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Blind spots on the map of aid allocations: Concentration and complementarity of international NGO aid

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Research Paper No. 2007/45

Blind Spots on the Map of Aid Allocations

Concentration and Complementarity
of International NGO Aid

Dirk-Jan Koch*

August 2007

Abstract

The budgets of development NGOs have risen dramatically over the last decades. In stark contrast to bilateral donors, the geographic choices of NGOs remain virtually unexplored. Using a new dataset and Lorenz curves, this paper shows that NGOs are very active in some countries and hardly active in others. A clustering of NGO activity takes place in UN-labelled high priority countries, but ample room for improved targeting exists. Aid concentration curves provide insight into whether NGOs target the same countries as bilateral donors. The article concludes that this is the case and that NGOs are thus acting as complements. The drawback of this complementary approach is that it reinforces the donor-darling/donor-orphan divide. The paper concludes with some research suggestions and preliminary policy implications.

Keywords: aid allocation, NGO, aid effectiveness, new geographical economics, donor darling

JEL classification: O20

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Acronyms

MDGs Millennium Development Goals

NGOs nongovernment organizations

ODA official development aid

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1 Introduction

The Central African Republic is an extremely poor, landlocked country where around three million people live below the poverty line. Similarly, Malawi is also a poor country with no access to the sea, and four million poor. One would expect these two countries to receive roughly the same volume of aid from organizations such as Care, World Vision and Plan. In reality, however, 50 of the world's largest nongovernmental (NGOs) development organizations spend only about €1 million a year in the Central African Republic, compared with more than €80 million for Malawi. This example suggests that there might be countries where aid to NGOs is sparse, and others where it is generous, which causes concentration of aid. Perhaps NGOs made this choice because official donors were focusing on the Central African Republic? To the contrary: official donors provided Malawi in excess of €480 million in 2005, compared to only €71 million to the Central African Republic.

This paper aims to answer two questions: is NGO aid heavily concentrated in some countries while leaving other countries behind? In addition, if NGO aid is concentrated, is it concentrated in countries where other actors are not active? Concentration is not necessarily a bad thing; it depends on the countries in which concentration is taking place—is it taking place in priority countries or in countries where NGOs enjoy comparative advantage? Reliable datasets on the expenditures of international development NGOs do not exist. Therefore, a new dataset was developed for this article, in which the country allocations of twenty of the world's leading international development NGOs are compiled (Appendix 2 provides an overview of the NGOs included in the sample). In addition, 21 interviews were held with key NGO decisionmakers and four with government officials of relevant ministries.

Many scholars focus on the country allocations of bilateral and multilateral donors (Burnside and Dollar 1997; Collier and Dollar 2002; Hansen and Tarp 2000). In addition, many academics research NGO aid at the subnational level, but not at the country level (e.g., Zeller et al. 2001; Bebbington 2004; Fruttero and Gauri 2005; Barr and Fafchamps 2005). There seems to be a blind spot in research when it comes to country allocations of international development NGOs, the recent work by Yontcheva and co-authors (2005 and 2006) being a notable example. The lack of academic or political debate on this subject is surprising, given that aid allocations through these agencies have risen dramatically. In 2004 at least US\$4 billion was spent by donors on NGOs (Agg 2006). The combined budget of the 100 largest development NGOs was approximately US\$12 (Koch, own calculation) in 2004-05. Yet, it is not only the financial size of NGO aid that makes it valuable as a distinctive field of research. Policy documents from the World Bank (1998) and the United Nations (2005), among others, suggest that many are of the opinion that NGO aid can be effective in a different policy environment than government-to-government aid, thereby turning the current dominant aid effectiveness paradigm ('aid is more effective in countries with good governance') at least partially upside down (Burnside and Dollar 2000).

The remainder of this article commences with a theoretical framework for analysing the concentration and dispersion in NGOs' choice of location. Thereafter, section 3 examines the background on the geographic decision process of international development NGOs. Subsequently, section 4 demonstrates how NGOs concentrate their activities, shedding light on differences between donors and different types of recipients. Section 5 shows that NGO aid is behaving more as a complement than as a

substitute to bilateral aid. Finally, drawing on the theoretical framework and the empirical analysis, the paper concludes with some policy suggestions.

2 Nonprofit location theory

Many factors influence the NGOs' choice of location. Scholars on organizational design and psychology explain country allocations by focusing on the structure of organizations (for instance, whether NGOs have existing country desks) and on the role of individuals within this structure (for instance, the personality of country officers). Others point to the historical and cultural ties between the NGOs and certain countries, and of course the political preferences of back donors. While acknowledging that these factors probably play a role, they fall beyond the scope of this article. This paper focuses on theories that deal with concentration and dispersion effects.

To understand the forces that drive the geographic decision of NGOs, the literature on nonprofit location theory provides some interesting frameworks. Nonprofit location theory is not a distinctive field within geography, which is not surprising since even the public location theory is only a few decades old (DeVerteuil 2000). Most of the time, scholars of the nonprofit theory use a supply and demand framework, with supply referring to the presence of funding and demand to the needs of the local population (Gronbjerg and Paarlberg 2001; Wolch and Geiger 1983). In this model, location choices are a tradeoff between these two forces. Weisbrod (1988) has made a famous specification of this model; he shows that demands for nonprofit organizations may be greater in heterogeneous areas, as the government fails to cater to all the disparate preferences.

2.1 Concentration

Recently scholars have applied insights from the new geographical economics to the field of nonprofit location theory, thereby shifting the focus to processes of concentration and dispersion (Bielefeld and Murdoch 2004). These insights come from the work on for-profit firms by Krugman, who explains concentration as 'pervasive increasing returns and imperfect competition, multiple equilibria everywhere and often decisive role for history, accident and perhaps sheer self-fulfilling prophecy' (Krugman 1991 and 1998). This article examines in more detail four factors that lead to concentration (centripetal forces): internal economies of scale, external economies, a thick labour market and blame-sharing effects. It subsequently discusses four factors that stimulate dispersion (centrifugal forces).

First, internal economies of scale arise when an organization achieves more of its aims by clustering its activities. As economists put it, when there are increasing returns at the organization level induced, for instance, by capital-intensive machines, this will stimulate a multinational organization to concentrate its investments. In the case of NGOs working in field offices, it is more efficient to reduce the number of countries where they are active, as they can use the overhead for additional programme officers instead of constructing facilities.

Second, external economies of scale arise when organizations can achieve a greater number of their goals when they cluster their activities. Economists show that a

decrease in average costs, for instance because of cheaper inputs, encourages organizations to locate near each other (concentrate). These concepts are often applied in business analysis (Porter 2000; Morosino 2004; Keeble et al. 1999). In nonprofit location theory, this is rare but Bielefeld and Murdoch (2004) address these effects and call them agglomeration economies. They include such factors as (i) shared infrastructure, which reduces transportation, communication and supply costs; (ii) access to a pool of labour or specialized inputs; (iii) knowledge spillovers between organizations as a result of contact between firms and people; (iv) information on the demand or feasibility of production at a particular location and (v) reduction of consumer search costs, which leads to increased demand at a particular location. In the case of international development NGOs, these effects are, for instance, visible for those that work through local partners. When one international NGO has invested time and money in the financial management systems of a local partner, it is attractive for other international NGOs to work also with this partner, instead of going to another country where partners still need to be introduced to similar western systems.

Venables (2001) analyses why economies of scale can lead to long-term division between the *core* and *periphery*. According to Venables, the combination of forward and backward linkages creates a potential process of cumulative causation: expansion of downstream activity increases demand for upstream output that attracts entry, improving the supply (price or varieties) of intermediates, attracting further downstream entry, and so on. In the international NGO scene, one can think of local consultants and evaluators. When their number increases in a particular location, more NGOs will choose to locate in that particular country, as qualified local consultants are present, leading yet to another increase in their numbers and quality. This can result in a constantly self-reinforcing pattern of location choices that can stimulate the formation of the core and the periphery (Brakman, Garretsen and van Marrewijk 2001). Most of the production takes place at the *core*, whereas the *periphery* remains largely an inactive area.

Third, the mobility of international NGO staff contributes to the agglomeration of NGOs. Labour mobility implies the flexibility of workers to move from one region to another. The factor driving people to migrate to different regions is a higher real wage. If real wages (or the quality of life) are higher in another region, a part of the labour force is likely to move. International NGO staff can be considered to be internationally mobile and to contribute to agglomeration; they move from one 'hotspot' to the next, be it Kosovo, East-Timor or Sri Lanka. The movement of labour has consequences: the labour market for personnel with particular skills expands in these agglomerations. Past and present organizational arrangements are also an important factor explaining new organizational growth, as it strengthens the organizational capacities of a population (Lincoln 1977). He finds that the strongest predictor of any one category of voluntary association is the presence of other voluntary organizations. In the case of development NGOs, it is clear that the discourse that local organizations need to master to obtain international funding, such a log frame analysis, requires training. Once local organizations master these skills, other international NGOs are more likely to fund these organizations as well, contributing to further agglomeration.

Fourth, Easterly, drawing on the agency theory, presents another argument to explain why NGOs might cluster their activities. 'Agencies handle the high risks in foreign aid by the time-honoured bureaucratic strategy of sharing blame. The bureaucracies

intermingle their outputs so evaluators don't know who to blame for bad outcomes' (Easterly 2002: 31).

2.2 Dispersion

This paper also deals with the four centrifugal forces—competition effects, dispersion of demand, reputation concerns and transport costs.

First, authors analysing the location choices of nonprofit actors recognize that the desire to avoid direct competition could induce organizations to locate away from other similar agencies (Bielefeld and Murdoch 2004; Baum and Oliver 1996). The resulting pattern in a given area would be dispersion. If one applies the theory to international development NGOs, one can see this happening. In relatively new geographic areas, it is easier to find exclusive partners as there are no competitor international NGOs.

Second, the dispersion of demand creates a centrifugal force. The majority of the impoverished, who live in poor regions and need the services of NGOs, are rather immobile and dispersed, which stimulates the dispersion of NGOs. Krugman refers to this force as the immobility of inputs.

Third, Fruttero and Gauri (2005) focus on how the concerns for reputation affect location decisions. If NGO reputation is important to donors, as it appears to be, then new and unknown NGOs might undertake risky action which, if successful, could endorse their ability. This will promote operations in regions and countries where none or few other actors are active. (Organizations that already have a good reputation, however, will prefer to remain in countries where others are active, so that if there is project failure, they will not lose their reputation, as others can be blamed.)

Fourth, high transport costs constitute a centrifugal force, as production of the good needs to be in the proximity of the end-user of the service and the end-users may be dispersed (Mayer 2004). In terms of international development NGOs, for those sectors in which tacit local knowledge, for instance, is important—such as family planning programmes (for which transport costs are high, if it can be transported at all)—NGOs would prefer to be close to the end-users, resulting in a pattern of dispersion.

Discussion of the agglomeration and dispersion effects has been a key concern for public location theorists, a realm that attempts to find a balance between equity and efficiency. For some of the reasons pointed out above, an efficient allocation tends to be one in which the facilities are located in the proximity of each other. Yet, equity concerns favour dispersion, as this increases the access of the population to services. Consequently, there are competing forces at hand. This resonates with the theoretical debates taking place within the aid allocation literature. Terminology differs, but the underlying theory is the same. One school of thought, known as the utilitarian approach, focuses on reaching the maximum number of people (e.g., Collier and Dollar 2002), whereas another school focuses on creating an approach based on equality of opportunity (Llavador and Roemer 2001; Cogneau and Naudet 2004). The former criticizes the latter for achieving too little results, whereas the latter blames the former for too great a concentration and subsequent neglect of many countries.

Table 1
Forces influencing NGO locations

Centripetal forces	Centrifugal forces
<ul style="list-style-type: none"> ▪ Internal economies of scale ▪ External economies of scale ▪ Labour mobility ▪ Blame-sharing effects 	<ul style="list-style-type: none"> ▪ Avoiding competition, increasing coverage ▪ Dispersion of demand ▪ Reputation effects ▪ High transport costs

In the literature on NGOs, there is some concern that nonprofit organizations ignore equity. Schmid (2003) argues that nongovernmental agencies can ignore equity in the delivery of services. While government agencies have to be universalistic, nonprofit agencies can be particularistic. Whereas bilateral aid has the characteristics of a public good (non-exclusionary and non-subtractable), NGO aid shares characteristics more with a toll good (exclusionary) and common pool good (non-subtractability), depending on the intervention strategy used (Ostrom and Ostrom 1999). Governments must have clear criteria for targeting, while nonprofit agencies do not need to serve all the people within their target group and can select clients according to a group characteristic, for example, the place of residence (Lipsky and Smith 1990).

The first part of this report examines the question of whether international aid NGOs display a pattern of concentration and if so, the type of countries and regions where this is taking place (section 4). Yet, it is not advisable to research NGO aid in isolation. Earlier research by Koch (2006) suggests that bilateral aid generates positive externalities that pull NGOs in the direction of countries where bilateral aid is also present. Joassart-Marcelli and Wolch (2003) also find these interaction effects and demonstrate that government support pulls NGO aid into certain regions. The second part of this report (section 5) deals with the relationship between the geographic choices of bilateral donors and NGOs.

3 Background on the country allocation processes of international development NGOs

The first question that this paper addresses is whether a process of concentration is affecting the country allocations of NGOs. To understand the basis of country allocation decisions taken by NGOs, interviews were conducted with 21 major international NGOs from Germany, Norway, the United States and the Netherlands.¹ Several reasons promoted this choice: these four countries, together with Switzerland and the United Kingdom, house the largest development NGOs; and they represent four distinct co-financing systems. The German system is clearly corporatist, the Norwegian system social-democratic, the American system liberal and the Dutch is changing rapidly from a corporatist to a liberal system.

¹ The following criteria are used for the selection of NGOs: (i) they must have an annual budget of at least €10 million; (ii) at least 50 per cent of funding needs to be development related; (iii) they need to be independent from sister organizations in their decision process on country allocations; and (iv) organizations providing mainly technical assistance are excluded. A list of the included organizations is given in Appendix 2.

The country allocation processes of these NGOs are quite distinct. Whereas the American government earmarks their funding for certain countries and thus exercises direct influence on the country allocations of its organizations, this is not the case for the NGOs from the three other countries. The governments of the Netherlands and of Germany give a block grant to the most important organizations, a fact which severely restricts, both directly and indirectly, the influence of the bilateral donor on the allocation of countries. The system in Norway lies somewhere in between; according to Norwegian organizations, the government does not influence their country allocations directly, but has some impact indirectly through discussion. Even though the American government is clearly the most prescriptive in the country allocations of its NGOs, these appear to be least affected by it, mainly because of their relative financial independence from the government (Koch, Westeneng and Ruben 2007).

The country allocation process of the NGOs is divided into two stages. First is the actual selection process of countries (what Neumayer calls the eligibility stage), and then, the actual decision allocation (level stage). There are significant differences in the manner in which organizations deal with the eligibility stage. Forty per cent of those interviewed stated that their organization had a formalized country selection process, meaning that the organization makes an official decision regarding the countries where it is active and that certain variables regarding the objectives of the NGO guide this decision. Most of these organizations undergo a country-selection exercise every 3-4 years when the NGO submits a major grant proposal to the back donor. Typically, the highest administrative level of the NGO is involved in the decisionmaking process. Many organizations start the process by selecting some relevant international poverty indicators, such as the human development index for general organizations, or child welfare indicators for agencies focussed on children. Rigid adherence to these indicators in the country selection process can lead to drastic changes in the choice of countries. Often, in addition to poverty indicators, other criteria are included, such as whether the NGO is already present in a country and how successful its programmes have been.

Also, 40 per cent of the interviewees (not necessarily the same as above) stated that their organizations had a formalized country allocation process (the level stage). Officials with agencies with no formalized country-allocation system explain that as these are donor driven, they cannot make the choice themselves, or that they had an informal system. In organizations with an allocation system, it was obvious that employees at lower administrative levels were responsible for actual country allocations. If the agency had regional desks, as most do, various regional departments were allotted predetermined shares of the total budget, which they distributed among the countries on that particular organization's 'list'. The specific share of the budget is often based on the region's previous level of funding. Some organizations, mainly those that have country offices, used a more market-oriented system and country offices submitted grant proposals to headquarters, where the best are selected.

4 Concentration

Various ways to measure concentration exist. For this research, the Gini coefficient was selected. The Gini coefficient is a measure of the inequality of distribution, defined as the ratio of the area between the Lorenz curve of distribution and the curve of uniform distribution, to the area under uniform distribution. It is a number between 0 and 1,

where 0 corresponds to perfect equality (i.e., everyone has the same income or any other measure of interest) and 1 corresponds to perfect inequality (i.e., one person has all the income while everyone else has zero income).

4.1 Data

This analysis is based on the self-reporting data of international NGOs, covering actual disbursements in fiscal year 2004. The data cover total expenditures of the organizations, including both private and public funding. Dependency on public funding is high, except for the American NGOs (Wang 2006; Koch, Westeneng and Ruben 2007).

Figure 1
Lorenz curve for NGO aid, 2004

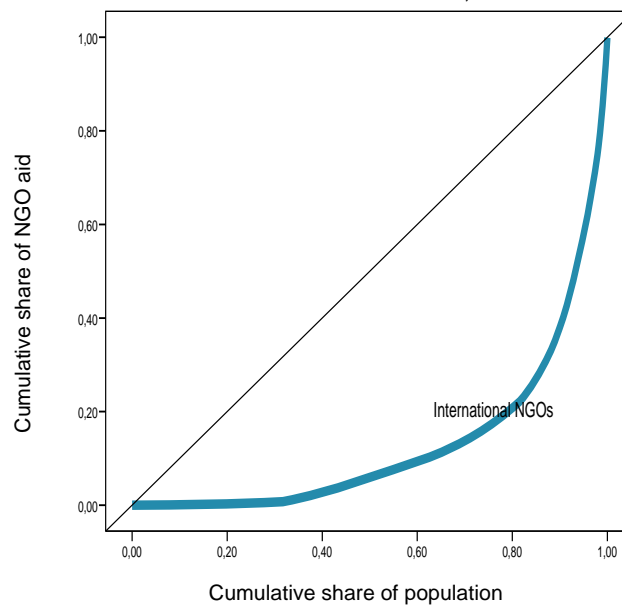
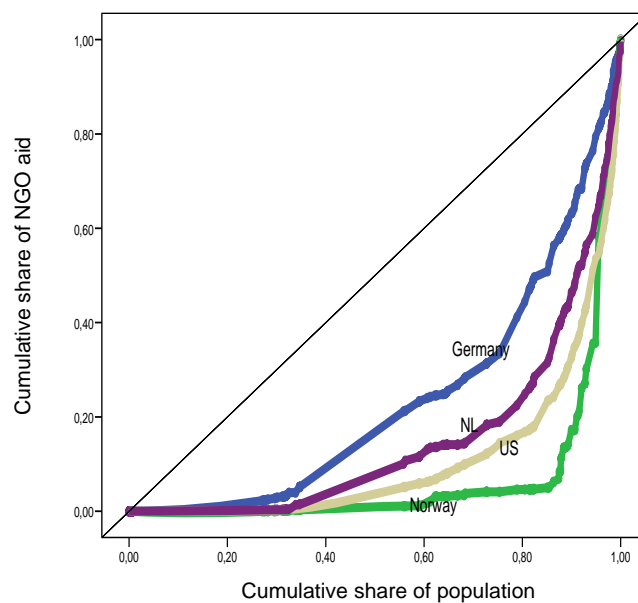


Figure 2
Lorenz curve for NGO aid per donor country, 2004



Source: Compiled by author based on data provided by NGOs.

These 22 NGOs spent €2.04 billion in DAC countries, or about €90 million per organization. This sample comprises all the countries that were included in the 2005 DAC list because aid to these recipients qualifies as official development assistance (ODA).

The Lorenz curve of total international NGO aid (Figure 1) shows that concentration is evident; 80 per cent of the people who live in DAC countries with the lowest share of NGO aid per capita receive only 20 per cent of the international NGO aid, and vice versa. Specific examples can elucidate this: Zambia, Nicaragua, Malawi and El Salvador receive more than €5 per capita of international NGO aid (from the NGOs in this sample) whereas Nigeria, the Central African Republic, India and Moldova receive less than €0.50 per capita. The Gini coefficient for total international NGO aid is 0.53, comparable to the income distribution of Latin American countries such as Mexico and El Salvador.

Figure 2 shows that there are some differences between the organizations of the four countries. Norwegian NGO aid is the most concentrated, and German aid the most dispersed. Higher levels of concentration are not necessarily a bad thing; if concentration takes place in countries that are very needy, this could be a benefit. UNDP's *Human Development Report 2003* categorizes countries into three priority levels—*non-priority*, *high priority* and *top priority*. These can be used to analyse concentration.

Table 2
NGO aid allocations according to UN priority status, back-donor and recipient regions, 2004
(in Euros per capita)

Total NGO aid per capita in recipient countries	Regions						Total
	Africa	East Asia & Pacific	Europe & Central Asia	Latin America & Caribbean	Middle East & North Africa	South Asia	
Non priority							
German NGOs	0.12	0.04	0.13	0.15	0.15	0.11	0.11
Norwegian NGOs	0.04	0.02	0.13	0.05	0.04	0.10	0.05
American NGOs	0.35	0.15	0.58	1.36	0.99	0.32	0.75
Dutch NGOs	0.12	0.02	0.15	0.96	0.15	0.12	0.39
Total	0.63	0.22	0.99	2.51	1.32	0.64	1.31
High priority							
German NGOs	0.42	0.12	0.02	0.18	0.01	0.16	0.24
Norwegian NGOs	0.24	0.12	0.00	0.03	0.00	0.02	0.13
American NGOs	1.95	0.64	0.04	0.46	0.01	0.14	1.05
Dutch NGOs	0.35	0.10	0.18	0.00	0.00	0.13	0.22
Total	2.96	0.98	0.23	0.67	0.02	0.46	1.64
Top priority							
German NGOs	0.13		0.03	0.35	0.00	.	0.13
Norwegian NGOs	0.12		0.00	0.14	0.33	.	0.12
American NGOs	1.47		2.42	4.00	1.35	.	1.58
Dutch NGOs	0.22		0.16	0.54	0.02	.	0.23
Total	1.95		2.61	5.03	1.70	.	2.07

Source: Compiled by the author based on data provided by NGOs.

Table 2 displays the average per capita allocation in euros, broken down by region, country of origin of donor organization, and by type of recipient country. The level of priority depends on two factors: the level of human poverty and the progress of these countries in achieving the Millennium Development Goals (MDGs). Thirty-one countries are classified as *top priority*, 28 as *high priority*, and the remainder as *non-priority*.

The table appears to demonstrate that NGOs in general allocate more aid to top-priority countries than the other two country groups. Caution is needed, however, as the size of the American NGOs and their focus on Latin America and the Caribbean substantially influence the results. Important differences emerge between different donors and between different regions. As the table shows, a substantial amount of NGO aid is earmarked to Latin America and the Caribbean as well as Africa, but little to South Asia or the Middle East and North Africa. A non-priority country in Latin America and the Caribbean receives many times the amount of aid per capita than high priority countries in the Middle East and North Africa or South Asia.² Looking at the NGOs, grouped by country of origin, it becomes clear that there are significant differences among them. The German and Dutch organizations do not target the priority and top-priority countries, while the American and Norwegian organizations do. In analysing targeting at the regional level, it becomes evident that targeting is rather well done in East Asia and the Pacific (countries on the priority list receive on average substantially more aid per capita than those on the non-priority list) and reasonably well in Africa. However, in Europe and Central Asia, Latin America, the Middle East and North Africa and South Asia, targeting is rather weak because high-priority countries in these regions receive less than the non-priority recipients. That said, top-priority countries receive on average most aid per capita in all regions.

Overall, the top-priority countries receive the most generous amounts of aid per capita, but there are significant differences between regions and donor countries. There appears to be considerable clustering in non-priority countries, which indicates that if the MDGs are the reference point, there are still possibilities to enhance the targeting of NGO aid. As stated, there is a multitude of factors that influence country-allocation decisions. This paper does not aim to identify all these factors; it merely attempts to establish if concentration is taking place, and if so, where.

What is also salient is the relationship between population size and per capita aid. The more populous a country, the less aid per capita it receives from the NGOs (in this sample). In countries of less than five million, inhabitants receive on average €24 annually, €10 in countries with populations of 5-20 million, about €6 in countries with 20-100 million, and one euro in nations with populations exceeding 100 million (all from NGOs). There is a negative correlation between population and NGO aid per capita of -0.33 (significant at the 1 per cent).³ This confirms earlier studies by Teune and Dietz (2003), who observe that this small country bias is already evident in the Dutch NGO allocations.

² Measured in purchasing power parity (PPP), the differences might be less, but the differences are striking.

³ To reduce skewness in the sample a logarithm was used of the population variable. Very small countries (less than 1 million inhabitants) are excluded.

In sum, NGO aid is clearly concentrated, indicating that centripetal factors are stronger than centrifugal factors. In some countries NGOs are very active, whereas in other countries they are only marginally active or not at all. Clustering does not automatically develop in high-priority countries, as non-priority countries in Latin America, for instance, receive more aid per capita than top-priority ones in the Middle East and North Africa, for example. In addition, NGOs tend to concentrate their efforts in less populous countries. Interviews with the NGOs provided some insight as to why the abovementioned pattern of country-wise aid allocation has emerged. The reason for the focus of many NGOs on high-priority countries is reflected in their response to the question: how important are the *needs* of the local population in determining allocations? This item was rated on average 4.0 out of 5. At the same time, the interviewed NGOs also made it clear that in their country-allocation process, the presence of qualified local personnel was almost as important a determinant (3.8 out of 5). The better the local personnel situation, the more funding would go to that particular country. This is consistent with the new geographical economics argument of a thick labour market and external economies of scale. New NGOs take advantage of the available human capital that had been trained by agencies already present, thus stimulating concentration.

5 NGO aid: complement or substitute?

In economic terms, a good is considered a substitute for another kind of good insofar as the two can replace each other at least in some of their possible uses. The demand for the two kinds of good will be linked by the fact that customers can substitute one good for the other when it becomes advantageous to do so.⁴ Thus, an increase in price for one type of a good results in an increased demand for its substitute, while a price drop results in less demand for its substitutes. In this section ‘demand’ refers to the government aid agencies in OECD countries. Theoretically, they have two options for distributing aid: bilateral aid (government-to-government) and through NGOs. Thus, if the ‘price’ of the bilateral aid rises (that is, in countries where aid effectiveness is low and overhead costs high), the demand for NGO aid rises. But if the ‘price’ of bilateral aid decreases in these countries, the government aid agency’s need for NGO aid decreases. A complement good is the opposite of a substitute. This means that if more of one specific good is bought, more is also purchased of its complement.⁵ If NGO aid with respect to country allocations behaves as a complement, higher levels of bilateral aid to a particular country will also induce higher NGO allocations of aid.

5.1 The substitute view

Assuming that the goal of both types of aid is poverty reduction, the comparative advantages of NGO aid and bilateral aid need to be considered in order to comprehend the substitution effect. This can provide insight into the relative ‘price’. Various authors

⁴ A standard example for substitute goods is margarine and butter. When the price of one good decreases, the demand for the other decreases.

⁵ The typical example of a complement good is hamburgers and buns; when the price of hamburgers decreases, their demand will increase, and so will the demand for buns.

have similarly concluded that NGO aid has a comparative advantage in countries with low levels of democratic governance, thus stimulating democratic governance (see Koch 2006 for an extended literature review on this topic; Steering Group 2002; Fowler and Biekart 1996; Blair in Helmich, Lehning and Bernard 1998; Edwards and Hulme 1998; DFID 2006a). In economic terms, the relative 'price' of bilateral aid is high in countries with poor democratic governance which leads to greater demand from the government aid agency for NGO aid. Conversely, in countries with high levels of democratic governance, the 'price' of bilateral aid is low. The World Bank publication *Assessing Aid* was the first to propagate that government-to-government aid should go only to countries that already had good governance. Based on statistical research, Levin and Dollar (2004) conclude that this policy selectivity started to take shape in the 1990s, when there was a clear relationship for the first time between the level of bilateral aid and the quality of governance in recipient countries. This low 'price' of bilateral aid in countries with good democratic governance theoretically should lead to less demand from government aid agencies for NGO aid in such recipients. To conceptualize NGO aid as a substitute for bilateral aid, this scenario is elaborated here for various levels of democratic governance.

In dictatorships, it is almost impossible for any type of aid actors to operate, be it bilateral or NGOs. In such cases, the government-to-government aid relationship is limited as donors are unwilling to finance dictatorships. Thus financing NGOs might be desirable from a theoretical perspective but in some cases is simply too dangerous. In countries like North Korea and Myanmar, aid to pro-democratization NGOs is certainly important, but because of its covert nature, such support is rather limited. When dictatorships enter a period of relative openness, flows to opposition movements can increase, indicating a slightly relative decrease in the price of NGO aid, leading to a relative drop in demand for bilateral aid from the government aid agency.

According to the substitute view, countries that have partially democratic governance should be the focus of NGO aid, as these are the type of countries in which it can make a difference. When bilateral and multilateral aid cannot reach the poor, NGO aid should step in. As the World Bank (1998: 104) puts it:

in highly distorted environments the government is failing to provide supportive policies and effective services. That is why government-to-government financial transfers produce poor results. Effective aid in such an environment often involves supporting civil society to pressure the government to change or to take service provision directly into its own hands (or to do both).

Dutch policy documents argue along similar lines (Netherlands Ministry of Foreign Affairs 2001a):

in cases of bad governance, bilateral aid relationships are often underdeveloped; cooperation from civil society to civil society is the only way.

An anonymous representative from the NGO department of the German Ministry of Economic Cooperation and Development states:

In fragile states we cannot work with the government, but NGOs can work on social networks and institutions. When a reasonable level of this is in place, the direct government support can take over.

The supporters of the substitute view argue that in partially democratically governed countries, there are only some agents and drivers of change that merit support. If all countries with less than total democratic governance were deprived of bi- and multilateral aid, virtually no country would qualify for this type of assistance (Hout and Koch 2006). Yet, as the high costs of monitoring aid to countries with only limited democratic governance drive up the ‘price’ of bilateral and multilateral aid, the demand for this type of aid should be less than the demand for aid to governments of countries with firmly established public accountability mechanisms.

According to the substitute view, once a country improves its level of democratic governance, the comparative advantages of government-to-government aid increase. The comparative advantages of NGOs remain strong in some sub-sectors such as democratic governance, for example, but will disappear in other sectors, such as education. Once a state becomes progressively more democratic and accountability mechanisms are in place, funds can be channelled increasingly through the government and monitoring costs reduced. If the funding level of NGOs in these policy environments remains high, they are effectively taking over the role of the state. Since the accountability structure between local and international NGOs is by definition unequal (local organizations cannot vote international aid agencies out of power), it is desirable that funding for service delivery is increasingly channelled through the government budget.⁶ A democratically-elected government could still choose to channel the funding through local NGOs. In countries with good democratic governance, NGOs can still engage in setting the political agenda by promoting, for instance, the cause of marginalized groups. It is clear that these types of activities can hardly be substituted by bilateral aid, regardless of the policy environment.

5.2 The complement view

The view of complement NGOs casts doubts on two of the main tenets of the substitute theory, namely that (i) government-to-government aid is more effective in countries with good governance than in countries without it and (ii) NGO aid can be effective in countries with poor governance. According to those advocating the complementary view, if NGOs and bilateral donors are active in the same country, synergy effects can occur which means that the total impact of aid can be more than the sum of its parts. As the Director of the Division of Effectiveness of Quality of the Netherlands Ministry of Foreign Affairs states:

In our policy dialogue with national governments of our priority countries, we can *create* space on the negotiating table for local civil society organizations. However, we cannot *fill* this space ourselves. Dutch NGOs can stimulate local organizations to make use of this

⁶ The relationship between donor and recipient government is also unequal, but recipient governments have a relative stronger position as they are a monopoly provider; costs of exit are high for the donor government.

vacuum that we create. We as a bilateral donor are good at the macro-level, civil society organizations are strong at the micro level; by working in the same countries we can effectively bridge the micro-macro gap.

According to the supporters of the complement view, government-to-government aid is not necessarily more effective in countries with better governance, but rather is dependent on the type of government-to-government aid being provided. Whereas general budget support can be provided in countries with good governance, section support and/or project support is possible in countries where only certain ministries are functioning properly, and/or in cases where governance is weak across the board, respectively.

The second assumption of NGO aid as a substitute is that these agencies can be relatively effective in countries lacking good governance. The proponents of the complement view disagree with this assumption on two accounts: the interviewed government officials argue that if NGOs were to receive significant amounts of financing but local governments not, this could lead to unaccountable parallel structures, creating an unbalanced society (DFID 2006b). NGOs point out that in countries with poor governance, it is often not possible to find good partners.

According to the complement theory, NGOs have comparative advantages, but are country neutral; that is, NGOs have a comparative advantage in building civil society, for instance, and enjoy this comparative advantage in all types of countries, be it well or badly governed. Similarly, the assumed comparative advantage of NGOs in developing innovative approaches applies to all types of countries.

5.3 Empirical evidence

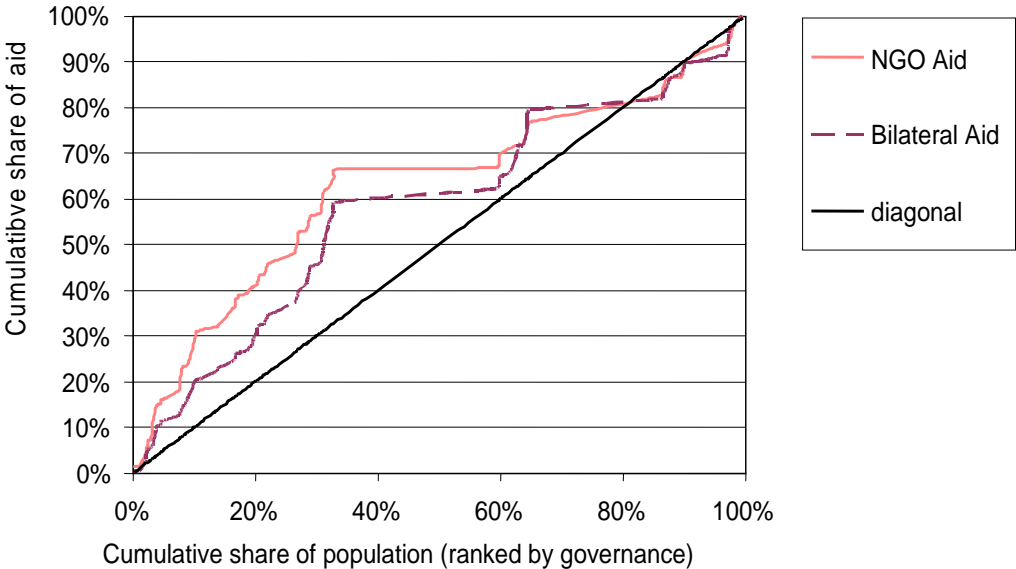
Do the NGOs behave as substitutes or as complements? Do they operate in countries where bilateral donors are active, or do they specialize in other countries? It is important to note a difference between behaving as a complement, and actual complementary behaviour. This paper examines whether NGOs and bilateral aid statistically complement each other. It makes no decision on whether this statistical complementary behaviour actually translates into synergy effects in developing countries, or whether the combination of bilateral and NGO aid leads to a decrease in the micro-macro gap. The first simple test shows that NGO aid behaves more as a complement than as a substitute. In the recipient countries, there are significant and positive correlations between total bilateral aid per capita and total NGO aid per capita of 0.725 (at 0.01 significance). Thus, higher per capita aid revenues from bilateral aid are related to higher per capita NGO revenues. An in-depth analysis shows that these results also hold for all donors individually at the same significance level.

An aid concentration curve provides a graphical means to determine whether donors target specific types of countries. The aid concentration curve plots the cumulative percentage of some measure of aid (in this case ODA and official aid in 2004 based on OECD/DAC statistics) versus the cumulative percentage of a specific population variable (in this case, the total population). The diagonal line projects the allocation if aid were provided in direct proportion to the share of world's poor living in each country. When countries on the x-axis are ranked on the basis of their level of

governance (as is done here), the aid concentration shows the extent to which a donor focuses on countries with different levels of governance. People living in poor-governance countries are on the left side of the graph, and people in countries with good governance on the right side. Countries such as Liberia are situated on the left side, while countries such as Uruguay are on the right. An aid curve above the diagonal signifies that a donor is focusing on countries with bad governance.⁷ If NGO aid is behaving as the substitute as predicted in the theoretical framework, one would expect NGO aid to be above the diagonal and bilateral aid below, reflecting the assumed comparative advantages of bilateral donors in countries with relative good levels of governance and those of NGOs in countries where this is absent. In this figure, countries are represented by lines: flat lines are the populous countries that receive relatively small amounts of aid per capita, such as Nigeria, India and China.

As this figure shows, the lines are above the diagonal, indicating that both aid channels spend more aid per capita in countries with rather poor governance. For instance, 66 per cent of NGO aid and 60 per cent of bilateral aid go to the 40 per cent of the population living in developing countries with the worst governance record. Because of the correlation between the level of economic development and governance, the apparent focus on countries with low levels of democratic governance could also be a reflection of an emphasis on the poorest countries. Either way, Figure 3 makes it clear that there is little difference in the ‘governance targeting’ of the two channels. The figure suggests that aid targeted through the different channels operates more as a complement good (as explained, not necessarily working in a complementary way) than as a substitute good.

Figure 3
Concentration curves of bilateral and NGO aid
ranked by governance situation in recipient countries, 2004



Source: Compiled by author, based on data provided by the NGOs.

⁷ In this case, governance is measured by the factor score of the six Kaufmann indicators on governance in 2004: (i) voice and accountability; (ii) government effectiveness; (iii) control or corruption, (iv) regulatory quality, (v) rule of law and (vi) political stability. Gross national income per capita (PPP average 1995-2004). The sample consists of all DAC countries (2005 list) for which governance data exist.

The statistical representation of this aid concentration curve is the Suits index⁸ (Baulch 2003). It can vary between -1 and +1, and an index of -1 corresponds to the situation in which a donor gives all its aid to the country on the left side of the figure (in this case, the worst governed country, Somalia). A Suits index of +1 implies that a donor gives all its aid to countries on the right side (in this case, Chile, the best-governed country in the sample), while 0 represents the situation in which a donor distributes its aid in exact proportion to the number of poor people, with no reference to the level of governance of the countries.⁹ The Suits index is -0.24 for NGO aid and -0.15 for bilateral aid. NGOs focus their aid marginally more on countries with poor governance.¹⁰ Nevertheless, the similarities are more pronounced than the differences. Both channels on average allocate more aid per capita in countries with the lowest levels of governance. China and India, the two flat areas, receive the least, confirming the small country bias.

Thus, taking into consideration both the positive correlation between NGO and bilateral aid, and the similar pattern of the concentration curves (ranked by governance), it would appear that NGO and bilateral aid do not act as substitutes. In fact, it may be quite to the contrary; countries that receive more aid per capita from bilateral donors also receive more aid per capita from NGOs, which suggests that the two sources of aid behave as complements. Thus, the suggestion from the World Bank, among others, about a country-wise division of labour between NGOs and bilateral donors is not confirmed. NGOs tend to follow the priorities of their donor countries, or put differently, they appear to operate in the slipstream of their back donors. Why is this?

5.4 Discussion

Interviews with nongovernment organizations indicate that in the discussion of comparative advantages, and how these influence their country allocations, NGOs often refer to the comparative advantage of their specific organizations versus that of other agencies, instead of the comparative advantages of the NGO sector versus other types of donors. This makes it clear that considerations of comparative advantage between different aid delivery channels—which is what the substitute view is all about—are probably unimportant to NGOs in decisions regarding country allocation.

Two contradictory theories exist to explain why NGOs choose to operate in the same countries as their back donors. A bleak theory, offered by the neoinstitutionalists, predicts that when nonprofit organizations are subject to external scrutiny and regulation, they gravitate to isomorphic transformation (Frumkin 1998: 22). This homogenization occurs as the nonprofit sector adapts practices because of perceived expectations of public authorities. NGOs, replying more on the government, will concentrate on the priority areas of the government. Although most NGOs are independent to choose their sphere of operations, and claim that the government has no

⁸ The Suits index is calculated as follows = $1 - \sum p_i (CA_i + CA_{i-1})$, with p_i being the share of the number of poor people in country i and CA_i the cumulative aid share of country i and all poorer countries.

⁹ Note the difference with the GINI coefficient, which measures the level of concentration regardless of country characteristics and which has a value between 0 and 1.

¹⁰ Iraq is excluded as an outlier because so much American bilateral aid went there in 2004. Its inclusion would nullify the slightly stronger focus of NGOs on poorly governed countries.

direct or indirect impact on country allocations, more subtle processes may be at play. Interviews with NGOs indicate that these would like to have visibility vis-à-vis their government's representation abroad. For example, if a back donor has an embassy or an office in Cameroon, the NGO may prefer to fund projects there instead of the Central African Republic, for instance, where there is no donor government representation.

According to a more positive explanation, NGOs believe that they can be more effective if they complement the efforts of their bilateral donor and thus adjust their country allocations accordingly. This study does not identify which factors determine complementary behaviour. What it does attempt to do is to map the consequences of the apparent predominance of the complementary behaviour. Does the absence of a division of labour between NGOs and bilateral donors in terms of country allocations contribute to the donor darling/donor orphan divide? A cross-sectional analysis shows that it probably does, because some countries receive considerable aid amounts while others receive virtually nothing (see Appendix 1 for an overview).

Before offering recommendations, some deficiencies of the current data and research method need to be made explicit. Even though a large number of NGOs consented to interviews and provided data, there may be some data bias. NGOs from only four countries are included in the sample, and agencies from countries such as France and the United Kingdom are missing. Except for colonial ties, which work in different directions for these countries, there is no reason to believe that French or British NGOs would behave fundamentally different from the sample country NGOs. However, only research with data from the excluded NGOs can validate this assumption. Another caveat that merits mention is the possibility of reverse causality. The current research method does not deal with causality. It may also be possible that a bilateral donor operates in the slipstream of the NGO, rather than vice versa. When NGOs operate in a certain country, they act as a constituency and lobby for the back donor to assume the role of bilateral donor there. A panel analysis could shed more light on which effect dominates the relationship between bilateral and NGO aid allocations. Yet irrespective of who influences whom, the result is the same: NGOs are active in the same types of countries as bilateral donors.

6 Conclusions and implications

The first conclusion of this research is that there is a high level of concentration in the international NGO aid sector: certain countries receive significant amounts of aid, others relatively little. Second, NGOs behave more as complements rather than substitutes to bilateral aid: NGOs tend to spend their resources in countries where bilateral donors are also active. These conclusions introduce new research questions: does this concentration lead to the self-reinforcing clusters of NGOs, as can be seen in the for-profit sector? Does this concentration take place because of competitive pressure for funding? Would it be beneficial for NGOs and bilateral aid to act more as a substitute, or is the current state of affairs satisfactory? With regard to the last question, even though there are theoretically clear merits to the complementary approach, this study indicates that there are potential drawbacks as well. As identified here, the main drawback of behaving as a complement is that it can increase the donor darling/donor orphan divide. The study has shown that countries such as Nigeria, Guinea-Bissau, Togo, India, Moldova and Central African Republic are now largely bypassed by both

bilateral donors and NGOs. This is in sharp contrast to countries such as Uganda, Mozambique, Nicaragua, Tanzania and Peru where generous bilateral aid is complemented with equally generous assistance from NGOs. Only after all these questions have been answered can definitive policy recommendations be given. Based on this analysis, some initial policy suggestions can be offered, but these should be treated with appropriate caution.

NGOs on average gave more aid per capita to countries ranked by the United Nations as high priority. Yet, from this general pattern there were significant deviations that could merit a policy response. Deviations embody certain donors, certain regions, and certain size of countries.

Certain donor countries, particularly the Dutch and the German, could do more to ensure that their NGOs target the high-priority countries better. The policy adopted by NORAD, the implementing agency of the Norwegian government, could serve as an example. The head of the civil society department stated:

through having discussions with NGOs we convinced them that they should spent at least 50 per cent in the least developed countries. It has taken us years, but our NGOs—because of our active policy towards them—have reached this percentage.

Specific incentives can entice NGOs to become more active in certain underfunded regions, notably in the priority and top-priority countries of South Asia and the Middle East and North Africa. Yet this policy recommendation is based on the assumption that NGOs can work effectively in these countries, an assumption that merits further research.

As is clear from the above analysis, there is a pattern of strong concentration in the allocation of NGO aid. Conditional to better insight into the effects of this concentration at the field-level, greater dispersion in international NGO aid appears to be desirable. To this end, the theoretical framework suggests ways to stimulate dispersion: strengthening the forces that lead to dispersion and minimizing those that lead to concentration. It is clear that some of the centripetal and centrifugal forces are stable and independent from policy. These include thickness of the labour markets, dispersion of demand and transportation costs. Conversely, policy can influence certain factors, such as the importance NGO decisionmakers attach to the low 'price' of inputs. The theoretical part of the paper explained that as the size of the market expands, the decreasing price of input stimulates concentration. If an NGO is the first nongovernment agency in a location, the costs for entry (in time and finance) will be high; once other NGOs have settled in the country, costs are lower for new entrants. Theoretically, if the pressure of reducing costs is relaxed, i.e., if donors refrain from applying a standard overhead percentage, the emphasis on market size becomes less important, which in turn should stimulate dispersion. Promoting an environment that encourages risk-taking and openness can downplay another centripetal factor, the blame-sharing effect. Instead of withholding finances for NGOs because of unsuccessful projects, donors should assess whether these have analysed potential risks in advance and have taken precautionary measures and remedial action; steps that government agencies should applaud. By stimulating risk-taking, NGOs will be more likely to venture into territories that remained hitherto unexplored.

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Appendix 1

Appendix Table
Aid allocations by Germany, Netherlands, Norway and United States
(in millions €), 2004

Country	NGO total	Bilateral*	Total	Country	NGO total	Bilateral*	Total
Albania	8.39	129.4	137.79	Lebanon	10.96	53.2	64.16
Algeria	0.55	10.2	10.75	Lesotho	12.6	10.6	23.2
Angola	70.86	141.3	212.16	Liberia	8.56	165.8	174.36
Argentina	3.91	12.8	16.71	Libya	–	2.8	2.8
Armenia	7.43	130.3	137.73	Macedonia	1.84	109.8	111.64
Azerbaijan	10.49	71.2	81.69	Madagascar	16.12	64.7	80.82
Bangladesh	85.96	274.7	360.66	Malawi	59.11	110.0	169.11
Belarus	0.4	20.0	20.4	Malaysia	0.24	6.6	6.84
Belize	0.05	2.5	2.55	Maldives	0.0	0.2	0.2
Benin	6.21	84.3	90.51	Mali	29.87	118.6	148.47
Bhutan	1.46	0.3	1.76	Mauritania	8.83	28.5	37.33
Bolivia	35.93	335.0	370.93	Mauritius	0.06	0.4	0.46
Bosnia-Herzegovina	9.51	127.2	136.71	Mexico	19.63	116.4	136.03
Botswana	4.85	32.7	37.55	Moldova	2.6	55.1	57.7
Brazil	56.34	121.5	177.84	Mongolia	4.29	70.8	75.09
Burkina Faso	5.1	67.4	72.5	Morocco	4.46	271.9	276.36
Burundi	15.96	90.6	106.56	Mozambique	46.61	196.6	243.21
Cambodia	24.07	85.1	109.17	Myanmar	8.0	20.2	28.2
Cameroon	10.38	257.6	267.98	Namibia	5.18	55.0	60.18
Cape Verde	0.0	19.5	19.5	Nepal	22.77	144.3	167.07
Central African Rep.	1.02	19.6	20.62	Nicaragua	30.36	602.9	633.26
Chad	10.25	86.8	97.05	Niger	15.19	23.5	38.69
Chile	7.68	39.3	46.98	Nigeria	38.76	154.1	192.86
China	11.02	442.5	453.52	Oman	0.0	0.6	0.6
Colombia	16.8	709.3	726.1	Pakistan	19.11	262.1	281.21
Comoros	0.0	0.0	0.0	Palestine	29.42	11.0	40.42
Congo, Dem. Rep. of	43.29	320.7	363.99	Panama	1.57	219.8	221.37
Congo, Rep. of	0.22	3.8	4.02	Papua New Guinea	0.66	2.4	3.06
Costa Rica	4.1	18.2	22.3	Paraguay	3.21	27.1	30.31
Côte d'Ivoire	2.95	46.3	49.25	Peru	51.18	369.4	420.58
Croatia	4.3	59.8	64.1	Philippines	27.59	145.4	172.99
Cuba	2.62	12.4	15.02	Rwanda	19.84	100.0	119.84
Djibouti	0.0	3.8	3.8	Saudi Arabia	0.0	1.9	1.9
Dominican Rep.	2.02	51.4	53.42	Senegal	9.76	83.0	92.76
Ecuador	17.72	153.1	170.82	Sierra Leone	16.79	43.4	60.19
Egypt	14.59	747.7	762.29	Solomon Islands	–	0.0	0.0
El Salvador	31.12	69.9	101.02	Somalia	27.36	66.1	93.46
Equatorial Guinea	0.06	0.2	0.26	South Africa	33.06	234.3	267.36

Table continues

Note: * = Germany, Netherlands, Norway, US.

Appendix Table (con't)
Aid allocations (in millions €), 2004

Country	NGO total	Bilateral*	Total	Country	NGO total	Bilateral*	Total
Eritrea	10.53	106.8	117.33	Sri Lanka	25.42	79.1	104.52
Ethiopia	124.69	615.6	740.29	Sudan	61.93	613.1	675.03
Fiji	1.03	1.8	2.83	Suriname	3.22	75.2	78.42
Gabon	1.23	4.3	5.53	Tanzania	42.68	2.2	44.88
Gambia, The	2.47	3.4	5.87	Thailand	10.81	22.4	33.21
Georgia	12.39	154.0	166.39	Timor-Leste	3.66	69.5	73.16
Ghana	25.27	137.9	163.17	Swaziland	7.37	239.2	246.57
Guatemala	37.03	126.8	163.83	Syria	2.62	34.6	37.22
Guinea-Bissau	1.03	78.5	79.53	Tajikistan	16.0	31.2	47.2
Guinea	3.14	0.9	4.04	Togo	2.18	11.6	13.78
Guyana	0.69	40.5	41.19	Trinidad & Tobago	0.08	2.8	2.88
Haiti	39.3	168.6	207.9	Tunisia	0.43	56.5	56.93
Honduras	26.26	150.7	176.96	Turkey	1.01	104.5	105.51
India	136.97	344.8	481.77	Turkmenistan	0.0	7.7	7.7
Indonesia	49.11	402.6	451.71	Uganda	58.25	378.6	436.85
Iran	5.65	67.0	72.65	Ukraine	1.58	165.8	167.38
Jamaica	0.31	44.2	44.51	Uruguay	0.63	2.1	2.73
Jordan	4.28	430.8	435.08	Uzbekistan	4.42	53.3	57.72
Kazakhstan	2.12	81.0	83.12	Venezuela	1.99	19.1	21.09
Kenya	54.16	294.0	348.16	Vietnam	11.89	132.0	143.89
Korea, Rep. of	0.71	69.1	69.81	Yemen. Rep. of	0.48	153.7	154.18
Kyrgyz Rep.	4.39	47.8	52.19	Zambia	45.86	191.3	237.16
Laos	4.59	34.0	38.59	Zimbabwe	80.33	43.9	124.23

Note: * = Germany, Netherlands, Norway, US.

Source: OECD/DAC (for bilateral figures). NGO figures provided by NGOs.

Appendix 2: List of interviews with organizations and institutions

A Nongovernmental organizations

Netherlands

- Cordaid
- ICCO
- Hivos (not interviewed)
- Novib (now OxfamNovib)
- Plan Nederland (not interviewed)

Germany

- Kinder Nothilfe Deutschland
- Evangelischer Entwicklungsdienst
- Friedrich Ebert Stiftung
- Konrad Adenauer Stiftung (no country data)
- MISEREOR

Norway

- CARE Norway
- Norwegian Church Aid
- Norwegian People's Aid
- Redd Barna (Save the Children)

United States

- CARE USA
- Christian Children's Fund (not interviewed)
- Mercy Corps
- Oxfam United States
- Population Services International (PSI)
- Save the Children USA
- World Vision USA

B International nongovernment organizations

- International Planned Parenthood Federation

C Institutions

- Netherlands Ministry of Foreign Affairs, Division of Effectiveness and Quality (interviewed 6 September 2006)
- German Ministry of Economic Cooperation and Development (BMZ), NGO Division (interviewed 8 September 2006)
- Norwegian Ministry of Development Cooperation (NORAD), Civil Society Department (interviewed 11 September 2006)