



The Role of Foreign Aid in Post-Conflict Countries

Léonce Ndikumana

October 2015

WORKINGPAPER SERIES

Number 405

POLITICAL ECONOMY
RESEARCH INSTITUTE

The Role of Foreign Aid in Post-Conflict Countries¹

Léonce Ndikumana²

University of Massachusetts, Amherst

October 2015

Abstract

This paper discusses the role that international development assistance can play in helping post-conflict countries address their structural constraints and avoid or at least minimize the risk of new conflict. The paper argues that the success of the post-conflict reconstruction agenda is contingent on the existence of a capable state that is able to deliver on its core functions, especially security, law and order, provision of public services, and revenue mobilization. The paper singles out revenue mobilization as important not only for the performance of other core functions of the state, but also for building the required policy space needed to genuinely own the national development agenda.

Key Words: post-conflict countries; aid; state building; revenue mobilization; institutions; peace building.

¹ This paper is forthcoming as a chapter in *Building Sustainable Peace: Timing and Prioritization of Post-Conflict Reconstruction and Peacebuilding*, edited by Arnim Langer and Graham Brown, Oxford University Press, 2016

² Professor of Economics and Director of the African Development Policy program at the Political Economy Research Institute (PERI) at the University of Massachusetts Amherst. Contact information: Gordon Hall, 418 N. Pleasant Street, Amherst, MA 01002; Tel: +1-413-577-0241; Email: ndiku@econs.umass.edu.

1. Introduction

In a recent paper by Pritchett et al. (2012, p. 2), the authors asked the following question: ‘How do donor and recipient countries manage to engage in the logics of “development” for so long and yet consistently acquire so little administrative capability?’ While this question addresses the broader engagement between donors and developing countries in the process of institutional building and economic development, it is even more pertinent in the case of post-conflict countries. Despite substantial assistance from the international community, these countries face critical challenges stemming from the effects of the destruction of economic activity and the deterioration of state capacity and national institutions sustained during conflicts. In many cases, the end of the war is accompanied by protracted instability, exposing the countries to high risk of reoccurrence of conflicts. Thus, post-conflict countries face high risks of fragility. In fact, a majority of countries classified as fragile states are countries that are in conflict or have experienced conflicts in the past (OECD, 2014). While post-conflict countries face urgent needs for economic reconstruction, they have weak capacity to mobilize domestic resources. This is often the case also for resource-rich post-conflict countries where natural resources are often one of the factors of conflicts.

Unable to mobilize their own resources, post-conflict countries are therefore forced to depend on foreign aid to finance the reconstruction agenda. The question then is what role aid can play in helping these countries to address their structural constraints, avoid or at least minimize the risk of new conflict, and set them on a path of sustainable development. This question is particularly important because failure of post-conflict reconstruction increases the risk of new conflicts and systemic fragility. The issue is not just about the volume of aid channeled to post-conflict countries. It is also about how the aid is delivered. Especially important are the instruments used, the choice of the sectors and activities to be supported by aid, the sequencing of aid delivery, and the contribution of aid to state building and institutional reforms.

The success of the post-conflict reconstruction agenda is critically contingent on the existence of a capable state that is able to deliver on its core functions, especially security, law and order, provision of public services, and revenue mobilization. The latter function is especially important not only for the performance of the other core functions of the state, but also for enabling the government to build the required policy space needed to truly own its development agenda. Effective revenue mobilization is key to setting the country on a sustainable development path and to eventually graduate from aid dependence. This paper therefore argues that state building must feature prominently among the objectives of international assistance. This implies that evaluation of aid effectiveness in post-conflict countries needs to be expanded beyond the conventional criteria that focus on growth and other macroeconomic performance targets to include goals related to peace consolidation, state capacity building, and improvement in the quality of institutions. The paper discusses the challenges associated with promoting state

building in post-conflict countries, the key one being that there is no standard model or blueprints to emulate. There is therefore a risk of conflating functions and the form of institutions, the outcome being the establishment of institutions that have the ‘right form’ but are not functional. It is therefore important to design institutional reforms that are tailored to the particular circumstances of each country with the ultimate focus being on creating a state that can consolidate peace through inclusive institutions and that has the capacity to design and implement a pro-poor and inclusive development agenda.

The paper is organized as follows: the next section discusses the challenges associated with aid delivery in post-conflict settings. Section 3 summarizes the debate in the empirical literature and the aid profession on the effectiveness of aid in post-conflict and fragile states. Section 4 discusses the role of aid for state building and institutional reforms. Section 5 provides some evidence on aid in post-conflict, emphasizing sectoral allocation of aid. Section 6 concludes the paper.

2. Post-conflict countries: a challenging environment for foreign aid

The notion of post-conflict situation is not always straightforward; it is often difficult to determine when the conflict has ended, especially given that the risk of a new conflict remains high in the period immediately after the end of the war. Indeed, often ‘there is no easy “before” and “after” conflict’ ((UNDP, 2008, p. xviii). In practice, the post-conflict recovery process is a complex continuum of peace building milestones. Countries move through these milestones at varying pace, with varying degrees of risk of backsliding into conflict. The key milestones are (UNDP, 2008, p. xviii): easing of hostilities and violence; signing of peace agreements; demobilization, disarmament and reintegration; return of refugees and internally displaced persons (IDPs); establishing the foundation for a functioning state; initiating reconciliation and societal integration; and commencing economic recovery. Clearly each milestone is complex and it can take various amounts of time. For example, the return of refugees and resettlement of IDPs is a long process, which, if poorly managed can delay or even derail post-conflict recovery. Moreover, these milestones are not necessarily sequential, and they may interact in complex ways that affect post-conflict reconstruction. The challenge for donors is to determine the appropriate volume, sequencing, allocation and disbursement modalities of aid to best assist countries in moving through these milestones. This implies an approach that is tailored to each country’s circumstances, which imposes a heavy knowledge and capacity premium on donors.

The post-conflict period is typically characterized by high risks of fragility. Indeed, the majority of countries that are classified as fragile states are in conflict, emerging from conflict, or have experienced conflict in the past. In the case of sub-Saharan Africa, half of the 28 countries classified as fragile states by the OECD (2014) are also post-conflict countries per UNDP classification (UNDP, 2008). Fragile states are those that fail or are at high risk of failing along three key dimensions: authority, service provision and legitimacy (Stewart and Brown, 2009).

Conflicts undermine state capacity along all these three dimensions. Therefore, donor intervention in post-conflict countries is confronted with the structural challenges inherent to fragile state situations.

Delivering aid in post-conflict countries poses deep rooted questions about the choice of aid instruments and the implications of such choices for aid effectiveness. Considering the key features of the three most commonly utilized aid instruments can help illustrate this problem: budget support, multi-donor trust funds, and aid for regional public goods. While budget support is the predominant instrument used by multilateral and bilateral donors, it is also the one that raises tensions the most between the interests of donors and those of the recipients. On the donor side, budget support takes away the ability to link aid directly to specific outcomes as aid is fungible with other government resources. Fungibility of budget support increases the risk of misuse and embezzlement of aid. As a result, in an attempt to minimize reputational risk and increase aid effectiveness, donors resort to stricter conditionalities. The risks associated with budget support also explain the higher preference for project aid by donors. On the recipient side, budget support is a preferred instrument as it enables alignment of aid with the national development agenda. Moreover, budget support implies lower cost of aid management and donor coordination compared to project aid. In the case of post-conflict countries, the tensions surrounding budget support are exacerbated by the structural and institutional challenges faced by these countries. In particular, administrative and technical capacity is generally weak following conflicts, and institutions are of poor quality in all dimensions. Yet, competent institutions and technical capacity are vital conditions for effectiveness of budget support.

The second set of instruments includes trust funds and other pooled funds or basket fund arrangements. These instruments have potential advantages, including—at least in principle—providing a vehicle for pooling resources from multiple donors in support of a particular cause, facilitating aid coordination, and providing increased space for control of the post-reconstruction agenda by the recipient (Barakat, 2009). These instruments also allow leveraging of managerial expertise of agencies and specialized development financing institutions such as major development banks in the implementation of aid funded projects. By facilitating the pooling of funds, trust funds increase the long-term sustainability of external financing. However, the success of these instruments in post-conflict countries has been quite limited. Trust funds and basket-fund instruments in general take away the ability of individual donors to influence directly the allocation and utilization of funds. Thus, they are less appealing for donors than direct project funding. This bias against multi-donor trust funds is exacerbated in the case of post-conflict countries due to institutional deficiencies, capacity shortages, and political uncertainty. These weaknesses on the recipient side combined with ineffective coordination on the donor side often result in proliferation of pooled funding instruments (Barakat, 2009; Chandy, 2011). In the case of South Sudan, for example, an OECD report attributed the proliferation of multi-donor funds to donors' unrealistic expectations about what could be delivered through these funds and the time

required to operationalize them (OECD, 2014). Such aid fragmentation severely undermines aid effectiveness.

The third set of instruments is used to support regional post-conflict reconstruction initiatives. An example is the trust fund established by the International Conference on the Great Lakes Region (ICGLR) for reconstruction in the Democratic Republic of Congo (DRC). In this case, donors' concerns may arise not only from problems inherent to the post-conflict environment in the Democratic Republic of Congo but also the DRC's relationships with its neighbors, and bilateral problems among the neighboring countries. As a result of these problems, it has been difficult to mobilize funding from the donor community, despite clear potential gains from a regional approach to post-conflict reconstruction in the DRC.

As donors seek to maximize 'value for money' in aid management, they are confronted with three fundamental risks. The first risk is the developmental risk, which is the risk of deterioration of the conditions in aid recipient countries during the implementation of donor-funded interventions. Indeed, even as donors inject more funds in a post-conflict country, the political and economic situation may deteriorate due to factors that aid has not addressed and cannot address. The second risk is project risk, which is the risk of failure to meet the project's objectives. This risk is higher in the post-conflict setting due to the difficult environment that undermines project implementation. For example, weak capacity in project implementation units causes delays that undermine aid effectiveness. The third risk is institutional risk or reputational risk, which is the risk of damage to the donor's standing and integrity in the event of failure of an intervention. In the post-conflict setting these risks are higher than in stable countries. As a result of these risks, despite evidence of high financing needs in post-conflict countries, and despite substantial agreement among donors on the need to support post-conflict reconstruction, actual delivery of aid often falls short of expectations.

Effectiveness of foreign assistance in post-conflict countries requires making the design, implementation and evaluation of donor intervention *conflict sensitive*. This requires substantial innovations relative to standard practice in aid delivery. In particular, there is a need to consider key factors and objectives that are either specific to post-conflict countries or are more prominent in post-conflict countries than in other aid recipients. These include (1) explicit consideration of peace and state building as well as conflict prevention as central objectives in aid interventions; (2) taking into account the distribution of the benefits from aid across political, social and regional entities, with particular attention to groups that were actively involved in conflict; (3) systematic awareness of capacity constraints in post-conflict countries; (4) focusing on a limited number of objectives and properly sequencing aid delivery to achieve maximum impact.

Setting priorities in post-conflict countries is particularly challenging as these countries face myriads of needs, where each one appearing to be urgent. The setting of priorities and the sequencing of aid are closely related; and the link is more pertinent in post-conflict countries. In

these countries, the primary objective is to consolidate peace and minimize the risk of re-occurrence of conflict. Unless the bases of peace are consolidated, any success along economic dimensions may be wiped out in the event of new conflicts. Therefore, in the immediate post-war period, aid must be geared to support the establishment of institutions that foster power sharing in the political process and in the security system as a means of ensuring integration and representation of all segments of the population. Emphasis must be on correcting past practices of exclusion and discrimination that may have been the root causes of the conflicts. At the same time, delivery on the economic front is also essential for consolidating peace. The resumption of public service delivery and the creation of employment and income generating opportunities constitute the ultimate peace dividend that the population expects to get from the end of the war. When such expectations are not fulfilled, there is a high risk of conflict recurrence. Thus aid delivery strategies in post-conflict countries must consider peace consolidation and economic reconstruction as interlinked objectives.

3. Does aid work in post-conflict countries?

There is a long-standing debate in the literature on effectiveness of aid in yielding tangible outcomes in terms of economic and social development. In one strand of the literature, there is strong support for a positive effect of aid on economic growth (see Ndikumana (2012) for a survey of the literature). Under this view, low volumes of aid are partly to blame for sluggish growth; hence the call for a ‘big push’ or scaling up of aid disbursements to accelerate economic development (Sachs, 2005; Sachs et al., 2004). In another influential strand of the literature, it is argued that aid yields positive results only in well-governed countries (Burnside and Dollar, 2000; Collier and Dollar, 2001; Collier and Dollar, 2004). This view has substantially influenced the debate on aid in fragile states and post-conflict countries throughout the 2000s. In 2002, the World Bank’s Task Force on low income countries under stress (LICUS, the precursor of the ‘fragile states’ classification) concluded that ‘aid does not work well in these (fragile) environments because governments lack the capacity or the inclination to use finance effectively for poverty reduction’ (World Bank, 2002, p. 1). This view generated substantial donor bias against aid to post-conflict countries and fragile states.

The economic argument against aid to post-conflict countries and fragile states is based on the premise that the gains from aid arise from alleviating market failures, especially through the provision of public goods. Post-conflict countries and fragile states face government failures which are adverse consequences of government action or inaction rather than market failures. These failures, so the argument goes, cannot be addressed by injection of foreign aid. The implication is that donors are better off focusing on countries which combine demonstrated high needs and good governance. Indeed, since the 1990s, there was evidence that donors tended to focus on stable low-income countries where they felt ‘comfortable working’ and where they had ‘established significant experience’ (Chandy, 2011, p. 3).

Aid to post-conflict countries is therefore faced with a long standing tension between the two key criteria for aid allocation, namely development needs and good governance. Because of this tension, post-conflict countries and fragile states are found on the losing end. While they have high demonstrated needs, they also are typically characterized by poor governance and weak institutions. Thus, in a framework where good governance is considered as a prerequisite for aid allocation, naturally post-conflict countries and fragile states are at a severe disadvantage.

Further empirical investigation and field evidence, however, have demonstrated that the arguments against aid to post-conflict and fragile states rest on weak conceptual and empirical grounds. Technically the results in studies that inspired this view were found to be not statistically robust, hence not reliable (Easterly, 2003; Easterly et al., 2003). From a practical perspective, there is substantial evidence of positive effects of aid in some of the most difficult environments including in fragile states and post-conflict countries. In fact the World Bank's independent internal evaluation reports have demonstrated that the ratings of aid-funded projects in fragile states and post-conflict countries compare reasonably well with those in stable countries. The 2001 evaluation report found that 'Bank-supported project outcome ratings in fragile and conflict-affected states do not show significantly worse ratings than in other countries' (World Bank, 2011a, p. xx).

What the evidence demonstrates, however, is that for aid to be effective in difficult environments such as in fragile and post-conflict countries, donors have to be innovative to adapt their approaches to local conditions (Chandy and Linn, 2011; Manor, 2007). As Chandy points out, 'aid is capable of achieving excellent results in fragile states when it is appropriately targeted, designed, and delivered. Successful aid in fragile states requires moving away from a stable-country analysis and approach to address different kinds of development challenges and to establish alternative forms of partnership with recipient countries' (Chandy, 2011, p. 5). In practice, however, operating in post-conflict countries requires managing difficult trade-offs. In these environments, it is difficult to guarantee financial efficiency and soundness in the management of aid, and economic outcomes are typically lower than in stable countries. But second best outcomes along economic lines may be acceptable and losses of economic efficiency may be the price to pay to preserve and consolidate peace. In other words, in the case of post-conflict countries, it may be necessary to shift the weight must shift in favor of institutional and peace outcomes relative to economic effectiveness.

To increase the effectiveness of foreign aid in the difficult environments prevailing in fragile states and post-conflict countries, donors have sought to focus their interventions rather than attempting to do everything. The idea is to find 'the right focus' in aid allocation (Chandy, 2011; World Bank, 2011a). Inspired by the 2011 *World Development Report*, donors have emphasized the need to focus aid effectively, especially targeting sectors that contribute to strengthening the core functions of the state and improving citizen-to-state trust. The core functions of the state include security, law and order, public service delivery, resource mobilization and public

infrastructure. The rationale for this approach is that success in state building is a foundation for success in other development efforts. While ‘the right focus’ view has a strong conceptual foundation, its operationalization can prove challenging in fragile states and post-conflict countries. First, the notion of focus implies a hierarchy of objectives and needs, which is difficult to establish in countries facing myriad needs, many of which appear to be priorities. Second, the ‘right focus’ approach implies sequencing of aid delivery and policy interventions, with the view that success in the early stages facilitates success in subsequent ones. The challenge is that governments may not have the luxury of relegating particular needs to the back burner, and often have instead to keep many balls in the air while putting down many fires at once. Thus, ‘the right focus’ approach may be difficult to sustain politically.

Micro level evidence suggests that successful donor interventions in post-conflict countries and fragile states have either built on existing local institutional strengths or found ways to skillfully circumvent local institutional deficiencies. An example of the first scenario is the program funded by Save the Children Norway in Ethiopia, the Alternative Basic Education for Children out of School (ABEC) which leverages the organizational sophistication of local administration, enabling to build domestic support and ensure sustainability (Baird, 2010; NORAD, 2004). An example of the second scenario is the provision of health services in the rural sector in Afghanistan through NGOs and private actors. A key to the success of the program was the use of ‘a bidding process that results in signed, time-limited performance-based partnership agreements’ (Chandy, 2011, p. 12). The evidence clearly showed that the quality and scope of service delivery exceeded expectations.

An important limitation of the empirical literature on aid effectiveness is that it has focused on growth as the primary and ultimate objective of international assistance. Thus, aid is assessed as effective if it stimulates growth acceleration. In the case of post-conflict countries, the criteria for aid effectiveness need to be adapted and expanded to include peace consolidation and state building. Post-conflict countries may grow slowly while making progress in establishing power-sharing institutional arrangements that preserve peace in the long run. Aid that supports such successful institutional reforms and state building should be assessed as effective. This means that empirical frameworks and tools used to assess aid effectiveness in post-conflict countries need to be expanded and fine-tuned to incorporate peace building, institutional reforms, and state building goals in addition to macroeconomic performance goals, while also paying attention to both short-run and long-run goals.

4. Aid and state building

The main argument advanced in this paper is that successful peace consolidation and achievement of sustainable development in post-conflict countries is contingent on success in building a capable state. Thus, aid will be effective if it contributes to the goal of state building.

This section provides the rationale for this argument and discusses the challenges associated with state building.

Why focus on state building in post-conflict countries?

The ultimate objective of international assistance to developing countries in general, and post-conflict countries in particular, is to help accelerate economic development. This is an ambitious objective in general, and it is more so in the case of post-conflict countries. In the case of post-conflict countries, success in economic development is contingent on success in establishing an institutional environment that consolidates peace and social cohesion, and minimizes the risk of recurrence of conflicts. As a result, the objectives of economic development and peace consolidation are closely interdependent in these countries.

Economic development in post-conflict countries therefore involves not just the resumption of growth and wealth accumulation, but fundamental transformation of key features of society that require sustained institutional engineering and adaptation to shocks and change. The question is what role aid plays or can play in achieving these objectives. A helpful definition of economic development that fits our question, i.e., the role of aid in post-conflict countries is provided by Pritchett et al. (2012, p. 2) who consider economic development as ‘a cumulative historical process whereby economies grow through enhanced productivity, prevailing political systems represent the aggregate preferences of citizens, rights and opportunities are extended to all social groups, and organizations function according to meritocratic standards and professional norms.’ Seen through these lenses, economic development involves progress in a nation’s capacity to manage its economy, polity, society, and public administration. This is what Pritchett et al. (2012, p. 2) refer to as the fourfold transformation of the state’s *functional capacity*. This view of economic development reveals the centrality of the role of the state. Specifically, economic development requires strengthening the capabilities of the state to manage state-societies relations and to improve the functioning of markets and production systems.

The increased awareness, or rather, the resurgence of attention to the role of the state and institutions, which some have branded as ‘a new development paradigm’ (Gisselquist, 2014; Marquette and Beswick, 2011; Rocha Menocal, 2011), is a result of a number of developments in the academic literature, the development assistance profession and global geopolitics over the past decades. In the academic literature, as indicated earlier some have argued that aid is effective only in countries with good policies and institutions (Burnside and Dollar, 2000). But policies and institutions are not exogenous. They are influenced by many factors, including foreign aid. An important question is therefore whether aid can help strengthen institutions and improve the capacity of the state to design and implement ‘good policies’, whatever those may be, thus enabling improved overall economic performance. This implies that the question about aid to post-conflict countries is not just about the volume of aid but about the role of aid in helping to foster an institutional environment that is conducive for economic development.

In the development assistance profession, the search for improved aid effectiveness has enhanced the attention to the role of institutions and state capacity. Moving beyond conventional conditionalities, contemporary development frameworks prescribe directly or indirectly to foreign aid a role in strengthening state capacity. For example, under the Paris Declaration, donors committed to use national systems in aid delivery rather than going around them as donors may be tempted to do in countries with weak institutions. Thus, donors committed to invest in strengthening national policy frameworks and project implementation systems (e.g., public procurement systems, monitoring and evaluation systems). In the case of post-conflict countries, national systems are particularly weak, which is a constraint to aid delivery. It is therefore in the interest of donors to invest in strengthening the capacity of the state and institutions in these countries if they seek to maximize aid effectiveness.

The interest in building state capacity also derives from international interest in advancing global security (Benthuisen, 2015). Endemic political instability in weak and failed states provides potential breeding ground for negative forces including terrorist movements. Thus, using foreign aid to assist post-conflict countries in consolidating the capacity of the state can help achieve global security objectives.

From a conceptual perspective, there seems to be ample agreement on what state building and institution-building entail in countries facing conflict or emerging from conflict. While there may be variations in the formulation of the process, state building generally involves ‘strengthening the capacity, legitimacy, and authority of the state’ (Gisselquist, 2014, p. 10). From a practical perspective, however, there is less clarity on exactly what a capable state means, and how to achieve and consolidate the legitimacy and authority of the state, especially in countries facing or emerging from conflict. Thus, the process of state building in post-conflict countries faces several risks and challenges. One important risk is conflation of the functions of the state and institutions with their form. Obviously what matters are the functions of the institutions, not their form. The problem is that there are no blueprints or ‘best practices’ to guide the choice and establishment of the right state institutions and capabilities. Yet, in practice, post-conflict countries are constantly advised, if not forced, to establish specific types of institutions and frameworks that are deemed to be the recipe for moving onto a path of political stability and sustainable economic development. So post-conflict countries are urged to democratize, liberalize, decentralize, privatize, etc.; that is, establish the ‘good governance’ mechanisms that arguably have enabled other countries to reach higher levels of development. To satisfy donor demands and secure funding, governments of post-conflict countries must go along and embark on reforms aimed at establishing proforma institutions or presumed global ‘best practices’, a process that some have referred to as ‘institutional monocropping’ (Evans, 2004). But such reforms and institutions often fail to yield the expected outcomes because they are not adapted to local circumstances, compounded by the fact that the state lacks the capacity to implement reforms. There is therefore a risk that state building and institutional reforms degenerate into ‘isomorphic mimicry’, a low-equilibrium situation characterized by ‘the ability of organizations

to sustain legitimacy through the imitation of the forms of modern institutions but without functionality' (Pritchett et al., 2012).

State building in post-conflict countries is bound to be a long process, where progress is potentially mixed with backsliding along the way. Some post-conflict countries may be caught in a 'state capability trap' (Pritchett et al., 2012, p. 8), a long cyclical process that can take many generations before they can achieve superior levels of state capacity (also see World Bank (2011b)). Simulations by Pritchett et al. (2012) suggest that for many developing countries, it would take centuries to reach the level of state capacity enjoyed by Singapore today. For many developing countries, it would take forever to achieve Singapore's level of bureaucratic efficiency. Post-conflict countries feature prominently on the top of the list, including Afghanistan, Haiti, Cambodia, Sierra Leone, the Democratic Republic of Congo, to name just a few.

Given the complexity of institutional change in post-conflict countries, it may be more prudent to limit ambition in setting aid targets with regard to state building. In other words, 'Small Development' rather than 'Big Development' (Pritchett et al., 2012) may be a more realistic goal for foreign aid with regard to its contribution to state building. Specifically, aid may be more effective if it is targeted to achieve localized successes rather than grand institutional development schemes. Localized successes may be more adapted to state capability, and most importantly, they are likely to be more sustainable after the withdrawal of foreign aid. Moreover, strengthening some specific core functions of the state will help achieve other objectives in institutional reforms. The remainder of this section focuses on one case of localized intervention of foreign aid to promote state building, namely the role of aid in improving domestic resource mobilization through the strengthening of state capacity to mobilize government revenue.

Building state capabilities: the case of government revenue mobilization

Government revenue mobilization is one of the core functions of the state and it is a critical dimension of state building in post-conflict reconstruction. While developing countries in general face substantial constraints in mobilizing government revenue, the problem is more pronounced in the case of post-conflict countries as a result of the combination of the deterioration of the functionality of the tax system and the shrinking of the tax base that follow the collapse of economic activity during conflict.

The reform of the tax system and improvement in tax collection are critical for the consolidation of the state, peacebuilding and political stability for two key reasons. First, the ability to mobilize tax revenue is a key prerequisite for establishing state legitimacy. It is a demonstration of competence on the part of the state as well as evidence of buy-in on the part of the population with regard to the national development agenda. Effectiveness in tax mobilization is a function of tax compliance, and the latter in turn is a function of effectiveness of service delivery,

government accountability and low corruption, all of which are important attributes of a capable state.

Second, strong performance in tax mobilization enables the government to deliver public services while limiting its dependence on foreign aid. Thus, effective tax mobilization helps to consolidate the state-to-society contract, which consolidates state legitimacy. Third, effective revenue mobilization helps to expand fiscal policy space, which is key to the government's ability to own the national development agenda. Therefore, effective tax mobilization can serve as a powerful indicator of progress in state building in post-conflict settings.

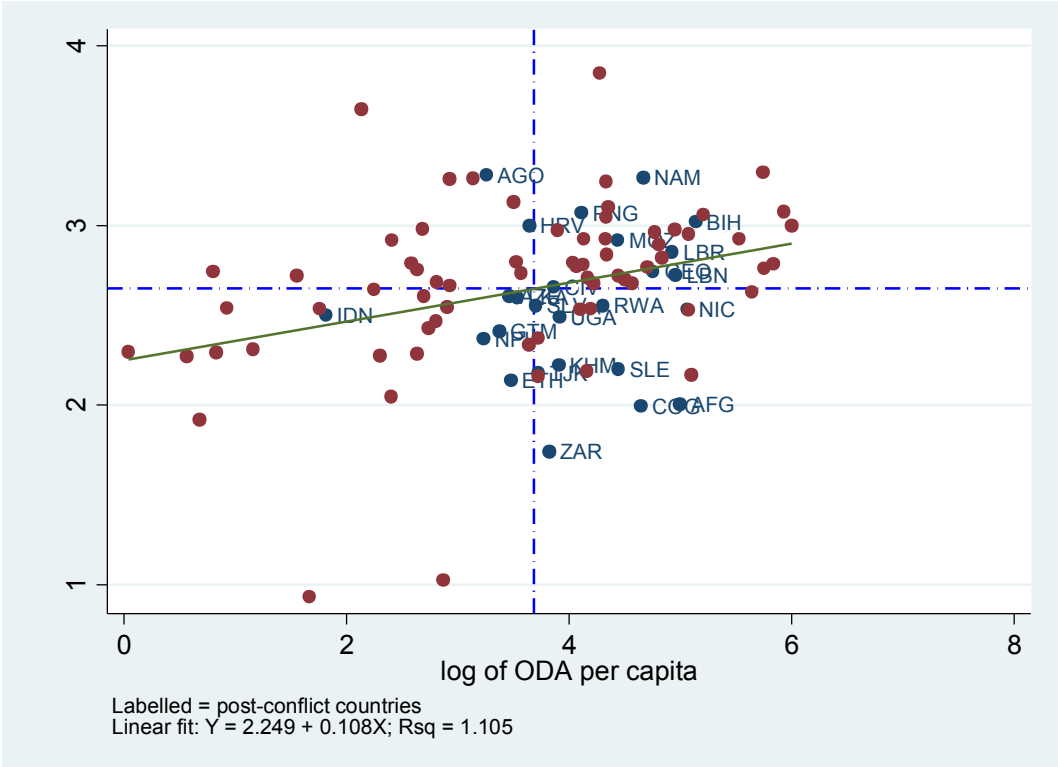
Targeted foreign aid can help build the capacity of the state to mobilize tax revenue by supporting reforms of tax administration and through technical capacity building. A good example of 'localized success' is the case of aid-funded establishment of autonomous tax authorities in post-conflict countries. In the case of Uganda, for example, the Uganda Revenue Authority was established in 1991 at a critical juncture in post-conflict reconstruction where the economy needed a boost to sustain the positive momentum (Ndikumana and Nannyonjo, 2007). The reforms were accompanied by increased tax revenue resulting from enhanced effectiveness and broadening of the tax base. The reforms also helped to offset negative effects of trade liberalization on government revenue increasing domestic tax revenue collection. For example, income tax increased from less than one percent of total revenue before 1990 to 14.1% in 1996-97 and 22.5% in 2003-04 (Ndikumana and Nannyonjo, 2007, p. 31). Today Uganda's tax incidence remains relatively low, indicating persistent inefficiencies and untapped tax opportunities. Note, however, that like for any other institutional reforms, the establishment of autonomous tax authorities is not a panacea. Accompanying measures and improvement in overall economic conditions matter a great deal for the success of tax reforms.

There remains a great deal of debate in the economic literature with regard to the overall impact of foreign aid on tax mobilization. The empirical question is whether foreign aid crowds-in or crowds-out tax revenue mobilization. On the one hand, foreign aid may crowd-out tax revenue by reducing the incentives on the part of the government to increase taxation which is both technically demanding and politically costly. Crowding-out effects may also arise from tax exoneration of aid-funded activities, especially given the high presence of the international assistance community. On the other hand, foreign aid may crowd-in tax revenue through its positive impact on the efficiency of the tax system and its effects on the tax base through the multiplier effects of aid-funded expenditures.

There is no empirical evidence on the potential crowding-out effects of aid on tax revenue (Alonso and Garcimartín, 2011; Clist and Morrissey, 2011). At the same time, evidence on the crowding-in effects is also lacking. In the case of post-conflict countries, there is no systematic relationship between tax revenue mobilization and foreign aid. The data exhibits wide cross-country variations in this group of countries as in all developing countries. Figure 1 plots the

average tax to GDP ratio against average aid per capita for all developing countries over the 2000-13 period. The data shows a positive but weak correlation between the tax to GDP ratio and aid per capita. Post-conflict countries are as likely as other developing countries to be below the regression line; that is, having high aid per capita but with tax incidence below potential. The cross-country variations illustrate disparities in local policies, institutional capacity, and differences in the structure of the domestic economy. While there is no conclusive evidence on the aid-tax relationship, at the very least, we can conclude that aid does not systematically crowd-out tax revenue mobilization in post-conflict countries.

Figure 1: Tax/GDP and aid per capita, 2000-2013



Source: World Bank, World Development Indicators (online).

While the discussion in this section has focused on tax revenue mobilization, the capacity to mobilize non-tax revenue is also important, especially in the case of post-conflict countries that are endowed in natural resources. Thus far these countries have not been able to harness their resource endowment, in major part due to weak capacity of the state to manage the natural resource sector. International assistance can help in building technical expertise to negotiate beneficial rent sharing arrangements with resource exploitation corporations and to design revenue utilization strategies to maximize the gains in terms of growth, economic transformation and social development. Increased allocation of aid in this area will enhance overall aid effectiveness over time and help resource rich countries to graduate from aid dependence.

5. Aid flows to post-conflict countries

This section offers an overview of evidence on aid allocation to post-conflict countries, with a view to assess whether such allocation helps achieve the goals of peace consolidation and state building which, as this paper argues, are central to the success of the post-conflict reconstruction agenda. The analysis of the data focuses on the five-year period following the end of hostilities, either through signing of a peace agreement or victory by one side to the conflict. The post-conflict period is compared to the pre-conflict period and the conflict period. Post-conflict countries as a group are also compared to the group of fragile states. The list of post-conflict countries is obtained from the UNDP 2008 report (UNDP, 2008), while the list of fragile states is drawn from the OECD 2014 report on fragile states (OECD, 2014). The aggregate data is obtained directly from the World Bank's World Development Indicators while the disaggregated data by sector is compiled using data from the Country Reporting System of the OECD/DAC. For consistency, cross-country comparisons are based on aid per capita converted into real values using the US GDP deflator considering 2013 as base year. This is important given that the conflict and post-conflict periods happen at different times across countries.

The first question is whether donors scale up financial assistance to countries following the end of hostilities. Increased aid could be motivated by the wish to use economic reconstruction as a foundation for peace building. As can be seen in Table 1, post-conflict countries have received substantially higher volumes of aid during the five-year period following the end of hostilities than during conflicts. However, ten out of the 34 post-conflict countries with complete data experienced a decline in aid per capita during the 5-year post-conflict period compared to the conflict period. Note, however, that as these are simple averages, the results may be driven by outliers. For example, in the case of Rwanda, the high average aid per capita during conflict is driven by the massive inflow of humanitarian aid in 1994 after the genocide. Naturally, given the vast heterogeneity across the group of post-conflict countries, the volume of aid also varies substantially across the sample. Among the top 20 countries, the volume of aid ranges from \$51 per person in Haiti to \$462 in Solomon Islands. Half of the top 20 recipient countries are in Africa.

Table 1: Aid per capita (constant 2013 \$): pre-conflict, conflict, post-conflict period

Country	during conflict	5-year post-conflict	% change From conflict to post-conflict
Afghanistan	21.2	201.9	853.5
Angola	27.2	36.1	32.8
Azerbaijan	8.7	24.1	177.6
Bosnia and Herzegovina	145.7	344.3	136.4
Burundi	40.2	54.9	36.5
Cambodia	30.2	48.7	61.2
Chad	50.7	48.2	-4.8
Congo, Dem. Rep.	4.9	57.9	1083.4
Congo, Rep.	109.3	26.0	-76.2
Cote d'Ivoire	36.7	41.4	12.8
Croatia	n.a.	23.1	n.a.
El Salvador	105.5	87.8	-16.8
Eritrea	3.3	44.3	1231.1
Ethiopia	21.5	26.6	23.9
Georgia	22.7	73.0	222.0
Guatemala	28.6	31.3	9.7
Guinea-Bissau	81.3	80.2	-1.4
Haiti	65.1	51.6	-20.7
Indonesia	10.4	4.5	-56.5
Lebanon	132.3	80.3	-39.3
Liberia	58.1	166.1	185.7
Mozambique	63.4	94.9	49.7
Namibia	26.6	148.2	457.4
Nepal	22.1	30.8	39.7
Nicaragua	87.6	205.0	133.9
Papua New Guinea	128.5	71.9	-44.0
Rwanda	83.2	60.1	-27.8
Sierra Leone	60.5	88.9	47.0
Solomon Islands	152.2	462.8	204.1
Somalia	104.2	110.3	5.8
Sri Lanka	47.6	44.2	-7.1
Sudan	37.8	43.4	14.7
Tajikistan	14.5	31.1	114.0
Timor-Leste	13.0	274.7	2019.3
Uganda	32.0	51.9	62.1
GDP-weighted average	47.2	93.1	97.1

Note: no ODA data for Kosovo

Source: World Bank, World Development Indicators (online).

One of the challenges faced by post-conflict countries and donors is the transition from financing humanitarian interventions during conflict to financing economic reconstruction and state building in the post-conflict period. In other words, they face the challenge of moving from humanitarian aid to development aid. Table 2 presents average aid per capita over the 5-year post-conflict period by key sector, namely humanitarian, productive sectors (infrastructure and agriculture), and social sectors (health, education, water and sanitation). In 14 out of the 36 post-conflict countries, humanitarian assistance accounted for the highest volume of aid per capita. The fourteen countries include those with long drawn-out wars such as Burundi, the Democratic Republic of Congo, Liberia, Sierra Leone and Sudan. In these countries, conflicts have displaced a large number of people who required extended assistance even after the end of the war.

The allocation of foreign aid by sector poses some challenges for both recipients and donors. On the one hand, following protracted conflicts, most sectors are in dire need of rebuilding and all sectors may appear as urgent priorities. The challenge is how to set priorities to meet the most urgent needs and generate the maximum returns to foreign aid. On the other hand, interventions in sectors require specialized skills that are difficult to assemble for any individual donor. So the donors face a dilemma. If they attempt to meet the seemingly urgent needs in multiple sectors, they run the risk of exposing their technical weaknesses in some areas, resulting in suboptimal outcomes. If they choose to concentrate their resources in a small number of sectors where they have the most experience and expertise, they may be perceived as not responding to the needs on the ground and instead satisfying their own preferences. There is no easy solution to this dilemma. In line with the central argument advanced in this paper, the allocation of aid needs to accord adequate importance to state building and institutional reforms that are critical to peace consolidation and prevention of conflict. Thus far, it is not evident from the data whether this consideration has been taken on board. This may partly explain the high risk of fragility observed among post-conflict countries and the overall poor quality of institutions and policies in these countries. It is clear that to achieve better results, there needs to be a paradigm shift in aid allocation strategies to prioritize state building and peace consolidation.

Table 2: ODA per capita by sector (\$) during 5-year post-conflict period

Country	Health	Education	Water	Agriculture	Infrastructure	Humanitarian
Afghanistan	7.5	8.5	1.7	10.2	22.4	20.5
Angola	2.8	2.3	1.2	0.6	0.6	7.5
Azerbaijan	0.1	0.0	0.0	0.3	0.9	0.1
Bosnia	3.5	1.9	1.1	1.3	8.8	7.8
Burundi	2.5	2.6	0.9	1.8	1.6	14.8
Cambodia	0.3	0.1	0.2	0.4	1.1	0.5
Chad	1.1	1.0	1.4	0.9	1.5	8.4
Congo, Dem. Rep.	1.6	0.8	0.3	0.4	1.4	4.5
Congo, Rep.	1.6	6.5	0.6	0.3	2.4	2.8
Côte d'Ivoire	1.4	2.0	0.5	1.9	1.0	3.1
Croatia	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
El Salvador	0.6	0.6	0.9	0.9	2.9	0.0
Eritrea	0.2	0.1	0.4	0.2	0.4	1.1
Ethiopia	0.1	0.1	0.1	0.3	0.1	0.2
Georgia	0.2	0.1		0.6	3.3	0.6
Guatemala	0.6	1.1	2.4	1.0	0.6	0.3
Guinea-Bissau	5.4	6.4	2.4	1.7	6.7	1.9
Haiti	0.5	0.5	0.5	1.1	1.9	0.1
Indonesia	0.7	1.6	0.6	1.1	2.5	0.8
Kosovo	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Lebanon	0.1	0.9	1.8	0.1	0.6	0.3
Liberia	5.3	1.8	0.4	0.9	6.4	38.3
Mozambique	0.4	0.7	0.4	1.2	2.4	0.8
Namibia	3.1	6.2	1.8	2.7	2.8	0.3
Nepal	2.6	4.5	0.7	1.2	4.6	1.9
Nicaragua	2.9	0.1	1.0	3.4	3.8	0.1
Papua New Guinea	4.7	10.1	0.7	2.5	16.4	2.3
Rwanda	0.3	0.5	0.9	0.2	0.9	2.5
Sierra Leone	4.2	2.7	1.0	0.8	4.9	13.5
Solomon Islands	32.0	23.7	1.2	10.2	22.0	7.0
Somalia	0.0	0.0	0.0	0.0	0.0	1.0
Sri Lanka	1.0	2.5	2.8	2.6	6.0	8.4
Sudan	1.8	1.1	0.3	0.3	0.1	29.8
Tajikistan	0.4	0.2	0.1	1.5	0.3	1.7
Timor-Leste	3.8	15.1	5.3	5.7	6.0	36.2
Uganda	0.4	0.1	0.6	0.3	0.7	0.1

OECD/DAC, Country Reporting System (online).

6. Conclusion

This paper has raised and discussed a number of important issues associated with aid delivery in post-conflict countries and its impact on post-conflict reconstruction. It has highlighted the difficulties faced by donors operating in challenging environments in these countries. Donors must make difficult decisions regarding the choice of instruments for aid delivery, allocation of aid, and sequencing of aid, considering the weak state capacity in these countries. The preferences and interests of donors are often at variance with those of recipient governments, creating tensions that affect delivery and effectiveness of aid. Donors also face a dilemma of selecting the sectors where to concentrate their attention and resources. In practice, getting ‘the right focus’ in aid delivery is difficult operationally and politically because post-conflict countries face myriads of needs, all of which appear as priorities. Thus, setting the goals for foreign aid is also a challenge. This paper has argued that the goals of international assistance in post-conflict countries must include peace consolidation and prevention of recurrence of conflicts as priorities. Hence, aid allocation decisions must give due attention to institutional reforms aimed at fostering power sharing among various social groups, especially those that were involved in the conflicts.

Success of the post-conflict reconstruction agenda is critically contingent on the capacity of the state to perform its core functions, notably security, law and order, resource mobilization, and provision of public services. Therefore, donor interventions in post-conflict countries need to prioritize state building as a primary objective. While all the core functions of the state are critically important, this paper has singled out the capacity of the state to mobilize domestic revenue as key to success in post-conflict reconstruction. Effectiveness in revenue mobilization enables the government to fulfil its part in the state-people contract by delivering public services, which builds state legitimacy and credibility. Moreover, having adequate revenue provides the government with the needed policy space to own the national development agenda. Therefore, to the extent that aid can help build the capacity of the state to mobilize revenue, it will have positive indirect effects on the other core functions of the state that are critical for the post-conflict reconstruction agenda. Such an approach is therefore strategically effective.

References

- Alonso, J. A. and Garcimartín, C. (2011). Does aid hinder tax efforts? More evidence. Nottingham, UK: CREDIT Research Paper 11/04.
- Baird, M. (2010). Service delivery in fragile and conflict-afflicted states. Background Paper to the World Development Report 2011. Washington, DC: The World Bank.
- Barakat, S. (2009). The failed promise of multi-donor trust funds: Aid financing as an impediment to effective state building in post-conflict contexts. *Policy Studies*, 30 (2), 107-126.

- Benthuisen, J. V. (2015). In-between anarchy and interdependence: from state death to fragile and failing states. *Third World Quarterly*, 36 (1), 22-39.
- Burnside, C. and Dollar, D. (2000). Aid, policies and growth. *American Economic Review*, 90 (4), 847-868.
- Chandy, L. (2011). Aiding stability: Improving foreign assistance in fragile states. *Global Views, Policy Brief 2011-09*.
- Chandy, L. and Linn, L. (2011). Taking development activities to scale in fragile and low capacity environments *Global Working Papers* (Vol. 41). Washington, DC: The Brookings Institution.
- Clist, P. and Morrissey, O. (2011). Aid and tax revenue: Signs of a positive effect since the 1980s. *Journal of International Development*, 23 (2), 165-180.
- Collier, P. and Dollar, D. (2001). Can the world cut poverty in half? How policy reform and effective aid can meet international development goals. *World Development*, 29 (11), 1787-1802.
- Collier, P. and Dollar, D. (2004). Development Effectiveness: What Have We Learnt? *The Economic Journal*, 114 (496), F244-271.
- Easterly, W. (2003). Can foreign aid buy growth? *Journal of Economic Perspectives*, 17 (3), 23-48.
- Easterly, W., Levine, R. and Roodman, D. (2003). New data, new doubts: A comment on Burnside and Dollar's 'Aid, Policies, and Growth' (2000). *NBER Working Papers*, 9846.
- Evans, P. (2004). Development as institutional change: the pitfalls of monocropping and the potentials of deliberation. *Studies in comparative international development*, 38 (4), 30-52.
- Gisselquist, R. M. (2014). Aid and institution-building in fragile states: What do we know? What can comparative analysis add? *The ANNALS of the American Academy of Political and Social Science*, 656 (1), 6-21.
- Manor, J. (2007). *Aid That Works: Successful Development in Fragile States*. Washington, D.C.: The World Bank.
- Marquette, H. and Beswick, D. (2011). Introduction State Building, Security and Development: state building as a new development paradigm? *Third World Quarterly*, 32 (10), 1703-1714. doi: 10.2307/41341195
- Ndikumana, L. (2012). Applying evaluation to development and aid: Can evaluation bridge the micro-macro gaps in aid effectiveness? In F. Bourguigno, M. A. Clemens, J. Mirrlees, J.-D. Naudet, L. Ndikumana, J. Nelson, C. Paradeise, R. Ruben and M. Székely (Eds.), *Evaluation and Its Discontents: Do We Learn from Experience in Development?* (pp. 123-150). Paris: Agence Française de Développement.
- Ndikumana, L. and Nannyonjo, J. (2007). From failed state to good performer? The case of Uganda. In J. K. Boyce and M. O'Donnell (Eds.), *Peace and the Public Purse: Economic Policies for Postwar Statebuilding*. Boulder, CO: Lynne Rienner.
- NORAD. (2004). Study of the Impact of the Work of Save the Children Norway in Ethiopia: Building Civil Society Evaluation (Vol. Study 6). Oslo: NORAD.
- OECD. (2014). *Fragile States 2014: Domestic Revenue Mobilisation*. Paris: OECD.
- Pritchett, L., Woolcock, M. and Andrews, M. (2012). Looking like a state: Techniques of persistent failure in state capability for implementation. *The Journal of Development Studies*, 49 (1), 1-18.

- Rocha Menocal, A. (2011). State Building for Peace: a new paradigm for international engagement in post-conflict fragile states? *Third World Quarterly*, 32 (10), 1715-1736. doi: 10.1080/01436597.2011.610567
- Sachs, J. D. (2005). *The End of Poverty, Economic Possibilities for our Time*. New York: Penguin Press.
- Sachs, J. D., McArthur, J. W., Schmidt-Traub, G., Kruk, K., Bahadur, C., Faye, M. and McCord, G. (2004). Ending Africa's poverty trap. *Brookings Papers on Economic Activity*, 1, 117-240.
- Stewart, F. and Brown, G. (2009). Fragile states. *CRISE Working Paper* (Vol. 51). Oxford: Centre for Research on Inequality, Human Security and Ethnicity.
- UNDP. (2008). *Post-Conflict Economic Recovery: Enabling Local Ingenuity*. New York: UNDP: Bureau for Crisis Prevention and Recovery.
- World Bank. (2002). *World Bank Group Work in Low-Income Countries Under Stress: A Task Force Report*. Washington, DC: World Bank.
- World Bank. (2011a). *Results and Performance of the World Bank Group 2011*. Washington, DC: The World Bank: Independent Evaluation Group.
- World Bank. (2011b). *World Development Report 2011 : Conflict, Security, and Development*. Washington DC: The World Bank.