

# Democracy and Foreign Aid

Marie Bjella



*Master Thesis in Political Science  
Department of Political Science  
Faculty of Social Sciences  
University of Oslo  
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Marie Bjella

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# Abstract

Since the end of the World War II foreign aid has been at the center of development politics. Foreign aid has been promoted as one of the main tools for eradicating global poverty, but its effectiveness has been contested. Over the last decades researcher have debated whether aid is good for economic growth, has no effect, or whether it is in fact hindering economic development (Radelet 2006). However, some agreement has formed between researchers on foreign aid in that aid works under specific conditions (see e.g. Burnside & Dollar 2000, Collier & Dollar 2002). Thus, for now, what is most pressing, is to find the conditions for when aid has the most effect. Mostly, the research on the conditions for aid's effectiveness has been directed at economic policies of the country, not its political institutions. Despite the fact that increasing amounts of aid are being tied to demands for democratization and political reforms, there has been relatively few studies that examine the impact of aid in democratic regimes in comparison with autocratic regimes; especially in relation to its effect on poverty levels.

My main hypothesis is that foreign aid will be more effective in reducing poverty in democratic regimes than in autocratic regimes. I base this argument on political and economic theory, and test it through the use of both statistical techniques and qualitative analysis; more specifically a Time-Series Cross-Section (TSCS) analysis and a case study of a Norwegian aid project in Tanzania. The causal effect of democracy on aid effectiveness is examined through the use of statistical tools, while the potential causal mechanisms behind such an effect is studied through the use of process tracing in the case study. The quantitative data is made up of 155 countries in the period from 1960-2011, consisting of all the countries in the world that have received foreign aid at least once in this period. In the case study, I look closer at a Norwegian development project, namely the subsea cable from Tanga on the mainland of Tanzania to one of the islands of Zanzibar; Pemba, to highlight the mechanisms of aid allocation in a democracy.

The findings of this thesis indicate that aid becomes more effective in alleviating poverty at higher levels of democracy. However, it is clear that there are several processes and mechanisms that work in parallel, and there are some uncertainties tied to

the importance of the democratic mechanisms highlighted in this thesis. The results of the statistical analysis reflects this, turning out non-robust and relatively low point estimates of a democratic effect. However, the case study highlights the potential importance of contested elections, as well as a minimum level of political rights and civil liberties for the effective allocation and distribution of aid.

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The data sets used in this thesis, and the pertaining do-files are available upon request.

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# Acronyms

- ASP: Afro-Shirazi Party
- CCM: Chama Cha Mapinduzi (the Party of the Revolution)
- CPI: Corruption Perceptions Index
- CUF: Civic United Front
- DAC: Development Assistance Committee
- FDI: Foreign Direct Investment
- FHI: Freedom House Index
- GDP: Gross Domestic Product
- GMM: Generalized Method of Moments
- HDI: Human Development Index
- HFO: Heavy Fuel Oil
- ICRG: International Country Risk Guide
- ILPI: International Law and Policy Institute
- IMF: International Monetary Fund
- MDG: Millennium Development Goal
- NGO: Non-Governmental Organization
- NVE: Norwegian Water Resources and Energy Directorate
- ODA: Official Development Assistance
- OECD: Organisation for Economic Co-operation and Development
- OLS: Ordinary Least Squares

- PPP: Purchasing Power Parity
- REP: Rural Electrification Project
- RNE: Royal Norwegian Embassy
- TANU: Tanzania African National Union
- TSCS: Time-Series Cross-Section
- UN: United Nations
- WDI: World Development Indicators
- ZID: Zanzibar Identification Card
- ZNP: Zanzibar Nationalist Party

# Chapter 1

## Introduction

Global poverty is persistent. Despite more than half a century of massive efforts at alleviating global poverty, almost half of the world's population live on less than \$ 2 a day (Global Issues 2010). With the rise in global food prices, rising populations, economic crisis as well as the volatility of global climate, there has never been more people vulnerable to poverty, in absolute numbers, than today. It might be true that the last decades have seen impressive decreases in the relative share of global poverty (World Bank 2011a), but this can mainly be attributed to lower levels of poverty in India and China (United Nations 2011). Other regions, mainly in sub-Saharan Africa and South Asia, see a different picture. Since 1981 the number of people living on less than \$ 1.25 a day in sub-Saharan Africa, has increased from 211 million to 597 million in 2005 (World Bank 2011b). Even when accounting for population growth, this is a depressing increase. In fact, almost half of the people in sub-Saharan Africa today live on less than \$ 1.25 a day, while one third suffers from chronic malnutrition (World Bank 2011b).

One main tool for addressing such massive and widespread poverty has traditionally been Official Development Assistance (ODA) and other forms of foreign aid (OECD 1999). In fact, since the end of World War II and the Marshall aid, foreign aid has been at the center of the development debate (Moyo 2009, 10). However, the strategy for *how* aid should affect poverty has changed over the years. Historically, it was economic growth that was promoted as the primary development tool, and for a long time it was assumed that economic growth in time would lead to poverty reduction on its own accord (Gilbert & Vines 2000). Over the decades, however, the development agenda and the conditions for aid has gone from direct financing and large-scale infrastructure projects in the 1950s to "neoliberalism" and market liberalization in the 1980s (Gilbert & Vines 2000). The 1990s saw a move away from the neoliberal agenda of structural adjustment programs, towards the emphasis on human rights and provi-

sion of basic services (Gilbert & Vines 2000). During the last decade, democracy and good governance has been promoted as tools for eliminating poverty and creating economic growth, but the empirical evidence of the effects are, so far, inconclusive (see e.g. Przeworski, Alvarez, Cheibub & Limongi 2000, Doucouliagos & Ulubasoglu 2008).

The existing quantitative research on aid effectiveness has showed inconclusive and non-robust results on the relationship between foreign aid and development, for the most part measured as economic growth. Some findings have been more influential than others, and have been decisive in our understanding of aid effectiveness (see e.g. Burnside & Dollar 2000, Collier & Dollar 2002, Easterly 2003). These articles, for the most part, examine the conditional relationship of aid on growth, focusing on the quality of economic policies as a condition for effective aid allocation. Although there are studies that claim that foreign aid is bad for development (see e.g. Boone 1996, White 1992), there is now a general understanding of foreign aid as an effective tool in creating growth when certain conditions are present. This indicate that the assumption of a linear relationship between aid and growth is not valid, leading to alternative methods for clarifying and exposing the underlying causal links.

The aim of this thesis is to look further into the conditions for successful aid allocation and implementation by examining whether and how democracy affects aid effectiveness in reducing poverty.<sup>1</sup> I take advantage of both quantitative and qualitative methods to clarify this causal relationship between aid, democracy and poverty. Time-Series Cross-Sectional (TSCS) statistical models reveal and indicate the general causal effects of democracy on aid effectiveness in recipient countries of foreign aid; while an in-depth case study examine the democratic mechanisms at work in a low-quality democracy in sub-Saharan Africa. Combining the two methods allows me to draw general conclusions while at the same time providing an opportunity to expand on the causal patterns revealed and the underlying causal mechanisms.

## 1.1 Research Question

The research question for this thesis is based on three broad justifications, which represents the research gap in the aid literature this thesis attempts to fill. The first concerns the dependent variable of most research on aid effectiveness. Traditionally, development in the setting of economic growth means rising per capita Gross Domestic Product (GDP) (see e.g. Burnside & Dollar 2000, Svensson 1999, Hansen & Tarp 2001, Kosack 2003). Economic growth has proven to lift people out of poverty; China pro-

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<sup>1</sup>In this thesis, aid is understood and operationalized as ODA. ODA has two defining characteristics; firstly it includes all transfers from official sources with at least a 25 % grant element, and secondly it has to go fully towards improving human or economic welfare (World Bank 2011a).

vides an important example where millions of people have escaped poverty because of the mere scale of economic growth (see e.g. Chen & Wang 2001). However, economic growth can also create more economic inequality, and Kuznets (1955) shows that economic growth might raise the income of the skilled workers to a larger degree than the income of the unskilled worker. Following Kuznets (1955), Acemoglu & Robinson (2000) indicate that inequality increases in the early stages of modernization, making economic growth an obsolete measure of poverty reduction in these situations.

Even though GDP level is an indication on how the general economic situation in a country is, it tells nothing of the distribution of the resources within a community (Kosack 2003, 2). In fact, looking solely at the rise in GDP per capita could be especially dangerous in the context of aid effectiveness, as an increase in the resources of the elite (potentially from aid), would yield a higher GDP per capita even though the average citizens receives no extra services, income or social benefits. I therefore argue that the effectiveness of aid should be assessed by the level of poverty and its ability to decrease poverty levels, rather than by its ability to increase GDP.

The choice of dependent variable becomes especially relevant when considering that poverty reduction has been, and is today, Western donors' overarching goal of development assistance. The intention of aid is not to enrich the elite, but to lift as many people as possible out of poverty. I argue that the effect of aid, especially when it is combined with the effect of democracy, will be more explicit when looking at the changes in the level of poverty in any given country. It is a better indication of how well aid is working, because it includes an explicit element of distribution; whether the aid is contributing to a rise in the quality of life of most people or only for the elite is an important factor in determining its effectiveness. The dependent variable of this thesis is therefore not economic growth as is usual in the literature, but poverty, as I consider it to be more appropriate in the setting of foreign aid in relation to both its effects and intentions. Aid effectiveness will therefore be directly measured by the induced change in poverty levels; a large decrease in poverty levels related to aid equals effective aid allocations.<sup>2</sup>

The second justification for the research question in this thesis concerns the conditions for the effectiveness of aid. The research on aid effectiveness has traditionally been focused on how *economic policies* affect aid effectiveness, and has to a large extent

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<sup>2</sup>In this thesis, I define poverty in accordance with the "capability approach" by Sen (1992, 109) as: "the failure of basic capabilities to reach minimally acceptable levels". Capabilities are defined as the ability to pursue actions and values a person has reason to value. Rather than seeing poverty as purely income poverty, this approach defines poverty as capability deprivation and thus incorporates the importance of basic capabilities (such as the access to clean water, housing and food) in the experience of poverty. Poverty in this thesis is thus perceived as a multi-dimensional phenomenon.

ignored the importance of *political institutions*. However, the importance of political freedoms in improved living standards is receiving increased attention in the international community, highlighting the need for more research on the field. International aid donors, especially Western, are increasingly making their aid conditional on democratization and enhanced political rights and civil liberties (Banik 2010). In fact, Alesina & Dollar (2000) have found evidence supporting the claim that countries that democratize receive more aid. The aim of this thesis is to look further into the conditions for successful aid allocation and implementation by examining whether and how *democracy* affects aid effectiveness.<sup>3</sup>

The third, and last justification for the research question is the importance of the underlying mechanisms in a potential democratic effect on aid effectiveness. Given the generally non-robust conclusions in previous research on aid effectiveness, it is not only important to clarify the causal effect, but also the causal mechanisms behind such an effect, or perhaps; the lack of one.<sup>4</sup> Complex interactions and mechanisms, along with problems of endogeneity, have most likely contributed to the inconclusive results in TSCS research. This highlights the importance of digging deeper into the issue than merely looking at the overall effect of aid on poverty. The identification of the mechanisms behind a potential democratic effect on aid effectiveness is a crucial step in the direction of global poverty reduction and, a hopeful eventuality, its elimination. The causal path of this relationship and the causal direction of the effect must be clarified in order to improve the effectiveness of future aid flows and investments.

I will therefore look further into the effects of democracy on aid effectiveness in reducing poverty, and examine some of the mechanisms that might contribute to or even explain such an effect. The research question is as follows:

*How does democracy affect aid effectiveness in regard of poverty reductions in countries that receive foreign aid?*

## 1.2 Theoretical Framework

One of the most cited reasons for the ineffectiveness of aid has been the corruption and ignorance of autocratic leaders (Knutsen 2009, Meredith 2006, Ayittey 2005, Baland,

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<sup>3</sup>In this thesis democracy is understood in the accordance with the understanding of Diamond (1996) and Sen (1981, 1999) in that political rights and civil liberties are inherent parts of a democracy and cannot be separated from the holding and respecting of free and fair elections. Notwithstanding the importance of electoral democracy, this thesis operates with a liberal, or substantive, understanding of the concept.

<sup>4</sup>Mechanisms are for the use in this thesis defined as "recurrent processes linking initial conditions and a specific outcome" (Mayntz 2003). When discussing democratic mechanisms, it will only reflect the mechanisms addressed in this thesis.



Moene & Robinson 2010). Such leaders direct valuable resources and aid away from the people and towards his own personal wealth and security. Morgenthau (1962) was amongst the first to argue that aid did not contribute to political and social changes in recipient countries because such changes were not beneficial for the incumbent leader. Other empirical studies have shown that development aid to autocratic regimes has in fact been detrimental to the average welfare of the country's citizens, as the aid can help the regime consolidate its power through corruption and exploitation, rather than spending the aid on effective public policies (Bueno de Mesquita, Smith, Siverson & Morrow 2003, Easterly 2003, Wintrobe 1990, van de Walle 2001).<sup>5</sup>

It seems plausible to assume that a higher degree of transparency and accountability of the government would lead to a more effective environment for eliminating poverty. I argue that the different regime types provide different incentives for how and where to invest; democracies and non-democracies allocate resources differently. The political mechanisms at work in a democracy increases the likelihood that the desire for political survival leads to the provision of public goods and distribution of aid as means to win votes. In autocratic regimes, the political mechanisms fail to provide the same outcome because political survival is ensured through other institutions than contested elections. Thus, there is no need for autocratic leaders to use the allocation and distribution of aid as means to obtain votes. The result is that while democracies more often tend to invest the resources, including foreign aid, in poverty reducing projects, non-democracies invest the resources in promoting the regime's own position of power.

Both the theoretical and empirical literature linking democracy and aid effectiveness are limited, but many of the theories on democracy's effect on economic growth and poverty reduction can also be related to increased aid effectiveness. In order to answer my research questions, I therefore take advantage of the theoretical contributions of Bueno de Mesquita, Smith, Siverson & Morrow (2003), Sen (1981, 1999) and Meltzer & Richards (1981). I argue that these theories provide implications and predictions to why democratic regimes are better equipped at allocating aid more effectively than non-democratic regimes.<sup>6</sup> More specifically, these contributions provide a theoretical framework for the possibility that democracies promote aid effectiveness through the

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<sup>5</sup>When talking about regime type or regime, I refer to whether a country constitutes a democracy or an autocracy; not to the transition of governments or leaders. Democracy is one regime type, while autocracy or non-democracy is another. There are of course degrees of these two regime types, and democracy is therefore measured as a continuous variable, going from one extreme to the other on a continuous scale.

<sup>6</sup>My thesis does not claim that autocratic leaders never redistribute aid, solely that the aid distributed will be more effective in democratic regimes than in non-democratic regimes.

relative size of the winning coalition and elections; political rights and civil liberties and accountability; and political pressure.<sup>7</sup>

This thesis suggests that the theoretical contributions are all related to one another by several political steps, from the political pressure of the poor to the relative size of the winning coalition and the importance of political rights and civil liberties in this process.

### 1.3 Research Method

According to Hansen & Tarp (2001, 555), there are strong indications that most of the explanatory variables in the large-N research on aid are endogenous; meaning that it is difficult to perceive of aid as something that is independent of the existing level of poverty in recipient countries. Several studies have indeed established empirically that there is such a connection (see e.g. Boone 1996, Alesina & Dollar 2000, Burnside & Dollar 2000). This implies that the existence of country-specific effects might lead to correlation between a variable and the error term (Hansen & Tarp 2001, 556). In panel data, when a variable is correlated to the error term, it has traditionally been modeled into the analysis by estimating the effects using a Fixed Effects estimator. This estimator, however, demands full exogeneity of the explanatory variables in relation to the error term, which is most likely not the case in the relationship between aid and poverty. A model using the Arellano-Bond Difference Generalized Method of Moments (GMM) might therefore be the most appropriate statistical model to answer the research question of this thesis. This model controls for both endogeneity and country-specific effects by differencing the data (Hansen & Tarp 2001, Mileva 2007, Arellano & Bond 1991). However, both the Fixed Effects and GMM estimators pose heavy restrictions on the data, increasing the possibility of making type II errors: keeping a false null-hypothesis. In other words, using these methods may lead me to reject an effect of democracy on aid effectiveness even if there actually is an effect. I therefore take advantage of both Ordinary Least Squares (OLS), Fixed Effects and GMM in my analysis when attempting to reveal and clarify the causal relationship between democracy and aid effectiveness.

The unit of analysis in the statistical analysis is country-years in countries that has

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<sup>7</sup>Democratic elections are also considered a political institution, and one that is of decisive importance for democratic mechanisms (Dahl 1959, Beetham 1999). In this thesis, however, I am first and foremost interested in the relationship between accountability and coalition size, highlighting the relationship between the political pressure from the people living in poverty and the attentiveness and responsiveness of the government. In this thesis, the importance of democratic elections is therefore mostly viewed as a mechanism in how it affect this relationship between the relative size of the winning coalition and accountability of the government.

received ODA in more than one year in the period from 1960 to 2011. It is thus a TSCS analysis of all the countries in the world that have received foreign aid in the given period. In the full data set, there are 8020 observations, consisting of 155 countries over a period of 52 years. The data is mostly made up from aggregated variables at country level from the World Bank's World Development Indicators (WDI), but some variables have been collected from other sources. Chapter 5 will thoroughly go through the different variables and the origins. My dependent variable, poverty, and the democratic interaction with aid will distinguish itself from the literature, but aside from these elements the statistical analysis in this thesis draws heavily on the political and economic literature of aggregate effects of aid effectiveness.

However, there are certain aspects of the relationship that cannot be addressed using statistical tools alone. In fact, in this thesis, the question of the causal path seems too complex and too difficult, requiring too many unmeasurable variables, to allow for a cross-sectional analysis as the only research method (see Gerring 2007, 47). Qualitative methods can clarify the underlying mechanisms and processes leading from the independent variables to the dependent variable, as well as increasing the contextual specificity of concepts such as democracy and poverty (Adcock & Collier 2001). Moreover, the problem of endogeneity can to a larger degree be taken into account by applying a case study and elements of process tracing in the analysis. This method of analysis is especially suited to examine complex processes and questions of "how", and aims at clarifying the causal path from the independent variable(s) to the dependent one (Gerring 2007). This resolves the problem of an unclear causal direction and can therefore contribute in illuminating the process from aid to poverty reduction through democratic mechanisms.

The complementary nature of a statistical analysis and a case study ensures that I am able to draw generalizations of a causal effect, while at the same time obtaining in-depth knowledge of the mechanisms and processes behind this causal effect, or potentially; the lack of one. Because of the lack of robustness in statistical research on aid effectiveness, it is fruitful to incorporate both strategies in order to come closer to the actual nature of the relationship between aid and poverty. The full clarification of the relationship between aid and poverty, however, cannot be achieved solely through this thesis, but it does provide an important step in the clarification of the relationship with regards to aid's effectiveness in democratic regimes.

The first step in the research process is the statistical analysis, highlighting areas where further investigation is needed. The two main hypotheses in this thesis are tested through the application of statistical tools in the TSCS analysis. These hypotheses evolve around the causal effect of democracy and political rights and civil liber-

ties on the effect of aid in reducing poverty. The hypotheses test the implication that democratic regimes provide more effective allocation and distribution of aid than non-democratic regimes, and that stronger protection of political rights and civil liberties increases the effectiveness of aid in reducing poverty. Given that the sample consists of countries that have received foreign aid, many of the countries included in the sample of the statistical analysis are poor and developing countries where democratic practices and institutions build on traditional patterns of power and influence. Many of the countries are located in sub-Saharan Africa where neo-patrimonial traditions linger, putting restraints on the democratic quality and political processes (Bratton & van de Walle 1997). This affects both the application of the term "democratic" and its potential effect. However, this does not automatically mean that democracy has no function or that democratic reforms have always turned out unsuccessful. The challenge is to find a suitable definition of democracy and democratic mechanisms in the context of developing countries. More fine-grained theoretical implications and predictions will therefore be examined empirically in the case study, hopefully highlighting some of the challenges facing newly established democracies in sub-Saharan Africa, shedding light on the results from the statistical models. The theoretical contributions of Bueno de Mesquita et al. (2003) and Sen (1981, 1999) are examined through the use of both the quantitative and qualitative methods, while the theoretical model of Meltzer & Richards (1981) is only explored in the case study.

### **1.3.1 Short Background on the Case**

The case selected to highlight the mechanisms and processes behind an aid allocation is a Norwegian development project in Tanzania. More precisely, the case study analyzes the process behind the subsea cable from mainland Tanzania to one of the islands of Zanzibar; Pemba.<sup>8</sup> The cable provides the island of Pemba with electricity, which previously was supplied by old and run-down generators. Work on the cable started in 2008, and was completed within time and budget in 2010 (Poyry 2011). The project is expected to contribute to a significant decrease in poverty on the island, and in every respect the cable is perceived as a successful development project (Poyry 2011, Government of Norway 2009). The process with the cable is portrayed as a prime example of good governance and cooperation, providing the people of Pemba with substantial efforts at alleviating poverty. Moreover, the aid from the Norwegian government was provided as a grant and conditional on the implementation of the cable to Pemba, providing an opportunity to study the effects of conditional aid in a low-quality and

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<sup>8</sup>Zanzibar consists of two islands: the larger one known as Unguja, the island most often referred to when talking about Zanzibar, and its smaller neighbor Pemba.

low-income democracy. The political situation in Zanzibar makes this an especially interesting case that can illustrate many of the challenges facing new democracies in sub-Saharan Africa, adding valuable information that can help clarify and supplement the results from the statistical analysis.

There are only two *de facto* political alternatives in Zanzibar, the Chama Cha Mapinduzi (Party of the Revolution, CCM) and the Civic United Front (CUF).<sup>9</sup> Traditionally, Unguja has been the major source of support for CCM, while Pemba has been the same for CUF. Since the revolution in 1964, CCM has held the presidency; leading to social conflict and political unrest between CCM supporters and the rest (Tronvoll 2010a). Since 1995, when the first multi-party election in Zanzibar was held, CUF has steadily received more and more votes, and have claimed more than once that the elections were rigged in favor of CCM (Informant 2 [Interview])(Poyry 2011). This has evolved into an inter-island conflict, where political divisions run parallel to social and economic grievances (Tronvoll 2010a). The people of Pemba have rightfully claimed that their island has received little of the development and aid projects experienced in Unguja, adding fuel to the social and political divisions. However, the political climate is changing, and the establishment of the Government of National Unity in 2010 was a turning point in the political stability of the islands and between the supporters of the two parties (Informant 4 [Interview])(Tronvoll 2010a).

The subsea cable was implemented just at the time of transition from multi-party democracy to the Government of National Unity, and there are certain elements about this case that make it especially interesting for studying the importance of competitive elections, political rights and civil liberties as well as political pressure in the effective allocation of aid. Hence, the case study is selected strategically in order to illuminate and illustrate the importance of the mechanisms hypothesized about in this thesis.

## 1.4 Findings

Both the statistical analysis and the case study give indications of a democratic effect on aid effectiveness; more precisely, that democracy contributes to more effective aid allocation in reducing poverty. There is little difference between electoral and substantive democracy in effective aid allocation, indicating that other mechanisms than political rights and civil liberties might be more influential in the effective allocation of aid. In fact, the case study indicates that elections and the political competition for

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<sup>9</sup>When talking about *de facto* political alternatives, I refer to the political alternatives in Zanzibar that are large enough to receive a seat in the House of Representatives. Although Zanzibar has many other political parties, none are large enough to receive sufficient votes in any given constituency to win a seat in the House of Representatives.

voters were the decisive mechanisms in the allocation of aid to the cable and to Pemba. It was the political pressure on the CCM, and the growing support for CUF, that forced CCM to look for new voters and thus expand the size of the winning coalition. However, the case study also revealed that it is not that political rights and civil liberties do not matter; they matter in as much as providing the basis for *contested* elections. Before the 2010 elections in Zanzibar, elections proved ineffective in allocating aid to Pemba and ensuring an equal distribution between Unguja and Pemba. However, in the run-up to the elections in 2010, the support for CUF had become so pronounced that the CCM could no longer ignore it. Thus, it was the presence of political pressure and *contested* elections, and the inherent element of a minimum level of political rights and civil liberties for elections to be meaningful, that ensured the implementation of the subsea cable from Tanga to Pemba.

It is likely that the measure of electoral democracy in the statistical analysis picked up the importance of a minimum level of political rights and civil liberties for elections to be meaningful. This would explain the results from the statistical analysis that political rights and civil liberties provided no further effect on aid effectiveness; the difference in the effect of electoral and substantive democracy is marginal in the effective allocation of aid. Political rights and civil liberties are instrumental in the effective allocation of aid in that it intensifies political competition for voters among politicians who desire to be elected.

## 1.5 Structure of the Thesis

This thesis consists of a total of eight chapters. Chapter 2 gives an overview of the existing empirical research on the field. It focuses on the literature on aid effectiveness and gives a brief presentation of the most influential contributions and important discoveries in relation to the nature of the aid-poverty relationship. Chapter 3 presents the theoretical framework, drawing on theory on the distributive effect of democracy in highlighting the importance of the mechanisms of the winning coalition and elections; political rights and civil liberties and accountability; and political pressure. It also highlights important empirical contributions in conceptualizing democracy, as well as important findings on democracy's effect on economic growth and the provision of public goods. Chapter 4 outlines the research method, while chapter 5 provides an operationalization of the variables and concepts used in this thesis. Chapter 6 presents the statistical results and analysis, while chapter 7 analyzes the importance of the different mechanisms presented in this thesis for the implementation of the subsea cable from Tanga to Pemba in Tanzania. Chapter 8 summarizes the most important findings and draw conclusions from this thesis, as well as suggesting areas for further research.

# Chapter 2

## Literature Review: Empirical Findings on Aid Effectiveness

### 2.1 Introduction

The overarching problem with the empirical literature on the effectiveness of aid is that there is limited theory to guide the selection of appropriate specifications for aid effectiveness; there is no clear theoretical model on how aid will affect growth (Easterly 2003, 23). This has led to rather diverse and complex results in the research on aid effectiveness, and the general conclusions are incoherent. This chapter will give an overview of the existing research on aid effectiveness, which has often been assessed in relation to economic growth. Although this literature does not address poverty as such, it still holds important insights and empirical implications for my thesis on the overall effectiveness of aid.

According to Radelet (2006) there are generally three broad schools of thoughts on the effectiveness of aid: aid has a positive relationship with economic growth; aid has no effect on economic growth, and might in fact be detrimental to development, and; aid has a conditional relationship with economic growth, accelerating growth under certain conditions. The first category consists mainly of single case studies, which have found that aid has, on average, worked. However, the cases have found little systematic evidence of aid contributing to economic development or poverty reduction (see e.g. Rosenstein-Rodan 1961, Chenery & Eckstein 1970). The second school on aid effectiveness has only had a few studies published, but has been rather influential in policy making. These studies apply cross-sectional data and methods to clarify the relationship. However, most of the studies that reach the conclusion that aid does not work, impose unrealistic constraints in their analysis, such as the assumption of a linear relationship (see e.g. Boone 1996, White 1992). The third school of thought seems to

provide an explanation to why aid has worked in some cases and not others. As with the previous school of thought, these studies apply mostly quantitative research methods and statistical large-N analysis. These studies rely mainly on different interaction terms with aid, depending on the nature of the conditional relationship. The interaction terms that have been used, have generally been relatively fragile, not holding up against robust checks (see e.g. Burnside & Dollar 2000, Collier & Dollar 2002).

## 2.2 Important Contributions

The 1990s saw a new generation of aid research appear, revived by the research of Boone (1996, 1994) and his article "Politics and the Effectiveness of Foreign Aid". Boone (1996, 1994) put a new direction on the research on aid effectiveness by including political determinants of aid effectiveness and focusing on the relationship between aid, growth and policies in his analyses. He concludes that aid has no effect on growth or investment. The article analyzes the effects of aid in different regime types; elitist, egalitarian and laissez-faire. Elitist regimes have governments that seek to maximize the welfare of the ruling elite; egalitarian regimes seek to maximize the welfare of its' poorest citizens; and laissez-faire regimes seek to minimize taxes and market distortions (Boone 1996, 3). He finds that egalitarian regimes or democracies do not use aid any differently than elitist or laissez-faire regimes; all regimes tend to use the resources from aid towards consumption rather than towards investments. However, he does find that democratic regimes have substantially lower infant mortality rates than the other regimes, attributing this effect to higher empowerment of the poor in liberal political regimes and the corresponding pressure on the government to obtain basic services (Boone 1996, 4). Boone points to two plausible implications of his results; that support of liberal regimes might be a more effective way of fighting poverty, or alternatively, that there are underlying factors that influence aid effectiveness but these are not influenced by the current type of regime (Boone 1996, 29).

The Burnside & Dollar (2000) article "Aid, Policies and Growth" received much attention as it addressed the pessimism from Boone's work, as well as the lack of consensus from earlier research (Easterly 2003). It was, at least partly, responsible for bringing attention to the conditionality of aid (Easterly 2003). Their study finds a positive relationship between aid and growth, but only in the presence of good policies. As summarized by Burnside & Dollar (2000, 847): "We find that aid has a positive impact on growth in developing countries with good *fiscal*, *monetary*, and *trade* policies but has little effect in the presence of poor policies" [emphasis added]. In order to create a variable for "good policies", Burnside & Dollar (2000) constructed an index using the budget surplus, the inflation rate and a measure of openness of the economy



developed by Sachs & Warner (1995). Their article has been one of the most influential articles on the effects of aid on economic growth. In many ways, their article was instrumental in promoting the neoliberal agenda of developing and implementing sound economic policies as a condition for aid. The article contributed strongly to a general understanding of an increase in aid effectiveness under sound economic policies, and the Economist (2002) posted that "there is now a strong body of evidence, led by the research of David Dollar, Craig Burnside and Paul Collier, all economists at the World Bank, that aid does boost growth when countries have reasonable economic policies". However, "Aid, Policies and Growth" and its findings have been subjected to close scrutiny, and replication studies that use different data sets, different regression specifications or different estimators have failed to find the same significant effect of policies and growth (see e.g. Dalgaard & Hansen 2001, Hansen & Tarp 2000b, 2001, Hudson & Mosley 2001, Lensink & White 2001, Lu & Ram 2001, Easterly et al. 2003).

The reason for the different conclusions in Boone (1996, 1994) and Burnside & Dollar (2000) can be traced back to the growth model which they base their analyses on. Boone (1996) assumes that there is a linear relationship between aid and growth, while Burnside & Dollar (2000) treat the relationship as being non-linear by introducing an interaction term between policies and aid. Their article also point to the fact that the impact of aid on growth is subject to diminishing returns; meaning that the impact of aid decreases after a certain point. When including a quadratic term of aid they obtain a statistically significant negative estimate, indicating that the relationship between aid and growth is not only non-linear, but also experience a fall in effectiveness after a certain point is reach, creating an inverted U-shape.<sup>1</sup>

## 2.3 Aid Conditionality

Some of the cross-country evidence can be interpreted as giving evidence in favor of aid conditionality, but there is also widespread evidence that the quantity of aid does not necessarily lead to a change in the quality of policies, even when conditionality has been used. In fact, the fulfillment of aid conditionality has a poor completion and enforcement rate (Alesina & Dollar 2000, Collier 1997, Rodrik 1996, Williamson 1994). The International Monetary Fund (IMF) and the World Bank have for the last decades tied parts of their aid to policy reform in recipient countries. The practice of aid conditionality was originally introduced by the IMF, and was conditioned on the recipients' reduction of fiscal and current account deficits. In the 1980's IMF started to tie its aid to structural adjustments, which also included public sector reform and large privatization projects (Montinola 2010, 358). A study by Haggard (1985) ana-

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<sup>1</sup>This relationship was elaborated on by Hansen & Tarp (2001).

lyzing IMF programs in the period from 1974 to 1984, finds that out of 30 programs only 14 were completed. And of the ones that were completed, less than half were implemented as they were intended to. Another study of IMF programs by Ivanova et al. (2001) showed a completion rate of only 56 % in the period from 1992 to 1998. Dollar & Svensson (2000) conducted a similar study, only with World Bank structural adjustment programs rather than IMF programs. Their study show that in the period from 1980 to 1995, only two thirds of all the programs were in fact completed. As a consequence, there is a general lack of trust in the conditionality of aid, especially regarding structural adjustment programs and other market-oriented policies (see e.g. Collier 1997, Killick et al. 1998, 165).

### **2.3.1 Donor Interests**

Alesina & Dollar (2000) turn the question of aid effectiveness around, and ask to what extent the failure of aid can be contributed to the pattern of donation from industrialized countries. They find evidence in support of the claim that bilateral aid is first and foremost given in accordance with political and strategic considerations, rather than being given to countries that pursue healthy reforms or good policies. A former colony with poor political institutions and economic policies, receive more aid than a non-colony with superior political and economic institutions. The quantity of aid is therefore uncorrelated with the quality of institutions and policies. However, they did find that countries that underwent democratization processes received more aid than countries who did not democratize, despite colonial history or strategic political considerations (Alesina & Dollar 2000, 50-52).

In line with this argument, Bearce & Tirone (2010) claim that the effectiveness of aid is contingent on the strategic interests of the donors. If the donors have a large strategic interest in the recipient country, aid will be less effective as the donors cannot credibly enforce their conditions for economic reform. The conditionality of aid has therefore not been regarded seriously by recipient governments, because as long as the donor government benefits strategically or politically from distributing aid, the aid flow will most likely continue even when recipient governments fail to enact the requested policies (Bearce & Tirone 2010, 839). Killick et al. (1998, 165) concluded that "in the general case, conditionality is not an effective means of improving economic policies in recipient countries. The incentive system, most notably the absence of a credible threat of punishment of non-implementation, is usually inadequate in the face of difference between donors and governments about objectives and priorities". Only in an environment where donors are not driven by strategic interests can the threat of withdrawing aid be regarded as credible.

Collier (1997) make the claim that conditionality has failed. He argues that the reason for this failure is not that the wrong policies have been promoted, but that it has failed to achieve them (Collier 1997, 58). He points to the reluctance of donors to actually implement the punishment and withdraw aid in the case of a breach to any condition, as *the* reason for the failure of aid conditionality. The punishment of aid withdrawal seems much too strict for a minor breach to any agreement, and lacking any lesser punishment, the donors therefore prefer to waiver the conditions (Collier 1997, 60). He concludes that "aid has simply failed to induce policy change", and that "the attempts to do so has resulted in aid being wasted in policy environments where it cannot be effective" (Collier 1997, 75).

However, Montinola (2010, 358) highlights the importance of identifying under which conditions aid conditionality has been successful. She finds that aid from the IMF and the World Bank (multilateral aid) has indeed promoted fiscal reform, but only in more democratic countries. She argues that "recipient governments' willingness to comply with policy conditions depends on the degree to which aid promotes their political survival, and since the impact of aid on government survival increases with recipient country's level of democracy, governments' responsiveness to conditionality should increase with recipient countries' level of democracy" (Montinola 2010, 361).

Montinola's argument is based on the political survival model of Bueno de Mesquita et al. (2003), which argues that cumulative aid increases the likelihood of survival for an autocratic regime, while the current flow of aid increases the probability of leaders' survival in democratic regimes. This makes autocratic leaders less dependent on aid, and as a consequence such leaders have less incentive to comply with aid conditions. Because democratic regimes do not have any extra resources in times of emergency, they are more dependent on foreign aid. This dependence on aid naturally increases the incentives to comply with aid conditions. Even though the conditions for aid might be far from compelling, it is better than the alternative; facing current and future crises without aid (Montinola 2010, 379). Kono & Montinola (2009) test empirically the foundations of the political survival model of Bueno de Mesquita et al. (2003), explicitly including the impact of aid on political survival. They find evidence in favor of this model, and conclude that donors should make aid conditional on the type of regime in recipient countries.

## **2.4 Aid and Democracy**

Boone (1996) is one of the few that has explored the effect of political variables, notably regime type, on aid effectiveness. His general findings indicated that the impact of aid on consumption and investment does not vary between regime types, and that

there is no relationship between aid and growth. Svensson (1999) also looked into the effect of political variables on growth, and contrary to Boone's findings, he found a positive relationship between aid and growth. Svensson (1999) explored the impact of democracy and civil and political liberties on aid effectiveness, and found that aid has a positive relationship with growth in countries with institutionalized checks on governmental power. The institutionalized checks are the democratic institutions, consisting amongst others of political parties, elected representatives, free speech and the right to organize (Svensson 1999, 276). He concludes that the impact of aid is conditional on the level of political and civil liberties in a country. Svensson (1999, 276-277) himself point to four possible explanations for the differences in his findings and the findings of Boone (1996). Firstly, Svensson (1999) examines the relationship between aid and economic growth, not the relationship between aid, consumption and investment, which is the focus of Boone's study. Secondly, Svensson uses another data set on foreign aid which includes both direct grants and the grant component of concessional loans. Thirdly, Svensson's sample is larger than Boone's and includes all the recipient countries with available data. Lastly, Svensson treats both the level of aid and the degree of democracy as endogenous. His finding that the amount of foreign aid is determined by political and strategic considerations for a few donors, is in line with the findings of Alesina & Dollar (2000). He finds no indications of more aid being allocated to democratic countries by France, Germany and Italy. Rather, he finds that the allocation of aid is mostly dictated by political and strategic considerations for these countries (Svensson 1999, 291). However, his findings contradict those of Alesina & Dollar (2000) in that he finds little significance between bilateral aid flows and democracy after 1990. His results indicate that donors do not allocate aid systematically to countries with a higher degree of democracy.

Kosack (2003) investigates aid's impact on the quality of life. He does not find a significant relationship between aid and the quality of life, but in combination with democracy the effect of aid becomes both substantial and significant (Kosack 2003, 7). Autocracy has the opposite effect; aid becomes ineffective (and potentially harmful) in an autocratic political environments. Quality of life is measured by the Human Development Index (HDI), which includes three elements of welfare: income, as measured by GDP per capita; longevity and health, as measured by life expectancy; and education, as measured by school enrollment and the level of literacy. The primary measure of democracy is taken from the Polity IV Index. He also uses other measures of democracy, including the measure from Freedom House (Kosack 2003, 4, 8). His results indicate that aid's effect of the quality of life becomes more positive the more democratic a country is, and more negative the more autocratic a country is. He also

finds that poor democratic countries have lower growth in the quality of life than less democratic countries, but that aid reverses this negative relationship; spurring a higher quality of life in a democratic environment. In autocracies, however, aid will cause the quality of life to grow at a lower rate than it would have without aid (Kosack 2003, 11). Kosack concludes that in order to work, aid needs democracy.

His findings are sharply contradictory to those of Boone (1996), and Kosack promotes two possible explanations for this. Firstly, Kosack uses a continuous measure of autocracy and democracy, while Boone classifies the regimes as either one of his three options. Kosack point to the fact that his results indicate that only the more democratic countries spend aid wisely, and that Boone therefore might have missed this point by taking democracy as a whole. Secondly, Boone compares aid and its effect in the same period, while Kosack assumes that the effect of aid will take some time to show itself, and therefore lagged the measure of quality of life one period (Kosack 2003, 7).

Isham et al. (1995) explore the relationship between civil liberties and government projects that has been financed by the World Bank, and find that investment projects have been more effective in countries where the citizens enjoy civil liberties. Even after controlling for the level of democracy, the effect of civil liberties remains strong.

## **2.5 The Fungibility of Foreign Aid**

There has also been research on the fungibility of aid, meaning that the money donated for specific aid projects release resources for the government to spend elsewhere. Feyzioglu et al. (1998) and Pack & Pack (1993) show that aid is relatively fungible, even more so than anticipated. This indicates that the recipient government spends the money differently than the donors might wish, making it difficult for donors to target particular groups or use aid strategically to change the level of poverty or distribution of income. The fungibility of aid also makes it harder to evaluate the effectiveness of aid, as the aid makes it possible for the recipient government to reallocate their other resources as they see fit. This brings up the question of how would things be had there been no aid in the analysis and evaluation of aid's success (World Bank 1998, 60-61). In cases where aid is fungible, success should not be evaluated after the how much aid has been spent, but rather on how they have contributed to the improvement of overall efficacy in government spending (World Bank 1998, 61). Feyzioglu et al. (1998) draw the general conclusion that when aid goes mostly to government spending, it is largely fungible between consumption and investment. The fungibility of aid implies that aid is considered to be in the same category as natural resources such as oil and gas; economic resources of "unearned" income or non-tax revenue (Wright 2008, Moore 1998, 2001). This provides the government with additional resources to distribute freely to

its key constituents without introducing more taxation. An important implication of this argument is that the potentially negative effect of such resources results from an interaction between a regime's institutions and the resources (Morrison 2007). Thus, in regimes with poor institutions, foreign aid is used to the benefit of the ruling elite, while in regimes with strong democratic institutions, the resources from aid can be used to improve the welfare of the citizens. Either way, resources from aid can be used to strengthen the regime (Smith 2004).

## 2.6 Conclusion

With the articles mentioned above in mind, the cross-country evidence can be interpreted as giving evidence in favor of aid conditionality. All in all, it looks like researchers agree that aid works under certain conditions, and donors and development economists are now trying to come to an agreement on which conditions make aid most effective in alleviating poverty and creating economic growth. However, there also seems to be an understanding that conditionality and economic reform has not always transformed things to the better. The structural adjustment programs have been accused of only creating more poverty, as donors have obliged recipient governments to introduce fees for primary education and basic health care (Oxfam 1995). Economic conditions, such as "good" economic policies, structural adjustments and fiscal reform, have been the dominant preconditions for receiving aid in the last decades, while political factors have been largely ignored. This does not imply that political conditions has never been at the center of any research, it simply means that the economic conditions for aid's effectiveness has been the focus of international donors and development thinkers alike. However, there are clear indications of a growing realization of the importance of political factors, and especially that of democracy, in the effectiveness of aid; donors tie increasing amounts of aid to democratic reform, and make aid conditional on democratic practices. The emergence of democratization as a condition for aid, highlights the need for more research on the field, as the direct effects of democracy on development are not sufficiently understood. Many have written about the impact of aid on poverty, or about the effect of democracy on aid effectiveness, or even about the link between democracy and poverty levels, but none (as far as I am aware) have examined the impact of democracy on the effect of aid in reducing poverty. This thesis is a contribution to the debate over which conditions make aid most effective, and gives a clarification of the importance of democracy in the effectiveness of aid in reducing global poverty.

# Chapter 3

## Theoretical Framework

### 3.1 Democracy

Defining democracy is not an easy task, and is not without challenges. Minimalist definitions of democracy stress the need for a minimum level of political rights and freedoms in order for political participation and competition to be seen as meaningful (Diamond 1996, 21). Schumpeter (1947, 269) provides the classical minimalist definition of democracy as a system "for arriving at political decisions in which individuals acquire the power to decide by means of a competitive struggle for the people's vote". This definition emphasizes the electoral elements of democracy, and is therefore sometimes termed definitions of "electoral democracy". In this understanding of democracy, the voting power constitutes the minimum level of political rights and freedoms that must be present for a regime to qualify as a democracy (Banik 2010, 87). At the opposite end of the scale is the broader concept of liberal democracy, which includes a wide range of features for a country to qualify as democratic. Diamond (1996, 23-24) promotes the concept of liberal democracy, and argues that a regime must support political participation through other means than solely elections. He argues that for a country to be democratic, it must hold free and fair elections with universal adult suffrage, as well as boosting the importance of democratic institutions, such as the system of checks and balances, upholding a rule of law, the rights of citizens to information, to assembly, to speech etc.

There are, of course, numerous definitions of democracy that operate in between the two definitions of electoral and liberal democracy. Dahl (1959, 1971) presents an extension of Schumpeter's notion of electoral democracy, and put forward a set of conditions that are required for a polyarchy; which arguably constitutes a subdivision of democracy. Dahl emphasizes that "a key characteristic of a democracy is the continued responsiveness of the government to the preferences of its citizens", and specific

conditions must be present for a government to be responsive and accountable. He highlights two dimensions in a polyarchy; contestation and participation. Thus, Dahl (1959, 1971) emphasizes both the importance of the political contestation as stressed by Schumpeter (1947), and the political participation of voters to actively join in political processes.

Przeworski, Alvarez, Cheibub & Limongi (2000), however, disagree strongly with Dahl, and argue that concepts such as "accountability", "responsiveness", "responsibility" and "participation" should not be included in a definition of democracy as such. They believe that "the question whether or not regimes characterized by freedom of opinion, widespread participation, and repeated elections are in fact responsive is best left open for investigation, rather than resolved by definition" (Przeworski et al. 2000, 33-34). Instead, Przeworski (1991, 10) propose another minimalist definition where democracy is "a system in which parties lose elections". According to this definition there are two central components of democracy; the government should be filled (indirectly or directly), and the filling of this government must happen through contested elections (Banik 2010, 88-89).

Beetham (1999) recommends to distinguish the *concept* of democracy from the *theories* of democracy. Notwithstanding that there is "a basic core to the meaning of democracy", he argues that the definition of democracy should not be confused with the judgement of whether it is good, or how good it is (Beetham 1999, 2). He proposes two basic principles of democracy; "popular control" and "political equality". To him, democracy is a rule of the people where civil and political rights are inherent parts of democracy, and particular institutions, such as elections, are only democratic in as far as they contribute to the realization of the two basic principles of democracy.

## **3.2 Previous Empirical Findings on Democracy and Development**

Lipset (1959) was one of the first to look at the possibility of a casual relationship between economic growth and democracy. He promoted the idea that as a regime experienced economic growth, a transition to democracy became more likely. Ever since Lipset, the relationship between economic growth and democracy has been the subject of a heated debate.

A much quoted study on the field of democracy and economic growth by Przeworski and Limongi is the article "Modernization: Theories and Facts", published in 1997. In this article, the authors examine two theories of economic growth and democratization in order to examine the resilience of democracy. In relation to Lipset's



hypothesis that democracy is dependent on economic growth, Przeworski & Limongi (1997, 156-157) find two reasons for this potential relationship. One is endogenous; that democratic governance becomes more likely as countries develop economically. The other is exogenous; that democratic governance establishes itself independently of the level of economic development, but is more likely to survive in developed countries. Their findings suggest that the emergence of democracy is independent of the level of economic development, but it has a greater chance of survival if it has been established in an affluent country (Przeworski & Limongi 1997, 166). The authors find that the emergence of democracy can happen at any level of economic development; thereby finding no support for the endogenous explanation. They also find that when established, the chances of survival increase with the level of economic development; thus finding support for the exogenous explanation on the relationship between democracy and economic development (Przeworski & Limongi 1997, 177).

Boix & Stokes (2003) challenge the conclusion of Przeworski & Limongi (1997), however, and argue that endogenous democratization also possesses explanatory power. They find evidence that there are certain "thresholds" of income levels that make countries more likely to embark on a democratic transition. However, this threshold has varied over the years, and they find that the threshold is much higher today than it was before 1950 (Boix & Stokes 2003, 540). They propose that income and economic equality was reached at a lower level of economic development before the 1950s, yielding a stronger endogenous democratization effect before the 1950s than after (Boix & Stokes 2003, 544).

Turning to the reversed causal relationship; whether democracy contributes to increased levels of development, Przeworski & Limongi (1993) has written one of the most cited contributions in the debate. They find no evidence in the direction that democracy fosters economic growth, nor that democracy hinders economic growth. The authors point to the fact that there exists little theory on the determinants of economic growth in general, making it even harder to pinpoint the effect of politics (Przeworski & Limongi 1993, 64). They highlight the political differences between regimes that have experienced economic development, and draw the conclusion that it is not regime type (democracy or autocracy) *per se* that makes the difference in how a country performs, but something else (Przeworski & Limongi 1993, 65). However, what that else is, remains unresolved. A few arguments are proposed as to how regime type could affect economic growth, including property rights, pressures for immediate consumption, and the autonomy of dictators. To summarize the statistical findings on the field, they compare 18 statistical studies and 21 findings where eight studies found evidence in favor of democracy, eight found evidence in favor of authoritarianism, and

five discovered no difference (Przeworski & Limongi 1993, 60). Their results and conclusions indicate "that political institutions do matter for growth, but thinking in terms of regimes does not seem to capture the relevant differences" (Przeworski & Limongi 1993, 51).

However, Knutsen (2011a) takes a closer look at the study of Przeworski & Limongi (1993) and re-evaluates their theoretical framework. He argues that the elements included by Przeworski & Limongi (1993) in a democratic effect on economic growth are more positively correlated with democracy than assumed. His general finding is that democracy does indeed contribute to economic growth, and that the empirical evidence point towards a "democratic advantage" in creating economic growth and prosperity.

When looking at the debate on the provision of public goods and regime type, Baum & Lake (2001) investigate whether democracy enhances the provision of certain public goods related to education and health care. They promote the hypothesis that democratic regimes earn less monopoly rents, and provide a higher level of services than autocratic regimes. Their results support this hypothesis, and they conclude that democracy has indeed had an impact on people's lives and contributed to a higher level of well-being. Other empirical contributions that have examined the effect of democracy on the social spending on education, health and social security compared to that of non-democratic regimes reach the same conclusion (see e.g. Avelino, Brown & Hunter 2005, Rudra & Haggard 2005, Kaufman & Segura-Ubiergo 2001, Besley & Kudamatsu 2006, Nooruddin & Simmons 2006). The overall findings suggest that democracies do, but only to a certain extent and with varying ability, provide a higher level of public goods and social spending than non-democratic regimes.

### **3.3 Theoretical Point of Departure**

My basic argument in this thesis is that the different regime types provide different incentives for how and where to invest; democracies and non-democracies allocate resources differently. The different functions of political mechanisms in a democracy and an autocracy ensure that desire for political survival results in poverty alleviating aid allocations in democracy, but not necessarily in an autocracy. While democracies invest the resources, including foreign aid, in poverty reducing projects to increase the likelihood of political survival, non-democracies invest the resources in promoting the regime's own position of power. In explaining why democracies will allocate aid more effectively than autocracies, I take advantage of and base my argument on existing theory in the literature of the provision of public goods and redistribution of resources in different regime types. More specifically, my theoretical point of departure will be

Bueno de Mesquita, Smith, Siverson & Morrow (2003), Sen (1981, 1999) and Meltzer & Richards (1981).

### **3.4 Selectorate Theory**

Bueno de Mesquita et al. (2003) develop a theory that attempts to explain how regime institutions account for the provision of public goods. The first assumption of the theory is that all political leaders seek to maximize their time in office. Furthermore, it assumes that all polities are dependent on two institutions; the selectorate and the winning coalition. The winning coalition is the segment of the population the leader is dependent on to stay in power. The selectorate is a collection of individuals "from which a leader draws supporters to form a winning coalition" (Bueno de Mesquita & Smith 2009, 314). Leaders must maintain the support of the winning coalition or risk being deposed. Democratic states typically have a selectorate existing of all adult citizens and a winning coalition made up by a relatively large part of this selectorate. Autocracies, on the other hand, have relatively small winning coalitions, while the selectorate can vary greatly. In order to increase the likelihood of political survival, incumbent leaders buy the coalition's support by allocating the state's resources between private goods and public goods. Public goods provide benefits for all members of society, while private goods only provide benefits to members of the coalition. The relative size of the winning coalition is decisive in how resources are allocated between private and public goods. As leaders are motivated by the desire to stay in office, they will allocate resources to reward its coalition members. When the coalition is small, state resources can be utilized to attain private goods and provide a corresponding high level of benefits for the members of the coalition. However, private goods become an increasingly ineffective and expensive reward mechanism as the coalition size increases. In fact, it is the provision of public goods that proves the most efficient when coalition size is large. As summarized in Smith (2008, 780) "Leaders choose between a public goods or a private rewards policy focus depending upon how many supporters they need to survive in office".

#### **3.4.1 Selectorate Theory, Foreign Aid and Conditionality**

Bueno de Mesquita and Smith apply their theory to the allocation of foreign aid in their articles from 2007 and 2009. As highlighted by Bueno de Mesquita & Smith (2009, 36-337), selectorate theory accounts for a number of other political, economic and social phenomenon, making it an attractive model for the examination of aid. The inclusion of endogenous institutional changes in the theory means that it accounts both for the occurrence of aid, and for its political consequences.

In these articles, they model how the size of the winning coalition influences trade-offs between policy concessions and aid, as well as examining decisive determinants in aid transfers between donors and recipients. They argue that the willingness to approve policy concessions for aid is dependent on to which degree the leader can compensate his supporters for the potential losses such a concession would mean. When incumbent leaders rely mostly on public goods to reward their supporters, implying that coalition size is large, compensating for potential losses becomes increasingly difficult. It is much easier for leaders of small-coalitions to provide compensation, as they rely more on private goods to retain office. The model provides three predictions; firstly that aid is given by wealthy, large-coalition systems; secondly that the most likely to receive aid are relatively poor small-coalition systems; and thirdly, that if the country receives aid, the amount of aid is likely to increase as the country's coalition-size, wealth and policy salience increases (Bueno de Mesquita & Smith 2009, 309).

One implication of selectorate theory with regards to aid is that it suggests that corrupt practices are an essential part of donors' decision to provide aid, as well as being in the interest of corrupt leaders to receive aid (Bueno de Mesquita & Smith 2009, 335). According to the theory it will be easier to enforce policy concession in countries with small coalitions; reflecting success back on the donor government. The general conclusion is that aid transfers in exchange for policy concessions prolong the survival of leaders in both recipient and donor countries, while harming the citizens of the recipient nation by helping autocratic leaders hold on to power and enforcing policies they did not ask for (Bueno de Mesquita & Smith 2009, 336). In this regard, selectorate theory presents a depressing picture of the effectiveness of aid in alleviating global poverty.

In the articles from 2007 and 2009, however, the authors measure the effectiveness of aid in accordance with policy implementation, not to the degree it reduces poverty. In this context, aid effectiveness is measured by how quickly, or how well, one policy is implemented. Consequently, it examines the determinants of which countries are regarded as strategic cooperation partners, as well as the inconvenience of the leaders of different regime types to accommodate for the conditions tied to the aid. Bueno de Mesquita & Smith (2009, 2007) argue that autocracies will follow through on policy concessions in exchange for aid as long as the compensation to its followers for the changes in policy is reasonable. Following the logic of Wintrobe (1990, 1998), and assuming that autocratic leaders use the excess resources on private consumption, unconditional aid might not work in autocracies while conditional aid can be influential at promoting the desired reforms. In democracies, on the other hand, conditional aid might not work because the compensation to the leader's followers will be too ex-

pensive when the coalition is large. For this reason, selectorate theory predicts that conditional aid will be better at promoting reforms in autocracies than in democracies.

However, Bueno de Mesquita & Smith (2009, 2007) assume that the policy concessions and reforms promoted by aid conditionality is bad for the citizens of the recipient country. If it is not, however, aid conditionality can also work in democracies, as the compensation to supporters might not be necessary as the policy concession includes a change for the better for the supporters. As a matter of fact, and quite contrary to the theory's predictions, suggestions have been made that conditionality will work better when the recipient country is democratic, because they are more dependent on the continuation of aid flows than autocratic regimes (see e.g. Montinola 2010). Political competition compels democratic leaders to spend all the aid at once, while autocratic leaders are able to stockpile the aid, saving it for a rainy day. Montinola (2010) argues that the willingness to comply with policy concessions is dependent on whether aid promotes leaders' political survival; aid flows therefore have a larger impact on the political survival of democratic leaders than the political survival of autocratic leaders (Montinola 2010, 360-361). This line of argument, however, assumes that there is a bigger political loss in not receiving aid than in implementing policy concessions for democratic leaders. If the political loss in implementing the policy concessions is bigger than the political loss in not receiving any more aid, the predictions from selectorate theory will still be valid.

The theoretical arguments presented above lead me to believe that there are three inferences that can be drawn from selectorate theory to the context of aid conditionality and democracy in this thesis, given that the implementation of the aid is fully monitorable.<sup>1</sup>

Firstly, as both theory and empirical evidence predict that democracies will provide more public goods than autocracies, it is logical to assume that even when aid is unconditional it will be spent on public goods in democratic regimes. The depressing picture painted by Bueno de Mesquita & Smith (2009, 2007) is based on the relationship between regime type and *aid conditionality*, and selectorate theory has not examined to

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<sup>1</sup>This is a necessary assumption for testing the implications of selectorate theory in this thesis. However, it might be difficult for the population of foreign governments to control and monitor the aid flows because the process might be far from transparent and available for all to investigate, thereby making it harder to hold politicians and other government officials responsible for the use of aid. Especially if the aid is given on conditional grounds, the population and the voters might have substantially less influence than what is assumed here, further removing the ability of the population to hold a decisive vote in the allocation of aid. This highlights the need for further research on the general effect of conditional and unconditional aid; more so than what could be done in this thesis because of both time and resource constraints.

which degree unconditional aid influence the recipient government and citizens. I argue that the provision of unconditional aid provides a much more optimistic picture of aid effectiveness in regards of poverty reduction in democratic regimes. The predictions of the theory is based on the fact that donor countries want recipient countries to fulfill policy reform, and this is easier in autocratic regimes. Donors therefore prefer to not give aid to democratic countries, where the policy reform is more difficult to implement. However, if the aid was unconditional, it removes any hidden agenda or strategic consideration of the donors with regards to policy reform, and therefore gives a clearer picture of how effective aid has the potential of being in reducing poverty. I therefore argue that unconditional aid will be more effective in alleviating poverty in democracies than in autocracies.

Secondly, unconditional aid will also be more effective in alleviating poverty than conditional aid in democracies when the condition for aid is regarded as a public bad for the leader's supporters. With a public bad, I mean a policy that is perceived to be detrimental to the interest of the local population. The often cited failure of aid conditionality has to a large degree been attributed to the fungibility of aid and commitment problems by both the donors and recipient countries (see e.g. Montinola 2010, Collier 1997). Recipient countries just did not believe that donor threats were serious, and therefore had little incentive to implement the promised reforms (Collier 1997, 59). Another important point is that conditions imposed by donor countries often ignore or neglect the local context. The lack of adaption to the local environment and the failure to take into account local knowledge, have proven to have potentially grave consequences for recipient countries. One illustrative example is provided by the structural adjustment programs of the World Bank and the IMF in the 1980s and 1990s, as well as more recently liberalization and market reform conditions (Haggard 1985, Ivanova et al. 2001, Dollar & Svensson 2000).

A related implication of the failure to adapt to local contexts is the disregard of the sovereignty of the recipient state. As pointed out by Bueno de Mesquita & Smith (2009, 2007), the citizens in the recipient state have little say in the formulation and implementation of the policy conditions, especially so in autocracies. However, individual aid projects can be regarded as a breach of state sovereignty also in democracies. This results in a lack of ownership over aid programs, thereby decreasing the commitment to making it viable (Collier 1997, 63). Bueno de Mesquita & Smith (2009, 2007) are therefore on relatively safe grounds when claiming that policy concessions in exchange for aid is generally perceived as a public bad. By the same token, this challenges the conclusion of Montinola (2010) who assumedly perceives the required policy condition as a lesser evil than the abrupt interruption of aid flows.

Thirdly, if the policy concession is considered a public good, however, then conditional aid should be just as effective in reducing poverty as unconditional aid in a democratic regime. Thus, the crucial point is whether the concessions for aid are perceived to be beneficial or detrimental to the voters.

### **3.4.2 Aid Effectiveness in the Context of Poverty Reduction**

Given the inferences mentioned above, aid will be the most effective in alleviating poverty in democratic regimes when aid is unconditional or considered a public good. When the conditions for aid is considered a public bad, democratic leaders will, according to selectorate theory, have greater difficulties in implementing the aid project because of compensation to their followers. Under such circumstances, conditions for aid will therefore be more easily implemented in autocratic regimes.

This suggests that an overall implication of selectorate theory in relation to poverty reduction is that aid (if not dictated by donor interests) will be more effective in large coalition regimes, where large parts of the additional resources from aid are allocated to public goods, and only a small amount of resources are available for discretionary use by the leader (Bueno de Mesquita & Smith 2007, 280). Democracies, which tend to have large coalitions, are more likely to provide public goods than autocracies, which traditionally have had small coalitions and have therefore preferred to allocate state resources towards private goods. The empirical literature support this theoretical framework, and strong evidence suggest that democracies indeed provide a higher level of public goods than its autocratic counterpart (see e.g. Baum & Lake 2001, Przeworski et al. 2000, Nooruddin & Simmons 2006).

I argue that the fact that democracies provide more public goods than autocratic states, indicates that democracies will be more effective in allocating the resources from aid towards poverty alleviation. The resources from aid are more likely to go towards the provision of public goods in democracies than in an autocratic state; and this provision will affect the level of poverty as the people living in extreme poverty will have access to a minimum level of basic services. It will increase the availability and accessibility of clean water, of public education and health care, eventually providing the poor with the skills and security they need to escape poverty.

It follows that in the context of aid's overall effect on poverty reduction, selectorate theory predicts that aid will be more effective in democracies than in autocracies. Notwithstanding donors influence on the application of aid money, democratic leaders will direct the aid, conditional or unconditional, towards the provision of public goods in order to maximize the likelihood of political survival. Autocratic regimes, on the other hand, will distribute the aid through private goods, thereby directing the aid

away from poverty alleviating policies. I therefore argue that aid will be the most effective in a democratic environment - whether this aid is unconditional or conditional. From the abovementioned theoretical inferences, I arrive at my main hypothesis to be tested in the statistical analysis:

**Hypothesis I:** Aid is more effective in alleviating poverty in democratic regimes than in non-democratic regimes.

### 3.4.3 Empirical Implications

Selectorate theory also provides more detailed empirical implications, which are presented here and examined in the case study. The mechanisms accounted for by Bueno de Mesquita et al. (2003), is the selectorate and the relative size of the winning coalition. The first implication to be examined in the case study is therefore that the relative size of the winning coalition is decisive in the allocation of aid. More specifically, it implies that a relatively large winning coalition promotes the distribution of aid as a public good. However, in countries where population groups are clearly separated into distinguishable territories, the provision of goods is more likely to be focused on the geographical area where the support of the winning coalition is rather than being equally distributed to all areas. In such cases it can be much easier to focus the provision of public goods to only one or a few segments of the population. Especially where social or political divisions within the population are coinciding with the geographical positioning of voters, goods will only be provided to the segments of the population necessary to ensure political survival for the party in power. The distinction between who to reward and not, is easier to make when the geographical positioning of voters physically separates the source of support from the source of opposition, even if the winning coalition is large. Thus, the relative size of the winning coalition might not have the same effect in states where voters are clearly separated into different areas, thus making it relatively easy to isolate the political support and the subsequent provision of goods.

Only when the winning coalition cannot be sustained on the support from only one or two geographical areas, where the leader is dependent on general support through all divisions, will goods truly be of a public nature, and not a local one. A further implication is therefore that a relatively large winning coalition does not necessarily lead to the provision of public goods when the political support and the political opposition are physically separated in different geographical areas. Under these circumstances, the relative size of the winning coalition is decisive for the allocation of local goods, not public ones. To ensure the provision of public goods, the leader must be dependent on support from all geographical segments of the voters. An implication from the



theory is therefore that the allocation of aid will be in line with what is conceived as necessary for political survival by the party in power.

The relative size of the winning coalition is based on the size of the support needed to sustain a leader in power. A political party is dependent on a certain number of supporters in the selectorate to sustain a winning coalition large enough to stay in or gain power. In democracies, this support is materialized through elections. The size of the coalition is decided by the support a party obtains in elections. Moreover, in a two-party system, the incentive for the political party in power to expand its winning coalition is in proportion to the relative size of the support for the opposition. The more support the opposition receives, the more the party in power needs to expand its own winning coalition to remain in power. The smaller the opposition is, the less incentive does the leader have to attract new voters and expand his winning coalition. If political parties are in competition over the voters, there is a greater likelihood that the winning coalition will be large as it is a necessity for the political party in power to have a larger coalition than the opposition party. An implication of the theory is therefore that democratic elections ensure that the desire for political survival enhances the struggle for votes; and the political struggle for votes ensures the expansion of the relative size of the winning coalition. In accordance with the above discussion, one of the ways political parties/the government gain votes and win elections is to provide public goods and redistribute aid. Another important implication is therefore that elections promote a political competition favorable to a fair and equal distribution of aid.

From these implications of selectorate theory certain empirical findings from the case study can be expected. Political divisions in Zanzibar are in line with the geographical positioning of voters, with each political party having the majority of the support from one island; CCM on Unguja and CUF on Pemba. With CCM in government since 1964, one expected find is therefore that the provision of public goods, as well as foreign aid, in Zanzibar has largely been directed towards the largest island, Unguja, where most of the support for CCM can be found.

Selectorate theory, however, also provides an explanation for why the cable was implemented on Pemba when most of CCM's support can be found on Unguja. Given the growing support for CUF, I expect to find that the competition for voters was more fierce before the 2010 elections than in previous elections. In a two-party system, like the *de facto* political system in Zanzibar, this might have contributed to CCM needing to attract new voters to increase the likelihood of political survival. I therefore expect to find that CCM needed to expand their winning coalition because CUF posed a threat to the political survival of the party. I further expect to find that the CCM govern-

ment implemented the cable to attract new voters on Pemba. Another implication and expected find is that elections contributed to the decision of implementing the cable on Pemba, and that the struggle for political votes was instrumental in ensuring its efficient implementation.

Furthermore, the grant from the Norwegian government was conditional on the implementation of the cable (Informant 1 [Interview]). Thus, it provides an interesting case for studying the effects of conditional aid in democracies. The process with the cable is framed and promoted as an example of good governance and cooperation, providing the people living in poverty with substantial efforts at development. An expected finding is therefore that the cable was considered a public good and not a public bad, as assumed by Bueno de Mesquita & Smith (2009, 2007).

### **3.5 Theoretical Modifications: Political Rights and Civil Liberties**

One of the most cited reasons for a democratic effect on improved living conditions, is the "Dahl theorem". It asserts that contested elections and a minimum level of political and civil rights and liberties ensure that the government is held accountable to its citizens (Dahl 1959). Because democratic rulers and politicians are judged retrospectively, they cannot behave in a self-interested manner without risk losing office in the next election. The incumbents would therefore prefer to extract lower rents for a longer period, rather than higher rents during a short period (Cheibub & Przeworski 1997, 120-121). Citizens of democracies have the opportunity to exert pressure from below by the virtue of their vote and political mobilization, as opposed to citizens of autocracies (Sen 1994, Banik 2010, 108). The democratic system of checks and balances, as well as a functioning multiparty political system, can put controls on and criticize government inaction and failures, leading to a government that is attentive to the pressure from below (Banik 2007, 16). The system of checks and balances both guarantees rights and entitlements to citizens and restrain arbitrary use and abuse of power (Bova 1997). Accountability, meaning that the government will be held responsible for its actions, perhaps by not getting re-elected or being publicly criticized by the opposition, is therefore prevalent in democracies but not in autocracies (Banik 2007, 23). Democratic institutions decrease the probability of predatory behavior by incumbent leaders, and the accountability of the government stems directly from the fact that elections are held and respected (Banik 2010, 111). As highlighted by Knutsen (2011a, 26): "In democracies, leaders who try to engage in predatory activities are more likely to be detected because of freedom of media, more likely to be stopped by other institutions like the

legislature and courts, and more likely to be thrown out of office in the next election".

According to Sen (1999), democracies are more responsive towards its citizens than autocratic regimes, because democratic leaders fear not being re-elected. In addition to the holding and respecting of regular elections, a minimum level of political rights and civil liberties ensures that democratic institutions are used in the manner, and for the purpose for which they were designed and intended; it is political freedom that provide the democratic institutions with substance and real meaning.

Linking selectorate theory to the "Dahl theorem" and the findings of Sen (1981, 1999), I argue that democracies with a minimum level of political rights and civil liberties are more effective at allocating foreign aid towards poverty reducing initiatives than electoral democracies. Selectorate theory considers the relative size of the winning coalition to be the most important mechanism in the effective allocation of aid. As discussed in the previous section, in a democracy the relative size of the winning coalition is decided by the political support the government obtains in an election. The theory of Sen (1999) promotes the idea that other mechanisms might be important for effective aid allocation. In fact, it implies that without a minimum level of political rights and civil liberties, the mechanisms proposed by selectorate theory are rendered ineffective in ensuring a reduction in poverty from aid.

Instead of including coalition size, as selectorate theory would command, I have therefore chosen to use the term of democracy in my hypothesis - as well as through the rest of my thesis - rather than coalition size. Institutions that ensure the accountability of the government to as large a part of the population as possible is contingent on the maintenance and upholding of a certain level of political rights and civil liberties. This leads me to my second hypothesis to be tested in the statistical analysis, on the importance of political and civil rights in the allocation of aid.

**Hypothesis II:** Stronger protection of political rights and civil liberties increases aid effectiveness.

### 3.5.1 Empirical Implications

As with selectorate theory, the ideas of Sen (1981, 1999) also provides more fine-grained implications to be examined in detail in the case study. When the relative size of the winning coalition is relatively large, but does not automatically lead to the provision of public goods, other mechanisms must ensure the equal and fair distribution of aid. An implication of Sen (1981, 1999) in relation to aid effectiveness, is that accountability and political rights and civil liberties are decisive mechanisms in effective aid allocation and implementation.

There are two general forms of accountability; horizontal and vertical. Horizon-

tal accountability is ensured through strong and stable political institutions, such as a strong parliament, an independent judiciary and regular elections. Vertical accountability is when interactions between elected officials and citizens happen through more direct routes, ensuring transparency in all aspects of policy making (O'Donnell 1998). A free press is of paramount importance for the maintenance of vertical accountability, along with contested elections (Fox 2000). The two forms of accountability accounts for different mechanisms in keeping the government responsible and responsive, but weak institutions under horizontal accountability can easily prove to put limitations on vertical accountability as well (Fox 2000, 1). One implication with regards to the role of accountability is that formal and stable political institutions ensure accountability of the leadership as the leader must act in accordance with the interest of the voters to increase the likelihood of political survival. Another implication is that elections and a free press ensures that the government is held responsible for its decision, as it provides a direct link between the governed and the governing. Moreover, transparency works to improve the accountability of the government and the processes it implements, and decreases the barrier for participation in political processes. The result is that accountability leads to more responsible and responsive leaders, making democracies more well-equipped to provide efficient aid allocation than non-democratic regimes. However, when the political institutions are of poor quality, democratic mechanisms such as elections and a free press lose their ability to generate distributive outcomes. Accountability is therefore instrumental in ensuring effective allocation of aid.

However, in many of the countries in the sample, accountability and responsible behavior of the leadership is still merely a theoretical possibility. The politics of low-income democracies does not operate independently, but is highly contingent on historical and geographical factors (Bratton & van de Walle 1997). Many of the democracies in developing countries today are so-called semi-democracies or low-quality democracies, where the political processes do not work according to the design of the political institutions (van de Walle 2001, 236). In many poor democracies, democratic attributes are somewhat of a recent phenomenon, where democratic practices are still being developed. Some of the new democracies have also kept parts of old structures of power alive, and incorporated it into the new democratic structures; the current democratic institutions are shaped by the institutional legacy (Bratton & van de Walle 1997, 234). Such democratic systems, especially frequent in Africa, have numerous shortcomings, including weak opposition parties, intimidation of political opposition and a lack of leadership turnover (Bratton & van de Walle 1997, 81-82). This goes to show that when democratic institutions go unchecked and unconsolidated, the leaders have little incentive to stick with the democratic practices. The prevalence of neo-patrimonial

rule in post-colonial Africa, has led to a system where the formal rules of electoral democracy overlap with informal personal ties between a country's "big men" (Bratton & van de Walle 1997, 82). Bratton & van de Walle (1997, 233) named this new form of government "big-man democracy", where the formal institutions of democracy co-exist with neo-patrimonial political practices to form and define national politics. The economic situation in many low-income countries is the result of decades of economic policies designed to facilitate rent-seeking and clientelism, and newly formed democratic regimes cannot escape this heritage and its inherent limitations on the prospect for political change.

Given the potentially low quality of democratic regimes in countries that receive development aid, democratic mechanisms might not work according to its intention, if it works at all. Political rights and civil liberties might therefore not be fully developed and implemented, leading to questions of democratic validity. A further implication of Sen (1999), is that political rights and civil liberties are prerequisites for the proper functioning of democratic mechanisms, such as elections, and thus also meaningful political participation. It is the presence of political rights and civil liberties that make elections an effective mechanism in the distribution of aid in recipient countries. It follows that without political rights and civil liberties, elections will prove an inefficient mechanism in the effective allocation of aid.

The above discussion has certain empirical implications for the expected findings from the case study in chapter 7. First of all, given that the project is considered an undisputable success, and given the importance of accountability in effective aid allocation, I expect to find that holding the leadership responsible and accountable has been decisive in the effective implementation of the subsea cable from Tanga to Pemba. Secondly, I expect that the presence of both vertical and horizontal accountability contributed to meaningful political participation and processes. Thirdly, according to the theory, it is likely that I will find that there was a minimum level of political rights and civil liberties that was instrumental in creating enough political pressure from below to tip the decision in favor of laying the cable. If the theory of Sen (1999) is correct, I further expect to find that it was the presence of political rights and civil liberties that drove the political competition and the subsequent decision of the CCM to expand their winning coalition. Thus, the theory predicts that it was the presence of political rights and civil liberties that ensured that elections achieved the political competition necessary for the allocation of aid to the cable project.

### 3.6 Redistribution in Democracies

The model presented by Meltzer & Richards (1981) might be considered an interesting extension of selectorate theory and Sen (1981, 1999), and implies that more inequality leads to more redistribution in democracies. I argue that this theory gives an explanation to why democracies should allocate resources to the poorest segments of the population, and hence achieve a more effective use of the resources from aid.<sup>2</sup>

According to the theory of Meltzer & Richards (1981), the decisive voter in a democracy is portrayed as the median voter. As long as his income is lower than the mean income, there will be redistribution from the rich to the poor and middle-income voters. It is the tax rate that determines the level of redistribution; high tax levels lead to more redistribution, low tax levels lead to less redistribution. The assumption is therefore that if the decisive voter is poor (with an income lower than the mean income), he would want to raise taxes; and if the decisive voter is rich (income level higher than the mean income) he would choose a lower level of taxation. When the mean income rises more than the income of the median voter, there will be more redistribution, and vice versa (Meltzer & Richards 1981, 924). As it is based on the level of inequality in income distribution, it implies that higher inequality in income levels leads to more redistribution. Meltzer & Richards (1981) point out that in regimes with majority rule, the voter with median income is the decisive voter. This implies that democracies will redistribute its resources to a larger degree than autocracies.

Acemoglu & Robinson (2000) expand the theoretical model of Meltzer & Richards (1981), and argue that democratization shifts the identity of the median voter; in autocracies the median voter is part of the rich elite, while in democracies the median voter is much poorer and part of the larger masses. Non-democracies are defined as regimes in which an elite hold power while the poor are largely excluded. Democracies, on the other hand, are regimes built around political equality where the poor have the ability

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<sup>2</sup>Foreign aid classifies as "un-earned" income, meaning that the state has obtained the resources without using taxation of the population in the process (Moore 2001). A general problem here, as pointed out by Morrison (2007), is that the models of Meltzer & Richards (1981) and Acemoglu & Robinson (2000) rely on taxes as the redistributive mechanism. However, when a country receives aid and similar un-earned income, marginal revenue on government spending decreases. Morrison (2007) argues that this leads to a situation where the poor might want to keep much more of his income rather than having it taxed. In some cases where the aid is benefiting the poor, a decrease in tax rate might in fact *reflect* the wishes of the poor. In this situation, the models of Meltzer & Richards (1981) and Acemoglu & Robinson (2000) are inadequate. Notwithstanding this important implication, however, for the purpose of this thesis, I assume that the resources from aid alone is not enough for the poor to want a zero tax rate. This is because this thesis examines the overall effects of aid and democracy and not the specific effects of aid at certain levels of taxation. Interesting enough, it is the topic for another study.

to press their demands more effectively. In other words, they focus on who controls political office.

### 3.6.1 Empirical Implications

Meltzer and Richards' model is somewhat static and unidimensional. There is no room for redistribution from the poor to the rich, or from the rich and poor to the middle-classes; the only redistribution is from the rich to the poor and middle-classes (Wintrobe 1997, 137). This implies that the potentially arbitrary behavior of dictators is not captured in the model, and the effect of democracy might therefore appear smaller than it actually is. Moreover, a crucial part of both the model of Meltzer & Richards (1981) and the model of Acemoglu & Robinson (2000) is that democracy makes redistribution credible; implying that democracies will automatically redistribute because the median voter is poorer than the median voter in autocracies.

Knutsen (2011b), however, argue that the political reality is much more complex. The models imply that if elections were held on whether to redistribute resources to the poorest segment of the population, the majority of the voters would have to be a part of this segment for redistribution to take place. For instance, if this segment is defined as the people living on less than \$ 2 a day, most people would have to belong to this segment if there was to be a chance of redistribution.

However, there are certain general implications that can be drawn from the contributions and examined closer in the case study regarding the role of political pressure.<sup>3</sup> The first implication of the models of Meltzer & Richards (1981) and Acemoglu & Robinson (2000), is that the ability of the population to exert political pressure and influence the government lead to more redistribution of aid in low-income democracies. This is because the general voter will be poor, and if he is decisive for political survival the leaders will ensure the redistribution of aid to his segment. Because of this, the ability of the poor to exert political pressure also implies that more aid is allocated to those segments of the population that are relatively poor in democracies. A third implication follows in that the ability of the poor to press their demand is important for the effective allocation of aid.

Nonetheless, for the model of Meltzer & Richards (1981) and Acemoglu & Robinson (2000) to hold any predictive power, the poor need to stand collected in their desire for poverty reduction. The ability of the poor to press their demand is dependent on their

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<sup>3</sup>The income of the median voter is promoted as an important mechanism in the redistributive qualities of democracies in the models of Meltzer & Richards (1981) and Acemoglu & Robinson (2000). However, for the sake of this thesis, it provides a much too technical and complex mechanism to examine in detail. However, the models highlight the importance of political pressure as a consequence of the ability of the population to demand redistribution; which is the focus from these models in this thesis.

capacity to stand collected. This theory implies that the poor median voter will want to redistribute, but experience has shown that this is not always the case. This assumption has numerous empirical failings, and the poor can make up a large part of the electoral without experiencing a higher level of redistribution. The poor do not necessarily vote as a collected economic group, but are divided along other political dimensions. This can be because the rich and the poor in a country have some sort of alliance, patron-client relationships or ethnic or religious solidarity (Chabal & Daloz 1999, Banik 2007). If the population vote for a party based on social belonging, it decreases the ability of elections to function as a control mechanism on the elected representatives. Politicians might be elected over and over again without fulfilling any of the promises made. This implies that democratic elections might lose some of its intended functions, as political parties are not held responsible or to account for its decisions and actions. As such, a final implication of these models is that the ability of the poor to exert pressure is dependent on their ability to stand united as an economic *and* political group. If they do not, elections might lose its intended and distributive qualities.

The inferences above lead to certain empirical implications for the expected findings from the case study in chapter 7. Firstly, I expect to find that the cable was implemented as a direct result of pressure from the people living in poverty. Secondly, I also expect to find that the reason for the cable's success has been that the government was attentive to the desire of the people living in poverty. Thirdly, as a result of their ability to exert pressure on the government, an expected find is that the cable benefits the very poorest in the community.

### **3.7 Concluding Remarks**

To sum up, I would say that my theoretical framework is threefold. Firstly, I believe - and selectorate theory predicts - that whether aid is conditional or not is irrelevant in democratic regimes if the conditions for aid are seen as a public good, as the additional resources from aid would be spent on the provision of public goods whether these resources were conditional or not. However, if the conditions for aid are seen as a public bad, conditional aid will be ineffective in democratic regimes. Notwithstanding the implications of conditionality on the distribution of aid, however; selectorate theory predicts that the aid will be more effective at alleviating poverty in democratic regimes than in autocratic regimes because the resources from aid will be distributed through the provision of public goods rather than private goods. Secondly, I argue that democracies are better at directing aid towards poverty reducing programs than autocratic leaders because of the presence of accountability and a higher level of political rights and civil liberties. Thirdly, I make the proposition that more aid will be directed at the



people living in poverty in poor democracies because of the influence of the decisive voter.

Selectorate theory make the implication that aid plays an important role in the political survival and motivation of leaders. The theory focus on how economic resources are channeled and what accounts for the distribution of resources in different political systems. One important implication of this theory is that democracies are more likely than autocracies to provide their citizens with a higher level of public goods and services. Basically, an important inference from the theory is that when it is not in the interest of the leader to redistribute resources, aid will have no effect in alleviating poverty. Democratic institutions ensure that redistribution of resources, including aid, is a crucial part of the political survival of leaders, and hence one of the most important reasons for political power. Sen (1999) adds to the theoretical contribution of Bueno de Mesquita et al. (2003) in highlighting the importance of political rights and civil liberties in keeping the government responsive and responsible. In cases where a large winning coalition does not automatically lead to the provision of public goods, other mechanisms become all the more important; such as the presence of a minimum level of political rights and civil liberties. The model of Meltzer & Richards (1981) bring a different perspective into the theorizing about a democratic effect on poverty and aid effectiveness. Instead of looking at the motivation or survival of leaders, they focus on the position of the electorate and how this affects the redistribution of resources within a community. Democracies have a greater likelihood of redistributing a larger proportion of the state's resources as the general voter is poorer than the elite.

All in all, institutional limitations in democracies restrict the level of private consumption, and thus ensure a higher provision of public goods, as well as a higher level of redistribution. Linking the three contributions together, I argue that this theoretical framework presents an overall picture of democratic regimes' superior ability to reduce poverty levels in comparison with non-democratic regimes and to allocate aid more effectively than autocratic regimes. Selectorate theory highlights the importance of the relative size of the winning coalition and the role of elections in democratic regimes; Sen (1981, 1999) points out the decisive role of political rights and civil liberties in making elections meaningful and creating a government that is accountable to the people; and Meltzer & Richards (1981) highlight the importance of political pressure from the people living in poverty; as crucial mechanisms in the effective allocation of aid. These mechanisms provides a justification for a democratic effect and are the basis for examining how democracy affects aid effectiveness.

The three theoretical contributions are all related to one another by several political steps, from the political pressure of the poor and the growing support of the CUF,

to the subsequent expansion of the winning coalition and the importance of political rights and civil liberties in this process. I therefore expect to find that the pressure experienced by the CCM was rooted in the presence of political rights and civil liberties, which again ensured the competitiveness of elections and the distribution of aid to the poor.

# Chapter 4

## Research Method

### 4.1 Introduction

As revealed in the previous chapters, the relationship between aid and poverty is both a complex one and one where conclusions are hard to draw. In attempting to account for this, I apply both quantitative and qualitative methods to reveal and explain the hypothesized relationship in this thesis; that between democracy and aid effectiveness. More specifically, I apply both a statistical analysis and a case study to answer my research question.<sup>1</sup>

The difference between case studies and statistical analysis has traditionally been encapsulated in the number of observations analyzed. Case studies were regarded as "small-N" studies, while statistical studies were characterized as "large-N" studies (George & Bennett 2005, 17). According to George & Bennett (2005, 6), the methodology of statistical analyses and case studies differ in important ways, from the selection of cases to the operationalization of variables. However, this does not mean that they are mutually exclusive, but rather that they complement each other, and should be used together when one measure alone is unsatisfactory. Case studies have their strengths where statistical analysis has its weaknesses, and vice versa. While statistical analyses are good at discovering causal effects and in their ability to make generalizable assumptions and inferences, case studies are better at accounting for causal mechanisms and have high levels of conceptual validity (George & Bennett 2005, 19).<sup>2</sup>

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<sup>1</sup>According to George & Bennett (2005, 17), a "case" is defined as "an instance of a class of events", where a class of events can be any phenomenon within the social sciences. A "case study" is thus "the intensive study of a single case where the purpose of the study is - at least in part - to shed light on a larger class of cases (a population)" (Gerring 2007, 20). Although a case study can apply statistical methods in its analysis, I refer here to case studies, following Gerring (2007, 31), as intensive within-case analysis in contrast to large-N analyses.

<sup>2</sup>A case study research design makes it easier for the researcher to identify appropriate indicators for

This means that while the statistical analysis can provide indications of a general effect of democracy on aid effectiveness, the case study can examine how democracy contributes to such an effect, strengthening the internal validity of the analysis.<sup>3</sup>

Nevertheless, when drawing general conclusions of a democratic effect and its origins, case studies are generally not very well suited. It is difficult to determine the representativeness of the case used in this thesis as it is only one aid project of a sample that is much larger. Thus, the external validity of the case study is by definition much smaller than for the statistical analysis.<sup>4</sup> Combining the two research designs therefore attempts to account for the other method's flaws and limitations. It improves the validity of my conclusions by strengthening both the external validity and internal validity, hopefully providing a contribution to the debate over and further research on aid effectiveness.

## 4.2 Why Apply Both?

My motivations for applying both is to clarify the causal path between democracy and aid effectiveness. Earlier quantitative empirical findings on the relationship between aid and development have proven to be less than robust. Many of the analyses are riddled with more or less important flaws, and the relationship seen too complex to be fully clarified using quantitative methods alone. There is a good chance that in this case and with this relationship, the causal path is simply too complex and difficult to be accurately specified by TSCS analysis. Moreover, when considering the conceptual challenges with both democracy and poverty, two very central concepts for this thesis, it might be legitimate to state that the statistical analysis operates with unmeasurable variables or at least variables that are difficult to capture in a single number, contributing to the difficulties in correctly specifying the relationship. The application of a case study provides flexibility in the use of concepts such as democracy and poverty and enables me to explore more fully people's understandings of these concepts, strengthening the conceptual validity of my research.<sup>5</sup>

The complimentary nature of statistical analyses and case studies have resulted in that many scholars have urged for the increased integration of the two method-

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the theoretical concepts, as she is closer to the objective.

<sup>3</sup>Internal validity reflects a research method's ability to establish and prove, to a certain extent, a causal connection between the independent and dependent variables (Gerring 2007, 43).

<sup>4</sup>External validity refers to the ability of a study to generalize its conclusions based on the representativeness of the sample in relation to the population (Gerring 2007, 43).

<sup>5</sup>Conceptual validity refers to the application of concepts that might have different meanings in different contexts and settings. To achieve as high conceptual validity as possible, the measure must be adapted to fit the local context (Adcock & Collier 2001).

ological approaches (Lieberman 2005, Achen & Snidal 1989, Tarrow 1995). Lieberman (2005) argues that the synergy effect of using two different methodological approaches makes the collected analysis more valuable than the sum of each individual part by itself. Starting with a large-N analysis, the analysis can provide the basis for focused case studies and comparisons. The small-N analysis can draw on the findings from the large-N analysis to specify the causal relationship and exclude rival explanations (Lieberman 2005, 435).

Moreover, there are certain aspects of the hypothesized relationship that cannot be tested statistically. The case study's complementary nature makes it well-equipped to illuminate further questions about this relationship. While the statistical analysis tests the hypothesized causal relationship between democracy and aid effectiveness, the case examines the specific mechanisms behind aid allocation within a democracy. This is done to find specific evidence of whether the patterns of democratic organization hypothesized is in fact manifested in reality. The case is included to observe, clarify and assess the plausibility of the observed statistical relationship between democracy and aid effectiveness; it possesses additional theoretical and empirical value that could not be revealed in statistical models.<sup>6</sup> The case study can illuminate political actions and considerations that are not clear from secondary sources and aggregated data. There is a great potential for strengthening the findings, both from previous research and for my analysis, in examining both the causal *effects* of democracy on aid effectiveness and the causal *mechanisms* generating this effect. Indeed, an attribute that ranks high for case studies is their ability to provide valuable insights into the underlying mechanisms (Gerring 2007, 45). Given the weak conclusions of previous research on aid effectiveness, this is a necessary and important precondition in order to be able to say anything meaningful about the democratic effect on aid effectiveness; or perhaps, the lack of one.

### 4.3 The Problem of Endogeneity

One of the more pronounced problems with large-N cross-country research on aid effectiveness, is the endogeneity between aid and development. The previous statistical research might very well yield such non-robust results because of the fact that aid is endogenous to development. In many statistical models this would manifest itself by producing results seemingly disfavoring the effect of aid if it has not been properly ad-

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<sup>6</sup>It is important to highlight that the case study is not a test for my statistical analysis, as it cannot conclusively test the empirical implications of my statistical results by itself. This is because the case has been chosen deliberately based on its value on the independent variables. It is far too unproblematic to find single cases to confirm or disconfirm the theory and the mechanisms at work, to rely on the findings from one case study in order to draw general conclusions.

dressed in the model. Otherwise, the effect displayed might be due to the simple fact that poor countries receive more aid. A clarification of this relationship is therefore utterly important, as statistical results can easily estimate a smaller impact of aid on poverty than what is actually true.

To account for this in my statistical analysis, I apply the Difference GMM model proposed by Arellano & Bond (1991). Although this model probably provides the best solution to the problem of endogeneity in large-N statistical research, it has so far only been used in a few studies on the effectiveness of aid (see e.g. Hansen & Tarp 2001). Thus, this thesis represents an addition to cross-sectional aid research in trying to account for this problem to a larger degree than what has been attempted in the majority of existing research on the field.

The case study provides further steps in ensuring that the problem of endogeneity is minimized. Correlation does not automatically imply causation, and in order to be able to provide a causal explanation about the effects between democracy and the effectiveness of foreign aid, it is just as necessary to understand the causal mechanisms behind this relationship as the causal effects (George & Bennett 2005, 8), especially when considering the problem of endogeneity.

## **4.4 Quantitative Data**

The statistical analysis is the first step in clarifying the relationship between democracy and aid effectiveness. Statistical methods have their strength in making general conclusions about causal effects, and pointing out general tendencies. Large-N research is always more representative of the population than small-N research, increasing the external validity of my conclusions. In this thesis, statistical models are applied in order to clarify the causal effect of democracy on aid effectiveness, hopefully enabling me to draw general conclusions about the effect of democracy on the effectiveness of aid with a certain confidence.

The variables included in the statistical analysis, and the justification for the inclusion, are thoroughly discussed and explained in the next chapter. This section will deal with the statistical model specifications and problems related to the structure of the data and overall foundation for the statistical analysis. Hopefully, this will contribute in making the study more easily replicable and transparent.

The data has panel data structure where country-year is the unit of analysis; one unit of analysis is for instance Afghanistan 2005, another is Afghanistan 2006. This means that the data observes changes in variables over time and over countries; more specifically it constitutes a TSCS analysis. There are 155 countries included in the analysis; all the countries in the world that has received ODA in one or more years in the

period from 1960 to 2011. Appendix A provides a list of the countries included in the sample. In total there are more than 8000 observations. The data for the statistical analysis is mostly collected of aggregated variables from the WDI, but some variables are also collected from other sources, as will be discussed in the next chapter.

The statistical analysis is applied to test hypothesis I and II from the previous chapter; hopefully revealing the general effects of democracy, and political rights and civil liberties, on aid effectiveness. Different measures of democracy are applied, namely the Polity Index and the Freedom House Index (FHI) to examine the differences in effect when highlighting the importance of political rights and civil liberties. The Polity Index constitutes the more limited measure of democracy, while the FHI measures the effect of political rights and civil liberties. By applying the different measures, I am able to examine the effect of democracy when political rights and civil liberties are considered secondary to the effective implementation of aid, and when political rights and civil liberties are considered an intrinsic part of this relationship.

Unless otherwise stated, it is the FHI that is applied as the measure for democracy. An increase on the scale, implies that a country becomes more democratic, while a decrease on the scale means that a country becomes less democratic. It is important to highlight that poverty is undesirable, indicating that a negative estimate means decreasing levels of poverty. Thus, a negative relationship between democracy and aid effectiveness is in fact a good thing, as it indicates that democracy leads to aid being more effective in reducing poverty.

## 4.5 Statistical Analysis

Both the relationship of aid on poverty and of democracy on poverty are controversial and inconclusive. Ross (2006) argues that democracy does not contribute in any significant way to the reduction in poverty levels. His paper suggests that earlier quantitative studies on the relationship between poverty and democracy have ignored important characteristics of the data when finding this relationship. First, country-specific effects are ignored; second, exogenous factors are ignored; and third, missing data has removed important aspects of the data. I try my best to account for these potential dangers, by applying an OLS model with panel-corrected standard errors, a Fixed-Effects model and a Arellano-Bond GMM model with imputed data, as well as including decade dummies for each decade between 1960 and 2011 to account for exogenous trends. Moreover, I account for the problem of missing values by using the procedure for multiple imputation as suggested by Honaker & King (2010), coined Amelia II.

### 4.5.1 OLS Panel-corrected Standard Errors

Given the structure of the data, as well as the diversity of the previous findings in the literature, I apply different specifications as well as different estimators in order to test the robustness of the results and to adjust the statistical model as best as possible to the presumed relationship between aid and poverty. The first estimator is an OLS with panel-corrected standard errors. This is the most basic model, applying less restrictions than the other estimators used in this thesis. The OLS estimator is used on the original data and on the imputed data, giving an indication of the differences in data structure when comparing them. The other estimators are only applied to the imputed data.

With continuous dependent variables, OLS estimators have been shown to be appropriate. However, for this to be true, numerous conditions must be fulfilled (Beck & Katz 1995). The primary characteristic of TSCS data, is its repeated observations within units, in my case countries. Both the temporal and spatial properties of TSCS data produces problems with the use of OLS estimators. Because of interdependencies between observations, biased estimates can result if not controlled for (Green et al. 2001, 441). Descriptive statistics and diagnostics of my variables showed that there were heteroscedasticity and autocorrelation in the data.<sup>7</sup> This affects the standard errors of the models, potentially leading to "extreme overconfidence" in the results (Beck & Katz 1995, 634). Increasing the risk of making errors of type I (rejecting a true null-hypothesis) could imply that my hypothesis testing becomes invalid, as the standard errors are wrong.

Beck & Katz (1995) make the case that OLS estimates of TSCS data often perform well in practical research, even though the estimates may not be optimal. Seeing as the standard errors of OLS estimates might be inaccurate with such data, they propose to hold on to the OLS estimator, while introducing panel-corrected standard errors (Friedrich 1982, 806). To solve this problem and control for heteroscedasticity and autocorrelation in the data, I use panel-corrected standard errors in my OLS estimator (Beck & Katz 1995, 640). However, whether this approach leads to overestimated or underestimated standard errors depends on the sample Beck & Katz (1995). It could therefore render hypotheses testing invalid.

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<sup>7</sup>The total chi-square is 1937.29 when applying White's General Test for Heteroskedasticity. In this test, a high chi-square generally means that heteroscedasticity is present in the data. The p-value for the serial correlation test proposed by Drukker (2003) was 0.0000, indicating the presence of serial correlation.



## 4.5.2 Fixed Effects

The assumption behind the OLS estimation is that the independent variables control for any cross-sectional differences, and if they are not included they are uncorrelated with the predictors that are included in the model. If this assumption does not hold, OLS estimation is unfit (Green et al. 2001). Remembering that the unit of analysis is country-year, this assumption of OLS might not hold. Countries are heterogeneous units, where geographical, historical and cultural characteristics (amongst others) potentially correlated highly with the level of poverty. If any of these country-specific variables affect both the level of poverty, the level of aid and the level of democracy, its elimination from the statistical model leads to omitted variable bias (Ross 2006, 863).

The second estimator applied is therefore a Fixed Effects regressor that control for unobserved country-specific variables that might bias the results. This estimator controls for unobserved heterogeneity between countries when this heterogeneity is constant throughout the period of analysis and correlated to the independent variables in the analysis. The panel corrected standard-errors of OLS estimation might take into account the potential bias of the standard-errors in panel data, but it does not control for unobserved country-specific variables that might affect both the independent variables and the dependent variable. This may cause each country to have its own rate of poverty reduction or intercept (see Green et al. 2001, 442). While in OLS, each country is assumed to have the same intercept, in fixed effects each country is assigned its own (Green et al. 2001, 442). When there are country-specific effects, and when these effects are correlated with the independent variables, regression estimates in OLS will be biased (Green et al. 2001). To ensure that I am in fact capturing the effect of aid and democracy on poverty, I control for Fixed Effects and hence potential unobserved variable bias. Especially with regards to the role of democracy in my analysis, Fixed Effects regressions should be appropriate. This is because it is probable that countries differ systematically in ways that is not captured by this concept.

However, problems of endogeneity between the variables can make Fixed Effects models unreliable, as the variables included in the model will be systematically correlated to the error term. In fact, the Fixed Effects estimator requires strict exogeneity of the independent variables in relation to the error term, because country-specific time averages are used to transform the independent and dependent variables by introducing the time averages of random shocks. If some of the independent variables at time  $t$  are correlated with a random shock at time  $t-1$ , the Fixed Effects estimator is inconsistent (Mileva 2007, Hansen & Tarp 2001).

Moreover, the estimator's ability to control for unobserved heterogeneity that stays constant over time, implies that the Fixed Effects estimator controls for variation *within*

countries, but does not account for unobserved differences *between* countries. It also makes it relatively unfit for estimating the impact of and on slow-changing variables. The level of poverty, along with democracy, might very well be too slow-moving variables for the Fixed Effects regressor to pick up. Thus, it might be very little information for the regressor to estimate the effects from.

Because of the inconsistency of the Fixed Effects estimator that might arise from endogeneity and slowly changing variables, I apply a third and final estimator that accounts for both endogeneity and country-specific effects (Mileva 2007). The GMM-analysis from Arellano & Bond (1991) measures the degree of change in the dependent variable given a change in the independent variables; thereby minimizing the problem of endogeneity.

### 4.5.3 Arellano-Bond Difference GMM

Hansen & Tarp (2001, 556) propose the specific use of GMM in aid regressions, as studies have showed that most of the explanatory variables in the aid literature are endogenous (see e.g. Boone 1996, Burnside & Dollar 2000, Hansen & Tarp 2001). In fact, the non-robust relationship that the literature on aid effectiveness have produced between aid and economic growth, might very well be caused by problems with endogeneity. This implies that the unstable results from different studies might just as well, and quite likely, be caused by the fact that relatively poor countries receive more aid than relatively rich countries (see e.g. Boone 1996). In the statistical models applied in TSCS aid research so far, endogeneity might have contributed to uncertainty over the causal direction of the relationship. This would result in the same estimates, whether aid contributes to more poverty or whether more aid is given to relatively poor countries. Trying to account for this is therefore an important step in clarifying the relationship.

The Arellano-Bond estimator was designed for situations with "1) "small T, large N" panels, meaning few time periods and many individuals; 2) a linear functional relationship; 3) a single left-hand-side variable that is dynamic, depending on its own past realizations; 4) independent variables that are not strictly exogenous, meaning correlated with past and possibly current realizations of the error; 5) fixed individual effects; and 6) heteroskedasticity and autocorrelation within individuals but not across them" (Roodman 2006, 1). These characteristics fit very well with the relationship between aid, democracy and poverty as presumed in this thesis. Especially regarding the first point, as short time-series might lead to bias in the Fixed Effects estimator. Hence, I argue that this is the most plausible model specification for the relationship, and therefore constitutes the main statistical model of my quantitative analysis. The fact that all the three poverty measures indicate the same relationship with this regressor, further

strengthens the validity of this estimator (see Appendix B), and hypotheses testing is conducted with this estimator.

The Arellano-Bond GMM estimator transforms the regressors through differencing; meaning that it subtracts the current value of the variables from the value of the variables at  $t-1$ . Thus, it allows for the assumption that the level of aid is highly correlated with the initial level of poverty (Mileva 2007, Hansen & Tarp 2001). In doing so, it measures the effect of a change in the independent variables on the change in the level of poverty. For instance, the change in the amount of aid received will not likely be caused by a change in poverty levels from one year to the next, but rather the level of poverty in a country. This way, the problem of endogeneity is minimized.

However, when country-specific effects are removed by differencing, there are generally three issues that arise in relation to the consistency of the estimator (see Hansen & Tarp 2001). Firstly, as the country-specific effect are removed, the country means are removed simultaneously. This loss of information could lead to a critical loss of variation in the data; but this depends on the topic and the data. For the use in this thesis, the loss of variation is not critical as it is the rate of poverty reduction/increment of the countries that are compared, not the level. The second issue relates to the timing of the relationship. I have therefore experimented with using different lags, both for the dependent and the independent variables. Hansen & Tarp (2001) showed this to be rather useful. However, using different lags in this analysis showed no significant change in the relationship, resulting in the use of only a one year lag in the models in chapter 6 when the level of poverty is applied as the dependent variable. The last issue, and perhaps the most important in this case, is the potential correlation between the instruments and the error term. Regarding this issue, I have performed the Sargan test for over-identifying restrictions in all models to ensure the consistency of the GMM estimator throughout the analysis. The null hypothesis under this test is that the instruments are not correlated with the error term in the first-difference equation, and thereby valid. A significant result, could be because the instruments included in the analysis are not sufficient to account for the endogeneity in the models (Hansen & Tarp 2001). In all GMM-models in this thesis, this test is performed to ensure the consistency of the estimator, and displayed at the bottom of the table.

#### **4.5.4 Multiplicative Term between Aid and Democracy**

To capture the effect of democracy on aid effectiveness, I apply a multiplicative term between democracy and aid. This implies that the effect of aid on poverty varies according to the level of democracy in any given country. More specifically, I believe that the incline or decline of the slope of aid is different at different levels of democracy.

Introducing an interaction term in the model, although complicating interpretations of the estimates, relaxes the assumption of an additive relationship between aid and poverty (Friedrich 1982). The major difference between an additive model and an interactive one, is the understanding of the regression coefficients as terms of a *conditional* relationship rather than a *general* one (Friedrich 1982).

## 4.6 Quantitative Challenges

There are several challenges for the validity of the statistical analysis. First of all, the countries included in the sample are mostly developing countries with poor democratic history and traditions. Those that qualify as democratic are often newly established democracies where democratic institutions and practices are based on old structures of power and influence (Bratton & van de Walle 1997). Moreover, political rights and civil liberties are far from fully implemented in many of the countries included in the sample, and democratic institutions do not always work in accordance with their intention. One consequence is that the estimates for democracy's effect on aid effectiveness could turn out non-robust, or show a smaller effect, or even another effect, than hypothesized in this thesis.

Secondly, there is the problem of endogeneity. Hopefully, however, this problem is minimized through the application of both the Arellano-Bond GMM and the case study to further clarify the causal direction. Nevertheless, it is hard, if not impossible, to tell when endogeneity is not an issue in aid research. It is therefore important to remain critical towards the estimates in the statistical models.

Thirdly, there are very few measures in the original data set, and especially on the poverty headcount ratio, which is included in the operationalization of poverty in this thesis. It is likely that the missing values are not random, which could give a larger effect of aid and democracy on poverty than what is true. This problem will be further addressed in the next section.

### 4.6.1 Missing Values

A general challenge in TSCS data is a lack of data on key variables (Honaker & King 2010, Hoeyland & Nygaard 2011, Ross 2006). The data I apply is no exception, and especially the poverty headcount measures are scarce. Moreover, and more importantly, the pattern of missing data is most likely not random. In examining the effect of democracy on poverty, Ross (2006) finds that data on infant mortality rates in non-democratic states are more likely to be missing than data from democratic states. He also finds that the authoritarian states that performed the best were also the ones with the least data. If such a pattern is present in the data for this analysis, it can create seri-

ous bias in my sample, and hence also biased results. In fact, according to Ross (2006), the non-randomness of missing variables has resulted in that quantitative research has overstated the effect of democracy on poverty reduction.

However, a closer inspection of the data used in this thesis revealed that the measures of the poverty headcount is to a larger degree missing in countries that generally perform less than average. Zimbabwe and Somalia for instance, have no measures of the poverty headcount ratio, but is repeatedly rated two of the worst countries to live in in the world (World Bank 2011a). Thus, it might be true that the measure of infant mortality rate is less reported in better performing autocratic states than in worse performing authoritarian states as Ross (2006) assumes, but it would seem that with the measure of the poverty headcount it is the countries that perform the worst that also has the most missing values. This could indicate that the missing data on the poverty headcount are the countries where the link between aid and poverty, and democracy and poverty, is less profound than in the countries where data is not missing. This could imply that there is bias in my data, and could indicate non-randomness in the structure of the missing values.

To account for this I have taken advantage of Amelia II from Gary King and associates, to fill in missing values in my data (see Honaker & King 2010, Honaker et al. 2011). Amelia II uses multiple imputation to calculate probable values for missing data, drawing on information from other variables included in the data set as well as earlier and later observations of the same variable. The basic idea is "to extract relevant information from the observed portions of a data set via a statistical model" (Honaker & King 2010, 561). The Amelia II program allows for time trends, cross-sectional variability and time and space correlations, creating more accurate imputations than alternative methods of filling in missing values, such as listwise deletion and best guess imputation (Honaker & King 2010, 561). However, there is also an inherent element of insecurity in the imputed values. As Ross (2006) demonstrated, the missing values on infant mortality rates led to selection bias in that well performing authoritarian regimes do not report their measures as often as not-so-well performing authoritarian regimes. This leads to bias in the data, exaggerating the negative effect of authoritarian regimes. That there are significant amounts of data missing in the original data I apply, could imply unsystematic variation in the values that are not missing. This could potentially lead to large standard errors on the imputed data. Unless the imputed data predicts extremely accurately, it is plausible that this is the case. A consequence is therefore that even after filling in the missing values, selection bias can be present. No matter how sophisticated the measure of imputation is, the fact remains that the missing values are not known, nor observed (Hoeyland & Nygaard 2011, 6).

The data I apply to examine the relationship between democracy and aid effectiveness, is the mean value of five different imputed data set. Honaker & King (2010) suggest to use "Clarify" in order to account for between imputation variation for each imputed data set. However, this is not possible in this thesis as "Clarify" does not support the models applied in the analysis in chapter 6. I have therefore attempted to account for uncertainties related to between imputation variation by taking the average value of the five data sets, combining them in the final data set. This is a precaution to achieve the best possible fit between the imputed value and the actual value. However, it is wise to keep in mind that there is an uncertainty linked to the values in the data when drawing conclusions and inferences.

#### **4.6.2 Remarks on the Quantitative Analysis**

The challenges mentioned above reflect uncertainty about the variables used, about the nature of the causal relationship and about the quality of the available data. This could affect the results of my analysis, and potentially lead to problems of reliability and validity. Thus, when interpreting the estimates in the statistical models, caution must be executed when drawing general conclusions. However, the case study is included in this study as an attempt to improve my understanding of the effects of some of these issues on the statistical results.

By using multiple imputation to minimize the problem of non-randomness in the missing data, applying decade dummies to account for exogenous global changes and taking advantage of the Arellano-Bond GMM to control for country-specific effects and endogeneity, I hope to have escaped the the three most common flaws in TSCS on democracy research as argued by Ross (2006). Hopefully, despite the shortcomings of the quantitative data, this thesis will bring valuable insight into the general effect of aid and its conditions for succeeding in alleviating global poverty.

### **4.7 Case Study**

Although researchers seem to agree that foreign aid works under certain conditions, there is surprisingly little knowledge of the processes and mechanisms underlying this relationship and causing effective implementation of aid (see e.g. Easterly 2003). Given the democratic challenges and limitations assumedly facing many of the countries included in the statistical analysis, as discussed in chapter 3, the case study is included to enable me to draw further inferences on the relationship between democracy and aid effectiveness in a low-quality democracy. A close examination of within-case processes provides the interpretation of the results from the statistical analysis with important insights and detailed knowledge and can help tie together important findings from both

analyses. The aim of the case study is not to provide generalized assumptions for democratic mechanisms in all democracies that receive development aid. However, hopefully the case can yield useful contingent generalizations for how the democratic mechanisms address can influence aid effectiveness in countries where democratic institutions and practices are of poor quality (George & Bennett 2005). This might help in illuminating the background for statistical research, and highlight how the effect of aid on poverty might be influenced by democratic mechanisms and practices.

Case studies are generally well suited for studying causal mechanisms, but a general challenge for case studies is that evidence about the relationship between the independent and dependent variable is hard to pinpoint because of the multitude of confounding factors. It might be difficult to separate rival explanations from one another, as several causal paths could have led to the outcome on the dependent variable. This could lead to problems in identifying which causal mechanisms were the most important in the decision to implement the cable. Thus, the case study might fail to clarify the causal direction of the relationship as it might be hard to distinguish the effect of democracy and aid from other effects. Thus, special care has been taken to assess the plausibility of other explanations in the case study, hopefully making it an important contribution in eliminating the problem of endogeneity and the uncertainty of the causal direction. Moreover, elements of process tracing is employed in the analysis, increasing the likelihood that confounding factors can be controlled for; although this threat is still valid.

#### **4.7.1 Process Tracing**

Process tracing is an informal research method that collect incomparable observations into a potentially long causal chain with the aim of saying something substantial about the effect of the independent variables on the dependent one (George & Bennett 2005). Process tracing draws attention to the causal processes involved in political life; and the mechanisms behind it that links causes to effects (George & Bennett 2005). Especially when considering the endogeneity problems surrounding the research on aid and poverty, it becomes a matter of utter most importance to establish the causal link between aid and poverty, and the processes and mechanisms in between. Elements of process tracing within a case study framework enable me to make structural empirical inferences based on deductive logics and assumptions about how the world works in order to clarify the causal path between aid, democracy and poverty. Moreover, the internal validity of my thesis is improved by applying elements of process tracing method in my analysis.

The idea behind process tracing is to use different contextual evidence to recon-

struct causal links; it is a formal investigation into causality that often involves clear theoretical implications and expectations. Process tracing is based on contextual assumptions and ideas about how the world works (Gerring 2007, 185). In this case, the effect of the cable and the effect of democracy, can be illuminated by comparing the state of Zanzibar as it is, and how it could potentially have been had the value on the independent variables been different.

Causal mechanisms are located at an analytical level below that of theories, and can therefore increase the credibility of a theory by creating specific explanations and predictions (Checkel 2007, 2). In this thesis I examine the importance of three sets of political mechanisms: the relative size of the winning coalition and elections; accountability and political rights and civil liberties; and political pressure from the poor. This allows me to infer theoretical implications between democratic institutions and aid effectiveness. Process tracing seeks to arrange for fine-grained research, revealing the critical steps and stages of political decision making (Tansey 2007, 771). This implies that I examine a series of theoretically predicted intermediate steps (Checkel 2007, 3). While the statistical analysis examine the general and overall effects of democracy on aid effectiveness, the case study applies a micro-perspective, examining the mechanisms and processes within a country instead of between countries.

However, as pointed out by Gerring (2007, 182), process tracing is not a quick fix solution to get to the bottom on the aid-poverty relationship, much depends on the quality of the data obtained and the way they are analyzed. As with traditional case study design, the presence of confounding factors can make it hard to establish the causal link between aid, democracy and poverty reduction. George & Bennett (2005) highlight one challenge related to causal complexity, in that certain conclusions might be hard to draw when the causal path is vague or frequently interrupted by other elements. Moreover, and more relevant to my findings as chapter 7 will reveal, is that when several different causal paths are consistent with the evidence, it is hard to point out the correct explanation.

#### **4.7.2 Validity and Process Tracing**

According to Gerring (2007, 184), the validity of the process tracing process is based on two issues: (1) the clarification of the argument, and (2) the verification of each step of the model and an estimate of relative uncertainty. The clarification of the argument is more or less dependent on the researcher conducting the study, and I can only hope that it is sufficiently clear in this thesis. Estimates for uncertainty are hard to establish, making it difficult to say something about the likelihood of each rival explanation (Gerring 2007, 182). This can result in that the conclusions from my case study is ex-



aggerating the role of democracy in the implementation of the subsea cable, giving less credit to rival explanations than their actual impact. Because of this, I have taken special care to consider the probability of other motivations and mechanisms in the process with the cable, which is reflected in the analysis in chapter 7.

However, when executed with caution and in the correct manner, process tracing has unrivaled internal validity. Gerring (2007) argues that process tracing incorporates great potential for the close examination of micro-mechanisms, which is needed to understand the interaction effect between democracy and aid effectiveness. It has its strengths in answering questions of "how" and to map out complex interaction effects and decision-making processes (Checkel 2007, Tansey 2007, 765), and is therefore especially suitable for application in this thesis. Mixing elements of process tracing with a formal case study research design and statistical analysis, can strengthen the validity of my findings and highlight the importance of each mechanism involved.

### 4.7.3 Case Selection

One of the most challenging aspects of case study as a research design is the selection of case(s), and a common critique is that case studies often suffer from "selection bias".<sup>8</sup> Lieberman (2005) suggests multiple ways of selecting appropriate cases based on the results from the statistical analysis. For instance, cases can be selected based on predicted and actual scores on the dependent or independent variables. In cases where the statistical results are non-robust and unsatisfactory, the case should be selected in accordance with the scores on the dependent variable. He argues that cases should not be chosen randomly, but rather deliberately in order to have a constructive role in illuminating the hypothesized relationship.

In choosing a case study for this thesis I was on the look-out for a project that had a high level of government involvement, was given as bilateral aid directly or indirectly from the Norwegian government, and where the political processes of a democracy could be observed. Early in the process, Tanzania was depicted as a possible country for in-depth analysis of development aid, both because it is one of the countries in sub-Saharan Africa where democracy is evolving, and because it is one of the largest recipients of Norwegian bilateral aid (Norad 2010). Being conscious of Tanzania's observed poverty scores compared to how the country was predicted to score, made it possible to establish that Tanzania had a poverty score consistently higher than what was predicted by the statistical model when applying a panel-corrected standard error

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<sup>8</sup>The most common and most severe selection bias in case study research designs is selecting cases only according to the variation on the dependent *and* the independent variables. This implies that cases are selected according to the levels on the dependent and independent variables the theory would predict, ignoring cases that could and would contradict the theory (George & Bennett 2005, 24).

OLS estimation (see Appendix C).<sup>9</sup>

In order to find a project that would make a good case within Tanzania, I had close contact with representatives of Norad and the Royal Norwegian Embassy (RNE) in Tanzania. It was in the archives of Norad that I first became aware of the electrification project of Zanzibar that had been going on since 1986. This project was separated into several different phases, where the first part involved the electrification of Unguja from 1986 to 1992. The last part of the project was the electrification of the island of Pemba, and was initiated in 1994 and extended to include a subsea cable from the mainland of Tanzania to Pemba. After careful consideration, I decided to focus on the subsea cable only, in order to obtain an in-depth analysis of this project and the political processes behind it.

The specific case within Tanzania was chosen in accordance with the values on the independent variables; aid and democracy. The project needed to qualify as development assistance in order to be useful in this thesis. Moreover, this case included elements favorable to the examination of democratic mechanisms. Today, Zanzibar is classified as a "democracy", but at the time of the implementation of the cable it was characterized as a "hybrid regime"; neither democratic nor autocratic (African Elections Database 2010). This made Zanzibar a more difficult test case than originally thought, reflecting poor democratic traditions and institutions. Nevertheless, there were certain aspects of the case that made it an especially interesting one.

Firstly, the case provides a good example of studying the mechanisms behind the allocation of aid just when democratic processes were evolving in Zanzibar, hopefully highlighting differences between this allocation and previous allocations. The case presents an unique opportunity to study the effects and mechanisms related to the allocation of foreign aid in a low-quality democracy, where multi-party elections are held, but political and civil rights not necessarily implemented or respected, making it easier to trace the effect back to its respective mechanism. Thus, the case provides additional knowledge of the importance of the mechanisms under examination, and provides empirical insights into theoretical concepts, such as the importance of the relative size of the winning coalition in countries where the voters are clearly separated into distinguishable territories. This provides the analysis with aspects and nuances that could not be obtained in a statistical analysis alone.

Secondly, because of the limitations of Zanzibar democracy at the time the cable

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<sup>9</sup>The reason for testing the residuals from this model is based on the fact that both the Fixed Effects and the GMM model control for country-specific effects. The case study is applied in order to closer examine exactly what these country-specific effects are, and should therefore be selected in accordance with a model that do not control for such effects (Rohlfing 2007).

was implemented, it is likely that if a causal relationship between democracy and aid effectiveness is indeed observed in this case, the effect will also more likely be present in other cases where democracy is more or even fully developed.

Thirdly, the case presents an elegant solution to the issues related to endogeneity. Tanzania has been receiving development assistance from Norway for decades, and it was made a priority cooperative partner in 1966 (Regjeringen 2006). Today, Tanzania is the largest recipient of Norwegian aid, besides from Brazil, and the country received more than 700 million NOK in aid in 2010 from Norway alone. The fact that Norway has donated aid to Tanzania for such a long time most likely means that the aid to Tanzania is less dependent on the level of poverty in the country; meaning that Tanzania does not receive more aid because people are becoming poorer. In fact, despite a decreasing number of people living in poverty since the early 1960's, Norwegian bilateral aid has only been increasing, with the current amount of aid being the highest in the history of Tanzania-Norwegian relations (Norad 2010). Consequently, this case assumedly have less endogeneity between aid and poverty than other countries or projects. Although the case may not be strictly exogenous, it is easier to rule out endogenous explanations of a change in poverty with this research design than in a statistical analysis alone. This case provides an opportunity to look at aid without the problem of endogeneity, but rather as an exogenous element to an issue riddled with dependencies and contingencies.

Lastly, the case is an example of conditional aid in a democracy, thus providing an opportunity to examine the theoretical implications of Bueno de Mesquita & Smith (2009, 2007) on aid conditionality and effectiveness in democratic regimes.

It follows that the case has been selected deliberately because of its unique context, specific attributes and inherent importance for pinpointing the importance of the relative size of the winning coalition and elections; accountability and political rights and civil liberties; and political pressure. The case is not strictly just one case, as one data point in my statistical analysis is country-year. Given that the process with the cable lasted over several years, from 2006 to 2010, it strengthens the argument of applying elements of process tracing in the analysis (Lieberman 2005, George & Bennett 2005). Causation can be directly measured as a linear line from point A when the cable was implemented to point B, the effect that is visible now. The aim and purpose of this case is to highlight the mechanisms behind the allocation of aid in a low-income democracy that cannot be captured by statistical models, and pinpoint the difference these mechanisms made during the process with the cable and during the transition to the Government of National Unity.

## 4.8 Qualitative Data

The case study has a variety of data sources, further strengthening a research design incorporating process tracing. From aggregated data on Tanzania to detailed election data on the elections in Zanzibar, elite interviews and other field work, e-mail correspondence and other secondary sources on the project and the historical context of Zanzibar democracy. These sources are not necessarily comparable, but they all contribute in creating a broad understanding of the project and its context.

### 4.8.1 Secondary Literature

To obtain the data needed to perform the analysis, I firstly take advantage of the documents already produced on the subject. The RNE has extensive records of the communication between the RNE and the government of Zanzibar, as well as the communication between the Embassy, Norad, Statnett and other parties involved in the project. Furthermore, the Embassy also has a record of minutes from meetings, as well as the different appraisals and end reviews of the project. These documents present a non-intrusive way of collection data, and provide a proper basis for understanding the contextual factors. The intention is to obtain an overview of the project and the processes behind it, as well as its progress and the relationship between the different parties involved. This prepared me for the interviews, and allowed me to ask relevant and to-the-point questions.

### 4.8.2 Interviews

In this case, process tracing involves the analysis of political decisions made at the highest level of government, making elite actors a critical source for information about the process behind the implementation of the subsea cable and its operation. For the most part, I conduct elite interviews, involving high ranking members of the government, of CCM and of CUF. Appendix D provides a list of the informants I was able to interview during field work in Zanzibar and Tanzania.

Tansey (2007) promote elite interviewing as a useful tool when applying the process tracing method. Tansey (2007, 767) argues that "when interviewees have been significant players, when their memories are strong, and when they are willing to disclose their knowledge of events in an impartial manner, elite interviews will arguably be the most important instrument in the process tracer's data collection toolkit".

As the goal of process tracing is to gain information about specific events and processes, it is logical that the sampling procedure thus identify key political actors and those that were heavily involved in the process (Tansey 2007, 765). It follows that random sampling will be inappropriate in a process tracing setting, as it risks excluding

important respondents. I have used both positional criteria of respondents to identify the most relevant one to this process, and criteria related to their deemed influence in the process with the cable by their own peers, as suggested by Tansey (2007). To a certain extent, the snowball sampling method was applied to obtain further contacts and respondents. Farquharson (2005) argues that the snowball method is successful in identifying influential actors that the researcher might otherwise have missed, as elites often suggest influential players not obvious to the researcher. However, the snowball method can also lead to informants suggesting people that share their own view point, or in this case, people with the same political affiliation. This could influence my results in that I do not receive the same amount of information from both sides, and might become biased towards one political party. In order to avoid missing key players and policy makers, and to limit the potential danger of selecting only respondents of the same opinion, I have taken advantage of both methods of choosing respondents.

The findings from the secondary sources are corroborated by using elite interviewing to strengthen the robustness of my findings. Process tracing is thus contributing to the method of triangulation in that findings from the secondary sources are cross-checked through other sources of data (Tansey 2007). Moreover, the interviews also provide additional information and fill in gaps in the data from the secondary sources.

The elite interviews are instrumental in examining the decisions and actions that was behind the implementation of the cable. Through semi-structured and direct questioning, I was able to imagine and reconstruct political decisions and the processes behind them, based on the respondent's testimony. As highlighted by Tansey (2007, 767): "By interviewing key participants in the political process, analysts can gain data about the political debates and deliberations that preceded decision making and action taking, and supplement official accounts with first-hand testimony". The structure of the interview also allowed me to go deeper into the process and its dilemmas than any written source of information I could find, allowing me to obtain a higher understanding of the underlying context. George & Bennett (2005, 103) point out that documents often conceal the informal processes and considerations involved in the decision-making process, and interviews can help fill this gap.

### **4.8.3 Issues of Validity Related to Interviews**

There are also questions of validity related to the qualitative part of my thesis, and especially in relation to the interviews. The interviews are conducted as semi-structured interviews, with a list of questions that is used for every respondent, but with the possibility of making small changes throughout the interview. This contributes in the standardization of data and ensures as high validity and reliability of the data as possible,

making systematic comparison and cumulation of findings possible (George & Bennett 2005, 67). At the same time it allows for flexibility and adaptation to the individual interviewee. Appendix E provides the list of questions I used during the interviews. However, this list does not contain all the questions asked to all the informants, but gives the basic list for all interviews.

I use mostly open-ended questions to achieve flexibility and depth in my data. According to Barry (2002, 681): "Open-ended questions have the virtue of allowing the subject to tell the interviewer what's relevant and what's important rather than being restricted by the researchers' preconceived notions about what is important". However, open-ended questions could lead to potential problems of validity and reliability. There is no guarantee that the respondent will tell the truth or that one version might seem more convincing than another. Respondents might have their own motivations for agreeing to the interview; perhaps wanting to promote their own point of view (Barry 2002, 680).

### **Reporting Bias**

Elite interview as a data collection method has its draw-backs and limitations. The most relevant to my thesis is the potential reporting bias by influential politicians and governmental officers. The politicians I spoke to might have overstated their own role, while minimizing that of his opponents. I found that both CCM members and CUF members highlighted their own role in laying the cable as the decisive reason for its implementation, while thoroughly disregarding the role of the other party. George & Bennett (2005, 102) observe that in the immediate aftermath of a decision or process, policy-makers often have an incentive to discredit the other parties involved to give the picture of a "careful, multidimensioned process of policymaking". In this case, some of the merits of the government and its representatives, perhaps also of the opposition, is highly likely to be exaggerated to create a favorable picture of one's own actions and motivations. This might have influenced my results in that the role of political pressures might have been overstated and exaggerated. However, objective accounts of voting data do give the indication that support for CUF was increasing, automatically putting pressure on the CCM. Nonetheless, this is a limitation that is important to keep in mind when interpreting the data and critically examine the answers.

In addition to exaggerating their own role, the respondents might be believable to overstate the role of the *project* in creating development and stability on Zanzibar in order to increase the probability of increased aid from Norway. Although I do not consider myself a very influential player in the development of Norwegian aid policy, the respondents might have considered that my thesis would be interesting for Norwegian policy makers.

## 4.9 Conclusion

This thesis draws on both quantitative and qualitative measures to clarify the relationship between aid and poverty, and the democratic mechanisms influencing this relationship. In combining the two methods, this thesis aims at revealing both the causal effect and the causal mechanisms behind this effect; examining the causal path and process from the donation of aid to its allocation and, hopefully, the subsequent reduction of poverty.

It is not sufficient to scratch at the surface of this relationship examining overall effect at the country-level; nor is it sufficient to look at the interaction effects and democratic mechanisms of only one case. To make up a complete picture of the relationship between aid, democracy and poverty, both between-cases and within-case analyses must be applied. The case study will draw on the findings from the statistical analysis, expanding on the relationship and adding to my understanding of the factors that might influence aid effectiveness in low-income democracies. In this thesis, the case is used to answer those questions left open by and expand on the patterns indicated in the statistical analysis, increasing both the external, internal and conceptual validity. By applying both methods, I am able to examine the issue beyond what has previously been attempted, hopefully revealing new aspects and further develop the debate on aid and the conditions for its effective implementation.





# Chapter 5

## Operationalizations

### 5.1 Introduction

Concepts such as poverty and democracy are controversial and hard to measure. Especially the measurement of my dependent variable, poverty, has long been the subject of debate. A crucial part of this thesis is therefore the operationalization of the relevant concepts. This chapter will present a definition and operationalization of the variables used in the analysis and discuss the choice of variable and its application, especially in regards to the statistical analysis.

As the conceptual validity of case studies are generally much higher than in statistical research, the case study provides a much more flexible way of conceptualizing the variables applied in this thesis. The operationalizations in this chapter is therefore first and foremost related to the statistical analysis and the variables applied there. However, to be sure that I am in fact measuring the same concepts in the statistical analysis and in the case, the following operationalizations also make up the basis for the understanding of the concepts in the case study. Descriptive statistics of the variables used in the original data and in the imputed statistical analyses can be found in Appendix F.

### 5.2 Dependent Variable: Poverty

The most fundamental issue in poverty research is the identification of the poor; exactly who are the poor, and what makes them poor (Lambert 2001, 133, 136). There are those who believe that poverty is *relative*, meaning that their standard of living must be seen in comparison with the general standard of living in their country of residence. By definition, according to this approach, there will always be people living in poverty in every country in the world (Ross 2006). On the other hand, there are those that argue that poverty cannot be relative; it is *absolute*. People who hold this view believe

that only those that fall below a certain universal level of deprivation can be counted as poor, be it income, calorie consumption or living standards (Sen 1983b). Determining a set poverty line has been one of the major methodological challenges in poverty research, and the lines that are used are always chosen rather arbitrarily (Foster & Shorrocks 1988a, Zheng 1997). This is most likely because there is no set level of income, food intake or housing that have the same consequences for all people; the input is the same but the output is different - leading back to associations of relative notions of poverty (Atkinson 1987, 226). However, those who believe in absolute notions of poverty, believe that there are certain basic elements of poverty, such as hunger, that are not experienced by people living in relative poverty (Ross 2006, Sen 1983b). In this view, extreme poverty is absolute, while the conditions of living in poverty in a more general way, can be relative.

Another question on the measurement of poverty, is the question of how poor the poor are; more precisely the intensity of poverty. When a poverty line is set, improvements below this line are ignored, making it hard to capture successful poverty alleviating policies. A third question evolves around how to aggregate poverty, as it is experienced differently from one person to another (Lambert 2001, 133, 134).

Income has traditionally been the measure for which poverty is defined. However, it is increasingly becoming common to view income only as one part of what it means to be living in poverty (Ross 2006). Income does not reflect a family's accessible economic resources, as they might have other assets to rely on in difficult times. Moreover, income only reflects the possession of private goods, whereas the access to public goods are excluded from the concept. Thus, income measures might not capture the way in which the life of poor people are improved by government actions and provision of public goods (Ross 2006, 6, 7). This is especially relevant for the use of the concept of poverty in my thesis, given that I partly base my theoretical argument on Bueno de Mesquita et al. (2003) and the provision of public goods as a reason for democracy's superior ability to reduce poverty with aid.

Zheng (1997, 125) states that "The concept of poverty is essentially multi-dimensional, income is only one of many factors in the identification of the poor". In this thesis, I follow this definition and argue that poverty is more than a lack of economic income. I further expand on the notion of poverty in accordance with Sen (1992, 109): "the failure of basic capabilities to reach minimally acceptable levels". Based on the discussion above, in this thesis "capacity" is considered to be a product of income, health and education. Income is included in the definition, but not by itself and merely as one element of what it means to be living in extreme poverty. Poverty in this thesis, is thus perceived as a multi-dimensional phenomenon. The following sections provide

an operationalization of poverty for the use in this thesis.

### 5.3 The Capability Approach

I base my operationalization of poverty on Amartya Sen's "Capability Approach" (Sen 1981, 1983, 1987, 1992, 1999), incorporating the importance of basic capabilities in the experience of poverty. In this approach, poverty is more than just inadequate income or economic resources; it is the lack of opportunities as a direct result of material shortcomings. Rather than seeing poverty as purely income poverty, this approach defines poverty as capability deprivation. You are not poor just because you have little or no economic resources, you are poor because you do not have the possibility or freedom of pursuing "functionings" or actions that you value. This may be because of an inadequate level of income, but it can also be because of social, cultural or political constraints. The capability approach draws attention to the role of political and economic institutions' role in enhancing people's capabilities over time, which is an important part of my theoretical framework. Sen incorporates an element of freedom in his definition of poverty, and by expanding the freedoms people value, one automatically reduces capability poverty (Alkire 2007, 2).

Despite his belief in poverty as a lack of capabilities, Sen (1983b, 159) believes that poverty must consist of an absolute core. He observes that "*absolute* deprivation in term of a person's capabilities relates to *relative* deprivation in terms of commodities, incomes and resources". According to Lambert (2001, 136), "Sen believes that the capabilities to live without shame, to participate in the activities of the community and to have self-respect are absolutes which have "extremely variable resource requirements"". Poverty, even though absolute, is dependent on individual preconditions for taking advantage of opportunities. The differences between individuals decide to what extent people can convert resources into capabilities, and the conditions that are important for the full utilization of resources would therefore vary from person to person. In contrast to other poverty measures, the capability approach takes into consideration this "human diversity". However, seeing as poverty has basic, absolute elements, it is only possible to incorporate this to a certain extent. Capabilities are most useful as an objective measure in the identification of poverty, not as a measure of personal preferences (Sen 1983b, 159).

It is clear that Sen attached a practical aspect to a rather normative concept (Sen 1992, 11), with the inherent empirical difficulties in operationalizing and utilizing the concept. Numerous examples of potential operationalizations can be found in the literature, but its empirical utilization is still rather limited (see e.g. Robeyns 2000, Nussbaum 2003, Alkire 2007).

### 5.3.1 Challenges

The emphasis of the approach is the identification and prioritization of values and freedoms people appreciate (Alkire 2007, 2). In relation to extreme poverty in developing countries, Sen (1992, 44-45) recognizes that there are certain basic capabilities which fulfillment will have a large effect and only demands limited efforts, such as the ability to be well nourished and well-sheltered, as well as the capability of escaping premature morbidity. The primary concern in the selection of variables, should therefore be what one would expect people to value or have reason to value (Alkire 2007, 2).

Secondly, freedom has intrinsic value according to Sen (1999, 53), and people have to be agents in their own lives: "The ends and means of development call for placing the perspective of freedom at the center of the stage. The people have to be seen, in this perspective, as being actively involved - given the opportunity - in shaping their own destiny, and not just as passive recipients of the fruits of cunning development programs".

The last challenge of the foundations for the approach is its counterfactual nature (Comim 2001, 7). This implies that a person might have a great deal of freedom, but without actually achieving much (Sen 1987). A capability could therefore be regarded as a possibility that might be exercised or might not be exercised (Williams 1987, 96); individuals might choose not to act upon their capabilities, or they may prioritize certain freedoms over others. Sen, however, claims that this counterfactual nature of the approach does not necessarily affect its practical use, as the nature of counterfactual choices can be easily found (Sen 1992, 66); people would gladly try to avoid elements of sufferings, such as famines, chronic hunger and epidemics, thereby creating a core to the freedoms people can be assumed to choose (Sen 1999, 131).

### 5.3.2 Choosing Indicators

Because of the counterfactual nature of the approach, practical compromises are necessary for putting it into empirical use (Comim 2001, 9). The operationalization of the concept should therefore be based on pragmatic considerations of available information. It should be pursued in the context of a specific analytical purpose, and the choice of variables and unit of analysis should be made in light of this purpose (Comim 2001, 11,14). Quoting Sen (1992, 44-45) at length (as quoted in Comim (2001, 5)):

"In dealing with extreme poverty in developing economies, we may be able to go a long distance in terms of a relatively small number of centrally important functionings (and the corresponding capabilities, such as the ability to be well-nourished and well-sheltered, the capability of escaping avoidable morbidity and premature mortality and so forth). In other contexts,

including more general problems of assessing economic and social development, the list may have to be much longer and much more diverse."

The HDI was developed by the United Nations (UN) as an operationalization of the approach, but Sen himself is sceptical towards one permanent list of the characteristics of poverty because of the nature of human diversity (Sen 2004, 77). He "was concerned by the difficulties of capturing the full complexity of human capabilities in a single index" (Fukuda-Parr 2003, 305). Moreover, a general problem with the HDI is that it measures the level of *average* national income, excluding measures of equality when assessing a country's performance (Anand & Sen 1994). There have also been discussion on the weighting of the different variables included in the measure, giving rise to accusations of arbitrarily rewarding the dimensions with different importance, as well as contributing to potential data errors (Noorbakhsh 1998). Lastly, the index have been accused of failing to capture the reality of the experience of living in poverty and of the world it attempts to portray (Sagar & Najam 1998). Because of this, I have decided to construct my own index for the use in this thesis, basing it on Sen's doubt for a permanent list and the HDI's failure to capture conditions of extreme poverty, creating a index that is suitable for the use of the concept of poverty in this thesis.

## 5.4 Operationalization of Poverty

As this paper will measure the level of poverty in developing and low-income countries, the operationalization of poverty will first and foremost focus on basic capabilities in accordance with Sen (1996, 57-58). The operationalization of the capability approach in this paper will draw on existing empirical analysis, normative assumptions, as well as available data and indicators that have been the subject of public debate (see Alkire 2007, 7-13). Poverty will be explored as a multidimensional and participatory concept, building on important economic and non-economic aspects of poverty. However, because of limited available data on several of the possible dimensions of poverty, I have chosen to restrict myself to three dimensions that I consider to be relevant according to the capability approach; namely economics, health and education. For reasons of parsimony, there is only one indicator for each of these dimensions. The aspect of agency that is stressed in the capability approach is difficult to operationalize and could be the topic for a thesis in its own right. It also includes a political element, which could potentially correlate quite highly with the measure of democracy. It would therefore be methodologically unwise to include political variables in the dependent variable, as such variables would also be a part of my explanatory variable. I have therefore chosen to focus on the fulfillment of basic capabilities, justifying this limitation by arguing that it is in line with Sen's own comprehension of extreme

poverty.

### **5.4.1 Economic Dimension**

The first dimension of poverty is the economic aspect of poverty, chosen with the basis in Sen (1976) and his theoretical assumptions, as well as UN's poverty measures for the Millennium Development Goals (MDGs) (United Nations 2011). Notwithstanding the aspect of human diversity in the capability approach, low or no income is an important part of what it means to be living in poverty. Income, although not conclusively or exclusively, does impose important constraints on living conditions and is a large part of what it means to be living in extreme poverty.

#### **Poverty Headcount Ratios and Poverty Gaps**

There has been many suggestions and discussion on how to best measure and aggregate economic poverty (see e.g. Zheng 1997). The poverty headcount ratio counts the number of people living on less than \$ 1.25 or \$ 2 a day. This measure is good at identifying who the poor are, but lack a way of measuring the depth of poverty. It tells us nothing of the extent of deprivation experienced by the poor, and is hence unsatisfactory if the intensity of poverty matters as well as the incidence of it (Lambert 2001, 137). As a consequence, the measure is not ideal for examining the success rate of poverty reducing policies, as it only records those policies that bring people out of poverty. The fact that poverty might have become less intense is ignored. It is therefore a measure of poverty elimination policies, and does not account for policies aimed at alleviating poverty (Zheng 1997, 125). According to this measure, only people that fall below this poverty line of \$ 1.25 or \$ 2 a day are classified as poor. There are also other limitations to this measure, in that it disregards the subjective parts of poverty; the feeling of poverty. The idea that a single number like 1.25 alone determine who are the poor and who are not, has been heavily criticized (Lambert 2001, 135). It does not take into consideration local living standards, nor the social aspect of poverty; poverty as a relative concept is excluded from this measure.

Another widely used indicator of poverty, is the income gap ratio. It measures poverty as a function of income shortfall, or the deprivation someone experiences relative to someone who has just sufficient standard of living (Lambert 2001, 134). This measure accounts for the poverty headcount ratio's limitations, as it takes into consideration the intensity of deprivation. However, it does only measure changes in the mean income of the people living below the poverty line. Hence, it does not distinguish between policies aimed at helping the poorest of the poor and the general population of poor (Zheng 1997, 125). On its own it is unsatisfactory in the measurement of proportion of people that share a given average income below the poverty line (Lambert

2001, 137).

For the use in this thesis there are several important advantages with utilizing the poverty headcount ratio for the measure of income poverty; still the most widely used indicator of poverty in policy making and research (Zheng 1997, 153). Firstly, the distribution-sensitive measures of poverty are much more sensitive to the quality of the data than poverty headcount ratios, as the headcount ratios only need information on the poverty status. Given the generally high level of measurement errors in income microdata, Zheng (1997, 153) points to this parsimony as a significant advantage in using the headcount ratios. Moreover, as Foster & Shorrocks (1988a,b) showed, that when the poverty line is allowed to vary, the poverty headcount ratio might very well prove to be the most powerful measure of poverty. I have therefore chosen to utilize the poverty headcount ratio as the indicator for income poverty. For the purpose of this thesis, it does provide a suitable operationalization of the absolute core to poverty. In measuring income poverty, the headcount ratio might very well provide a fruitful measure when a minimum income is seen as a basic right. As pointed out by Atkinson (1987), under such circumstances "the headcount may be quite acceptable as a measure of the number of people deprived of that right". Following Foster & Shorrocks (1988a,b), by varying the poverty line I can show both the incidence and intensity of poverty in a given country. I therefore take advantage of both measures of the poverty headcount ratios, both at \$ 1.25 and \$ 2 a day, to examine the effects of changing the poverty line. They are both found in the WDI, and are available from 1978, although with very few measures (World Bank 2011a). I am aware of the fact that this measure alone ignores the extent to which poor people experience less intense poverty, and therefore does not incorporate the results from potentially successful poverty alleviating policies. This might influence the results of my analysis, and show a smaller effect and causal relationship than is actually the case. However, in addition to varying the poverty line, this is why I have chosen to operationalize and define poverty as a multi-dimensional concept, so that the effects left out in this indicator hopefully is picked up by another indicator of poverty in my definition. Despite its' many downsides and limitations, this indicator does place importance on and highlights the special situation of people living in extreme poverty.

#### **5.4.2 Social Dimensions**

As discussed earlier, there is a great likelihood that income measures do not capture the full context of living in poverty. Moreover, and especially important for the use in this thesis, is that income measures alone do not account for increases in living standards based on the provision of public goods. In accordance with my theoretical framework,

I argue that the level of public goods is an important aspect of what it means to be living in poverty, and one of the most important tools for fighting poverty. It is also an important aspect of the distribution of aid and of aid's ability to reduce poverty levels.

Following Baum & Lake (2003), I look at output indicators, instead of the level of government consumption or expenditure in the operationalization of the social dimensions of poverty. As they put it (Baum & Lake 2003, 336):

"A politically corrupt state that is capturing larger rents and distributing them to its supporters through inflated or unnecessary expenditures, for instance, may appear to be spending more on education than a politically efficient regime, but the level of actual services delivered to citizens will be much lower in the first than in the second case. [...] For these reasons, output indicators provide a much "cleaner" test of our theory; conversely, controlling for government expenditures or consumption would mask much of the very effect we are trying to isolate".

Measuring the effect of aid on poverty demands the use of output indicators, rather than the spending level of the government in providing health care and public education.

### **Infant Mortality Rate**

The second dimension of poverty that is used in this operationalization of poverty, is the measure of infant mortality rate. In the aid literature, this variable is considered to be a "flash" indicator of improved living standards and decreasing levels of poverty (Boone 1996, Ross 2006). Other possible measures of good health service include life expectancy and maternal mortality, but there are less data on these indicators. In addition, the measure of life expectancy changes slowly, whereas infant mortality changes quickly, making it easier to observe and pinpoint a causal relationship between aid and poverty. It is useful to analyze variables that change rapidly; meaning that changes in living conditions are noticeable within a short timespan and can therefore be attributed to the independent variables with a certain likelihood. The indicator also corresponds to the idea of basic capabilities envisioned by Sen (1996, 57-58), in the right to escape "avoidable morbidity and premature mortality". In fact, it captures the most essential of all basic capabilities; the right to life. Moreover, infant mortality rates have been recognized as good indicators of other dimensions of extreme poverty, such as the lack of access to clean water and sanitation, low education and literacy rates among mothers, inadequate prenatal and neonatal health services, insufficient calorie intake, vulnerability to disease and low income (see e.g. Sen 1999, Government of Norway 2009). In this way, it captures a large part of the living conditions of the poor (Ross 2006). Fur-



thermore, empirical evidence indicate that high infant mortality is concentrated in the lowest income decile, making it a good indicator of poverty (Kanbur & Squire 2001). Data on this variable is widely available, in contrast to many other social indicators, contributing to the validity of my results. The measure is defined as the yearly estimate for children who die before the age of 1 per 1.000 live births, and is found in the WDI. It is widely available from 1960 (World Bank 2011a).

### **Universal Education**

The third dimension of poverty is the level of universal education. This dimension of poverty has been proposed by the MDGs (United Nations 2011), as well as multiple empirical research on poverty (see e.g Narayan et al. 2000, Baum & Lake 2003). To capture this dimension I use the gross female secondary school enrollment ratio from the WDI. This measure is defined as the ratio of total enrollment to the female population of the appropriate age, and is available from 1970 (World Bank 2011a). This indicator was turned, so as to indicate the same direction as the other indicators; lower values indicate lower levels of poverty. Baum & Lake (2003, 338) convincingly argue that indicators dealing with female participation are more sensitive towards variations in regime type than the same indicators for men. They state that:

"Even in autocracies, men may receive some health care and education, and typically more than women, reducing the aggregate disparity between different regime types. As the base of political participation expands, however, and especially once women are allowed to vote, citizens often demand improved health care and education for all members of society. Regime differences are, thus, likely to be revealed more starkly in the provision of public services for women than for men".

Secondary education is chosen because there is far more variance on this variable than for primary education, while tertiary education is still something that is reserved for the rich and middle classes (Baum & Lake 2003, 338).

Przeworski et al. (2000) draw attention to the possibility that in countries where living standards are low and far from adequate, individuals invest more in children (extra labor) than in education. Only when living standards improve and reach a certain threshold, does education become important to citizens. By including an indicator for each of these phases, I am more likely to capture the effect of democracy and aid in both very poor and less poor recipient countries. Moreover, these indicators can also function as indicators of the depth and intensity of poverty. Increased democracy and aid in poor countries, would manifest itself through lower infant mortality rates, while when more and more people are able to escape poverty, education becomes important.

### **5.4.3 Remarks on the Operationalization of Poverty**

These variables have been chosen because I believe that they reflect the basic components of extreme poverty in developing countries, as well as representing values and rights that people have reason to value. Many of the indicators have been subject to public debate, and could therefore constitute universal experiences of poverty. Moreover, these indicators of poverty restrict people's basic capabilities, and improvements in some of these variables have an instrumental effect in reducing poverty, while other variables represent intrinsic dimensions of poverty to such a degree that an improvement by itself would be valuable for people living in poverty. This means that the variables are chosen in accordance with two criteria; their universal value and their basic nature in relation to human dignity. Together these variables are chosen to measure poverty.

Besides from including the poverty headcount ratio in my operationalization of poverty, I have refrained from setting a threshold for poverty for the collected poverty index in the statistical analysis in the next chapter, as these lines always are chosen rather arbitrarily (see e.g. Lambert 2001). Because of this, the estimates must be interpreted as tendencies and trends in changes of poverty, and not as exact estimates of the proportion of people living in poverty. Moreover, the index is measured on a continuous scale from -2.27 to 2.62. This adds to the justification for interpreting the estimates as indications of trends and tendencies, not as exact proportions. The small scale of the index furthermore means that even though the estimates seem small, their impact might in fact be quite large compared to the point of departure.

## **5.5 Independent Variables**

### **5.5.1 Democracy**

As democratic countries can be as different as democratic and autocratic regimes, it is hard to find one clear understanding of what democracy is. Democracy as an ideal is associated with numerous different understandings and values, given the vast heterogeneity among the people and the nations of the world (Banik 2010, 89). As discussed in chapter 3, the concept of liberal democracy is close to meaningless in many countries that today claim themselves to be democratic (van de Walle 2001, 238). The operationalization of democracy in this thesis cannot ignore this fact; nevertheless it complicates the implications from the theoretical framework. The implications outlined in chapter 3 are dependent on the quality of the regime. There are only a few cases, if any, where democracy and autocracy are as clear-cut as the theory assumes. However, this does not necessarily mean that political reform has been insignificant,

nor that all countries have only poor imitations of democracy. The challenge is to find a valid measure of democracy in a contemporary context for developing countries.

### **5.5.2 Measuring Democracy**

As democracy is such a complex and disputed concept, it is hard to capture with only one single variable. All of the democracy indexes today are in fact facing problems with validity and reliability (Munck & Verkulien 2002). Measurement errors are common as a result of subjective indicators being included in the operationalization of democracy. However, if one chooses to exclude subjective indicators, the operationalization has low validity when looking at the *actual* virtues of democracy (Knutsen 2011a, 84). On the other hand, if one includes too many broad indicators of democracy, one might face the problem anticipated by Przeworski et al. (2000); that one defines democracy in accordance with the consequences of democracy, not what it is. The TSCS of my study will use both the Polity Index and the definition from Freedom House as measures of democracy. Both measures are relatively extensive in the different aspects of democracy that are included, but their structure of additive cumulation does not fit very well with theoretical specifications of democracy (Munck & Verkulien 2002). The measure from Freedom House is an unweighted index that perhaps should have been weighted, while the Polity Index is weighted but with consequences for empirical research (Knutsen 2011a, Goertz 2005).

#### **The Freedom House Index**

This thesis uses the FHI as the primary measure of democracy. The FHI consists of two different indexes, the Political Rights Index and the Civil Liberties Index. These indexes are the aggregated variables of many more indicators. Freedom House (2011) highlights seven dimensions of democracy which are incorporated into both political rights and civil liberties: "Political rights enable people to participate freely in the political process, including through the right to vote and stand for public office, and elect representatives who have a decisive impact on policies and are accountable to the electorate. Civil liberties allow for the freedom of expression and belief, associational and organizational rights, rule of law, and personal autonomy without interference from the state". In this thesis, it is the unweighted average of these two indexes that are used as a measure of democracy. On the original scale, 1 is most democratic, and 7 is least democratic. In this thesis, however, the scale has been turned, making 1 the least democratic and 7 the most. The measure is available from 1972.

The criteria for scoring the indexes are relatively subjective, which might lead to biases and unsystematic measurement errors (Knutsen 2011a, 89). However, several studies show that the FHI does not produce substantially more measurement errors

than other indexes, such as the Polity Index (see e.g. Bollen 1993, Bollen & Paxton 2000). There are also problems in connection with the original data that Freedom House does not release publicly. This creates problems for replications and further discussion of validity and measurement errors (Knutsen 2011a, 90). Despite the many shortcomings of this measure, it is one of the most widespread measures of democracy. It is based on the presence or absence of different institutions, but it also takes into account how the different institutions *function*. Thus, it is considered to be "suitable for operationalizing a substantive democracy concept" (Knutsen 2011a, 86). Moreover, as pointed out by Knutsen (2011a, 87), the measure balances the formal political reality with the subjectiveness of democratic virtues.

### **The Polity Index**

An alternative measure of democracy that is used in this thesis, is the measure from the Polity Index. This is more narrow than the measure from Freedom House and generally only incorporates formal institutional structures, excluding civil liberties or other elements necessary for operationalizing substantive democracy (Knutsen 2011a, 91). This way, the problem of subjectivity bias, as in the FHI, is irrelevant. However, it creates other validity problems, especially in relation to the divide between formal institutions and its actual use. The index consists of two measures; Democ for the degree of democracy and Autoc for the degree of autocracy. The index ranges from -10 (most autocratic) to +10 (most democratic), where the most important dimensions are competitiveness and openness of political participation and executive recruitment, as well as constraints on the chief executive (Polity IV Project 2012). The primary advantage of Polity over Freedom House is that the Polity data set have cross-sectional data ranging all the way back to 1800, while Freedom House start their time series in 1972. Thus, there is a greater certainty in relation to this measure in the imputed data.

Compared to the FHI, the Polity Index represents a rather limited measure of democracy that could be defined as "electoral democracy". It is designed to reflect the minimal practices incorporated in the concept of democracy, and not its fundamental institutions such as the rule of law, or its consequences such as property rights (Baum & Lake 2003). An electoral democracy places importance on the electoral proceedings of democracy, while the measurement of democracy from Freedom House give greater attention to widespread civil liberties and political rights than the Polity Index. The FHI could therefore be used as an indication of "liberal democracy" or substantive democracy, where democracy and freedom are seen as closely connected (Banik 2010, 91).

In this thesis, I am foremost interested in substantive democracy, and have therefore chosen to use the FHI as my primary measure and operationalization of democ-

racy. This is also reflected in the analysis of the case study in chapter 7. However, in the statistical analysis, the Polity acts as a robust check on my results, as well as potentially highlighting the importance of political rights and civil liberties in the concept of democracy.

### 5.5.3 Foreign Aid

According to the Development Assistance Committee (DAC) of the Organization for Economic Co-operation and Development (OECD), the standard definition of aid consists of the grants and concessional loans net of repayment of previous aid loans. This means that forgiveness of past loans are treated as new loans and therefore current aid (Easterly 2003, 29). This measure is called net Official Development Assistance (ODA), and is included in the WDI (World Bank 2011b). For the purpose of this thesis, it makes up the operationalization of foreign aid. ODA has two defining characteristics; firstly it includes all transfers from official sources with at least a 25 % grant element, and secondly it has to go fully towards improving human or economic welfare. This excludes military assistance and other forms of assistance that do not have the primary aim of development (OECD 2008). The measure for ODA is collected by the OECD, and often reported by the donor countries (OECD 2008). In regards to ODA from Non-Governmental Organizations (NGOs) and multilateral organizations, some donations qualify as ODA while other do not, and are collected in cooperation between OECD and the agencies. However, new agencies are becoming increasingly numerous, and it is doubtful whether OECD is able to collect the correct number for ODA from all organizations and agencies (OECD 2008).

Indeed, there are some troubles with this measure. Aid being as fungible as it is (see Feyzioglu et al. 1998), means that aid intended for development purposes might just as easily contribute to higher spending on the military or further repression of citizens. Thus, it becomes hard to measure the actual impact of aid on poverty, as other resources that might work against the purpose of development aid are likely to be freed up. Moreover, the condition that it has to go fully towards improving a country's welfare is often a question of intention, sometimes making it hard to make out whether a donation is in fact ODA or something else (OECD 2008). This could provide donors with some degree of flexibility in their loans and grants; perhaps disguising donations that do not qualify as ODA. Furthermore, aid donors influence the way in which the aid money are spent and what they are spent on (Bueno de Mesquita & Smith 2007, 2009, Alesina & Dollar 2000). That the measure does not separate conditional aid from unconditional aid is therefore another important drawback. As discussed in chapter 3, the conditionality of aid can be decisive in its effectiveness, especially in relation to

regime type. This implies that the statistical analysis is not able to distinguish between the two types of aid, potentially missing important nuances in how aid affects poverty levels. The case study does to a certain extent make up for this short-coming; however, it can only account for how conditional aid affects poverty in a low-income and low-quality democracy. Thus, the effectiveness of both unconditional aid in democracies and autocracies, and conditional aid in autocracies are not sufficiently clarified.

However, because of a lack of other appropriate measures and in line with the literature on aid effectiveness (see e.g. Burnside & Dollar 2000, Svensson 1999, Easterly 2003, Hansen & Tarp 2001), I have chosen to apply the official measure of ODA as a share of GDP as the measure for foreign aid in this thesis. This might influence my results in that the effect of aid might not be as clear as it actually is, creating a higher uncertainty than is the case. In this way, using the official number for ODA might underestimate the effect of aid on poverty reduction. The measure is found in the WDI, and is available from 1960.

## 5.6 Control Variables

The choice of control variables has important implications for the validity of the analysis and its results. It is important that they capture the aspects of the context that might influence the dependent and independent variables, so that the measured effects of aid and democracy are not spurious. The choice of variables in this thesis, is based on the assumption that they influence both the dependent variable and the independent ones. If left out of the analysis, this could lead to omitted variable bias, making the estimated effects inconsistent. Variables that have been widely used in the literature on aid effectiveness include dummies for the different regions (e.g. sub-Saharan Africa, Latin American and the Franc Zone), GDP, GDP per capita, Institutional Quality and Policy Index, Population, Openness, Inflation, Foreign Direct Investment (FDI) and Corruption (see e.g. Burnside & Dollar 2000, Easterly 2003, Hansen & Tarp 2001, Rajan & Subramanian 2005, Easterly & Levine 1997). The underlying strategy in identifying controls for aid-growth regressions, is to account for different institutional and policy characteristics that might influence, and perhaps also explain, the performance of poor countries. By doing this, researchers ensure that their results are robust, and that the effect from aid is not spurious (Burnside & Dollar 2000, 849). In addition to the variables mentioned here, decade dummies for 1960s, 1970s, 1980s, 1990s, 2000s and 2010s have been included in the analysis to account for global changes in living standards.

### 5.6.1 Population

The discussion on the relationship between poverty and population goes all the way back to the 18th century and Malthus (1798)'s controversial book *Principle of Population*, but is still a highly undetermined relationship. What is clear, however, is that population is an important factor in aid allocation (see e.g. Alesina & Dollar 2000). There is also empirical evidence showing that smaller countries receive more aid relative to GDP (Burnside & Dollar 2000). The measure of population can be found in the WDI, and is widely available from 1981 (World Bank 2011a).

For the use of population in this thesis, I have chosen to transform the variable using the natural logarithm of population. I have chosen to do this as it transforms multiplicative values into additive ones, and are therefore better suited at describing relative differences and changes (Skog 2009). By transforming the variable to a logarithm, the change from 1 to 10 will be the same as the change from 100 to 1,000 (namely a tenfold), while the change will not be the same in absolute terms. I argue that the relative importance of population growth can lead to very different consequences and outcomes. For instance, a population growth of 10 people, is more important when a country goes from having 10 inhabitants to having 20, than for a country with 1,000,000 people to grow to 1,000,010.

### 5.6.2 GDP per capita

GDP per capita can be found in the WDI, and is widely available from 1981 (World Bank 2011a). In this thesis I employ the real GDP per capita in current US Dollars. This means that the value has been adjusted for inflation and the exchange rate. This measure includes more values than the Purchasing Power Parity (PPP) adjusted measure for GDP, leading to a higher certainty around this measure in the imputed data. GDP per capita is included to control for the level of economic development, as it is highly likely that the level of economic development is relevant for the level of poverty in a given country. Moreover, GDP is known to correlate highly with democracy, and estimates of democracy on poverty could therefore have captured the effect of GDP on poverty rather than the effect of democracy had GDP per capita not been controlled for.

Most of the studies dealing with economic growth and development, use GDP per capita as a logarithm. This is mainly because, as with population, relative changes are more important than absolute changes. It is intuitive and logical to assume that a \$ 10 increase in GDP per capita is more important in poor countries where GDP per capita is less than \$ 1,000, than in rich countries with GDP per capita of more than \$ 20,000.

Given that I am looking at aid as a share of GDP while also controlling for GDP,

this could potentially cause troubles in my analysis. If foreign aid constitutes a large part of a country's GDP, then a change in aid could easily constitute a change in GDP. However, if the aid a country receives is fairly independent of its level of GDP, or if the share of aid to GDP is small, this should not constitute a large threat to the validity of the results. In the data for this analysis, just over 10 % of the country-years have aid as share of GDP levels above 20 %. Thus, it is unlikely that this influences the results in any substantial direction in the following analysis.

### **5.6.3 Corruption**

Corruption is often stated as the number one reason for the ineffectiveness of aid (see e.g. Knutsen 2009, Meredith 2006, Ayittey 2005, Baland et al. 2010, Boone 1996). It is therefore important to control for the effects of corruption, as the reality in many poor democracies is that corruption is wide-spread despite democratic institutions and regular elections.

One measure of corruption can be found in the Corruption Perceptions Index (CPI), developed by Transparency International (Transparency International 2011). These indicators are available from 1995 and onwards, and are widely used in literature concerning corruption. It is an aggregate index that measures the perceived corruption among public officials. An alternative measure of corruption comes from the International Country Risk Guide (ICRG) and is available from 1977 and onwards (PRS-Group 2011). I have chosen to include this latter measure of corruption in my analysis, as there are considerably more data points. More importantly, however, is that it measures the aspects of corruption that are the most interesting for my thesis, as it includes the paying of bribes as well as "the actual or potential corruption in the form of excessive patronage, nepotism, job reservations, "favor-for-favors", secret party funding, and suspiciously close ties between politics and business" (PRS-Group 2012).

### **5.6.4 Bureaucratic Quality**

The quality of institutions is an important control in the aid literature, and especially in relation to democracy in order to ensure that the effects seen in the analysis does in fact stem from democracy and aid, not how good the institutions in the regime are. However, instead of using an aggregated index as many do, I have chosen to deconstruct the concept of institutional control into specific contributions to pinpoint exactly which dimension of institutional control is most important in reducing poverty. For the purpose of this thesis, the ICRG's Bureaucratic Quality Index has been chosen as an indicator and proxy for institutional quality. However, it also holds significant importance on its own. This variable measures to which degree policies are implemented in a suitable and practical way. In countries with a strong bureaucracy, a regime change



or a change of leadership have little importance on the continuity of policies and government services. In a weak bureaucracy, however, a change in leadership might lead to interruptions and even cancellations of policy formulation and administrative functions. The index is available from 1984 and onwards, and ranges from 0 to 4, 4 indicating highest possible quality, and 0 the least (PRS-Group 2012). This dimension of institutional quality has been chosen because the impact of policies and the implementation of such policies holds strong significance for the people living in poverty. It is also independent of and relatively uncorrelated with regime type, and therefore functions well as a control on the effect of democracy on aid effectiveness.

### **5.6.5 Macroeconomic Policy**

It is also important to control for macroeconomic policies, as these can be quite important for poverty levels. Easterly & Levine (1997) show that there are significant correlations between macroeconomic policy indicators and country-specific cultural and socioeconomic characteristics. I have therefore chosen to include two measures of macroeconomic policy, namely economic openness and inflation. The indicator for openness of the economy is available from the Sachs and Warner data set, but the number of observations is limited (Sachs & Warner 1995). Another measure of openness that has been used in the literature is therefore the share of the sum of exports and imports to GDP (see e.g. Sadni-Jallab et al. 2008), which captures trade policy. These indicators are found in the WDI, and is widely available from the 1960s and 1970s.

Inflation is used as a proxy for macroeconomic stability and monetary policy (see e.g. Burnside & Dollar 2000, Svensson 1999), and is measured by inflation by the consumer price index from the WDI. It is available from 1961. The index is designed to capture the annual percentage growth in the cost to one consumer in acquiring a basket of goods and services (World Bank 2011a). It is the natural logarithm of the indicator that is used in this thesis, because of the presence of extreme values in the data. The Democratic Republic of Congo in 1994, for instance, has a much higher level of inflation than normal and could in this way influence the validity of the results.

### **5.6.6 Foreign Direct Investment**

In order to ensure that the change in poverty levels is attributable to development aid, it is important to control for other inflows of resources to a country. Foreign Direct Investment (FDI) has a considerable impact on growth, because FDI is dependent on the country's policies and institutions, as well as being an important carrier for technology transfers (Hansen & Tarp 2001, 563). In this thesis I employ the net inflows of FDI as a share of GDP. This indicator measures investments that aim at obtaining a long-term management interest (a 10 % or larger voting stock) in a different country from that

of the investor. The indicator is, as shown in the balance of payment, the sum of both short- and long-term capital and reinvestment on earning (World Bank 2011a). The measure of FDI is taken from the WDI, and has data from the 1970s up to today. The FDI to GDP ratio can proxy for the degree of integration into world markets and degree of globalization in certain areas (Sadni-Jallab et al. 2008, 8). Moreover, Hansen & Tarp (2001, 563) argue that FDI has a triple role; "as a flash indicator of good institutions and good policies, by contributing to capital accumulation, and by increasing total factor productivity".

However, there are several problems associated with the process of collecting and reporting of FDI data. The measure is collected by the IMF and OECD, but many, especially low-income countries, find it difficult to follow the strict guidelines for calculating FDI stocks and flows (Bellak 1998). Moreover, as FDI is guided mostly by the law of the host country, different FDI regulations apply in different countries. It is therefore a lack of consistency in international measures, leading to large discrepancies in aggregated data (Zhan 2006). However, since FDI is only introduced as a control in the following analysis, it is unlikely that it will lead to large problems in the data. Nevertheless, it is important to keep in mind when interpreting the results from the statistical analysis.

### **5.6.7 Ethnic Fractionalization**

Ethnic Fractionalization measures the degree of segregation between different ethnic groups in a country, and Easterly & Levine (1997) find that it is correlated to bad policies and poor growth rates. It is therefore important to include the variable in the analysis, as it could account for some countries performing worse than other countries - regardless of regime type. The variable ranges between 0 and 1, with 1 indicating the highest level of ethnic fractionalization. This variable is constant over time, and therefore captures long-term characteristics of a country, while influencing both policies and poverty (Burnside & Dollar 2000, 850). This variable is exogenous, meaning that it is not influenced by shocks to the level of poverty or to the level of aid. However, it might be endogenous in relation to democracy, in that it influences the composition of the institutions and the policies.

The measure is taken from Fearon (2002), and is based on secondary literature and other available lists of ethnic fractionalization, such as the *Atlas Narodov Mira*. However, there are several general problems related to the measure of ethnic fractionalization. Ethnic classifications vary between time and space, making it troublesome that the measure is constant. Moreover, ethnic classifications are often complex, leading to doubts over whether it can be captured in only one number (Alesina et al. 2003).

However, Fearon (2002) argues that the measure constructed in his article accounts for some of the flaws from previous measures of ethnic fractionalization in the literature, as he includes all ethnic groups that make up more than 1 % of the population in any given country. This list is shown to correlate quite highly with other commonly cited measures in the literature. Thus, notwithstanding the limitations of the general measurement of ethnic fractionalization, this measure presents as good a solution to its operationalization as any.

### **5.6.8 Donor Interest**

Empirical evidence point to the fact that aid is at times given in accordance with donor interest and strategic considerations (Alesina & Dollar 2000, Burnside & Dollar 2000, Boone 1996). To proxy for donor interests, I have included dummies for certain regions that are strongly influenced by donor policies. These include the Franc Zone in Africa, and Central America and Egypt which are included in the US "sphere" of influence. These variables were identified as exogenous by Svensson (1999), in that they influence poverty only through their effect on aid flows. As such they can function as instrumental variables.

The countries that score 1 on the dummy for the Franc Zone are eight countries of West Africa, Benin, Burkina Faso, Ivory Coast, Guinea Bissau, Mali, Niger, Senegal and Togo; and seven countries from Central Africa, Cameroon, Central African Republic, Chad, Congo, Equatorial Guinea and Gabon; as well as Comoros. The countries scoring 1 in the Central American US Sphere of Influence include Guatemala, Honduras, El Salvador, Nicaragua and Costa Rica (LaFeber 1993). In addition there is an individual dummy variable for Egypt, in accordance with the work of Burnside & Dollar (2000).

## **5.7 Statistical Models**

I employ five different models for each specification of the relationship between democracy and aid effectiveness. Most of the tables in the following chapter include only one specification of the relationship, but with different sets of control variables. Two of the tables include 10 models, and in these tables models 6-10 will have a different specification than models 1-5. If this is the case, it is explicitly stated in the text in the next chapter. The first (sixth) model in each table is the general effects of aid and democracy on poverty. This model gives the estimates for democracy and aid independently of one another. Model 2 (7) in each table, presents the baseline model, where the interaction between aid and democracy is introduced for the first time. Thus, it is possible to see the differences between aid and democracy separately as in model 1, and compare it to the estimated effect when the effectiveness of aid is assumed to vary in accordance

with the level of democracy (model 2). The next model, model 3 (8), introduces new controls on the relationship. Corruption and Bureaucratic Quality are included to control for institutional characteristics and quality. They are introduced simultaneously because they both represent measures of the quality of the institutions in any given regime. Thus, model 3 (8) controls for institutional characteristics that might influence aid's effect on poverty, and ensure that a potential effect from democracy is not spurious. Model 4 (9) introduces a different set of controls, namely Inflation, Economic Openness and Foreign Direct Investment. These variables are included to control for economic policies and overall investment environment, so as to decrease the likelihood that overall economic management and other economic flows than aid are the reason for a potential change in poverty. Models 3 (8) and 4 (9) thus test that the relationship between democracy and aid effectiveness is in fact causal and not spurious. The last model, model 5 (10), is the full model where all the controls are included. This models shows the effect of democracy on aid effectiveness when both institutional quality and economic environment has been controlled for.

### **5.7.1 A Note on Imputed Data**

The variables that have no substantively negative values have received a lower bound of 0 in the imputed data. This reflects the uncertainty involving the imputed values, and is an attempt to minimize the influence of imputed data that do not have a substantial value. The variables that have received a lower bound of 0 are GDP per capita, Population, Infant Mortality Rate and School Enrollment for Females. Since it makes little sense to have a negative number for population, the negative values were set to 0. However, when transforming the variable to the natural logarithm, the 0 value was excluded from the analysis, explaining the different observations for different variables (see Appendix F). The same was true for the measure of GDP per capita. FDI and Inflation was transformed using a logarithm that incorporated the negative values on the scale in the transformation. This was done because the negative values have a substantive interpretation.

Generally, for variables that are on a set scale, like the FHI, bounds were set in the imputed data so that the values never became less than the minimum value, or more than the maximum value, in this case 1 and 7 respectively. This applies to the Polity Index, Corruption, Bureaucratic Quality and Ethnic Fractionalization.

# Chapter 6

## Statistical Analysis

### 6.1 Introduction

The general relationship between aid and poverty is disputed. Moreover, there is a lack of research on how democracy affects the ability of foreign aid to reduce *poverty levels* in any given country. This chapter aims to give a general picture of the relationship between aid, democracy and poverty by using different statistical tools to reveal the causal effects of aid and democracy on poverty levels.<sup>1</sup>

Each table will be discussed, but substantive interpretation of the results and hypotheses testing will only be addressed in relation to the Arellano-Bond GMM estimator in table 6.4. The OLS and Fixed Effects estimators are applied to test the robustness of the relationship, as previous results in the cross-sectional research have been incoherent. The Arellano-Bond GMM estimator addresses the issues of both country-specific effects and the endogeneity of aid, implying that this thesis controls for these issues to a larger extent than most previous quantitative research. I therefore consider this estimator to be a better fit to the presumed relationship between aid, democracy and poverty and therefore captures the effect of democracy on aid effectiveness better than both the OLS and Fixed Effects estimators. Hopefully, this will help in making this thesis a useful contribution to the debate over aid effectiveness.

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<sup>1</sup>As discussed in chapter 5, when applying the poverty headcount ratio and allowing the poverty line to vary, it might very well turn out to be one of the most appropriate and comprehensive measures of poverty in statistical research (Foster & Shorrocks 1988a,b). However, varying the poverty headcount ratio between \$ 1.25 and \$ 2 a day had little effect on the results, and I have therefore chosen to only display the results when the dependent variable included the poverty headcount ratio of \$ 1.25 a day. However, the results from using the poverty headcount ratio at \$ 2 a day, can be found in Appendix G.

## 6.2 OLS Panel-corrected Standard Errors

As discussed in chapter 4, I apply an OLS estimator with panel-corrected standard errors as the baseline regressor. This estimator takes advantage of changes in the variables both within countries and between countries, while avoiding to a larger degree than the Fixed Effects and GMM regressors to put heavy restrictions on the data (Beck & Katz 1995). As described in the previous chapter, the poverty measure consists of an index of the poverty headcount ratio at \$ 1.25 a day, the gross secondary school enrollment for females and the infant mortality rate, and is on a scale from -1.2 to 3.12 in the original data.

Table 6.1: OLS Panel-corrected standard errors: Original Data

	(1)	(2)	(3)	(4)	(5)
	Poverty	Poverty	Poverty	Poverty	Poverty
Aid	0.0204*	0.0589***	0.0750**	0.0532**	0.0505*
	(0.0100)	(0.0136)	(0.0252)	(0.0163)	(0.0229)
Democracy	-0.0723**	-0.00500	0.00465	-0.0280	-0.0102
	(0.0250)	(0.0224)	(0.0286)	(0.0275)	(0.0292)
Aid*Democracy		-0.0115***	-0.0143**	-0.00895***	-0.00660
		(0.00278)	(0.00497)	(0.00257)	(0.00431)
Log GDP per capita	-0.609***	-0.637***	-0.589***	-0.572***	-0.494***
	(0.0671)	(0.0644)	(0.0645)	(0.0783)	(0.0799)
Log Population	0.0400	0.0453	0.0485	0.0310	0.0754*
	(0.0362)	(0.0343)	(0.0361)	(0.0516)	(0.0358)
Ethnic Fragmentalization	0.520***	0.488***	0.739***	0.338***	0.666***
	(0.147)	(0.131)	(0.130)	(0.102)	(0.0960)
Franc Zone	0.838***	0.957***	0.734***	0.998***	0.863***
	(0.118)	(0.136)	(0.175)	(0.123)	(0.127)
US Sphere of Influence	0.0813	0.140	0.173	0.205	0.275**
	(0.121)	(0.0901)	(0.0943)	(0.122)	(0.103)
Egypt	-0.617***	-0.562***	-0.500***	-0.603***	-0.464***
	(0.0716)	(0.0873)	(0.116)	(0.0708)	(0.0724)
Corruption			-0.0245		-0.0318
			(0.0327)		(0.0245)
Bureaucratic Quality			-0.0701		-0.0704
			(0.0633)		(0.0477)
Log FDI				0.0155	0.000794
				(0.0402)	(0.0403)
Log Inflation				-0.0154	0.0346
				(0.0277)	(0.0308)
Log Openness				-0.231*	-0.157
				(0.104)	(0.0908)
Observations	296	296	243	272	225

Standard errors in parentheses

\*  $p < 0.05$ , \*\*  $p < 0.01$ , \*\*\*  $p < 0.001$

Decade dummies included in the analysis, but removed from the table.

Poverty is measured on an Index from -1.2 to 3.12, consisting of the Poverty Headcount Ratio at \$ 1.25 a day, Infant Mortality Rate and Gross Secondary School Enrollment for Females. Democracy is measured by the Freedom House Index.

The estimates in Table 6.1 show the effect of democracy and aid on the level of poverty using the panel-corrected standard errors of OLS estimation on the original data before imputation. It is important to note that these estimates are not as easily interpreted as linear OLS estimates, because of the interaction between democracy and aid. The estimate for "Aid\*Democracy" is the interaction effect between the two, and

measures the change in aid effectiveness due to a movement to a higher democratic value. As mentioned in chapter 4, the introduction of an interaction term leads to the *conditional* interpretation of the estimate rather than a *general* one. This means that the interaction estimates indicate the effects of democracy when democracy is zero. Moreover, the regressor for aid, estimates the particular trends of change in poverty with changes in aid when democracy equals zero. And likewise, the estimate for democracy shows the particular trends of changes in poverty with changes in democracy when aid is zero.

The estimates for aid's effect on poverty in table 6.1 are significant at a 0.05 level across all models, but indicates a positive relationship. In following these estimates, it looks like aid contributes to more poverty. However, this is where the problem of endogeneity becomes obvious. As discussed in chapter 4, the presence of endogeneity in aid research can lead to difficulties in pinpointing the causal direction of the effect. In this case, it is likely that the estimates show a positive effect (meaning that it increases poverty) because relatively poor countries receive more aid than relatively rich countries. Because of this risk, the estimates in these models should not be taken as definitive proof of such a relationship.

The estimates for democracy's effect on poverty are insignificant in all models except from model 1. This could indicate the presence of multicollinearity when introducing the interaction term (see e.g. Friedrich 1982). It does not necessarily mean that democracy has no effect on poverty, it could simply just be because of multicollinearity with the interaction term, making it hard to separate the effects from one another.

The results for the interaction term, or for democracy's effect on aid effectiveness, in table 6.1, models 2-5, can be interpreted as indicating that democracy increases the effectiveness of aid in reducing poverty. All estimates for democracy's effect on aid effectiveness, except from the one in model 5, are significant and indicating a negative direction. If a conclusion should be drawn on these estimates alone, it would look like democracy contributes to increased aid effectiveness. However, the estimate for democracy's effect on aid effectiveness is insignificant in model 5, perhaps indicating a spurious connection.

The loss of significance can perhaps be attributed to the inclusion of all the control variables in model 5. Most likely, the effect of both institutional quality and sound economic management picked up substantial amount of the democratic effect and the effect from aid on poverty, thus eliminating democracy's direct effect on aid effectiveness. Judging from these estimates, perhaps regime type becomes irrelevant in the provision of public goods when economic policies and institutional quality is controlled for. It might be that democracies generally have a higher level of economic control and

institutional quality, thereby making democracy significant when these characteristics of a regime are not controlled for; while in fact it could be that it is these institutions and not regime type *per se* that accounts for the effect. When they are controlled for, democracy loses its effect on aid effectiveness. This is somewhat in line with the findings of Przeworski & Limongi (1993), in that the effect of democracy on aid effectiveness seem not to be captured by the regime type, but perhaps rather by economic control and institutional quality.

Selectorate theory predicts that in countries where the coalition size is large, the leadership will allocate most of the resources towards the provision of public goods in order to maximize the chances of political survival. An implication of this is therefore that democracies have a more effective aid allocation than autocratic regimes, as most of the aid goes towards public goods, rather than private goods as it would in an autocratic regime. A higher level of public goods directly impact on the lives of the poor by creating a higher general standard of living, as well as giving access to basic services such as education and health care. Moreover, Sen (1981, 1999) argues that democracies are more responsive and accountable to their citizens because of a higher level of political rights and civil liberties. Such freedoms and rights increase aid effectiveness, as the leadership is forced to listen to the people if it wants re-election.

The findings from table 6.1 in relation to selectorate theory and Sen (1981, 1999) indicate that democracy has no effect on aid effectiveness when all the controls are included. This could imply that it could be the economic policies and institutional quality of a country that dictates the provision of public goods and perhaps the responsiveness of the government, rather than regime type *per se*. Alternatively, it could indicate that the provision of public goods and the presence of an accountable government and a minimum level of political rights and civil liberties, do little to make aid more effective in alleviating poverty when these controls are present. Thus, model 5 challenges my hypotheses that democracy, and political rights and civil liberties, increase aid effectiveness, and the findings are contrary to the predictions of both selectorate theory and Sen (1981, 1999).

However, given that these estimates are based on the data before imputation, there is most likely a non-random pattern in the missing values creating bias in the results. More specifically, it might have led to selection bias and an exaggeration of the effect of democracy on aid effectiveness, as the poverty headcount was missing in countries that are often ranked as some of the poorest and least democratic countries in the world. Thus, filling in the missing values with multiple imputation might lead to less bias and control for the non-randomness of missing values in the data. Applying the same estimator to the imputed data, generates the estimates in table 6.2.



Table 6.2: OLS Panel-corrected standard errors: Imputed Data

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
	Level of Poverty	Level of Poverty	Level of Poverty	Level of Poverty	Level of Poverty	Change in Poverty	Change in Poverty	Change in Poverty	Change in Poverty	Change in Poverty
Aid	0.0040*** (0.000585)	0.000871 (0.00118)	0.00227 (0.00118)	0.00191 (0.00118)	0.00348** (0.00119)	0.000203 (0.000276)	0.000643 (0.000438)	0.000572 (0.000445)	0.000610 (0.000441)	0.000671 (0.000454)
Democracy	-0.0669*** (0.00566)	-0.0740*** (0.00587)	-0.0699*** (0.00558)	-0.0661*** (0.00547)	-0.0614*** (0.00550)	-0.000797 (0.00100)	-0.000174 (0.00109)	0.000157 (0.00115)	0.0000363 (0.00110)	0.000586 (0.00119)
Democracy*Aid		0.000825** (0.000289)	0.000555 (0.000284)	0.000662* (0.000287)	0.000297 (0.000287)		-0.000121 (0.000114)	-0.000119 (0.000114)	-0.000101 (0.000114)	-0.0000841 (0.000113)
Log GDP per capita	-0.122*** (0.0115)	-0.123*** (0.0115)	-0.124*** (0.0105)	-0.128*** (0.0112)	-0.126*** (0.0103)	-0.00295 (0.00209)	-0.00292 (0.00209)	-0.00206 (0.00215)	-0.00184 (0.00204)	0.0000608 (0.00203)
Log Population	0.0756*** (0.00577)	0.0748*** (0.00577)	0.0810*** (0.00614)	0.0590*** (0.00590)	0.0610*** (0.00621)	-0.00254 (0.00164)	-0.00260 (0.00166)	-0.00266 (0.00166)	-0.00304 (0.00196)	-0.000426 (0.000773)
Ethnic Fractionalization	0.931*** (0.0545)	0.957*** (0.0549)	0.920*** (0.0519)	0.909*** (0.0504)	0.889*** (0.0525)	0.00432 (0.00673)	0.00419 (0.00671)	0.00664 (0.00664)	0.00690 (0.00677)	0.00875 (0.00673)
Franc Zone	0.935*** (0.0311)	0.926*** (0.0320)	0.834*** (0.0268)	0.911*** (0.0335)	0.789*** (0.0273)	-0.00573 (0.00474)	-0.00617 (0.00477)	-0.00642 (0.00476)	-0.00846 (0.00490)	-0.00744 (0.00473)
US Spere of Influence	0.243*** (0.0450)	0.286*** (0.0452)	0.193*** (0.0474)	0.250*** (0.0400)	0.174*** (0.0434)	-0.00736 (0.00685)	-0.00744 (0.00685)	-0.0120 (0.00763)	-0.00963 (0.00695)	-0.0133 (0.00757)
Egypt	0.217 (0.215)	0.225 (0.215)	0.179 (0.192)	0.205 (0.212)	0.183 (0.192)	-0.0108 (0.0185)	-0.0104 (0.0186)	-0.00686 (0.0189)	-0.00924 (0.0191)	-0.0114 (0.0188)
Corruption			0.0262** (0.00833)		0.0245** (0.00830)			0.00498* (0.00229)		0.00439 (0.00228)
Bureacratc Quality			-0.122*** (0.0129)		-0.100*** (0.0121)			-0.00474 (0.00287)		-0.00449 (0.00288)
Log FDI				-0.0101*** (0.00294)	-0.00778** (0.00300)				-0.00680*** (0.00187)	-0.00678*** (0.00187)
Log Inflation				0.000181 (0.000810)	0.0000296 (0.000828)				-0.000245 (0.000644)	-0.000338 (0.000637)
Log Openness				-0.156*** (0.0171)	-0.163*** (0.0168)				0.00211 (0.00383)	0.00596 (0.00332)
Observations	7369	7369	7369	7369	7369	7369	7369	7369	7369	7369

Standard errors in parentheses

\*  $p < 0.05$ , \*\*  $p < 0.01$ , \*\*\*  $p < 0.001$

Decade dummies have been included in all models, but removed from the table.

Poverty is measured on an Index from -2.27 to 2.62, consisting of the Poverty Headcount Ratio at \$ 1.25 a day, Infant Mortality Rate and Gross Secondary School Enrollment for Females.

Democracy is measured by the Freedom House Index.

Models 1-5 in table 6.2 show the results from the same analysis on the imputed data with the level of poverty as the dependent variable. Models 6-10 use the same regressor, but applies the *change in poverty* instead of the level in poverty as the dependent variable. The application of the change in poverty rather than the level of poverty, is because it is more relevant for the use in this thesis to examine the change in poverty given a change in the independent variables, rather than measuring the level of poverty given a change in the independent variables. Moreover, it might highlight the differences in the effect of aid and democracy in the long run and in the short run. In the models with imputed data, the operationalization of poverty contains the same variables, but poverty is measured on a scale from -2.27 and 2.62.

Starting by looking at the effects of the level of poverty, the estimate for the effect of aid on poverty is significant at the 0.001 level in model 1, but the same estimates in models 2-4 are not significantly different from zero. As with democracy in the previous table, this could be because of multicollinearity. Thus, it does not necessarily mean that aid has no effect, the loss of significance is simply due to the introduction of the interaction term. The estimates for democracy's effect on poverty, on the other hand, are negative and significant at a 0.001 level in models 1-5, indicating that democracy decreases poverty.

With regards to democracy's effect on aid effectiveness in models 1-5, these estimates show a very different picture than the previous table. In models 2 and 4, the effect of democracy on aid effectiveness is in fact positive and significant, indicating that

democracy contributes to *decreased* aid effectiveness. This could imply that corruption and poor bureaucratic procedures contribute in undermining effective aid allocation. This is somewhat in line with the argument that corruption is the primary obstacle for effective aid allocation (see e.g. Knutsen 2009, Meredith 2006, Ayittey 2005, Baland et al. 2010), as it indicates that when corruption is not controlled for democracy leads to *decreased* aid effectiveness. However, when controlling for corruption and bureaucratic quality in models 3 and 5, the effect of democracy on aid effectiveness is no longer significant. This indicates that when institutional quality is controlled for, democracy no longer contributes to decreased aid effectiveness. Thus, when corrupt practices are present in a democracy, it might not work as hypothesized in this thesis. This could reflect the poor quality of many new democracies, especially in sub-Saharan Africa as discussed in chapter 3, and the challenges of making democratic institutions work in accordance with their intentions in such regimes.

However, even when such practices are controlled for, democracy does not contribute to increased aid effectiveness, as the results from the interaction term is insignificant in models 3 and 5. As with the previous findings from table 6.1, these findings could indicate that the provision of public goods and the presence of a minimum level of political rights and civil liberties have little impact on aid effectiveness. Thus, the results from models 1-5 in table 6.2 are contrary to the empirical expectations and hypothesizing in this thesis, and further challenges the hypotheses promoted in chapter 3. However, the change in direction of the democratic effect on aid effectiveness from table 6.1 could also reflect the uncertainties around the imputed data; highlighting the need for caution when drawing general conclusions from these models.

When turning to models 6-10 and the change in poverty, it would seem like democracy has no effect on aid effectiveness, as all of the estimates for the interaction term are insignificant. In fact, when switching to to the change rather than the level in poverty it is not only democracy's effect on aid effectiveness that turns insignificant, the effect of democracy on poverty no longer has a significant effect; neither does aid. This may indicate that there is a much smaller reaction to aid inflows and democracy in the short-run than in the long-run. Generally, there are very few estimates that are significant in the models measuring the effect on a change in poverty. Only the logarithm of FDI is significant in all estimates, and corruption is significant on a 0.05 level in model 8 only. The indications from these models, that democracy has no effect on aid effectiveness, are contrary to selectorate theory and Sen (1981, 1999), and further challenge my hypotheses. In line with the previous findings, these models also indicate that the presence of political rights and civil liberties, as well as the provision of public goods, do little to improve the effectiveness of aid in reducing poverty.

To sum up the findings from the OLS estimation, it looks like democracy has no significant impact on aid effectiveness; implying that the provision of public goods and the presence of a minimum level of political rights and civil liberties have little effect on the effectiveness of aid in reducing poverty. This is contrary to the predictions of selectorate theory and the theory of Sen (1981, 1999), and challenges the hypotheses put forward in chapter 3. However, the results from the different specifications of the relationship vary greatly; making it clear that the effect of democracy on aid effectiveness cannot confidently be drawn from the OLS results alone. Democracy's effect on aid effectiveness is far from clear and the interaction effect is non-robust. Performing the regression on the original data, democracy seems to contribute to increased aid effectiveness in the alleviation of poverty in some models, in others the democratic effect is not significantly different from zero. On the imputed data, however, the effect is the opposite; that democracy contributes to decreased aid effectiveness. Furthermore, when applying the change of poverty instead of the level of poverty, the results turn out insignificant. In these models alone, the interaction effect has gone from negative and significant to positive and significant to negative and insignificant.

Moreover, there are several indications that an OLS estimation with panel-corrected standard errors is not the correct specification of the relationship. As observed by Green et al. (2001), when there are country-specific effects in the data, and when these effects are correlated with the independent variables, regression estimates in OLS will be biased; even if the OLS uses panel-corrected standard errors. Beck & Katz (1995) show that whether the standard errors estimated in OLS with panel-corrected standard errors are overestimated or underestimates depends on sample variation. Omitted variable bias and country-specific effects can easily prove to make these results inconsistent. The changes in significance and direction of the estimates from Table 6.1 to Table 6.2 models 1-5, is most likely based on unobserved variables that correlate systematically with the error term. In TSCS data, this is often caused by unobserved country-specific effects. As discussed in chapter 4, the assumption behind the OLS regressor is that omitted variables do not correlate with the variables included in the model. This could lead to insignificant estimates, as observed in table 6.2, because of an enhanced error term. Thus, it seems fairly plausible that the assumptions for OLS estimation do not hold, and that country-specific effects must be controlled for.

### **6.3 Fixed Effects**

The Fixed Effects estimator accounts for country-specific effects by introducing a constant for every country included in the sample, controlling for time-invariant variables that correlate with the variables included in the analysis. Thus, it should provide a

more appropriate specification of the relationship than the OLS estimator.

Table 6.3: Fixed Effects

	(1)	(2)	(3)	(4)	(5)
	Change in Poverty	Change in Poverty	Change in Poverty	Change in Poverty	Change in Poverty
Aid	0.00169*** (0.000378)	0.00185* (0.000809)	0.00169* (0.000807)	0.00191* (0.000811)	0.00162* (0.000811)
Democracy	-0.0128*** (0.00327)	-0.0124*** (0.00370)	-0.0102** (0.00370)	-0.0104** (0.00371)	-0.00906* (0.00370)
Democracy*Aid		-0.0000449 (0.000212)	-0.000106 (0.000211)	0.00000386 (0.000212)	-0.0000399 (0.000211)
Log GDP per capita	-0.0230*** (0.00394)	-0.0230*** (0.00394)	-0.0175*** (0.00400)	-0.0169*** (0.00402)	-0.0130** (0.00405)
Log Population	0.0126 (0.0102)	0.0126 (0.0102)	0.0163 (0.0102)	0.0190 (0.0102)	0.0214* (0.0102)
Ethnic Fractionalization	-0.147 (0.191)	-0.146 (0.191)	-0.135 (0.191)	-0.136 (0.191)	-0.125 (0.190)
Corruption			0.0278*** (0.00532)		0.0265*** (0.00542)
Bureaucratic Quality			-0.0432*** (0.00687)		-0.0376*** (0.00700)
Log FDI				-0.0158*** (0.00247)	-0.0154*** (0.00247)
Log Inflation				-0.000833 (0.000764)	-0.000842 (0.000762)
Log Openness				-0.0178 (0.00962)	-0.00382 (0.00985)
Observations	7369	7369	7369	7369	7369

Standard errors in parentheses

\*  $p < 0.05$ , \*\*  $p < 0.01$ , \*\*\*  $p < 0.001$

Decade dummies were included in the analysis in the analysis, but have been removed from the table.

Poverty is measured on an Index from -2.27 to 2.62, consisting of the Poverty Headcount Ratio at \$ 1.25 a day, Infant Mortality Rate and Gross Secondary School Enrollment for Females.

Democracy is measured by the Freedom House Index.

Table 6.3 shows the results when applying a Fixed Effects regressor on the change in poverty, thereby controlling for country-specific effects and omitted variable bias. The fact that many of the estimates that were not significant in the OLS models are now significant, can indeed indicate that there were country-specific effects that were not controlled for in the OLS, that now are modelled into the analysis. Implicitly, the region dummies for the Franc Zone, the US Sphere of Influence and Egypt have been removed from the analysis, as the Fixed Effects control for the effect from these variables whether they are explicitly included or not.

The effect of aid on poverty in this table indicates that aid contributes to more poverty. The estimates for aid's effect on poverty are both positive and significant at the 0.05 level across all models. The estimates for democracy's effect on poverty indicate the opposite relationship; that democracy contributes to decreased poverty and are significant at a 0.05 level across all models. However, again this could be due to the presence of endogeneity; not only between aid and poverty, but also between democracy and poverty. In the same way as relatively poor countries receive more aid than relatively rich ones, relatively democratic countries might experience less poverty than relatively autocratic ones. This highlights the importance of clarification of the causal

direction, and further urges the need to apply a statistical model that accounts for this problem to as large an extent as possible.

Turning to the effect of democracy on aid effectiveness in table 6.3, there seems to be no such effect present as none of the interaction terms are significant. This creates even more doubt of the existence of such a relationship. However, the Fixed Effects estimator draws heavily on the variation in the variables *within* countries, and correspondingly less on the variation *between* countries. Given that both the level of democracy and the level of poverty change slowly within countries, valuable variation can have been lost in the estimation of the effects. This could explain why the effect of democracy on aid effectiveness remains insignificant.

The results from the Fixed Effects regression on democracy's effect on aid effectiveness, indicate that democracy has no significant impact on aid effectiveness. As with both the findings from table 6.1 and 6.2, this could imply that the provision of public goods and the presence of an accountable government and a minimum level of political rights and civil liberties are not as important as hypothesized in this thesis. That all the models so far indicate this relationship, or rather the lack of such a relationship, strengthens the inference that no such relationship exist; or at least, that such a relationship is not captured in these models. This is contrary to the predictions of selectorate theory and Sen (1981, 1999), and challenges my hypotheses. Moreover, although the model of Meltzer & Richards (1981) is not applied directly to the statistical analysis in this thesis, the lack of a robust relationship between democracy and aid effectiveness in the models so far, could indicate that the redistributive qualities of democracy, as addressed in their model, does not apply to the allocation of aid. As aid qualifies as un-earned income, the findings could indicate that the leadership in a democracy does not consider it necessary to redistribute the aid to the same extent as the income from taxes. Thus, it might be harder to establish a robust effect of democracy on aid effectiveness, than on democracy's effect on poverty.

However, a Fixed Effects regression applies rather stringent use of the data and eliminates cross-sectional variation in the dependent variable, and the limitations of the OLS can have rendered the results inconsistent in that estimator. To ensure that I do not keep a false null hypothesis, I should be careful to reject the hypothesis that democracy increases aid effectiveness based on these results alone.

## 6.4 Arellano-Bond Difference GMM

The results in the analyses so far has challenged the claim that democracy contributes to increased aid effectiveness and questioned the ability of the provision of public goods and a minimum level of political rights and civil liberties to improve the ef-

fectiveness of aid. Both the OLS and Fixed Effects regressors showed few indications of a robust effect of democracy on aid effectiveness. However, I argue that these models might have failed to correctly specify the relationship between aid, democracy and poverty; because of the complexity of the causal relationship and because of problems in the data that could not be sufficiently addressed by these estimators.

As discussed in chapter 4, the Fixed Effects regressor might be inconsistent when there is endogeneity between the variables in the analysis. Endogeneity has proved to be an issue in most aid research, potentially rendering the Fixed Effects estimator inappropriate. Moreover, few serious measures have been taken to account for endogeneity in the existing TSCS aid literature (see e.g. Boone 1996, Burnside & Dollar 2000, Hansen & Tarp 2001). Mostly, it has been modelled into the analysis by applying exogenous variables as instruments. However, such a method leaves no room for unobserved effects. When country-specific effects are correlated with the initial level of poverty, it would render the instrumental variables inconsistent. The third estimator applied in this thesis, the Arellano-Bond GMM estimator, takes into account that the variables are correlated with the error term, and there is support in the literature for its application in TSCS research on aid effectiveness (see e.g. Hansen & Tarp 2001).

Table 6.4 shows the results from the Arellano-Bond GMM estimator. Models 1-5 show the estimated effects when democracy is measured by the Polity Index, thus representing the estimated effects of electoral democracy. Models 6-10 measures the estimated effects when democracy is measured by the Freedom House Index, thus constituting the estimates of substantive democracy. The differences in effects between the two measures are the basis for testing my two hypotheses; on the effect of democracy on aid effectiveness, and the significance of political rights and civil liberties.

The "Sargan test" at the bottom of the table shows the p-value for the sargan test for overidentifying restrictions. When this value is larger than 0.05, the GMM estimator should be consistent. In models 1, 2 and 3 for the Polity measure, the Sargan test is significant, indicating that the instruments could be correlated with the error term, thereby making the applied instruments invalid. The instruments refer to the lag(s) between the independent and dependent variables (see e.g. Hansen & Tarp 2001). Invalid instruments could indicate that there is still unmodelled and uncontrolled endogeneity in these models. In models 4 and 5, however, the Sargan test is insignificant, leading to conclusions of validity of the instruments. In models 6 and 7, when measuring democracy by the FHI, the Sargan test is significant, indicating that the instruments are not enough to account for endogeneity in the model. However, in models 8,9 and 10, the test results are insignificant, implying that the instruments included in the model are valid and that the GMM estimator is consistent.

Table 6.4: Arellano-Bond GMM

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
	Poverty	Poverty	Poverty	Poverty	Poverty	Poverty	Poverty	Poverty	Poverty	Poverty
L.Poverty	0.387*** (0.0114)	0.417*** (0.0110)	0.422*** (0.0104)	0.431*** (0.0102)	0.423*** (0.00991)	0.407*** (0.0115)	0.441*** (0.0111)	0.446*** (0.0104)	0.448*** (0.0103)	0.437*** (0.00993)
Aid	0.00312*** (0.000351)	0.00322*** (0.000353)	0.00306*** (0.000363)	0.00411*** (0.000342)	0.00335*** (0.000336)	0.00271*** (0.000359)	0.00413*** (0.000773)	0.00449*** (0.000736)	0.00490*** (0.000735)	0.00468*** (0.000710)
Democracy	-0.0111*** (0.000769)	-0.0103*** (0.000858)	-0.00902*** (0.000866)	-0.00777*** (0.000797)	-0.00700*** (0.000764)	-0.0218*** (0.00325)	-0.0168*** (0.00359)	-0.0115*** (0.00337)	-0.0127*** (0.00332)	-0.00906** (0.00320)
Democracy*Aid		-0.0000205 (0.0000475)	-0.0000474 (0.0000486)	-0.000113* (0.0000455)	-0.000109* (0.0000442)	(0.000325)	-0.000348 (0.000199)	-0.000665*** (0.000190)	-0.000329 (0.000189)	-0.000498** (0.000183)
Log GDP per capita	-0.0962*** (0.00506)	-0.0943*** (0.00486)	-0.0827*** (0.00444)	-0.0834*** (0.00444)	-0.0741*** (0.00424)	-0.0962*** (0.00508)	-0.0940*** (0.00491)	-0.0816*** (0.00453)	-0.0820*** (0.00450)	-0.0728*** (0.00430)
Log Population	-0.0640*** (0.0105)	-0.0574*** (0.0104)	-0.0615*** (0.00978)	-0.0559*** (0.00982)	-0.0542*** (0.00940)	-0.0695*** (0.0106)	-0.0640*** (0.0105)	-0.0641*** (0.00992)	-0.0580*** (0.00991)	-0.0554*** (0.00949)
Ethnic Fractionalization	-0.0169 (0.172)	-0.0326 (0.173)	0.0408 (0.168)	-0.0113 (0.169)	0.0249 (0.165)	-0.106 (0.175)	-0.0862 (0.176)	-0.0252 (0.171)	-0.0448 (0.171)	-0.0111 (0.167)
Corruption			0.0580*** (0.00462)		0.0517*** (0.00459)			0.0571*** (0.00471)		0.0513*** (0.00466)
Bureaucratic Quality			-0.0968*** (0.00603)		-0.0843*** (0.00597)			-0.0957*** (0.00616)		-0.0839*** (0.00607)
Log Inflation				-0.000796 (0.000725)		-0.000572 (0.000696)			-0.000907 (0.000737)	-0.000715 (0.000706)
Log FDI				-0.0316*** (0.00234)		-0.0319*** (0.00224)			-0.0322*** (0.00238)	-0.0324*** (0.00228)
Log Openness				-0.110*** (0.00965)		-0.0720*** (0.00943)			-0.116*** (0.00975)	-0.0792*** (0.00953)
Sargan test	0.00	0.00	0.03	0.33	0.18	0.00	0.00	0.11	0.55	0.31
Observations	7020	7020	7020	7020	7020	7020	7020	7020	7020	7020

Standard errors in parentheses

\*  $p < 0.05$ , \*\*  $p < 0.01$ , \*\*\*  $p < 0.001$

Decade dummies were included in the analysis of all the models, but have been removed from the table.

Models 1-5 are the estimates effects when democracy is measured by the Polity Index, while models 6-10 are the estimated effect when democracy is measured by the Freedom House Index.

Poverty is measured on an Index from -2.27 to 2.62, consisting of the Poverty Headcount Ratio at \$ 1.25 a day, Infant Mortality Rate and Gross Secondary School Enrollment for Females.

The overall picture that can be drawn from this table is that while both aid and democracy has a significant relationship with poverty, they also have the opposite effect. This is the same relationship as displayed in the previous tables. While an increase in democracy decreases poverty, an increase in aid does in fact lead to an increase in poverty. These effects are significant at the 0.01 level across all models. The estimates of the interaction effect between democracy and aid in the alleviation of poverty are negative in all models, but only significant under certain specifications.

For electoral democracy, in models 1-5, the estimate for democracy's effect on aid effectiveness is significant at the 0.05 level in models 4 and 5. These are the models where economic policies and management are controlled for, and in these models the effect of democracy on aid effectiveness is negative and significant in that it increases aid effectiveness. In models 2 and 3, on the other hand, it seems like there is no effect of democracy on aid effectiveness as the estimates are insignificant.

The lack of significance in the democratic effect on aid effectiveness, could indicate omitted variables bias. This means that in models 2 and 3, there are effects influencing poverty, democracy and aid that are not controlled for. When controlling for economic policies, the effect of democracy on aid effectiveness becomes significant at the 0.05 level, indicating that omitted variable bias might very well be the source of the non-significant estimates in the other models. Indeed, it might indicate that when leaving out the set of controls for economic policies, the model fails to capture the effect of democracy on aid effectiveness as the controls influence both.

As argued in the previous chapter, these sets of controls are included because I expect them to influence both democracy, aid and poverty. Leaving them out could therefore lead to omitted variable bias, as could be the case in this instance. If this is the case, it is likely that it is models 4 and 5 that reflect the best fit of the relationship between democracy and aid effectiveness. The results from the Sargan test confirms that models 1, 2 and 3 might be inconsistent, corroborating the suggestion of the most suitable model specification for models 4 and 5.

However, the significance of the estimate for democracy's effect on aid effectiveness in models 4 and 5 could also indicate that these controls could be endogenous to democracy. This means that the level of FDI, inflation or openness could be influenced by the level of democracy; that democracy affects aid effectiveness through its influence on economic policies. Again, this goes to show that caution must be executed when drawing conclusions from this analysis. This is a complex relationship that probably works through many channels and causal paths, leading to unstable and non-robust estimates.

Despite the shortcomings of the data and the complexity of the real causal relation-



ship, however, models 4 and 5 in table 6.4 nevertheless indicate that democracy does in fact increase aid effectiveness, and the effect is significant at a 0.05 level.

Turning to models 6-10 and the effect of substantive democracy on aid effectiveness, the effect seem contingent on a different relationship. Only in models 8 and 10 are the estimates significant; the models where corruption and bureaucratic quality are included. As with the models for electoral democracy, this could be an indication of omitted variable bias, in that corruption and bureaucratic quality influence both democracy, aid and poverty. If this is the case, the estimates in models 8 and 10 might very well be the correct specification of the relationship. This suggestion is corroborated by the insignificant test values for the Sargan test in models 8 and 10. Indeed, this might indicate that these are the most plausible model specifications for the relationship. However, as with electoral democracy, this effect could also be due to the endogeneity of corruption and bureaucratic quality in relation to democracy. It is therefore difficult to say anything certain about a democratic effect on aid effectiveness. Nevertheless, models 8 and 10, as models 4 and 5, does indicate that there is a significant effect of democracy and that this effect increases aid effectiveness. This could imply, contrary to the findings in the other tables, that the provision of public goods and a minimum protection of political rights and civil liberties improves the effectiveness of aid in relation to poverty reduction. Furthermore, it could also imply that the redistributive qualities of democracy as highlighted by Meltzer & Richards (1981) also applies to resources from aid, even though these resources qualify as un-earned income.

## 6.5 Hypotheses Testing

For the sake of hypotheses testing I apply the full models (models 5 and 10) because of the test value for the Sargan test and the significance of the estimates. Because of the risk of omitted variable bias in the other models, I argue that these models present the most plausible specifications of the relationship. Thus, I test the effect of political rights and civil liberties in a democracy where economic policies and institutional quality are controlled for. This might affect the results of the analysis, but is a necessary precaution to ensure that I measure the effect of democracy in a model that is consistent (referring back to the test results for the Sargan test).

At the first glance at table 6.4, it does seem like substantive democracy has a more significant impact than electoral democracy on the effectiveness of aid, as the effect of democracy on aid effectiveness in models 6-10 have both smaller p-values and a larger estimated effect. This is in line with the theoretical predictions of Sen (1999) in that democracies with a minimum level of political rights and civil liberties are more re-

sponsive and attentive to the needs of the people and therefore distribute more aid to where it is the most effective. These estimates also question the importance of elections as the only tool for ensuring democratic processes. However, it is important to recall that the estimates for democracy's effect on aid effectiveness are the effects of democracy when democracy is 0. This means that for Polity this is for a regime that is neither a democracy nor an autocracy. The interpretations of the estimates in models 6-10, however, are stated in hypothetical terms, because the FHI does not incorporate the value 0. The estimates are thus extrapolations beyond the observed range, making it more fruitful and appropriate to evaluate the conditional relationship within the observed range of values of democracy. Moreover, the supposedly stronger effect of substantive democracy could be due to the fact that the Polity Index is a more fine grained index, with 21 different categories compared to Freedom House's 7. This would manifest itself in showing a larger effect of the FHI, just because one step higher on the scale implies a larger increase of democratic transition than one step higher on the Polity Index. To inspect the effect of democracy on aid effectiveness at higher levels of democracy, further inspection of the data is needed.

### Polity

In order to be able to say anything about the effect of democracy at higher levels of democracy, or indeed to say anything meaningful about the effect of substantive democracy compared to electoral democracy, some calculations must be employed. The generalized linear model specification for interaction effects is (see Friedrich 1982):

$$Y = b_0 + b_1 X_1 + b_2 X_2 + b_3 (X_2 X_3) \quad (6.1)$$

Which can be rewritten as either:

$$Y = (b_0 + b_1 * X_1) + (b_2 + b_3 * X_1) X_2; \text{ or} \quad (6.2)$$

$$Y = (b_0 + b_2 * X_2) + (b_1 + b_3 * X_2) X_1 \quad (6.3)$$

Examining the impact of the Polity Index and applying the generalized linear model specification for interaction effects to model 5, the specification is:

$$Y = (-0.007 * X_2) + (0.00335 - 0.000109 * X_2) * X_1 \quad (6.4)$$

The effect of aid ( $X_1$ ) is

$$Y = (0.00335 - 0.000109 * X_2) \quad (6.5)$$

This gives a model for the effectiveness of aid at different levels of electoral democracy ( $X_2$ ):

$$Y = (-0.007 * X_2) + (0.00335 - 0.000109 * X_2) * X_1 \quad (6.6)$$

$$X_2 = -10 : (-0.007 * -10) + (0.00335 - 0.000109 * -10) * X_1 = 0.074X_1 \quad (6.7)$$

$$X_2 = -6 : (-0.007 * -6) + (0.00335 - 0.000109 * -6) * X_1 = 0.046X_1 \quad (6.8)$$

$$X_2 = -3 : (-0.007 * -3) + (0.00335 - 0.000109 * -3) * X_1 = 0.025X_1 \quad (6.9)$$

$$X_2 = -2 : (-0.007 * -2) + (0.00335 - 0.000109 * -2) * X_1 = 0.018X_1 \quad (6.10)$$

$$X_2 = -1 : (-0.007 * -1) + (0.00335 - 0.000109 * -1) * X_1 = 0.01X_1 \quad (6.11)$$

$$X_2 = 1 : (-0.007 * 1) + (0.00335 - 0.000109 * 1) * X_1 = -0.0038X_1 \quad (6.12)$$

$$X_2 = 3 : (-0.007 * 3) + (0.00335 - 0.000109 * 3) * X_1 = -0.018X_1 \quad (6.13)$$

$$X_2 = 6 : (-0.007 * 6) + (0.00335 - 0.000109 * 6) * X_1 = -0.039X_1 \quad (6.14)$$

$$X_2 = 10 : (-0.007 * 10) + (0.00335 - 0.000109 * 10) * X_1 = -0.068X_1 \quad (6.15)$$

It is clear from these calculations that the more democratic a regime is, the more effective is the aid in reducing poverty. I have chosen not to include calculations of the effect of democracy on aid effectiveness at all levels of democracy because the included calculations clearly reflect the direction and trend of the relationship. When a country is rated with a score of 6 on the Polity Index for instance, which makes up 25 % of my data and is where a country is first classified as a "democracy", aid decreases poverty with 0.039 for every 1 % increase in aid as a share of GDP on the poverty scale from -2.27 to 2.62. When the country is classified as an "open anocracy" at score 3, aid only decreases poverty with 0.018 for every 1 % increase in aid as a share of GDP. What is most worrisome, though, is that when a country classifies as a "closed anocracy" or "autocracy", aid does in fact increase poverty with 0.025 and 0.046 for every 1 % increase in aid as a share of GDP respectively. Between the score 0 and 1, that is in an "open anocracy", democracy leads to aid being able to decrease poverty, rather than to increase it. 45 % of the units of analysis are in this category or higher, leaving 55 % in lower categories. According to these calculations, this implies that in most cases aid is in fact contributing to more poverty. However, when a country becomes democratic from "open anocracy" or higher, aid becomes effective in alleviating poverty. This indicates that, according to the Polity Index, a country needs democracy from "open anocracy" or higher for aid to work.

It could be useful to look at the effects of democracy on aid effectiveness in relation to specific country examples to illuminate its importance. For instance, when looking at the predictions of the model in relation to Benin, a clear pattern surfaces. In only a few years, Benin went from being ranked as an "autocracy" in 1989 to be classified as a "democracy" in 1995 according to the Polity Index. Looking at the difference in

effectiveness of aid when keeping aid constant at 1989-level, gives an indication of the effect of democracy on aid effectiveness as predicted by this model when looking at aid's ability to decrease the level of poverty in 1989 and 1995.

In 1989, Benin scored -7 on the Polity Index, and received aid amounting to 17 % of GDP. This gives a predicted effect of aid on poverty:

$$Y = (-0.007 * -7) + (0.00335 - 0.000109 * -7) * 17 = 0.053 * 17 = 0.9 \quad (6.16)$$

According to the predictions of this model, aid contributed to a rise in poverty of 0.9 points on the poverty scale from -2.27 to 2.62 in Benin when the country was an anocracy. Comparing this effect to the effect of aid when Benin was a democracy (received a score of 6 on the Polity Index), gives the predicted level of aid effectiveness:

$$-0.039X_1 = -0.039 * 17 = -0.66 \quad (6.17)$$

According to the predictions of this model, aid contributed to a decrease in poverty of 0.66 on the scale from -2.27 to 2.62 when Benin was ranked as a democracy. Holding everything else constant, this indicates that democracy increased the effectiveness of aid in Benin with 1.56 points on the poverty scale. In other words, these numbers indicate, and the model predicts, that democracy increased aid effectiveness in Benin as the country became more democratic.

However, these numbers say nothing of the uncertainty related to the estimates in table 6.4. Figure 6.1 illustrates the marginal effect of aid as democracy increases with 95 % confidence intervals. The marginal effect of aid is based on the estimates in table 6.4, model 5. The figure shows that a 1 % increase in aid as a share of GDP is increasingly effective (meaning that it leads to less poverty) with higher levels of democracy. The effect is significant at a 0.05 level at most levels of the Polity measure. In this figure the Polity measure was transformed to a continuous scale with a minimum of 0 and a maximum of 1, so as to make it easier to compare the effects of Polity to the effects of Freedom House, which is transformed in the same way in the next figure (the tables belonging to these figures can be found in Appendix H). In this way, the differences in scale is no longer relevant, making it easier to spot the differences in effect and test the second hypothesis in my thesis. The figure illustrates the relationship between democracy and aid effectiveness, and it indicates that the effectiveness of aid do increase with higher levels of democracy; aid becomes more effective in reducing poverty as democracy increases. This could indicate that the relative size of the winning coalition and elections, are important mechanisms in the effective allocation of aid. Furthermore, it could imply that the provision of public goods does in fact impact on the effectiveness of aid in reducing poverty.

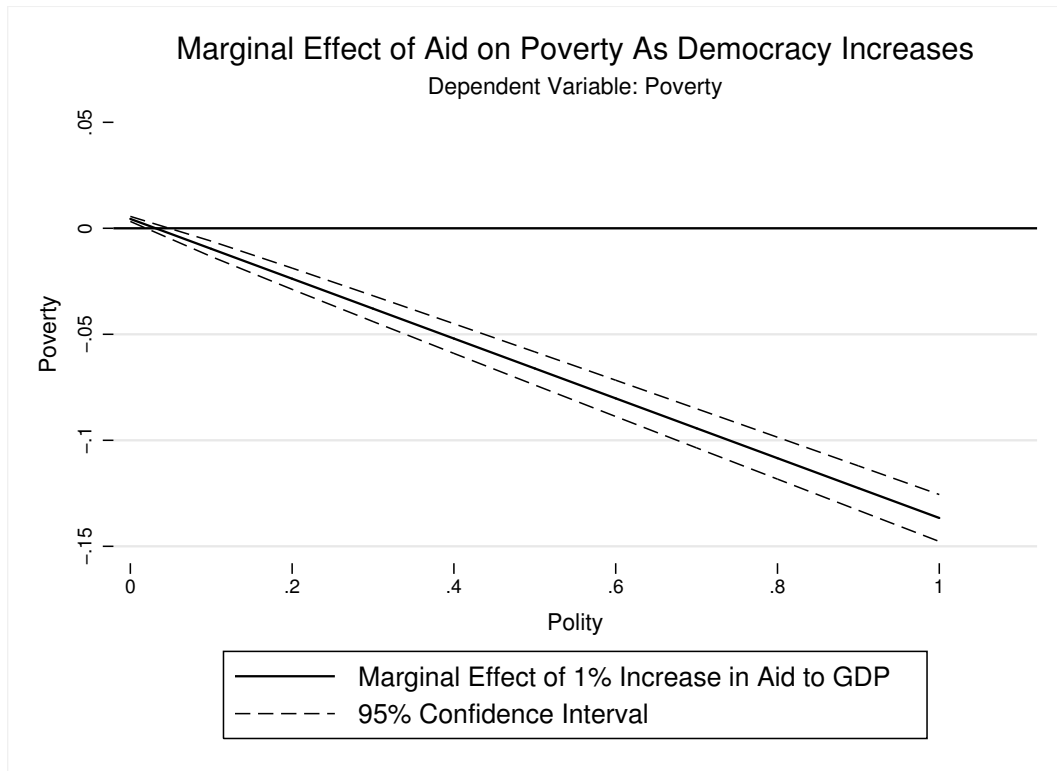


Figure 6.1: Marginal Effect of Aid on Poverty as Democracy Increases: Polity

### Freedom House

In order to see whether political rights and civil liberties have any additional effect on aid effectiveness at higher levels of democracy, the same calculations must be performed on the measure from Freedom House. By plotting in the numbers from table 6.4, model 10, I get the predicted effect of aid at different levels of substantive democracy:

$$Y = (-0.00906 * X_2) + (0.00468 - 0.000498 * X_2) * X_1 \quad (6.18)$$

The effect of aid ( $X_1$ ) is

$$Y = (0.00468 - 0.000498 * X_2) \quad (6.19)$$

This gives a model for the effectiveness of aid at different levels of substantive democracy ( $X_2$ ):

$$X_2 = 1 : (-0.00906 * 1) + (0.00468 - 0.000498 * 1) * X_1 = -0.0049X_1 \quad (6.20)$$

$$X_2 = 2 : (-0.00906 * 2) + (0.00468 - 0.000498 * 2) * X_1 = -0.014X_1 \quad (6.21)$$

$$X_2 = 3 : (-0.00906 * 3) + (0.00468 - 0.000498 * 3) * X_1 = -0.024X_1 \quad (6.22)$$

$$X_2 = 6 : (-0.00906 * 6) + (0.00468 - 0.000498 * 6) * X_1 = -0.052X_1 \quad (6.23)$$

$$X_2 = 7 : (-0.00906 * 7) + (0.00468 - 0.000498 * 7) * X_1 = -0.062X_1 \quad (6.24)$$

These calculations reveal that a country that scores 6, and is thus rated as "free" in the FHI, decreases poverty by 0.052 for every 1 % increase in aid as a share of GDP. However, only 6 % of the units of analysis are ranked this high, or higher. Most of the country-years in the sample are ranked at 3.5 or lower, decreasing the effect of aid to only -0.024 for every 1 % increase in aid as a share of GDP when a country is ranked as "partly free". In the lowest category "not free", aid only decreases poverty by -0.0049 for every 1 % increase in aid as a share of GDP. However, less than 10 % of the sample is in this category.

Expanding on the effect of substantive democracy, it is useful to look at the case of Benin to examine the effect of substantive democracy on aid effectiveness as well. Benin went from scoring 1 and being ranked as "not free" in 1989 to scoring 6 and being ranked as "free" in 1995 on the FHI. As mentioned earlier, the country received aid amounting to 17 % of GDP in 1989. Predicting the effectiveness of aid in 1989 from the estimated model, gives:

$$-0.0049X_1 = -0.0049 * 17 = -0.08 \quad (6.25)$$

This means that poverty decreased by 0.08 on a poverty scale from -2.27 to 2.62 when Benin was ranked as "not free". When holding the level of aid constant, the effectiveness of aid in 1995 when Benin was "free", gives:

$$-0.052X_1 = -0.052 * 17 = -0.88 \quad (6.26)$$

This model predicts that aid decreased poverty by 0.88 on a scale from -2.27 to 2.62 in Benin in 1995. It is obvious that the effectiveness of aid increased dramatically in only 6 years, and holding everything else constant, indicates that democracy is the source of this increase. Notwithstanding the uncertainties attached to these estimates, the effects do point towards a democratic effect on increased aid effectiveness.

Returning to the general effect of democracy on aid effectiveness, it is interesting to note that while the lower categories of the Polity Index contribute to aid increasing poverty levels, this is not the case with the FHI. According to the FHI, democracy is

not needed to make aid effective. This could indicate that there are certain aspects of the volatility of autocracies that the FHI does not pick up. The assumption of a linear relationship, although no longer additive, can also conceal some of the effect, as it gives the *average* effect of moving from one point of democracy to one higher point. However, this could deflect on the effect of aid, as the estimate for aid's effect on poverty in model 10 of table 6.4 is higher than the estimate in model 5 in table 6.4. According to the estimates in these models, the effect of aid on poverty is more damaging when using the FHI, while the effect of democracy on poverty is all the more substantial compared to the Polity Index.

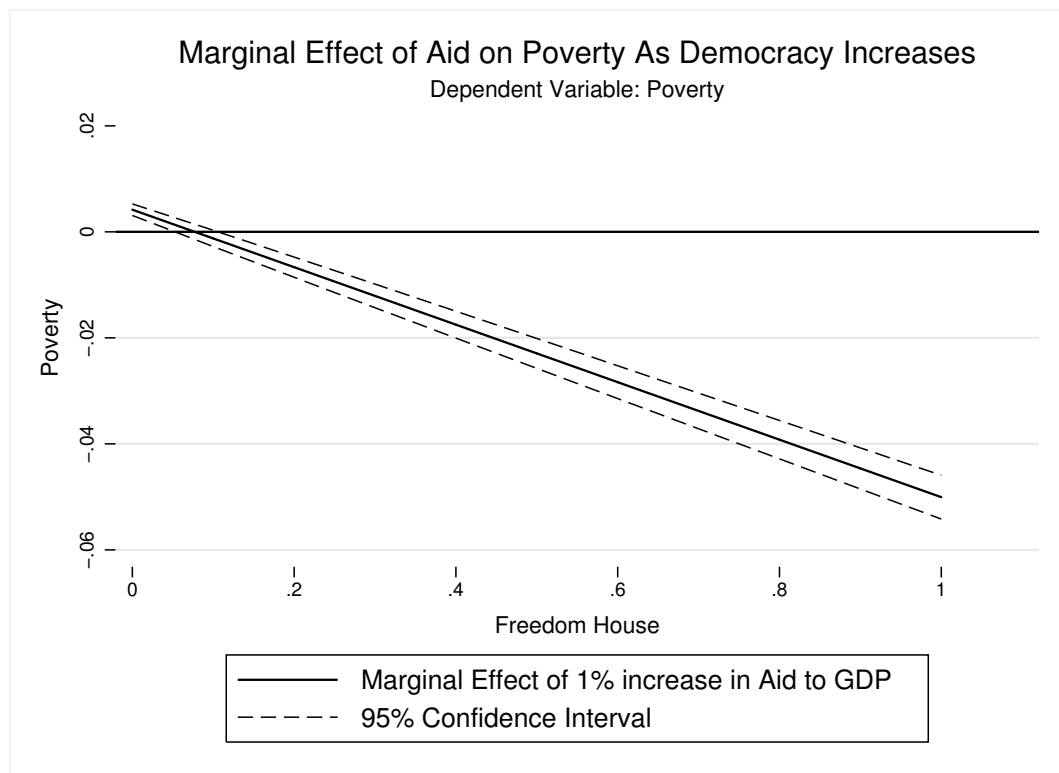


Figure 6.2: Marginal Effect of Aid on Poverty as Democracy Increases: Freedom House

Moreover, despite the seemingly larger and more substantiated effect of substantive democracy on aid effectiveness in table 6.4, the calculations indicate that it is in fact the Polity estimate that has the largest effect on aid effectiveness at higher levels of democracy. This relationship is corroborated when displaying the relationship graphically.

Figure 6.2 illustrates the marginal effect of aid as democracy increases when democracy is measured by the FHI. It is based on the estimates in model 10 in table 6.4. The figure shows that a 1 % increase in aid as a share of GDP is increasingly effective (meaning that it leads to less poverty) with higher levels of democracy. The effect of

substantive democracy is significant at a 0.05 level at most levels of democracy. Figure 6.2 illustrates that aid becomes increasingly effective at higher levels of democracy; the same relationship as detected in figure 6.2. However, the effect is slightly smaller in this figure.

Along with the calculations, figure 6.1 and 6.2 indicate that electoral democracy has a larger effect on aid effectiveness than substantive democracy. This could imply that political rights and civil liberties perhaps are not as important as hypothesized in this thesis. In relation to my theoretical framework, it could further imply that the provision of public goods are more important than a minimum level of political rights and civil liberties in the effective allocation and implementation of aid, indicating the importance of the relative size of the winning coalition and elections in effective aid.

### **6.5.1 Concluding on Hypothesis I: The Democratic Effect**

When the controls for economic management and institutional quality are present, the findings from this analysis are in line with the predictions of selectorate theory; that democracies provide more effective aid allocation. There are clear indications of a democratic effect on aid effectiveness, also at higher levels of democracy. In fact, figures 6.1 and 6.2 clearly indicate that as democracy increases, so does aid effectiveness. Both figures are in line with the predictions of selectorate theory in that democracies provide more effective aid than non-democratic regimes. In accordance with selectorate theory, this could imply that democracies allocate more of the aid towards public goods, and that the provision of aid as public goods leads to aid being more effective in alleviating poverty.

When these controls are not present, however, the findings indicate that democracy has no effect on aid effectiveness, which is contrary to the predictions of selectorate theory. This result is in line with the findings from the analysis when applying the OLS or Fixed Effects estimators. Nevertheless, assuming that the GMM regressor provides the most appropriate specification for the relationship between democracy and aid effectiveness, and that the inclusion of economic policies and institutional quality provides for the correct causal specification, the results indicate that democracy does increase aid effectiveness. More formally, these results corroborate hypothesis I; that democracy leads to higher aid effectiveness. According to selectorate theory, democratic regimes provide a higher level of public goods than autocratic regimes because of the leader's desire for political survival. Following Bueno de Mesquita et al. (2003), the democratic effect on aid effectiveness indicated in these results might stem from the fact that more of the aid is directed towards the provision of public goods rather than private goods in democracies. Aid will therefore have a larger effect in democratic



regimes than in autocratic regimes, as the aid directly impacts on the living conditions of the poor by the provision of a higher level of public goods. This implies that the relative size of the winning coalition and elections might very well prove to be important mechanisms in the effective allocation of aid. The case study in the next chapter expands on this notion and illuminates the importance of these mechanisms on the effectiveness of aid in a low-income democracy.

## **6.5.2 Concluding on Hypothesis II: The Effect of Political Rights and Civil Liberties**

The same relationship between democracy and aid effectiveness is detected in both figure 6.1 and figure 6.2, although the effect is slightly smaller in figure 6.2 than in figure 6.1. This could indicate that political rights and civil liberties might not contribute further to increased aid effectiveness in democracies as measured by the Polity Index. In fact, it might indicate that the democratic elements and aspects highlighted in the Polity measure, such as competitiveness and openness of political participation and executive recruitment, are more important for the effective allocation of aid than political rights and civil liberties. This is contrary to the predictions of Sen (1999), in that regimes with a minimum level of political and civil rights will be more effective in allocating aid than regimes without these freedoms and rights. These results therefore challenge the second hypothesis that political rights and civil liberties enhance the likelihood of effective aid allocation. This could indicate that the winning coalition is indeed an important mechanism for effective aid allocation in democracies, perhaps even more so than political rights and civil liberties.

One possible implication of these results is that in democracies that experience fair electoral procedures, political rights and civil liberties do little to improve the effective allocation of aid. Assuming that democratic leaders are motivated by the desire for political survival, elections might very well be a more effective mechanism in the allocation and distribution of aid than the presence of political rights and civil liberties. Democratic leaders might choose to distribute the aid in accordance with the allocation that brings in the most votes in fear of not getting re-elected. Thus, elections as a mechanism might be sufficient to ensure that aid allocation is in line with where the aid is most effective. However, as discussed in chapter 3, Sen (1999) argues that it is the presence of political rights and civil liberties that ensures that elections are meaningful and competitive, and thus an important mechanism in effective aid allocation. This effect might have been picked up by the Polity Index by measuring the competitiveness of executive recruitment and the openness of political participation. In fact, these elements of the democratic election process might be dependent on an existing minimum

level of political rights and civil liberties, thereby implicitly including an element of the importance of these rights and freedoms in democratic processes. However, this cannot confidently be concluded from this study alone, and whether this is the case can be further substantiated and clarified by the case study in the next chapter.

## 6.6 Short Discussion

It is clear from the analyses above that the choice of estimator matters a great deal when examining the relationship between aid and poverty. The estimated effect of democracy on aid effectiveness is highly sensitive to different specifications of the relationship. In the OLS regression, the interaction effects between democracy and aid were negative and significant in the original data, but positive and significant in the imputed data. Moreover, when measuring the change in poverty rather than the level of poverty, democracy seemed to have no effect on aid effectiveness. The same relationship was observed when applying the Fixed Effects estimator; democracy had no impact on the effectiveness of aid. However, when applying the GMM estimator, democracy had a negative and significant impact on aid, indicating that democracy contributes to increased aid effectiveness. This goes to show that only minor adjustments and specifications of the statistical model might have potentially large consequences for the conclusions of a democratic effect on aid effectiveness. Nevertheless, as thoroughly established in chapter 4 and here, the Arellano-Bond GMM has several features that render this the most plausible model for capturing the relationship between aid and poverty. Consequently, the statistical results of my thesis would indicate that democracy contributes to higher aid effectiveness. Nonetheless, that the results from the different analyses are highly sensitive to the use of estimator, indicates that caution has to be executed when drawing conclusions and generalizations despite the convincing characteristics of the Arellano-Bond GMM model.

It is also worth noting that the effects of both democracy and aid are significant across most of the models included in this analysis. The difficulty in establishing a robust relationship between democracy and aid effectiveness might therefore reflect that there is an extra challenge in making foreign aid effective in reducing poverty, perhaps because of some of the characteristics of aid as discussed in chapters 2 and 3; including the conditional nature of much foreign aid, the fungibility of aid and strategic considerations of the donors. Moreover, it could also reflect the democratic limitations and challenges facing many low-income democracies, as discussed in chapter 3. When trying to account for both these measures in the effect on poverty, it might be hard to pinpoint a clear and robust effect because of the inherent difficulties in both measures.

### **6.6.1 A Note on Endogeneity and Aid**

It is worth noting in all tables, the seemingly positive effect of aid on poverty; meaning that aid contributes to more poverty. This is a highly controversial statement, and it is likely that the estimated effect is due to problems in the data that could not or have not been properly addressed. Most likely it is caused by problems of endogeneity. That aid seemingly contributes to more poverty could indicate that there is still endogeneity in the data that has not been sufficiently controlled for, even after applying the Arellano-Bond GMM estimator to account for this problem. However, it could also indicate that the effect is in fact present, and that foreign aid does contribute to higher levels of poverty.

Notwithstanding the ability of the Arellano-Bond GMM estimator to correctly specify the relationship, I urge for further research on the relationship between aid and poverty before jumping to conclusions of aid's failure to lift people out of poverty. The model might have failed to remove all endogeneity, or the relationship might be too complex to be captured in a statistical model. By the same token, it is also wise to keep a little scepticism of such a profound democratic effect on poverty levels. Given the potential presence of endogeneity, this effect might be because democracies generally have lower levels of poverty; not because democracy leads to less poverty.

## **6.7 Concluding Remarks**

In addition to the issue of endogeneity in aid regressions, a general note of caution is due as these results are based on imputed data. Although estimates of the most plausible specifications of the relationship indicate that democracy has a desirable effect on aid effectiveness, this relationship is not robust nor undisputable. Nevertheless, the results from the Arellano-Bond GMM models do indicate that democracy contributes to increased aid effectiveness, increasing the confidence on the existence of such a relationship. However, political rights and civil liberties seem to add little to the effectiveness of aid compared to an electoral democracy.

This analysis revealed interesting aspects of the relationship between democracy and aid effectiveness, and the case study in the next chapter expands on the findings in this chapter. How does this democratic effect play out in a low-quality democracy? Why is it that political rights and civil liberties seem less important than hypothesized? The next chapter will look closer at some of the mechanisms underlying the democratic effect on aid effectiveness and hopefully bring clarity on the aspects that are still left unanswered by the statistical models; such as the importance of the relative size of the winning coalition, elections and the role of political rights and civil liberties in the effective allocation and implementation of aid.



# Chapter 7

## Democracy and Norwegian Aid in Zanzibar

### 7.1 Introduction

The statistical analysis in the previous chapter indicates that democracy contributes to increased aid effectiveness. However, these results are neither robust nor conclusive. As illustrated by the discussions in chapter 3, the mechanisms that are at work in a democracy are many and complex, and there is a good chance that the full extent of the relationship was not captured by the statistical models. Moreover, the statistical analysis could not clarify the importance of the relative size of the winning coalition or political rights and civil liberties. Chapter 3 highlights the importance of the relative size of the winning coalition and elections; accountability and political rights and civil liberties; and political pressure as important mechanisms in effective aid allocation. In order to answer my research question, an in-depth study of the democratic mechanisms at work in a low-income democracy in relation to aid allocation is necessary. This chapter and case study will clarify the causal relationship between democracy and aid effectiveness and highlight the importance of the mechanisms discussed in chapter 3.

I have chosen to look into the process with and implementation of a subsea cable from mainland Tanzania to Pemba, and hopefully find and illuminate the democratic processes and mechanisms in Zanzibar<sup>1</sup> that took place during this project.

However, the democratic processes in Zanzibar are questionable, and the democratic values and meanings of its institutions are limited. This makes Zanzibar a rather

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<sup>1</sup>The project was under the jurisdiction of the Ministry of Water, Land, Construction and Energy, a Ministry that is autonomous to Zanzibar and independent of the Union with Tanzania. Notwithstanding the importance of the support from CCM on the mainland, the project was the responsibility of the government of Zanzibar alone, making the Union government more or less irrelevant in this project.

difficult test-case, and the democratic limitations might lead to less effective aid allocation and implementation. The case illustrates some of the main dilemmas facing developing democracies, and illuminates the processes behind aid allocation in a low-quality democracy. Amongst other, the case highlights the importance of elections as a means to exert political pressure, as well as the importance of political and civil rights to achieve a fair and equal distribution of development aid. In fact, as a consequence of the general lack of political rights and civil liberties in Zanzibar, democratic mechanisms does not always work as expected, if they work at all. Democracy, as such, might therefore not have the modifying effect on aid effectiveness as hypothesized in this thesis.

## 7.2 Short Background and History

The United Republic of Tanzania is made up of mainland Tanganyika and the islands of Zanzibar. Zanzibar consists of two islands; Unguja, which is normally the island addressed as Zanzibar, and its smaller neighbor Pemba (Jahre 2008, Bakari 2001).

The current political situation is complex, with Zanzibar having their own separate government as well as the Union government consisting of Zanzibar and Tanganyika. The two governments are independent of each other in several areas, while at the same time, the government of Zanzibar is not completely autonomous and many aspects of Zanzibar politics is controlled by the government in Dar es Saalam (Tronvoll 2010a, Brown 2010, Jumbe 1994).

The International Law and Policy Institute (ILPI) (Tronvoll 2010a) sum up the electoral process and democratic institutions of Zanzibar in a short and concise matter: "The Zanzibar president is elected through direct popular vote. In the House of Representatives (HoR), with a total of 81 members, 50 seats are directly elected through the first-past-the-post single-member constituency system for a five-year term. Presidential appointees fill another 11 seats; including two seats from the opposition and one seat for the Zanzibar Attorney General". Further five seats are reserved for regional commissioners appointed by the government, and 15 seats are especially reserved for women.

Historically, Zanzibar has been a commercial center between Africa and the Arab countries, and a strategic point for both European and Arab countries (Bennett 1978). The islands have a long history, including both Arab, Portuguese and British rule. It was the strict British hierarchy where Europeans were on the top, Africans at the bottom, and Arab in between, that led to an establishment of a sultanate at the time of independence in 1963 (Bennett 1978). The British backed the Arab dominated Zanzibar Nationalist Party (ZNP) in government despite the victory of Afro-Shirazi Union

(later the Afro-Shirazi party - the ASP) in the first election. However, this proved to be a fateful alliance. Only a month after receiving its independence as a sultanate, in January 1964, a violent and bloody revolution overthrew the government as the nationalist ASP couped the power and proclaimed Zanzibar a republic (Brown 2010).

It was the leader of the ASP, Sheik Abied Amani Karume, that was installed as President of the new republic (Brown 2010). In 1964, Tanganyika president, Julius Nyerere, approached Karume with the intention of creating a union, and together the two countries formed the United Republic of Tanzania. In 1977, the ASP united with Nyerere's party, the Tanzania African National Union (TANU), to form the Chama Cha Mapinduzi (the Party of the Revolution) (CCM). Following the revolution and the formation of the Union with Tanganyika, a one-party system was introduced in Zanzibar, as in Tanganyika (Brown 2010).

### **7.2.1 Politics in Multi-party Zanzibar**

Although Zanzibar has multiple political parties, only two of them are large enough to win constituencies and thereby have members in the House of Representatives. The CCM has held the Presidency in Zanzibar since the revolution, while the major opposition in Zanzibar was and is the Civic United Front (CUF), the heir of the ZNP (Brown 2010, Bakari 2001).

The CUF was created in 1992, when the country opened up for more than one political party. It was established by old members of the CCM, that had either been fired or been thrown out of the CCM, and subsequently put in prison and treated poorly. When they were allowed to create their own party, they drew from their own experiences with the state's abuse of power to create a party with a much clearer focus on human rights than the CCM. They became a party that articulated people's frustrations with the state's abuse of power (Informant 2 [Interview]).

The first multi-party election was held in 1995, with subsequent elections every five years. The elections in 1995, 2000 and 2005 were all characterized by accusations of election fraud, political violence and civil unrest as CUF claimed that the CCM used undemocratic measures to ensure victory (Tronvoll 2010b).

Today, Zanzibar has a coalition government named the Government of National Unity, consisting of both CCM and CUF. The reconciliation process between the two parties officially started on the 5th of November 2009, and ended in a referendum in October 2010, giving a 66.4 % majority in favor of the suggestion of a Government of National Unity (Tronvoll 2010b, 4). The Presidential election in 2010 following the referendum showed a different side to Zanzibar democracy that had been absent in previous elections: Despite the narrow margin differentiating the two presidential can-

didates from CCM and CUF,<sup>2</sup> the reactions following the announcement of the winner were mostly positive and peaceful (Tronvoll 2010a, 24).

### 7.3 Political Roots

Ever since the reign of the sultan, there has been a gap in the development happening in and resources being invested in Unguja and Pemba.<sup>3</sup> This divide was only strengthened by the 1964 revolution, because of Pemba's unwillingness to participate actively in the revolution.<sup>4</sup> Since then, they have been regarded as traitors and cowards by the people of Unguja (Informant 2 [Interview]). The government created immediately after the Revolution did not hold any positions for the people of Pemba; all leaders involved in the revolution came from Unguja, and hence all subsequent ministers and government officials came from Unguja (Informant 7 [Interview]). Without democracy there was no need for such a government to divert resources to Pemba. For this reason Unguja has received more attention, more resources and more development.

The CCM and the CUF each represent more or less half of the population of Zanzibar, and each political party represents its own island; CCM on Unguja, CUF on Pemba (Tronvoll 2010a,b). The differences and rifts within the population of Zanzibar are expressed through politics, more specifically through support for these two political parties. The fact that there are two parties of nearly equal strength vying for power and control of the government,<sup>5</sup> has created a cocktail of political instability, inter-island conflict, contested elections and violence (Tronvoll 2010b, 4).

The political system only allowed for one party in government, completely excluding the opposition from partaking in governmental affairs (Tronvoll 2010b, 4). The exclusion of CUF from government has led to political tension and violent clashes between the two political groups. There is a widespread perception that Pemba has been punished for its role in the revolution, and until recently it still manifested itself in the government policies between the two islands, as Pemba did not receive as many benefits, aid or attention as Unguja (Informant 2 [Interview]). The result is that Pemba is not only much poorer than Unguja, it is in fact the poorest region in Tanzania. It has created the most profound division amongst Zanzibaris; that between Pemba and

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<sup>2</sup>The CCM Presidential Candidate, Ali Mohamed Shein, only received 3,471 more votes than the CUF candidate, Seif Sharif Hamad (African Elections Database 2010).

<sup>3</sup>Because of a feud between Sultan Said and a local tribe in Pemba, the Sultan put his commercial center in Unguja.

<sup>4</sup>While the African population on Unguja rose up to the revolution, the African population on Pemba did not take part. The Indian and Arab population on Pemba was much more integrated than in Unguja (Informant 2 [Interview]).

<sup>5</sup>In the elections of 2010, CCM won with merely 50.11%, while CUF received 49.14 % of the votes (African Elections Database 2010).



Unguja, between CUF and CCM.

## 7.4 The Subsea Cable

Unguja has been provided with electricity through a submarine cable from Ras Kiromoni to Fumba, while Pemba did not receive the same level of quality electricity supply. Old and worn down equipment led to low capacity as well as pollution and frequent power outages; the transportation of diesel and the replacement of broken parts could be lengthy processes to fix. According to Zanzibar officials, the lack of reliable power in Pemba has led to the island falling behind on social and economic development (Informant 4, Informant 7, Informant 8 [Interviews]). Moreover, it also led to political unrest and a feeling of disunity between the two islands of Zanzibar (Informant 3 [Interview]).

In 1986 the Norwegian government was approached by the government of Zanzibar with the request of sponsoring the Rural Electrification Project (REP). During the early 1990s the Norwegian government financed three phases of the project, but the work was put on hold when political unrest broke out as a result of political reforms. However, phase IV was resumed in 2004 and completed in 2009 (Poyry 2011, 9). Despite the rural electrification of the two islands of Unguja and Pemba, supply of electricity was unsatisfactory in Pemba; it was unreliable and random, and the large generators supplying the electricity polluted its surroundings and the environment. The infrastructure on the island was there, but the source of the power was still unsatisfactory. Due to the positive consequences of REP, it was decided to add an extension of phase IV in 2006, that would include and finance a pre-feasibility study of laying a subsea cable from Tanga on the mainland to Pemba. This study concluded that it was not only technically possible but that it would be economically advantageous given the rise in oil prices (Poyry 2011, 9).

A subsea cable from the mainland to Pemba was first brought to the attention of the Zanzibar government in 1991. However, at that time it was considered technological impossible, and was rejected. It was only in 2006 that the project, as an extension of the REP, was suggested by the Project Manager, Norwegian Knut Riise, and promoted by the CCM government in accordance with his suggestions. The project was financed by a 300 million NOK grant from the RNE in Dar es Salaam, along with 100 million NOK from the Union and Zanzibar government (Lomoey 2008).<sup>6</sup> The work on the project

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<sup>6</sup>The total cost of the project was 400 million NOK, 150 million NOK more than originally estimated. As it were, NOK 400 million were far higher than what the Embassy could contribute to the project. Norad argued that the Embassy should conduct more detailed studies on possible alternatives for power supply on Pemba, and believed that investing in Heavy Fuel Oil (HFO) generation was the better al-

was concluded in May 2010, when Pemba was connected to the mainland electricity grid; ending the dependence on pollutive and unreliable generators.

### **7.4.1 Impact on Poverty**

Electricity, along with education, health care and clean water, is amongst the most important prerequisites for development (Informant 1 [Interview])(Baum & Lake 2003, Government of Norway 2009). The subsea cable, providing Pemba with stable electricity from the mainland, is therefore expected to contribute to the development of the islands of Zanzibar and the alleviation of poverty in Pemba. If implemented correctly and in accordance with democratic principles, the outcome of the cable is expected to be a significant decrease in poverty levels over the next 30 years (Informant 1 [Interview])(Government of Norway 2009). The impact of the cable is anticipated to be multi-dimensional and due to complex factors, and a baseline study was conducted in 2009 to collect information on the various variables that is likely be affected by the subsea cable (Government of Norway 2009). According to the baseline study (Government of Norway 2009), in 2004/2005 infant mortality rate was 61 per 1000 live births, secondary school enrollment for females was 88.5 %, and basic needs poverty headcount was 60 % in Pemba. Unfortunately, there are no measures of expected effects, and the first assessment of the impact of the cable is not due until 2014 (Government of Norway 2009, 54).

However, people on Pemba are already witnessing small changes in living conditions and prosperity. Before the project was implemented people were leaving Pemba; now they are building in Pemba. Pemba is changing. Informant 7 [Interview] states: "It is a promising attitude now, those who come to visit Pemba have enough power at an affordable price; there is money being invested in Pemba. Not only from outside investors, but also from the government". He continues: "The power supply to Pemba has done a lot for the people in Pemba, as well as for the government. The economy will be boosted, for the people on the district level to government level".

However, the project does not directly affect the very poorest segment of the population in Pemba. The primary beneficiaries are the people that can afford to pay the connection fee, or already have a connection, as they receive stable electricity straight into their homes (Informant 1, Informant 5, Informant 9 [Interviews])(Government of Norway 2009). From those who can afford to get the electricity to their homes, women and children are benefitting the most (Informant 4 [Interview]). In many communities

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ternative. In the end, RNE managed to raise the budget to NOK 300 million by postponing the Pemba Rural Road Project, releasing NOK 50 million (Lomoey 2008). The Union government and the government of Zanzibar were able to come up with the remaining NOK 100 million to get the project up and running.

in Zanzibar, water and housework is the domain of women. Women are responsible for fetching the water, cleaning and finding fuel for cooking dinner. Now, after the implementation of the cable, mothers do not have to walk for hours each day to get water and children can do their homework after school because they do not need to search for firewood for their family, or in the evening as the family does not depend solely on natural lights anymore (Informant 4, Informant 7 [Interviews]).

More importantly, however, is that this project carries with it numerous indirect effects for the people living in extreme poverty (Informant 1, Informant 3, Informant 7 [Interviews]). There is now streetlights and village waterholes, as well as stable electricity supply to schools and hospitals. People can start operating small machinery, and there is increased employment opportunities in building projects or administrative positions of new industry (Informant 7 [Interview]). All these examples represent benefits from stable electricity supply for the very poorest segment. Such public goods are indirectly improving the lives of whole communities, but arguably does not impact on the lives of the poorest in a direct way.

The allocation of aid towards this subsea cable is considered to be an effective way of reducing poverty in Pemba. It will most likely impact on the indicators chosen in the operationalization of poverty in this thesis, by contributing to more girls being able to stay in school longer, and increase employment opportunities and the establishment of small business and small-scale industry. It will likely also increase the quality of health care, thus improving maternal health and decreasing infant mortality. Moreover, this investment will probably have a larger effect on poverty levels than the same investment in Unguja. Because of the poor standards of public goods in Pemba compared to Unguja, this project will be more effective on Pemba than it would have been in Unguja. This is because the level of development is lower than on Unguja, automatically leading to a larger impact on Pemba. Because there was no stable electricity before this cable, the implementation of the cable will have a much larger effect than if reliable electricity was already present. The more developed a community is, the more effort must be put into making it even more developed. Because of the poor state of the living conditions in Pemba, it did not require a lot of effort to improve it significantly (Informant 3, Informant 6 [Interviews]). The cable represented one such effort, and its expected impact on poverty levels reflects this.

## **7.5 The Struggle for Political Influence and Survival**

Throughout the process, it was clear that the Pembans preferred the subsea cable to other alternative ways of bringing electricity to the island. Comparing their situation to the situation on Unguja, it seemed obvious that a cable would be the superior solu-

tion.<sup>7</sup> For the CCM, the cable presented an opportunity for giving Pemba some form of rectification; to redeem itself for all the years when Unguja had been prioritized. The cable was an attempt and a means to present the Pembans with tangible proof that they were being treated equally with Unguja (Poyry 2011, 1). However, CCM's desire to redeem and prove themselves to Pembans was rooted in political interest and the struggle for votes and political support.

After the introduction of multi-party democracy, CCM has been looking for ways to win elections. So far, the party has used both honorable and less honorable measures to ensure this (Informant 2 [Interview]). Some of the less honorable includes excluding CUF voters from the voter's register, physically restraining CUF supporters and other efforts generally aimed at undermining the democratic election process. It is a firm belief amongst CUF supporters in Zanzibar that the CCM cheated their way into government in each and all elections; 1995, 2000 and 2005 (Informant 2, Informant 6 [Interviews]). Indeed, the CCM has won the elections with merely some thousand votes; a very narrow margin, and with international observers noting irregularities in the election process (Tronvoll 2010a, 4).

However, in the election in 2005, the support for CUF on Pemba had become so solid that no matter how many CUF supporters they were able to exclude from the election the result was still victory for CUF on Pemba (African Elections Database 2010). With support for CUF increasing,<sup>8</sup> CCM most likely figured out that the election results from Pemba could not be manipulated to the extent of giving CCM seats on the island in future elections. CCM therefore turned to more honorable methods of collecting votes, most prominently the attempt to provide and implement development projects. CCM has explicitly used the provision of public goods as a strategy to win votes, while at the same time raising the question of what the CUF has ever provided for the population. During election campaigns and rallies, CCM has pointed to the provision of public goods that has taken place in Pemba as evidence of the party's ability to provide development (Informant 2 [Interview]). Their only opportunity to obtain any support on Pemba, and to keep their voters on Unguja, was to show that the CCM did in fact have good policies and delivered on their promises. The cable project was therefore initiated with the intention of showing the Pemba people once and for all who brought development to the island.

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<sup>7</sup>The people of Unguja, which had enjoyed the supply of energy through a subsea cable for more than 30 years, experienced far better quality in their supply than the Pembans (Jahre 2008, 27).

<sup>8</sup>Since the elections of 2000, CUF's total rating has gone up (African Elections Database 2010).

### 7.5.1 The Importance of the Winning Coalition

Remembering the definition of the winning coalition from chapter 3; that the winning coalition is the proportion of the electorate that is sufficient to keep the leader in power. The electorate is a collection of individuals "from which a leader draws supporters to form a winning coalition", and that the leader must have the support of the winning coalition to stay in power (Bueno de Mesquita & Smith 2009, 314). The electorate in Zanzibar consists of all Zanzibari adults over the age of 18 who are registered voters (Government of Zanzibar 1984).<sup>9</sup> In a democracy, the winning coalition is typically made up by a relatively large part of the electorate.

One implication of electorate theory is that a relatively large winning coalition would promote the distribution of aid as a public good. Compared to the electorate, Zanzibar did have a relatively large winning coalition at the time the process with the cable started in 2006. Of Zanzibar's 1 million inhabitants, 700,000 is found on Unguja and 300,000 on Pemba. The winning coalition of CCM was made up mostly of people from Unguja; and very few from Pemba. The fact that the government required a majority of the constituencies to hold power, implies that the winning coalition was indeed relatively large compared to the electorate. However, the distribution of aid as public goods was not completely equal nor public, in contradiction to what electorate theory predicts. Compared to Unguja, Pemba received very little aid as public goods.

The geographical positioning of the voters, with CUF supporters on Pemba and CCM supporters on Unguja, made it easier for the CCM government to isolate the provision of goods to only Unguja. When CCM held all political power in Zanzibar, or when they considered it an easier solution to cheat their way to political power, the winning coalition was made up of only supporters from Unguja. Hence, they only needed to provide goods for the people of Unguja. It is therefore possible to say that the provision of goods in Zanzibar was characterized as a mix of private and public goods, or local public goods; the government provided the people with goods, but only in Unguja where the support for the winning coalition was. This indicates that a relatively large winning coalition does not automatically lead to distribution of aid as the provision of public goods, as the geographical positioning of voters can make it easier to reward only one segment of the population while excluding others. This is contrary to the predictions of electorate theory.

Prior to the election in 2005, the CCM government failed to account for its whole population because it did not consider it necessary for political survival; Pemba did not constitute a part of the winning coalition of the party in power. CCM could easily retain

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<sup>9</sup>The status of who qualifies as a "Zanzibari" is somewhat ambiguous (see Tronvoll 2010a, 5-6).

power with the support of Unguja alone. This implies, as discussed and predicted in chapter 3, that the government allocated the aid in line with what it conceived as being necessary for survival in political office. As a consequence, the provision of goods, as well as foreign aid in Zanzibar has largely been directed towards the largest island, Unguja, where most of the support for CCM can be found.

However, given the strong position of CUF on Pemba and its increasing influence on Unguja after the election in 2005, CCM realized that it could no longer stay in power with support from Unguja alone. The party needed to attract new voters, including the voters on Pemba. Moreover, the solid support for CUF meant that the CCM government could no longer stay in power by using dishonorable measures, and needed votes to secure victory in the upcoming election. The cable was implemented as a legitimate political strategy to win votes in Pemba.

### **The Role of Elections**

This struggle over political votes demonstrates some of the mechanisms and processes at work in a democracy. In a democratic regime, political survival is obtained through re-elections in contested elections (Bueno de Mesquita et al. 2003). In this case, the desire for political survival ensured that CCM needed to attract new voters; and by this token, incorporating a larger proportion of the population in their coalition. The winning coalition could no longer be sustained on the support from Unguja alone; the party also needed the support of the people of Pemba. Thus, the relative size of the winning coalition grew compared to the size of the electorate as CCM realized its dependence on the support from Pemba as well as from Unguja for political survival.

The efforts made to ensure political survival was based in the fear of losing office in the upcoming election in 2010. The upcoming election worked as a mechanism to ensure that the desire for political survival led to competition over political votes and voters. Elections thus proved to be an important mechanism for the provision and fair distribution of aid in Zanzibar, as well as an important mechanism in determining the size of the winning coalition.

An empirical implication of this case is that the 2010 election in Zanzibar ensured a political competition favorable to the distribution of aid as a public good, as the desire for political survival increased the struggle for votes and enhanced the size of the winning coalition. In accordance with selectorate theory, an increase in the relative size of the winning coalition resulted in a higher level of aid as public goods being distributed and implemented in Pemba. More specifically, the inclusion of voters from all geographical segments of the population resulted in the allocation of aid to Pemba, but only when it was considered necessary for political survival. The growing support for CUF also indicates that the reduction of poverty is an important strategy for en-

hancing the likelihood of political survival in Zanzibar. Only when poverty reduction on Pemba became essential for re-election and political survival did the government consider Pemba a vital part of their winning coalition and implement the cable project.

However, elections alone are not a sufficient condition for effective aid allocation and implementation, as the allocation of aid prior to the competition for voters for the 2010 election demonstrated. The struggle for votes and political competition is an integral part of why elections proved such an effective mechanism in this case. This highlights the importance of *contested* elections and emphasizes the significance of the inherent ability of the population to put pressure on and influence the government.

## 7.6 Political Pressures

A theoretical implication of the contributions from Meltzer & Richards (1981) and Acemoglu & Robinson (2000) is that political pressure will lead to more redistribution of aid. Indeed, there was considerable pressure from the people of Pemba on the government, manifested through support for CUF (Informant 2, Informant 9 [Interviews]). CUF used the issues related to the "underdevelopment" of Pemba to stimulate support and put pressure on the government in Unguja. During election rallies, CUF pointed out the lack of development and the poor standard of public goods in Pemba, blaming it on the CCM. They used the campaign to show what Pembans did not receive from the government; they used it to show the failure of the government to account for the people on Pemba (Informant 2 [Interview]). The political pressure from CUF articulated a general dissatisfaction with the government, and the more issues the people were displeased with, the more support CUF obtained. Only when CUF obtained enough influence did CCM realize that their coalition would not be victorious unless they gained the support of the Pemba people and included them in the coalition. Political pressure from CUF was thus a considerable part of why the winning coalition could no longer be sustained on the support from Unguja alone and the subsequent decision to allocate aid to Pemba. It was thus pressure on the government by the opposition and the increased support of CUF that eventually led to an expansion of the winning coalition.

Although the provision of aid through public goods is determined by the relative size of the winning coalition, it would seem like it was the ability of the population to exert pressure on the government that led to an expansion of the winning coalition. However, when looking closer at the mechanisms for political pressure or popular pressure, there are indeed indications that this was less important than originally assumed, shedding doubt over the actual importance of democratic mechanisms in this case.

### 7.6.1 The Pattern of Political Support

The ability of the population to exert political pressure can be questioned when considering that voting patterns in Zanzibar seem to be independent of political policies of the two parties. According to the model of Meltzer & Richards (1981), the poor would exert pressure as a united group to achieve more redistribution. The theory predicts that the population would vote in accordance with the party that offered the most distribution of aid, and that effective aid allocation is dependent on that the poor stand united as an economic *and* political group. Furthermore, selectorate theory considers the provision of public goods a prerequisite for political survival, indicating that a party will survive in political office by providing public goods. However, all of CCM's measures to obtain more votes in Pemba has yet to pay off. CUF stands as strong as ever in Pemba, with the CCM receiving no more votes than they have always received (Informant 2 [Interview]). This is contrary to what both the theory of Meltzer & Richards (1981) and selectorate theory would predict.

It seems like there are other factors that determine how the people of Zanzibar vote than their interest for the provision of public goods or distribution of aid. It is a question of identity. There is no rational evaluation of political issues or which policies would benefit them. People vote in accordance with what their family has always voted, what their friends are voting (Informant 2 [Interview]). Especially on Pemba there is a very strong social justice; social cohesion is used to make people continue to vote CUF. Explicit references to the revolution and enemy images of the CCM as the "others" were being created; "you cannot vote for the people who killed your grandfather, they are mainlanders, they do not understand you". CUF used accusations about CCM to rally up support on Pemba, while CCM did the exact same in Unguja (Informant 2 [Interview]). The result was that the people of Zanzibar seemed unable to show disapproval of their government by voting for another party, as switching parties was synonymous with being cut off from friends and families in many parts of the islands. However, there is a possibility that people were not switching from CUF to CCM because they believe that CUF would provide them with more public goods, and redistribute more aid and development projects to Pemba than CCM.

A closer inspection of the election results from 2005 and 2010 (Tronvoll 2010a, 22-24) reveals that CUF has strengthened their position in Unguja, from 26 % of the votes in 2005 to 29 % of the votes in 2010. On the same token has CCM lost supporters in Unguja, from 73 % in 2005 to 70 % in 2010. Interestingly, CUF has lost almost 3 % support in Pemba, while CCM has gained more than 2 %. This could indicate that CCM's efforts are paying off, and that the social justice and cohesion previously experienced in Pemba is weakening. This is more in line with the predictions of both selectorate



theory and the theory of Meltzer & Richards (1981), that the provision of public goods and distribution of aid increase the likelihood of political survival.

Moreover, although it is hard to pinpoint the exact economic division of the voters, the voters on Pemba are generally conceived of as being poorer than the voters from Unguja (Government of Norway 2009). An implication of the theory of Meltzer & Richards (1981), is that when a large proportion of the population is poor, there will be more redistribution than if a small proportion of the population is poor. The empirical application of this inference is that even though a large part of the population is poor in Zanzibar, it did not automatically lead to more redistribution. However, the inclusion of Pemba into the winning coalition led to the implementation of the cable and thus increased the redistribution of foreign aid. This indicates that when a large part of the influential voters are poor, after the inclusion of Pemba in the winning coalition, democracy has gained the ability of further distribution of aid in Zanzibar.

As discussed in chapter 3, the poor do not necessarily vote in accordance with their economic position or as a united group. In this case, even though potentially less and less, other alliances are still more important than the economic interest, such as family ties and social bonds. This might inhibit the ability of the poor to press their demand, as they do not stand collected in the desire for economic benefits, which is contrary to what is expected from the model of Meltzer & Richards (1981). If social justice and political loyalty prevails before rational political considerations, the political consequences might be a total disregard for the well-being of the population and a switch back to private goods as a way to reward supporters. Moreover, elections might lose its distributive qualities as discussed in the previous section. Such a system, where people vote in accordance with social ties and loyalties provides few incentives for the politicians to provide development for anyone else than their own supporters. Nonetheless, if it is the case that social cohesion is decreasing, then the ability of the poor to stand united and put pressure on the government might be increasing. Fortunately, in this case the social alliance between Pembans and the subsequent support for CUF were conducive to the obtainment of public goods and alleviation of poverty.

## **7.6.2 The Distribution of Aid to the Poor**

A further implication of the contributions from Meltzer & Richards (1981) and Acemoglu & Robinson (2000) that is closely linked to the ability to exert pressure on the government, is that more aid is allocated to those segments of the population that are relatively poor in democracies, as inequality leads to more redistribution. If a large part of the population in a country is poor, democracies redistribute more of the aid to the very poorest segment in the country. Pemba is the poorest region in Tanzania

(Government of Norway 2009, 31), so in this way and in this project, it may be true that democracy contributed to aid being distributed to the poorest segment of the population. On the other hand, the poorest segment in Pemba is not the primary beneficiaries of this project. As such, aid has been allocated to the very poorest region in the country, but not to the poorest segment in this region. It can be argued, therefore, that the fact that the very poorest segment is not the primary beneficiaries of this project, is evidence of a lacking ability of the very poorest to press their demand.

The political pressure experienced by the CCM might not have been due to the desire of the poorest people in Pemba to receive the cable, but rather that the political opposition used the rugged conditions on Pemba strategically to point out flaws and limitations in the policies of the government, gaining political support for CUF. However, CUF could have been influenced by its voter segments in Pemba, and used this in the election campaigns. On the other hand, many of the most successful and influential Zanzibaris vote CUF (Informant 2 [Interview]). They could have promoted the subsea cable as a means to improve the conditions for overall development and create an investment-friendly environment. Their influence might have mattered more in the decision to provide Pemba with stable electricity than the pressure from the people living in extreme poverty. The fact that the outcome is the same, namely the implementation of the subsea cable, could be perceived as giving the poor more political power than they actually have. Indeed, that their interests were coinciding, although fortunate, might have been purely coincidental.

Coinciding interests call into question the theoretical assertion that the ability of the poor to press their demand was a decisive factor in the decision of laying the cable. This is contrary to the predictions and theoretical implications of the theories of Meltzer & Richards (1981) and Acemoglu & Robinson (2000), and indicate that the ability of the poor to influence the government is not the only way of achieving effective allocation of aid. Given that both poor and rich had the same interest at heart, namely the development of Pemba, the implementation of the cable and effective allocation of aid can have resulted without the interest of the poor having been a decisive factor in the decision-making process. An empirical implication of this process is therefore that the ability of the population to exert pressure could prove important, while the ability of the poor to do the same is more doubtful.

However, at this point, it is important to look at alternative motivations and incentives for the CCM government to implement the cable. If indeed it is true that political pressure and influence by the people living in extreme poverty is less important and less effective than predicted by the theories of Meltzer & Richards (1981) and Acemoglu & Robinson (2000), why did the CCM choose to implement the cable?

## 7.7 Rival Explanations

The alternative motivations and mechanisms presented in this section might have influenced the government in parallel to the mechanisms discussed elsewhere in this chapter, or they might have provided not only additional, but decisive, elements in the process.

First of all, the project held implicit economic benefits for the government and the islands. Pemba did not experience any foreign nor government investment, and people were left on their own to make a living. People were leaving Pemba, because there was no reason to stay behind: no roads, poor schools, even poorer health services, and no power for months at a time. Seeing how most of Zanzibar's clove production, as well as food production, comes from Pemba, the government realized the importance of keeping people on Pemba to ensure a continued supply of cloves and other resources.<sup>10</sup> Without providing public goods on Pemba, this production was almost certain to decline.

Secondly, the cable presented a method to appease the political situation and rivalry between CCM supporters and CUF supporters that had lasted a decade too many. There was reason to believe that a break-down of the Wesha power station where the generators were on Pemba could have triggered further political unrest and unsettled an already fragile stability (Kennedy 2006). In the opinion of the CCM, the cable represented tangible evidence to the people of Pemba that they were being treated equally with Unguja and were receiving an equal share of foreign aid (Poyry 2011).

Thirdly, the cable was the most cost-efficient solution to provide Pemba with a stable source of electricity for the Zanzibar government. The cable represented a low-risk investment financed primarily by another party. Even though the establishment costs were high, the maintenance cost for the cable was low and it was expected that the investment would last for 40 years.

Basically, the cable presented a solution for the CCM government to a social and political as well as an economic problem. There seems to have been many and complex mechanisms at work simultaneously in this process. It is close to impossible to pinpoint the importance of each motivation or each mechanism, and it is likely that the final decision to implement the cable was based on both political, economic and industry related considerations and interests.

However, this does not disconfirm the theory of Meltzer & Richards (1981) and Bueno de Mesquita et al. (2003), it is merely rival explanations for the implementa-

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<sup>10</sup>Pemba, often called the breadbasket of Zanzibar, needed development to keep the production going and meet demand. More than 90 % of Zanzibar's total clove production comes from Pemba, constituting more than 90 % of Zanzibar's foreign currency income (Informant 3, Informant 7 [Interviews]).

tion of the cable. It is important to note, though, that these rival explanations do not make the political motivations and processes irrelevant or insignificant. Given the fact that the Zanzibar and Union Government needed to contribute 100 million NOK to the project, indicates that there were indeed effective democratic mechanisms present in this case. In fact, although the interests presented here might have been important in the implementation of the cable, these had been present for quite some time. This could indicate that it was the upcoming election in 2010, and the increasing support of the CUF that represented the tipping point and the decisive mechanisms in the decision to lay the cable. This is in line with the predictions of selectorate theory, as well as the implications of Meltzer & Richards (1981). One empirical implication is thus that while other interests might have been influential in relation to the implementation of the cable, it might have been the fact that these interests coincided with political interests, and especially the upcoming election, that made sure the investment and the implementation happened at that time. Especially when considering that CUF's support was only increasing, CCM needed to act before the election to increase the likelihood of political survival.<sup>11</sup>

The obvious haste of which the Zanzibari government promoted the project, indicate that it's intentions was not purely humanitarian, nor economic; CCM was preparing for the upcoming elections in 2010. This highlights the importance of regular and competitive elections as a mechanism for effective aid allocation, as well as the importance of political pressure from the opposition in creating political competition favorable to the effective allocation of aid.

Nevertheless, the alternative mechanisms and motivations presented above cannot be ruled out as being decisive or at least influential in the process of implementing the cable. Especially when considering that political rights and civil liberties are far from fully implemented, this assumption becomes all the more plausible.

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<sup>11</sup>Even though it was a long process leading up to the cable, there are indications that the Zanzibar government was eager to get it done as quickly as possible. For instance, while both Norad and the Norwegian Embassy wanted strongly to tender the project in order to receive the most competent as well as cheapest contractor, the Zanzibar government pushed through their wish for a continuation of the contract with Norplan, who was the leading contractor for the REP. Despite the fact that such an approach would be highly controversial and contrary to Norwegian business principles, Norplan was awarded the project without a proper tender. Perhaps this was caused by the urgency of the matter, as the Zanzibar government argued that using the same contractor would save valuable time; time that could potentially cost the government much more than just money (Norwegian Ministry of Foreign Affairs & the Government of the United Republic of Tanzania 2006). To ensure the best possible result without a tender, it was decided that Zanzibar should receive expert input from Statnett/Norwegian Water Resources and Energy Directorate (NVE) (Kennedy 2006).

## 7.8 Political Rights and Civil Liberties

A theoretical implication of Sen (1999) is that the ability of the population to press their demands and exert pressure on the government is determined by the amount of political rights and civil liberties experienced by a population in a given country. Even though political pressure and the looming election in 2010 might have been decisive in the political process with the cable, there are certain indications that this political pressure and mechanism is now subsiding; leading to suspicions of limitations in political rights and civil liberties, and further questioning the ability of the people living in poverty to exercise meaningful political pressure.

The reason is that even now that the winning coalition of the government consists of both Unguja and Pemba, and is considerably larger than before, there is still limitations in the provision of electricity. The cable is now laid and functional, but there are still unannounced power outages due to load shedding from the government's side (Informant 6, Informant 10 [Interviews]).<sup>12</sup> The government does not inform the people of Pemba when power is cut or how long the power will be out (Informant 10 [Interview]). This indicates that a relatively large winning coalition and the struggle for voters might not be the only mechanisms needed to ensure effective aid allocation in Zanzibar. Moreover, it further questions the ability of the population to hold the government responsible and accountable by exercising political pressure. It seems clear that a general lack of accountability and transparency is putting restraints on the impact of the cable, suggesting that these mechanisms are just as important as the relative size of the winning coalition to ensure effective alleviation of poverty from aid. As discussed in chapter 3, accountability stems directly from the holding and respecting of democratic elections, which according to Sen (1999) comes from the upholding and maintenance of political and civil rights; it is the implementation of political and civil rights that ensure the accountability of the government. Democracies have a greater likelihood of effective aid allocation because the leader is held accountable by the public. Accountability, as such, can prove to be decisive in the effective implementation of aid.

### 7.8.1 Horizontal and Vertical Accountability

Horizontal accountability is ensured through formal democratic institutions that still seem lacking today. There are generally conflicting views of the the real democratic benefits of some of the democratic processes happening in Zanzibar today. The introduction of voter's register for instance, has been accused of leaving out CUF support-

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<sup>12</sup>Load shedding means planned power cuts.

ers so that they could not vote when election day came, claiming that the voters could not vote in this district because they belonged to another district (Informant 2 [Interview]). The process of introducing ID cards for being able to vote, has received the same criticism. CUF members claimed that the use of Zanzibar ID (ZID) cards were unconstitutional, other still did not have the card and were turned away when they came to vote. Furthermore, CUF complained that the process with the ZID "has been complicated, costly and biased, leaving many CUF supporters without a ZID" (Tronvoll 2010a, 7). Moreover, up until recently, criminal prosecution was handled by the police alone, without any formal judicial security or procedures (Informant 4 [Interview]).

Vertical accountability is the formal interaction between politicians and the people that guarantee transparency through all phases of policy making. A free media, for instance, is an important element of vertical accountability. Norad (2008) pointed out that "based on the documents available, it seems to have been little or no consultations with local NGOs". Nor was there a framework for consultations with the locals or other stakeholders. Moreover, procedures or feedback mechanisms were not in place for filing complaints or giving feedback during or after the completion of the project (Norad 2008, 3). Neither were there any workshops or seminars to incorporate the local population in the process. Furthermore, the press freedom in Zanzibar is more restricted than on the mainland, and public officials continuously monitor radio and television broadcast. Generally, the media avoid criticizing the leadership, and the CCM government was portrayed in a favorable light before election periods (Tronvoll 2010a, 11). In fact, the only daily paper in Zanzibar is the "Zanzibar Leo", which is published by the government. Television Zanzibar is also under government control, as well as the radio station Sauti ya Tanzania-Zanzibar. There are small private newspapers and radio stations, but these often have close connections to leading figures in the government (Freedom House 2010).

As discussed in chapter 3, horizontal and vertical accountability accounts for different mechanisms in keeping the government responsible for its decisions. Given how both types of accountability is limited in Zanzibar democracy, it is difficult to look at the empirical implications of functional accountability. However, it is obvious that a lack of both vertical and horizontal accountability has decreased the opportunity for meaningful political participation, leaving the government without being held fully responsible for its decisions. Moreover, it has increased the political distance between the governed and the governing, decreasing transparency and involvement of the local consumer. This is in accordance with the theory of Sen (1999), in that lacking accountability decreases the likelihood of meaningful political participation that makes the

leaders responsible and responsive. As a result, the leaders are inattentive to the needs of the population, possibly decreasing the impact from the cable. In fact, the lack of accountability might potentially have large consequences for the effectiveness of the cable, in that the project might not be as effective in alleviating poverty as expected. An empirical implication of the lack of accountability is that the local population is still hesitant to connect to the grid because of the uncertainty concerning unannounced load shedding (Informant 4, Informant 10 [Interviews]). Moreover, foreign and domestic investors are still hesitant and might prefer to invest elsewhere as electricity is still random (Informant 10 [Interview]). This clearly reflects the importance of accountability in the sustainability and effectiveness of the cable project.

## 7.8.2 Political Methods of Influence

The population in Zanzibar seems to have very few means of meaningful political participation except from voting at elections. They are not unaccustomed to demonstrations as a political tool, but demonstrations have been known to spiral into violent clashes between CUF supporters and the police.<sup>13</sup> It would seem like the the CCM was not very open to the idea of criticism or public opposition of the government, giving little regard to the opinion of the protesters and leaving demonstrations without its intended effect.

However, it is likely that there are some democratic processes happening in Zanzibar that are different from those in Western style democracy. It seems to be a much more informal route in making complaints or making your voice heard, as well as influencing decision-making processes. As discussed in chapter 3, neo-patrimonial practices often coexist with the formal institutions of democracy to shape national politics. The patterns of neo-patrimonial structures still linger in Zanzibar politics, and can potentially break the further progress of political change and democratic reforms. The informal routes and methods of making complaints or voicing an opinion, indicate that old practices of networks and personal contacts are more important than formal connections and relations. Generally, however, there seems to be very few mechanisms available for the people of Zanzibar to control their government, except from going to vote on election day.

A theoretical implication of Sen (1999), is that it is the presence of political rights and civil liberties that make elections an effective mechanism in the distribution of aid in recipient countries. In this case, political rights and civil liberties seems to be lacking,

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<sup>13</sup>In relation to the elections in 1995, 2000 and 2005 there were accounts of outbursts of political violence between CUF and CCM supporters, as well as between the police and CUF supporters. Multiple accounts of threats and forced containment of CUF supporters have also been reported (Brown 2010).

but the election in 2010 still resulted in the effective allocation of aid. This is contrary to the predictions of Sen (1999), in that competitive elections by itself might have been a sufficient mechanism for the implementation of the cable. With only limited political rights and civil liberties, the election still provided the basis for effective allocation of aid. However, it was the political competition and struggle for votes that turned the election into such an effective mechanism. This indicates the importance of *contested* elections, which is based on at least a minimum level of political rights and civil liberties. As such, an empirical implication of Sen (1999) is thus that the election in 2010 proved effective in the allocation of aid without the full implementation of political rights and civil liberties. True enough, Sen (1981) does highlight the importance of a *minimum* level of political rights and civil liberties in elections, the full implementation is not required.

Nevertheless, the lack of political rights and civil liberties might be a part of the explanation in how the supply of electricity to Pemba could be so much worse than the supply to Unguja for almost 30 years; and the reason there is still power outages and load shedding in Pemba. This lack of rights and liberties have resulted in limited political participation and pressure, as well as the absence of an accountable and responsive government. As such, it has directly affected the less than optimal operation of the cable.

### **7.8.3 The Distributive Effect of Elections and the Consequences of the Government of National Unity**

The government is not held to account for the power outages, perhaps because of a lacking ability of the poor to influence the leadership and exerting sufficient pressure. In fact, political pressures seem absent, or at least minimal compared to the pressure experienced prior to the election in 2010. So how come there was enough pressure for the government to implement the cable, but not enough pressure for the government to ensure the cable's full operation now? Indeed, although it is still some time before the next election in 2015, it seems like elections have lost some of the potentially important redistributive qualities it displayed in 2010.

One explanation for the lack of political pressure that is now present in Zanzibar democracy is the establishment of the Government of National Unity and the newly found political cooperation and peaceful ambience. Most people seem content with the current stability (Informant 3, Informant 6 [Interviews]), and perhaps in fear of destabilizing the young peace, or appear negative to the current coalition, people settle with what they have now; after all, it is better than before. Moreover, now that both political parties are in government, the political competition between the two has significantly



decreased.<sup>14</sup> Now that there are no parties in opposition, there are very few opportunities to cast a vote against the government. Although Zanzibar has several other political parties, none has so far received enough votes to win a seat in the House of Representatives. As such, there are no *de facto* political alternatives. With political participation mostly being synonymous with casting a vote on election day, the ability of the Zanzibaris to show disapproval or disappointment with the leadership has further decreased. Even if it is true that the social patterns in political votes are decreasing, the lack of an opposition further restrains the possibility for political pressure. This might explain why there was enough pressure to account for the implementation of the cable, but not enough pressure now to ensure its full operation. Again, this highlights the importance of *contested* elections in the effective allocation of aid.

To a certain extent, there were elements about the process leading up to the election in 2010 that made the CCM government more accountable than earlier. The political struggle for survival and political competition for votes were two of them; raising fear in CCM that the party might not be re-elected. This is in accordance with the theoretical assumptions of Sen (1999), in that contested elections increases accountability. However, now that Zanzibar has a government consisting of both political parties, it is likely that there will be a decrease in the distributive effect of elections. When elections do no longer possess the same element of political competition and struggle for political survival, accountability and transparency is compromised, together with the potential effects of the cable.

To sum up, I would say that the general lack of accountability and transparency in Zanzibar is most likely caused by the lack of meaningful political participation and involvement; a result of limited political rights and civil liberties. The institutions that ensure accountability are dependent on the maintenance and upholding of a certain level of political rights and civil liberties. When this is not the case, accountability is compromised, and the government is not held responsible for its decisions and actions. Elections proved to be effective in the implementation of the cable, but only when political pressure meant that the political parties either needed to address the needs of

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<sup>14</sup>The traditional Tanzanian and Zanzibar one-party political system has involved opposition within the one party, and not opposition from an outside party. In some ways, the Government of National Unity is more in line with the previous political model, in that the opposition comes from within the government (Informant 9 [Interview]). The government has assigned so-called back-benchers to work as a check on the government (Tronvoll 2010b). There is no doubt that the Government of National Unity has brought many positive features to both Zanzibar society and Zanzibar democracy that have not previously been present. Although this might be a better model in many ways for Zanzibar at this time, it has decreased the ability of the normal Zanzibari to voice disapproval of the government by voting for another party.

the people or risk losing office. Without political competition and pressure from the opposition, the government is not held accountable and the cable will perhaps prove less effective than its potential. This is in line with the theoretical implication and prediction of Sen (1999), in that political rights and civil liberties increase the likelihood of meaningful and competitive elections, as well as other forms of political participation and pressures.

## **7.9 A Different Scenario**

Given the complex nature of process tracing, the importance of the mechanisms in the process is illuminated by imagining a counterfactual scenario (see Gerring 2007). It is sometimes hard to assess the impact of foreign aid, because it is impossible to say how things would have been had aid not been given. In this case, however, the impact of electricity is relatively tangible, and it is possible to pinpoint direct effects of the cable. It is not so easy, on the other hand, to imagine what would have happened had Zanzibar been less democratic. However, it does seem fair to assume that the cable had not been implemented had it not been for the political pressure experienced by the CCM, that eventually led to an expansion of the winning coalition. This pressure was seemingly instrumental in the decision-making process with the cable, and reflected the importance of several democratic mechanisms, especially that of elections. Other motivations were in favor of the cable as well, but if it had not been for the upcoming election in 2010, there would not have been a time pressure on the government to the extent it was. Since elections had proved ineffective up until then, it is relatively likely that Pemba would still be without a cable had it not been for the political competition and struggle for voters experienced before this election.

On the other hand, had political rights and civil liberties been fully implemented and respected, the social and economic situation of Pemba and Unguja would probably not have been so unequal to begin with. Moreover, the cable would work at its full capacity, or if not, the people would be informed about the timing and duration of load shedding. Political participation would be meaningful to a larger number of people, and the locals would feel that their government was interested and took into consideration the opinion of the people living in poverty.

## **7.10 Norway's Role**

From the Norwegian perspective, there were several factors favoring the decision of the cable over other means of providing electricity. Firstly, the cable is much more environmentally friendly compared to HFO which could pollute both the fragile marine ecosystem around Pemba with oil spills and create acid rain if combusted (Norplan

2008, 4). In this way, a subsea cable was favorable to the Norwegian focus on energy and environmentally friendly development alternatives.

Secondly, the cable was requested by the Zanzibar government, making the decision of implementing the cable in accordance with the Paris Declaration on Aid Effectiveness of 2000. With the increased focus of recipient ownership and a feeling of responsibility of the project amongst international donors, the Embassy believed it to be important to follow the basic principles of the Declaration (Sverdrup 2008).<sup>15</sup>

Thirdly, the cable presented an option to bring Zanzibar closer to the mainland, creating an opportunity for further integration between the two countries in Union (Informant 1 [Interview]).

Fourth, and finally, perhaps also most importantly, it presented an important step in the Embassy's desire to support and promote the political reconciliation between the CUF and CCM in Zanzibar (Informant 2 [Interview]). The RNE had been highly involved in the reconciliation process between the CCM and the CUF, and had been in dialogue with Zanzibar since the election in 2005.<sup>16</sup> In an attempt to promote and further the reconciliation process, the Norwegian Embassy pushed forward on the implementation and completion of the subsea cable as the best alternative for a reliable supply of electricity to Pemba, directly going against the advise of Norad (Kjoelaas 2006). For the RNE, the project was a step in supporting the Union Government in its quest for the alleviation of poverty and creating development on Zanzibar (Informant 1, Informant 2 [Interviews]). Despite Norads concerns with cost-effectiveness, and even though the project might not have been economically sound for the Norwegian government, social and political factors led the Embassy to recommend the implementation of the project (Kjoelaas 2006).

Moreover, at the time when the decision needed to be taken, it had already been a long process. The Embassy had always assumed that this project was economically sound and feasible, and the negative appraisal by Norad came as a surprise. Promises had already been made, and expectations were high (Informant 1 [Interview]). Given the RNE's large part in the reconciliation talks between CCM and CUF, going back on its promises, not following through with the cable, could potentially have led to worsening relations between Zanzibar and Norway, and between CCM and CUF. The

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<sup>15</sup>There are five basic principles of the Paris Declaration. These are recipient ownership, alignment between donor and recipient, harmonization of donor procedures, focus on the result and mutual accountability between donor and recipient (OECD 2005).

<sup>16</sup>In fact, as the only foreign nation, the RNE was let in on reconciliation talks between CCM and CUF. According to the Minister of Agriculture and Natural Resources, RNE was the only institution both the CCM and CUF could work with. Even before the talks of reconciliation became known on the mainland, the RNE was already heavily involved (Informant 4 [Interview]).

stakes were too high and the consequences too grave for the RNE to go back on its promises, leaving RNE with little choice but to go through with the implementation of the cable (Informant 1 [Interview]).

### **7.10.1 A Note on Conditionality**

The aid from the Norwegian government was tied directly to the implementation of this cable; it was conditional on the cable being implemented according to Norwegian ideas and decisions. Had the CCM not been willing to install the cable on Pemba, but moved it to Unguja, the Zanzibar government would not have received the grant from RNE (Informant 1 [Interview]). As discussed in chapter 3, selectorate theory predicts that conditional aid will be less effective in democracies when the condition for aid is seen as a public bad. However, when the condition is perceived as a public good, conditional aid will be just as effective in democracies as in autocracies, if not more. In this project, the cable was clearly perceived as a public good by the population, leading to a satisfied population and a successful implementation of the cable. This project therefore corroborates the argument that conditional aid in democracies can be effective in alleviating poverty when the condition is considered to be a public good.

## **7.11 Conclusion**

I have no doubt that there was indeed significant pressure from the CUF on the CCM to provide more public goods and foreign aid to Pemba. The increasing support of CUF was threatening to the CCM's hold on power, and the party realized that it needed to attract new voters to increase the likelihood of political survival. As a direct result, CCM could not sustain its winning coalition on Unguja alone, the party also needed support in Pemba, thereby expanding the size of the winning coalition. What is doubtful, however, is that the decision to lay the cable was based on pressure from the people living in poverty alone. More likely, the decision was made due to a number of different considerations and interests. Both social, political, economic and industry related interests dictated the implementation of the cable, making it an easy decision for the CCM government. Had these interests been conflicting, however, there is a great likelihood that the result had been different and that the needs and desires of the very poorest had been ignored or at least given less priority to. In this case, though, political interests and the upcoming election in 2010 might have been decisive in ensuring that the implementation happened when it did; it might have been the the last motivation required for the CCM government to act.

Nevertheless, the cable is now laid and in operation, and other mechanisms must be applied to ensure the continued effect of the cable. With political pressures seem-

ingly absent, or at best ineffective, and a government that seems to be less than eager to solve the everyday problems of its citizens, democratic limitations hinder the further development of Pemba and the full operation of the cable. The newfound conciliation and prosperity might have created stability, but it has also led to limited political competition and might very well prove to compromise the potential distributive effect of elections. Along with a general lack of political rights and civil liberties, as well as limited accountability and transparency, the political environment can easily work to make the cable less effective than anticipated.

In conclusion, I would say that this case draws attention to the importance of the relative size of the winning coalition, as well as *contested* elections. Thus indicating the significance of the presence of a minimal level of political rights and civil liberties as mechanisms in the effective allocation of aid and its continued effect on poverty. Political competition seemed to be a driving-force behind the expansion of the size of the winning coalition and the subsequent implementation of the cable, perhaps indicating the importance of contested elections in other democratic settings in developing countries.



# Chapter 8

## Conclusion

The relationship between aid and poverty is a complex one. Adding democracy to the mix, does little to simplify it. It is clear from the conducted analyses in this thesis that the causal path from aid to poverty reduction is far from straight forward, and there are multiple mechanisms and processes happening simultaneously. Moreover, the data in the original data set has few measurements and is based on highly aggregated data. More importantly, however, the case demonstrates that the democratic institutions in low-income and low-quality democracies might not work as anticipated or as hypothesized in this thesis. If political rights and civil liberties are not properly implemented, other democratic mechanisms are likely to fail to ensure a fair distribution and allocation of aid. The result is that the effect of democracy on aid effectiveness is not as strong as it perhaps could be, neither in the statistical models nor in the case. Notwithstanding the limitations of this thesis and its empirical application, however, there are indications of a democratic effect on aid effectiveness despite the shortcomings of the data and the complexity of the relationship. More precisely, the findings of this thesis suggest that democracy does contribute to more effective aid in reducing poverty. Both the statistical analysis and the case study indicate this relationship, reinforcing the validity of the results and the probability of its existence.

This thesis draws on the theoretical contributions of Bueno de Mesquita, Smith, Siverson & Morrow (2003), Sen (1981, 1999) and Meltzer & Richards (1981) in clarifying the relationship between democracy and aid effectiveness. The mechanisms put forward in these contributions include the relative size of the winning coalition and elections; political rights and civil liberties and accountability; and political pressure. Highlighting and illuminating the importance of these mechanisms in the effective allocation and implementation of aid, provided the basis for examining how democracy affects aid effectiveness. In order to reveal the causal relationship between democracy and aid effectiveness and pinpoint the importance of each mechanism, I applied both

quantitative and qualitative research methods. The general effect of democracy on aid effectiveness was examined through the use of statistical models, while the causal mechanisms behind this effect was examined in a case study of a Norwegian development project in Tanzania. The overall findings of this thesis indicate that democracy contributes to increased aid effectiveness through the presence of contested elections and a minimum level of political rights and civil liberties.

## 8.1 The Effect on Poverty

The case study revealed that the main expectation to the subsea cable from Tanga to Pemba is that it will reduce poverty significantly over the next 30 years. Already, merely two years after its implementation, there were observable differences in living conditions in Pemba. Many of the people living in extreme poverty experience improved employment opportunities and increased ease of household chores. In fact, it is likely that the cable will influence all aspects of my measure of poverty; from the dimension of economic income to higher secondary school enrollment for females and improved infant mortality rate.

In the case study, the problem of endogeneity was minimized. The application of process tracing in the case study allowed me to observe the causal path from the independent variables to the dependent one; from the input of aid to the output of decreasing poverty. Thus, in this case study it seems relatively straight-forward that foreign aid contributed to a decrease in poverty. However, that the implementation of the cable, and the subsequent reduction in poverty was due to democratic mechanisms, also seem plausible. Moreover, the case study indicated that a lack of accountability and political pressure hindered the full operation of the cable, suggesting that a lack of democratic practices put limitations on the effect of aid on poverty.

When applying the Arellano-Bond GMM regressor, thereby controlling for endogenous factors, the statistical analysis displayed the same results. This model indicated that aid does not necessarily lead to decreased poverty levels; democracy is needed to ensure the effectiveness of aid in reducing poverty, or at least to make the aid more effective. The findings from the case study therefore corroborate the findings from the statistical analysis, in that aid contributes to decreasing levels of poverty as democracy increases. The hypothesis that democracy increases aid effectiveness in the alleviation of poverty (hypothesis I) is therefore corroborated by the analyses in this thesis. The importance of political rights and civil liberties, on the other hand, proved less effective in the allocation of aid than anticipated (hypothesis II) in the statistical analysis. However, the case study revealed that political rights and civil liberties matter to the extent of creating the basis for *contested* elections, indicating the importance of political



competition in the effective allocation of aid in reducing poverty.

However, these results should be viewed with caution. Imputed data adds an element of uncertainty to the statistical data, and the case study did reveal rival explanations to the implementation of the cable that worked parallel to the mechanisms under investigation. Nevertheless, that both research methods yielded indications of a democratic effect on aid effectiveness, strengthen the conclusions of this thesis and increases the likelihood that there are indeed aspects of a democracy that makes aid more effective in reducing poverty.

## **8.2 The Winning Coalition**

The argument that democracy increases aid effectiveness in the alleviation of poverty, is based on selectorate theory's assumptions about the relative size of the winning coalition. Selectorate theory predicts that a relatively large winning coalition would provide more public goods than a relatively small winning coalition. This assumption was corroborated by the case study, but certain empirical modifications were necessary. In fact, the case study showed that even though Zanzibar has had a relatively large winning coalition, the distribution of aid has been far from equal between the different segments of the population. This indicates that the winning coalition is not the only mechanism that is important in ensuring effective aid allocation; other mechanisms must keep the government responsive and attentive to the needs of the people when the relative size of the winning coalition is not sufficient.

Elections proved an ineffective mechanism in the effective allocation of aid before the political pressure on the CCM and the increasing support of the opposition became a threat to the party's political survival. This indicates that political pressure was important in CCM's decision to expand the winning coalition. Moreover, the relative size of the winning coalition in Zanzibar proved decisive in the effective allocation of aid only when the government needed to take into consideration the political pressure and the relative size of the opposition. Only when the CCM needed to attract new voters because of the political pressure from the CUF did the relative size of the winning coalition prove effective. This clearly implies that a minimum level of political rights and civil liberties is crucial in the proper functioning of other democratic mechanisms; such as elections and the relative size of the winning coalition.

## **8.3 Political Rights and Civil Liberties**

An indication of the importance of political rights and civil liberties in the quality of democratic institutions can be found in the case study. The statistical analysis showed that political rights and civil liberties were less important than anticipated in the ef-

fective allocation of aid. However, the case study revealed that it is not that political rights and civil liberties do not matter in effective aid allocation. They matter to the extent of providing and ensuring the presence of contested elections. This implies that the stronger effect observed when applying the Polity Index in stead of the FHI, can be due to Polity's focus on elections as the primary condition for a democracy. The competitiveness of elections and executive recruitment processes highlighted in the Polity Index might capture the minimum level of political rights and civil liberties Sen (1999) considers important for keeping the government and leadership attentive and responsive to the needs of the people. It is not that political rights and civil liberties do not matter, it is simply that contested elections was in this case the primary mechanism for effective aid allocation. However, according to Sen (1999) contested elections is based on a minimum level of political rights and civil liberties. Thus, political rights and civil liberties proved instrumental in the effective allocation of aid in Zanzibar. In fact, it is likely that the importance of political competition and contested election; based on a minimum level of political rights and civil liberties; proved decisive in the decision to implement the cable to Pemba.

## 8.4 Drawing General Conclusions

The case study was selected based on strategic considerations and the elements under study. Thus, it is difficult to say how representative it is of the larger sample of countries that receive development aid. However, with basis in the findings from the statistical analysis, democracy does seem to have an impact on aid effectiveness; although a very small one. The case study highlights potential mechanisms for this effect, and at the same time reveals why it is not as strong as the effect predicted by the theory. Nonetheless, the result from the statistical analysis of a democratic effect on aid effectiveness, along with the findings from the case study, could indicate that the mechanisms examined in this thesis might also be important in the effective allocation of aid in other countries.

However, it is probable that the relative size of the winning coalition works differently in other countries where voter segments are not as clearly separated from one another as they are in Zanzibar. This highlights the need for general caution when drawing generalizations from this thesis. Nonetheless, it is likely that the democratic challenges facing Zanzibar, are also present in other democratic regimes in the region. The low quality of democratic institutions in Zanzibar might explain why the results from the statistical analysis is not as clear-cut as the theory predicts, perhaps reflecting both the democratic limitations in Zanzibar *and* other countries in sub-Saharan Africa. Many of the countries receiving foreign aid are new democracies where accountabil-

ity is weak and political rights and civil liberties are lacking. A general low level of political rights and civil liberties, along with short traditions for contested elections might be decisive in the statistical estimate for a general causal effect of democracy on aid effectiveness. Thus, this thesis highlights possible explanations for a non-robust statistical effect of democracy's ability to increase aid effectiveness, as well as draws attention to potentially influential mechanisms in this process.

## 8.5 Further Research

This thesis attempted to fill the research gap in the aid literature relating to the impact of *democracy* on aid effectiveness in reducing *poverty levels*. The findings indicate that there is a democratic effect on aid effectiveness, but this relationship is not completely clear or robust. It is clear that further research is needed to establish a robust causal link between aid and poverty alleviation. One area of importance is to distinguish between the different types of foreign aid. The effect of direct budget support and hands-on project assistance is likely to be very different. The challenge is to find decent disaggregated measures of aid, so as to make it more likely to establish a causal effect. Moreover, and as implied in this thesis, the effect of unconditional and conditional aid can also prove to cause different outcomes in poverty levels. Especially in combination with different regime types. This highlights the need for research on the effectiveness of different types of aid, and how each type affects poverty levels.

Although this thesis has attempted to account for problems related to endogeneity as much as possible, and more than most existing research on the field, there are indications that there could be endogeneity left in the data. Given the significant test value of the Sargan test for some models, even more complex statistical models and estimators could be taken into use, perhaps clearly establishing the causal direction of the relationship between aid and poverty.

Moreover, further research is needed to specify the causal link between aid and poverty in other countries than Zanzibar and for other types of aid, to examine whether the mechanisms highlighted in this thesis are also important in other processes. Future research can draw on the findings of this thesis when examining even closer the mechanisms behind a democratic effect; both in Zanzibar and in other developing countries. Hopefully, the findings from this thesis can bring the aid research one step closer to the clarification of the importance of a democratic environment in effective aid allocation.

A clarification of the relationship is both important and necessary, and further research should focus on clarifying the causal path from the receiving of foreign aid to the subsequent alleviation of poverty. By clarifying the mechanisms behind effective aid allocation, future aid flows can become more effective as the aid can be focused on

the conditions and mechanisms that make it work. However, I do not suggest that aid should not be distributed to autocratic countries or non-democratic regimes; I simply suggest that one should focus on how to make the aid most effective by revealing how it works in alleviating poverty. In this way, future aid flows can be directly linked to these mechanisms, hopefully making a substantive contribution in alleviating global poverty.

## 8.6 Conclusion

Although the results in this analysis were not completely robust, there are indications that democracy promotes aid effectiveness through the holding of contested elections; and through the presence of a minimum level of political rights and civil liberties to ensure the competitiveness of elections and the ability of the population to exert pressure on the political leadership and the government. The desire for political survival and the fear of not being re-elected, might lead to a government that allocates aid to the degree it is considered necessary for political survival. The presence of contested elections; based on a minimum level of political rights and civil liberties; provides a political competition conducive to the effective allocation and implementation of aid.

However, when the government does not consider it necessary to obtain the support of all segments of the population, elections might not work according to its intentions and as hypothesized in this thesis. That is when the importance of political rights and civil liberties, as well as accountability and transparency becomes all the more important to ensure a fair distribution of aid. Without the presence of a minimum level of political rights and civil liberties, elections might not only fail to ensure political competition and the effective allocation of aid; the government might also fail to be accountable to all segments of the population.

To conclude my thesis and answer my research question, I would say that the findings in this thesis indicate that democracy leads to higher aid effectiveness through the holding of *contested* elections and the presence of a minimum level of political rights and civil liberties. It is the presence of a minimum level of political rights and civil liberties that ensures that elections are in fact *contested*, by providing the basis for meaningful political participation and political competition over votes. The political competition over votes that is present in a democracy and originates from the holding of elections and a minimum level of political rights and civil liberties, can prove decisive in the effective allocation of aid in reducing poverty.

# Chapter 9

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# Appendices



# **Appendix A**

## **Country Sample for the Statistical Analysis**

Table A.1: Countries included in the data sample

Afghanistan	Albania	Algeria	Angola
Antigua and Barbuda	Argentina	Armenia	Azerbaijan
Bahamas, The	Bahrain	Bangladesh	Barbados
Belarus	Belize	Benin	Bhutan
Bolivia	Bosnia and Herzegovina	Botswana	Brazil
Brunei Darussalam	Burkina Faso	Burundi	Cambodia
Cameroon	Cape Verde	Central African Republic	Chad
Chile	China	Colombia	Comoros
Congo, Dem. Rep.	Congo, Rep.	Costa Rica	Ivory Coast
Croatia	Cuba	Cyprus	Djibouti
Dominica	Dominican Republic	Ecuador	Egypt, Arab Rep.
El Salvador	Equatorial Guinea	Eritrea	Ethiopia
Fiji	Gabon	Gambia, The	Georgia
Ghana	Grenada	Guatemala	Guinea
Guinea-Bissau	Guyana	Haiti	Honduras
India	Indonesia	Iran, Islamic Rep.	Iraq
Israel	Jamaica	Jordan	Kazakhstan
Kenya	Kiribati	Korea, Dem. Rep.	Korea, Rep.
Kosovo	Kuwait	Kyrgyz Republic	Lao PDR
Lebanon	Lesotho	Liberia	Libya
Macedonia, FYR	Madagascar	Malawi	Malaysia
Maldives	Mali	Malta	Marshall Islands
Mauritania	Mauritius	Mexico	Micronesia, Fed. Sts.
Moldova	Mongolia	Montenegro	Morocco
Mozambique	Myanmar	Namibia	Nepal
Nicaragua	Niger	Nigeria	Oman
Pakistan	Palau	Panama	Papua New Guinea
Paraguay	Peru	Philippines	Qatar
Rwanda	Samoa	Sao Tome and Principe	Saudi Arabia
Senegal	Serbia	Seychelles	Sierra Leone
Singapore	Slovenia	Solomon Islands	Somalia
South Africa	Sri Lanka	St. Kitts and Nevis	St. Lucia
St. Vincent and the Grenadines	Sudan	Suriname	Swaziland
Syrian Arab Republic	Tajikistan	Tanzania	Thailand
Timor-Leste	Togo	Tonga	Trinidad and Tobago
Tunisia	Turkey	Turkmenistan	Tuvalu
Uganda	Ukraine	United Arab Emirates	Uruguay
Uzbekistan	Vanuatu	Venezuela, RB	Vietnam
Yemen, Rep.	Zambia	Zimbabwe	

## **Appendix B**

### **GMM with Each Poverty Indicator**

Table B.1: Arellano-Bond GMM for each Poverty Indicator

	(1)	(2)	(3)
	Infant Mortality Rate	Poverty Headcount	Secondary School Enrollment Female
L. Infant Mortality Rate	0.601*** (0.00890)		
L. Poverty Headcount		0.0563*** (0.0116)	
L. Secondary School Enrollment Female			0.482*** (0.00990)
Aid	0.159*** (0.0371)	0.138*** (0.0200)	-0.152*** (0.0289)
Democracy	-0.134 (0.167)	-0.384*** (0.0903)	0.283* (0.130)
Democracy*Aid	-0.0568*** (0.00959)	-0.00312 (0.00515)	0.00553 (0.00744)
Log GDP per capita	-2.373*** (0.222)	-1.320*** (0.119)	2.874*** (0.174)
Corruption	1.624*** (0.243)	0.851*** (0.131)	-2.446*** (0.190)
Bureaucratic Quality	-3.546*** (0.317)	-1.392*** (0.170)	3.039*** (0.246)
Log Inflation	-0.0146 (0.0368)	-0.0193 (0.0199)	-0.00712 (0.0287)
Log FDI	-1.900*** (0.120)	-0.435*** (0.0638)	0.876*** (0.0923)
Log Openness	-2.807*** (0.497)	-2.823*** (0.268)	1.821*** (0.385)
Log Population	-2.137*** (0.500)	-0.338 (0.266)	1.577*** (0.384)
Ethnic Fractionalization	5.682 (8.715)	-7.888 (4.700)	-0.897 (6.783)
Sargan test	0.7517	0.0015	0.2086
Observations	7020	7020	7020

Standard errors in parentheses

\*  $p < 0.05$ , \*\*  $p < 0.01$ , \*\*\*  $p < 0.001$

Decade dummies were included in all analyses, but have been removed from the table.

Democracy is measured by the Freedom House Index.

# Appendix C

## Predicted Residuals for Tanzania

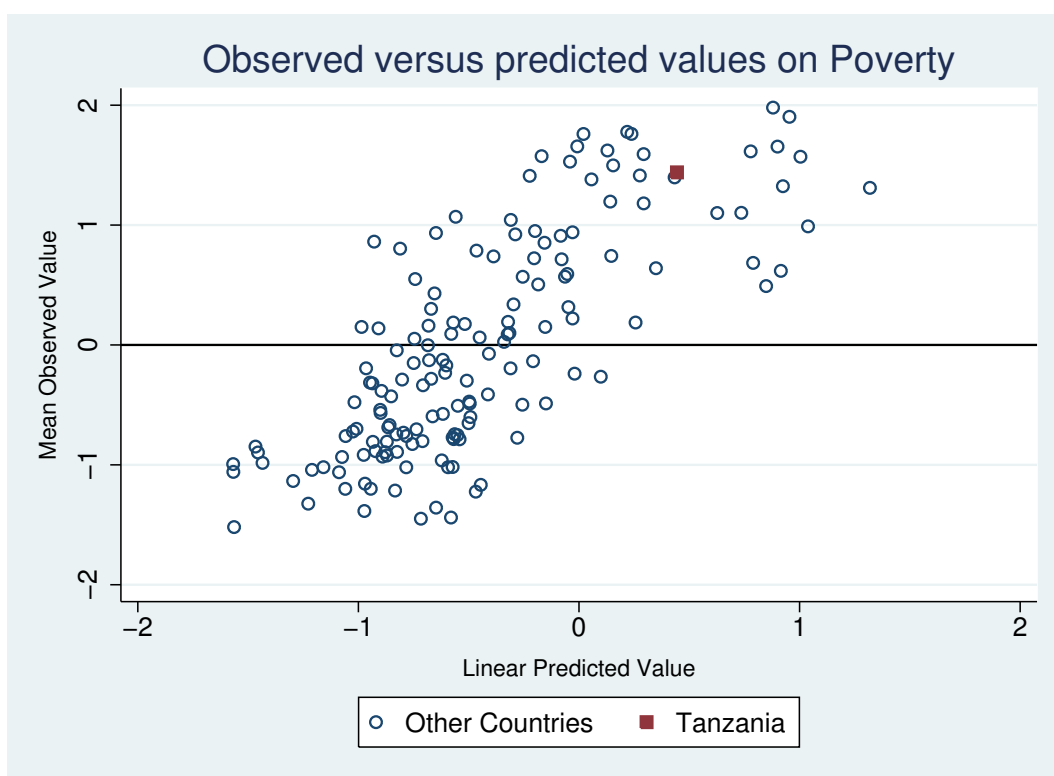


Figure C.1: Observed vs Preditd Score on Poverty





# Appendix D

## Informants

1. Counselor, Energy and Infrastructure, the Royal Norwegian Embassy, Dar es Salaam, Tanzania, 5 March 2012.
2. Political Officer, Political Issues, Governance, Culture and Communication, the Royal Norwegian Embassy, Dar es Salaam, Tanzania, 5 March 2012.
3. Advisor at the Second Vice President's Office, Stone Town, Zanzibar, 7 March 2012.
4. Minister, Ministry of Agriculture and Natural Resources, Stone Town, Zanzibar, 8 March 2012.
5. Assistant Project Manager, REP, Stone Town, Zanzibar, 8 March 2012.
6. Deputy Director of Finance, CUF, Zanzibar Town, Zanzibar, 8 March 2012.
7. Minister, Ministry of Trade, Industry and Marketing, Stone Town, Zanzibar, 9 March 2012.
8. Principal Secretary, Ministry of Water, Construction, Energy and Land, Stone Town, Zanzibar, 14 March 2012.
9. General Manager, ZECO, Zanzibar Town, Zanzibar, 14 March 2012.
10. Ward, Wete, Pemba, 20 March 2012.



# Appendix E

## Interview Guide

1. What is your position?
2. What has been your role in the electrification of Pemba?
3. Why was the initiative taken to electrify?
4. What was the motive behind the electrification? And why?
5. What were the determinant factors in the allocation of resources for the project?
6. What was the aim of the electrification? And to what degree has it been fulfilled?
7. What were the major challenges of the project?
8. Were there conflicting views in how the project should be carried out?
9. What was Norway's role? Did the Embassy put any restraints on the aid?
10. How did the project incorporate local knowledge? And what consequences did it have?
11. To what extent did the government of Zanzibar intervene in this project?
12. What were the decision-making channels?
13. How were local consumers involved in the process?
14. What has been the consequences of the project?
15. To what extent is the project reaching the poorest in the community?
16. Has it influenced poverty levels in the region?

17. How would you say that the political situation has changed and evolved since the democratization of Tanzania and Zanzibar in 1992?
18. Who are the primary beneficiaries of the project?
19. Anything that you would like to add?

# Appendix F

## Descriptive Statistics

Table F.1: Summary Statistics Original Data

Variable	Mean	Std. Dev.	Min.	Max.	N
Poverty Index \$ 1.25 a day	0	1	-1.196	3.118	415
Poverty Index \$ 2 a day	0	1	-1.267	2.961	415
Poverty headcount ratio at \$1.25 a day (PPP) (% of population)	20.07	23.226	0	92.55	619
Poverty headcount ratio at \$2 a day (PPP) (% of population)	33.786	29.981	0	98.45	619
Infant Mortality Rate	65.357	52.213	2.938	263.19	7393
School enrollment, secondary, female (% gross)	59.835	36.726	0	175.068	4509
Aid	7.562	11.73	0	241.706	5650
Freedom House	4.026	2.047	1	7	5673
Polity	0.346	7.468	-10	10	6688
Log GDP per capita	7.264	1.666	3.566	12.135	7551
Corruption	3.027	1.371	0	6.167	3338
Bureaucratic Quality	2.127	1.195	0	4	3340
Log FDI	1.218	1.212	-5.11	7.03	5847
Log Inflation	2.423	1.472	-5.298	10.796	6204
Log Openness	4.141	0.662	-1.707	6.100	6942
Log Population	15.081	2.167	8.717	21.015	9759
Ethnic Fractionalization	0.482	0.265	0.004	1	6607
Franc Zone	0.078	0.268	0	1	9984
US Sphere of Influence	0.026	0.159	0	1	9984
Egypt	0.005	0.072	0	1	9984

Table F.2: Summary Statistics Imputed Data

<b>Variable</b>	<b>Mean</b>	<b>Std. Dev.</b>	<b>Min.</b>	<b>Max.</b>	<b>N</b>
Poverty Index \$ 1.25 a Day	0	1	-2.271	2.618	8060
Poverty Index \$ 2 a Day	0	1	-2.413	2.693	8060
Poverty Headcount \$ 1.25 a Day	29.388	19.212	0	92.55	8060
Poverty Headcount \$ 2 a Day	45.252	23.463	0	100	8060
Infant Mortality Rate	71.017	48.689	-137.045	263.19	8060
Secondary School Enrollment Female	47.857	33.857	-48.429	161.052	8060
Infant Mortality Rates_bounds	71.149	48.439	0	263.19	8060
School Enrollment_bounds	48.25	33.203	0	161.052	8060
Aid	8.161	12.349	-15.778	241.706	8060
FH 0-1	0.419	0.269	0	1	8060
Freedom House	3.515	1.617	1	7	8060
Polity 0-1	0.474	0.318	0	1	8060
Polity	-0.51	6.36	-10	10	8060
Log GDP per capita	6.941	1.399	1.505	11.281	7569
Corruption	2.671	0.824	0	6	8060
Bureacratic Quality	1.632	0.785	0	4	8060
Log Inflation	1.778	3.827	-7.377	10.796	8060
Log FDI	0.934	1.629	-5.11	5.813	8060
Log Openness	4.2	0.635	-1.707	6.100	8059
Log Population	15.009	2.123	8.717	21.015	7981
Ethnic Fractionalization	0.537	0.215	0	1	8060
Franc Zone	0.097	0.296	0	1	8060
US Sphere of Influence	0.032	0.177	0	1	8060
Egypt	0.006	0.08	0	1	8060

# Appendix G

## GMM with \$ 2 a Day Poverty Measure

Table G.1: Arellano-Bond GMM with Dependent Variables Poverty \$2 a Day

	(1)	(2)	(3)	(4)	(5)
	Poverty \$2 a day	Poverty \$2 a day	Poverty \$2 a day	Poverty \$2 a day	Poverty \$2 a day
L.Poverty \$2 a day	0.409*** (0.0115)	0.447*** (0.0110)	0.450*** (0.0104)	0.446*** (0.0102)	0.435*** (0.00986)
Aid	0.00306*** (0.000353)	0.00429*** (0.000763)	0.00471*** (0.000725)	0.00499*** (0.000719)	0.00483*** (0.000696)
Democracy	-0.0236*** (0.00321)	-0.0206*** (0.00354)	-0.0151*** (0.00332)	-0.0165*** (0.00326)	-0.0127*** (0.00314)
Democracy*Aid		-0.000308 (0.000196)	-0.000635*** (0.000188)	-0.000288 (0.000185)	-0.000471** (0.000179)
Log GDP per capita	-0.0998*** (0.00503)	-0.0980*** (0.00486)	-0.0843*** (0.00447)	-0.0863*** (0.00442)	-0.0780*** (0.00422)
Log Population	-0.0683*** (0.0104)	-0.0659*** (0.0103)	-0.0667*** (0.00978)	-0.0567*** (0.00971)	-0.0552*** (0.00930)
Ethnic Fractionalization	-0.0342 (0.172)	-0.0701 (0.174)	0.0186 (0.169)	-0.0202 (0.168)	0.0264 (0.163)
Corruption			0.0558*** (0.00464)		0.0506*** (0.00456)
Bureaucratic Quality			-0.0908*** (0.00607)		-0.0793*** (0.00594)
Log Inflation				-0.00192** (0.000720)	-0.00171* (0.000690)
Log FDI				-0.0327*** (0.00233)	-0.0331*** (0.00223)
Log Openness				-0.117*** (0.00953)	-0.0795*** (0.00933)
Constant	1.850*** (0.192)	1.825*** (0.191)	1.686*** (0.184)	2.100*** (0.185)	1.822*** (0.180)
Sargan tes	0.000	0.0055	0.0799	0.4710	0.1499
Observations	7020	7020	7020	7020	7020

Standard errors in parentheses

\*  $p < 0.05$ , \*\*  $p < 0.01$ , \*\*\*  $p < 0.001$

Decade dummies were included in the analysis, but removed from the table.

Poverty is measured on an Index from -2.41 to 2.69, consisting of the Poverty Headcount Ratio at \$ 2 a day, Infant Mortality Rate and Gross Secondary School Enrollment for Females.

Democracy is measured by the Freedom House Index.





# Appendix H

## GMM with Democracy 0 to 1

Table H.1: Arellano-Bond GMM: Democracy 0 to 1

	(1) Poverty	(2) Poverty
L.Poverty	0.437*** (0.00993)	0.423*** (0.00991)
Aid	0.00418*** (0.000555)	0.00442*** (0.000605)
FH 0-1	-0.0542** (0.0192)	
FH*aid	-0.00299** (0.00110)	
Polity 0-1		-0.141*** (0.0153)
Polity*aid		-0.00215* (0.000883)
Log GDP per capita	-0.0728*** (0.00430)	-0.0741*** (0.00424)
Log Population	-0.0554*** (0.00949)	-0.0543*** (0.00938)
Ethnic Fractionalization	-0.0103 (0.167)	0.0229 (0.165)
Corruption	0.0513*** (0.00466)	0.0517*** (0.00459)
Bureaucratic Quality	-0.0840*** (0.00607)	-0.0842*** (0.00597)
Log Inflation	-0.000723 (0.000706)	-0.000547 (0.000696)
Log FDI	-0.0324*** (0.00228)	-0.0319*** (0.00224)
Log Openness	-0.0790*** (0.00953)	-0.0724*** (0.00942)
Observations	7020	7020
Sargan Test	0.3154	0.1742

Standard errors in parentheses

\*  $p < 0.05$ , \*\*  $p < 0.01$ , \*\*\*  $p < 0.001$

Decade dummies were included in the analysis of all the models, but have been removed from the table.

Poverty is measured on an Index from -2.27 to 2.62, consisting of the Poverty Headcount Ratio at \$ 1.25 a day, Infant Mortality Rate and Gross Secondary School Enrollment for Females.

