

**FOREIGN AID EFFECTIVENESS & STATE INSTITUTIONAL CAPACITY:  
The Case of Armenia**

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# Foreign Aid Effectiveness and State Institutional Capacity: The Case of Armenia

## TABLE OF CONTENTS

Acknowledgement .....	2
Introduction.....	4
Theoretical Framework.....	6
Literature Review.....	7
What is foreign aid? .....	7
Why does foreign aid fail? .....	8
The Role of Institutions in Development and Effectiveness of Foreign Aid .....	9
Good Governance.....	12
Transparency and Accountability.....	13
Methodology and Design.....	13
Data Collection.....	14
Discussion and Interpretation .....	15
Analytical framework.....	15
Conclusion .....	28
References.....	30
Appendices.....	32
Interview questionnaire for donor organizations .....	32
Interview questionnaire for recipient institutions.....	32

## ABSTRACT

Foreign aid is directed to developing countries to make recipient countries grow in spite of their limited resources. Not always do recipient states manage to reach success and one of the major reasons of their failure is the relatively low capacity of their state institutions. One such recipient of foreign aid is the Republic of Armenia. This research aimed at finding out the extent to which the capacity of state institutions in Armenia contributes to or hinders the effectiveness of foreign aid. A qualitative approach was used to collect data through interviews with state institutions and all major donor organizations operating in Armenia. The analysis of interview transcripts showed that generally the projects implemented in Armenia have been effective, but there have been staff competence issues and related encumbrances that have hindered reaching more effective outcomes. The main problems that this research identified included the inadequate expertise of civil servants in some areas of specialized interventions, lack of project management skills and absence of institutional and partnership arrangements that increase the incentive for taking ownership of projects. However, institutional reforms of the recent past have somewhat contributed to enhance the professional knowhow of government officials and staff. These reforms may have included improved hiring process that has successfully brought in qualified staff without regard to actions of nepotism and cronyism that have existed for long in the state apparatus. However, more work needs to be done to further improve the delivery of foreign aid and implementation of such projects in order to maximize their impact on state development. This research makes a few recommendations that would contribute to increasing the impact of foreign aid towards sustainable development.

## **INTRODUCTION**

Foreign aid is viewed by most of the world as one of the channels for reducing world poverty and recording economic growth, thereby achieving sustainable development. Even the development theories of the early sixties and seventies have addressed the importance of foreign aid and emphasized that without it developing countries would have problems moving out of being agrarian countries. It also helps in adopting new technologies and modernized production to sprint forward. However, in some countries of the world, the inflow of foreign aid has had slim or no impact and, even in some cases, negative effects on respective governments of the receiving countries (Easterly, 2003).

The current state of developing nations raises the question whether or not foreign aid contributes to or speeds up economic growth and efficacy in resource use. This issue has been tackled by many scholars and technocrats, but there is no consensus among them. In spite of numerous studies, there is little evidence of significant positive effect of aid on the long-term growth of underdeveloped or developing countries. Results show that aid works better when the country has well-functioning institutions and the policy environment is conducive to growth, which however does not hold in all cases, rendering findings less generalizable.

The question is often raised whether or not ineffective aid is caused by the recipient country or whether donors also play a role in its failure. Moreover, should donor countries select recipients on the basis of their established mechanisms of governance, capacity of institutions versus other political interests and considerations?

The first part of the research reviews existing theories of foreign aid and their relative impact on growth and development. The second part of the research covers the existing literature examining the success or failure of foreign aid in underdeveloped or developing countries and

identifying the main obstacles of the effectiveness of foreign aid. The next section aims at investigating the foreign aid situation in Armenia and the reasons or drivers of successes or failures. This is done by collecting and analyzing qualitative data to help delve into issues related to understanding why foreign aid goals and objectives are not always fully achieved, what is the role of local state institutions in the success of foreign aid, and related questions?

## **THEORETICAL FRAMEWORK**

For long, many international organizations such as the IMF, the World Bank, the UN and governments of developed nations have provided foreign aid to poor and developing countries to reduce poverty and contribute to their advancement. In the mid-twentieth century, the Harrod-Dommar model claimed that the best way to achieve economic growth and development is to increase the rate of savings which will lead to increase in investments. This was in a way an affirmation that both savings and investments are a necessary precondition for economic growth. But, this did not prove to be enough. Later, Solow added another element to the model arguing about the importance of technology along with capital and labor (Todaro and Smith, 2015; Solow, 1956). Subsequently, Rostow's model for economic growth added yet another element to the above, arguing that foreign aid is essential to speed up development in most countries that did not have resources for moving ahead. He claimed that the foreign aid can fill the gap between the domestic saving and the needed investments (Todaro and Smith, 2015; Rostow, 1960).

In most instances and over many decades since the sixties and seventies of the twentieth century, however, foreign aid or development assistance did not pay off, prompting donor nations/organizations to look for the reasons of its failure. This led to the Washington Consensus (1989) that established a ten-point policy agenda that, from the standpoint of the International Monetary Fund, the World Bank and the U.S Treasury would produce tangible results. The

Washington Consensus offered to move toward neo-liberal principles, which subsequently came across severe opposition (Frey, 2008; Filbo, 2010). This led to discussions among economists and leaders of both donor and recipient countries followed by the Paris Declaration. Thus it was not until the turn of the century when focus was placed on the institutional capacity of recipient countries and issues related to good governance, which were set as ground rules for cooperation between donor and recipient countries (OECD, 2008).

Having recognized the role of institutions in development, it has become imperative to study what types of approaches or foreign aid arrangements would work best in both helping poor countries realize reform while also making development advances (Grey and Khan, 2006). This topic continues to be at the center of recent debates and is at the center of the current research question. In the case of the Republic of Armenia, finding an answer to the dilemma between setting development priorities and reforming institutions would be most advantageous to moving the country forward.

## **LITERATURE REVIEW**

### **What is foreign aid?**

The emergence of foreign aid received attention in the aftermath of WWII primarily to address the negative impact of the war. Today, donor countries and organizations view the components of foreign aid in a variety of ways. Official Developmental Aid (ODA), a term used by OECD and others may include humanitarian and poverty reduction assistance, infrastructure, economic and social development (Akramov, 2006; Radelet, 2004; Bandyopadhyay and Vermann, 2013; Thomas and Viciani, 2011).

The delivery of foreign aid developed phases, taking on different objectives. During 1970s donor countries focused on the basic needs of people, such as healthcare and education. Starting from 1980s the developmental strategies evolved to focus on the macroeconomic indicators of recipient countries through market liberalization and financial policies which would lead to economic growth. This approach too did not result in significant advances and led donor countries to rethink the structure of foreign aid. In the 1990s, donors moved to paying attention to the institutional and governance arrangements prevalent in recipient countries. Purely market led development was not a solution. Some state led development models were deemed necessary for reaping the benefits of foreign aid (Akramov, 2006; Frey, 2008; Qian, 2014; Radelet, 2004; Thomas and Viciani, 2011; Carothers and Brechenmacher, 2014).

### **Why does foreign aid fail?**

The history of foreign aid has shown that not in all countries aid reaches its destination or contributes to the focus area of the recipient's development strategy. Researches have demonstrated that while providing ODA donor countries are paying little attention to the institutional capacities and good governance principles and procedures that may impede the effectiveness of aid (Carothers and Brechenmacher, 2014; Williamson, 2009; Radelet, 2004). Many donor organizations and countries established minimum criteria for receiving aid and conditionalities for managing aid to ensure effectiveness. But adopting the same approach to all aid would not always have the intended impact considering deviation from the developing strategies, if any, of recipient countries (Brookings, 2010; Radelet 2004; Chong and Granstein, 2006; IEG, 2008).

Moreover, achievement of economic growth is not a short term process, since it requires all the institutional, economic and development indicators to serve well. It is rather easy to



achieve basic developmental goals in the short term but the sustainability of any development achievement highly depends on the institutional capacity of recipient countries. Aside from requiring that the institutional capacity of recipients is in place, foreign aid provided need to also consider the priorities of the recipients, as established in their development strategy documents. Adopting individual approaches for every country would enable the most effective and results-driven way of allocation of foreign aid (Williamson, 2009; Radelet, 2004; Thomas and Viciani, 2011).

### **The Role of Institutions in Development and Effectiveness of Foreign Aid**

Institutions, as defined by Douglas North and subsequently used by many scholars, establish the fundamental rules of the game defining how the state and the people would interact and work together to produce best outcomes for the state. This would produce positive changes in society over time, whether economic, political or social. The instruments of interaction and transaction among formal institutions of government, non-governmental and private organizations, and even individuals must be well-structured so as to ensure that any development allocations, whether local or foreign, are used effectively, efficiently, and equitably. Well-functioning institutions play a significant role in driving sustainable development, economic growth and sustainability (Douglass, 1990; Elobeid, 2012; Acuna and Thommasi, 1999; IEG, 2008).

The institutional capacity has an essential role for sustainable development and growth of any country developing or underdeveloped country. The effective and efficient functioning of institutions ensures economic growth and improves people's quality of life. Well-functioning institutions would (a) possess the necessary expertise for the appropriate use of funds in terms of managing allocations, promoting good governance practices, and transparent processes; and (b)

provide for responsible linkages between government and society and other actors engaged in development. Sound management practices would allow focusing on more people-responsive policies and decrease the level of corruption (OECD, 2015; Acuna and Thommasi, 1999; Elobeid, 2012).

The literature covering the role of institutions in delivering effective foreign aid articulates that the size of aid is not as relevant as the methods and ways in which aid is delivered and used. With a small amount of aid but with good policies and strong institutions recipient countries can achieve developmental goals more effectively and efficiently than those receiving larger aid packages but have weak and corrupt institutions. Scholars posit that for a state to achieve significant development, strong institutions are of utmost significance arguing that low-performing institutions are reason for poor countries to stay poor regardless of foreign aid (Dietrich, 2015; Brown, 2010, Pande and Undry, 2005).

Many scholars claim that foreign aid can promote significant economic growth when receiving countries have well-functioning institutions, with good fiscal and monetary policies and commensurate development strategies that are adhered to when managing foreign aid or local development programs (Easterly, 2003; Burnside, Dollar 2000; Erbeznik, 2011; Radelet, 2004; Painter and Khoi, 2009). When the recipient country has weak and not well-functioning institutions, it increases the risks associated with the proper use of foreign aid primarily caused by the lack of expertise in managing projects and corruption in administering the allotted aid (Dietrich, 2015; TI, 2007).

Further, donor countries and organizations also point to the importance of a well-functioning civil service, with a merit-based hiring and rewarding system. This, they claim, would prevent nepotism, cronyism and political patronage in recruitment and promotion, as well

as enable performance-based management processes that would increase the success rate of state-funded as well as foreign aid programs and projects (Kauznya and Balogun, 2005; UNDP, 2004).

Thus, scholars investigating the ineffectiveness or failure of foreign aid have found positive correlations with the lack of institutional capacity of recipient countries and the effectiveness of foreign aid. This reveals the necessity of institutional reforms aimed at improving the performance of institutions through building technical expertise, administrative capacity and increasing the cooperation between civil service and the private sector. Well-functioning institutions have transparent hiring procedures, performance plans and targets geared to achieving organizational goals, and administrative procedures that produce measurable results (UNDP, 2010; OECD, 2015; Acuna and Thommasi, 1999; Elobeid, 2012).

For the sake of improving public sector management, many recipient countries have made efforts to improve internal management systems to meet conditionalities imposed by donors. These efforts were mostly directed to increasing organizational structures and reporting schemes, improving personnel policies and processes, adopting pay schemes that are based on performance or productivity, and ensuring that position descriptions and incumbents are in sync (Kauznya and Balogun, 2005; UNDP, 2004; IEG, 2008).

The donor countries are more inclined to provide foreign aid to those countries that are more accountable to the citizenry, meet the institutional conditions related to minimum expertise, and realize the changes necessary for the transparent delivery of public services. These countries allocate the aid more effectively and efficiently and have higher possibility to match the donor countries criteria for receiving foreign aid (IEG, 2008; UNDP, 2004; OECD 2015).

## **Good Governance**

Good governance has always been at the core of arguments by scholars and development practitioners alike, since it is the key requisite for the prosperity of a country and a vital element for its development. But, without the existence or lack of good governance there cannot be sustainable development. Good governance helps to alleviate the level of poverty of a country and to push forward its socioeconomic development. Many scholars and foreign aid organizations consider good governance as an all-encompassing word to mean transparency, accountability and absence of corruption, including cronyism and nepotism in recruitment and procurement practices (Frey, 2008, Kabumba, 2005; Elobeid, 2012). For other scholars, however, good governance also means expertise in decision-making, capacity of institutions, efficient and effective public services, fair and public-driven policies, and the extent to which the rule of law is enforced. All the above mentioned characteristics have a profound impact on the sustainable development of a country, but mostly in long term basis (Uddin, 2010; UNDP, 2014; Akramov, 2006; Frey, 2008; IEG, 2008).

Moreover, the role and importance of good governance are essential not only for the development of a country but also for many organizations and donor countries that are willing to provide assistance to developing or underdeveloped countries. Most donors are considering the level of good governance of the recipient country and including conditionalities in aid packages since it is essential for the effectiveness of aid. As stated earlier, the size and the delivery of foreign aid is not a necessary precondition for sustainable development or economic growth; rather, it is the quality of governance of aid that produces effective and sustainable development (Akramov, 2006; Kabumba 2005).

## **Transparency and Accountability**

Transparency and accountability are the essential components supporting good governance and providing for the open flow of information to the public and holding government accountable to society for its actions and decisions. These features of good governance promote the improvement of service delivery, reduction of corruption, improved institutional responsiveness and greater citizen participation. According to many international donor organization and countries transparency is a prerequisite for effective aid, since it provides for improved ownership of funds received and increased accountability (Carothers, and Brechenmacher, 2014; McGee and Gaventa, 2010; OECD, 2015).

The 2008 Paris Declaration addressed the importance of these elements emphasizing that transparency and accountability are necessary conditions for foreign aid. The Paris Declaration also makes reference to mutual accountability, implying that both the donor and recipient countries should hold each other accountable for targeted objectives and results. It also refers to involving all key stakeholders in planning and providing for the transparent flow of information (Carothers, and Brechenmacher, 2014; OECD, 2008).The Paris Declaration goes further addressing the requirement of harmonization among donors as a critical element of aid effectiveness, where donors coordinate their programs to avoid duplication, needless overlap, and wasteful allocation of resources (Carothers, and Brechenmacher, 2014; Booth, 2011; OECD, 2008; Radelet, 2004; Lawson, 2013).

## **METHODOLOGY AND DESIGN**

This research uses a qualitative methodology aimed at assessing the role of Armenian state institutions in the effectiveness of foreign aid. More specifically, the study aims at

identifying the extent to which the current structure and capacity of state institutions contributes to or encumbers the effectiveness of foreign aid. The case study method is selected for this research because considering that Armenia is a developing and major foreign aid recipient, this approach will provide rich data from multiple perspectives of donor as well as recipient.

Thus, the research tries to answer the following questions:

RQ1: How does state institutional capacity impact the effectiveness of foreign aid to the Republic of Armenia?

RQ2: What are the specific institutional capacity issues that must be treated as priority areas to reform?

H1: Strong state institutions contribute to the effectiveness of foreign aid (as measured by the level of expertise available and good governance practices of the recipient government).

## **Data Collection**

The research used primary data collected through interviews and official reports to analyze and understand the role of institutions in the effectiveness of foreign aid. For this purpose in-depth interviews were conducted with experts from both donor organizations and recipient side government representatives in top managerial and leadership positions. The sampling used a purposive approach to include donor side interviews with staff in decision-making authority that also have experience in the sphere of foreign aid to state institutions. Donor organizations interviewed included the U.S. Agency for International Development (USAID), the European Union (EU), the UN Development Program (UNDP), UN Industrial Development Organization (UNIDO), Swiss Development Cooperation (SDC) and Gesellschaft für Internationale Zusammenarbeit (GIZ). Additionally, representatives from a target segment of

recipient government agencies were interviewed, namely Ministry of Agriculture, Ministry of Healthcare, Ministry of Emergency Situation, Ministry of Energy, Infrastructure and Natural Resources and Ministry of Territorial Administration and Development.

## **DISCUSSION AND INTERPRETATION**

### **Analytical Framework**

As discussed earlier two groups of interviews were conducted to understand the role of institutional capacity in the effectiveness of foreign aid; particularly, to identify the specific ways in which the institutional capacity of the Republic of Armenia contributes to or hinders the effectiveness of foreign aid to Armenia. For the purpose of analyzing the interviews two main categories or dominant themes and related codes were derived from the existing theory for coding the interview transcripts and documents selected for this purpose. They are the following:

*Capacity of state institutions*, coded by professional knowhow; subject matter expertise; project management skills; ability to manage resources; technological knowledge; technical knowledge and skills; recruitment and hiring practices; priority institutional reforms; and related words and phrases.

*Aid effectiveness*, coded by meeting project objectives; feasibility of objectives and targets; smooth implementation of projects; recipient ownership of project; monitoring mechanisms; level of cooperation between donor and recipient; level of involvement of staff; new skills and practices acquired in the process; sustainability of project; and related words and phrases.

According to the literature, the effectiveness of foreign aid depends, to a great extent, on not the amount of aid that the recipient country gets but on the way in which foreign aid is delivered combined with the institutional capacity of the recipient country. If the state

institutions of the recipient do not possess the technical and management capacity to take ownership of and lead projects, then foreign aid does not contribute either of the two components of foreign aid: (a) delivery of foreign aid or (b) sustainable impact of foreign aid on the development of the country. Well-functioning institutions encompass the level of expertise of personnel, transparent and accountable governance, selection and assignment of staff in positions absent considerations of patronage, nepotism and cronyism. If state institutions are not functioning well, then not only does this hinder development, but also it hampers the ability of donors to realize the intended objectives.

## **Content Analysis of Interviews**

### **Aid Effectiveness**

Discussing aid effectiveness, all interviewees articulated that one of the most important criteria that would ensure successful implementation of projects under foreign aid is setting feasible and attainable project objectives. More importantly, the interviewees emphasized that both the donor organizations and recipient institutions must agree to the established objectives and targets jointly. The implementation of project objectives is one of the indicators through which both the recipients and donors measure the level of effectiveness of foreign aid, particularly pertaining to the extent to which the project objectives and targets are achieved.

In order to measure the feasibility of project objectives and their successful achievement, donors and recipient agencies must work to jointly create results matrix or log frame, which delineates the specific activities and changes that the program is trying to attain in the implementation of the project leading to the intended results. All the interviewees in recipient institutions claimed that in the majority of cases they do set intended objectives and targets that are not always fully achieved.



Interviewees from donor organizations claimed that there can be minor issues emerging during the implementation, but they are usually addressed and resolved, and do not always affect achieving the primary objectives and targets set upfront. Two interviewees from recipient agencies highlighted the importance of project objectives stating that *“those aim at achieving the sustainable development goals of Armenia, as set in the Development Strategy Paper.”* Moreover, they consider the realization of project objectives as a critically important prerequisite for effective foreign aid, which also contributes to sustaining or even increasing the amount of foreign aid allocated to Armenia. However, one donor respondent mentioned that more attention and time should be devoted to developing the project log frame in order to increase the effectiveness and efficiency of each foreign aid intervention. This would enable more thorough formulation and establishment of project purpose, goals, objectives, indicators, as well as assumptions and risks thereby affording a better understanding of the intervention and associated activities.

Subsequently, the same interviewees, as well as three others from donor organizations mentioned that during last decade the amount of foreign aid approved for Armenian institutions has significantly increased, which is somewhat indicative that prior interventions have successfully achieved the objectives they were set out to reach and have had a positive impact on state development. One of the interviewees also stated that *“recently we got 100 percent funding from one of our donors, which had not been the case previously; since, generally speaking, you can get such funding support only when you have fully met the objectives and targets of the earlier intervention. This is proof that in previous programs we had managed to do that to their satisfaction.”* Both government and donor representatives agree that the increase of foreign aid is derived from the effective implementation of the overarching goals of projects.

According to foreign aid respondents, project ownership by the recipient agency plays a crucial role in the effective delivery of foreign aid. As covered in the literature on this topic, to realize the most effective and results-driven foreign aid, it is important to establish specific approaches and targets for each recipient country focusing on local peculiarities and priorities. This can be done by relinquishing authority to aid receiving state agencies thereby encouraging them to take ownership of respective projects. Almost all the interviewees, four out of five, mentioned that taking ownership would enable them to push forward towards achieving their priorities and focus on those sectors that are the most critical for development.

Further, one interviewee claimed that *“in most of the cases there is a problem in the aid allocation process whereby one region or sector always gets the most attention and no other projects in other critical sectors are funded. Taking ownership provides the opportunity to avoid duplications and allocate resources to regions most needing it.”* The interviewee also mentioned that not all donors accept the recipient’s ownership of projects and continue to rely on their own roles in managing projects. Another interviewee from donor organization stated that ownership would lead to sustainable development of the country and *“the recipient institutions would play a greater role in the decision making process, even more so than in any other cases or phases.”*

Nevertheless, one of the interviewees clarified that in foreign aid projects taking ownership by recipients is not a necessary precondition for achieving successful results. Moreover, the same person claimed that donors make interventions according to their own priorities and desirable results rather assisting recipient states with their national strategic development goals.

According to the literature, in most cases the effectiveness of foreign aid does not only depend on the amount of assistance, but how the allotted funds are used to bring about

sustainable development. In foreign aid projects, one of the most important components for measuring aid effectiveness is the way the project is implemented. Four out of five aid recipient representatives and all interviewees from donor organizations argue that almost in all projects some problems arise stemming from institutional arrangements, which most often bring to unnecessary slowdowns or delays in project implementation.

Interviewees claimed that project slowdowns sometimes result from the lack of experience or knowledge of civil servants in local institutions, which naturally prolongs achieving the intended results. Interviewees in donor organizations also added that there should be more coordination and project management skills to improve the timeliness and quality of implementation of projects thereby preventing failures or other problems. However, almost all interviewees in donor organizations claimed that they are addressing these issues along with local institutions and implementation is getting smoother compared to what it was a few years back. One of the interviewees from donor organizations mentioned that *“we can see the difference, the situation is improving, though slowly but surely.”* They believed that this improvement is not only the result of experiences gained by the institutions they have worked with, but also due to the young and more educated civil servants involved in foreign aid projects.

Further, in the opinion of both recipients and donors, the key component for achieving successful results is instituting effective monitoring mechanisms. All the interviewees from state and donor organizations mentioned that the mechanisms are mandatory and they are a way to ensure the overall effectiveness of foreign aid. However, donor organizations and recipient institutions perceive the importance of these mechanisms with a slightly different lens. Interviewees from donor organizations view monitoring as an important tool for overseeing implementation throughout the process and for reducing the risks of failures for a number of

reasons, including corruption, not implementing the activities in the log frame, shifting priorities midcourse, etc. Monitoring also affords the opportunity to uncover or identify what is not working well in the project or what issues are hindering the effective use of foreign aid.

Further, one interviewee from a donor organization mentioned that the positive influence and impact of monitoring on effectiveness of aid depends on the actions it entails and mechanisms it has built in arguing that *“if any project fails or does not achieve its goals, this means that our monitoring mechanisms are not appropriate and not working well.”* Along those lines, one interviewee from a state institution argued that *“monitoring mechanisms can also have negative impact in instances where the established mechanisms are very strict, require strict procedures to be followed precisely, which may even slow down the implementation of the project.”* Later on he added that *“regardless of the negative side monitoring is a necessary requisite of effective foreign aid.”*

Improvements in the implementation of projects and capacity to achieve objectives are partially due to effective cooperation between donors and recipients. All interviewees from both donor and recipient institutions claimed that cooperation between donors and recipients is crucial for obtaining the desired impact on development. The involvement of recipient institutions not only is beneficial for the recipient side from the standpoint of pushing state strategic priorities, but also for enhancing the capacity of state institutions in terms of knowledge, skills, and technical abilities. However, one interviewee added that *“the less recipient institutions are involved in the process, the less possible that foreign aid would be effective and the less it would contribute to sustainable development of the recipient country.”*

Overall, all interviewees claimed that foreign aid could be more effective if it were based on closer cooperation between donor organizations and recipient agencies. There was only one

recipient state representative who did not consider the involvement of the recipient institution a success factor. The interviewee claimed that since all the resources come from the donor organization, it should be the major decision-making and implementing body of the intervention receiving foreign aid.

In contrast, however, the involvement of local state institutions would contribute to increasing the capacity of institutions through enhancing the collective knowhow and expertise invested in the project. In most cases, the local experts possess better grasp of the environment than foreign experts or consultants, who possess technical expertise but little knowledge about the nuances involved in the application of the intervention to Armenia, which makes the involvement of local experts necessary for preventing failures related to lack of knowledge of local peculiarities.

However, some level of project ownership is necessary for state institutions to be able to involve local experts and civil servants. This aspect is strongly emphasized by recipient institutions as argued by one respondent who brought the example of a donor organization that had failed to effectively deliver the project because of its insufficient involvement in it. The recipient characterized it as follows: *“they decided the sector, as well as all the details of the project and implemented it without our involvement in it.”* The donor organization did not refute that the failure was primarily their fault, reiterating that their involvement in and control of the project was more than was necessary. However, the respondent added that there were also other reasons, such as changes in funding structures and other related aspects that may have contributed to the project failure.

All interviewees from donor organizations emphasized the importance of involving staff from recipient institutions. They argued that the more civil servants are involved directly in the

project, the more they would gain expertise and knowledge in the implementation process. It would enhance their individual level of expertise and also would strengthen and contribute to the project implementation process. Moreover, the involvement of institutions in the implementation would ensure building the level of knowledge and skills of personnel involved in those projects, which in its turn would contribute to the sustainability of projects implemented in Armenia. All the interviewees from donor organizations mentioned that for assuring the effectiveness and efficiency of foreign aid projects, it is important not only to achieve project objectives but also to create incentives that would lead to the delivery of aid by the same donor organizations in the future. He stated that *“the objective of getting foreign aid is not only getting funding for projects, but creating a strong structure that would lead to implementing such programs on our own in the future.”*

Speaking about local state institutions and their role in effectively realizing foreign aid projects, almost all respondents (both from donor organizations and three out of five from state institutions) labeled them as “reliable partners”. Moreover, they claimed that if the projects had not contributed to sustainable state development and if the projects implemented in Armenia were not successful or effective, donors would not consider Armenia a reliable partner in foreign aid.

### **Capacity of State Institutions**

As discussed earlier the high capacity of state institutions ensures economic growth and sustainable development. Also, the capacity of state institutions is regarded as a critical factor for aid effectiveness, considering that many donor organizations and foreign countries implement development projects together with state institutions. If those implementing partner institutions were not equipped with the capacity needed for project implementation, then aid would not lead

to sustainable development. All the interviewees both from donor organizations and from state reiterated that the capacity of state institutions, particularly the level of pertinent subject matter expertise, plays a crucial role for optimal impact of foreign aid. As claimed by Acuna and Thommasi (1999) and Elobeid (2012) the capacity of state institutions in terms of the resident level of expertise of civil servants (including what is derived from state recruitment and promotion practices) is instrumental for high impact governance.

Elucidating on the issue of subject matter expertise, one interviewee explained that there are continuing issues with that in spite of regular trainings aimed at improving the level of expertise, knowledge and skills in respective fields. One interviewee also mentioned that most often the local trainings and informative sessions are organized and initiated by the state but supported and financed by donor organizations. Moreover, interviewees from donor organizations also stated that the level of subject matter expertise is not always sufficient for sustainable development, but measurable improvements have resulted from the trainings and state institutional capacity has increased with recently hired civil servants that possess the knowledge and skills applicable to their respective positions.

On the topic of state institutions' capacity, there were slight differences among interviewees. One interviewee mentioned that it is really difficult to generalize the professional knowhow and expertise of state institution staff, arguing that *“there are ministries where the officials are really educated, skilled and understand their respective responsibilities very well; but there are also other ministries where the officials don't have the basic knowledge and skills to work in their positions.”* This could imply that the effects of nepotism, cronyism and patronage continue to exist in recruitment and promotion practices.

In contrast, one interviewee argued that it is very easy to work with local civil servants, because they are very qualified and well educated. But the problem, according to this interviewee is that the workload is centralized and put only on those few people assigned to a project and *“if they were to leave I don’t know with whom I would work.”*

Another important criterion that plays an essential role for aid effectiveness is the level of project management skills of civil servants. All the interviewees from donor organizations acknowledged that noticeable improvements have been realized in the recent past, but there are continuing issues with civil servants’ project management skills. Several interviewees claimed that delays in project implementation are not a result of those skill gaps but are attributed to the management structure of state institutions. They believe that the overall management structure should transition to less overbearing forms not only for increasing foreign aid effectiveness, but also for boosting the capacity of state institutions through staff development and empowerment, thereby contributing to development.

The majority of interviewees highlighted the importance of foreign aid reiterating that technical knowhow plays an essential role for achieving the objectives and planned targets of projects. Many interviewees acknowledged that the situation has improved significantly in the past decade, but the technical expertise that donors provide is still necessary for the development of Armenia. One of the interviewees from state believed that *“no doubt the situation did improve, but right now they can’t achieve great success without foreign aid, at least not right now.”*

In regard to the capacity of state institutions to manage resources, all the interviewees from donor organizations did not face any issues with resource management in state agencies. Conversely, two interviewees from state agencies mentioned that while creating the log frame of



the project, they pay significant attention to the financing of each project component or activity. These interviewees claimed that donor organizations usually allocate more money for engaging external experts invited specifically for respective projects than they would prefer to do. For this purpose, they are keen to reducing the funding allocated to experts and instead increase the local expertise and institutional capacity in terms of what is allocated to the implementation of projects.

Speaking about the technical knowledge and expertise of the staff assigned to projects, donor respondents stated that if any problems emerged with the expertise of state staff, they were immediately addressed and resolved. They affirmed that they are very attentive to eliminating the possibility of failure arising from the lack of capacity through project monitoring activities. One interviewee from state mentioned that “*there were cases when such issues emerged, but they were rare.*” Another interviewee also from state mentioned that “*we are having such issues more than they do, but these cases are not so much.*” However, another respondent from a recipient state agency mentioned that the expertise, experience and knowledge of invited external experts alone are not sufficient for the successful implementation of projects.

Interviewees from donor organizations also highlighted the importance of institutional reforms, which would not only contribute to smoother project implementation and increase the effectiveness and efficiency of foreign aid, but also would lead to sustainable development. They claimed that, though the capacity of institutions varies, there is a need for civil service reform particularly from the standpoint of recruitment, hiring, and retention processes. According to donor organizations, developing appropriate position descriptions with qualification requirements that fit respective positions, state institutions would be able to increase expert

capacity with more technocrats in relevant positions. Another necessary reform mentioned by respondents is the need to make state institutions flatter and less bureaucratic.

Another institutional issue that the donor organizations face is the lack of prioritization of development strategies, which not only affects the effectiveness of foreign aid, but also slows down the development process of the country. Along those lines, three interviewees from donor organizations expressed positive comments about the newly created Center for Strategic Initiatives, which is the result of a joint effort by the state and donor organizations or individuals. The creation of this Center is expected to enable the prioritization of development strategies as well as attend to necessary reforms.

## **MAIN FINDINGS AND RECOMMENDATIONS**

The most dominant pattern emerging from the interviews is that foreign aid delivery has been rather successful and effective, but still facing several hindrances and difficulties. There are major issues that need to be addressed and resolved by recipient institutions, including the level of needed expertise and technical skills of local staff. There are weaknesses related to taking ownership of foreign aid projects by state agencies, which often lead to project delays and unsustainable results.

However, along with ownership the donor's direct involvement and monitoring activities are vital for ensuring that foreign aid reaches its intended purpose. Monitoring mechanism and donor-recipient cooperation enable the mitigation of risks of failure or addressing issues related to or stemming from the insufficient expertise of civil servants or experts involved in the projects. Donors, that possess a more skilled and experienced capacity, can enable and drive the achievement of project objectives and targets thereby contributing to the development of

Armenia. Although in the majority of cases state institutions manage to achieve the goals and targets established at start, there are issues in implementation process concerning project management and collective level of resident expertise. The majority of interviewees claim that the level of professional knowhow and expertise of officials in state institutions has significantly increased in the past decade. This, however, refers to only high ranking incumbents, who have relatively higher levels of education and experience, but the lower level civil cadres still lack the qualifying skills and experience.

Overall, the foreign aid allocated to Armenia helps not only financially, but also in terms of technical knowledge and skills. The projects implemented by donors help to increase the professional knowhow and expertise of staff involved in projects, which also contributes to the sustainability of those projects.

## **Recommendations**

Research showed that several areas in donor-recipient cooperation need to be addressed to improve the quality of aid in Armenia. However, the areas to be reformed do not only imply changes in state institutions, but also have relevance to changes necessary for donor organizations that play an essential role in the reform process.

These findings lead to the following recommendations:

- Taking ownership by recipients: In order to ensure the successful delivery of foreign aid, it is critical to establish specific approaches and partnered arrangements that contribute to empowerment and taking ownership of interventions by recipient agencies. Such ownership of projects by recipient institutions would help to push the development objectives forward, attract donor attention to specific priority areas or sectors that are vital to sustainable development.

- Recruitment and promotion practices: Augmenting the level of expertise and professional expertise currently absent in some parts of state institutions is a necessary requisite for development. Reforming the recruitment, hiring and retention practices would enable the state apparatus, including ministries and agencies, to minimize or eliminate nepotism, cronyism and patronage and to enhance the overall capacity of state institutions.
- Better focus on training and staff development: Although in most local institutions civil servants attend trainings and workshops to increase their expertise, but this is not structured and performance related in most cases. Training programs in state institutions should be better coordinated and organized strategically to fit into the development agenda of the state and fir individual staff expertise and performance skills gaps.

## **LIMITATIONS OF THE STUDY AND CONCLUSION**

The current research used only a qualitative method, collecting data from interviews with representatives from both donor organizations and state institutions. However, the number of interviewees was relatively small considering time constraints. Moreover, the period of data collection coincided with the national pre-election period, which hindered the research process as many potential interviewees were too preoccupied with the campaign and/or refused to be interviewed.

In conclusion, the study tried to investigate whether the foreign aid provided to Armenia was effective and whether it brought economic growth or contributed to sustainable development of Armenia. It also tried to explore what institutional factors hindered or promoted aid effectiveness and what institutional reforms Armenia need to do to achieve more effective and efficient foreign aid.

As was presented in the literature, foreign aid is not always conducive to growth and development of recipient countries. However the interviews showed that the project implementation process is not always smooth and optimally productive mostly due to the relatively weaker institutional capacity of state institutions. A reformed civil service could reduce or eliminate nepotism, cronyism and patronage and focus on hiring the best qualified of applicants. This would increase the level of effectiveness of foreign aid.

Despite existing issues and hindrances in the implementation of development projects throughout the ministries, the overall results from foreign aid projects have been rather successful, especially in the more recent past that has seen significant improvement in the professional knowhow and expertise of officials. Considering that the effectiveness of foreign aid is also due to the skills and knowledge acquired by civil servants and state officials in prior joint projects with donor organizations, as well as some institutional changes and trainings contributing to it, on-the-job as well as formal training programs should become an integral part of the state development agenda.

Nevertheless, it is important to note that earlier reforms realized in state institutions have significantly impacted the delivery of foreign aid, an opinion that was consistency expressed by all donor organizations interviewed. But these reforms must continue in order to fully achieve sustainable development.

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## APPENDICES

### Interview questionnaire for donor organizations

1. What are the most important criteria for you in selecting or designing intervention programs? Are these decisions made by your office here in Armenia or they are determined by bi-lateral agreements with the Armenian government?
2. From your perspective, have the interventions you realized fully meet the strategic goals and objectives of your program in Armenia. What were the impeding factors that have impacted the effectiveness of your aid/ program?
3. What is (are) the biggest issue(s)/problem(s) in Armenia that needs to be reformed in order to increase the effectiveness of foreign aid?
4. What role do the local institutions play in the effectiveness of foreign aid?
5. In your opinion, what are the specific institutional problems that are hindering or slowing down the development of Armenia?
6. How can those problems be resolved? What priority reforms would you recommend for improving the state institutional capacity?

### Interview questionnaire for recipient institutions

1. Do you have any involvement in the decision making process as to where/how to allocate the aid or is the decision made solely based on the donor's strategic agenda/priorities?

Երբ միջազգային ընկերություններն գումար են տրամադրում զարգացման ծրագրեր կամ նախագծեր իրականացնելու համար, արդյոք դուք ունեք որևէ ներգրավվածություն որոշումներ կայացնելու գործընթացին, թե այդ որոշումներն կայացվում են միայն ըստ իրենց առաջնահերթությունների և նախապատվությունների:

2. What are the largest and most problematic issues that you face while implementing the programs/ projects/ aid provided by donors? Are there any institutional problems that you face while implementing them (viewed both from your and from their sides)? Are there issues with expert knowledge necessary in implementation?

Որո՞նք են ամենամեծ կամ ամենախնդրահարույց հարցերը/ոլորտները այս ծրագրերը իրականացնելու ժամանակ: Ունենում եք արդյոք որևէ ինստիտուցիոնալ խնդիրներ, թե՛ ձեր և թե՛ նրանց կողմից: Կա՞ն արդյոք խնդիրներ փորձագետների փորձառության, գիտելքիների հետ այս ծրագրերն իրականացնելու ժամանակ:



3. To what extent these projects/programs promote the overall development of Armenia?

Որքանով են այս ծրագրերը նպաստում Հայաստանի զարգացման գործընթացին:

4. What are the most important programmatic issues that are considered to be priority for Armenia's development? Did you draw the attention of donors to these problems?

Որո՞նք են ամենակարևոր կամ ամենամեծ ծրագրային խնդիրները, որոնք համարվում են Հայաստանի զարգացման համար առաջնահերթություններ: Երբևէ նրանց ուշադրությունները հրավիրե՞լ կամ փորձե՞լ եք հրավիրել այս առաջնահերթությունների վրա:

5. What are the mechanisms through which the donor checks the use of funds in return to achieve objectives/results? Are these mechanisms acceptable to you?

Որո՞նք են այն միջոցները կամ մեխանիզմները, որոնց միջոցով միջազգային կառույցները ստուգում կամ հետևում են ծրագրերի իրականացման գործընթացին և արդյոք այս մեխանիզմներն ընդունելի են ձեզ համար:

6. According to you and your experience what are the greatest drawbacks in donor-recipient cooperation, or what would you change?

Ըստ Ձեզ, որո՞նք են ամենամեծ խնդիրները կամ բացթողումները այս երկկողմանի հարաբերությունի մեջ՝ ելնելով ձեր փորձից: