lending meant to catalyze policy reforms. That is, it does not go to fund any specific investments. This is not to say that investment

Bank lending is for specific investment projects. Over the period 2000 – 2010, two-thirds of World Bank lending financed investment projects. Among the poorest borrowers – those who receive money from the Bank's concessional lending wing, the International Development Association (IDA) – the ratio was even higher: over three-quarters of Bank financing went to investment projects.

Within these investment projects, the World Bank often is only one of several financing entities. In many cases – over 70 percent of projects – the borrowing country itself agrees to make financial contributions to the investment project.[2] As the World Bank commits money to build schools, upgrade irrigation infrastructure, train nurses or provide microloans to entrepreneurs, the Bank usually does so in the context of an agreement where the aid-receiving country agrees to supply some portion of this funding. This is also true of investment projects funded by other multilateral (and some bilateral) donors.

What influences the size of these counterpart commitments? We imagine two bargaining scenarios – one in which the investment project under consideration originates with the World Bank and one in which the project originates with the recipient country. We suggest a set of governance and economic-based factors that will influence the amount of counterpart funding that the World Bank is likely to request for a given project based on the Bank's perception of how these factors relate to the borrower's likelihood of properly implementing a project and subsequently repaying the loan. We assume that borrowing countries prefer providing less of their own funds towards a project and suggest a set of factors that will influence the amount of counterpart funding that recipient countries are willing to commit to a given project and the amount of leverage that they have for negotiating smaller

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projects do not have a reform element to them; they often describe specific reforms that the government should undertake.

[2] A substantial number of projects – about 20 percent – include funding from other bilateral or multilateral donors. Alternatively, other bilateral or multilateral donors may finance complementary projects based on negotiations with the World Bank and/or the aid-receiving state; general data on this type of cofinancing pattern is not available.

commitments. We anticipate that the set of governance-based factors will also influence the likelihood of a project originating with the recipient country.

To assess the relative weight of the factors that influence the amount of financing contributed by recipient countries to World Bank-sponsored projects, we use an original dataset compiled from the World Bank's Projects Database.[3] In the data, we find that countries with access to more external aid and that are democratic make smaller counterpart commitments, while countries with greater external debt or greater debt to the World Bank make larger counterpart commitments. We find that countries with the most effective governments make larger counterpart commitments. Geostrategic relationships between World Bank principals and borrowing countries seem to have little influence on counterpart commitments.

Contracting Foreign Aid

Much of the theoretical literature on aid contracting starts from the assumption that donors are benevolently concerned with poverty reduction and economic development.[4] It then demonstrates the ways in which incentive structures in the principal-agent relationship between donors and aid-receiving states limit the effectiveness of foreign aid for achieving these purposes. Much of this literature portrays a Samaritan's dilemma in which donors' desire to provide assistance to impoverished populations creates aid dependency and limits the effectiveness of aid: although donors want to alleviate poverty, governments like receiving foreign aid and therefore lack the incentive to see that the

[3] The portal to the Projects Database can be found at http://go.worldbank.org/0FRO32VEI0.

[4] The empirical literature on aid allocation has convincingly shown how wrong this assumption is, demonstrating that international donors consistently privilege their own geostrategic and commercial interests or historical relationships with particular countries over need when allocating aid (McKinlay and Little 1979; Maizels and Nissanke 1984; Alesina and Dollar 2000; Berthélemy and Tichit 2004; Berthélemy 2006; Bueno de Mesquita and Smith 2007, 2009). The influence of developed country strategic and commercial interests has been shown to extend to multilateral donors, such as the World Bank and the IMF (Frey and Schneider 1986; Thacker 1999; Stone 2004; Barro and Lee 2005; Andersen, Hansen and Markussen 2006; Fleck and Kilby 2006; Dreher and Jensen 2007; Dreher, Sturm and Vreeland 2009), although some authors argue that multilateral donors are less likely to be driven by geostrategic interests and more likely to give aid for the purposes of encouraging development and economic growth (Maizels and Nissanke 1984; Girod 2008).

aid is used for the purpose of poverty alleviation. Svensson (2000) argues that aid fails to catalyze reform in aid-receiving countries because the threat to withdraw aid is not credible. He suggests that providing foreign aid through an international agency with *less* aversion to poverty – and hence a more credible threat of withdrawal – would lead to superior economic development outcomes.[5]

Other solutions to the Samaritan's dilemma include increased selectivity in choosing recipients or increased interventionism on the part of development agencies. Azam and Laffont (2003) show that donors will have difficulty creating pro-development contracts in countries where there is strong favoritism for non-poor groups. They suggest that aid allocation should follow the country selectivity principle with donors giving development funds only to countries that can be trusted to make good use of them. Pedersen (1996) argues that aid organizations are insufficiently interventionist in recipient countries, creating incentives for borrowing governments to underinvest in their economies, which leads to long-run negative outcomes; he calls for increased conditionality and improved enforcement of that conditionality. Lahiri and Raimondos-Moller (2004) similarly argue that, for aid to be pro-poor, donors must be willing to reduce aid when the government is not allocating sufficient amounts of resources to the poor.

The literature on conditionality in structural adjustment programs reaches a similar conclusion about formalized World Bank policy prescriptions having been ineffective because of the unwillingness of the Bank to punish poor implementation through the refusal of future credit. Mosley, Harrigan and Toye (1991) recommend a strategy of random punishment in the wake of implementation failure in order to balance the need for credible conditionality against the Bank's need to keep lending money. Bueno de Mesquita and Smith (2007, 2009) also think about donors and recipients contracting over

[5] In addition to the credibility problem created by donors' poverty aversion, there is also the issue of the intense "disbursement culture" that prevails within aid agencies. Bureaucratic incentives within aid organizations reward complete disbursement of available budgets rather than the design of effective programs. This culture additionally hinders the ability of a donor to credibly threaten the withdrawal of aid in the event that it has been used inappropriately (Mosley, Harrigan and Toye 1991; Killick 1998; Easterly 2002; Svensson 2003; Woods 2006).

policy concessions, but they take a much broader view of the policies being bargained over, allowing them to be strategic or commercial and not just developmental or humanitarian. They conclude that bargains are most likely to be struck between wealthy democracies and poor non-democracies, and they explicitly do not expect aid to be used for poverty alleviation or investment in economic growth.

In all of these models, aid is conceptualized as a transfer from an international agency to a domestic government, where the latter makes decisions about how to actually use the money. In this paper, we study the common real-world scenario in which a domestic government not only receives an international transfer but also agrees to contribute its own resources to an investment project. This specific type of bargain has not been addressed in the theoretical or empirical literature to date. We draw attention to counterpart funding as an important component of aid contracts.

To a certain extent, we have no reason to think that these contracted counterpart commitments are any more credible than the well-studied structural adjustment commitments made under programmatic lending. Indeed one of the most frequently cited problems in the implementation reports issued by the World Bank at the conclusion of its projects is exactly the failure of governments to provide agreed-upon counterpart funding (Winters 2011). But as with policy conditionalities, requirements for counterpart financing are, at a minimum, another tool at the disposal of international donors for trying to bring about pro-development outcomes in developing countries.

Bargaining Over Who Pays: What Explains the Size of Counterpart Commitments in Development Projects?

There are two sides that participate in the negotiation of an international development project – development agency staff and borrowing-country technocrats. Both aid agency staff and aid-recipient technocrats have preferences over aid projects that involve a mix of aid agency money and recipient-country counterpart funding. Either the aid agency or the recipient country might initiate a project, and an agreement might either be feasible or not. We depict these four scenarios in Figure 1.[6]

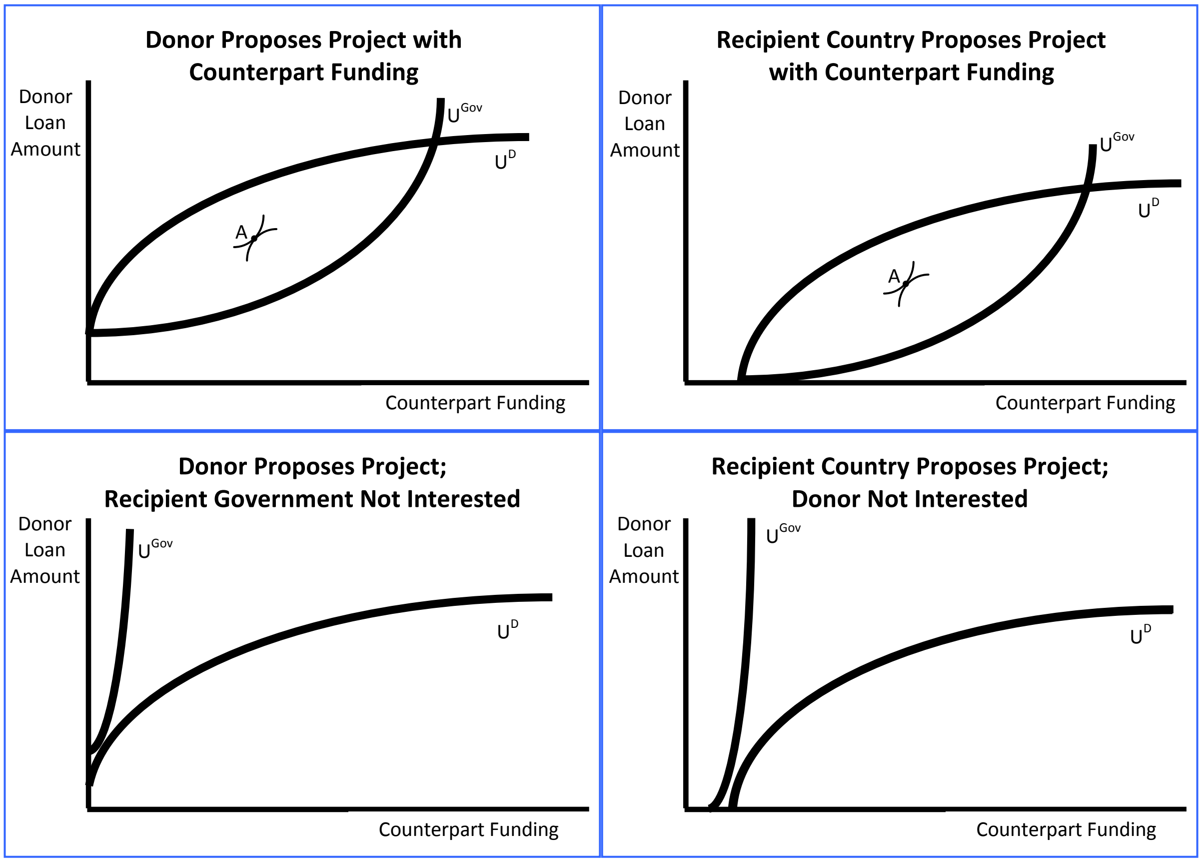

Figure 1. Possible Scenarios in Donor-Recipient Country Bargaining over Project Design

In the upper left hand corner, the project is initiated by the donor. The donor is willing to dedicate some money to the project even if the recipient country is not willing to dedicate any. As the country becomes willing to provide money for the project, the donor is willing to provide additional aid money, although the marginal amount is decreasing as project size increases. And therefore an agreement can be reached that includes some donor funding and some counterpart funding. Similarly, as pictured in the upper right hand corner, there may be a project initiated by the government, where it

[6] We gratefully acknowledge Christopher Kilby's advice on how to depict the bargaining space.

will undertake the investment on a certain scale even if the donor provides no money. Then as the donor provides more money, the government also will be willing to provide additional funding. Both the donor and the government have some maximum amount of money that they would be willing to contribute to the project. Based on the decreasing marginal utility of contributing additional amounts of one's own money, the two sides reach agreement on a certain mix of recipient-government and donor funding.

In the lower left hand corner, the government is willing only to contribute a small amount of money – it quickly reaches its tolerance for counterpart funding – and therefore the donor opts to undertake a relatively small project with no counterpart funding involved. In the lower right hand corner, the government is willing to contribute a certain amount and no more, and this amount is not enough for the donor to be ready to finance part of the project. In this case, the government finances a relatively small project on its own without any donor funding.

What are the factors that influence the willingness of an aid agency to provide more or less funding for a given amount of counterpart funding? And conversely what are the factors that influence the willingness of an aid-receiving state to agree to more or less counterpart funding for a given level of international aid?

In what follows, we think specifically of the World Bank as our aid agency of interest. We expect the World Bank to request smaller counterpart commitments from democratic countries, countries with more external debt, and countries with a lower GDP per capita, whereas we expect it to request greater counterpart commitments from countries that already carry a large debt to the Bank. We expect borrowing countries with greater bargaining leverage - measured through access to more sources of foreign capital, greater geostrategic relevance to the Bank's principals and more domestic veto players - will commit to aid projects with smaller counterpart commitments in their aid projects. Our expectations with regard to governance quality are mixed as we suggest that the World Bank will request smaller counterpart commitments from better governed countries but also anticipate that better governed countries are more likely to originate projects and thus have a greater willingness to commit to projects with larger counterpart funding. We begin by discussing this relationship between good governance and counterpart funding and then discuss other potentially relevant economic and political factors.

Governance. Thinking about preferences on the World Bank's side, we propose that World Bank staff are concerned about whether or not aid will be used for the purposes of poverty alleviation and catalyzing economic growth. In general, there has been a concern at the World Bank with tying aid allocation to borrowing country performance since at least the 1969 Pearson Commission Report (see the discussion in Easterly 2007). In particular, since the 1998 *Assessing Aid* volume, which argued that countries with good policies and institutions make better use of foreign aid (as per the results found in Burnside and Dollar 2000), the World Bank has emphasized allocating aid to those countries that have a certain set of allegedly beneficial institutions and policies. Most notably, this can be seen in the Performance-Based Allocation System used to divvy up IDA funding (see the discussion in Winters 2010). The observed reality seems to match the stated intent to some extent: a series of studies find some evidence – although not overwhelming evidence – that governance characteristics predict aid allocation patterns at the World Bank and for IDA funding in particular (Neumayer 2003; Dollar and Levin 2006; Easterly 2007; Winters 2010).

We extend the empirical analysis of the relationship between governance and World Bank aid allocation down to the project-level, arguing that not only should governance predict overall aid allocation but that it also should predict the design of specific aid projects.[7] In better-governed

[7] This mirrors the expectations in Winters (2010) that the World Bank should use more programmatic lending and more nationwide investment lending in better-governed countries. In that paper, good governance is positively associated with increased nationwide investment lending for both the IDA and IBRD, whereas good governance is associated with increased programmatic lending only for the IBRD and surprisingly with decreased programmatic lending among IDA borrowers.

countries, the World Bank will be more willing to dedicate its own funds for a given level of project financing. Insofar as the Bank believes that its money is going to be used for the intended development purposes, it should be more willing to provide funding even when the country is not providing large amounts of its own money for the project.

At the same time, however, we also argue that well-governed countries may be more likely to come to the World Bank with projects in hand and are perhaps only looking for limited amounts of World Bank funding to compliment the money that they already are willing to commit to the project. That is, countries with highly effective governments are more likely to have prepared projects for which they want only additional financing or technical expertise from the Bank. If this is in fact the case, then it may be difficult to find a uniform effect of governance on counterpart fund levels in World Bank projects, since good governance might either decrease the level of counterpart funding desired by the World Bank or else increase the level of counterpart funding offered by the aid-receiving country.

Democracy. As compared to our two-sided expectations about how governance quality might affect counterpart funding, we view democracy as something likely to affect World Bank decision making about counterpart funding but less likely to directly affect the government's willingness to commit counterpart funds. On the World Bank side, we expect democratic countries to be regarded, on average, as better public goods providers (Lake and Baum 2001; Baum and Lake 2003) such that the World Bank will be more willing to dedicate funds to projects in democratic countries even when there is a lower level of domestic funds on offer for the project.

Economic Factors. There are several economic characteristics of countries that might affect either their willingness to contribute counterpart funding or else the World Bank's desire to see more or less counterpart funding. A country's level of economic development (as measured by its GDP per capita) should positively predict the willingness of countries to provide counterpart funding insofar as the opportunity cost of providing such funding is lower in richer countries. External debt, on the other hand, raises the opportunity costs of providing counterpart funding and so should reduce a country's willingness to do so. We expect the World Bank to be in agreement on this issue insofar as high levels of external debt indicate economic precariousness. If the World Bank is interested in the overall stability of its borrowing countries, it should demand less domestic funds for projects in debt-burdened countries.

Aid-Related Factors. A robust finding from the conditionality literature is that countries with access to alternative sources of financing have been most able to resist harsh conditions in their structural adjustment programs. Mosley, Harrigan and Toye, for instance, find that "large countries with a great deal of scope to borrow elsewhere" are those with the loosest conditionality (1991: 105), and Killick identifies "a clear inverse relationship between the use of conditionality and recipient governments' access to alternative sources of financing" (1998: 12). Therefore, we expect those countries that have access to a larger variety of financing sources similarly will be more able to avoid counterpart funding commitments. Countries that have access to foreign aid coming from multiple sources are less dependent on World Bank aid flows in particular. Therefore, these countries should be less willing to exchange their own domestic funds for World Bank funds if they might be able to gain access to external financing elsewhere. Countries that are more reliant on the World Bank, on the other hand, have fewer outside options to which they can turn and therefore might have to make greater contributions to investment projects for the same levels of counterpart funding.

Domestic Politics and Geostrategic Importance. Finally, we highlight two factors that might influence a country's bargaining leverage vis-à-vis the World Bank and make it more able to gain access to larger World Bank loans even given a relatively small counterpart commitment. World Bank projects are like international treaties and therefore often require parliamentary approval, implying that projects might be derailed by domestic institutions even after agreement has been reached at the international level.[8] To the extent that there are more veto players in a country who might be able to stop a World Bank project from gaining full approval, we expect to see fewer counterpart commitments, since veto players might complain about the amount of financing being requested of the borrowing country.[9] In a study of IMF conditionality, Stone (2008), for instance, finds less conditionality in countries where there is a powerful domestic opposition.

Similarly, if an aid-receiving country is geo-strategically important, such that the United States or other developed country principals at the World Bank might bring their influence to bear on aid agency technocrats, we expect that the country will be able to offer less counterpart funding for the same level of World Bank funding. The threat of external pressure on the Bank shifts the bargaining space in favor of the country. An extensive literature finds that the interests of important developed countries predict patterns in overall World Bank aid allocation (Frey and Schneider 1986; Andersen, Hansen and Markussen 2006; Fleck and Kilby 2006; Dreher, Sturm and Vreeland 2009). Stone (2008) finds evidence that the United States uses its informal power to reduce the level of IMF conditionality for certain countries, while Stone (2002) finds that strategically important countries are less likely to suffer from punishment if they fail to live up to their commitments to the IMF.[10]

Disentangling Project Origins. Insofar as some projects are originating with recipient countries and not the World Bank, this presents a major concern for our analysis. In these cases, the developing countries will not always view counterpart funding in a negative light – we are on the right hand side of Figure 1, where countries are willing to provide some project financing even if the donor will not be providing any. Where the World Bank is truly being used as a development bank, countries may

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[8] In December 2009, for instance, the Nigerian House of Representatives rejected a $300 million World Bank loan, saying that the president had not sufficiently consulted with the National Assembly before agreeing to the loan (Nzeshi 2009).

[9] Vreeland (2003) examines the way in which a single veto player influences the design and negotiation of IMF programs.

[10] Winters (2010), on the other hand, finds only mixed support for the hypothesis that strategic interest variables will predict project design. That paper presents some evidence that those countries that vote with the United States at the United Nations are more likely to receive national projects. On the other hand, countries that engage in significant levels of trade with the United States are less likely to receive fungible programmatic lending.

approach the World Bank needing only a limited amount of additional financing in order to realize an investment project or else wanting the World Bank to contribute only its technical expertise rather than a large amount of funding. Where this is the case, a high level of counterpart funding is not a sign of bargaining weakness, and some of the hypotheses described above will not apply. Looking at the raw data, we see a number of cases where this scenario is, in fact, likely to be the truth: the very high levels of funding coming from the recipient country suggest that the project is country-driven rather than Bank-driven.

Description of the Data

To assemble data on counterpart funding, we downloaded the entire World Bank Projects Database as of the end of the 2010 calendar year. We retained only those projects classified as "IBRD/IDA" projects, which represent the subset where the Bank is the least constrained in its decision making (as compared to those projects that are part of the Global Environment Facility or other World Bank-administered trust funds). These projects represent 86 percent of entries in the database. We then eliminated all development policy lending projects on the grounds that an initial review of such projects found that they do not require counterpart commitments from the borrowing countries.[11] Eliminating pipeline projects, dropped projects and projects that listed no lending amount, we were left with 9,726 IBRD and IDA projects dating back to 1948. For this paper, we use a random sample of 1,565 projects (out of 2,633) from the years 2000-2010. In the future, we will complete the coding for these 10 years and extend the time period back.

For each project, we recorded from the "financial tab" found in the Projects Database, the amount of project funds coming from both government and non-government sources in the aid-receiving country. We also recorded this same information from the Project Appraisal Document (PAD)

[11] This makes sense in terms of programmatic lending going directly into the national treasury without having a dedicated purpose

associated with each project or from another relevant document (usually the Project Paper) when the PAD was unavailable. The PAD-derived data reflect counterpart commitments at the time of project approval by the World Bank Board of Directors, whereas the financial tab data reflect counterpart commitments after revisions to the project during the implementation process.

Because of the way that additional funding for projects is recorded in the project database, a number of our observations are not new projects but rather supplementary funds for existing projects. These instances of supplementary funding do include counterpart funding, but in some instances, we remove them from the analysis, since the decision making about these project ledger entries may be different from the initial decision making about new projects.

In the next two sections, we provide descriptive results at the project-level using two outcome variables: an indicator for whether or not a project has any counterpart funding commitment at all and then the ratio of counterpart funding to the total project size. The total project size includes the World Bank's commitment, funding from other multilateral and bilateral donors and the counterpart commitments if any. The descriptive statistics reveal that more counterpart commitments are provided in large infrastructure projects and that levels of counterpart funding decrease during project implementation.

Dividing the Tab on Big Infrastructure Projects

Of the 1,565 projects in our dataset, three-quarters of them feature some level of counterpart funding at approval. On average, almost one-quarter of project financing is expected to come from within the borrowing country. (As we discuss in the next section, this level of financing actually declines as project implementation progresses.) Figure 2 and Figure 3 show the way in which counterpart funding commitments are distributed across different project types.

Figure 2 shows the proportion of projects with counterpart funding and the average percent of project funding that come from borrowing-country counterparts across the World Bank's classifications of project type. In infrastructure-heavy sectors, such as water and sanitation, transportation, and energy and mining, we find both higher proportions of projects with counterpart funding and higher levels of counterpart funding within those projects. Projects that support programming in the information and communications, finance, public administration, and industry and trade sectors, on the other hand, are less likely to involve counterpart financing and involve somewhat smaller amounts when they do. The agriculture, fishing and forestry sector is an interesting case. Although projects in this sector are the most likely type of projects to include counterpart financing, the amount of financing is relatively less than for most other sectors.

In Figure 3, we show the relationship between total project size and the amount of counterpart financing. There is a positive association between the two with larger projects requiring more financing from sources within the borrowing country. The plot makes clear that there are some very large projects where the borrowers supply almost *all* of the financing. The countries involved in these projects are some of the biggest World Bank borrowers: Argentina, Brazil, China, Mexico, India and Indonesia. The plot also makes clear the level of variation possible within individual countries. India has had similarly-sized investment projects where only a small portion of the money (less than 20 percent) comes from the World Bank and where a large portion of the money (almost 80 percent) comes from the World Bank.

Therefore, in our first glimpse at the data, we find that infrastructure-heavy projects are likely to involve larger amounts of counterpart funding and that the costliest projects with which the World Bank is involved are often majority-financed by sources within the borrowing country. Importantly, these patterns suggest that a mixture of processes may be determining the levels of counterpart commitments in World Bank projects. Where projects are majority-financed by the borrowing country,

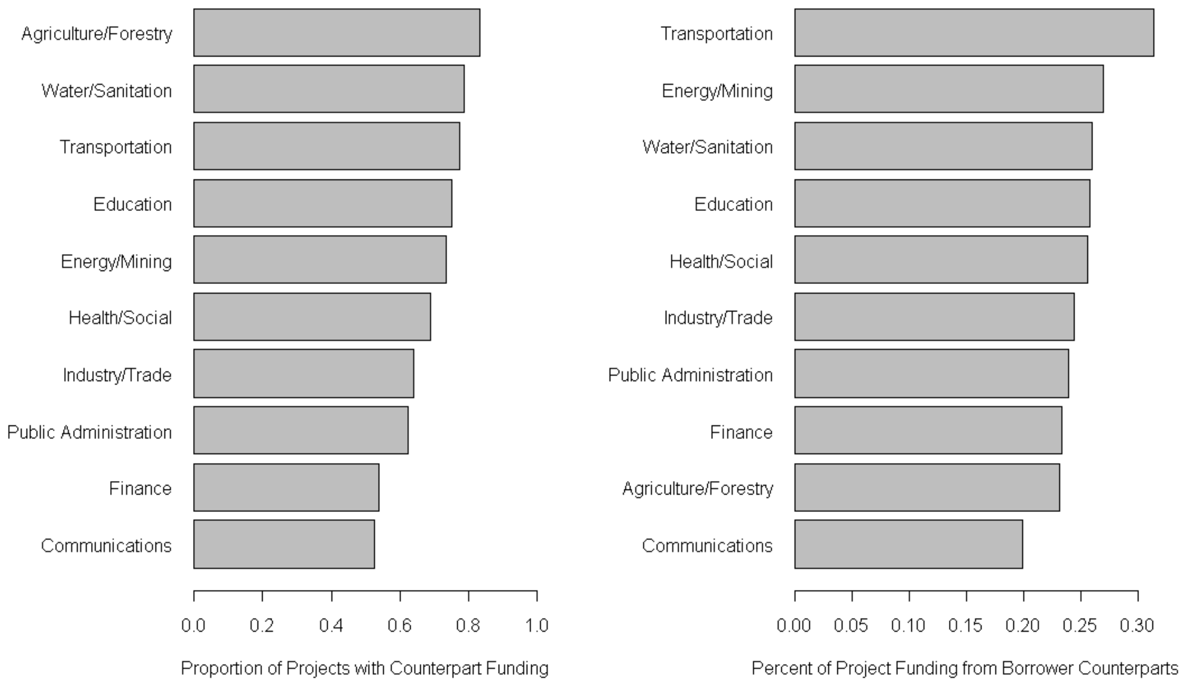

Figure 2. Counterpart Funding by Project Sector. The right-hand plot includes only projects with positive levels of counterpart financing.

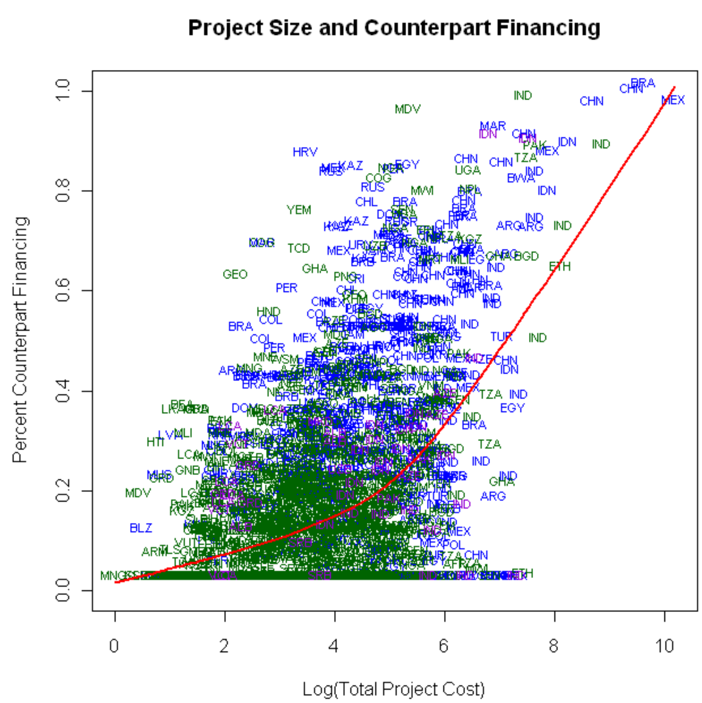

Figure 3. Project Size and Counterpart Financing. IBRD projects in blue; IDA projects in green; blend projects in purple. The trend line is a locally-weighted regression line.

it seems likely that the project originated within the borrowing country, which then asked the World Bank to contribute to the project either because of the need for some additional financing or, more likely, because of a desire for the Bank's expertise.

Renegotiating Over Time: Counterpart Commitments from Project Approval to Project Implementation

The second trend that becomes apparent by looking at the project-level data on counterpart commitments is that some level of renegotiation between the Bank and its borrowers occurs over time. In Table 1, we report the data from both the Project Appraisal Document, which is presented to the Board of Directors and therefore reflects counterpart commitments at the time of project approval, and from the financial tab of the Projects Database, which reflects counterpart commitments at the time when we collected the data (after project implementation had begun in most cases). As can be seen by comparing the third and fourth columns and the fifth and sixth columns, the likelihood that a project will have any counterpart financing and the level of that counterpart financing both decrease from the project approval data to the implementation phase data. For some projects, therefore, it seems that counterpart financing comes to make up a smaller proportion of total project funding or to cease to be a component of project funding altogether as project implementation advances.

Table 1 also shows the variation in counterpart financing across projects for the two wings of the World Bank – the concessional-lending International Development Association (IDA) and the near-market-rate-lending International Bank for Reconstruction and Development (IBRD) – and for projects that are jointly financed by the IDA and IBRD within the small set of countries that is approved for borrowing from both (so-called "blend" countries or projects). Similar to the patterns observed in Figure 3, the data reveal that World Bank projects in the middle-income countries that borrow from the IBRD or from both the IBRD and the IDA are more likely to involve counterpart financing and are likely to involve higher levels of counterpart financing.

On the one hand, these differences make intuitive sense. IBRD and blend borrowers are wealthier countries and therefore have a greater capacity to make contributions and to make larger contributions to investment projects. On the other hand, however, we might have expected IBRD borrowers to have more leverage with the World Bank in terms of their willingness to accept counterpart commitments, particularly since the World Bank is, in fact, dependent on IBRD borrowers for its continued existence. But the data suggest that insofar as IBRD borrowers do have such bargaining power, they are not exercising it to the extent where their counterpart commitments look like those of IDA borrowers.

World Bank Division	Number of Projects in Dataset	Percent of Projects with Any Counterpart Financing at Approval	Percent of Projects with Any Counterpart Financing at Time of Data Collection	Average Percent of Total Project Financing from Borrowing Country at Approval	Average Percent of Total Project Financing from Borrowing Country at Time of Data Collection
IDA	972	68	64	16	12
Blend	42	90	88	26	22
IBRD	551	88	83	35	29
Total	1,565	76	72	23	19

Table 1. Counterpart Financing Over Time and Across World Bank Lending Wings. Data in columns three and five comes from the Project Appraisal Document (PAD), Project Paper or similar pre-implementation document; data in columns four and six comes from the Financial Tab of the Projects Database. In the combined data, paired difference-in-means tests for the percent of projects with any counterpart funding ($p < 0.00$) and the average percent of total project financing from the borrowing country ($p < 0.01$) show significant changes between the approval data and the data at the time of collection. (For each individual lending wing, the significance levels drop.) Difference-in-means tests for the percent of projects with counterpart financing are significant for IDA against either IBRD or blend projects ($p < 0.00$). Difference-in-means tests for the average percent of total project financing show significant differences between the IDA against IBRD or blend projects ($p < 0.00$) and also between IBRD and blend projects ($p < 0.01$).

The fact of declining counterpart commitments over time shows that bargaining between the World Bank and its borrowers continues after initial project approval. As obsolescing bargaining theory would predict, after a country achieves an initial agreement with an outside donor – in this case, the World Bank – it can later renege on some amount of its commitment. Perhaps because of the repeated game nature of being a World Bank borrower, the amount of reneging that we observe is relatively minor, but nonetheless we are able to observe significant differences between the amount of counterpart funds that were supposed to be devoted to a project at the time of the project's approval and the amount that actually are disbursed during project implementation.

Governance Quality and Counterpart Funding

In this section, we focus on our main variable of interest: the quality of governance. Thinking from the World Bank's perspective, we believe that the Bank will want more poorly-governed countries to show their commitment to particular development projects by making greater counterpart commitments. In order to use country-level predictors to explain patterns in counterpart funding, we create a country-year dataset in which the outcome variable is the average proportion of counterpart financing across World Bank-funded projects in a given country for a given year.

At first glance, the data do not support the claim that poor governance positively predicts levels of counterpart funding. The left panel of Figure 4 shows the bivariate relationship between the average value for a country on the six World Governance Indicators and the average amount of counterpart financing in the projects agreed upon by that country and the World Bank. The relationship is positive and significant. A one-point increase on this scale of governance corresponds to a seven percentage point increase in the average amount of counterpart funding in a World Bank project. This would seem to disconfirm our argument that the World Bank is requiring more counterpart funding of more poorly-governed countries. Instead it lends some support to the notion that better-governed countries are coming to the World Bank with projects for which they want additional financing or technical assistance.

The second panel of Figure 4 similarly shows no relationship between counterpart funding and the widely-used Polity measure of democracy. More democratic countries – by the Polity measure – have neither greater nor lesser levels of counterpart funding commitments in their World Bank projects. If we instead compare the amounts of counterpart funding across democracies and non-democracies as defined by the Cheibub, Gandhi and Vreeland (2010) Democracy and Dictatorship dataset, we find a marginally significant ($p < 0.07$) difference where democratic country-years have projects with an average of 18.5 percent counterpart funding and non-democratic country-years have projects with an average of 16.2 percent counterpart funding. The direction of this difference again goes against our expectations.

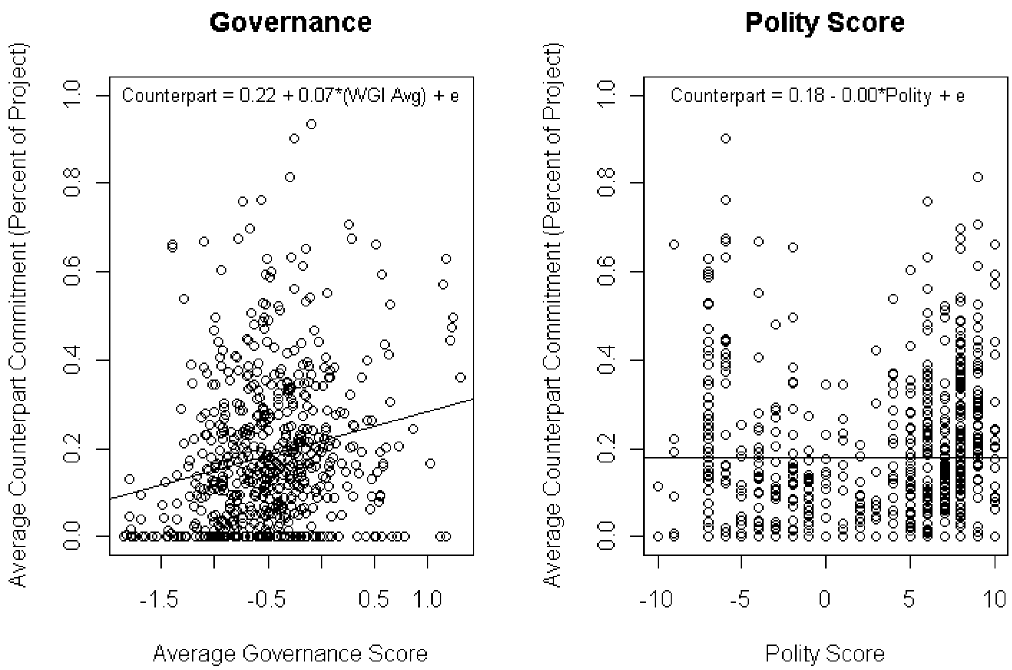

Figure 4. Bivariate Relation Between Counterpart Commitments and Governance. Each data point is a country-year observation. Average governance score is the mean value of the six World Governance Indicators. The trend line is from the bivariate regression equation reported at the top of each figure.

In order to diagnose the finding for the governance variable, we examine the six different indicators that we had averaged into the overall governance indicator. The first column of Table 2 shows the bivariate relationship between each indicator and the average level of counterpart funding. The largest relationships are for government effectiveness and regulatory quality, suggesting that the positive relationship between governance and counterpart funding might actually be driven by recipient-country decision making rather than World Bank decision making – specifically, it might be that more capable countries propose projects which include larger amounts of counterpart funding. This again complicates donor-driven views of aid allocation.

World Governance Indicator	Bivariate Relationship with Average Counterpart Funding	Coefficient in a Multivariate Regression Predicting Average Counterpart Funding
Voice and Accountability	0.03*** (0.01)	-0.02 (0.01)
Political Stability	0.02** (0.01)	-0.02 (0.01)
Government Effectiveness	0.11*** (0.01)	0.21*** (0.04)
Regulatory Quality	0.09*** (0.01)	0.02 (0.03)
Rule of Law	0.06*** (0.01)	-0.03 (0.03)
Control of Corruption	0.06*** (0.01)	-0.07** (0.03)

Table 2. Governance and Counterpart Funding. * - p < 0.10; ** - p < 0.05; *** - p < 0.01. Multivariate regression includes an unreported constant. Data comes from the Project Appraisal Document (PAD), Project Paper or similar pre-implementation documentation.

This conclusion is reinforced by the multivariate regression reported in the second column of Table 2, which uses all six governance indicators to predict counterpart funding. Although these point estimates should not be entirely believed because of lack-of-complete-overlap issues when using all six governance indicators as predictors, we see that government effectiveness is large, positive and significant, whereas four of the other indicators are not significant at conventional levels. In the multivariate regression, as in the series of bivariate regressions, we find evidence that capable governments are committing more of their own funding to World Bank projects.

However, we do not want to put too much stock in these results at first, since World Bank lending patterns will be determined by a variety of factors, some of which may be highly correlated with a country's quality of governance. Therefore, the bivariate results may actually represent a different phenomenon, where some factor correlated with governance is predicting the observed level of counterpart funding. To address this possibility, we turn to a multivariate analysis. We predict counterpart contributions as a percent of total project cost at the time of project approval using a set of economic and governance indicators.

The model includes four economic indicators: GDP per capita PPP, external debt normalized by GNI, overall aid dependence normalized by GNI, and outstanding debt to the World Bank. We expect wealthier countries to have a greater capacity to make counterpart commitments and therefore either to be more likely to propose projects with large counterpart commitments to the Bank or else be less able to negotiate smaller counterpart commitments when making agreements with the Bank. We expect more indebted countries to have a reduced capacity to make counterpart commitments and therefore more able to negotiate smaller counterpart commitments – an example of the bargaining strength of the weak. Countries that receive a lot of aid have more options when it comes to sources of external financing; we therefore expect them to have a stronger negotiating position with the World Bank and to make smaller counterpart commitments. On the other hand, if countries are receiving lots of money from the World Bank itself, they are less likely to be able to assert themselves vis-à-vis the Bank and more likely, as a consequence, to end up having to agree to larger counterpart commitments. All four of these expectations are supported in bivariate analyses.[12]

On the political side, we include the measures of governance described above, the measures of democracy described above and also a variable that captures the number of institutional veto players in the country. We expect there to be a negative relationship between veto players and counterpart commitments, since more constrained countries should be able to negotiate smaller commitments.

Because of the large number of observations where there were no counterpart funds in a given country-year, we use a Tobit model that takes account of this left-censoring.[13] Table 3 presents the results of these analyses.

[12] Results not reported.

[13] That is, the latent variable might be the some sort of affection factor that counterpart funding proxies for, and this factor could conceivably be greater than some value that results in zero counterpart financing. The Tobit model addresses this.

	(1)	(2)	(3)	(4)	(5)
	World Governance Indicators Average	Government Effectiveness	Government Effectiveness with Democracy	Polity	Data from Financial Tab
World Governance Indicators Average	0.025 (0.02)				
WGI Government Effectiveness		0.045** (0.02)	0.046** (0.02)	0.040* (0.02)	0.016 (0.02)
Democracy Indicator			-0.036* (0.02)		-0.057*** (0.02)
Polity Score				-0.005*** (0.00)	
Log(GDP Per Capita PPP)	0.050 (0.04)	0.033 (0.04)	0.045 (0.04)	0.065 (0.04)	0.068 (0.04)
Log(External Debt/GNI)	0.042 (0.03)	0.050* (0.03)	0.053* (0.03)	0.052* (0.03)	0.016 (0.03)
Log(ODA/GNI)	-0.073*** (0.02)	-0.072*** (0.02)	-0.072*** (0.02)	-0.065*** (0.02)	-0.072*** (0.02)
Log(Outstanding Debt to World Bank)	0.057*** (0.02)	0.052*** (0.02)	0.052*** (0.02)	0.052*** (0.02)	0.042** (0.02)
Veto Players	-0.003 (0.00)	-0.002 (0.00)	0.001 (0.00)	0.004 (0.01)	0.004 (0.005)
Constant	-0.508 (0.26)	-0.409 (0.26)	-0.450* (0.26)	-0.530* (0.28)	-0.404 (0.27)
Log Likelihood	83.24	84.6	86.4	80.87	42.74
N	467	467	467	440	489
Uncensored Observations	411	411	411	389	405

Table 3. Multivariate Tobit Analysis of Governance, Economic Indicators, and Counterpart Funding. Data comes from the Project Appraisal Document (PAD), Project Paper or similar pre-implementation documentation in columns (1) through (4). Column (5) uses data from the Financial Tab of the Projects Database. The unit of analysis is the country-year. The outcome variable is the average proportion of counterpart funding across projects in a given country-year; we consider it left-censored when it takes the value 0. * - $p < 0.10$; ** - $p < 0.05$; *** - $p < 0.01$.

In the first column, we find – in line with the bivariate results – that the overall governance average is a positive but insignificant predictor of counterpart commitments; similarly, in the second column, government effectiveness shows up as a significant, positive predictor of counterpart commitments. In the third column, we add the Cheibub, Gandhi and Vreeland (2010) dichotomous indicator of democracy. Here we find that democracies make smaller counterpart commitments, while also continuing to find that countries with more effective governments make larger counterpart commitments. The same results obtain when measuring democracy using the Polity score in the fourth column. Therefore, in contrast to the bivariate results that showed little evidence of democracies being treated in a different fashion from non-democracies, here we find that democratic countries are likely to contribute lower levels of counterpart funding to World Bank projects.

There are at least two explanations for why we would see this pattern in the data. On the one hand, the World Bank may view democracies as more credible implementers of its projects. If this is the case, the Bank might require additional counterpart financing from non-democracies as a way of forcing those countries to demonstrate their commitment to implementing the agreed-upon project. On the other hand, democracies may be better able to negotiate smaller counterpart commitments because of the threat that the legislature will reject a proposed project if the requested counterpart commitment is too large. However, we try to control for this possibility by directly measuring the number of veto players within a country using the appropriate variable from the Database of Political Institutions. This variable consistently comes up as insignificant in the regressions (and positively signed in the models where democracy is also included). Therefore, we are inclined to think that the negatively signed democracy variable actually provides information about the Bank's decision making process rather than being indicative of democratic countries having additional leverage in the negotiating process.

In the fifth column, we use the data collected from the Projects Database Financial Tab. This data reflects changes made after project implementation has begun. In this data, democracy still negatively predicts counterpart commitments, but government effectiveness is no longer a significant predictor, although it remains positively signed.

Across all of the models, we see that countries with a high dependence on aid enter into agreements with the World Bank that include lower counterpart commitments, while countries that already have high outstanding debt with the World Bank contribute more of their own money toward projects. The former result might suggest either an ability of countries with a high degree of aid dependence to be more selective about which World Bank projects they choose, or alternatively it might suggest some substitutability between government funding and funding from other donors: the World Bank is looking for someone to cofinance the project, and it can either be the borrower itself or else other donors. The latter result seems to suggest that large World Bank borrowers need to commit more of their own funds for additional projects, either because the Bank needs this level of commitment from these borrowers or perhaps because these countries are more aggressive about asking the Bank to join them for specific projects that they want to accomplish.

Our multivariate analysis reveals two consistent and important patterns. First, democracies commit fewer counterpart funds to World Bank projects as compared to non-democracies, holding other country characteristics constant. We believe that this is a result of World Bank decision making that views the commitment of a democratic country to implement a project as more credible than a similar commitment by a non-democratic country. Second, countries receiving more aid in general make smaller counterpart commitments, whereas those receiving more aid from the World Bank make larger counterpart commitments. We believe that this reflects negotiations between the World Bank and its borrowers in which having access to alternative sources of finance gives bargaining strength to the borrowing country, whereas being reliant on the World Bank results in bargaining weakness.

How Deep Does External Influence Go? The Strategic Manipulation of Counterpart Commitments

Previous literature has found evidence of U.S. influence at the World Bank when it comes to the Bank's overall patterns of aid allocation (Frey and Schneider 1986; Andersen, Hansen and Markussen

2006; Fleck and Kilby 2006; Dreher, Sturm and Vreeland 2009). However, there is less evidence that this influence extends to the level of project design (Mosley, Harrigan and Toye 1991; Winters 2010); that is, the U.S. may be able to influence which countries are getting money, but decisions about how exactly they get that money are made by World Bank staff.[14] Therefore, on the one hand, we might expect that countries of strategic interest to the U.S. would be asked to make smaller counterpart commitments in World Bank projects, such that they would be receiving aid money more cheaply (i.e. with fewer conditions). But on the other hand, we might expect World Bank staff to maintain operational independence when it comes to decisions on counterpart financing, such that strategic interest variables that predict overall World Bank aid allocation do not, in fact, predict counterpart commitments.

We use five variables to identify countries in which the United States might have a particular interest and thereby examine the role of U.S. influence at the World Bank when it comes to decisions on counterpart funding. In a series of regression models, we proxy for U.S. interest with the amount of ODA and the amount of military assistance that the United States sends to a given World Bank borrower (as reported to the OECD-DAC and in the U.S. Greenbook respectively), with a measure of the similarity of voting at the United Nations (a measure based on Barro and Lee 2005 from the updated dataset associated with Dreher and Sturm 2006), and with measures of U.S. exports to and total trade with a given World Bank borrower (data from the OECD web site). Taking model (3) from Table 3 as our baseline, Table 4 presents results from models where each of these variables is included as a proxy for U.S. strategic interest.

The inclusion of the strategic variables does not change any of the core results reported above. Government effectiveness remains a significant, positive predictor of counterpart funding, and we see the same pattern of democracies making smaller counterpart commitments. Countries that receive

[14] That said, there is evidence that U.S. influence mediates the severity of punishment for non-compliance with World Bank (and IMF) agreements (Mosley, Harrigan and Toye 1991; Stone 2002; Gould and Winters 2007).

more aid make smaller counterpart commitments, and those that have a larger outstanding loan portfolio at the Bank make larger counterpart commitments.

	(1)	(2)	(3)	(4)	(5)
Measure of Strategic Interest	Log(U.S. ODA)	Log(U.S. Military Assistance)	Voting with U.S. at the U.N.	Log(U.S. Exports)	Log(Total Trade with U.S.)
Strategic Interest Variable	-0.012 (0.013)	0.00059 (0.035)	0.16 (0.13)	0.013 (0.015)	0.022* (0.013)
WGI Government Effectiveness	0.041* (0.024)	0.053** (0.022)	0.048** (0.022)	0.046** (0.022)	0.050** (0.022)
Democracy Indicator	-0.032* (0.019)	-0.040** (0.019)	-0.042** (0.020)	-0.038** (0.019)	-0.039** (0.019)
Log(GDP Per Capita PPP)	0.080* (0.041)	0.042 (0.042)	0.025 (0.044)	0.043 (0.041)	0.043 (0.040)
Log(External Debt/GNI)	0.054* (0.030)	0.057** (0.029)	0.049* (0.029)	0.057* (0.029)	0.061** (0.029)
Log(ODA/GNI)	-0.057** (0.022)	-0.072*** (0.021)	-0.077*** (0.020)	-0.063*** (0.022)	-0.054** (0.022)
Log(Outstanding Debt to World Bank)	0.078*** (0.021)	0.048*** (0.017)	0.049** (0.017)	0.046** (0.018)	0.041** (0.018)
Veto Players	-0.0017 (0.0049)	0.0011 (0.0050)	0.0016 (0.0050)	0.0010 (0.0050)	0.0010 (0.0050)
Constant	-0.71** (0.29)	-0.40 (0.27)	-0.36 (0.27)	-0.51* (0.27)	-0.55** (0.27)
Log Likelihood	94.68	89.38	87.16	86.82	87.78
N	424	464	467	467	467
Uncensored Observations	374	410	411	411	411

Table 4. Multivariate Tobit Analysis of Strategic Variables and Counterpart Funding. Data comes from the Project Appraisal Document (PAD), Project Paper or similar pre-implementation documentation. The unit of analysis is the country-year. The outcome variable is the average proportion of counterpart funding across projects in a given country-year; we consider it left-censored when it takes the value 0. * - p < 0.10; ** - p < 0.05; *** - p < 0.01.

With regard to the measures of strategic interest, the only variable that shows a statistically significant relationship is the total trade variable, and in this case, the relationship is positive, meaning that World Bank borrowers who trade more overall with the U.S. make larger counterpart commitments. Most likely, this relationship has little to do with the status of these countries as large

U.S. trading partners. Therefore, we ultimately find little evidence that U.S. strategic interest in borrowing countries predicts the amount of counterpart funding that they are asked to contribute to World Bank projects.

Discussion and Future Research Directions

Foreign aid projects are negotiated between donors and recipients. In the literature, there often appears to be an implicit assumption that these negotiations are rather one-sided with donors giving what they want and recipients accepting whatever they get. We question this donor-dominant view by looking at the levels of counterpart funding in World Bank projects and proposing factors that would influence the preferences of the World Bank and the recipient state as well as recipient states' negotiating power. We argued that the World Bank is likely to want more counterpart funds from poorly governed and non-democratic states and that states might have more bargaining power where they have outside options for foreign assistance or are of strategic importance to the Bank's rich-country principals.

Our results show that governance and economic characteristics of the recipient country relate to the varying levels of counterpart commitments, while a borrower's strategic relevance to the World Bank's principals bears little influence on commitment size. We find that non-democracies do, in fact, make larger counterpart commitments. We also find, however, against our expectations that well-governed countries also make larger counterpart commitments. We find that countries receiving more ODA – and therefore having more options for foreign financing – are likely to make smaller counterpart commitments. However, countries that are more in debt to the World Bank make larger counterpart commitments. There is little evidence that strategically relevant countries are able to bargain for smaller counterpart commitments, suggesting that U.S. influence at the World Bank does not extend down to the level of project design. Countries with more veto players also appear unable to turn this into a bargaining advantage that reduces counterpart funds.

In developing our initial hypotheses we assumed that the desirable outcome for recipient countries was to have smaller required counterpart contributions. However, the descriptive statistics show a substantial number of projects in which the recipient governments make the majority contribution. These projects are likely recipient-drive projects. Insofar as the World Bank's involvement in such projects comes at the country's request, the bargaining over counterpart commitments is likely to be a very different phenomenon from the cases where the Bank and the country have developed a project in consultation. At the moment, we do not know how to distinguish these two types of projects a priori, and so the seemingly contradictory results on governance and democracy may result from the mixture of project types and project negotiation processes in the data.

In the descriptive statistics, we also showed that counterpart funding, on average, declines between project approval and project implementation. This would be a useful area for future resource: which countries see the largest reduction in their counterpart commitments after project implementation begins? Are there any factors that predict increased counterpart funding over time? We believe that the new source of data we have exploited in this paper will help to push forward the aid allocation literature beyond questions of overall aid flows and further into considering project design decisions.

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