

Caught in the Middle:
Multilateral Development Bank Responses to Environmental Performance

by

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Dissertation submitted in partial fulfillment of
the requirements for the degree of Doctor of Philosophy in the
Nicholas School of the Environment
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ABSTRACT

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Abstract

Since their creation, the multilateral development banks have accumulated performance records that include both substantial successes and stunning failures. Nowhere have their performance records been more mixed and controversial than with respect to environmental management issues. The multilateral development banks have financed projects that are widely considered to be environmental disasters, but have also financed projects that successfully included best practice environmental mitigation measures. They have wasted hundreds of millions of dollars financing unsuccessful environmental protection programs, while at the same time supporting programs that contributed to the rapid development of environmental management capacity in less-developed countries. The purpose of this dissertation is to explore when and why monitoring and evaluation can prompt the multilateral development banks to move away from poor performing projects and towards high performing projects.

This type of *performance-based allocation* has been repeatedly highlighted as a key element in the successful delivery of development assistance. To test when the multilateral development banks practice performance-based allocation, I assembled a team that coded environmental performance information from 960 project evaluations, 174 program evaluations, and 74 civil society complaints. I use the resulting data to model when four multilateral development banks – the World Bank, Asian Development Bank, Inter-American Development Bank, and African Development Bank – make performance-based allocation decisions about environmentally-risky and environment-improving operations. In addition, I visited the headquarters of each of these organizations and conducted interviews with 54 staff members about the processes that are in place to use monitoring and evaluation information as part of decision-making.

I find that the establishment of monitoring and evaluation systems at the MDBs has not created incentives for staff to practice performance-based allocation. Instead, performance information influences allocation decisions when it helps MDB staff approve future projects more quickly. It does so by helping staff identify development projects that are likely to face significant delays due to the inability of the borrowing country to manage negative environmental impacts and to identify the borrowing countries that are likely to successfully implement environment-improving operations.

Dedication

To my wife Ryoko, who has taught me the meaning of patience and persistence.

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1 The Problem of Performance at the Multilateral Development Banks

1.1 A Mixed Bag of Environmental Performance

In the course of designing and implementing their project portfolios, the multilateral development banks (MDBs) have accumulated performance records that include both substantial successes and stunning failures. Nowhere have the records of the MDBs been more mixed and controversial than their environmental performance. The MDBs have been credited with causing alarming deforestation because of poorly designed road projects, while at the same time they have supported borrowing countries in adopting national-level environmental regulatory frameworks (Independent Evaluation Group [IEG], 2008b; B. Rich, 1994). The MDBs have funded some of the largest, high-polluting, fossil fuel energy projects in the world, while concurrently becoming the largest donor-assisted financiers of clean energy projects globally during the last decade (Bretton Woods Project, 2010; Independent Evaluation Group [IEG], 2010a). They have financed large dam projects that displaced thousands of people and inundated vast tracks of natural areas, but they have also supported innovative, community-driven natural resource management projects that addressed the connection between poverty and environmental degradation in rural areas (Khagram, 2004; Kumar, Saxena, Alagh, & Mitra, 2000). Many activists regard the MDBs as harbingers of environmental destruction, whereas government leaders have turned to them to manage international financing efforts on climate change, forest conservation, and pollution prevention.

The performance records of the MDBs, especially their shortcomings, have been documented extensively. The purpose of this dissertation is not to retread this same ground. I begin from the premise that the MDBs have been successful in some respects

and unsuccessful in others. Instead, I ask a follow-up question that is likely to have significant implications for the way development and environmental financing is managed in the future: *are the MDBs responsive to their mixed performance records by moving away from low-performing projects and towards high-performing projects?*

The MDBs operate in borrowing countries with poor governance and high levels of political uncertainty. They manage technically complex projects and attempt to solve development problems that do not have clear solutions. Moreover, the norms about what constitutes a successful environment or development program have shifted substantially during the time that the MDBs have been in existence. Under such conditions, some level of failure is inevitable. As former World Bank president Robert McNamara argued, the crucial task for the development banks is to respond effectively to their performance:

“Certainly the Bank has had its failures... it has learned and is continuing to learn from its failures... Taking account of these lessons will, I believe, increase the Bank’s rate of success for the future” (2003, p. ix).

This dissertation specifically focuses on the ability of the MDBs to respond to evaluations of their environmental performance, an area where the MDBs have accumulated their most controversial records. Since the early-1990s, the MDBs have been under pressure to both decrease the environmental damages associated with their development projects and to finance more projects that improve environmental conditions in their borrowing countries. Under pressure from donor countries, the MDBs adopted formal policies that require them to consider the environmental impacts of their activities. They have also developed concrete strategies for investing in environment-improving operations and integrating environmental activities into development projects across their portfolios. The implementation of these new policies and strategies has not always been smooth, but it has afforded the MDBs with ample

opportunities to learn about which borrowing countries successfully mitigate environmental damages when implementing infrastructure projects and where environment-improving operations can be pursued successfully.

They are able to do so because along with new environmental commitments, the MDBs have invested in monitoring and evaluation systems that provide information about when and why projects succeed and fail. Independent evaluation departments review a sample of projects each year and measure not only development performance, but also how well different borrowing countries and MDB operational departments achieve environmental goals. Independent evaluation offices also produce multi-year evaluations that examine when the entire suite of projects in a particular country have successfully reached general goals, which often include environmental goals. In addition, formalized complaint mechanisms that allow civil society groups to petition for redress when they suffer environmental damages as the result of projects have been established at each of the MDBs. Combined with environmental policies and strategies, these information provisioning mechanisms provide ample opportunity for the MDBs to improve their performance by making better allocation decisions in future periods.

In 1984, for example, the Asian Development Bank approved the Fisheries Infrastructure Sector Project in Indonesia (Asian Development Bank [ADB], 1997a). This project was intended to support increased fishing effort in Indonesia in underutilized coastal areas and promote economic development in fishing communities. The project produced poor results, especially with regards to environmental performance. The independent evaluation completed for this project described how:

“the landing area has become polluted from uncontrolled discharge of wastes... contributing to a deterioration in fish quality... the rapid growth in the number of small boats, many of which use the Project facilities, is contributing to overfishing in many coastal areas” (ibid., p. iv).

The evaluation concluded that the project was poorly designed and that Indonesia's fisheries agency was poorly capable of carrying out similar projects. It recommended future operations "should incorporate measures to limit fishing effort in coastal waters or focus on aspects that do not encourage increase fishing," which would represent a shift in the portfolio composition (ibid., p. iv). That same year, the ADB Board approved the Coastal Community Development and Fisheries Resources Management Project. This new project directly followed the recommendations of the independent evaluation, having primary goals to "conserve coastal fisheries resources" and to "rehabilitate the physical fisheries facilities... to improve environmental and sanitation conditions" (Asian Development Bank [ADB], 1997b, p. ii-iii).

This case suggests that the Asian Development Bank responded to Indonesia's poor performance mitigating environmental damages. However, a number of questions follow from this possibility. Is this type of response common and systematic across the MDBs, or are such instances only accidental? What practices and policies within the MDBs support this type of response? What types of external pressures make the MDBs more responsive to performance information about environmental damages? Answers to these questions have important implications for the ability of the MDBs to ensure that their development projects meet environmental standards.

Or take for example, the controversy surrounding the Chad-Cameroon Oil Pipeline and the civil society outcry about its negative environmental consequences. Despite being portrayed as one of the most state-of-the-art, environmentally-friendly oil projects in the world, the World Bank has been embroiled in controversy ever since it approved financing for the project. In 2001, more than 100 resident across three areas in Chad filed a formal complaint with the World Bank's Inspection Panel alleging that the environmental assessments and management plans for the project were insufficient to

protect them from negative environmental impacts. In particular, the complaint alleged that the pumping of oil across Chad had the potential to destroy important medicinal plants, pollute surface waters used by local communities, and negatively impact agricultural production. Similar concerns were echoed by other environmental groups (e.g., Horta, Nguiffo, & Djiraibe, 1999).

Under great scrutiny, the World Bank Inspection Panel investigated these allegations. The investigation report found that while the implementing department made “substantial effort” to mitigate negative environmental impacts, shortcomings were evident in the environmental assessment process, the environmental management plan, and the implementation arrangements that were made for the environmental management plan (Inspection Panel, 2002, p. xii). The Inspection Panel report called for improved environmental assessments and management plans as the project continued. In response, the World Bank management remained committed to the project but agreed to prepare a regional development and environmental assessment plan, convene an expert advisory panel to oversee compliance with environmental safeguard policies, and collect further baseline data on the health of local population to allow for more effective monitoring of environmental impacts (International Bank for Reconstruction and Development [IBRD] & International Development Association [IDA], 2002, p. 17-19).

This case demonstrates that civil society groups have the potential to push the MDBs for better environmental practices by using their voice and access to complaint mechanisms. Since civil society groups provide monitoring of environmental performance of their own accord, they could be instrumental at providing states with monitoring information that can be used to choose better projects. But, when are civil society groups likely to provide monitoring or file complaints? When do the MDBs respond to the pressures from civil society groups to improve their environmental

performance? Does civil society opposition to environmentally risky projects cause the MDBs to avoid future projects in countries where they are likely to face opposition, or do they just implement projects more diligently in those countries? Answers to these questions have important implications for the role that civil society groups can play in securing better environmental practices at the MDBs.

The opportunity to respond to performance extends beyond mitigating environmental damages. Using information from evaluations, MDB staff can identify borrowing countries that successfully implement environment-improving operations. In 1993, for example, the World Bank approved the \$76 million Environmental Technical Assistance Project for China. This project was designed to upgrade the institutional capacity of the State Environmental Protection Agency and the Chinese Academy of Science, and thereby address China's rapidly deteriorating environmental conditions. An independent evaluation found the project to be "highly successful" and noted substantial achievements, including the introduction and improved implementation of national environmental legislation (Independent Evaluation Group [IEG], 2007). The conclusion of the evaluation noted the need for a "continuing role for the Bank in strengthening monitoring and enforcement at the provincial level, and a strong desire for a second technical assistance project targeted to provincial Environmental Protection Bureaus" (ibid., p. 17). Because the project was successful, all parties showed a desire to pursue similar projects in the future. According to the World Bank project database, China borrowed more than \$3 billion of environmental financing in the three years following the evaluation, much of which was directed to provincial or municipal implementing agencies.¹

¹ The World Bank project database is available at: <http://go.worldbank.org/KPMUDAVVT0> (Accessed May 2011).

In this case, the successful implementation of an environment-improving project created an opportunity to finance related projects in the future. The World Bank fulfilled donor expectations to increase environmental financing in ways that achieved results. Is this type of response limited to high-performing countries or have all countries received more environment-improving projects? With plans in place to drastically increase the availability of environment-improving financing in the coming decade, it will be important to know whether scalability and selectivity can work together. If not, important trade-offs between coverage and effectiveness of environmental financing must be made.

Each of the above examples showed a positive response to measured environmental performance, but counterexamples also exist. In 2004, for instance, the Asian Development Bank evaluation department completed an evaluation of the Cambodia lending portfolio during the previous decade (Asian Development Bank [ADB], 2004). This evaluation paid particular attention to environmental management activities in the Tonle Sap region, which covered 38% percent of the Cambodia's area and whose fisheries "provide for up to 80% of the protein intake for Cambodian people, 50% of whom depend on the lake's resources, directly or indirectly" (ibid., p. 17). The country program evaluation chronicled how a series of technical assistance and investment projects achieved less than satisfactory results, owing to the fact that the programs did not properly account for Cambodia's poor institutional capacity (ibid., p. 16-18). The evaluation recommended that future programs should be "modest" in nature. In the years that followed, several technical assistance projects were approved,

eventually leading to the \$40 million Tonle Sap Poverty Reduction and Smallholder Development Project in 2007.²

In this case, poor performance at meeting environmental goals did not decrease investment in future Tonle Sap natural resource management and development programs. Given that poor institutional capacity was a key reason for poor performance in past operations, it is reasonable to expect that the current round of projects will face similar performance issues. However, ADB staff prioritized continued engagement in the natural resource management sector and development in the Tonle Sap region, despite past performance issues. Does borrowing country need, donor project supply preferences, or bureaucratic inertia account for this response? Can planning processes that are based around a borrowing country's most pressing development needs promote selectivity in the types of projects that are chosen? Answers to these questions have important implications for the ways that country lending strategies for borrowing countries should be developed.

These examples are a small subset of the opportunities that the MDBs have had to respond to the environmental performance of their projects. This dissertation aims to explain when and why this happens. What types of oversight, administrative policies, and external pressures make them responsive to their environmental performance? When they are not responsive to their environmental performance, what is to blame? Misaligned staff incentives? Inappropriate donor state mandates? Insufficient monitoring and evaluation information for the member states of the MDBs to provide oversight? Presence or absence of civil society or international groups who monitor outcomes and issue public criticisms? By examining different types of environmental

² For information on the components of this project, see the project information website at: <http://www.adb.org/projects/project.asp?id=41435> (Accessed May 2011).

performance information and MDB allocation decisions over time, I intend to answer these questions.

1.2 The Loan Approval Culture and the Problem of Performance

The MDBs are among the largest international organizations and have collectively approved more than \$1.3 trillion in project and program financing between 1973 and 2001 (Hicks, Parks, Roberts, & Tierney, 2008, p. 184). The largest of the MDBs is the World Bank, which was originally created to facilitate the reconstruction of Europe after World War II. Since that time, it has expanded to finance development projects around the world. The World Bank is complemented by the regional development banks, which carry out similar operations, but operate within particular regions. The largest regional development banks that are engaged in public sector lending are the Asian Development Bank, Inter-American Development Bank, and African Development Bank. Although these MDBs are based in different places around the world, they all serve one core function: to allocate and manage development financing delegated to them by states.

In the process of carrying out this function, the MDBs have not escaped controversy. At times, insiders have been among the most important critics of MDB performance and allocation practices. In September 1991, Lewis T. Preston became the eighth President of the World Bank.³ In the years immediately prior to the Preston presidency, the World Bank became entangled in a number of controversies about its performance. The most important controversy centered on its financing of the Narmada (Sardar Sarovar) Dam Project. Civil society groups around the world mobilized and protested the project's lax environmental and social standards (Cullet, 2007). The

³ This information is taken from the World Bank's published institutional timeline, available at: <http://go.worldbank.org/7ATOENILQ0> (Accessed May 2011).

negative attention generated by this project put the performance of the entire World Bank portfolio into the spotlight. For example, the US Congress held a variety of hearings about the performance of the World Bank in response to the issues raised by the Narmada project.⁴

One of the first actions that Preston took upon assuming the World Bank presidency was to establish an internal task force to examine performance issues across the World Bank portfolio, led by Vice President Willi Wapenhans. While the resulting 1992 World Bank Portfolio Management Task Force Report (a.k.a. “Wapenhans Report”) was intended to be an internal document, it was soon leaked to the press, which created an uproar among both donor states and civil society groups (Shihata, 2000). The report chronicled a significant deterioration in the performance and effectiveness of World Bank programs, with 20% of active projects in 1991 having “major problems” (Wapenhans, 1992, p. ii). The report cited an entrenched “approval culture” as one of the main reasons for this decline:

“There are also aspects of Bank practice that either may contribute to portfolio management problems or are insufficiently effective in resolving them. Underlying many of these aspects is the Bank’s pervasive preoccupation with new lending. In the eyes of Borrowers and co-lenders as well as staff, the emphasis on timely loan approval (described by some assistance agencies as the “approval culture”) and the often active Bank role in preparation, may connote a promotional – rather than objective – approach to appraisal” (Wapenhans, 1992, p. iii)

Additionally, the report described how the career and promotion prospects of Bank staff were dependent on planning new operations, rather than successfully managing existing projects (ibid., p. 17-18). The report stated that this incentive structure was derived from “a predominant Board interest in new lending,” which makes “the

⁴ For example, a US Congressional hearing on the replenishment of the World Bank’s International Development Association, the Global Environment Facility, and the Asian Development Fund included substantial discussions of the environmental shortcomings exposed by the Narmada project at the MDBs. See the House Subcommittee on International Development, Finance, Trade, and Monetary Policy hearing “Authorizing Contributions to IDA, GEF, and ADF” (HRG-1993-BFU-0087) on May 5, 1993.

task of engineering cultural change in support of portfolio performance management considerably more difficult" (ibid., p. 18). Thus, while the characteristics of borrowing countries certainly influenced the performance of individual projects, the fundamental problem of performance for the World Bank was an inability to put supervision, careful project design, and selectivity ahead of the organizational necessity to approve new projects.

Indeed, one of the primary recommendations that came out of the Wapenhans report was that "if the Bank is to remain effective, portfolio performance must be taken into account in the Bank's country assistance strategies, business processes, and personnel policies" (Wapenhans, 1992, p. ii). Under an incentive structure that rewards new project approvals, being selective about projects based on past performance runs counter to MDB staff interests. Unless donor states or civil society groups are able to alter the incentive structure facing MDB staff, performance-based allocation is unlikely.

The attention created by the Wapenhans report soon rippled out to the other MDBs. In the following two years, the Asian Development Bank, African Development Bank, and Inter-American Development Bank all completed portfolio performance reviews. Each one reported performance problems associated with the same type of approval culture (Asian Development Bank [ADB], 1994; Inter-American Development Bank [IADB], 1993; Knox, 1994). For example, the Asian Development Bank Task Force produced the following findings:

"An important issue that has emerged from the analyses of the Task Force is the need for the Bank to reconcile its resource transfer and development objectives. Its resource transfer role is to transfer programmed amounts of financial resources annually to its developing member countries. This sometimes translates into an emphasis on obtaining loan approvals as per the annual program. Related pressures are created during the project preparation and implementation processes, sometimes leading to compromises on project quality and on potential development impact. This phenomenon has been termed the 'approval culture' in the Bank" (1994, p. 5).

The member states of the MDBs expect a certain amount of financial resources to be transferred, which causes MDB staff to take shortcuts in order to approve more loans. Indeed, one of the main findings of the ADB review was that “feedback from lessons of past experience are not fully utilized in programming and project design, and in implementation activities” (ibid., p. iii).

These findings have been echoed in a great deal of scholarly work on the performance problems at the MDBs (Nielson & Tierney, 2003; Svensson, 2003; Weaver, 2007, 2008; Weaver & Leteritz, 2005). As Weaver writes about the approval culture:

“There is equal skepticism regarding the extent to which [the evaluation department’s] findings are taken into consideration by project managers within the organizations culture, which rewards project approval but until recently made little visible effort to hold managers accountable for the outcomes of projects” (2008, p. 67).

Like other types of bureaucratic agencies, entrenched incentives have developed at the MDBs that are difficult to dislodge. With their delegated authority and resources, the MDBs are expected to carry out activities and achieve results in line with the interests of states, which in this case includes effectiveness. It is clear, however, that IOs do not always achieve the results that are expected from them by their member states (Abbott & Snidal, 1998; Barnett & Finnemore, 1999; Gutner, 2005; Martens, 2005; Nielson & Tierney; Pollack, 1997; Weaver, 2010). In particular, IOs can develop interests to increase their budgetary resources, maintain internal practices that benefit top decision-makers, and adhere to professional or technical norms (Barnett & Finnemore, 1999; Weaver, 2008). The approval culture at the MDBs is a clear example.

Scholars have questioned whether states and other external actors are able to significantly change the incentive structure and internal culture of international organizations. International organizations often control technical expertise and have a great deal of autonomy in their actions as a result (Barnett & Finnemore, 1999). At the

MDBs, an entrenched set of practices has developed around using technical expertise to secure new lending, not only in terms of tangible career incentives, but also in terms of intangible professional norms (Weaver, 2008, p. 26-31). As long as member states task the MDBs with meeting lending targets, these practices will be difficult to dislodge.

The portfolio performance reviews of the early-1990s recommended that the MDBs redouble effort on monitoring and evaluating to address the “approval culture.” As the Asian Development Bank review stated, for example, “a major feedback activity, post-evaluation, has provided limited feedback into Bank operations until recently. Monitoring of implementation has rarely extended beyond routine aspects of physical and financing progress.” One of the primary recommendations of the ADB report was to reorient evaluation to focus on performance during implementation and the impact of projects on development (ibid., p. iv). In this way, staff would have better information about effective project design and donor states would have the information they needed to provide better oversight. It remains unclear, however, that better monitoring and evaluation can overcome the approval culture and its associated problems for performance.

1.3 Can Monitoring and Evaluation Overcome Poor Performance?

1.3.1 The Principal-Agent Framework

To address whether monitoring and evaluation can help to overcome the approval culture and associated problem of performance at the MDBs, it is first necessary to establish the political context that shapes decisions about where to allocate aid and lending. Researchers have recognized that the way public organizations use performance information are inextricably bound up in the political incentives facing those organizations and the personal incentives of their staff (Cronbach, et al., 1980;

Weiss, 1973, 1988, 1998). Like other research on the actions and behavior of the MDBs, I begin with a principal-agent model to describe how the MDBs interact with their member states (Lyne, Nielson, & Tierney, 2006; Milner, 2006; Nielson & Tierney, 2003).

The activities of the MDBs are based on authority delegated to them by member governments. The fundamental feature of such a relationship is “a conditional grant of authority from a *principal* to an *agent* that empowers the latter to act on behalf of the former” (Hawkins, Lake, Nielson, & Tierney, 2006, p. 7). Delegation is prevalent throughout economic and political contexts. Owners delegate decision-making authority to business managers, for example (Feltham & Xie, 1994). Examples in political contexts include US Congressional delegation to executive agencies (Weingast & Moran, 1983), public delegation of war-making powers to executives of nation-states (Downs & Rocke, 1994), the delegation of shared defense functions to military allies (Lake, 1996), and the delegation of authority to finance development to the MDBs (Nielson & Tierney, 2003). In all of these contexts, the principal empowers the agent to act on the principal’s behalf.

The particularly interesting part of this relationship arises when the interests of the agent do not align with the interests of the principal. Under these conditions, the agent might use the authority and resources delegated to them in ways that do not benefit the principal. However, it can be difficult for the principal to detect that their agent is acting in this way. In his seminal article, Eisenhardt describes how information problems are central to issues that arise between principals and their agents:

“Agency problem that arises when (a) the desires or goals of the principal and agent conflict and (b) it is difficult or expensive for the principal to verify what the agent is actually doing. The problem here is that the principal cannot verify that the agent has behaved appropriately” (1989, p. 58).

If principals were able to monitor the activities of their agents in costless ways and could easily sanction their agents or withdraw delegated authority in the event that their agents acted counter to the principals’ interests, then the agency problem would

not exist over the long term. However, principals often lack the ability to monitor agents and cannot easily sanction their agents. For these reasons, problems in performance often arise when principals delegate powers to their agents. The degree to which agents' preferences differ from those of their principals is called agency slack. Agents like agency slack, which constitutes autonomy from oversight and interference, offers the opportunity for agents to implement their own preferences instead.

Delegation of authority and resources to the MDBs is a classic example of a principal-agent relationship in international relations (Milner, 2006; Nielson & Tierney, 2003). States collectively created the MDBs and delegated substantial authority and resources to design and implement development projects to the MDBs. The continued delegation of authority continues to this day. In 2008, for example, donor states to the Asian Development Bank agreed to replenish the concessional lending resources with \$11.3 billion (Asian Development Bank [ADB], 2008a). In 2009, the same donor states chose to triple the general capital resources available for market-rate lending of the Asian Development Bank to \$165 billion.⁵ As of 2009, the World Bank Group had more than 10,000 staff, lent more than \$50 billion annually, and maintained an annual administrative budget of more than \$1 billion (World Bank, 2009b). While member states oversee the high-level strategic directions of the MDBs, they are not substantially involved in day-to-day project design and implementation decisions, which they delegate to the MDB staff.

Because the MDBs have resources to carry out a wide range of activities independently from their member states, they have the potential to act in ways that are counter to the interests of their member states. Most notably, the approval culture

⁵ See the brochure "General Capital Increase V," available at: <http://www.adb.org/Documents/Brochures/InFocus/2010/General-Capital-Increase-V.pdf> (Accessed May 2011).

described above incentivizes staff to choose large projects that can be approved quickly, potentially at the expense of donor state preferences for effectiveness. Donor states lack the ability to perfectly monitor whether the MDBs are acting in their interests because (1) they cannot observe day-to-day decisions; (2) they cannot determine whether design decisions made about projects are based on incentives to approve loans or to achieve development objectives; and (3) decisions made about the design of projects are technical in nature, which obscures the motivations of MDB staff and managers.

Given this framework for analysis, there are three possibilities for how monitoring and evaluation might help to overcome environmental performance issues at the MDBs. First, when monitoring and evaluation information is available, it may give donor states the information they need to provide oversight or use administrative procedures to prompt better allocation decisions. Second, it might be the case that even when information about performance of recipient governments or projects is made available through monitoring and evaluation, donor states lack the tools to sanction the MDBs for poor performance and are unable to withdraw the authority that they previously delegated. Third, it may be the case that donor states do not have a strong interest in environmental performance, in which case monitoring and evaluation is unlikely to prompt performance-based allocation. I explore these three possibilities in turn.

1.3.2 Do Donor Countries Lack Information to Provide Oversight?

The problem of performance at the MDBs might simply be rooted in the inability of donor states to monitor performance. The MDBs engage in a wide range of highly technical activities and address development problems that do not have clear solutions. Thus, it can be very difficult for donor states to assess whether choices made by bank staff are optimal for achieving development outcomes that are prioritized by donor

states. In addition, it is difficult for donor states to monitor implementation efforts for individual projects, since their primary function is to discuss and approve new lending operations through the Board of Executive Directors.

Indeed, the question of information asymmetries between states and international organizations (IOs) has been a central part of the study of IOs. In an important early study, Pollack writes that “monitoring and sanctioning are costly to member state principals,” which provides a way for European Community organizations to act independently of the EU’s member governments and influence European integration (1997, p. 101). Likewise, in their seminal article, Barnett and Finnemore argue that “IOs have become autonomous because of their embodiment of technical rationality and control over information” (1999, p. 709). State principals may delegate to international organizations precisely because the latter are able to coordinate specialized expertise in ways that are not possible for the principals themselves, making it even more difficult for donor states to understand what activities are best suited to achieve their interests (Hawkins, et al., 2006, p. 13-15). For example, Lipson (2010) finds that because the relationship between UN peace-keeping activities and outcomes is highly ambiguous, it is almost impossible for state principals to assess and respond to performance. Similarly, Vreeland (2006) argues that it has been difficult for states to insist on reforms at the International Monetary Fund because they do not understand the reasons why programs have been unsuccessful. Under conditions of uncertainty, therefore, IOs have substantial abilities to act in ways that are counter to state interests in effectiveness.

With the establishment of *independent evaluation departments*, which report directly to the Board of Executive Directors (member state representatives) at each MDB, a new source of information about performance became available. Because the

evaluation departments do not depend on operational departments for their funding, they lack incentives to produce flattering assessments of staff and borrowing country performance. In addition, the evaluation departments are staffed by sector specialists that are able to evaluate the appropriateness of technical decisions. As such, information about performance contained in evaluations should address asymmetries in information between donor states and MDB staff that are at the heart of many principal-agent issues.

If the MDBs are widely responsive to information in evaluations across different borrowers and sectors, then it is likely that asymmetries of information are at the heart of the poor performance at the MDBs. This would suggest that establishing better monitoring and evaluation systems at the MDBs would significantly improve the banks' environmental performance.

1.3.3 Do Donor Countries Lack the Ability to Require Performance-Based Allocation?

Even if monitoring and evaluation provide donor states with the information that they need to identify failing operations, they may not have the tools to insist on allocating the next round of lending based on evaluations of recipients' previous performance. Researchers working on other areas of state-IO relations, have found that member states sometimes fail to produce sufficient incentives for IO staff to change their practices, despite clear preferences on the part of member states. Pollack and Hafner-Burton (2010) found, for example, that gender mainstreaming policies promoted by member states have had limited effects in the European Commission because they fail to provide "hard incentives" for staff to change their practices. Other studies across a variety of contexts have found that sanctioning can be very costly for principals, even when they have information about poor performance (Elgie, 2002; Pollack, 1997; Wilks, 2005). In these cases, member states to international organizations have no credible way

to sanction their agents for failing to carry out their mandates. Because IO activities serve multiple purposes, shutting down programs for poor performance in certain areas can harm the overall interests of member states. In addition, even if member states to IOs are able to monitor organization-level performance, it can be difficult to monitor the individual staff performance, which may be necessary when aggregated performance is based on the diffused decision-making of individual staff.

A more fundamental issue for the MDBs is that they exist to transfer development resources to less-developed countries, many of which suffer from significant governance problems. As Easterly argues, “the success of past aid to follow conditions and the failure of past aid to follow conditions are both taken as justification for future aid” (2003, p. 38). Given that a primary mandate of the MDBs is to make development investments where private sector lending is unavailable, the MDBs have only been willing to withdraw from lending to particular countries in extraordinary circumstances.⁶ Donor states and MDB staff often view ineffective project outcomes as necessary costs on the path to long-term capacity development in recipient countries. Because donor states are reluctant to stop financing flows for poor performance, they lack other tools to ensure that the MDBs act in their interests even when they have information about performance.

In addition, member states to the MDBs do not have uniform interests, which may make it difficult to coordinate demands for performance at the Board level (Lyne, Nielson, & Tierney, 2009; Waterman & Meier, 1998). For instance, when the World Bank Inspection Panel was established to provide civil society groups an institutionalized way to pass along environmental performance information, there was

⁶ For example, the World Bank suspended lending to Zimbabwe in 2000 after it failed to repay existing loans, following a period of violent political repression and understated war spending (Nyahti, 2000).

significant disagreement among member country about which allegations should be investigated (D. Clark, 2003, p. 11-15). At the African Development Bank and Inter-American Development Bank, donor states hold a minority of shares, which has resulted in their inability to maintain a strong focus on environmental reforms (staff interviews with author).⁷ Thus, to the extent that the different MDBs are selectively responsive to environmental performance in ways that correspond with policy or oversight differences, it might be the case that donor states lack the tools to induce performance-based allocation. Under these conditions, it will be important to find the tools that donor states can use to constrain the approval culture at the MDBs.

1.3.4 Do Donor Countries Not Have Strong Environmental Interests?

Donor states have distinct and oftentimes competing interests about how development financing should be allocated at the MDBs. Nowhere is the potential for competing interests as high as between development and environment goals (Gutner, 2002, 2005). Donor states have repeatedly indicated that they want the MDBs to promote both economic development and environmental protection. This leads to the potential for significant trade-offs between these two goals across specific country portfolios. For example, a borrowing country might want to increase the capacity for generating energy, but doing so quickly could have negative environmental consequences. Donor states may wish to promote biodiversity conservation, but doing so might slow a borrowing country from expanding production of prized cash crops for export. Thus, MDB decision-makers must balance decisions allocating funds to different

⁷ The IADB and AfDB have articles of agreement that require borrowing countries to maintain a majority of the capital stock and voting power at the Board of Executive Directors. For information on the Inter-American Development Bank, see: <http://www.iadb.org/en/about-us/capital-stock-and-voting-power,1352.html> (Accessed June 2011). For information on the African Development Bank, see: <http://www.afdb.org/fileadmin/uploads/afdb/Documents/Boards-Documents/2011-vp-eng-may.pdf> (Accessed June 2011).

recipients and projects so that they reflect the diverse goals and broad mandate that they receive from their member states. Donor states might be willing to allow slippage in some areas of performance in order to achieve better outcomes in other areas.

In addition, donor states have expressed preferences for rapidly expanded financing in certain areas, rather than a process of slowly scaling up financing based on experimentation and selectivity. This corroborates critical literature on MDB practices, which emphasizes that the need to approve financing is more important than achieving certain outcomes (Caufield, 1996). For example, on the behest of donor states, the Asian Development Bank has increased its financing for clean energy projects by an order of magnitude since the early-2000s.⁸ When donors express preferences for such rapid expansions in financing and delegate the necessary resources, the approval culture is reinforced. Under these circumstances, when donor states do not have an interest in performance-based allocation practiced by selectivity, increased monitoring and evaluation will do little to address the problem of performance.

1.4 Performance-Based Allocation as a Coordination Problem

This dissertation examines how monitoring and evaluation might address the problem of performance in light of these possibilities. I argue that independent evaluation does not itself change MDB staff incentives or the approval culture. Instead, I argue that the MDBs practice performance-based allocation when the cost of approving new operations is contingent on the performance of past operations. I show that there are limited conditions when this occurs as related to environmental performance.

To demonstrate this argument, it is necessary to understand when and how donor states and other civil society groups are able and willing to act on poor

⁸ See the news release “New ADB Policy Targets Secure, Clean Energy for Asia,” available at: <http://www.adb.org/Media/Articles/2009/12917-asian-clean-energies-policies/> (Accessed May 2011).

environmental performance in MDB projects in ways that impose costs on MDB staff. In addition, it is necessary to understand when borrowing countries are likely to select new operations based on successful experiences with past operations. To bring these factors together, I frame MDB decisions about allocating financing to different projects as the process of coordinating borrower country demands with the lending supply preferences of donor states at the lowest possible cost for MDB staff.

Simple principal-agent models are insufficient to capture how performance information is used in MDB allocation decisions, given that donor states have multiple, oftentimes competing interests and borrowing countries must, at the very least, consent to projects. Borrowing countries must eventually repay the principal from MDB loans as well. This means that borrower states should be likely to accept only those projects that are either a high priority or that are expected to generate sufficient revenue for repayment. Because borrowers have the ability to be selective about the development loans that they accept, MDB decision-makers cannot normally pursue allocation decisions that are counter to demands made by a borrowing country.⁹

Under these conditions, MDB decision-makers are “caught in the middle” of a difficult coordination problem (Figure 1). As reviewed above, the most basic incentive for MDB staff is to solve this coordination problem at the lowest possible costs (Wapenhans, 1992). At the organizational level, replenishment of concessional funds and increases in general capital resources by donor states are based on the ability of the MDBs to effectively mobilize financing. Because the high-level management of the MDBs are interested in expanding the resources that they control, they place pressure on department heads to maximize lending. Indeed, most operational units measure their

⁹ A possible exception might be when they can link the allocation of highly demanded projects to projects that fulfill MDB organizational mandates, but are in lower demand.

overall performance in terms of the amount of financing that they are able to get approved within a particular fiscal year. Filtering down to the staff level, this means that the career progression of individual MDB staff is based on their ability to steer project and program investments through the approval process smoothly.

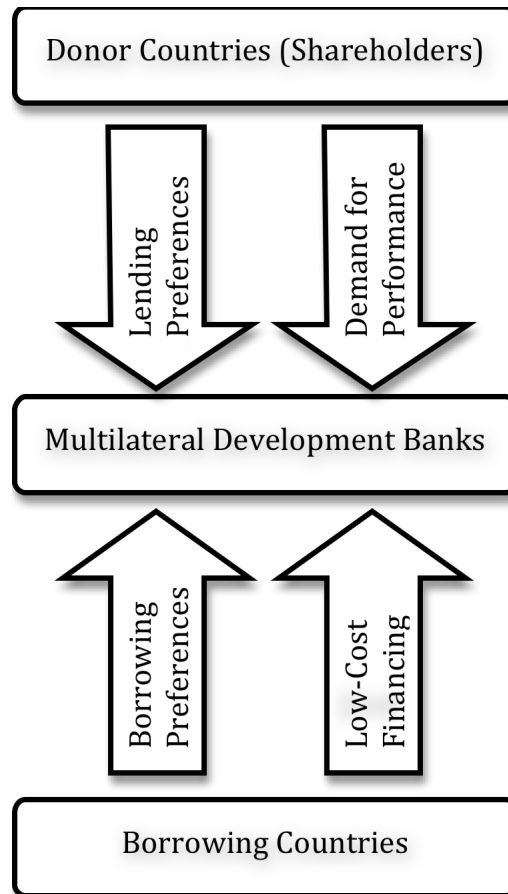


Figure 1: External demands on multilateral development bank decisions

Given this institutional arrangement, performance information might influence allocation decisions in a number of ways. First, performance information might influence the lending supply preference of donor states, which could hold the MDBs accountable for poor performance either through negative votes at the Board level for certain types of projects or through resistance to replenishments and capital increases. Second, performance information allows borrowing states to identify the types of

investments that produce the greatest development results, thus potentially affecting their borrowing demands. Third, information about past performance could be used by MDB staff to identify the types of projects in particular countries that are likely to require fewer of their administrative resources to approve and implement.

In the chapters that follow, I address each of these potential responses to information about past performance and test the conditions under which performance-based allocation can emerge with respect to environmentally-risky and environment-improving projects. Environmentally-risky projects are development projects that are likely to have significant and negative environmental impacts. Environment-improving projects are operations that attempt to improve environmental conditions. I show that when donor states are able to establish policies that make it costly for MDB staff to pursue projects in borrowing countries with poor environmental performance, there is a strong response to information about past performance. This argument confirms that principals can use administrative procedure and policies in lieu of active oversight (McCubbins, Noll, & Weingast, 1987; G. J. Miller, 2005). Adherence to administrative procedures is easier to monitor and can force staff to act in ways that promote successful environmental outcomes. Likewise, I show that high performing borrowing countries are likely to select successful projects in future periods.

1.5 Research Plan

The emphasis on accountability and performance-based programming has grown among many types of international development organizations during the previous two decades.¹⁰ However, very little evidence exists about when and why

¹⁰ In 2005, for example, more than 100 state representatives joined the Paris Declaration on Aid Effectiveness, which emphasized mutual accountability for performance between development donors and recipients, as well as an increased focus on measuring and responding to results.

international development organizations are able to put the “results agenda” into practice by adjusting their allocation decisions to reflect performance. Moreover, little evidence exists about when development organizations respond to evaluation in general (Brandon & Singh, 2009; Forss, Cracknell, & Samset, 1994). This dissertation seeks to remedy these shortcomings by examining when the MDBs respond to their measured environmental performance.

Research examining MDB allocation decisions have focused primarily on aggregate financing, rather than responses to performance in particular types of projects.¹¹ While the MDBs have formal performance-based allocation systems at the aggregate country level, MDB staff have considerable independence to make decisions about the *composition of the overall lending portfolios*, or the division of aggregate lending among different sectors and project types. Indeed, the MDBs have the flexibility to move in and out of different sectors because of their broad mandates. Thus, examining how past environmental performance in individual recipient countries influences the decisions about allocating financing to environmentally-risky and environment-improving projects is a unique way to understand when and why performance-based allocation can be accomplished through decisions about the composition of lending portfolios.

The 1990s, which is the time when this research picks up, was a period when environment-improving activities and environmental mitigation requirements were routinely built, at least formally, into most projects. By the mid-1990s, the MDBs had all adopted clear rules that require the completion of impact assessments, monitoring plans, and mitigation strategies for projects that are expected to have negative environmental

¹¹ For a general treatment of the subject, see: (for general treatments of the subject, see Gibson, Andersson, Ostrom, & Shivakumar, 2005; Martens, 2005; Martens, Mummert, Murrell, & Seabright, 2002; van Ufford, Kruijt, & Downing, 1988).

impacts. Projects that have high environmental risks are assigned to a high risk category (category “A” or “I”), which is part of the data assigned by bank decision-makers when they appraise projects for financing. Because environmental mitigation is supposed to be carried out across many different sectors, performance in implementing environmental safeguards is one of the most widely evaluated types of performance. This performance information makes it possible to test how external pressures from shareholder states and international civil society groups influence responses to performance with regard to environmental safeguards across a large number of projects.

From a methodological point of view, decision-making about allocating financing among environmentally-risky and environment-improving projects is a unique area to make progress on understanding how international organizations respond to information about past performance, for three reasons. First, data on decisions about how to allocate funds to different programs and projects in a portfolio, including environmentally-risky and environment-improving projects, are very detailed over many years. Second, evaluations about project outcomes, including environmental results, are available in across MDBs over many years. And third, the political factors that frame allocation decisions at development banks have been well-theorized, as will be reviewed in the next chapter.

To carry out this research, I assembled a team of research assistants who coded every publicly available project evaluation, country program evaluation, and complaint mechanism case from 1990-2008 for environmental performance in a double-blind fashion. I use this data, combined with project approval data for either environmentally-risky or environment-improving projects, to model whether particular MDBs are responsive to different types of information about environmental performance. I also visited the headquarters of each MDB considered here and conducted interviews about

decision-making processes, which I use to interpret and extend model results. The empirical analysis proceeds as follows.

In Chapter 2, I review the theoretical literature on the determinates of aid allocation and development lending, explain how allocation decisions are made at the MDBs, describe the evaluation processes that have been put in place, and chronicle how the environmental mandates of the MDBs have developed since the early-1990s. By doing so, I lay a common foundation for the empirical chapters that follow, since the outcome of interest throughout this research is decisions about how to allocate financing among project types.

The next two chapters explore how information about how past performance at mitigating environmental damage influenced decisions about allocating funds to environmentally-risky projects. In Chapter 3, I test whether safeguard policies that make it costly for MDB staff to seek approval for environmentally-risky projects affect their incentives to respond to evaluations of past performance. By doing so, I examine the ability of donor states to use administrative procedure in lieu of active oversight to incentivize certain IO activities. In Chapter 4, I investigate how the establishment of mechanisms to make the MDBs accountable to external observers, which have also made it possible for civil society groups to lodge complaints about poor performance in mitigating environmental damages, may have influenced lending decisions about environmentally-risky projects. In essence, these accountability mechanisms provide a formal way for civil society to reveal performance information to member states and to force MDB management to address performance concerns.

In the chapters that follow, I shift focus and consider environment-improving projects. In Chapter 5, I examine how information about the achievement of environmental targets, as revealed in project evaluations, influences decisions about

allocating funds to projects whose primary purposes are environmental in nature. In particular, I examine how differences in preferences for environment-improving projects that target local environmental issues (of greater concern to borrower states) versus global environmental issues (of greater concern to donor states) drive different responses to information about past performance. In Chapter 6, I continue to examine the allocation of funds to projects that emphasize local versus global environment-improving objectives, but I do so with respect to evaluations of country programs, which assessing performance across an entire country portfolio for several years. Because country program evaluations are part of decisions about multi-year lending strategies, they are likely to influence decisions about the allocation of projects following their completion.

In Chapter 7, I sum up the contributions that this research has made to the literature on the performance of the MDBs and explore new issues that have been raised by this research. At a time when donor states are planning to drastically scale up the financing of clean energy projects by channeling such funds through the MDBs, the findings here point to the need to ensure that the process of allocating funds to projects actually constrains the notorious “approval culture” at the MDBs.

2 Environmental Performance and Lending Decisions At Multilateral Development Banks

2.1 The New Environmental Project Types of the Early-1990s

The 1992 Rio Earth Summit set the tone for environmental and development assistance for years to come. At the Rio meetings, world leaders came together and formally decided that environmental concerns would guide a large portion of international development assistance. The Rio Declaration on Environment and Development, which was adopted by more than 150 heads of states, declared, “in order to achieve sustainable development, environmental protection shall constitute an integral part of the development process and cannot be considered in isolation from it.”¹ In his own speech to the Rio Earth Summit, World Bank President Lewis Preston seized on these intentions and proposed that donor states delegate an addition \$5 billion to the World Bank’s concessional lending organization (IDA) for environmental programs (P. Lewis, 1992). While this amount never fully materialized, these meetings marked a time when the world was united in its recognition of environmental issues. The MDBs responded to the possibility of being key players in the new sustainable development agenda.

With such intense attention directed towards environmental issues during this period, environmentally damaging projects at the MDBs came under significant scrutiny by donor states and civil society groups. *Safeguard policies* were put in place on the behest of these groups that required the MDBs to prevent environmental damages that resulted from infrastructure, forestry, and hydropower projects. These safeguard policies were established at the World Bank and Asian Development Bank in the run up

¹ The Rio Declaration on Environment and Development is available at: <http://www.un.org/documents/ga/conf151/aconf15126-1annex1.htm> (Accessed May 2011).

to the Rio meetings, and immediately following the Rio meeting at the Inter-American Development Bank as part of its 8th General Resource Increase (Board of Governors, 1994; Large, 2005). The safeguard policies required the multilateral development banks to assess formally the negative environmental impacts of development projects before approving projects, to prevent environmental damages from occurring during implementation, and to consult with local people about their environmental concerns.

Donor states, acting on strong domestic lobbying, insisted that safeguard policies at the MDBs exist on more than just paper. Offices and departments were created to oversee the implementation of the new safeguard policies. In 1987, the World Bank established the Environment Department, which was subsequently tasked with ensuring that environmental assessments were completed before a project could proceed to the approval process at the Board (Operations Evaluation Department [OED], 2001a). In 1990, the Asian Development Bank's Environment Unit was upgraded to the Environment Office. In 1995, it was upgraded again to the Environment Division, largely because it would need greater resources to oversee implementation of newly required safeguard policies (Environment Division, 1995). In 1994, the Sustainable Development Department was established at the Inter-American Development Bank in order to meet Rio commitments and was charged with aligning bank practices to emerging donor state priorities that had been expressed at the Rio Convention (Sustainable Development Department [SDD], 2002). This included establishing an inter-departmental Committee on Environment and Social Impacts to review individual projects for compliance with safeguard policies prior to Board approval. With administrative resources behind them, each of these departments sought to ensure that safeguard policies were followed by MDB staff.

At the same time, staff at the MDBs developed new types of projects that aimed to improve environmental conditions in borrowing countries, in line with commitments made by donor states at the Rio meetings. Due to international attention on environmental degradation, the amount of financing approved by the MDBs for forest conservation, biodiversity protection, ozone protection, and climate change prevention escalated rapidly across the MDBs around the time of the Rio meetings in 1992 (Hicks, et al., 2008, p. 189). Donor states looked to the MDBs as a way to coordinate the financing of international environmental efforts, even when civil society groups opposed MDB involvement (Shabecoff, 1990). When rich nations came together to discuss financing assistance for less-developed nations in line with Rio commitments, they decided to channel the initial \$2 billion through the Global Environment Facility, the United Nations Environment Program, and the World Bank (P. Lewis, 1994).

The new environmental offices described above expanded rapidly to accommodate the influx of resources for environmental programs. While these new departments did not change the MDBs into paragons of environmental responsibility (Gutner, 2005; Nielson & Tierney, 2003), they had a significant influence on MDB lending strategies. To this day, the organization-wide lending strategies at all of the MDBs prioritize environmental issues, at least formally. As a result, the MDBs have become the primary conduits of international environmental assistance in terms of the volume of flows (Hicks, et al., 2008, p. 28).

In this investigation, I consider allocation decisions about three types of projects that emerged during this period. The first type, *environmentally-risky projects*, are all development projects that require environmental assessments and management plans because they are likely to harm the environment. As I will describe further in Chapter 3, the environmental safeguard policies require that all projects be assigned to an

environmental risk category, each with distinct requirements for preparing projects. The assignment of projects to risk categories is typically the responsibility of the office or department charged with implementing the safeguard policies. Staff in the relevant “safeguard” units assign projects that they expect to have major environmental damages to the high risk category (“A” or “I,” depending on the bank involved), which then triggers requirements for designing full environmental impact assessments and environmental management plans before the project can advance to consideration for approval by the Board. Thus, the environmental safeguard policies created a new category of project with its own distinct requirements for planning and implementation, in contrast to projects less likely to have damaging impacts on the environment.

In addition to emphasizing the mitigation of environmental harms in all projects, the MDBs rapidly scaled up investments that addressed transboundary or global environmental issues, such as biodiversity loss, deforestation, ozone depletion, and climate change. These projects, which I call *global environment-improving projects* are expected to benefit both donor and borrowing states through the management of environmental resources that cross borders. The Rio Conference focused on these types of projects, given that all countries have a stake in protecting resources that produce transboundary benefits. With global environmental projects, donor states cannot secure the protection of important environmental resources unless they work directly with less-developed countries, which control significant portions of resources like biodiversity and tropical forests. Even in the case of global environmental goods, like greenhouse gases, for which developed countries are largely responsible to date, large developing economies like China, India, and Brazil now play an enormous role as well.

Finally, the environmental mandates of the MDBs recognized that conventional economic development produces significant environmental damage in many countries.

Much of this harm is confined within the territorial borders of individual nations, including borrowing countries. While both donor and borrower states have been interested in addressing environmental issues such as sanitation and sewerage, abatement of industrial pollution, management of solid waste, and soil conservation, the benefits of doing so primarily accrue to the borrowing country. I call these types of project *local environment-improving projects*. As I will argue in later chapters, donor state lending preferences will be different for global versus local environment-improving projects.

The research in the following chapters will focus on decisions about allocating funds to these three types of projects – environmentally risky, global environment-improving, and local environment-improving projects. While these projects have unique characteristics and create unique incentives for lending and borrowing, the decisions about funding them all go through a similar design and approval process at the MDBs, just like all projects. It is essential, therefore, to build on what is already known about the factors that influence decisions about allocating funds to projects for development. It is also necessary to take stock of what is already known about when and why the MDBs respond to information about past performance when making their decisions about funding.

2.2 Theories on Aid and Development Assistance Allocation

Research about international aid and decisions about allocating loans is not new. When scholars recognized that foreign assistance had become a lasting part of statecraft and foreign policy, research emerged that attempted to define its role in international politics. For example, Shelling (1955, p. 606) recounts how American foreign assistance became “a main – sometimes the main – vehicle of American diplomacy and military cooperation” following World War II. Never before had the world seen financial

transfers between countries such as those that occurred with the Marshall Plan. This raised questions about the motivations of donors and how successful aid could be at achieving foreign policy goals. These questions formed the basis of a significant, and still growing, research program on the political, economic, and cultural factors that account for global flows of aid.

In general, researchers have carried out this research program by examining whether broad and contextual factors, such as military alliances or trade relations between donor and recipient states, explain flows of aid. Until recently, most research focused on aggregate flows between donor-recipient dyads, rather than specific types of aid aimed at achieving particular outcomes, like the environmental projects introduced above. Very little research has examined how decisions about the allocation of aid are actually made. This has limited the ability of existing research to explain when and why aid donors respond to their performance.

2.2.1 Bilateral Donors and the Beginning of Aid Allocation Research

As with most research programs, initial analysis of how states allocate foreign aid sought to build conceptual foundations and outline reasons why states would use foreign assistance as an element of foreign policy. For example, Morgenthau described six types of aid: “humanitarian foreign aid, subsistence foreign aid, military foreign aid, bribery, prestige foreign aid, and foreign aid for economic development” (1962, p. 301). According to Morgenthau, each type of aid influenced recipient countries in unique ways, which explains why donor states choose among them. Interestingly, Morgenthau questioned whether aid for economic development could be an effective component of foreign policy, given that its benefits “are likely to appear only in the more distant future” (ibid., p. 308). This reflection raised questions about why states allocate aid for economic development.

Researchers developed empirical models to explain aid allocation in terms of relationships between donor and recipient countries. Dudley and Montmarquette (1976) developed a model of bilateral aid supply based on the benefit that donor countries derive from supplying aid and found that pre-existing political links with recipients are highly predictive of bilateral aid flows, rather than measures of need in recipient countries. McKinley and Little (1979) put forward two competing models of allocating aid – based on interests of donors or needs of recipients – and found that the geopolitical interests of the U.S. during the Cold War offered a much better explanation for U.S. aid allocation patterns than the economic characteristics of the recipient country. Thus, aid for economic development can be broader understood as a way for bilateral donors to cement ties with recipients, even when development outcomes are uncertain.

Findings based on these early articles examined a broader array of strategic reasons why bilateral donors would allocate aid including security arrangements, military cooperation, economic potential, cultural similarity, recipient need, proximity, and governance characteristics (Dowling & Hiemenz, 1985; Schraeder, Hook, & Taylor, 1998; Turnbull & Wall, 1994). This body of research widely agrees that bilateral donors allocate aid largely based on their foreign policy interests.

2.2.2 Multilateral Development Banks

Whereas bilateral aid is clearly a part of foreign policy, it is not immediately clear why donor states would transfer a portion of their available development assistance to MDBs. By delegating the allocation of resources for development assistance to multilateral organizations, individual donor states force themselves to coordinate their activities with other states and greatly complicate their ability to direct resources to the recipients and projects that most directly suit their national interests. Indeed, researchers have long asked why states would ever delegate authority and resources to international

organizations (Abbott & Snidal, 1998; Jupille & Snidal, 2005; Lyne, et al., 2006; Thompson, 2006). On the question of why nations delegate such important decisions to the MDBs, three primary answers have emerged.

First, it has been argued that MDBs, as specialists and collective actors, are better able than national governments to collect and process information about the types of programs and projects that are likely to be successful. As Milner recounts in her review of delegation, because “information about recipients is a collective good, it will tend to be underprovided by individual donors. Multilateral agencies are supposedly better at providing information, especially that necessary to monitor the recipient” (2006, p. 109). If multiple national governments all try to gather information, study recipients and projects, and monitor outcomes, there is enormous risk of wasteful duplication of effort. Preventing such waste may be worth forfeiting some control when national governments delegate resources and decision-making to multilateral organizations. As a result, the MDBs now have more staff than most bilateral aid agencies and they tend to work in more sectors and have more projects, perpetuating the gains in efficiency from joint effort as opposed to multiple efforts by single nations. At this stage, the MDBs’ massive scale of operations gives them greater ability than bilateral aid agencies have to generate information about the capacity and needs of the recipient countries where they work.

Second, officials in recipient countries might be more willing to reveal information about their development needs, given that their negotiations with multilateral organizations are not directly linked to military matters or trade, than would be the case with bilateral donors. Since multilateral organizations do not have direct political interests in particular recipient countries, they may even be more able than national governments to practice allocation based on conditionality, performance,

and outcomes. Indeed, there is some evidence that the public perceives multilateral organizations to make decisions for technical rather than political reasons, thereby increasing their expectation that projects will be effective (Milner, 2006). According to Milner, because voters in donor countries have no way to measure the outcomes of aid despite their preferences for effective aid, they prefer that it be allocated through mechanisms that are not influenced by strict political goals.

Third, the previous decade has seen a surge of attention to the ways that aid coordination can improve its effectiveness, in contrast to past experience with bilateral aid that was neither jointly planned nor particularly effective (Acharya, de Lima, & Moore, 2006). When donor states are interested in the same outcomes from development assistance, it can be in their interest to find mechanisms to lower the costs of coordination, and delegating resources to MDBs is one way to address coordination problems among themselves. Moreover, the MDBs have all increased the attention that they devote to coordinating among partners in recent years, recognizing that coordination gives them a comparative advantage (Eriksson, 2001).

Using this reasoning, recent research has advanced four primary hypotheses to explain how decision-makers at the MDBs allocate lending projects between sectors and countries. I will control for these factors in models that follow in the subsequent chapters.

First, some authors have suggested that MDBs are better than bilateral donors at tracking the macro-economic policies and performance of borrowers, and at selecting recipients who will be able to make better and more responsible use of aid. Because political factors do not force the MDBs to continue lending to particular countries, researchers find that the MDBs are more able to practice conditionality and react to indicators of performance on aid projects within specific borrowing countries. Indeed,

many of the development banks now produce broad indices of policy performance and use these indices within a formulaic framework to determine aggregate lending amounts to individual borrowing countries (Asian Development Bank [ADB], 2008a). However, empirical evidence for this hypothesis is mixed (Alesina & Dollar, 2000; Cline & Sargen, 1975; Dollar & Levin, 2005; Hicks, et al., 2008; Neumayer, 2003).

Second, results of earlier research suggest that the MDBs are more responsive to actual needs of borrowing countries than are bilateral donors. Maizels and Nissanke (1984) show that multilateral aid is more likely to go to low-income recipients than is bilateral aid, presumably because development banks do not have direct geopolitical concerns. Frey (1985) also reports that development banks appear to direct more aid to recipients with lower per capita income than do bilateral donors, although the low-income recipients with a better track record of repayment receive more aid than do the low-income recipients with a history of defaulting on loans. Dowling and Hiemenz (1985) also find that multilateral development aid tends to go to recipients with lower per capita income, and in addition that aid from MDBs is less likely than bilateral aid to go to relatively populous countries. However, research examining environmental aid allocated through the Global Environment Facility has found that high scores on indicators of democracy and substantial amounts of biodiversity in recipient countries are more important than the severity of local environmental problems in predicting flows of aid (T. L. Lewis, 2003). This finding suggests that lenders prefer democracies as recipients, but also that they are more likely to direct their environmental aid to nations that control a significant portion of global environmental resources, which responds to the preferences of donor countries.

Third, some research findings suggest that MDBs do in fact respond the way bilateral donors do to their own geopolitical concerns in choosing recipients for aid,

because the major shareholders and donors as principals try, often successfully, to treat the MDBs as their agents and to drive the lending priorities of the MDBs (Fleck & Kilby, 2006; Harrigan, Wang, & El-Said, 2006; Schraeder, et al., 1998). Top shareholders of the MDBs may direct lending in order to win trade concessions from recipient nations (Morrissey, 1993) or to maintain military alliances with recipients (Alesina & Dollar, 2000). Bilateral donor countries often use “tied aid” that requires the recipient country to contract their own firms in providing services. Previous research has also shown that bilateral donors decrease aid allocations to countries that have high levels of exports to the donor country (Lundsgaarde, Breunig, & Prakash, 2007). To the extent that top bank shareholders influence the allocation of development bank lending, we may see more loans and grants going to borrowers that have special relations with top shareholders, regardless of their economic need or qualities of democracy, macroeconomic policy, levels of poverty, environmental or other resources to rescue, or environmental damage to be arrested.

Finally, it has been suggested that the size of the recipient country, either in terms of population or GDP, explains some of the variation in aid allocation, probably due to the ability of large countries to accept and implement more projects (Dowling & Hiemenz, 1985; Neumayer, 2003). Lenders may see efficiency gains in the administration and implementation of multiple lending projects, as compared to the costs of implementing a smaller number of projects, and insofar as the goal is to approve loans (the “approval culture”) and move money, moving large amounts of money to large nations certainly works. The “large nations” may also receive more aid due to their geopolitical and global economic importance, making it valuable for lender countries, either singly or in MDB groupings, to curry favor with them because they already have major bargaining leverage in international economic and environmental negotiations.

2.2.3 *Towards Performance-Based Portfolio Composition*

In order to achieve successful development, donors must allocate financing to the particular countries and types of projects that are likely to be successful. While this may seem like a simple proposition, it has proven difficult for donors to guide their aid in this way. The problem for donors is that “the success of past aid to follow conditions and the failure of past aid to follow conditions are both taken as justification for future aid” (Easterly, 2003, p. 38). Since multilateral donor agencies in particular are relatively inclined to base allocation of funds on recipients’ needs, they have actually found it been difficult to withhold assistance at the aggregate level to borrowing countries with poor performance (Svensson, 2000, 2003). Thus, experts repeatedly highlight the importance of moving allocation towards successful projects and away from unsuccessful projects as a key ingredient in making assistance succeed.

Development scholars and practitioners recognize this practice of directing funds toward projects likely to succeed because projects like them have succeeded in the past as *performance-based allocation*. Interest in performance-based allocation grew out of experiences with procedural conditionality that was routinely built into MDB lending programs. Until the late-1990s, MDB projects often included numerous conditions that borrowing countries had to meet in order to trigger the disbursement of loans. In general, this type of conditionality has been found ineffective at changing the practices and policies of borrowing countries because the MDBs have ignored their own terms and given out funds anyway (Collier, Guillaumont, Guillaumont, & Gunning, 1997; Killick, 1997; Svensson, 2000, 2003). Donors do not always have incentives to impose strict conditionality, and even when they meet conditions very specific to implementation of the project, borrowing countries have little incentive to make *long-term and systemic* policy changes because these will disrupt current patterns of exchange

and hierarchy within existing political arrangements. Thus borrowers may systematically avoid making the changes that might actually improve their trajectory for development. The failure of conditionality has inspired much of the research on whether development assistance is capable of providing long-term solutions to entrenched problems in economic development (Burnside & Dollar, 2000, 2004; Easterly, 2003; Gibson, et al., 2005; Guillaumont & Chauvet, 2001; Hansen & Tarp, 2000).

The goal of performance-based allocation is to assess outcomes and adjust lending decisions accordingly (Gilbert, Powell, & Vines, 1999), as opposed to conditionality that requires certain procedures during implementation but is not directly concerned with outcomes. Under performance-based allocation, borrowing countries have flexibility in implementation, but are responsible for results, which could be held against them in later lending. Researchers have focused on the importance of accountability for results, mutually agreeable standards of performance, and allocation that directs financing to the places where it will most likely achieve successful outcomes, particularly for environmentally-targeted financing (Davis & Dadush, 2009; Ghosh & Woods, 2009; Werksman, 2009). Thus, attention within the development community has shifted towards allowing more flexible implementation arrangements, but increasing accountability of borrowers for results that will be used to guide future allocations.

In actual practice, donor organizations have mixed incentives to practice both performance-based allocation and conditionality (Rowat & Seabright, 2006). The problem for donors is that assistance is intended to address the causes of under-development, which often includes poor institutional capacity or performance in the borrowing country. Thus, if donors were only to approve financing for high-performing countries, they would be giving assistance to those who may not need it, and they would not be contributing to any development in the least developed countries. This

would prevent the MDBs from fulfilling their broader mandate to generate development. In particular, the MDBs often justify their lending activities, especially for the least-developed countries, by pointing out that private markets do not offer financing to such countries (Hostland, 2009). This problem has been dubbed the “Samaritan’s Dilemma” and is the source of significant debate within the development community about how donors should work in the poorest countries (see Easterly, 2003; Gibson, et al., 2005).

Since multilateral donors are often prone to make allocation decisions based in part on recipient need, it has often proved difficult to practice performance-based allocation for entire country portfolios (Svensson, 2000, 2003). International development organizations face the “budget-pressure problem,” which requires them to fully disburse all funds regardless of performance to maintain future budget levels (Svensson, 2003). On the other hand, if donors actually want to get the highest development return for scarce resources, they should have incentives to expand programs in high-performing countries since these are the ones that make best use of the aid they receive (Pietrobelli & Scarpa, 1992). MDB budgets and capital reserves are partly determined by whether their primary shareholder states can identify programs on offer from the MDBs that they perceive to be likely to achieve their interests (Fleck & Kilby, 2006). In turn, then, MDBs are under significant pressure to demonstrate the positive results of their past programs and to design and select future projects based on the demonstrable likelihood of good performance in the future. Unfortunately, little evidence exists about how the MDBs address these tensions in their allocation decisions.

In particular, the substantial majority of the research reviewed in the previous section deals with decisions about aggregate, country-level allocation at the MDBs, rather than what projects to fund within the available level of country financing. While

this research indicates that the MDBs are insulated from direct foreign policy concerns, it does not necessarily follow that the MDBs practice performance-based allocation in their decisions about how to assemble a portfolio of projects within a country. Indeed, by focusing on decisions about the total funds to be allocated to countries, rather than to individual projects within countries, research to date has overlooked ways that the MDBs might be able to practice performance-based allocation. The MDBs have flexibility in the delivery of loans and in using a number of different methods of financing and directing it to a variety of sectors within a particular country's portfolio.

Just because a country has better bureaucratic capacity and macroeconomic policies than others, for instance, does not necessarily imply that it will have more stringent or more effective environmental policies. While it might make sense to base aggregate, country-level allocation decisions on factors related to bureaucratic capacity or macroeconomic policies, these types of indicators provide little guidance about the most important choices facing MDB staff – the choice between a new expressway or an upgraded metro system; the choice between a new hospital or a sewage project; the choice between a solar power plant or a large hydropower project. The most important decisions facing MDB staff involve assembling portfolios of projects that are likely to be successful in particular borrowing countries.

The information needed to make performance-based decisions about the composition of a country's portfolio is fundamentally different from the information that is often used to determine the country's overall eligibility for lending. Surprisingly, existing research has not made this distinction, findings to date do not tell us how lenders choose among projects. There are certain conditions that are likely to render all development assistance ineffective, such as violent political instability or poor macroeconomic policy. These conditions aside, performance-based allocation at the level

of designing a portfolio of projects for a country remains a distinct possibility for almost all remaining countries. To understand whether the MDBs are positioned to be more effective due to their possible advantages in having information, being insulated from some political pressures, and coordinating with others, we must at decisions about how projects are chosen within an available amount of country financing.

I do so by looking beyond the standard metrics of performance that have been used in past research, like indices of a government's capacity, effectiveness, or macroeconomic performance. Instead, I collect project-level data on environmental performance and then use it to gauge whether the MDBs appear to adjust their decisions about environmentally-risky and environment-improving projects in response to past results in a particular country. By examining whether MDBs actually use past performance to improve their allocation of funds and the resulting outcomes from projects, we can determine whether the efforts now being devoted to evaluating projects are actually worthwhile or are simply making development assistance more expensive than ever.

The majority of studies that examine the use of evaluations are based on reports directly from decision-makers about what they learn from evaluations, but a recent review cast doubt on the validity of the research instruments being used to understand how evaluations affect decision outcomes (Leviton, 2003). The same problem is also visible in a recent study of performance-based budgeting by government ministries in the Netherlands (van der Knaap, 2007). This study simply lists whether measures of outcomes are include in budgeting documents, and then offers a narrative explication of the policy process, but it does not examine actual outcomes of decisions. The study does not really tell us whether decision-makers paid attention to past outcomes, nor does it

tell us whether the round of outcomes after decisions taken after the completion of evaluations actually improved at all.

Clearly, we can improve our understanding of whether evaluations of the past are really used in allocating funds to projects and whether this practice improves the outcomes of those projects by combining two methods of research: building a rich account of decision-making processes and collecting data that can verify decision outcomes over time and across individual projects. That opportunity now exists, thanks to the two decades of effort at the MDBs to monitor and to evaluate projects in terms of their environmental goals.

2.3 Evaluation and Monitoring at the Multilateral Development Banks

2.3.1 Purpose of Evaluation at the MDBs

Evaluation is meant to help donor organizations improve the design of their projects and allocate future funds so that their projects will be more effective. Love and colleagues (2004, Annex 9) report that the World Bank, Asian Development Bank, and African Development Bank spend 1.5%, 3%, and 1.6% respectively of their administrative budgets on independent evaluation. For the World Bank, this 1.5% translates into an evaluation budget of over \$20 million per year.² These resources would be wasted if the outcomes of evaluations did not help the MDBs to improve their performance. According to Robert McNamara, President of the World Bank from 1968-1981, this was the very reason why an evaluation function was established in the World Bank:

² Estimate given by the OED website, last updated in 2003 and available at: <http://lnweb90.worldbank.org/oed/oeddoelib.nsf/DocUNIDViewForJavaSearch/07b77ffd822c789285256d110057731c?OpenDocument&Click=> (Accessed May 2011).

“All large organizations, and all administrators, managers, and professionals, if they’re honest with themselves, will admit that they have successes and failures... We should learn from these experiences of success and failure. It was for that reason that I set up the Operations Evaluation function in the Bank... It’s very, very difficult for any of us who take pride in our activities to admit failure, and it’s very difficult, therefore, for us to examine the causes of it. That can best be done by an independent organization, and that was the structure we provided for Operations Evaluation in the World Bank” (2003, p. ix).

Evaluation at the other development banks was also set up to offer better feedback on performance. For example, a report prepared for discussion by member states to the Asian Development Bank highlighted the important role of evaluation in ensuring scarce resources are used wisely:

“Operations Evaluation Department undertakes evaluation activities to help the ADB management and decision-makers in developing member countries who are responsible for planning, designing, and implementing projects and programs to understand whether resources are well spent, and whether the planned outcomes are achieved. The principal goals of evaluation are to distill lesson learned for future operations... to ensure accountability for the use of resources for improving development effectiveness” (Asian Development Bank [ADB], 2003, p. 1).

Despite the stated importance of evaluation for improving decision-making, research on whether this goal has been accomplished is scarce. In the past, there simply were not enough publicly available evaluations to examine responses to evaluations systematically. Existing research is based on operational staff reporting the extent to which they used evaluations in their day to day tasks (Independent Evaluation Group [IEG], 2008a, Appendix C; A. R. Love, et al., 2004).

2.3.2 *A Brief History of Evaluation at the MDBs*

Like many other types of organizations, the World Bank and the regional development banks have all greatly increased their capacity to conduct evaluations in recent decades, with the intention of contributing usefully to future decisions about

awarding funds.³ Whereas evaluations in the early 1990s rarely extended beyond looking at the administrative and budgetary practices of MDB programs, since that time evaluation departments have expanded their activities to measure outcomes and impacts, as noted below.

World Bank. The evaluation function at the World Bank was created during McNamara's presidency (Grasso, et al., 2003, Annex C). Initially, the evaluation unit was staffed with five professionals, who were tasked with conducting evaluations of World Bank operations in Colombia and electricity sector investments. These pilot evaluations were considered successful by donor countries and by 1973 the evaluation office was elevated to the Operations Evaluation Department, with responsibilities for by broad evaluations and audits of individual projects following their completion. By 1974, the Operations Evaluation Department reported directly to the Board of Executive Directors, for the stated purpose of avoiding conflicts of interest with World Bank management.

The World Bank entered the 1990s with a need to improve performance, given both internal and external indications that the performance of Bank projects was poor, which generated strident external criticism (Picciotto, 2002). In 1992, member states discussed the now famous "Wapenhans Report," which chronicled deteriorating World Bank performance (Wapenhans, 1992). This event spawned a renewed interest in increasing the World Bank's capacity for evaluating its own programs, and in response, the World Bank increased both staff and resources for evaluation. At this stage, the World Bank evaluation office emphasized defining indicators of performance,

³ The academic discipline of program evaluation has grown substantially and has produced a vigorous and extensive literature on different ways to collect, analyze, and use evaluation data within organizations (for recent broad reviews, see e.g., McDavid & Hawthorn, 2006; Schwartz & Mayne, 2005). As a scholarly discipline, program evaluation has primarily been methods-driven and has focused on ways to produce valid and reliable evaluation information. Program evaluation is routinely applied in a variety of contexts, including conservation biology (Ferraro & Pattanayak, 2006; Stem, Margoluis, Salafsky, & Brown, 2005), international development projects (Woolcock, 2009), loan programs for pollution abatement (Akihisa, 2008).

measuring baseline data to which outcomes could be compared, monitoring results, and reporting findings in ways that both satisfied methodological concerns and scientific methods and also generated results useful for decision-making within the bank (Kusek & Rist, 2004).

Asian Development Bank. The ADB evaluation unit has changed its location within the organization and increased in importance with several formal upgrades in status over the last several decades. In 1978, the Post-Evaluation Office was established and tasked with evaluating the results of bank projects. To reflect a broadening mandate, the Post-Evaluation Office was renamed the Operations Evaluation Office in 1999. The ADB elevated its evaluation body to the departmental level, naming it the Operations Evaluation Department (OED) in 2001. This placed the head of the Department on equal organizational status with the heads of the operational departments. The ADB also established its own Development Effectiveness Committee during 2001, which became the formal mechanism through which OED reported to the Board of Executive Directors, thereby enhancing its accountability function (Asian Development Bank [ADB], 2003). Further reforms were carried out to make the OED more autonomous and independent in subsequent years, and as of 2004 the Department reports directly to the Board of Directors rather than the ADB President. Currently, the OED has a broad mandate to evaluate projects, policies, and Bank-wide strategies. The OED was renamed the Independent Evaluation Department in 2009.

Inter-American Development Bank. At the behest of the US, the Group of Controllers of the Review and Evaluation System was created in 1968. This group was in charge with conducting high-level audits of bank programs and reporting them to the member states through the Board of Executive Directors (Comptroller General, 1974). At the time, only six technical staff were assigned to audit the whole of bank operations.

Over the next decade, the audit and evaluation function grew considerably. By the 1980s, evaluation was split between the Operations Evaluation Office and the Office of External Review and Evaluation. The former office reported directly to the IADB president and was responsible for “evaluating the economic and social impact of the Bank’s operations” (Inter-American Development Bank [IADB], 1985, p. 23). The later reported directly to member states through the Board of Executive Directors and assessed performance in “problem areas and sectors” (ibid., p. 12). Like the World Bank and Asian Development Bank, greater resources were directed to evaluation in the early 1990s, as reports of declining portfolio performance rippled across the different MDBs (Inter-American Development Bank [IADB], 1993). During 1999, the Office of Evaluation and Oversight (OVE) was elevated to a more independent status that reported direct to member states through the Board of Executive Directors.⁴ Since that time, its work plan has emphasize broad, strategic level evaluations that are aimed at address decisions made at the Board level.⁵

African Development Bank. Evaluation at the African Development Bank was established later than the other MDBs. In 1980, the Evaluation Division was created within the Department of Planning and Research. While this division began the work of evaluating completed operations, it was unable to control staffing and administrative resources, as it reported to bank management, rather than to the Board of Executive Directors from donor countries. As a result, donor states were unable to learn about or to raise concerns about the independence and objectivity of the Evaluation Division (General Accounting Office [GAO], 1986). Reflecting these concerns, the Evaluation Division was promoted to the Operations Evaluation Office. Member states altered the

⁴ Information about the recent history of the Office of Evaluation and Oversight is available at: <http://www.iadb.org/en/office-of-evaluation-and-oversight/about-ove,1556.html> (Accessed May 2011).

⁵ As of 2003, however, OVE has conducted post-project validations of every completion report produced by operational departments.

organizational hierarchy further so that the Evaluation Division reported directly to the President beginning in 1987 and then to the Board of Executive Directors (representatives of member states) in 1993. In 1995, the Board committed additional resources to evaluation and upgraded the unit to the Operations Evaluation Department (OPEV).⁶ Since that time, OPEV has been involved in evaluations and even higher-level consideration of themes, targets, and goals of development.

2.3.3 Main Types of Evaluation and Monitoring at Development Banks

I examine two primary types of evaluations and an institutionalized complaint mechanism in the following chapters. In reality, the MDBs conduct many different types of evaluations, including one-time evaluations of topics that are of momentary interest to the Board of Executive Directors representing member states. However, all of the banks consistently complete project evaluations and country program evaluations, but not all of the banks consistently perform one-time special evaluations on particular topics. Thus, these two types of evaluations offer the opportunity to compare how responses to performance information vary across different organizations and project types.

Project evaluations analyze the results of individual projects. They are completed one to three years after a project has closed and after the team who actually implemented the project has completed its own self-evaluation. In general, project evaluations review the original objectives of the projects, the degree to which those objectives were achieved, the performance of the bank and borrowing country in implementing the project, and the steps that should be taken in future operations to address any shortcomings in the project design or implementation. At the World Bank,

⁶ Information about the recent history of the Operations Evaluation Department is available at: <http://www.afdb.org/en/operations-evaluation/history/> (Accessed May 2011).

project evaluations have the stated purpose “to help develop improved directions, policies, and procedures through the dissemination of lessons drawn from experience.”⁷ At each of the development banks, with the exception of the Inter-American Development Bank, project evaluations are the bedrock product from which evaluations across more projects, bank units, or other collectivities can be built. Project evaluations are carried out by teams of evaluation staff, who do not have incentives to produce flattering evaluations of performance because they are separate from operational staff.

Country program evaluations analyze the results of multi-year lending programs in individual countries and are meant “to draw lessons from the Bank's past activities to guide future strategies.”⁸ These evaluations are also completed by the independent evaluation departments. Unlike project evaluations, country program evaluations examine the entirety of bank programs in a country during a defined period and assess whether those programs successfully achieved prioritized development goals. Country program evaluations often use the evaluations of individual projects to arrive at their conclusions. Usually completed immediately prior to the discussion and adoption of new, multi-year country lending strategies, they may have special influence over allocation decisions.

Inspection Panel investigations address complaints from civil society groups that the MDBs have violated their own operational policies, often in reference to environmental or social safeguard policies. The investigation of complaints is carried out by an independent panel of experts. The investigations are meant “to address the concerns of the people who may be affected by Bank projects and to ensure that the Bank adheres to its operational policies and procedures during design, preparation and

⁷ As stated in the preamble of every Project Performance Assessment Report (referred to here as “project evaluation”) of the World Bank.

⁸ As stated in the preamble of every Country Assistance Evaluation (referred to here as “country program evaluation”) of the World Bank.

implementation phases of projects, " after complaints are filed and the expert panel produces an initial finding that bank management has violated an operational policy and not dealt with the concerns of affected groups.⁹ Thus, inspection panel reviews increase the accountability of bank staff to external actors, by forcing independent performance monitoring to be considered by bank staff.

Each of the development banks conduct all three of these types of monitoring and evaluation, for all of the countries where they place projects, so these three types of evaluations will form the basis of empirical analyses in the following chapters. First, I examine how these evaluations fit into the process of allocating aid, since incentives for MDB staff to use information about past performance will depend not only on the competing interests among projects, but also on the extent to which the process forces them to confront findings about monitoring and evaluation.

2.4 The Allocation Decision Process at the MDBs

Since the purpose of this research is to understand when and why the MDBs are responsive to their environmental performance, it is first necessary to look inside what is often the "black box" of allocation decision-making (Bourguignon & Sundberg, 2007). To this point, the vast majority of aid allocation research has ignored how the structuring of decision-making might influence allocation outcomes. Instead, researchers drop contextual factors into a regression equation and out come estimates of aggregate allocation amounts! While the question of how different donors select among recipients at the aggregate level addresses important strategic questions, this type of analysis is particularly weak at understanding how aid portfolios can be managed to improve performance.

⁹ See "Policies and Procedures," available at: <http://go.worldbank.org/3LO8WV1V80> (Accessed May 2011)

Over the last decade, practitioners and researchers have recognized that one-size-fits-all approaches to development assistance are less effective than designing project portfolios that best suit the needs and capacities of particular recipient countries (World Bank, 2009a). Thus, the connection between allocation decisions and performance is most fruitfully addressed by examining *portfolio composition* decisions made by donor organizations – do donor organizations approve the projects that are likely to succeed within specific recipient countries? The decision-making process used to set overall assistance levels for a particular recipient country is distinct from the process that is used to make decisions about portfolio composition.

To make portfolio composition decisions in ways that promote effectiveness, donor organizations must assess which types of projects will succeed in a particular recipient country. Donor organizations might use information about past project performance, recipient demand, and recipient governance capacity. Indeed, most country assistance strategies at the MDBs assess all of these factors (Operations Evaluation Department [OED], 2005a).

Each of the MDBs considered as part of this research follow a similar, hierarchical decision process to ultimately determine the portfolio composition for individual borrowing countries (Figure 2). The first major component of this process is the adoption of organization-wide lending strategies. These lending strategies reflect the development priorities as determined by the Board of Executive Directors for a particular sector or region over the next decade. These broad lending strategies are adopted by the member states, but often reflect the interests of donor states, who shape these strategies through their control over concessional fund replenishment and capital increases at the MDBs.

Organization-wide strategies set the lending supply preferences for the bank as a whole. For example, in 2008 the Asian Development Bank adopted Strategy 2020, which laid out prioritized areas for development investment over the next decade (Asian Development Bank [ADB], 2008b). These areas included clean energy, infrastructure, and regional cooperation. Likewise, in 2002, the African Development Bank adopted a strategic plan that prioritized water supply, primary education, and basic health, while calling for more limited investments in other areas (African Development Bank [AFDB], 2002). Instead of developing a bank-wide lending strategy, the World Bank develops strategies for specific investment sectors. For example, in 2003, the World Bank approved a strategy for the water sector that prioritized reengagement with environmentally risky water projects with the potential for high development impacts (World Bank, 2003). In each of these cases, member states approved organization-wide strategies and expected allocation decisions by MDB staff to reflect those strategies.

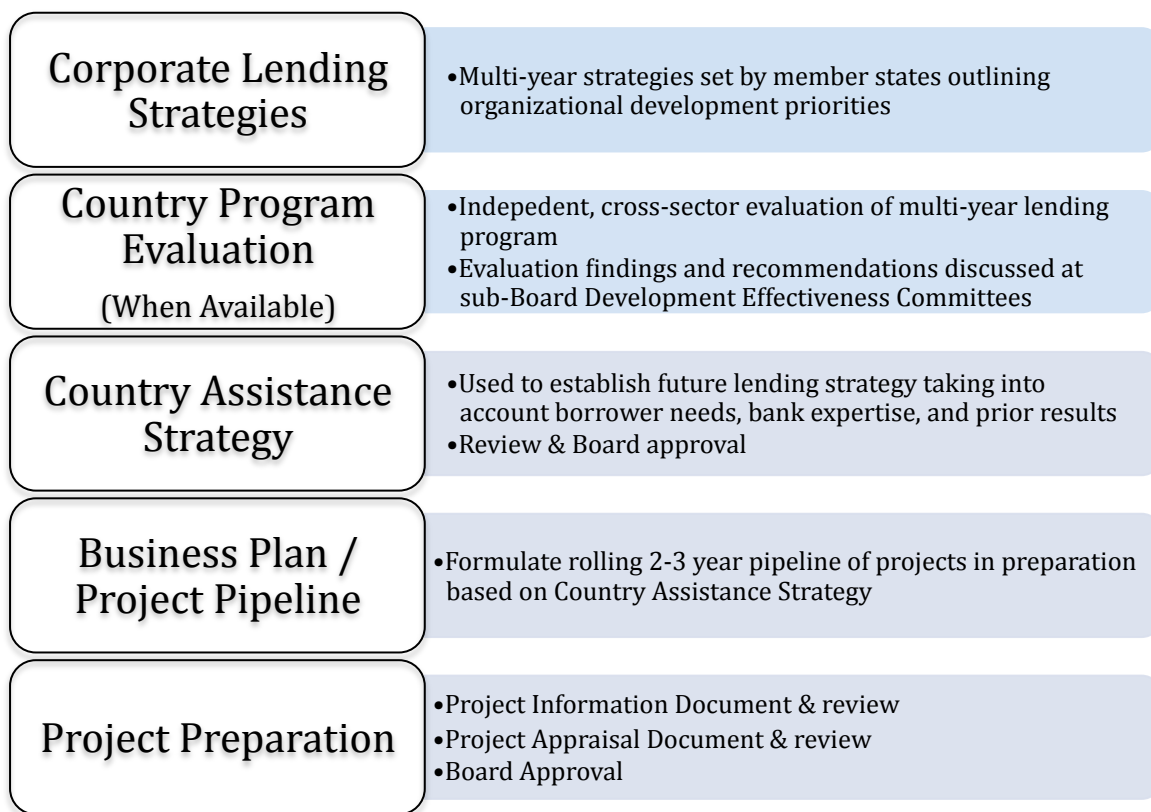


Figure 2: Allocation Decision Process at Multilateral Development Banks

At the annual meeting of the MDBs, when finance and treasury ministers come together to assess the overall lending performance of the MDBs, assessments of the MDB activities will often be based on the extent to which actual project approvals align with these lending strategies. For example, Naoto Kan, Japan’s Governor to the Asian Development Bank, highlighted a number of development challenges facing Asia in his speech to the 2010 Annual Meeting. However, in concluding he reemphasized the role that high level strategy play in guiding investment, “we strongly hope that the ADB keep playing a leading role in addressing such challenges as I have touch upon today,

under its long-term Strategy 2020.”¹⁰ Thus, at a general level, when designing lending portfolios in partnership with specific borrowing countries, MDB staff are incentivized to pursue projects that meet the objectives set by these organization-wide strategies. There is evidence that this occurs. For example, the Asian Development Bank has increased its clean energy lending by an order of magnitude during the past decade in response to a series of organizational strategies.¹¹ It may be the case that by requiring certain types of investments, these strategies incentivize the allocation of projects that are less likely to be effective.

Working within corporate lending strategies that are set by Board members, there are also specific processes in place to design country lending portfolios over several years, which I will call *country assistance strategies*.¹² Every three to five years, the team responsible for implementing projects in a particular country, which is usually a mix of in-country staff and headquarters staff with responsibility for a specific country, come together to formulate a new country lending plan, accounting for the demands of the borrowing country, the capacities of their particular bank, and the performance of previous projects. During this process, which is reviewed in much greater detail as part of Chapter 6, lending priorities for a specific country are determined. These lending priorities are intended to guide portfolio composition decisions that are made as part of managing an actual project pipeline through a business plan. The country assistance strategy must fit within organization-wide lending priorities, borrowing country demands, and is intended to be responsive to past performance. Unlike individual

¹⁰ A copy of the speech is available at: <http://www.adb.org/annualmeeting/2010/GOV/AM2010-JPN.pdf> (Accessed May 2011).

¹¹ See the news release “New ADB Policy Targets Secure, Clean Energy for Asia,” available at: <http://www.adb.org/Media/Articles/2009/12917-asian-clean-energies-policies/> (Accessed May 2011).

¹² I adopt this generic term for ease of use and consistency through the dissertation. In reality, each MDB has their own name for these strategies. The World Bank use country assistance strategy; the Asian Development Bank used country partnership strategy; the Inter-American Development Bank uses country strategy; and the African Development Bank uses country strategy paper.

project design decisions, donor states are significantly engaged in steering the country assistance strategy.

Prior to the formulation of a country assistance strategy, the evaluation departments at the various MDBs are sometimes available to produce a *country program evaluation*. This evaluation assesses the performance of the previous country strategy and lending program, for the purpose of helping the country team design and choose more effective projects in the next period. Unlike other types of evaluations, operational staff are required to account for the findings of country program evaluations during meeting with sub-Board committees that deal with the development effectiveness. These committees ensure that Board members are properly appraised of performance issues that come up in country program evaluations. During the meeting with this committee, operational staff must also specify the actions that they will take to address performance issues in future operations. Thus, the recommendations and findings of country program evaluations formally feed into the process of determining country assistance strategies, and thus the sectors and project types that will be emphasized during the following several years.

The country assistance strategy only outlines the sectors and project types that will be prioritized in the following several years. It is then the responsibility of the project team to negotiate with the particular borrowing country on the projects that will be part of the actual lending portfolio. During this process, the operational staff have a great deal of autonomy in generating a project pipeline, together with the borrowing country. The negotiation process to transform a country strategy into a project pipeline is informal and does not follow any prescribed process. There is no way for the Board to enforce strict compliance with the country assistance strategy. However, when the Board meets to discuss and approve a particular project, donor states will often question the

extent to which it addresses the major development concerns outlined in the country strategy. At some of the banks, such as the Asian Development Bank, adherence to the country assistance strategy is significant. At others, like the Inter-American Development Bank, the “improvisation rate” – the proportion of projects that deviate from the planned pipeline – is substantially higher (for example, Office of Evaluation and Oversight [OVE], 2009). Across all the MDBs, however, there is no formal way for Board members, evaluators, or civil society groups to influence how the country lending strategy is operationalized into a project pipeline. Thus, the process of deciding on specific projects comes down to the preferences of MDB staff and the borrowing country, as constrained by the broader planning process.

A number of different factors influence how MDB staff determine portfolio composition. Most importantly, MDB staff choose a project portfolio that defensibly corresponds to the country assistance strategy and that they will be able to design and approve quickly in order to meet new lending goals. Borrowing countries often have either general guidance on the projects that they would like to pursue, or in the case of middle-income countries, fully developed project proposals. These proposals usually serve as the basis of negotiations with the borrowing country, since borrowing country commitment to such projects is likely to speed their design, appraisal, and implementation. In addition, staff representing different technical sectors often vie for projects in their sectors, since incentives at both the individual and unit level revolve around securing new lending in their areas of specialization.

The country directors that I spoke with about the process of determining a project pipeline were very skeptical that evaluation information played a role in decisions. In general, they indicated that the country team did account for the types of projects that were likely to be problematic, either because of low borrower commitment

or because they entailed difficult design and implementation requirements. Thus, evaluation information at best has a direct role in formulating the country assistance strategy and an indirect role in revealing the types of projects that are likely to be problematic during pipeline discussions.

Once the project pipeline is determined, MDB staff go about the process of designing the actual projects. At this point, the portfolio composition of a particular borrowing country is basically set. While evaluation and monitoring information might help MDB staff to make better *design choices* within individual projects, the vast majority of projects that make it to the design stage are eventually approved by the Board. For example, of the 2930 operations for which an initial Project Information Document was prepared by the World Bank between 2000-2008, 2584 were eventually approved by the Board of Executive Directors.¹³ Thus, while decisions made at the project preparation stage are important for the effectiveness of individual projects, they are less pertinent to portfolio composition decisions that are at the core of this research.

The general process that MDB staff follow at the project preparation stage is to prepare an initial project information document and submit it to inter-departmental comment, and then prepare a full project appraisal and submit it to inter-departmental comment. During this process, various design and administrative requirements must also be met, which include the completion of an environmental impact assessment for environmentally-risky operations, consultations with civil society groups, and the formulation of a loan agreement and implementation plan with the borrowing country. Evaluation staff often use inter-departmental comment periods to disseminate the

¹³ Information calculated using the World Bank project database, available at: <http://go.worldbank.org/YLPQAHBY40> (Accessed May 2011).

lessons from evaluations and ask operational staff to account for how design decisions respond to such lessons.

Since this research examines portfolio composition outcomes over time, decisions that occur when designing a country assistance strategy and determining the project pipeline are the most important. It is only at the former stage that evaluation information plays a direct and institutionalize role in decision-making. Once a country assistance strategy is set, evaluation information only has the ability to indicate to operational staff the projects that are likely to be difficult to design and implement.

2.5 Environmental Performance and Allocation Decisions

This decision process has important implications for the way that decisions about environmentally-risky and environment-improving operations might be responsive to past performance. These two project types of the most dynamic parts of MDB portfolios over the last two decades because of the rapid rise in donor state interest in environmental performance. As Weaver points out, however, donor state and civil society interest in these areas has created friction with core MDB incentives to approve new lending:

“An organization must appear responsive to environmental demands in order to survive. Hypocrisy arises when these demands clash and the organization is compelled to separate talk from action so as to reconcile conflicting societal norms or placate multiple political masters with heterogeneous preferences”
(2008, p. 4-5).

The friction between the approval culture and the need to integrate environmental considerations into lending activities manifests itself in specific ways as part of the process outlined above.

In particular, MDB staff must assess whether environmentally-risky projects are likely to face significant delays in design and approval. Project types that have high environmental impacts include hydropower, electricity generation, roads, and other

heavy infrastructure. The development banks have all adopted clear rules that require the completion of impact assessments, monitoring plans, and mitigation strategies for these types of projects, owing to donor state pressures (see Gutner, 2002; Khagram, 2004; Nielson & Tierney, 2003; B. M. Rich, 1985; Weaver, 2007). Because environmental riskiness is an issue that is dealt with at the organizational-level through operational policies, but is not a project sector that is prioritized as part of the country assistance strategy, MDB staff must indirectly account for performance information that indicates whether an environmentally-risky project will allow them to meet lending goals without delays. Such delays often occur when donor states and civil society groups hold the MDBs accountable for implementing safeguard policies.

Environment-improving operations, on the other hand, are formally considered to be a priority investment sector throughout different stages of the planning process. Responding to donor-driven, organization-level strategies, environmental projects and project components are often prioritized as part of the country assistance strategy process. When it comes to negotiating with a particular borrowing country about a project pipeline, this often puts MDB staff in the position of trying to push projects in order to meet the lending supply preferences set by donor states in country assistance strategies (see Fairman & Ross, 1996). Because donor states have demanded expanded environmental lending, the opportunity for performance information to influence the decisions about the allocation of projects relates primarily to borrowing country demand. Evaluations may assist borrowing country representatives to select more environment-improving projects when they are successful in the past.

Both of these possibility are grounded in the expectation that MDB staff are trying to coordinate donor state lending supply preferences with borrower state lending demands. There is nothing about the decision process outlined above that forces MDB

staff to make performance-based allocation decisions as related to portfolio composition. Thus, I look to the incentives that this process creates to respond to different types of environmental performance in the following chapters.

3 Mitigating Negative Environmental Impacts and the Path of Least Resistance to Project Approval

3.1 Introduction

In the 1980s, non-governmental environmental groups highlighted a series of projects financed by the multilateral development banks that resulted in serious environmental damages (Schwartzman, 1985). Bruce Rich (1994), in his seminal book *Mortgaging the Earth*, described several of these World Bank “disaster projects.” He recalls the Northwest Region Development Program in Brazil, which caused more than a half a million settlers to move into forested areas in the Amazon due to the construction of highways and feeder roads and produced some of the highest deforestation rates in the world (p. 26-28). In India, a series of four loans amounting to \$850 million was approved for the construction of the Singrauli Super Thermal Power Plant, which resulted in high levels of mercury pollution in heavily populated areas (p. 40-42). In Indonesia, the Indonesia Transmigration project, which sought to alleviate population pressures on the inner island through the resettlement of people to less populated islands, mobilized 2.3 million settlers and was responsible for between 40,000 to 50,000 km² of deforestation (p. 34-38).

What these and similar projects demonstrated was that MDB policies and administrative procedures dealing with the mitigation of environmental risks were weak or non-existent, leading to devastating environmental outcomes in many development projects. Large infrastructure projects infrequently had plans to address negative environmental risks, and when they did, they were not implemented with any regularity (Bowles & Kormos, 1999; Gutner, 2002; B. Rich, 1994; Wade, 1997). In many cases, environmental assessments were completed as afterthoughts, well after the

associated project was designed and disbursed (e.g., B. Rich, 1994, p. 44). This severely limited their ability to mitigate environmental damages that resulted from projects.

In 1989, a group of U.S. senators threatened to withhold World Bank replenishment funding unless policies were adopted that addressed the negative environmental impacts of its projects (Nielson & Tierney, 2003). That same year, the U.S. Congress passed the International Development and Finance Act with provisions (i.e. "Pelosi Amendment") that required all multilateral development banks to publicly release assessments of the potential environmental impacts of planned projects well prior to Board votes in order to receive U.S. support. Subsequent to these threats, the World Bank adopted new environmental safeguard policies, including an Operational Directive on Environmental Assessment (OD 4.00, Annex A) in October 1989, which required environmental assessments for all project likely to have negative environmental consequences (World Bank, 1991, 1993). At the Asian Development Bank, an environmental safeguard policy and a requirement for environmental assessments of all projects with likely negative impacts became part of the Operations Manual in 1988 (Asian Development Bank [ADB], 2002).

The environmental safeguard policies that were adopted by the development banks in the early-1990s imposed new and costly planning requirements on the large dam, road, and irrigation projects that had traditionally been the focus of MDB lending portfolios. Safeguard policies required that environmental impacts assessments be completed and available to both Board members and local affected groups 120 days prior to Board approval meetings. Internally, new safeguard units were created with the ability to delay project approval if social and environmental risks were not adequately accounted for in project design decisions. Increased resources were devoted to the supervision of environmental mitigation activities. Since that time, bank management at

the MDBs has faced intense scrutiny from donor state shareholders over the implementation of safeguard policies, which have oftentimes spilled over into replenishment and negotiations about capital increases. A decade after safeguard policies were put into place, reports from both the World Bank and Asian Development Bank indicate that safeguard policies have substantially encumbered speed with which projects are approved (Operations Evaluation Department [OED], 2006; World Bank, 2001).

The multilateral development banks have always had strong organizational incentives to meet lending and disbursement targets (Asian Development Bank [ADB], 1994, p. v; Operations Evaluation Department [OED], 2006; Wapenhans, 1992). With the adoption of safeguard policies, development banks faced increasing risks that the time required for project approval would be lengthened, that financing disbursement rates would decrease, and that a higher proportion of scarce organizational resources would have to be devoted to assessing and monitoring negative environmental impacts for environmentally-risky projects (Operations Evaluation Department [OED], 2006; World Bank, 2001). In essence, the safeguard policies have made all environmentally-risky project more costly to approve and administer. However the extent of that cost varies by the likely safeguard implementation performance of the borrowing country.

Given this possibility, I argue that the MDBs have strong incentives to use information on past safeguard performance when making decisions about environmentally-risky financing. By establishing safeguard policies within the MDBs, donor countries use administrative practices in lieu of active project-level oversight of safeguard implementation. As is the case with domestic bureaucracies, I argue that administrative practices imposed by state principals can shape IO behavior and induce performance-based allocation by altering incentives around the core organizational

functions (see McCubbins, et al., 1987). The establishment of safeguard policies at the MDBs has made it costly for decision-makers to ignore past safeguard performance information, because it indicates how difficult it will be to approve and administer a project in a particular borrowing country.

This argument runs counter to general skepticism about whether donor organizations are able to practice performance-based allocation. Responding to past performance information has been repeatedly highlighted as key to achieving favorable outcomes in development assistance. If financing decisions are not adjusted to reflect performance, aid recipients may not have incentives to implement costly donor implementation requirements, such as strict financial accounting or environmental safeguard practices (Collier, et al., 1997; Guillaumont & Chauvet, 2001). To demonstrate credibility when requiring costly practices from aid recipients, donors must either reduce aid allocations for poor performance or reward high performance with additional aid (Drezner, 2003; Easterly, 2003; Svensson, 2000). However, despite the recent emphasis on performance-based financing across the development community, there exists very little evidence about when and why development organizations take information about performance into account when making financing decisions.¹ Indeed, scholars have expressed doubt that performance-based allocation is even possible for development donors (Gibson, et al., 2005). Given the general uncertainty surrounding whether information gained by evaluation is actually utilized to improve decision-making, taken together with the goal of managing development financing for results, it is incumbent on the development community to clearly how evaluation can be coupled with administrative policy to produce performance-based allocation.

¹ Researchers have raised general concerns that evaluation information is underutilized by organizations in a variety of contexts (Brandon & Singh, 2009; Patton, 2008; Torres & Preskill, 2001).

In this chapter, I test whether MDB allocation decisions about environmentally-risky projects respond to the safeguard performance information collected through project evaluations. No previous research has attempted to both measure environmental performance over time at the project-level and systematically test whether development organizations update their allocation decisions in response to environmental performance information.

3.2 Safeguard Policies and MDB Staff Lending Incentives

3.2.1 Environmental Safeguard Policies

Through the 1970s and 1980s, the portfolios of the MDBs centered on the types of projects that carry significant environment risks: large dams, new roads, large scale irrigation, energy generation, and the extraction of natural resources. According to the AidData database (Findley, et al., 2009), the World Bank supported 114 hydropower projects that totaled to \$11.9 billion in financing between 1980-1994.² The World Bank's own project database identifies \$15.9 billion of environmentally-risky financing committed between 1990-1994. Between 1980-1994, the ADB approved 22 loans hydropower plants totaling almost \$1.5 billion (Asian Development Bank [ADB], 1999, Appendix 1). Hydropower projects have generated significant concerns about environmental and social impacts across the multilateral development banks (Khagram, 2004). According to Hicks and colleagues (2008 p. 198-199), the amount of ADB financing directed to "dirty" projects was 10 times the financing allocated to environmental projects from 1980-1991.

Responding to pressures to account for the environmental consequences of its projects, the World Bank first adopted a policy statement about environmental

² This search was performed using the AidData online database, purpose code Energy Generation and activity code Hydropower Plant.

mitigation measures in 1984 (Operations Manual Statement 2.36, cited in World Bank, 1993). This policy statement encouraged operational staff to consider the environmental consequences of development projects and incorporate appropriate mitigation measures. In order to make progress on implementing environmental management practices, an Environment Department was established in 1987, along with Environment Divisions in each of the four regions (ibid.). This organizational reform laid the groundwork for a formal safeguard policy, the Operational Directive of Environmental Assessment (OD 4.00, Annex A), to be established in 1989. In 1991, the Environmental Assessment Sourcebook was first released, and included detailed operational procedures for assessing the potential negative consequences of development projects. This policy set the baseline administrative practices for environmental mitigation. In particular, projects were categorized according to environmental risks and environmental assessments were carried out in line with the applicable risk category.

The Asian Development Bank adopted environmental safeguard policies on a very similar timeline. Prior to 1987, the ADB did not have any policies or guidelines in place to assess and mitigate the negative environmental impacts of its lending portfolio. In 1987, the Environmental Unit was established with the responsibility of developing guidelines on assessing the negative environmental impacts of ADB projects (Turnham, 1991). By 1988, the ADB Operations Manual, which sets guidelines that staff must follow when implementing projects, formally required environmental assessments for environmentally-risky projects (as cited in Asian Development Bank [ADB], 2002). Throughout the early-1990s, the ADB clarified and strengthened its safeguard procedures in order to address the negative environmental impacts of its operations. Relevant policies and procedures included the 1993 Environmental Assessment Guidelines, the 1995 Bank Policy on Forestry, and the establishment of an Inspection

Panel in 1995 to ensure that external grievances, including those related to the environment, would be addressed by the ADB.³ By 2002, the ADB adopted a unified Environment Policy that requires environmental planning and management as part of all projects that have the potential for negative environmental impacts.⁴ Taken together, these policies increased the time and resources required to approve and implement environmentally-risky lending across the ADB lending portfolio (Operations Evaluation Department [OED], 2006).

The African Development Bank first adopted an environmental safeguards policy in 1990 and developed Environmental Assessment Guidelines in 1992 (African Development Bank [AFDB], 2001). These procedures required several actions that are similar to the procedures required above: (1) operational departments assign environmental risk category to projects; (2) borrowing country government are responsible for developing environmental management plans for projects that are likely to produce negative environmental impacts; (3) the sustainable development unit must clear the environmental management plans; (4) environmental management plans are included in loan covenants; (5) borrowing countries are responsible for implementing the environmental management plan. While the African Development Bank environmental safeguard policy was similar on paper, as will be discussed below its implementation was much weaker than was the case for the World Bank or Asian Development Bank. From 2000-2009, a decade after safeguard policies were adopted,

³ The 1993 Environmental Assessment Guidelines are summarized by the Canadian International Development Agency, available at: [http://www.acdi-cida.gc.ca/INET/IMAGES.NSF/vLUIImages/ea%20summaries/\\$file/AsDB.pdf](http://www.acdi-cida.gc.ca/INET/IMAGES.NSF/vLUIImages/ea%20summaries/$file/AsDB.pdf) (Accessed May 2010). The 1995 Bank Policy of Forestry is available at: <http://www.adb.org/Documents/Policies/Forestry/forestry.pdf> (Accessed May 2010). The 1995 Inspection Policy is available at: http://www.adb.org/Documents/Policies/Inspection/inspection_policy.pdf (Accessed May 2010).

⁴ Environment Policy available at: <http://www.adb.org/documents/policies/environment/default.asp?p=policies> (Accessed December 2008).

less than half of projects were being assigned environmental risk categories, as required by the environment safeguard policy.⁵

3.2.2 *Lending Incentives Created by Safeguard Policies*

Previous scholarship has highlighted the mixed incentives that donors have to allocate projects based on the past performance of recipients. On the one hand, multilateral development bank budgets are partly determined by whether their primary shareholder states perceive programs to be effective and aligned with their international interests (Fleck & Kilby, 2006). As a consequence, the MDBs have been under pressure to demonstrate performance, including successful mitigation of environmental damages, in order to maintain and increase their lending resources during concessional fund replenishments and general capital increases (Park, 2005; Weaver, 2007). On the other hand, some scholars have suggested that development organizations face the “budget-pressure” problem, which requires them to fully disburse all funds regardless of performance to maintain or increase future budget amounts (Svensson, 2003). In addition, career progression for staff members often depends on smoothly steering large projects through the approval pipeline (Weaver, 2008). These incentives have create a strong internal “loan approval culture” that values the approval and disbursement of loans above most other outcomes (Wapenhans, 1992).

Particular to environmental performance, the MDBs face the challenge of balancing the sometimes competing goals of economic development, loan approvals and ensuring that environmental standards are maintained. Given that staff incentives are based on loan approvals and portfolio outcomes have traditionally been evaluated using

⁵ The calculation was made according to an environmental risk category database that was supplied to the author during a visit to the temporary African Development Bank headquarters in Tunis, Tunisia during June 2010.

economic metrics, absent administrative procedures that make safeguard issues a relevant part of the costs to approving and administering projects, operational staff have incentives to deemphasize the environmental consequences of projects (Gutner, 2005). However, during the design phase of the project cycle, environmental policies can significantly delay project preparation and approval timelines. Thus, the adoption of safeguard policies have significantly increased the incentives to respond to past performance, as past performance within a particular borrowing country is likely to be a signal of the delays that will be faced during the preparation of projects, and potentially with the disbursements of funds. These incentives are laid out very clearly in a recent evaluation of the ADB safeguards policy (Operations Evaluation Department [OED], 2006, p. 57):

“There is recurring evidence of lending decisions being actively directed to avoid projects that might trigger environmental procedures... The decision to avoid environmentally sensitive projects is a rational response of ADB staff, given the existing incentive structure. Often this approach is preferred by the governments, as it fits their desire to expedite project processing and minimize project delays and the associated payment of interest and commitment charges. ADB staff have incentives to gain recognition for project approval, as this impacts on career progression. Environmental safeguard procedures can frustrate this, especially where there is a clash between ADB and national procedures. From the perspective of individual ADB staff and [Executing Agencies], it makes good sense to avoid or circumvent the environmental safeguard procedures.”

Similarly, a 2001 study of World Bank safeguard policies found that proper safeguard implementation, together with fiduciary policies, increased administrative costs for the Bank by an average of 20% in each project (World Bank, 2001). An evaluation brief completed by the then Operations Evaluation Department found that, “there is anecdotal evidence that some managers are discouraging their staff from tackling operational involving safeguard policies” (Operations Evaluation Department [OED], 2001b). The same evaluation brief reports that 55% of staff with experience in forestry projects reported that environmental safeguard policies were a key reason for declining investment in the forestry sector.

When considering environmentally-risky lending in countries with a record of good environmental performance, MDB staff have greater certainty that project preparation, including environmental assessments, will be completed in a timely manner, allowing staff to meet lending targets. Since completion of environmental assessments is the responsibility of the borrower in many instances, avoiding low-performing borrowers is one of the only ways that staff can control preparation costs and delays associated with environmental risks. A recent ADB evaluation found that mitigating the negative environmental impacts of development projects depends critically on the capacity and willingness of the borrowing country to follow through with environmental management and mitigation measures (Operations Evaluation Department [OED], 2006). In addition, the speed of loan disbursement is likely to be faster in countries that have a history of good environmental performance and the cost of supervision is likely to be lower. It may also be the case that environmentally-risky projects in high-performing countries will produce less negative attention by external stakeholders, which can also cause significant implementation delays or even project cancellations in some instances (Khagram, 2004; B. Rich, 1990).

In addition to the ways that safeguard policies incentivize staff to avoid environmentally risky projects in borrowing countries that have records of poor safeguard performance, there is evidence that borrowing countries themselves have sought other sources of financing for development projects when they experience significant approval and disbursement delays due to safeguard policies. For example, the 2007 Country Assistance Program evaluation for India reported (Operations Evaluation Department [OED], 2007b, p. 35):

“Concerns of the [Government of India and Executing Agencies] regarding the scope and detail of safeguard requirements are becoming a factor in their perceptions of ADB assistance. Safeguard-related issues are seen to cause substantial implementation delays, particularly in the transport sector... The

transport sector assistance program evaluation observed that [Government of India] and ADB officials try to avoid projects with major environment/resettlement/land issues and focus, for example, on rehabilitation projects, which can be categorized as category “B” [lower-risk] projects, rather than on new roads.”

Given that environmental safeguard policies have created strong incentives to avoid environmentally-risky projects, especially in borrowing countries that have not shown the capacity to properly implement environmental management plans, I posit the following hypotheses:

H1: Development banks will approve more and larger environmentally-risky projects in borrowing countries that have better safeguard implementation performance in past projects, when strong safeguard policies are in place.

Implication 1a: An MDB is more likely to approve an environmentally-risky project during a given year for an eligible borrower that has a record of good safeguard performance than for a borrower that has a record of poor safeguard performance, when strong safeguard policies are in place.

Implication 1b: Given that an MDB approves an environmentally-risky project during a particular year, the approved project value will be higher for a borrower that has a record of good safeguard performance than for a borrower that has a record of poor safeguard performance, when strong safeguard policies are in place.

3.3 Data & Model Specification

3.3.1 *Outcome Variable: Approval and Allocation of Environmentally-Risky Projects*

Two observable features of the process of approving projects are potentially important when modeling development bank allocation decisions. First, the decision to approve an environmentally-risky project during a given year provides information about how the MDBs screen projects for inclusion in a country lending portfolio. Second, the amount of money approved for projects contains information about the relative priorities of the development organizations when compared to their total budget constraint. Larger projects are likely to be more valuable to borrowers.

To examine specific types of projects as they are relevant to MDB environmental safeguard policies, I have compiled the environmental risk rating that was assigned to every project approved by the World Bank and Asian Development Bank from 1990 - 2008 from project approval documents and available project databases. I obtained risk categorization data directly from the African Development Bank for the period 2000-2009. Generally, the MDBs categorize projects according to whether they are expected to have a high, moderate, or no impact on the environment. For the analysis presented below, I consider environmentally-risky projects to be all projects that have been flagged for high expected impacts and that are not primarily intended to improve environmental management according to the project description (World Bank and ADB category “A”, African Development Bank category “I”).⁶ These projects require full environmental impact assessments and management plans according to the MDB safeguard policies. I

⁶ Environmentally-risky projects that have an AidData purpose code within “General Environmental Protection” are excluded, given that environmental projects with physical components often require environmental assessment, even though the goal is to maximize positive environmental outcomes.

consider all projects with no identified environmental risks to be no-risk projects (World Bank and ADB category “C”, African Development Bank category “III”).

3.3.2 *Primary Predictor Variable: Safeguard Performance*

Reflecting the seriousness ascribed to safeguard performance, all of the MDB evaluation departments have evaluated performance at implementing environmental safeguards in the course of both project and higher-level thematic evaluations.⁷ For this chapter, I focus on how the World Bank, Asian Development Bank, and African Development Bank have responded to safeguard implementation performance as reported in project evaluations that have been made publicly available since 1990.⁸ Project evaluation are completed for approximately 25% of completed projects and are the most basic building block for higher-level evaluations at all of the MDBs considered in this chapter. Given that I am interested in how the information available to decision-makers influences allocation decisions, determining selection into evaluation is not a significant concern. In many of the project evaluations considered as part of this chapter,

⁷ While this chapter does not deal with how aggregated evaluations impact lending decisions, it is worth noting that the evaluation departments have spent considerable effort to evaluate the safeguard performance of their respective bank and borrowing countries. Like project evaluations, these thematic evaluations have highlighted mixed safeguard implementation performance. Building upon project-level findings, the ADB evaluation office completed a 1998 Special Evaluation Study on Environmental Mitigation Measures in Selected ADB-Financed Projects, which found variable success and recommended that increased attention be paid to borrowing country management capacity and the performance of borrowing countries and contractors carrying out safeguard measures during project implementation. A follow-on study examined the implementation of ADB safeguard policies in selected hydropower projects (ADB, 1999). This evaluation recommended increasing implementation performance of safeguards in complex, environmentally-risky projects. Accumulating lessons on safeguard implementation, the OED conducted a broad review of the ADB safeguard policy in 2006 and recommended focusing less on procedural compliance and more on achieving environmentally favorable outcomes (Operations Evaluation Department [OED], 2006). This is all to say that OED has been closely involved with evaluating the environmental outcomes of ADB projects and environmental performance of the organization across the study period considered here. Given the bank-wide emphasis placed on environmental safeguard policies and the immediate involvement that evaluation has played in monitoring the implementation of environmental policies over time, the ADB offers an excellent opportunity to examine how environmental performance information impacts financing decisions about environmentally-risky projects. The World Bank Independent Evaluation Group also completed a broad study of safeguard policies as part of updating in safeguard policies in recent years (Independent Evaluation Group [IEG], 2010b).

⁸ The evaluation department at the Inter-American Development Bank does not conduct project evaluations.

a dedicated section in a project evaluation documents whether the implementation of the project adhered to environmental safeguard policies.

To compile this safeguard performance information in a systematic way, I assembled a team of research assistants to code safeguard implementation performance using a 4-point scale (Table 1). Coders were instructed to use language from project evaluations that indicated whether implementation of environmental safeguard measures met safeguard performance standards. All project evaluations were double-blind coded and I determined the final safeguard performance coding when there were discrepancies between the coders.⁹ By coding safeguard implementation performance in terms of the adherence to defined standards and implementation expectation, I produce a comparable measure across a large number of cases. While international environmental politics scholars have long discussed the advantages and disadvantages of using different conceptualizations of performance in empirical research (Gerlak, 2004; Keohane, Haas, & Levy, 1993; Young & Levy, 1999), in the case of performance implementing environmental safeguards, it is not possible to create comparable outcome variables (e.g., problem solving efficacy, environmental impact) given the wide range of potential outcomes across different project types.

⁹ The following are the inter-coder reliability rates for safeguard implementation performance within 1-point on the ordinal coding scale before adjudication by lead author: World Bank 76.3%; Asian Development Bank 74.2%; African Development Bank 78.2%.

Table 1: Coding criteria for safeguard implementation performance

Coding	Meaning	Criteria
4	Highly Satisfactory	Exceeds safeguard requirements or conditions; specifically mentioned for outstanding safeguard performance; Efforts significantly improve environmental outcomes as compared to pre-approval expectations;
3	Satisfactory	Meets all safeguard requirements or conditions with only minor exceptions observed; summary statement of performance is positive;
2	Partly Satisfactory	Meets some safeguard requirements or conditions with significant deficiencies observed; Does not meet monitoring or evaluation standards in projects with no discernable environmental impacts; summary statement of performance is negative;
1	Unsatisfactory	Does not meet most environmental goals or conditions with major deficiencies observed in most areas; Outright non-compliance with environmental loan conditions and/or non-achievement of safeguard requirements;
NA	Not Available	Project has no safeguard requirements OR insufficient information is available in evaluation report to assess recipient performance;

As might be expected, the data that we collected reveal mixed performance in implementing environmental safeguard policies, with approximately half of relevant project evaluations revealing major safeguard implementation problems or outright non-compliance with safeguard procedures (Figure 3). This means that all of the MDBs considered here have the ability to respond to both poor and good performance in systematic ways. In addition to collecting outcome data displayed in Figure 1, we also collected data on whether poor project design caused problems in implementation, thereby relieving the borrower of some responsibility.

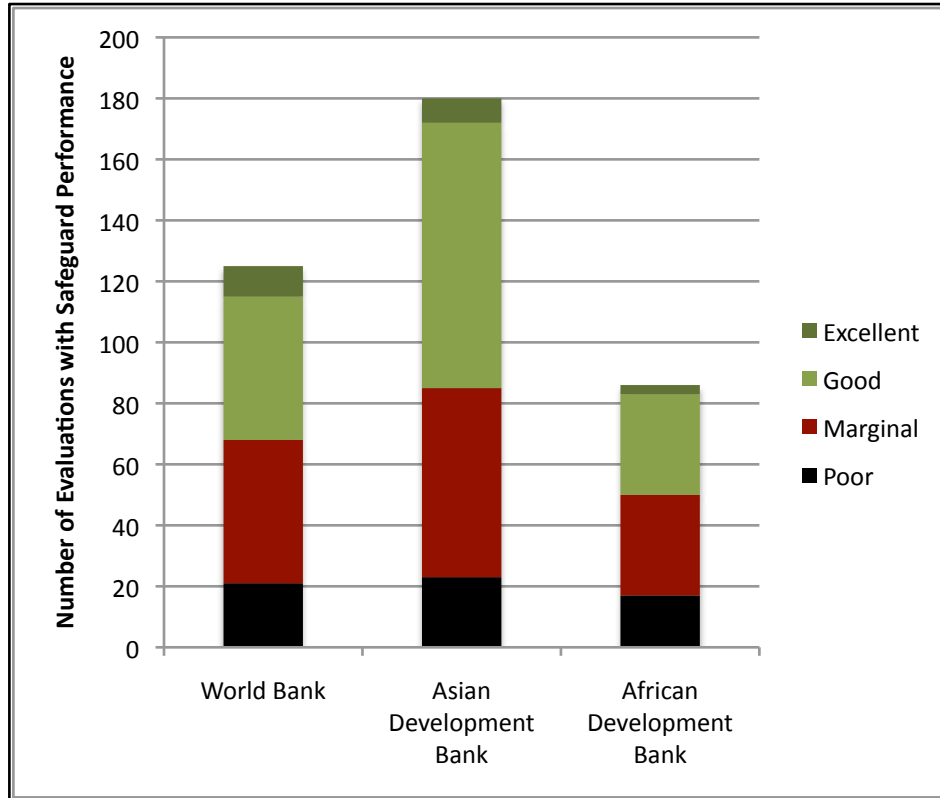


Figure 3: Evaluations with safeguard implementation performance information

For modeling purposes, I create three predictor variables from the data displayed in Figure 1. All project evaluations that had good or excellent safeguard outcomes were included in the variable NO. GOOD SAFEGUARD OUTCOMES, which is the count of good outcomes in a particular country during the past five years. Similarly, the variable NO. POOR SAFEGUARD OUTCOMES refers to the number of projects with poor safeguard outcomes during the past five years. To account for design problems, I also create the variable NO. POOR SAFEGUARD IMPLEMENTATION, which excludes projects with design problems from the larger pool of evaluations documenting poor safeguard outcomes.

3.3.3 Control Variables

I use several control variables in order to account for other determinants of MDB lending decisions (as reviewed in Chapter 2). First, it has been suggested that MDBs allocated more financing to borrowing countries that have good governance and satisfactory overall project implementation performance in the past. In fact, recent reforms at the MDBs have made these factors explicit determinants of overall country-level concessional lending.¹⁰ Thus, I calculate OVERALL REPUTATION based on the ratings for project outcomes in evaluations for each country over the past five years and use the World Bank Institute's rating of governmental effectiveness (GOVT.EFFECTIVE) to control for the governance and performance of each borrowing country.¹¹

During my interviews with MDB staff, it was suggested that the expected level of civil society opposition to environmentally-risky projects was a key determinant of whether such projects would be approved. Indeed, civil society opposition has been a primary reason why environmentally-risky projects are either delayed or canceled (Fox & Brown, 1998; Khagram, 2004). Thus, I include the Freedom House index of civil liberties (LESS CIVIL LIBERTIES) to control for the likely effect of civil society mobilization around risky projects.¹²

¹⁰ For more information on the performance-based allocation systems at the MDBs considered here, see for World Bank: "How IDA Resources are Allocated," available at: <http://go.worldbank.org/F5531ZQHT0> (Accessed April 2011). For Asian Development Bank see: "Fact Sheet on ADB's Performance-Based Allocation Policy," available at: <http://www.adb.org/ADF/PBA/fact-sheet.asp> (Accessed April 2011). For African Development Bank, see: "Country Resource Allocation," available at: <http://www.afdb.org/en/about-us/african-development-fund-adf/country-resource-allocation/> (Accessed April 2011).

¹¹ Consult Appendix 1 for Bayesian updating model used to produce this indicator.

¹² In some cases, GOVT.EFFECTIVE and LESS CIVIL LIBERTIES were only available biannually or for limited portions of the panel within a particular country. Since all of the control variables have most of their variation in the cross-section between countries, rather than over time within countries, I included the linear interpolation for all points between available control observations and extrapolated the exact endpoint value up to three years beyond the available variable dates where applicable. These decisions are based on the judgment that casewise deletion based on the non-availability of slow-changing variables would introduce more problems for inference than interpolation/extrapolation, where applicable.

I also expect that the MDBs allocate projects according to the stage of development for each borrowing country. Thus, instead of controlling for factors that are likely to predict overall lending levels, I take the step of more directly controlling for actual portfolio characteristics of each borrowing country. First, I use the percentage of total lending that is concessional in each country-year (CONCESSIONAL) as a control variable, because risky projects tend to be large infrastructure projects that are funded through market-rate lending. This type of lending tends to be available to countries that are middle-income and have low levels of external debt. Second, borrowing countries that receive more total projects are also more likely to receive at least one project that is flagged as environmentally-risky, thus the variable NO. PROJECTS controls for the overall size of the country portfolio in the approval models. In the allocation stage models, PORTFOLIO SIZE controls for the overall lending amount allocated within a particular country-year, again to account for the association between portfolio size and project size in all borrowers. This variable also controls for potential fluctuations in total MDB lending amounts and currency inflation.

3.3.4 *Model Specification*

Many studies on aid allocation have employed two-stage models to account for approval and allocation decisions separately (Cingranelli & Pasquarello, 1985; Hicks, et al., 2008; Neumayer, 2003). In the first stage, the decision to allocate aid in a particular category of interest is taken to be a binary variable. I refer to this as the “approval” stage and it models whether donors screen projects based on certain variables of theoretical interest. In the second stage, the amount of financing committed *given* that a project is approved during a particular time period is modeled. The “allocation” stage thereby tests whether variables of interest increase or decrease the amount of lending of a particular type. I follow a similar procedure.

Approval Model. For the approval stage of the model, each country-year is coded as a binary variable to indicate whether the ADB approved at least one environmentally-risky project during that year. This type of data structure is often modeled using the familiar probit link. I adopt a more conservative modeling approach than many researchers in the aid allocation literature by accounting for temporal dependence among observations and country-effects within the probit model. Since ADB operational departments are often organized by country, it may be the case that there are regular spacing intervals between projects or that the country program loses the staff expertise to approve and manage certain types of projects over time. Thus, I follow Beck, Katz, and Tucker (1998) and include dummy variables (TIME DUMMIES) for each time interval since the last project approval. This is equivalent to estimating a non-parametric event history model where the hazard function is not based on researcher distributional assumptions (Box-Steffensmeier & Jones, 2004). It is also possible that there are consistent country-effects that are not modeled with the included variables. Since a fixed-effects model is not identified because some of the countries do not have variation in the dependent variable (no projects are approved during the sample period), I employ a random-intercept model estimated by Laplace approximation to account for unobserved differences between countries (Gelman & Hill, 2007, Ch. 14). The random-intercept probit that I employ has the following form:

$$\Pr(Y=1 | X, \alpha) = \phi(\alpha_i + x_{it}\beta + T_{it})$$

$$\alpha \sim N(0, \sigma^2)$$

where Y is the binary dependent variable, X is the matrix of covariates, α is the random intercept, T is the time dummy that is turned on for country i at time t , and σ^2 is the variance of the random intercept.

Allocation Model. For the allocation stage of the model, the dependent variable is the amount of financing that was flagged as environmentally-risky, given that at least one such project was received during the country-year. Following a similar modeling strategy as above, I employ a random-intercept linear model fitted by Laplace approximation to account for any randomly distributed unobserved differences between countries that are not explained by the fixed coefficients (Gelman & Hill, 2007, Ch. 13).

$$y_{it} = \alpha_i + x_{it}\beta + e_{it}$$

$$\alpha \sim N(0, \sigma^2)$$

where y is the amount of environmentally-risky financing approved, X is the matrix of covariates, α is the random intercept, e is the error term, and σ^2 is the variance of the random intercept.

3.4 Model Results

3.4.1 Approval Decisions

The results of the random-intercept probit regression for the approval stage provides significant support for the hypothesis that the World Bank and ADB respond to past safeguard implementation performance, controlling for other potentially important variables. In three of four models, borrowing countries that achieved satisfactory safeguard performance in past projects were more likely to receive environmentally-risky projects in future time periods (Table 2, Models 1a, 2a-b). For the World Bank, I also find that the number of evaluations reporting that environmental damages were not mitigated during the implementation of projects is a strong predictor that the country will receive fewer environmentally-risky projects in future periods (Model 1a). For the Asian Development Bank, I find that the number of evaluation reporting that safeguard policies were not implemented, excluding instances where

safeguard measures where not designed properly, is a strong predictor that the country will receive fewer environmentally-risky projects in future periods (Model 2b). These results support Implication 1a, which states that project approval decisions for environmentally-risky projects will respond to the safeguard performance record of borrowing countries.¹³

¹³ As a robustness check, I examine the influence of environmental reputation and the other control variables on the value of approved no-risk projects for each borrower. I find that safeguard implementation performance does not influence whether no-risk projects are approved. While the full regression estimates are omitted for brevity, the only significant variables excluding fixed effects were portfolio characteristics, such as the number of project and size of the portfolio.

Table 2: Approval decisions about environmentally-risky development projects during years with positive allocations

Model	1a	1b	2a	2b	3a
MDB	World	World	Asian	Asian	African
NO. GOOD SAFEGUARD OUTCOMES	0.19** (0.09)	0.14 (0.09)	0.13* (0.07)	0.14* (0.07)	-0.33* (0.18)
NO. POOR SAFEGUARD OUTCOMES	-0.44* (0.24)		-0.25 (0.18)		0.65* (0.34)
NO. POOR SAFEGUARD IMPLEMENTATION		-0.07 (0.36)		-0.67** (0.30)	
OVERALL REPUTATION	0.16 (0.15)	0.16 (0.15)	-1.09** (0.41)	-1.09** (0.40)	0.57 (0.36)
GOVT.EFFECTIVE	0.25* (0.13)	0.25** (0.13)	0.59** (0.25)	0.53** (0.26)	0.16 (0.26)
LESS CIVIL LIBERTIES	0.17** (0.05)	0.17** (0.05)	0.32** (0.09)	0.30** (0.09)	-0.00 (0.10)
CONCESSIONAL	-0.28** (0.13)	-0.28** (0.13)	-0.17 (0.27)	-0.16 (0.27)	-0.51** (0.26)
NO. PROJECTS	0.17** (0.02)	0.17** (0.02)	0.11** (0.04)	0.11** (0.04)	0.20** (0.06)
TIME DUMMIES	all neg., 3+ gap**	all neg., 3+ gap**	neg., 4+ gap**	neg., 4+ gap**	
NO. RISKY TYPE 5YR.					-0.02 (0.07)
Random Intercept Variance	0.091	0.085	0.000	0.000	0.000
Observations (Countries)	1355 (134)	1355 (134)	280 (36)	280 (36)	317 (52)
Residual Deviance	943.2	947.0	169.7	166.1	213.7

Statistical significance: * p < 0.1, ** p < 0.05

I do observe differences in the negative safeguard performance variables that predict fewer environmentally-risky project approvals for the World Bank and the Asian Development Bank. For the Asian Development Bank, environmental safeguard performance is a standard component of all project evaluations, and is available for 180 of 283 project evaluations completed between 1995-2008. In contrast, environmental safeguard performance is not a standard component of project evaluations for the World Bank, and is only available for 125 of 472 project evaluations completed between 1995-

2008 (see also Figure 1). As a consequence, Asian Development Bank project evaluations documenting failed safeguard outcomes cover a much larger proportion of the total panel (74/280 country-years) than is the case for the World Bank (58/1355 country-years). For the Asian Development Bank, therefore, the number of project evaluations documenting safeguard failures regardless of issues in design fails to achieve statistical significance at conventional levels (Model 2a), while excluding safeguard failures associated with design problems proves to be a more discriminating test (Model 2b). For the World Bank, because safeguard performance is not a standard component of project evaluations, failing to mitigate environmental damages tends to be triggered by performance issues regardless of whether design problems are also noted. When excluding projects with design problems, a sufficient number of observations are not available for robust statistical testing (26/1355 country-years, Model 1b).

For both the World Bank and Asian Development Bank, several of the other control variables are significant predictors of whether environmentally-risky projects are approved in a given country-year. For the Asian Development Bank, borrowing countries that achieve above average outcomes across their entire portfolio actually receive fewer environmentally-risky projects (Models 2a-b).¹⁴ This is a peculiar result, possibly indicating that high-performing borrowers are more likely to take on non-infrastructure projects, such as financial sector reform programs or large policy-based loans.¹⁵ For both the World Bank and Asian Development Bank, borrowing countries with greater government effectiveness, an indicator of the host government's ability to

¹⁴ I have checked for the possibility that this result is driven by colinearity with the between safeguard implementation performance and overall performance reputation. In no case is the overall performance reputation indicator correlated with any safeguard performance variable by more than 0.28. When omitting OVERALL REPUTATION from the regression, Model 2a fails to produce significant results at conventional levels, while the results of Model 2b remain unchanged and statistically significant.

¹⁵ For example, when sorting the panel by overall reputation, Thailand accounts for the top 11 country-years in terms of this score. However, Thailand never received an environmentally-risky project during those years and instead borrowed primarily in the financial sector.

implement policies, receive more environmentally-risky projects. This indicates that these MDBs do respond to general governance conditions for projects that are likely to require a great amount of procurement and implementation oversight (Hout, 2007; Neumayer, 2003). In addition, borrowing countries that have low levels of civil liberties are more likely to receive environmentally-risky projects, indicating that opposition from civil society either decreases borrowing country demand for risky projects or MDB staff incentives to pursue risky projects in places where opposition is likely to delay approval and disbursement. This issue will be the subject of Chapter 4.

Also as expected, the number of projects in each borrower's portfolio has a large and significant impact on the probability of receiving environmentally-risky lending during any given year. There is also a very clear temporal dependence among the data, indicating that once environmentally-risky projects are not funded for a long time, they have less of a chance of being considered, perhaps owing to the atrophy of MDB expertise or the MDB-borrowing country working relations at the country level. In addition, time dummies control for countries that never or only infrequently receive environmentally-risky projects due to unobservable country characteristics.

To aid substantive interpretation of these model results, Figure 4 displays the *total model predictive intervals* at 90% confidence based on Model 2b for the Asian Development Bank. To produce these predictive intervals, I draw randomly from the estimated distribution of every model coefficient, set each model variable to the mean of the sample for continuous variables or the median of the sample for discrete variables, vary the levels of NO. POOR SAFEGUARD IMPLEMENTATION and LESS CIVIL LIBERTIES according to Figure 4, and predict the outcome using the model distribution

(probit).¹⁶ In this way, the predictive intervals show how poor safeguard implementation and the level of civil liberties influence the predicted outcomes and total model uncertainty. As can be seen in Figure 4, at both high and low levels of civil liberties, failing to implement safeguard measures when no design problems are noted strongly decreases the probability of receiving an environmental risky project. In addition, the substantive effect of having high civil liberties is extremely important, decreasing the probability of receiving an environmentally-risky project by almost an order of magnitude. While both of these effects are significant at all levels, there is still considerable total model uncertainty, indicating that there is still room to produce better fitting models. Given the large substantive effect of civil liberties, I investigate how MDB accountability to civil society groups might change allocation practices in Chapter 4.

¹⁶ Low civil liberties use the Freedom House score of 6, while high civil liberties use the Freedom House score of 2 for the civil liberties index. The other model variable are set to the following levels: OVERALL REPUTATION (panel mean); GOVT.EFFECTIVE (panel mean); CONCESSIONAL (0); NO. PROJECTS (panel median); TIME DUMMIES (project approved in previous year).

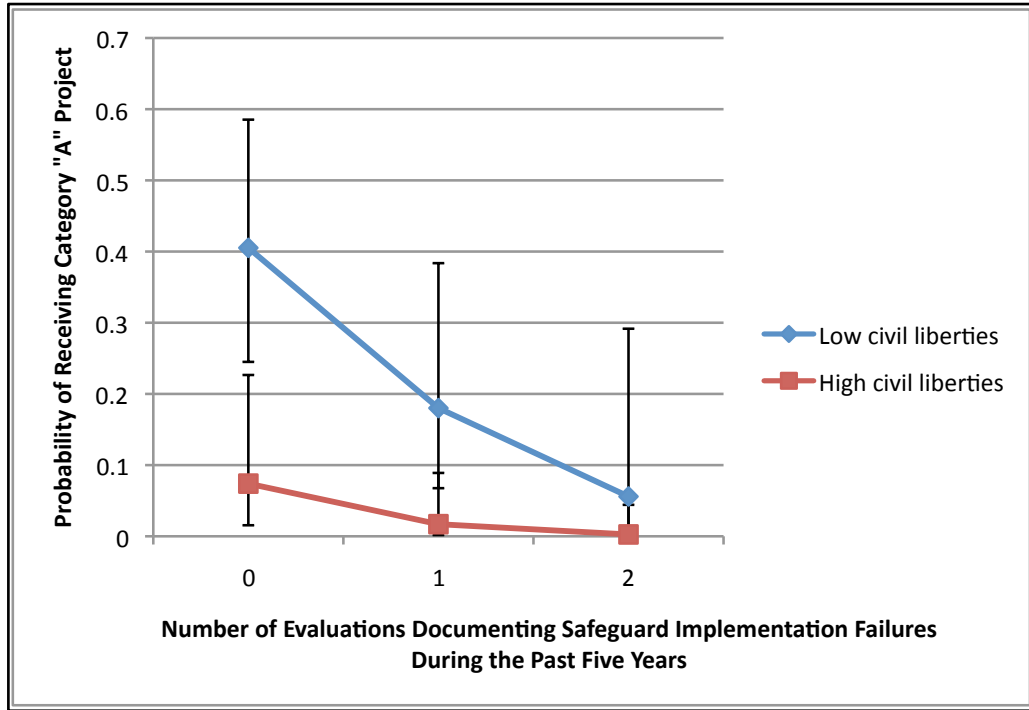


Figure 4: Predictive plot showing effects of safeguard implementation failures and civil liberties on Asian Development Bank project approval (Model 2b)

These models provide some of the first evidence that safeguard implementation performance has a large and important influence on the decision about whether to approve environmentally-risky projects for eligible borrowing countries. Based on these model results, it appears that both the World Bank and Asian Development Bank respond to past safeguard implementation performance, given that it is very costly to approve environmentally-risky projects in poor performing countries. In contrast, the African Development Bank exhibits very different behavior. As can be seen in Model 3a, the AFDB appears to approve environmentally-risky projects *counter* to what might be expected about past performance. Borrowing countries that are evaluated as having poor safeguard performance actually receive *more* environmentally-risky projects in future periods and vice-versa. This is an extremely peculiar result, until the much weaker safeguard practices at the African Development Bank are taken into account.

Unlike the other MDBs, which have systematically applied their safeguard policies and classified each of their projects according to environmental risk so that they could be designed and supervised accordingly, the African Development Bank has had weak systems in place to handle environmentally-risky projects. Indeed, in the project-level environmental classification data that I obtained directly from the AFDB, only 869 of 1746 project approved between 2000-2009 had been assigned to an environmental risk category for safeguard processing. Within the projects that are not assigned an environmental risk category, I find numerous examples of projects that are likely to be environmentally-risky, including large hydropower, fossil fuel based energy generation, and large scale water projects. Thus, it is possible that high-performing countries simply avoid having their projects processed through the safeguards policy. This finding indicates that while AFDB staff have not been incentivized to avoid environmentally-risky projects, but may be forced to submit projects that are likely to result in poor environmental safeguard outcomes to the safeguard process. As more stringent environmental policies have recently become a regular part of AFDB operations, with the associated approval and administration costs applied more systematically, it will be interesting to see whether this results changes.

3.4.2 Allocation Decisions

Thus far, I have only examined how past safeguard implementation performance influences the probability of receiving at least one environmentally-risky project in a particular year, regardless of the actual project value. Next, it is important to examine whether a better environmental implementation record also increases the amount of financing that is committed to environmentally-risky projects. It may be the case that the MDBs not only screen their projects based on past safeguard implementation

performance, but also approve larger and thus more complex projects for borrowers with better safeguard implementation records. In Models 4a-5b, I do not find support for Implication 1b, which states that borrowing countries with good safeguard implementation should receive greater amounts of environmentally-risky financing, controlling for possible screening decisions at the previous stage. In no case is either good or poor safeguard implementation performance a predictor of the amount of risky financing that will be received, given that at least one environmentally-risky project is approved during a given year.

Table 3: Allocation amounts for environmentally-risky development projects given positive approval decision

Model	4a	4b	5a	5b
MDB	World	World	Asian	Asian
NO. GOOD SAFEGUARD OUTCOMES	-9.9 (12.0)	-11.0 (12.1)	14.3 (17.9)	15.7 (17.5)
NO. POOR SAFEGUARD OUTCOMES	-8.5 (65.9)		10.9 (58.6)	
NO. POOR SAFEGUARD IMPLEMENTATION		17.0 (89.1)		-36.7 (102.7)
OVERALL REPUTATION	10.9 (31.3)	11.4 (31.3)	99.2 (111.3)	85.6 (96.6)
GOVT.EFFECTIVE	40.0 (39.8)	40.1 (39.8)	28.1 (120.8)	29.9 (120.3)
LESS CIVIL LIBERTIES	45.8** (13.3)	46.1** (13.2)	36.9 (37.4)	37.8 (36.8)
CONCESSIONAL	-33.7 (41.5)	-33.7 (41.6)	-88.2 (105.5)	-91.1 (105.1)
PORTFOLIO SIZE	0.32** (0.02)	0.32** (0.02)	0.28** (0.09)	0.27** (0.09)
Random Intercept St. Dev.	107.4	107.8	122.49	119.1
Observations (Countries)	215 (75)	215 (75)	45 (15)	45 (15)
Residual Deviance	2824	2824	600.8	600.7
Null Deviance	2989	2989	623.7	623.7

Statistical significance: * p < 0.1, ** p < 0.05

This result indicates that the effect of the safeguard policies is mostly applied at the approval stage when project are screened, rather than the allocation stage when it is decided how large projects will be. This might be expected, given that most projects

come into the approval pipeline with a predetermined level of financing, and all projects that trigger safeguards must have impact assessments and management plans regardless of project size. As discussed below, I found no evidence in interviews that project sizes were altered because of past safeguard performance.

3.5 Extending Model Results with MDB Staff Interviews

3.5.1 Safeguard Policies and MDB Staff Incentives

In order to understand how external pressures from state and non-state actors and organizational practices produce these model results, I visited the headquarters of the World Bank, Asian Development Bank, and African Development Bank and conducted interviews with 54 staff members about how the MDBs respond to safeguard performance information. Based on a semi-structured interview template, I asked questions about the ways that safeguard performance information is collected and transmitted within the different MDBs, when and why operational staff are incentivized to respond to that information, and how the MDBs might respond to safeguard performance information in ways that are not observable in allocation models (Appendix 1). When conducting interviews, I sought to meet with a wide range of evaluation, policy, and operational staff at each of the MDBs considered in this chapter to maximize variation in observations.

One of the key findings gained by these interviews is that across the MDBs there are no formal, institutionalized processes that require direct responses to safeguard performance issues that are identified in project evaluations. This was reported not only by operational staff, who are generally more skeptical of the direct influence that evaluations have on decisions, but also among evaluators. For example, a World Bank IEG evaluator indicated that very few project evaluations are formally considered at the

sub-Board Committee on Development Effectiveness level and that there is no process to track how the findings of previous project evaluations influence future lending decisions. A former manager of the Asian Development Bank evaluation department indicated that the evaluation department had long raised concerns about the usefulness of project evaluations, given that there is no direct “learning mechanism” in place to transfer findings into allocation decisions or operational practices. As one ADB evaluator commented, any risk-aversion to environmentally risky projects is likely to be “much more systematic than any specific project evaluation.”

Given the relative share of environmentally-risky projects has not significantly decreased over time in the lending portfolios considered here (Independent Evaluation Group [IEG], 2010b), it becomes important to understand how mandated administrative practices can drive different allocation responses in different borrowing countries. At both the World Bank and the Asian Development Bank, operational staff cited how the “hassle factor” of complying with environmental safeguard policies incentivizes them to respond to past safeguard performance. In particular, MDB operational staff have incentives to pursue projects that can be approved quickly at low costs, as this allows staff to seek career advancement at the individual level and sectoral units to be allocated higher budgets in future years by demonstrating an ability to meet lending targets. While certain environmentally risky projects might lead to important development outcomes, operational staff at both the World Bank and Asian Development Bank reported that lower risk projects might be pursued when there is a perception that safeguard concerns will disrupt or delay the project approval process.

The past safeguard implementation performance of borrowing countries is a strong signal to these staff about the delays that might be faced when seeking the approval of environmentally risky projects. Since the implementation of safeguard

policies is still basically the responsibility of the borrowing country (Independent Evaluation Group [IEG], 2010b; Operations Evaluation Department [OED], 2006), failure by a borrowing country to carry out safeguard requirements in past operations indicates that more time and resources will need to be devoted to designing, implementing, and supervising safeguard implementation performance in future projects. Indeed, even operational staff that were skeptical that safeguard performance resulted in changes to lending decisions indicated that borrowers who failed to properly implement safeguard policies in past operations required greater implementation support and supervision in future projects. Thus, when safeguard policies are not successfully implemented in past operations, it can create a “chilling” effect among operational staff who are accountable for using scarce administrative resources to approve and manage diverse portfolios of projects.

For example, operational staff at the Asian Development Bank described the onerous process of receiving a “safeguard compliance memo” from the Environment and Social Safeguards Division before a project was considered to be ready for Board approval. Operational staff reported instances where they were sent down to the safeguards division to “camp out” and wait for the approval of the safeguard compliance memo. Given limited Board slots available for considering projects, this process can delay approvals by bumping project consideration at the Board to the “next available” slot which may be several weeks or months in the future. I received reports that higher level operational management will some times get involved to tacitly pressure the safeguards division for release of a safeguard compliance memo that did not require significant changes to project design. These reports demonstrate that the process of achieving safeguard clearance while projects are in the pipeline can take considerable effort at all levels of the MDB operational units.

In addition to having safeguard measures formally approved by safeguard units, other time-consuming operational practices that have been put in place to deal with safeguard issues during the design stages of a project. At the Asian Development Bank, operational staff report an onerous “box-checking” exercise that is part of designing any project that is likely to trigger environmental or social safeguard policies. For example, the mandated procedures for conducting environmental impacts assessments at the Asian Development Bank are based on a 13-chapter, 356-page manual that includes a 72-item checklist of the criteria that will be used to review and approve an environmental impact assessment (Lohani, et al., 1997). The corresponding manual at the World Bank has 10 chapters and includes a checklist of 20 separate operational policies (each with their own requirements) that must be accounted for when designing an environmental assessment and environmental management plan (World Bank, 1999). Given that responsibility for carrying out these procedures rests with the borrowing country, past performance is an excellent indication of the speed at which these requirements will be fulfilled.

Because staff career advancement is strongly related to the ability to steer projects smoothly through the approval process, at both the World Bank and Asian Development Bank interviewees reported that decisions were often made to avoid project components in marginally-risky projects that were likely to trigger safeguard policies and cause delays in project approval and implementation. In both cases, operational staff reported incentives to have infrastructure project assigned to environmental risk category “B,” which does not require a full environmental impact assessment and environmental management plan in most cases. For example, one transportation staff member at the Asian Development Bank reported that highway projects are often classified as “rehabilitation” projects on existing right-of-ways, even if

project activities are substantially similar to building a new road (e.g., unimproved road to expressway). In this way, the transportation unit would not have to complete safeguard requirements for risky projects, but rather the less onerous “initial environmental assessment” for the less risky category “B” projects.

Another way of circumventing safeguard policies is for the MDBs to fund only the less risky parts of larger projects. One operational staff member in energy at the World Bank indicated that it has been common practice to finance the transmission lines from dirty power generating facilities, rather than the facilities themselves. At the Asian Development Bank, transportation staff will often seek to finance the less-risky portions of larger road projects, such as those that do not pass through sensitive ecological areas or national parks, knowing full well that the borrowing country in question will find other sources of financing to cover these more risky portions of the projects.¹⁷ For example, the ADB was considering financing improvement to the Mumbai airport, but because significant safeguard issues were raised with regards to resettlement and environmental management, the ADB instead moved forward with financing for a transportation framework that included roads and rail linking the Mumbai airport to surrounding areas.

In terms of learning from the outcomes of past projects through project evaluations and other project completion assessments, one operational manager at the Asian Development Bank believed the most significant “learning” for operational staff was that they should not get involved in projects that will be unnecessarily difficult. Many operational departments have learned that scarce administrative resources are best spent by “avoiding the hassle of category A projects,” according to the same

¹⁷ This funding pattern was reported to be especially likely for mid-income countries like India and China, which have access to competitive, commercial financing to pursue the most environmentally risky parts of transportation projects.

operational manager. The learning that takes place within operational units is thus about the types of projects that are likely to face significant delays in the design stage. At both the World Bank and Asian Development Bank, certain types of projects are now seen as universally too risky to be involved with, such as large hydropower projects and coal-fired power plants. However, at the country level, learning from past operations includes understanding the degree to which civil society groups will push for the strict adherence to safeguard policies. Thus, as was found in the models above, operational staff reported that an active and critical civil society is a key determinant of the risks faced when designing and implementing environmentally-risky infrastructure or energy projects. One ADB staff indicated that this is a primary reason why India has received fewer environmentally-risky projects over time than China, given that strong opposition to environmentally-risky projects in India is all but guaranteed.

Despite these incentives, some staff members, especially those at the Asian Development Bank, still believed that I would find greater “constructive engagement” based on past safeguard implementation performance than I would selectivity for environmentally-risky projects. Instead of leaving sectors because of poor safeguard performance, staff members might seek additional technical assistance for safeguard implementation or seek the approval of “easier” projects that are intended to improve capacity in this area. While this type of engagement is consistent with the model findings presented above, in the future it is important to address whether the MDBs respond to safeguard performance in other observable ways, like allocating greater amounts of technical assistance to deal with capacity problems that previous operations reveal.

3.5.2 *Safeguard Policies and Borrowing Country Demand*

It is not only MDB staff that have responded to environmental safeguard policies. During my interviews, it was reported several times that borrowing countries have also been deterred from pursuing environmentally-risky projects with the MDBs in recent years due to delays in project approval and implementation. When borrowing countries have access to other sources of financing, whether through commercial lending markets, the ability to self-finance infrastructure projects through tax revenue, or sources of development assistance that do not carry significant safeguard requirements (e.g., Chinese aid), borrowing countries have found the design and implementation of infrastructure projects to be much smoother. On several occasions, for example, it was reported to me that borrowing countries view the requirement that environmental impact assessments must be posted for 120 days before a project was eligible for Board approval to be particularly onerous.¹⁸

Asian Development Bank operational staff and evaluators cited specific countries that have become less interested in financing environmentally risky projects through the Bank because of delays caused by safeguard policies. For example, one staff member described how the Philippines has moved toward the more flexible program lending that provides general support to government ministries, as opposed to project lending that entails significant difficulties in implementing safeguard policies. A similar trend was reported for borrowing requests from Indonesia. In Southeast Asia, the MDBs used to be the primary financers of large hydropower projects. Because of the significant delays caused by environmental and social safeguard policies, the ADB and World Bank have funded very few large hydropower projects in the region in recent years, despite

¹⁸ As introduced above, this requirement has been standardized across the MDB public sector safeguard policies because of the “Pelosi amendment” in the 1989 US International Development and Finance Act.

the fact that the pursuit of such projects has accelerated. It was reported by senior operational management at the ADB that India has basically said it wants all its projects to be category “B” or it does not want ADB money. A recent \$600 million railroad project in India did not move forward because India wanted the project rated as a category “B” but the ADB safeguards unit required the full safeguard procedure for a category “A” project. Eventually in 2009, only a portion of the Railway Sector Improvement Project was approved as a category “B” project.¹⁹

On the other hand, China continues to receive a large number of category “A” projects primarily because it has a system in place to handle the safeguard policies of the MDBs. It was reported that China often approaches the MDBs with fully worked out project proposals, including the relevant environmental impact assessments. Thus, by taking on much of the burden for environmental assessments, China has ensured that significant delays will not be encountered, because little work is required of MDB staff other than checking the assessment. Thus, because China is a high-performer and has developed a domestic system to handle safeguard administrative procedures, it is unlikely to face the delays that cause such a strong response to past safeguard performance in other countries. In addition, it has shown the propensity to self-finance projects that are especially risky.

3.5.3 Contrast with African Development Bank

The model results reported above show that the African Development Bank does not show the same performance-based response to past safeguard implementation as the World Bank and Asian Development Bank. This contrast presents an opportunity to examine whether policy choices and administrative procedures are responsible for

¹⁹ See the project information document at: <http://pid.adb.org/pid/LoanView.htm?projNo=36317&seqNo=01&typeCd=3> (Accessed June 2011).

incentivizing MDB staff to respond to performance information. Whereas, the World Bank and Asian Development Bank both have very formalized safeguard policies that cause observable delays in project approval and implementation, the African Development Bank has had much weaker safeguard policies in place during the time period considered here. When the African Development Bank went through a restructuring in 2007-2008, a Safeguard Unit was created to ensure implementation of environmental safeguard policies. When I met with this unit, they indicated that prior to 2008, there was very little institutional ability within the African Development Bank to ensure the proper implementation of safeguard policies. This problem was more systematic than just safeguard policies. Prior to 2008, it was estimated that completion reports were written for only 8% of projects and that more than 40% of the total portfolio was considered problematic. Given the general state of portfolio disrepair, the Safeguards Unit was skeptical that the administrative procedures mandated by safeguard policies were a serious priority during the time period considered in this research.

When I spoke with operational staff at the African Development Bank, I was met with significant skepticism that safeguard policies had caused delays in project approval and implementation, or that safeguard policies had significantly shaped approval and allocation decisions. Most operational staff report that addressing the development needs on the African continent was the paramount priority, and would be pursued regardless if a project were likely to have negative environmental impacts. Operational staff generally regard environmental risks as only a small part of the overall costs of project approval and implementation. One ADB operational manager stated that “safeguards” was very much a Western, World Bank inspired term that had little relevance to decision made in the context of African development finance. Instead,

safeguards are viewed as just another standard procedure followed during project preparation.

Many operational staff at the African Development Bank were unable to recall specific instances of satisfactory or poor safeguard implementation. Instead, most staff indicated that the majority of administrative effort required by safeguard policies occurred during project preparation. For example, one staff member that had been task leader for transportation projects indicated that he was not able to comment on the track record of safeguard implementation during projects because their had been no systematic review of safeguard performance. In many cases, project teams use consultants to both write and supervise the implementation of environmental management plans. Because of the difficulty of implementing projects in many countries that are part of the African Development Bank portfolio, one staff member commented that management is less concerned with projects going out of safeguard compliance than they are about having a plan to deal with non-compliance. Accordingly, there were few reports of disbursement delays owing to problems in safeguard implementation.

In addition, AFDB staff reported that they do not feel significant pressure from civil society groups over safeguard implementation. One operational staff member stated that the World Bank is always afraid of civil society groups, particularly international environmental NGOs, whereas staff at the AFDB are “not afraid.” For example, there was a large hydropower project called Gibe III in Ethiopia to be jointly financed by the World Bank and African Development Bank. The International Rivers Network, an international NGO based in the US demanded that additional environmental studies be carried out prior to the project being approved. Whereas the African Development Bank was ready to go forward with the project after carrying out its own internal safeguard procedures, the World Bank insisted on more studies in line

with the International Rivers Network request. In the end, the project was “lost” because Ethiopia and the World Bank considered the safeguard issues to be too much of a constraint on the project. There are indications that the Chinese will finance the project instead, with very few safeguards in place (Rice, 2010).

As the implementation of safeguard policies becomes more stringent, it will be interesting to test whether the African Development Bank also responds to past safeguard implementation performance. Slowly, safeguard issues are becoming more prominent. During recent replenishment meetings, safeguard issues figured prominently into donor state demands for continued support of the AFDB.²⁰ In addition, as the Independent Review Mechanism has examined projects due to poor safeguard performance, such as the Bugali Dam project in Uganda, some operational staff have reported the need to spend more time studying and implementing environmental management practices.

3.6 Conclusions and Implications

Development organizations act credibly on their stated policy priorities when they adjust the allocation of development assistance to reflect the performance of aid recipients in past projects. The difficulty that donors have to act credibly and pursue performance-based allocation has been an ongoing area of inquiry. To this point, most empirical studies on performance-based allocation have only examined macro-indicators of recipient governance and aggregate flows of development assistance. In this chapter, I have taken a different approach by systematically examining how MDBs respond to project-level safeguard implementation performance information when approving and

²⁰ For example, see how safeguard issues figure prominently into the background paper that was prepared for meetings with donor countries about the 12th African Development Fund replenishment (African Development Fund [ADF], 2010).

allocating environmentally-risky lending. I find strong support that both the World Bank and Asian Development Bank screen projects based on the past safeguard implementation performance of borrowing countries.

This finding demonstrates that state principals can use administrative procedures to incentivize certain types of action, in this case by making it costly to disregard past safeguard implementation performance. The environmental safeguard policies that have been put in place at the MDBs increase the costs to design, approve, and administer environmentally-risky projects. However, decision-makers can take cues from past performance about the magnitude of these costs within specific borrowing country programs. For MDB staff and management, the costs of administering and supervising safeguard policies is higher for borrowing countries that have a history of poor performance than they are for countries that have a history of satisfactory performance. In this way, evaluations of safeguard performance can inform decision-makers how to best use scarce administrative resources and maximize lending.

Given the difficulty that development organizations have had in practicing conditionality at the project level and performance-based allocation at the aggregate level, this finding speaks to the importance of having administrative policies in place that systematically make it more costly for MDB staff to approve projects in countries with poor performance records related to areas of prioritized functional performance. Policies that attempt to support performance-based decision-making are likely to have the greatest influence when they are linked to core operational incentives, which are often to meet lending or grant-making targets (Operations Evaluation Department [OED], 2006). For example, development organizations might establish policies requiring more intensive (and expensive) preparatory analytical work and supervision of projects in countries with a history of low performance in relevant areas. This might

not only increase the quality of the project, but also induce development organizations to select the project types that are more likely to succeed in order to avoid projects with high administrative costs.

Another important implication of the findings presented here is that performance-based allocation may be more easily implemented by development organizations that have flexible portfolios consisting of different project types. Since it is difficult to implement conditionality through disbursements within a single project (Svensson, 2003) and organization-wide allocation practices are often slow to change (Gutner, 2005; Nielson & Tierney, 2003), development organizations are likely to be most effective when they adjust portfolio composition at the country level. Future work on performance-based development assistance should explore the possibility of practicing performance-based allocation using within-country portfolio composition decisions. To support performance-based allocation at this level, project evaluations should routinely include detailed evaluations of policy priorities that are identified in country-level assistance strategies. In terms of the environment, this means that more detailed performance information is needed at the project level for recipients with identified needs for environmentally-risky projects. Just as it is standard procedure to conduct environmental impact assessments for high-risk projects before approval, it should be standard to conduct environmental reviews following the completion of high-impact projects. This would ensure that the information necessary to act credibly on stated environmental policy priorities is available, given that policies are in place to incentivize the use of information.

Within the international relations literature on institutional design, scholars have inquired about the types of IO design features that can improve performance. In particular, scholars have been interested in understanding how the rules for controlling

the behavior of international organizations operate (Koremenos, Lipson, & Snidal, 2001). In terms of environmental policies, project-by-project oversight is not possible for the donor countries to the MDBs (Weaver, 2008). The results here show that by designing international organizations to have internal units with different interests (maximize lending vs. mitigate environmental damages) balanced against one another can be a key way to relieve state principals from the burden of providing oversight and ultimately sanctioning for poor performance. Instead, in the case of safeguard policies, donor countries have created a system of passive checks and balances within the MDBs that incentivizes responses to performance. As both practitioners and scholars alike become interested in the performance of international organizations, more attention can be paid to how internal policy choices can foster internal oversight and incentivize high performance.

However, owing to the delays caused by safeguard policies during project design and approval, there has been a large push, especially from borrowing countries, to streamline planning and safeguard requirements. For example, the Asian Development Bank is currently undergoing reforms that would decrease project preparation time by half, which some staff I interviewed believed would come at the expense of diligent safeguard policy implementation (Asian Development Bank [ADB], 2009a). This may decrease the incentives that staff have to actively take cues from past safeguard implementation performance. In addition, more borrowing countries are exercising their “exit options” by choosing to look elsewhere for environmentally-risky financing because of MDB safeguard policies. Many operational staff I spoke with at both the World Bank and Asian Development Bank highlighted the risks of driving borrowing countries to financing sources that require no environmental safeguard

measures. As more commercial financing is available to middle-income borrowing countries, this becomes a distinct possibility.²¹

One trend that might serve to preserve the incentives created by safeguard policies is the piloting of “country systems” for environmental safeguard implementation. The MDBs have recognized that for certain high-performing countries, the safeguard policies add substantial administrative burdens without adding much value in terms of safeguard outcomes (Independent Evaluation Department [IED], 2009; Independent Evaluation Group [IEG], 2010b). For these countries, both the World Bank and Asian Development Bank are experimenting with allowing the particular borrowing country to certify and implement safeguard mitigation measures according to their own procedures. In many cases, high-performing countries have complained that they must duplicate efforts because projects pass through both their own safeguard procedures and a separate set of procedures mandated by the MDBs. By ending the later requirements based on performance, there is a potential to incentivize countries to adopt strong policies of their own and implement them well in order to qualify for participation in country safeguard systems. This would also incentivize staff to pursue environmentally-risky project in the places with high safeguard performance. However, care needs to be taken to ensure continuous high performance once countries transition to country systems in order for these incentives to be preserved.

When speaking to MDB staff about environmental safeguard policies, it was clear that in addition to the incentives brought about by differences in compliance costs at the country level, that the threat of being subjected to an Inspection investigation might drive allocation and approval decisions. Recognizing the environmental and

²¹ This may even be a concern for low-income countries, as non-traditional sources of financing, like Chinese development assistance become available for environmentally-risky projects. This shift has already occurred for the financing of large hydropower projects in Southeast Asia, for example.

social implementation failures of the 1980s, three development banks established Inspection mechanisms that allowed civil society groups to formally petition for redress when safeguard policies were not properly implemented. Thus, in addition to the incentives created by organization-wide administrative procedures, the availability of oversight from non-state actors and the cost of sanctioning might have an additional effect on the allocation of environmentally-risky projects. The next chapter explores these possibilities.

4 Civil Society Claims for Environmental Performance: Operational Learning and Risk-Aversion at the Multilateral Development Banks

“It was hoped that this citizen driven process would provide some means of holding the bank accountable to the people affected by its lending decisions, and that having such a mechanism in place would lead to the avoidance of further disastrous projects.” (Clark, 2003, p. 2).

4.1 Introduction

By the late-1980s, opposition from civil society groups to environmentally damaging World Bank development projects had grown increasingly strident. The Narmada Dam Project, which was approved for financing by the World Bank in 1985, became a focal point for this opposition. When it became clear that thousands of people would lose their homes as a result of the project, and that vast areas of natural and agricultural land would be inundated by the dam construction, there was a massive mobilization by both Indian and international civil society organizations against the project and the World Bank. In India, this mobilization led to marches of hundreds of thousands of people and civil disobedience through the occupation of areas that were scheduled for inundation (D. Clark, 2003). These protest were followed and supported by civil society organizations around the world, leading to hearings in donor countries about the environmental and social practices of the World Bank and calls for reform at the World Bank by US and European political leaders. Among the chief critiques of World Bank practices was a recognition that private citizens and civil society groups in borrowing countries had little recourse when lending decisions at the World Bank and the other MDBs negatively impacted them. Indeed, protests at the time seeded a broader discussion about the “democratic deficit” of international organizations that had been delegated significant international authority (Nye, 2001).

In response to the Narmada protests, the World Bank agreed to form an independent commission to review the Narmada project. The commission found systematic flaws in the planning, design, and implementation of the Narmada project, reinforcing the claims of civil society groups (Morse & Berger, 1992). In 1993, facing growing criticism from both major shareholder states and civil society organizations, the World Bank canceled its support for the Narmada project at the request of India. In the following year, NGOs and some developed shareholder countries pushed to establish a permanent commission at the World Bank that would be available to review civil society claims of poor environmental and social safeguard policy implementation. In 1994, as part of the 10th International Development Association (IDA) replenishment, the US insisted that the World Bank adopt an inspection mechanism where civil society groups negatively impacted by Bank projects could seek recourse if safeguard policies were not implemented properly. Following a series of planned oversight hearings in the US Congress about World Bank environmental and social policies, a permanent Inspection Panel was established at the World Bank.¹ This reform was followed by the Inter-American Development Bank and the Asian Development Bank in a matter of months (McGill, 2001; G. D. Miller, 2001).

Establishment of an Inspection Panel at the World Bank and the regional development banks is remarkable because states have typically reserved the authority to hold international organizations (IOs) accountable for performance (D. Clark, 2003, p. 9). Civil society groups that wish to challenge the actions of IOs face the difficult task of appealing to state principals, which are not always receptive to their claims (Keck & Sikkink, 1998; Woods & Narlikar, 2001). Furthermore, given the long chains of

¹ For a more complete history of the establishment of the World Bank Inspection Panel, see (Shihata, 2000) and (D. Clark, Fox, & Treakle, 2003).

delegation between states and international organizations and the inability of states to directly collect information about IO performance in many instances, accountability for performance at IOs is generally weak (Gutner & Thompson, 2010; Lyne, et al., 2006; Nye, 2001).

To this day, the establishment of Inspection Panels at the MDBs represents the most direct and institutionalized way that civil society groups can hold international organizations accountable for environmental performance. Indeed, failure to implement environmental safeguard policies has been the primary reason why Inspection cases are triggered (Treakle, Fox, & Clark, 2003, p. 251). In essence, the Inspection process at the MDBs created the possibility for civil society groups to exercise a direct claim of accountability over IOs, by providing them a high-level, visible forum to reveal instances of poor environmental and social performance by the MDBs. While it has been recognized that civil society groups can provide important monitoring functions to states (Dai, 2007; Steffek & Ferretti, 2009), rarely do civil society groups in less-developed countries have the ability to publicize their grievances about IO performance in ways that attract significant attention from member states and potentially cause offending IOs to incur large financial and organizational costs.

When an inspection claim is received from a civil society group, the claim is made public and the panel determines whether the claim is eligible for investigation.² Owing to the high-level negative attention that MDB management receives from shareholder states and the significant resources that are required to defend themselves if an investigation is approved by the Board, typically both the management and borrowing country involved have responded vigorously that claimants are not eligible

² Across the three MDBs considered here, civil society claimants must show that they have experienced damages because MDB policies were not carried out, must have attempted to resolve the issue with bank management, and must file their claim while a project is active. For more specific rules on eligibility, see (D. Clark, 2003).

to file inspection requests (D. Clark, 2003, p. 12-13). If the claimant is found to be eligible, initial reports about the case are sent to MDB Board members, who are representatives of member states, for approval of a formal investigation. Owing to this high-level consideration and approval of an investigation, MDB management and staff generally spend large amounts of time and resources defending Bank actions when an investigation is approved. If the Inspection Panel finds evidence that environmental or social policies were not properly implemented during the design and execution of a project, it will make recommendations to the Board identifying remedial actions to be taken, which can impose further costs on MDB management. In addition, because of significant Board involvement throughout the inspection process, claims can seriously damage the international reputation of MDBs, making concessional fund replenishment and general capital increase negotiations with donor countries difficult.³

A critically important feature of the Inspection mechanisms is that the consent of the state principals is not required for a request to be filed. Because an Inspection requests automatically sets in motion a number of costly steps for the MDBs, the Inspection process allows civil society groups to independently impose substantial costs on the MDBs for poor implementation of environmental safeguards. It remains an open question whether this type of monitoring and accountability mechanism prompts the MDBs to become risk-averse to environmentally-risky projects and/or simply improve the implementation of safeguards.

Unlike project evaluations, which measure both satisfactory and unsatisfactory performance, Inspection cases are only triggered by instances of poor performance and produce recommendations that are limited in scope to single projects. This chapter

³ For example, US Congressional leaders have commissioned independent Government Accountability Office reports on the environmental and social practices as part of replenishment discussions. See GAO (General Accounting Office [GAO]).

examines two ways that the MDBs might respond to the Inspection process. First, the MDBs might simply avoid environmentally risky projects in countries where Inspection investigations have previously occurred. Misgivings about this likely project avoidance response were a core part of opposition to establishing an Inspection process. If the Inspection Panel causes the MDBs to become risk-averse to infrastructure projects, they might cease to be relevant development actors in the developing world, where infrastructure is a clear priority (World Bank, 2001). Second, the Inspection Panel might not cause project avoidance, but rather improve the environmental performance of MDBs and lead to fewer substantiated claims of poor environmental performance by making accountability a reality.

This chapter examines whether empowering civil society through the Inspection process has made the MDBs more responsive to negative performance information. To do so, I address three primary questions: (1) Does poor safeguard performance as documented in project evaluations predict that borrowing countries will be subjected to Inspection requests and investigations? (2) Has the establishment of the Inspection process promoted learning within the MDBs to avoid future Inspection requests? (3) Has the establishment of the Inspection Panel caused the MDBs to become averse to environmentally risky projects? I demonstrate that the borrowing countries targeted with Inspection requests tend to be high-performing with respect to safeguard implementation and have greater number of environmental NGOs. I argue that since high-performing countries tend to be the targets of Inspection requests, the MDBs respond by further improving safeguard implementation rather than avoiding environmentally-risky projects. This result underscores how the ultimate impact of civil society accountability is determined by the availability of groups to supply Inspection

requests and that potential for targeted borrowing countries to respond by either altering portfolio composition or improving performance.

4.2 Inspection Panels, Operational Learning, and Risk-Aversion at the MDBs

4.2.1 Accountability of International Organizations for Performance and the Inspection Panels

Existing studies of IO behavior have tended to examine how states drive broad organizational reforms at IOs and why the constellation of IOs and their activities have remained relatively stable despite drastic changes in the international system. Studies have documented various reasons why IOs do not always exhibit behavior that is consistent with underlying state interests, including the development of internal organizational cultures (Barnett & Finnemore, 1999), principal-agent problems such as asymmetric information and long chains of accountability (Hawkins & Jacoby, 2006; Woods & Narlikar, 2001), and the existence of veto power over organizational behavior among certain state principals (Woods, 2003). While it is clear from this literature that IO behavior does not always follow neatly from the underlying interests of states, the conditions that make it possible for external actors to hold IOs accountable for performance remain unclear.

In recent years, international relations scholars have delved more seriously into the politics of IO performance, recognizing that IOs have been delegated important authority to carry out a wide range of activities at the international level. Despite the recognition that some IOs are far more effective at carrying out the tasks that have been delegated to them, understanding of the internal and external factors that contribute to this variation is in its infancy. There are a wide variety of internal and external factors that might contribute to IO performance, including bureaucratic culture, organizational

resources, competing member state interests, incoherent mandates, and IO knowledge management practices (Gutner & Thompson, 2010). Furthermore, it is clear that internal and external sources of IO performance interact, with external state-IO accountability relationships, and influence the development of internal organizational norms and practices (Elsig, 2010; Johns, 2007; Reinalda & Verbeek, 2004).

The degree to which external actors are able and willing to hold IOs accountable for their actions is potentially an important external factor contributing to IO performance. In the context of IO performance, external actors hold IOs accountable by imposing costs/rewards on IOs in response to their performance. There are a number of ways that external actors are able to hold IOs accountable for their actions. States can decrease the amount of resources to IOs that fail to meet certain performance standards (Crane & Dusenberry, 2004). States are also able to change the mandate of IOs and restrict their activities in response to poor performance or grant IOs greater authority and resources in response to satisfactory performance, such as through MDB general capital increases. Non-state actors are able to impede the activities of IOs through protests, shaming, or by not providing cooperation that is necessary for IOs to carry out their mandates (Khagram, 2004; Simmons, 1998).

Despite the numerous ways that international actors are able to hold IOs accountable for their performance, the actual practice of accountability is less frequent than might be expected from standard statist models of international politics (Grant & Keohane, 2005; Reinisch, 2001). Particular to IOs involved with international development, the lack of organizational accountability has been cited as a key reason why development mandates are not successfully achieved (Wenar, 2006). However, unlike many other types of IOs, the MDBS and other international financial institutions

have a vibrant constellation of civil society organizations that monitor their activities and have displayed a willingness to seek accountability for poor performance.

Recently, researchers have recognized the critical role that civil society organizations might play in holding IOs accountable for their performance. One potentially important role that civil society organizations can play is to provide state principals with low-cost performance monitoring, thereby enabling more vigorous state responses to lapses in IO performance (Dai, 2007; Steffek & Ferretti, 2009). In the case of international development projects, it is often private citizens and domestic civil society groups that are best positioned to collect information about the outcomes. Indeed, one donor state executive director to the Asian Development Bank that I interviewed emphasized how NGOs serve as “watchdogs,” because of the inability of states to monitor the implementation of ADB programs. However, civil society organizations in less-developed countries have typically been blocked from participating in official decision-making about international development, both because their home states are unreceptive to their concerns and because they lacked a formal way to participate in IO decision-making (Acuña & Tuozzo, 2000; Keck & Sikkink, 1998).

Because civil society groups have not traditionally been able to participate in IO decisions that affect them, various scholars have been concerned with the “democratic deficit” of IOs (Nye, 2001; Stutzer & Frey, 2005). While there is evidence that more IOs, and especially the MDBS, are integrating civil society consultations into their decision-making processes, establishment of the Inspection Panels at the MDBs is one of the most significant and direct experiments with external IO-civil society accountability that has

been undertaken to date.⁴ By creating Inspection functions within the MDBs, the state shareholders have opened a new line of influence, where groups of private citizens and civil society groups no longer have to work directly through state principals to exert influence on IO behavior and performance (Figure 5).

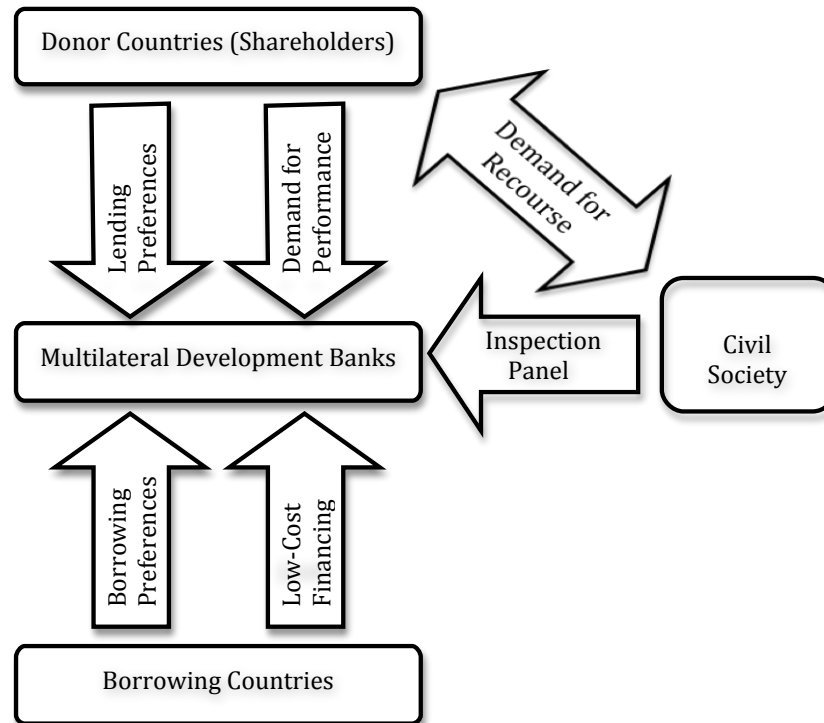


Figure 5: External Pressure on MDBs with Inspection Panels

While the formal rules governing Inspectional Panel claims at the various MDBs are documented extensively elsewhere, it is worth noting the main elements of the claims process that can be generalized across the MDBs.⁵ All of the MDBs have established policies about the environmental and social safeguards that must be carried

⁴ A related example is the establishment of the Ombudsman's Office at the World Bank International Financial Corporation. For more information, see: <http://www.cao-ombudsman.org/> (Accessed April 2011).

⁵ See McGill (2001) for a discussion of institutional design differences of ADB panel. See Miller (2001) for a discussion of institutional design differences of IADB panel.

out during the design and implementation of every project, for example the completion of an environmental impact assessment in the case of a project that is likely to cause negative environmental damages. If a group of people is negatively affected by an MDB project because these policies were not carried out with due diligence, then they can file a claim to the Inspection Panel for an investigation that will determine whether safeguard policies have been violated. The Inspection Panels are structured in a variety of ways, but generally consist of external experts with a mix of nationalities.

If the Inspection Panel determines that the claimants are eligible to make a claim and the Board approves a recommendation for an Inspection investigation, then the Panel conducts a formal investigation, which includes field visits, interviews with the claimants and Bank staff, and a review of project documents. Based on the investigation, the Panel produces a public report that documents its findings related to MDB safeguard policy violations and makes recommendations for remedial activities. The Board then chooses whether or not to adopt these recommendations, and if they are adopted they become a binding directive for MDB management. While various authors have noted that this long chain of events may decrease the effectiveness of Panels in providing accountability (Fox, 2000; Fox & Treacle, 2003), the systematic impact of this performance-revealing mechanism on allocation decisions about projects has not been examined. Most existing studies of the Inspection process rely on single cases examined at great depth (D. Clark, et al., 2003).

4.2.2 Inspection Panels and Learning from Failure at MDBs

One possible MDB response to the establishment of Inspection processes is that the MDBs simply respond by ensuring better safeguard policy implementation, rather than avoiding projects with environmental risks. Indeed, none of the Inspection Panel charter documents envision a situation where establishment of the Inspection process

would change allocation practices, but rather that MDB management would be accountable for diligently implementing operational policies.⁶ One of the reasons why international development organizations have not been responsive to their mistakes is that internal incentives reward continued project approvals, rather than responses to lessons of past operations (Biggs & Smith, 2003). The Inspection Panels made the costs of noncompliance with environmental safeguard policies high for staff and management, thereby increasing internal incentives to carry out safeguard policies with due diligence.

All of the MDBs have placed a great deal of emphasis on becoming “learning organizations,” mainly through increased transparency about the successful and unsuccessful attempts at promoting development (Asian Development Bank [ADB], 2009e; Ellerman, 1999). One of the most difficult parts of creating a “learning culture” within complex organizations is the lack of incentives to share and learn from examples of failed operations (Storey & Barnett, 2000). In a way, establishment of the Inspection process has forced the MDBs to directly deal with instances where they failed to implement environmental and social safeguard policies. Thus, the Inspection processes may have promoted “learning by doing,” whereby the MDBs become more acutely aware of the risks associated with their programs in particular countries and adjust to these risks when projects are subjected to the Inspection process. This leads to the following hypothesis:

Hypothesis 1: Borrowing countries that have experienced previous Inspection investigations will be less likely to have their projects subjected to Inspection requests and investigations in future periods.

⁶ See for example, the resolution establishing the World Bank Inspection panel, at: <http://siteresources.worldbank.org/EXTINSPECTIONPANEL/Resources/ResolutionMarch2005.pdf> (Accessed March 2011).

4.2.3 *Inspection Panel and Risk-Aversion at MDBs*

The Inspection process provides state principals of the MDBs with “fire alarm” oversight of MDB performance related to implementation of safeguard policies (McCubbins & Schwartz). While there are certainly systematic barriers to participation in the Inspection process (e.g., transaction cost of formulating a claim, previous attempt to address the issue with MDB management), a group of any size can submit a claim and if they are determined to be eligible, that claim will receive the attention of member states through the Board. At their core, the Inspection processes have created an avenue for civil society claims to be amplified and formalized at the international level. Civil society groups are not able to demand specific compensatory actions from the MDBs, but participate in a formalized “sunshine policy” for safeguard monitoring (Fox & Treacle, 2003, p. 282-283; Steffek & Ferretti, 2009, p. 41). Thus, the Inspection process functions by alerting MDB member states and other interest groups to instances of poor performance, but ultimately depends on member states (“the Board”) to approve any remedial actions to be taken because of poor performance.

Given that Inspection documents are made publicly available and receive immediate, high-level attention from member states, MDB management and many less-developed member states have feared that establishment of the Inspection Panels would make the MDBs overly *risk-averse* about infrastructure projects that are important for economic development (World Bank, 2001). Environmentally-risky projects are beneficial to the MDBs for two reasons. First, environmentally-risky projects tend to be large infrastructure projects that are a more efficient use of scarce administrative resources, because they quickly meet lending targets and potentially avoid the need to steer multiple, smaller projects through the approval process. Second, from the development outcome standpoint, infrastructure projects have generally achieved more

satisfactory outcomes because implementation requires meeting physical outputs that can often be sourced from contractors, rather than more difficult institutional outcomes that require a great deal of borrowing country commitment (Freeman, 2009). Thus, there have been fears that the establishment of the Inspection Panel would make MDBs risk-averse in the sense that they would choose less effective interventions in order to avoid the possibility of having a project subjected to an Inspection Panel investigation.⁷

This concern has been voiced both inside and outside of the MDBs, and especially the World Bank. Shihata (2000, p. 230), a World Bank insider, writes that there are two primary risks involved with establishing the Inspection Panel. First, there was a “perceived risk was that the establishment of the Panel might have a deterrent effect on Bank’s staff, causing them to be over-concerned with following the rules and procedures and less innovative in their work.” In other words, Bank staff would become so cautious that less-developed countries would lose access to needed infrastructure financing. Second, borrowing countries have resisted the establishment of Inspection Panels because of fears that they “internationalize” disputes with private citizens that should be handled domestically, making borrowers less likely to pursue projects with environmental risks through the MDBs. This might result in borrowing countries seeking financing for risky projects from sources that do not require any social or environmental safeguards, thereby making the net impact of the Inspection Panel negative.⁸

Based on Inspection Panel cases, developed shareholder states have shown a propensity to sanction MDBs for poor environmental performance. For example, the US

⁷ For an excellent exposition on defining risk-aversion for international relations theory, see (O’Neill, 2001).

⁸ For example, Khagram (2004) documents a decline in the number of dam projects financed by the MDBs over the last several decades. While the MDBs are no longer actively involved in this area, many new dams are now financed by the Chinese and other bilateral that do not require any social or environmental safeguards. For an NGO perspective on this process, see the International River Networks “Dams Built by China” page at: <http://www.internationalrivers.org/taxonomy/term/736> (Accessed March 2011).

and some European countries have consistently voted to authorize inspections of MDB projects despite opposition from borrowing countries (Fox, 2000, p. 303-305). In some instances, Inspection cases have resulted in hearings from the US Congress and other bodies.⁹ Discussions of Inspection cases and other “disaster projects” frequently arise as part of replenishment and capital increase negotiations and often lead to calls for MDB organizational reforms (Nielson & Tierney, 2003). Thus, establishment of the Inspection Panels might have created a strong reluctance towards pursuing environmentally-risky projects, which suggests the following hypotheses:

Hypothesis 2a: MDBs will be less likely to approve an environmentally risky project in any given year for a country where a previous project has been subjected to an Inspection Panel case.

Hypothesis 2b: Given that an MDB approves an environmentally risky project in a given year, the amount of environmentally risky financing will be lower for a country where a previous project has been subjected to an Inspection Panel investigation.

⁹ For example, Inspection cases that were filed relating to the Yacyreta Dam Project, which was jointly financed by the World Bank and Inter-American Development Bank, became a major part of a hearing on US appropriations to multilateral development banks in 1997. See minutes for appropriations hearing, US House Subcommittee on Foreign Operations, Export Financing, and Related Programs on 12 February 1997, available at: <http://www.gpo.gov/fdsys/pkg/CHRG-105hhrg41767/html/CHRG-105hhrg41767.htm> (Accessed March 2011).

4.3 Modeling Environmental Performance and Requests for Inspection Investigations

4.3.1 Description of Inspection Requests and Findings, 1994-2007

Previous studies have documented individual Inspection cases in great detail (e.g., D. Clark, et al., 2003). The purpose of this research is to understand whether past safeguard performance is a good predictor of Inspection requests and findings of noncompliance, in addition to understand how Inspection cases influence lending decisions about environmentally-risky projects. The vast majority of Inspection cases have been requested for World Bank projects, likely owing to its large portfolio and ability to attract international attention (Figure 6). For the purposes of this analysis, the African Development Bank is excluded because approval for an Inspection function was only finalized in 2004, and it took until 2007 for the first claim to be filed.

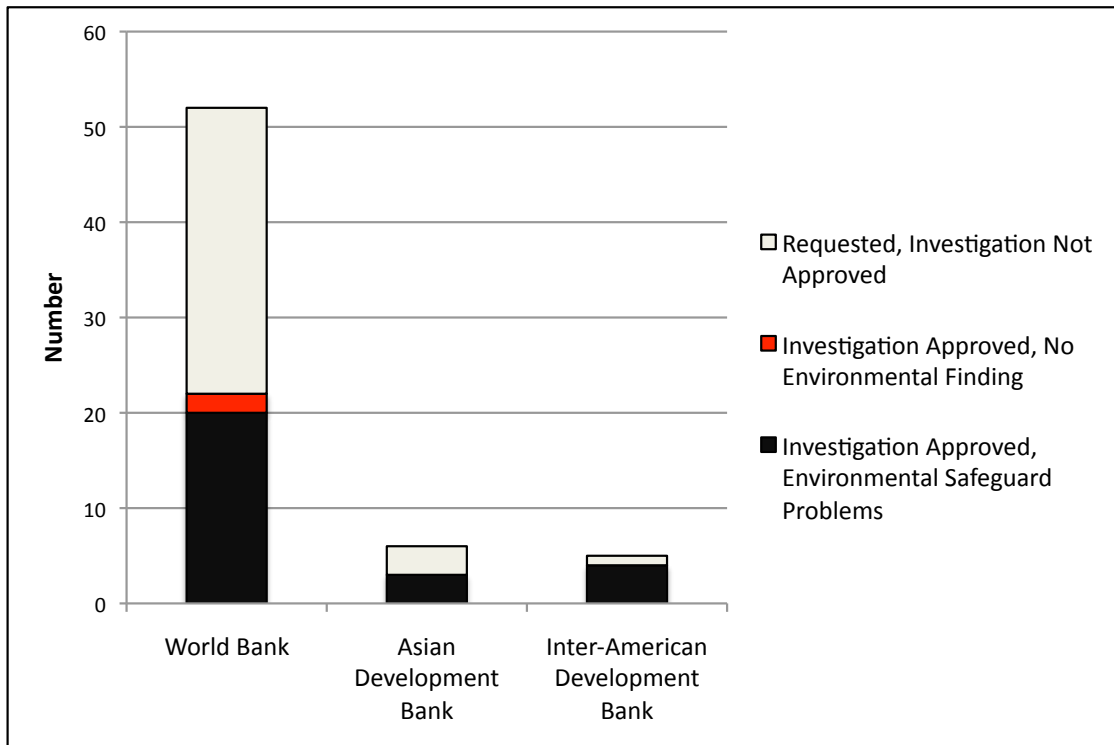


Figure 6: Description of Inspection Requests, 1994-2007

4.3.2 Factors Contributing to Inspection Panel Requests

The primary purpose of this section is to test whether establishment of the Inspection processes has created a “learning by doing” process whereby Inspection cases (NO. PREVIOUS INVESTIGATIONS) are less likely to be repeated within particular country lending programs, as stated in Hypothesis 1. However, there are several other potential predictors of Inspection requests and investigations that should be controlled for when modeling which borrowing countries are subjected to Inspection requests.

It is possible that establishment of the Inspection process simply reinforces performance information that the MDBs have already collected through project evaluations. As demonstrated in the previous chapter, both the World Bank and Asian Development Bank respond strongly to information about safeguard performance contained in project evaluations. Thus, if poor safeguard implementation performance

predicts Inspection requests and investigations, then the root causes of lending responses to safeguard performance would have to be carefully teased out. On the other hand, if Inspection cases are independent of general safeguard performance as documented in project evaluations, then it may be possible that multiple streams of performance information exert important influence on environmentally risky lending decisions. Thus, in order to test whether general safeguard performance is a good predictor of Inspection requests, I control for past safeguard performance using the variable SAFEGUARD REPUTATION, which is a model-based variable of expected environmental performance for any given country-year.¹⁰ Similarly, it is possible that the MDBs respond to the overall record of countries in achieving project outcomes, thus I generate the variable OVERALL REPUTATION to control for the expected overall performance of a project during any given country-year.

In addition, to be a likely target for an Inspection request, a borrowing country should have both a past history of receiving environmentally risky-projects and have a vibrant civil society. Thus, I include as controls the number of environmental NGOs that exist within a particular country-year (ENGOs) as documented in various editions of the *Environment Encyclopedia and Directory*. This includes both domestic and international NGOs that have physical offices and activities in the host country. In addition, I control for the number of projects flagged as requiring environmental impact assessments during the five years prior to any particular country-year (No. RISKY 5YR.). I employ a random-intercept probit model to account for other unobserved sources of heterogeneity between countries (Gelman & Hill, 2007, Ch. 14).

¹⁰ The procedure used to generate this variable is described in (Buntaine, 2011).

4.3.3 *Model Results*

Not initially confirming Hypothesis 1 for the World Bank, I find that borrowing countries with previous Inspection investigations do not have a decreased probability of being subjected to additional Inspection requests in future years (Table 4, Models 1a-b). However, upon closer examination of the data, I find that India is exerting strong leverage on the regression results, being the only country in the sample that has been subjected to four independent Inspection requests that allege environmental damages. Thus, if I remove India from the panel, I find that having a prior Inspection investigation is a strong predictor that projects in a borrowing country will not be subjected to additional Inspection requests (Model 1c).¹¹ This result suggests that the World Bank is able to adjust its operations to avoid repeated Inspection requests, confirming that the Inspection Panel has accomplished its primary function of promoting learning for better environmental performance.

¹¹ Further examination of the timing of Indian Inspection Panel requests confirms that omitting India from the panel is a reasonable modeling approach. The first Inspection Panel request alleging environmental damages was received on May 1, 1997 for the NTPC Power Generation Project. The three other Inspection requests alleging environmental damages and received through the end of 2007, two were approved prior to the first inspection request. In later years, India has sharply decreased its lending for environmentally risk projects in response to long delays and consistent civil society resistance (Operations Evaluation Department [OED], 2006).

Table 4: Requests for Inspection/Compliance Investigations at the World Bank

Model	1a	1b	1c
MDB	World	World	World
NO. PREVIOUS INVESTIGATIONS	-0.14 (0.21)	0.23 (0.20)	-0.75* (0.41)
SAFEGUARD REPUTATION	0.92* (0.55)	0.97* (0.57)	1.32** (0.04)
OVERALL REPUTATION	-0.14 (0.27)	0.05 (0.25)	-0.37 (0.30)
ENGOS	0.02** (0.01)	0.01** (0.01)	0.02** (0.01)
No. RISKY 5YR.	0.05** (0.02)	0.01 (0.02)	0.05* (0.03)
Random Intercept Variance	0.409	0.021	0.510
Data Subset	Full Panel	Received "A" in last 5 yrs.	Full Panel except India
Observations (Countries)	1496 (139)	541 (75)	1481 (138)
Residual Deviance	284.2	189.0	253.8
Null Deviance	300.2	197.8	272.7

Null Deviance is calculated using country random intercept as only predictor
 Statistical significant indicators are: * $p < 0.10$; ** $p < 0.05$

Because both the Asian Development Bank and the Inter-American Development Bank have only a few Inspection requests (see Figure 6), an examination of the predictors of Inspection requests using regression analysis is not possible. However, it is worth noting that Hypothesis 1 is entirely consistent with the observations that do exist (see Ragin, 2006). For the Asian Development Bank, there have been no repeated, independent requests for a Compliance investigation alleging poor environmental performance within a single borrowing country. Likewise, for the Inter-American Development Bank, only Argentina has been subjected to two, independent Inspection requests, and of these requests, only one was approved by the Board for Inspection.

In addition to previous Inspection requests, two other predictor variables are noteworthy. Contrary to the expectation that poor safeguard implementation performance in a particular country would increase the probability of Inspection

requests, I find that borrowing countries with *better* safeguard performance as recorded in project evaluations are much more likely to be subjected to Inspection requests for the World Bank (Table 4, Models 1a-c). This is a curious finding, indicating that countries subjected to Inspection Panel requests alleging environmental damages are not the countries with poor records implementing environmental safeguard policies. Thus, the Inspection process seems more able to identify one-time failures than it does in identifying systematic environmental safeguard implementation issues in a particular World Bank borrowing country. To check whether selection problems are causing this result, I specify Model 1b, which only includes the subset of country-years where an environmentally risky project was approved during the previous five years, thus avoiding countries that are less likely to be targets for Inspection requests. The predictor variable remains significant in this specification.

Interpretation of these results likely hinges on the strength of environmental civil society (proxied here by the number of domestically-based environmental NGOs) in the particular borrowing country.¹² As can be seen in Models 1a-c, the count of environmental NGOs in a particular country-year is a strong predictor of whether a project is targeted for an Inspection request.¹³ This means that in addition to receiving projects that are likely to make a borrowing country a target for an Inspection request, a constellation of environmental civil society groups needs to be available to supply the request. As shown with the 90%-confidence model prediction plot in Figure 7, projects in all borrowing countries, regardless of past requests, received more requests as the number of environmental NGOs increases. However, project in borrowing countries

¹² In the future, it may be important to further distinguish between the types environmental NGOs, particularly those that have strong connections of transnational advocacy networks. It might be expected that such NGOs have an even larger influence on supply Inspection requests (Keck & Sikkink, 1998).

¹³ Fredriksson, Neumayer, and Damania (2005) report the total number of environmental NGOs, using the 1994, 1997 and 2001 editions of the Environment Encyclopedia and Directory. Buntaine and Parks (in review) separately compiled data on the total number of environmental NGOs from the 2005 edition.

with previous Inspection requests are much less likely to receive additional Inspection requests, indicating operational learning on the part of the MDBs.

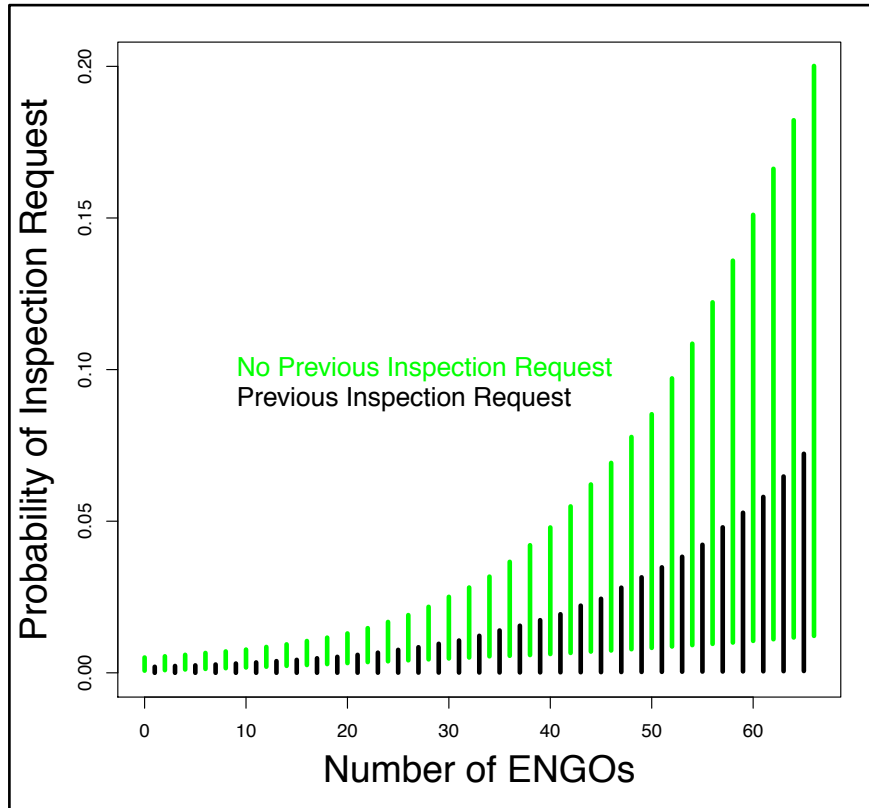


Figure 7: Predictive Probability of Receiving an Inspection Claim in a Given Years (Model 1c)

For the Asian Development Bank, I do not find that safeguard performance as reflected in project evaluations is a predictor of Inspection requests in set relational terms. Of the country-years where an Inspection request was made, one observation had more satisfactory safeguard implementation ratings than marginal/unsatisfactory ratings, one observation had the same amount, and three observations had fewer satisfactory safeguard implementation ratings than marginal/unsatisfactory ratings. Given the small size of this sample, I am not able to confirm the result using regression methods. Because the Inter-American Development Bank did not produce independent

project evaluations during the time period under consideration, I am unable to conduct a similar analysis.

To sum up, I do find support for Hypothesis 1 that the MDBs learn from prior Inspection investigations within the context of country programs. However, this result could come about in two ways. First, the MDBs could be exhibiting risk-aversion to infrastructure projects and simply decrease the amount of financing available for this type of project. Second, the MDBs could be learning from past mistakes and avoiding Inspection requests by improving implementation performance. The next section examines these possibilities.

4.4 Inspection Panel Cases and Aversion to Environmentally Risky Lending

4.4.1 Description of Environmentally Risky Project Data

This section tests whether countries that experience Inspection investigations are less likely to receive environmentally risky projects in future periods (Hypothesis 2a-b). It turns out that while projects flagged as needing environmental impact assessment because of their negative environmental risks are mostly large infrastructure projects, many environment-improving projects are also classified as risky. Thus, to the extent that the Inspection Panels are causing risk-aversion to these projects, it may be the case that fewer environmental interventions are approved. Thus, to examine this possibility, I split environmentally risky projects between “dirty” projects and “green” projects for the purpose of modeling.¹⁴ For comparative purposes, the total amount of “dirty” and “green” risky projects for each of the MDBs is displayed in Figure 8.

¹⁴ For both the World Bank and Inter-American Development Bank, “Green-Risky” projects are both flagged as requiring an environmental impact assessment by the MDB and classified as having a primarily environmental purpose in the AidData coding scheme.

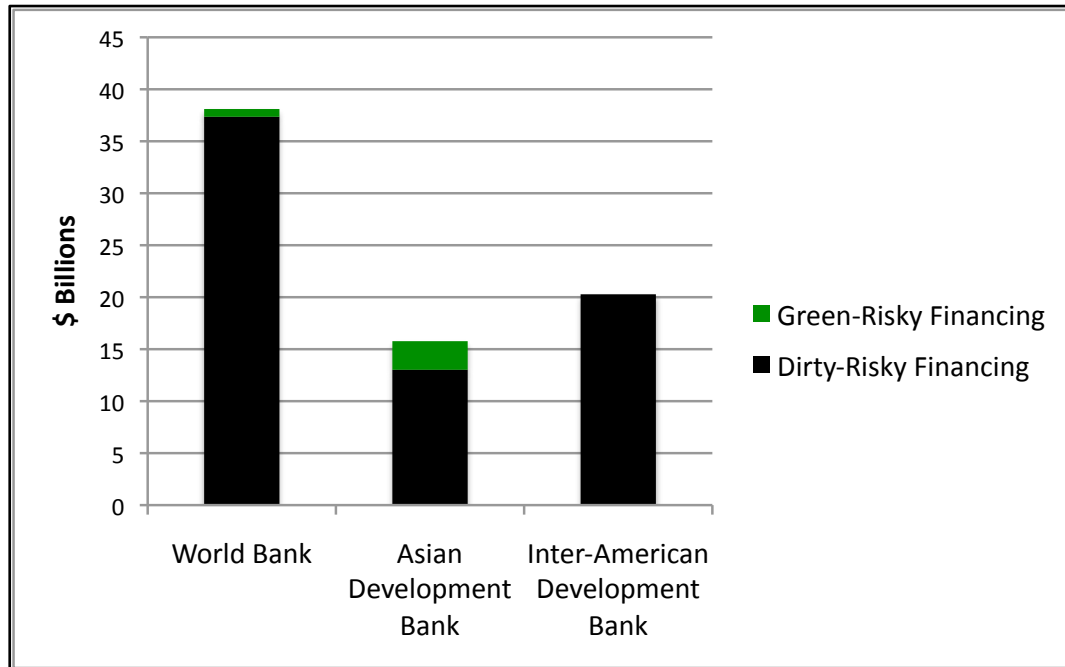


Figure 8: Total Amount of Environmentally Risky Financing, 1996-2007

4.4.2 Factors Contributing to Approval and Allocation of Risky Projects

The primary purpose of the models presented in this section is to test whether borrowing countries that have been subjected to previous Inspection investigations (PANEL INVESTIGATIONS) have a lower probability of receiving an environmentally risky project during any given year and when they do receive a risky project, whether its value is lower (see Hypotheses 2a-b). In addition, I control for the borrowing country's performance implementing environmental safeguards (SAFEGUARD REPUTATION), its overall project outcome performance (OVERALL PERFORMANCE), and the World Bank Institutes measure of government effectiveness (GOVT.EFFECTIVE), to control for more general indications of implementation performance.

Given that opposition to environmentally-risky projects originates with civil society groups, it is also possible that the MDBs avoid risky projects in borrowing countries where opposition is likely. Thus, I include the Freedom House index for civil

liberties (LESS CIVIL LIBERTIES) and the count of environmental NGOs (ENGOs) as control variables.

Approval and allocation decisions are also likely to be influenced by characteristics of the country portfolio that have little to do with different streams of information about performance or the probability that there will be opposition to environmentally risky projects. Borrowing countries that receive more total projects during any given year (NO. PROJECTS) should also be more likely to receive at least one environmentally risky projects. Likewise in the allocation model, countries that have a larger total lending amount during a given year (PORTFOLIO SIZE), should receive greater financing amounts for all projects. In addition, countries that primarily borrow from concessional lending windows (CONCESSIONAL), such as the World Bank's International Development Association, are likely to have fewer and smaller projects that may carry decreased risks. As described in the previous chapter, the approval model is a random-intercept probit, while the allocation model is a random-intercept linear model.

4.4.3 *Model Results*

For traditional development projects that are also environmentally risky, having prior Inspection investigations actually *increases* the probability of receiving risky projects in future period, contrary to the prediction of Hypothesis 2a. I find this result for both World Bank and Asian Development Bank decisions about traditional development projects that are flagged as environmentally risky (Table 5, Models 2,4). While I was not able to specify the same model for the Inter-American Development Bank, owing to the lack of project evaluations, I also do not find any support that borrowing countries that are subjected to Inspection requests are less likely to receive risky projects in future periods (Model 6). For both the World Bank and Asian

Development Bank, I find that past Inspection investigations have no influence on the approval of risky, environmentally targeted projects (Models 3,5).

Table 5: Influence of Inspection Panel Investigations on Environmentally Risky Project Approval Decisions

Model	2	3	4	5	6
Bank	World	World	Asian	Asian	IADB
Outcome Variable	dirty-risky	green-risky	dirty-risky	green-risky	dirty-risky
PANEL INVESTIGATIONS	0.27* (0.14)	0.10 (0.30)	1.07** (0.51)	-0.45 (0.69)	0.05 (0.24)
SAFEGUARD REPUTATION	0.12 (0.30)	0.87 (0.68)	-0.65 (0.57)	-0.53 (0.59)	
OVERALL REPUTATION	0.16 (0.15)	-0.54 (0.34)	-0.48 (0.49)	-0.49 (0.54)	
GOVT.EFFECTIVE	0.21 (0.15)	0.84** (0.40)	1.17** (0.40)	1.46** (0.50)	0.47* (0.25)
ENGOS	-0.00 (0.00)	0.03** (0.01)	0.02 (0.02)	0.02 (0.02)	0.01 (0.01)
LESS CIVIL LIBERTIES	0.21** (0.05)	0.24** (0.12)	0.60** (0.15)	0.38** (0.14)	0.16 (0.16)
NO. PROJECTS	0.17** (0.02)	0.08** (0.04)	0.09** (0.04)	0.13** (0.04)	0.23** (0.04)
CONCESSIONAL	-0.24 (0.15)	0.36 (0.40)	-0.16 (0.37)	-0.32 (0.49)	
Time Dummies	neg., 3+ gap*	n.s.			
Random Intercept Variance	0.092	0.066	0.245	0.061	0.081
Data Subset	Eligible Years	Eligible Years	Eligible Years	Eligible Years	Full Panel
Observations (Countries)	1062 (126)	1062 (126)	204 (34)	204 (34)	258 (26)
Residual Deviance	793.3	120.4	137.4	84.7	252.0
Null Deviance	877.2	140.8	173.7	108.6	307.3

Null Deviance is calculated using random country intercept and time dummies (if in regression) as predictors
 Statistical significant indicators are: * p < 0.10; ** p < 0.05

The result that borrowing countries that have been subjected to Inspection investigations are *more* likely to receive risky projects in future years is surprising, especially given MDB staff fears about the Inspection process causing project avoidance. The results shown in Table 5 demonstrate that the Inspection process is not causing the

MDBs to become more risk-averse about traditional infrastructure projects. Thus, the finding that the Inspection Panel induces improved safeguard performance discussed above is clearly not driven by the MDBs simply choosing to avoid environmentally-risky projects following Inspection investigations.

It is also notable that countries with lower levels of civil liberties and higher measures for government effectiveness were more likely to receive environmentally risky projects across the MDBs and across both “dirty” and “green” projects (Table 5). On civil liberties, this finding indicates that borrowing countries and the MDBs are more likely to finance environmentally-risky projects in the places where they could expect lower opposition from civil society because civil society groups have less ability to associate freely, express their views, and have access to the rule of law. At the same time, environmentally risky projects do seem to be approved for countries with higher broad measures of government effectiveness, indicating that the MDBs are concerned about implementation capacity in their approval decisions.

It is also possible that Inspection investigations would not decrease the probability of having an environmentally risky project approved during a given year, but would rather decrease the amount of financing allocated to environmentally risky purposes (Hypothesis 2b). For the World Bank, I do not find support for this hypothesis (Table 6). Neither being subjected to an Inspection investigation, nor having the Inspection Panel confirm poor safeguard implementation decreases the total amount approved for activities that were found to be risky. This result holds for the Asian Development Bank and the Inter-American Development Bank (omitted for brevity), where the only significant predictor of the amount of environmentally risky financing was the size of the particular country portfolio. This finding lends further support to the

finding that the Inspection Panels have not induced risk-aversion among the MDBs, but have rather improved implementation performance.

Table 6: Influence of Inspection/Compliance Panels on Environmentally Risky Allocation Amounts at the World Bank Conditional of Receiving a Project

Model	8a	8b	9a	9b
Outcome Variable	all risky	all risky	dirty-risky	dirty-risky
SAFEGUARD REPUTATION	-52.0 (73.4)	-39.7 (75.2)	-56.0 (76.1)	-43.1 (78.1)
OVERALL REPUTATION	-10.2 (31.6)	-7.47 (31.7)	-9.10 (33.3)	-6.70 (33.5)
PANEL INVESTIGATIONS	40.6 (25.5)		40.9 (26.4)	
PANEL FINDINGS		33.7 (30.1)		34.2 (31.2)
ENGOS	-1.96 (1.47)	-1.82 (1.47)	-3.67** (1.67)	-3.49** (1.67)
LESS CIVIL LIBERTIES	45.5** (14.8)	44.5** (14.8)	44.8* (15.3)	43.8** (15.4)
GOVT.EFFECTIVE	48.3 (42.3)	43.5 (42.3)	57.0 (44.1)	52.5 (44.1)
CONCESSIONAL	-47.4 (46.5)	-46.3 (46.8)	-52.3 (48.7)	-50.9 (49.0)
PORTFOLIO SIZE	0.33** (0.02)	0.33** (0.02)	0.33** (0.02)	0.33** (0.02)
Time Dummies	n.s.	n.s.	n.s.	n.s.
Random Intercept S.D.	105.3	106.3	108.8	109.7
Data Subset	Years with Risky Project	Years with Risky Project	Years with Dirty-Risky Project	Years with Dirty-Risky Project
Observations (Countries)	203 (65)	203 (65)	194 (63)	194 (63)
Model Likelihood	-1283	-1284	-1229	-1229
Null Likelihood	-1388	-1388	-1327	-1327

Null Deviance is calculated using country random intercept as only predictor
Statistical significant indicators are: * p < 0.10; ** p < 0.05

Similar to the approval stage models presented in Table 5, for the World Bank I find that borrowing countries will receive more “dirty-risky” projects if they have lower numbers of environmental NGOs and lower levels of civil liberties. Thus, it appears that

they logic of avoiding risky projects in the countries where significant opposition could be expected extends beyond approval decisions to the amount of “dirty-risky” financing approved.

To sum up, the models presented in this section have revealed a number of important findings: (1) Being subjected to Inspection investigations *does not* decrease a country’s probability of receiving environmentally risky projects in future period; (2) being subjected to Inspection investigations *does not* decrease the amount of risky financing that a country receives, conditional that it receives at least one risky project; (3) the MDBs are more likely to approve environmentally risky projects for borrowing countries where there is less likely to be civil society opposition. Given the “learning” hypothesis was supported in the previous section, it would appear that the Inspection process has served mainly to increase compliance, rather than to cause risk-aversion. These findings are compared to interviews of MDB staff about the impact of the Inspection process on lending decisions in the next section.

4.5 Extending Model Results with MDB staff interviews

From 2008-2010, I conducted semi-structured interviews with 54 MDB staff members. In general, I sought to interview the widest possible range of operational and evaluation staff in order to capture the full variation in observations about how the Inspection process influenced lending decisions. My interviews were often based on “snowball sampling,” with interviewees suggesting additional contacts in order to capture a wider variation in observations (Goldstein, 2002). In each interview, I utilized a semi-structured interview template and asked about what incentives the Inspection process created among operational staff, both in general and following Inspection requests. I also ask operational staff about ways they have seen approval and allocation

decisions influenced by the Inspection process in response to these incentives. I guaranteed all interviewees anonymity in order to generate candid responses.

Staff across the World Bank, Asian Development Bank, and Inter-American Development Bank reported that establishment of the Inspection processes were likely be primary routes through which performance information about environmentally risky projects impacted lending decisions. It was commonly reported that the costs to individual staff members career prospects for being involved in an Inspection cases were high. This cost was most frequently emphasized among World Bank evaluators and operational staff. In particular, evaluation staff believed that Inspection cases would have more of an impact on lending decisions than evaluation findings. Inspection Panel cases lead to actual costs to operational staff and the likelihood of Inspection requests is less predictable since they originate from outside of the Bank, leading to a much higher degree of caution on implementing environmental safeguard policies than might result from recommendations that come out of project evaluations. A recent Inspection Panel case in Albania resulted in the firing of a World Bank staff member, which is almost unheard of within the World Bank, and a result that never comes about due to evaluation findings.¹⁵

Operational staff within the World Bank, including one staff member who had recently been involved in an Inspection case, reported a high level of “neck protection” behavior among staff in World Bank operational departments involved in environmentally-risky project designs. While staff cannot avoid the risks associated with Inspection investigations entirely, project design teams often avoid project components that might lead to significant individual risks. In addition, the World Bank might fund

¹⁵ For more information on the Integrated Coastal Zone Management and Clean-Up Project case see: <http://web.worldbank.org/WBSITE/EXTERNAL/EXTINSPECTIONPANEL/0,,contentMDK:22512600~pagePK:64129751~piPK:64128378~theSitePK:380794,00.html> (Accessed April 2011).

only the lower-impact components of much larger, riskier infrastructure projects.¹⁶

According to another operational staff member, this behavior is elicited because Inspection cases take up management and staff time for months, which detracts from the ability of higher-level management to “push the pipeline” and reach lending goals. A policy staff member involved with coordinating management responses to Inspection cases reported that preparing a management response to an Inspection investigation takes a great deal of time and care in order to avoid upsetting donor relations.

Despite the reported behavior of avoiding the most risky project components, one of the most clear organizational impacts of the Inspection Panels has been the establishment of project management systems that are in place to avoid Inspection cases, possibly accounting for the “learning” finding related to Inspection cases that I find above. For example, according to one staff member, the World Bank Operations Policy and Country Services office has among its primary goals to “keep projects out of the Inspection Panel” by making sure that the Board is properly appraised of the risks involved with different policies and that safeguard policies are implemented with due diligence. One staff member reported that the shareholder states primarily sanction the management of the World Bank through approval and disbursement delays when they are “surprised” by allegations of poor implementation. When this happens, Inspection cases tend to become “high-profile” and attract significant attention by both donor shareholder states and external civil society groups. Thus, the World Bank has put systems in place to ensure safeguard policies are carried out with due diligence and that environmental risks are transparent to donor countries.¹⁷

¹⁶ This is reflected, for example, in the preference taken by the World Bank to fund electricity transmission projects over electricity generation projects in many places.

¹⁷ A copy of the rules and procedures used by the World Bank in preparing environmental impact assessments, for example, is available at: <http://www.env.go.jp/earth/coop/coop/document/10-eiae/10-eiae-7.pdf> (Accessed March 2011).

Among the Asian Development Bank staff that I interviewed in different departments and managerial levels, there were a variety of opinions about whether the Inspection process has caused “risk-aversion,” but near universal agreement that very specific safeguard procedures have been put in place to avoid the external risks associated with Inspection requests. In particular, the Asian Development Bank has created a very detailed “checklist” about project design requirements that is intended to shield staff members from Inspection investigations.¹⁸ Many operational staff members reported that the Asian Development Bank follows a Japanese style of management that seeks to address risk through procedure. One staff member stated that 90% of effort implementing safeguard policies occurs during project design. Indeed, this process can be seen as mostly successful, given that there have been very few high-profile Inspection cases. One operational staff member reported that the Chashma Right Bank Project, which was designed and approved during 1991-1992, has received the most attention within the ADB over its Inspection investigation. However, by the time that the Investigation requests were received in 2002 and the investigation was completed in 2004, the ADB had already moved away from large-scale irrigation projects. This left little room for the Bank to respond to the Inspection investigation in its decisions about lending.

Similar to the World Bank, Asian Development Bank operational staff reported that lending decisions are shying away from project components that might trigger Inspection requests. Thus, it may be the case that Inspection requests are generally not causing risk-aversion, but rather that the general threat of Inspection requests requires

¹⁸ A copy of the rules and procedures used by the Asian Development Bank in preparing environmental impact assessments, as well as the operational “checklists,” is available at: http://www.adb.org/documents/guidelines/environmental_assessment/environmental_assessment_guidelines.pdf (Accessed March 2011).

so much caution while implementing projects that there is an emerging consensus to avoid high-risk *project components*. For example, the Asian Development Bank has been involved in the Nam Theun II dam project for many years now and has devoted an extraordinary amount of resources to ensure that best-practice safeguard are diligently implemented. However, given continued delays and requests by local people for more studies to be conducted, additional compensation to be paid, etc., several staff members believed that the ADB would not pursue similar projects in future periods. The Jumana Bridge project in Bangladesh has met with significant delays owing to the difficulty of fully implementing safeguard policies. Thus, given the possibility of “losing face” at both the individual and organizational level if an Inspection case is triggered, the ADB is forced to undertake costly actions that may be affecting the cost-benefit calculations for large, risky infrastructure projects.¹⁹

One ADB operational staff stated that the main impact of the Inspection Panel has been that staff should not pursue projects that are “unnecessarily difficult” in terms of implementing safeguard policies. I was able to find instances where the Asian Development Bank funded less-risky components of larger projects. For example, one staff member reported that the Asian Development Bank financed a portion of the Laos Northern Economic Corridor project, but the more risky portion was financed by the Chinese government, which has caused some implementation difficulty and calls to coordinate safeguard policies. In addition, the level of civil society engagement on safeguard policies in particular borrowing countries has a large effect on what staff consider to be “unnecessarily difficult,” which was reported to be a reason why China has received many more risky projects than India over the past decade. However, the

¹⁹ One exception might be the recent emphasis and reengagement in hydropower, given international goals to increase power generation while decreasing emissions. For example, see the recent *Directions in Hydropower: Scaling Up for Development* (World Bank, 2009b).

data reported above suggest that avoiding difficult project components does not mean that fewer projects will require environmental impact assessments.

Several ADB staff reported that Inspection Panel investigations had a “chilling” effect within specific country-sectors. For example, after the Sri Lanka Southern Transport Development case, transportation became a “no touch” sector for staff in Sri Lanka. It may also be the case that this Inspection investigation slowed lending for transportation across the ADB portfolio. In the future, it will be important to examine the sector effects of Inspection cases, as lending decisions may be influenced at this level.

Inter-American Development Bank staff reported less of a reaction to the establishment of an Inspection Panel. One division manager reported that the IADB does not face the same level of NGO or US Congressional scrutiny as the World Bank, which is located right down the street. This has resulted in a weaker Environment & Safeguards Unit, because there has been less of a need to put up a robust defense against civil society claims of poor implementation. In addition, unlike the World Bank and Asian Development Bank, less-developed borrowing countries have a majority on the Board, which has resulted in less focus on environmental safeguard policies. However, some operational staff did anticipate that the Inspection Panel had caused a “chilling” effect at the sector level, specifically as related to hydropower projects, which have been the subject of more than half of requests.

It is also interesting to contrast the MDBs considered in the models above with the African Development Bank, which just established an Inspection Panel in 2004 and did not receive an Inspection request until 2007. Operational staff reported a growing recognition that failure to implement safeguard policies would entail financial risks because of the Inspection panel. Still, this recognition is nascent. One director who oversaw an infrastructure group reported that he was “not afraid” of civil society

groups like the World Bank. He pointed to the differences in organizational responses to the Gebay III hydropower project being cofinanced by the World Bank and AFDB. The World Bank is still mired in studies about the project because of concerns raised by civil society groups like the International Rivers Network, while the AFDB has moved forward. This illustrates that the Inspection process may have increased the emphasis that the MDBs that have experience Inspection cases have paid to protecting themselves against future cases. As the US and Nordic executive directors at the AFDB push the organization to improve safeguard performance and strengthen the Inspection process, this change might also reach the African Development Bank. For example, the Bugali Dam project recently came up for Inspection. The response was to conduct further studies, rather than to abandon the project.

4.6 Conclusions

The model results and interview data presented indicate that because Inspection requests tend to be filed against projects in *high-performing* countries, the MDBs have responded by upgrading their environmental safeguard practices, rather than changing decisions about how to allocate risky projects. This result suggests that environmental civil society groups can drive improved environmental performance at the MDBs, even if they are not able to directly influence broader approval and allocation decisions through the Inspection process. Instead, higher levels of civil liberties result in fewer environmentally-risky projects controlling for other factors, indicating that civil society groups mainly influence approval and allocation decisions based on their influence over borrowing country demand for environmentally-risky projects.

Previous scholarship has questioned whether it is possible to hold IOs accountable for technical performance, given that states may sometimes have little ability or desire to practice oversight themselves. Creation of the Inspection Panels is

one of the most important experiments in civil society-IO accountability. The results here show that this type of oversight can be very useful at driving the MDBs to improve their practices, even while not causing the MDBs to lose focus on infrastructure development that may be keep for economic growth and poverty reduction in borrowing countries. This type of oversight is especially important, given that donor countries would like to see due diligence implementation of safeguard policies, but that civil society groups are often best positioned to monitor safeguard implementation performance. While it does not appear that the Inspection Panels have changed overall lending practices, it is clear by allowing civil society groups to more easily provide information about implementation problems, MDB incentives to diligently implement safeguard policies have increased.

More broadly, this finding shows that the threat of sanctioning can induce improved implementation at the development banks. Previous research has shown that high level threats by donor countries to withhold financing have produced environmental policy reforms, but not necessarily the due diligence implementation of these new policies (Gutner, 2005; Nielson & Tierney, 2003). Because MDB member states are not often in a position to gather the type of information necessary for effective oversight of environmental policies, extending the possibility for civil society groups to submit claims appears to have been crucial to achieving better implementation of safeguards. Other international organizations, especially those involved with development, would do well to consider providing this type of oversight to ensure that development resources are spent wisely.

More generally, this shows that the “hidden hand” of sanctioning is more important at causing changes to IO behavior than the actual event of sanctioning (Drezner, 2003). Implementation performance improves under the provision of

information and the threat to incur costs for low performance. This indicates that if states wish to cause IO behavioral change, there need to be ways to monitor performance in ways that automatically trigger oversight. As Dai (2007) explores, civil society groups may be particularly adept at providing this type of oversight to improve IO performance. Notwithstanding, scholars have raised concerns that the environmental activity of civil society groups in driven by groups in developed countries, calling into question the broader effect of accountability apart from MDB projects (Linaweaver, 2003).

Several questions are left unanswered by this inquiry. First, it may be possible that risk-averse behavior is observed mostly at the sector level, rather than at the country level. This proposition could be explored by further sub-dividing environmentally risky projects into sector types. Second, both the Asian Development Bank and African Development Banks have recently revised their Inspection processes to include a “consultation phase” between civil society claimants and bank management. This has prevented many projects from automatically going to Inspection, and may serve to either enhance or detract from implementation performance. The relative balance of accountability and consultation and their effects on MDB behavior will be important considerations in the years ahead. Overall, however, it appears that civil society groups can play an important role in providing oversight for IOs to ensure high-quality implementation without causing risk-aversion to traditional development projects.

5 Approval and Allocation Decisions about Environment-Improving Projects

5.1 Introduction

During the last two decades, environmental protection and management has become a priority for development donors. International donor organizations have not only incorporated environmental goals into traditional development projects, but have also rapidly increased their support for projects that have a primary goal of improving environmental management in less-developed countries (Findley, et al., 2009; Hicks, et al., 2008). The multilateral development banks (MDBs) have played a prominent role in this transition, managing more than half of international environment-improving project financing, which amounts to more than \$6 billion annually (Hicks, et al., 2008). At the present, the multilateral development banks have all identified environmental management as a primary organizational concern and have given a prominent role to environmental financing in their strategies for lending.¹

Despite the prominence that environment-improving financing has gained in MDB portfolios, environment-improving projects and environmental project components within development projects have a mixed implementation record. Borrowing countries have demonstrated everything from negligence to highly satisfactory performance when implementing environment-improving projects and activities. On the negative side, an evaluation completed by the World Bank Independent Evaluation Group in 2005 found that environment-improving projects had one of the lowest success rates across different sectors of the lending portfolio

¹For example, the Asian Development Bank approved “Strategy 2020” in April 2008, which lists “environment” as one of the five main operational and lending areas during the following decade covered by the plan. The World Bank adopted an organization-wide Environment Strategy in 2001, which prioritized environmental management throughout the lending portfolio.

(Operations Evaluation Department [OED], 2005b). Several World Bank environment-improving projects have been subjected to the high-profile Inspection Panel process and canceled for failing to protect local people from pollution during project implementation.² An Asian Development Bank evaluation of joint ADB-GEF projects found examples of unsuccessful environment-improving projects that lacked “adequate ownership and clear implementation arrangements, and... implementation capacity of the executing agencies” (Operations Evaluation Department [OED], 2007a, p. vi). These issues were especially pronounced in projects like the Sundarbans Biodiversity Conservation Project, which was evaluated to be ineffective and was canceled due to implementation arrangements that were “inadequate given the weaknesses in governance capacity and practices in Bangladesh” (Operations Evaluation Department [OED], 2008, p. 6).

In contrast, a more recent evaluation of the World Bank portfolio found that more than 80% of pollution management and ozone-related projects successfully achieved their objectives (Independent Evaluation Group [IEG], 2008b). A World Bank report prepared to showcase successful projects touted results that included successful soil and conservation works for more than 200,000 hectares in India, solid waste projects in Bosnia and Herzegovina that improve the health of over half the population, and renewable energy, zero-emissions projects that have electrified communities in rural Nepal (World Bank, 2010). The Asian Development Bank has also funded several “highly successful” environment-improving projects, including the Shanxi Environmental Improvement Projects, which is “seen as [a] nationally important pilot project which can be replicated at local and national levels and have contributed to

² For Inspection Panel cases, see “Summary of Inspection Panel Cases,” available at: http://siteresources.worldbank.org/EXTINSPECTIONPANEL/Resources/Panel_Cases_2010_Nov_8.pdf (accessed February 2011).

national and provincial environmental policies” (Operations Evaluation Department [OED], 2007d, p.24). Indeed, reflecting such stories of success, some scholars have argued that the MDBs are uniquely positioned to finance global public goods like climate change mitigation (Gilbert, et al., 1999; World Bank, 2007).

This chapter tests whether MDBs respond to the past performance of borrowers in implementing environmental activities by increasing financing for successful borrowers. While there has been a great deal of conceptual and theoretical research about the sources of effective international environment-improving programs (Connolly, 1996; Haas, Keohane, & Levy, 1993; Independent Evaluation Group [IEG], 2008b, Ch. 7; Operations Evaluation Department [OED], 2007a), very few of the broad factors put forth in this line of research predict successful outcomes in environment-improving projects (Buntaine Parks, under review). Instead, donor agencies and organizations have increasingly recognized that projects need to be “demand-driven” and designed with an appreciation of the unique priorities and capacities of particular borrowing countries (Independent Evaluation Group [IEG], 2008b, p. xxxv). If this is the case, then adaptive responses to the performance of individual countries are necessary in order to make efficient use of scarce financing resources.

Since the MDBs manage the majority of international, environment-improving financing, it is important to understand whether their institutional design and relationships with other international actors supports an adaptive response to past performance information. Indeed, it has been suggested that donor countries delegate this financing authority to MDBs because they are shielded from the political influence of donor domestic constituencies and are better able to collect the rich information that is necessary to design and implement successful development portfolios (Milner, 2006; Rodrik, 1996). Scholars have highlighted the ability of IOs to process information as a

key reason why they might be more successful at managing environment-improving projects (Martens, 2005). If MDBs are able to direct financing to borrowing countries with good performance records, then they may indeed be well-positioned to be the primary mechanism to manage international environment-improving financing.

Contrasting more optimistic accounts of the MDBs, I argue that MDB institutional design and position relative to other international actors does not encourage them to respond to environmental performance as recorded in project evaluations, especially related to projects that produce global environmental goods. For clean-energy projects that address global climate change, the MDB donor countries have pushed for increased supply of climate investment, often without corresponding demand from borrowing countries. They do so because the benefits to global climate change projects are diffuse and because the support of clean-energy financing is a relatively low cost way to demonstrate a response to climate change internationally. Because the activities and incentives within the MDBs are still based around project approval, pressure from donor shareholders to rapidly increase the supply of climate change lending produces does not incentivize selectivity by MDB staff. In contrast, for urban environment projects that address problems confined within national borders, there is not as much lending supply pressure from donors, since benefits are localized. Thus, there can be a confluence between borrower need, borrower demand, and the MDB organizational necessity to approve projects, resulting in performance-based decisions about portfolio composition.

5.2 Responding to Environmental Performance

5.2.1 *Environmental Performance at the MDBs*

As introduced above, this chapter is motivated by the highly mixed record of environmental performance contained in MDB project evaluations. Given this mixed performance record, there is ample room to scale up environment-improving financing in high-performing countries and vice versa. This would ensure that scarce financing resources are used efficiently. Of the project evaluations with performance information about environment-improving project components, only 52% of World Bank evaluations, 44% of Asian Development Bank evaluations, and 32% of African Development Bank evaluations find satisfactory or highly satisfactory performance in meeting environmental goals (Figure 9). This data corroborates several thematic evaluations completed by MDB evaluation offices that highlight the mixed or “partially satisfactory” performance of bank-wide environmental programs (Asian Development Bank [ADB], 2009d; Independent Evaluation Group [IEG], 2008b; Operations Evaluation Department [OED], 2005b). Given the mixed nature of environmental performance at the MDBs, there are significant opportunities to increase the selectivity in allocation decisions to improve performance.

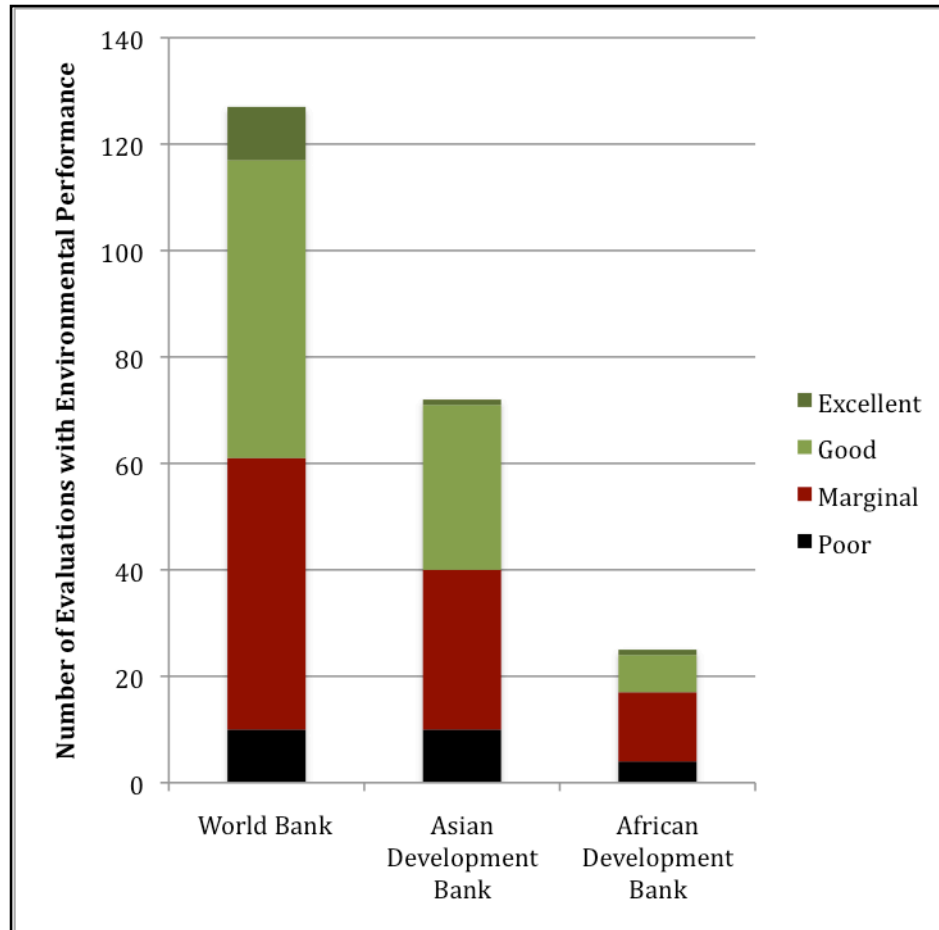


Figure 9: Coded environmental target performance ratings

5.2.2 *Independent Evaluation and Environmental Performance*

One of the primary ways that the World Bank, Asian Development Bank and African Development Bank have sought to become more responsive to the lessons generated by past operations has been strengthening the role of *independent evaluation* within their organizations. Recognizing that operational staff have few incentives to candidly evaluate their performance in achieving environmental goals, the shareholders states that made up the Board of Directors at the MDBs supported the creation of independent evaluation departments that reported directly to them, rather than to the

bank management.³ The stated purpose of independent evaluation has been to improve future operations through learning and accountability for performance. Indeed, a US report completed by the Government Accountability Office highlights the importance of independent evaluation for improving project performance and portfolio management (General Accounting Office [GAO], 1996). At the World Bank, the strengthening of independent evaluation during the 1990s responded to internal and external indications that the performance of projects was in decline (Picciotto, 2002).

The resources devote to independent evaluation have grown over time. Within each of the MDB evaluation departments, greater emphasis has been placed on assessing the environmental results of programming over time, corresponding to the adoption of policies at each of the banks that integrate environmental considerations into programming, as our research team observed in the amount of environmental performance information available at different times during the study period.

Project evaluations, which analyze the outcomes of individual projects, are the bedrock evaluation product on which other higher-level evaluations are constructed at the World Bank, Asian Development Bank, and African Development Bank. According to the preamble of World Bank project evaluations, the purpose a project evaluation is “to help develop improved directions, policies, and procedures through the dissemination of lessons drawn from experience.” Project evaluations generally compare the outcomes of a project against the targets that were set during project design, analyze the sources of success and failure in reaching project targets, and make

³ Independent evaluation departments were established at different times, but were all pushed by donor shareholders as a way to increase accountability. The World Bank Operations Evaluation Department (currently the Independent Evaluation Group) was established in 1975 and reported simultaneously to the Board of Directors and the President of the World Bank Group (see Grasso, et al., 2003). In 2001, the Asian Development Bank upgraded its evaluation office to become the Operations Evaluation Department, placing it on an equal organizational level to other departments. The African Development Bank Operations Evaluation Department began reporting directly to the Board of Directors as of 1995.

recommendations about future operations. As environmental protection and management has become a priority in MDB portfolios and more environment-improving targets are included in all types of projects, environmental target performance has become a regular part of project evaluations.

5.3 Institutional Positioning of the Multilateral Development Banks

When it comes to environment-improving projects, the MDBs face a number of internal and external incentives that shape approval and allocation decisions. In short, the MDBs must coordinate the lending supply preferences of their donor countries with the borrowing demands of recipient countries in order to achieve their primary function of approving and disbursing financing. Within the MDBs, there are very strong incentives for management and staff to choose projects that most easily solve this coordination problem, leading to what has been termed the “loan approval culture” (Svensson, 2003; Wapenhans, 1992). Operational departments are primarily responsible for ensuring that concessional financing is spent, in order to justify future replenishment by donor countries and that commercial lending is expanded, since it represents the main source of operating expenses for the MDBs (Vaubel, 1996; Weaver, 2007). As a consequence, career advancement for operational staff and management is largely dependent on the volume of lending that is approved and disbursed, rather than the outcomes and impacts of projects. Given the many projects are implemented over multi-year time horizons and that staff rotation within MDBs is extremely high, there are neither strong lines of accountability for project performance, nor significant incentives for management to prioritize project implementation and supervision, since these activities do not solve the central coordination problem facing the MDBs (Asian Development Bank [ADB], 1994; Wapenhans, 1992).

The institutional positioning and organizational incentives that operate within the MDBs have important implications for the ways that the MDBs respond to environmental performance when approving environment-improving projects. A 1998 World Bank report from the Environmentally and Socially Sustainable Development Network sums up these implications:

“Three main types of internal Bank problems negatively affect its [environment-improving] projects: (i) the incentives for task managers to promote large projects rather than skills transfer and improved management capacity; (ii) the project cycle, originally designed for infrastructure investments, is unsuited to a continuous, gradual capacity building effort; and (iii) blueprint solutions, which are inappropriate in the case of [institutional development] because of the individuality of countries and institutions.” (World Bank, 1998, p. 43)

Given the need to solve the lending supply and borrowing demand coordination problem, the MDBs are likely to approve large projects with low design and supervision costs. Because environment-improving projects rarely meet those criteria (Independent Evaluation Group [IEG], 2008b), absent strong lending supply preferences on the part of shareholding countries or demand from borrowing countries, few projects are likely to be pursued. Indeed, an examination of the MDB lending portfolios before the 1990s largely confirms this expectation (Hicks, et al., 2008, p. 33). Thus, because MDBs seek projects that most easily solve the donor-borrower coordination problem, decisions about environment-improving projects must be understood in terms of these external interests.

5.3.1 Donor countries

Ultimately, the authority of the MDBs to approve development financing is derived from their Board of Directors. The Board of Directors is comprised of the countries that fund the MDBs, with voting shares proportional to their subscription or contribution. At each of the MDBs, the Board not only approves individual projects (largely as a formality), but more importantly shapes and approves bank-wide and

sector-wide lending strategies. Although the Boards are made up of all the member states, in practice large members drive the overall lending priorities of the MDBs both as pivotal voters on the Boards and through having customary appointment power over the Bank presidents in the case of the World Bank (US) and Asian Development Bank (Japan) (Fleck & Kilby, 2006; Harrigan, et al., 2006; Schraeder, et al., 1998). Furthermore, only the largest shareholding countries at each MDB have their own Executive Directors, which makes it easier to exert influence as compared to smaller countries that must elect Directors as groups and face collective action problems (Lyne, et al., 2009). Since developed countries are the primary contributors to MDB concessional lending replenishments and capital increases, they exert considerable influence on broad policy shifts (Bowles & Kormos, 1999).

Broad increases in environment-improving lending at the MDBs can be traced back to the early-1990s, when there was a proliferation of interest among donor countries, and especially the US, to reduce the environmental damages of MDB development projects and increase lending for environment-improving activities (Bowles & Kormos, 1999). Indeed, the formation of the Environmental Department at the World Bank resulted from the US threatening to withdraw support for the replenishment of the World Bank Group's International Development Association (IDA) absent reforms to improve environmental management in Bank projects (Nielson & Tierney, 2003). Strengthening the environmental safeguards policy and redoubling a commitment to environmental lending were key commitments required by the US for a 2009 capital increase for the Asian Development Bank, with the US Executive Director on record stating that "a commitment to strengthened safeguards must be clear before any final consideration of an increase in the ADB's capital base" (Gopalakrishnan, 2009).

In the wake of the 1992 Rio Earth Summit, where an agreement was struck between developed and less-developed countries to finance environmental management activities in exchange for participation in several international environmental treaties, the development banks were pushed to prioritize proactive environmental management in their lending portfolios. Indeed, the 10th replenishment of the World Bank's International Development Association was completed in 1992 only after months of arduous negotiations when the Bank agreed to take on "new environmental responsibilities" (Brummer, 1992). Since this time, MDB environment-improving financing has taken two forms. First, the MDBs have undergone a process of "mainstreaming" the environment into their traditional development operations, which is the practice of including environment-improving project components into traditional development projects (Environment Division, 1995; Findley, et al., 2009) or integrating conservation and development activities (Barrett & Arcese, 1995).

Second, and more importantly for the analysis presented in this chapter, the MDBs increased their support for stand-alone environment-improving projects, oftentimes co-financing projects with organizations like the Global Environment Facility (Hicks, et al., 2008). These projects included financing for pollution control, sewerage and sanitation works, reforestation, and low-emissions energy development, among other types of projects. Throughout the 1990s and 2000s, donor countries have pushed lending for these projects. They likely do so because their own constituencies perceive these to be more important development issues than do political leaders in borrowing states. The donor countries are more attuned to the policy preferences of environmental NGOs based in their own borders, than to the development priorities of foreign groups and people. In addition to informing developed country preferences, civil society groups

from developed countries have special access to and influence on the World Bank because of its location in Washington, D.C. (Nelson, 2000).

Given donor lending supply preferences for environment-improving projects, the MDBs have been in a position to demonstrate to developed shareholders that they are “doing something” about the environment. This means persuading borrowing countries to accept projects that might not always be domestic priorities, a noted impediment of successful environment-improving financing (Connolly, 1996). Because donor countries have not been as critical of failures to achieve environment-improving goals as they have been of failures to mitigate damages associated with development projects, the management of the MDBs are mostly under pressure to *demonstrate action rather than results*. Indeed, the vast majority of summary program reports coming out of MDB environment departments focus on inputs and actions (i.e. amount of environment-improving financing; number of operations), as opposed to outcomes and impacts of environment-improving operations (e.g., Asian Development Bank [ADB], 2009d; World Bank, 2007).

Within environment-improving projects, the lending supply preferences of donor countries are strongest with regards to investments that mitigate environmental problems with transboundary externalities, such as tropical forest conservation and emissions that contribute to climate change. By supporting lending that addresses global environmental problems, developed donor countries directly accrue some of the benefits. By contrast, investment projects that focus on local environmental issues, such as sewerage or soil erosion, do not directly benefit donor countries. Thus, while these types of local environmental financing have received attention in international forums like the Millennium Development Goals process, they are not as likely to be pushed by donors without corresponding borrowing country demand. For these reasons,

developed shareholders have exerted the strongest lending preferences with regards to global goods issues. In particular, when large borrowing countries determine the provision of global public goods, developed shareholder countries must engage them in order to maintain the benefits of global environmental goods, since there are no other available suppliers. For these reasons, biodiversity conservation and climate change projects remain two lending areas that are substantially “donor-driven,” as reported by MDB staff members in interviews.

This lending supply preference is reflected in the statements the MDBs make about their project portfolios related to global environmental goods. For example, the IEG notes “the growing focus on climate change that responds in part to a 2005 request by G-8 countries for greater Bank Group international leadership” (Independent Evaluation Group [IEG], 2008b, p. 77). In a statement to the Asian Development Bank’s 40th Annual Meeting in 2007, the Japanese Minister of Finance highlighted climate change as one of the three major challenges in the Asian Pacific and argued that the ADB “should play a vital role in supporting efforts of the member countries to achieve energy efficiency.”⁴ Indeed, donor countries have been much more interested in the MDBs expanding their environment-improving operations than they are in having the MDBs be selective in their lending based on past performance, reinforcing the “do something” approach to approval and allocation decisions.

However, the preference for global environment-improving lending by donor countries has not decreased competing demands for economic growth and poverty reduction. Indeed, the MDBs have all redoubled their commitment to achieving economic development, even re-engaging in sectors such as hydropower that fell out of

⁴ Statement of Minister of Finance Koji OMI, 6 May 2007, available at: <http://www.adb.org/annualmeeting/2007/govs/am2007-jap.pdf> (Accessed February 2007)

favor due to the negative environmental impacts of projects (Asian Development Bank [ADB], 2009c). Gutner argues that the competing and sometimes irreconcilable goals of economic development have often caused the environmental performance of MDB projects and programs to be less than satisfactory (2002). Other authors have decried the “mission creep” of the MDBs and the operational conflicts that arise when the MDBs attempt to reconcile different goals (Einhorn, 2001). In an environment where the great majority of MDB development assistance is still directed towards promoting economic development, with environment-improving projects making up less than 5% of the MDB portfolios at most, the MDBs are under the most pressure to demonstrate development results.⁵ This serves to reinforce the “do something” approach to environment-improving finance, especially related to environmental issues that are important to the constituencies in donor countries.

Although the MDBs have all focused on developing monitoring and evaluation to improve effectiveness, at the behest of shareholder countries, there is less pressure to demonstrate selectivity to improve effectiveness for environment-improving projects. Although the MDBs are under considerable pressure to demonstrate success to external audiences (Bemelmans-Vidéc, Lonsdale, & Perrin, 2007; Ebrahim, 2003; Fox & Brown, 1998; Marra, 2007), much of the attention has focused on environment and social safeguards, as well as internal policies that make the MDBs more responsive to performance. In interviews, I found no evidence that shareholder countries are instructing MDBs to be selective about their environment-improving financing.

⁵ Relative value of stand-alone environment-improving projects calculated from the panel data considered below.

5.3.2 *Borrowing States*

It is well known that less-developed countries tend to have lower demand for environmental management as a matter of public policy (Selden & Song, 1994). With high levels of poverty, the benefit of additional economic output often exceeds the costs imposed by environmental degradation. As development levels rise in countries, so does the willingness to pay for costly environmental management activities as a matter of public policy, especially in countries with high civil liberties and political rights (Torras & Boyce, 1998). This has important implications for the type of borrowing demanded by less-developed countries.

Overall, the demand for environment-improving borrowing from less-developed countries is lower than the amount of environmental assistance donor countries would like for MDBs to supply. This is a key issue in the supply of environmental projects:

“Many ‘green aid’ programs face common predicaments. They are often characterized by conflicts between funders who want to ameliorate regional or global environmental problems and recipients who are more concerned with local issues” (Fairman & Ross, 1996, p. 29).

Indeed, a World Bank Environment Department report emphasizes that the “lack of political will” on the part of borrowing countries is one of the most important reasons why environment-improving projects tend to be less successful than other areas of their portfolio (Independent Evaluation Group [IEG], 2008a, p. 73; World Bank, 1998, p. 43).

Indeed, evaluations have highlighted the delicate role that the MDBs must play in order to encourage environment-improving projects:

“The Bank Group can do is ultimately limited by what governments want to borrow or seek policy advice for, even in countries facing serious environmental problems. [Country Management Units] are nonetheless encouraged to identify strategic entry points in their programs (perhaps in critical sectors such as energy) to help advance the Bank Group’s corporate environmental sustainability objectives.” (Independent Evaluation Group [IEG], 2008b, p. 77)

Given the generally lower demand for environment-improving projects, there are three primary reasons why less-developed countries borrow in this area. First, large

countries that determine global environmental outcomes, like Brazil and Indonesia with tropical forest conservation, or China and India with greenhouse gas emissions, are under substantial pressure to protect global environmental goods. Oftentimes these large countries have agreed to take environmental management action in exchange for low-cost financing from donor organizations like the MDBs (M. A. L. Miller, 1995). Thus, globally-important countries are likely to borrow for environment-improving projects that address global concerns as a low-cost method for demonstrating action at the international level.

Second, borrowing countries often have specific development projects in mind for financing, but do not have the credit rating or revenue stream that is necessary to borrow for them on international commercial markets. Oftentimes, these projects are brought to the MDBs for consideration, but may not align directly with MDB corporate priorities. Thus, there is bargaining to link priority development projects with complementary environmental projects. For example, the Asian Development Bank's Greater Mekong Subregion Biodiversity Conservation Corridors Project, which is the ADB's flagship biodiversity program in Southeast Asia, was linked to the approval of the Economic Corridors program that supported regional transportation development (interview, March 2010).

Finally, there are differences in demand for environment-improving projects among borrowing countries. As countries achieve higher per capita income levels, the demand for proactive environmental management as a matter of public policy generally increases. In addition, the management of environmental resources has become a means for political and social stability in some countries facing high levels of degradation (Economy, 2004). Thus, in some cases less-developed countries aggressively pursue environmental management. For example, Costa Rica is widely recognized as "a pioneer

in incorporating sustainable development into decision making at the national level” (IISD, 2004). In addition, as borrowing countries face increasingly severe environmental problems, the benefit of environmental projects increases as well, following a standard cost-benefit logic.

5.3.3 *Approval Decisions for Global Environment-Improving Projects*

Less-developed countries have frequently demanded financial and technical support as a condition for protecting global environmental goods such as ozone, biodiversity, and climate (M. A. L. Miller, 1995; Williams, 2005). Borrowing countries that can substantially impact important global environmental outcomes, like Brazil with tropical forests or China with climate change, are likely to receive more financing from donors (Hicks, et al., 2008, p. 194). This observation is likely due to the intersection of the lending supply preferences of donor countries and borrowing country impetus to demonstrate action, even if the borrowing country only delivers lackluster performance on environment-improving project objectives.

The global environmental politics literature has highlighted how “the power to destroy” is an important form of leverage within international environmental negotiations (Darst, 2001; M. A. L. Miller, 1995; Sell, 1996). For a large countries with substantial ability to alter the provision of global public goods, donor countries cannot turn to other providers. By contrast, borrowing countries that are not able to determine global outcomes to the same extent can be passed over if environmental projects are seen to be ineffective. Thus, it is reasonable to expect that countries with a large portion of the resources in question will not encounter as much performance-based selectivity regarding their past environmental performance as countries that are less important globally.

Because clean-energy projects are intended to address global climate change, are

easily identifiable (as described below), and represent a large portion of global environment-improving projects, I test the following general hypothesis using approval decisions about clean-energy projects:

Hypothesis 1: For projects that seek to secure global environmental goods, the use of evaluation information in decision-making is less likely the greater the ability of the borrowing country to determine global environmental outcomes.

Implication 1a: Development banks will approve a greater number and higher value of clean-energy projects for recipients with high carbon emissions, regardless of past environmental target achievement.

Implication 1b: For borrowing countries with low carbon emissions, approvals will be limited based on past environmental target achievement.

5.3.4 Approval Decisions for Domestic Environment-Improving Projects

Development bank decisions about environment-improving projects that involve local outcomes (e.g., sanitation, solid waste, water pollution) are not as likely to be influenced by donor country lending preferences. Instead, the MDBs must balance the costs/benefits of accountability for performance with borrowing country demand. Fortunately, when projects are “demand-driven,” they tend to be more successful because the borrowing country is invested in their success. There is an alignment between borrower demand and borrower lending results in more successful projects (Connolly, 1996). Therefore, borrowers that achieve success in past operations are more likely to demand similar projects in the future, while borrowers that do not achieve

success in past operations might choose other project types. Because urban environmental projects, which are intended to address localized environmental problems, are easily identifiable (as described below) and represent a large portion of domestically-focused environment-improving projects, I test the following general hypothesis using approval decisions about urban environment projects:

Hypothesis 2: Development banks will approve environment-improving projects that primarily involve local outcomes (e.g., sanitation, solid waste, pollution abatement) for borrowing countries that have high demand for such projects.

Implication 2: Development banks will approve a greater number and high value of urban environmental projects for borrowing countries that have high environmental target performance and face high levels of urban environmental damage.

5.4 Project Evaluations and Environmental Performance

5.4.1 Borrower Environmental Performance

For this project, I assembled a research team that coded implementation performance related to environment-improving targets from every publicly-released project evaluation completed between 1990-2008. Appendix 1 describes the coding procedures used to collect performance information from project evaluations in greater detail. As shown in Figure 10, a combined total of 943 project evaluations have been published by the World Bank (472 evaluations), the Asian Development Bank (283 evaluations), and the African Development Bank (188 evaluations). The Inter-American

Development Bank did not conduct independent project evaluations during the period under consideration. The project evaluations that are used for this research are all readily available on the websites of the respective MDBs. The projects are chosen for evaluation by the development banks based on "purposeful sampling," meaning that priority project areas will have more evaluations. This is appropriate for my research design, since I will assess how information that is available to decision-makers influences approval and allocation decisions.

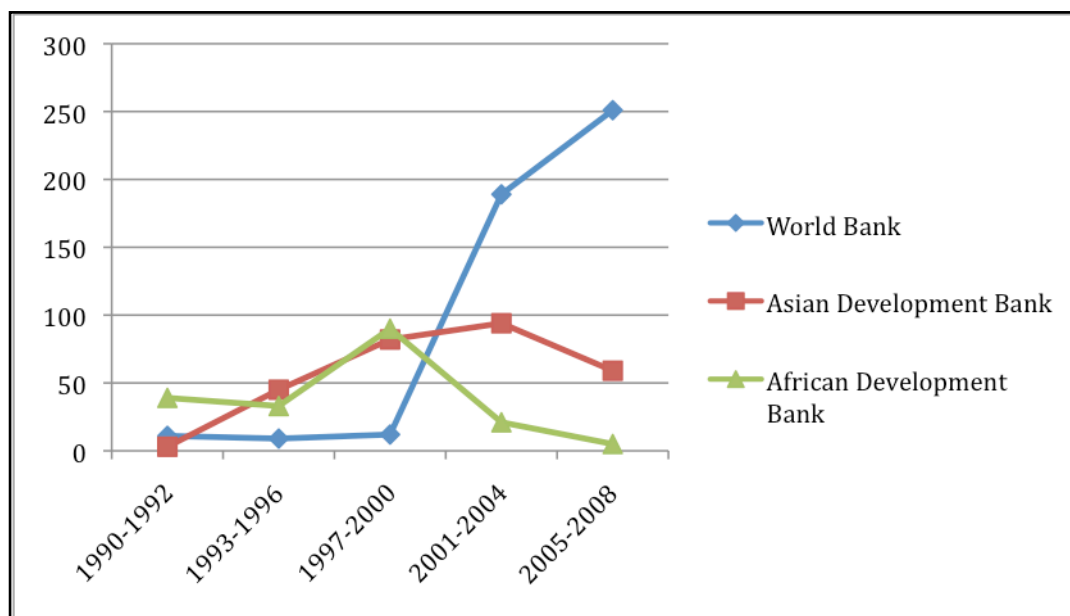


Figure 10: Total number of project evaluations per time period, 1990-2008

For this chapter, I use two pieces of information from project evaluations: (1) overall project implementation performance as coded by MDB evaluators; and (2) borrower environmental target implementation performance, as double-blind coded from evaluation texts. The overall performance rating is already assigned to each project by each MDB and is based on the extent to which outcomes reached targets (e.g., unsatisfactory, partly satisfactory, satisfactory, highly satisfactory). We used the same

ordinal scale to code for borrower environmental target implementation performance based on the narrative description of outcomes in project evaluations, if available (see Table 7).

Table 7: Environmental performance coding criteria

Coding	Meaning	Criteria
4	Highly Satisfactory	Exceeds environmental goals or conditions; specifically mentioned for outstanding environmental performance; efforts significantly improve environmental outcomes as compared to pre-approval expectations;
3	Satisfactory	Meets all environmental goals or conditions with only minor exceptions observed; summary statement of performance is positive;
2	Partly Satisfactory	Meets some environmental goals or conditions with significant deficiencies observed; does not meet monitoring or evaluation standards in projects with no discernable environmental impacts; summary statement of performance is negative;
1	Unsatisfactory	Does not meet most environmental goals or conditions with major deficiencies observed in most areas; outright non-compliance with environmental loan conditions and/or non-achievement of targets;
NA	Not Available	Project has no environmental aspects OR insufficient information is available in evaluation to assess recipient performance;

Of the evaluations, 27% of World Bank, 25% of Asian Development Bank, and 13% of African Development Bank project evaluations contained information on the implementation of environmental targets.

5.5 Modeling the Response to Environmental Performance

5.5.1 Model Specification

There are two primary decisions made about environment-improving projects within a country lending portfolio during any given year. First, a screening decision is made about *whether* to approve an environment-improving project. This decision is often referred to as the “*approval stage*” of decision-making. Second, an allocation decision is made about *how much* financing to approve for an environment-improving project. This

decision is often referred to as the “*allocation stage*” of decision-making.

Following other researchers, I use a two-stage model to examine approval and then allocation decisions (see e.g., Buntaine, 2011; Cingranelli & Pasquarello, 1985; Hicks, et al., 2008; Neumayer, 2003). In each stage, the variables on past performance are conditioned on one another as well as other control variables from the aid allocation literature (i.e. multiple regression analysis). In the first stage, the decision to approve a clean-energy or urban environment project during a given year is taken to be a binary variable. I employ a random-intercept probit model that accounts for unit-effects (Gelman & Hill, 2007, Ch. 14). I also introduce time dummies for the time since the last relevant project approved to control for temporal dependence within countries about the decision-making process (Beck, et al., 1998). This is equivalent to estimating a non-parametric event history model that does not require distributional assumptions on the temporal dependence between observations (Box-Steffensmeier & Jones, 2004). Thus, the approval stage models the probability of receiving a certain type of project in a particular year given past performance and other control variables.

In the second stage, I model the amount of financing approved for a particular project type *given* that a project is approved during a particular time period. The “*allocation stage*” thereby tests whether environmental performance increases or decreases the value of projects that are approved. At the allocation stage, I employ a random-intercept linear model (a.k.a. “linear mixed model”) on the total financing allocated for clean-energy or urban environment projects. In this way, I am able to account for potential unit-effects. Control variables that have little variation over time can usually be dropped in such a specification without significantly changing the estimate of interest, if the random-intercept model is a consistent estimator (Wooldridge, 2002, p. 286-288).

5.5.2 *Identifying Clean-Energy and Urban Environment Projects*

Clean-energy and urban environment projects were chosen for the panel investigation because they are relatively easy to identify and their benefits predominantly accrue globally and locally respectively. In addition, they represent a large portion of MDB environment-improving financing and thus avoid the difficulty associated with modeling rare events in panel data (King & Zeng, 2001). In both cases, identification of projects was predominately based on AidData purpose and activity codes, which have been assigned to every MDB project in the sample (Findley, et al., 2009). Each project is assigned one purpose code, which represents “the dominant, immediate sector or subsector each project was designed to target” (AidData, 2010 p. 20). Each project can be assigned multiple activity codes, which include all activities that were undertaken as part of a project.

I identified candidate *clean-energy projects* using information from both AidData and MDB project theme lists. Any approved project that had an AidData purpose code of renewable energy, an AidData activity code for energy conservation or renewable energy, or was identified as a clean-energy project by the environment department of the relevant MDB was considered a candidate clean-energy project. For each candidate project, I located project appraisal documents and included it in the panel if its primary purpose was to either decrease energy use through efficiency upgrades or support non-fossil fuel based energy development. Any project that was solely technical assistance and did not include an investment component was not included. In addition, only run-of-the-river hydropower projects were coded as clean-energy projects. Projects that support increased fossil fuel power generation, even if more efficient than prevailing power generation operations in the recipient country, were not included.

I identified *urban environment projects* using a similar procedure. Any approved

project that had an AidData purpose code of waste management/disposal, AidData activity codes of air pollution, prevention of water contamination, sewerage, domestic and industrial waste water treatment, or small system sewerage, or was self-identified by the relevant MDB Environment Department as an urban environment or pollution control project were considered candidate urban environment projects. For each candidate project, I located project appraisal documents and assigned a final urban environment project coding if the primary purpose of the project was to improve environmental conditions in urban areas. I excluded any project that addressed environmental problems in rural areas, multi-sector water projects that did not have at least 40% of financing directed to environmental purposes, and road projects with stated air pollution management goals.⁶

5.5.3 Operationalizing Environmental Performance for Models

The main predictor variable of interest in all of the model presented here is the past environmental performance of the particular borrower as measured in project evaluations. The coding scheme is described above. For the models, I create three binary variables that indicate whether the number of times environmental targets were successfully achieved exceeded the number of times targets were only marginally achieved or worse during the five years preceding the panel observation in question.⁷ First, I generated the binary variable ENVIRONMENT SUCCESS, which was positive whenever the number of successful environmental outcomes across all sectors (clean energy, natural resource management, rural environmental management, urban environmental management) exceeded the number of less successful outcomes. Second,

⁶ In the case of rural environmental projects, it is often much more difficult to consistently classify whether a project has an environmental purpose. For example, it is unclear whether agricultural projects that involve soil management are to be considered stand-alone environment projects.

⁷ In general, country planning cycles occur every five years, taking into account performance from the previous five years.

I test how environmental performance relates to clean-energy or urban environment targets influences approval decisions. Thus, I create two binary variables that are positive when there are more successful clean energy outcomes than less successful outcomes (CLEAN ENERGY SUCCESS) and when there are more successful urban environmental outcomes than less successful outcomes (URBAN.ENV SUCCESS) during the preceding five years.

5.5.4 Controlling for Other Factors

Drawing from the literature on aid allocation, I control for several other factors that might influence approval and allocation decisions about environment-improving projects. First, other types of non-environmental performance may impact approval and allocation decisions. A great deal of the aid allocation literature has emphasize the importance of good governance in achieving aid outcomes and has found that donors tend to allocate more financing to recipients with good governance (Cline & Sargen, 1975; Hicks, et al., 2008; Neumayer, 2003). While broad measures of governance quality do not contain information about recipient performance in bank projects, MDB decision-makers may use such general information given the uniqueness of each project design. Thus, I use the World Bank Institute's Government Effectiveness index (GOVT.EFFECTIVE) to control for general governance quality. In addition, when coding environmental performance as described above, we also collected the overall outcome rating given to each bank project by the evaluators. I control for overall project outcomes using the binary variable OVERALL SUCCESS, which is positive if the number of successful outcomes a borrowing country achieved exceeds the number of project outcomes that are marginal or worse during the preceding five years.

Previous research on the allocation patterns of multilateral donors has shown that recipients with greater "need" for development assistance, often operationalized as

lower per capita income receive more concessional loans from multilateral donors at the aggregate level (Dowling & Hiemenz, 1985; Frey, et al., 1985; Maizels & Nissanke, 1984). In terms of environment-improving projects, more projects and greater allocation amounts are likely to be directed to recipients with greater environmental damages or the need to demonstrate international action. In the case of clean-energy projects, there is much greater pressure internationally for countries with high emissions levels, such as China and India, to manage greenhouse gas emissions. Both because large borrowers are face international pressure to demonstrate action and because MDBs must increase clean-energy lending due to donor country pressures, borrowing countries with high carbon emissions levels (CO₂.GT) might receive more projects and greater allocation amounts.⁸ Likewise, more urban environment projects might be directed to recipients with higher levels of urban environmental degradation. Thus, I take the air pollution damage for each borrowing country, as recorded in the World Bank's Adjusted Net Savings data, and divide it by the total urban population in each country-year to produce an estimate of the urban per capita air pollution burden (POLLUTION BURDEN).

There are a number of characteristics of the MDB portfolio allocation process that are likely to influence decisions about both clean-energy and urban environment projects. First, bank-wide decisions to emphasize certain sectors, oftentimes operationalized through the adoption of new policies or strategies, can alter allocation patterns of certain project types across the bank (Nielson & Tierney, 2003). Thus, I code a binary variable (CLEAN ENERGY INITIATIVE) for any year after the conclusion of the Kyoto Protocol for the World Bank and any year after the initiation of the Energy

⁸ I use the compiled emissions data from Carbon Dioxide Information Analysis Center, available at: http://cdiac.ornl.gov/trends/emis/meth_reg.html (Accessed April 2011).

Efficiency Initiative for the Asian Development Bank in 2005.

In addition, there might be important differences in allocation decisions for countries that have access to highly concessional loans as compared to countries that borrow from the MDBs at market rates. In general, low-income countries that have very low per capita income, high external debt levels, and low project implementation capacity receive highly concessional financing, consisting mainly of loans with interest rates as low as 0.75% and grants. For the MDBs considered here, these funds come from the World Bank's International Development Association (IDA), the Asian Development Bank's Asian Development Fund (ASDF) and the African Development Bank's African Development Fund (AFDF). Each recipient that borrows concessional financing receives a set allocation amount each year, leaving limited room to increase or decrease financing based on performance, unless other sectors are deemphasized. By contrast, middle-income countries that have higher per capita income and lower external debt tend to borrow from the MDBs at market rates, through the World Bank's International Bank for Reconstruction and Development (IBRD), the Asian Development Bank's Ordinary Capital Reserves (OCR), and the African Development Bank's Ordinary Capital Reserves. There is no set cap on the amount of financing that can be borrowed from these sources and since borrowing takes place at market rates, the projects that are financed tend to be very demand-driven and much larger. Thus, owing to income effects and the amount of financing that can be approved from the market lending window, countries that borrow at market rates are more likely to receive both clean-energy and urban environment projects. Thus, I create a variable (CONCESSIONAL) that represents the proportion of concessional lending as part of the total lending amount approved for each country in a given year.

Researchers have also found that "recipient size" is a determinate of multilateral

aid allocation. In operational terms, this has meant either population or size of the economy (Dowling & Hiemenz, 1985; Neumayer, 2003). In terms of approved and allocation decision, we would expect borrowers that have a greater number of project (NO. PROJECTS) or a greater portfolio size in a particular year (COUNTRY PORTFOLIO SIZE) to receive more projects and higher allocation amounts.

5.5.5 Sub-setting the Panel

For each of the models presented below, I use the same predictor variable on two subsets of the data. The first subset includes in the sample all years when a borrowing country received at least one project (“a” models). Because aggregate or total allocation decisions are made prior to project approval decisions, it would bias estimates to include country-years in the approval panel when the borrowing country would not receive any projects due to aggregate pipeline decisions. The second subset includes all country-years when a project evaluation was completed during the previous five years (“b” models). Because projects are not assigned randomly to evaluation and because I cannot rule out missing evaluations during the early years of the panel, model estimates might be biased by selection effects of which borrowers were evaluated. To the extent that model estimates are similar across these two subsets, concerns about selection effects are diminished.

5.6 Model Results

In this section, I test how past environmental performance influences the approval and allocation of clean-energy and urban environment projects by three development banks. I report results for the World Bank and Asian Development Bank below. I also ran the data for the African Development Bank, but because both clean-energy (4 projects) and urban environmental projects (13 projects) are not a significant

part of the portfolio since 1990, there were no significant predictors of approval decisions. In recent years, environmental considerations have become a priority within African Development Bank strategies, suggesting that this inquiry could be replicated several years in the future.

In terms of the approval of clean energy projects, I found that the amount of carbon emissions has a positive impact on the probability of receiving such a project across all models, supporting Implication 1a (Table 8, Models 1a-4b). This provides evidence that both the World Bank and Asian Development Bank are acting in accordance with the lending supply preferences of donor countries to finance clean-energy projects in globally important countries. As expected, past environmental performance was not a predictor of clean-energy approval decisions in most cases. For the World Bank, high cross-sector environmental performance only positively influences approval decisions about clean-energy projects in countries with low emissions levels (Models 1a/1b). Because of the interaction between environmental performance and emissions of the borrowing countries, there is not a significant difference in predicted approval decisions between good and poor performers that have high emission levels (Figure 11).

For the Asian Development Bank, in no case does past environmental performance predict clean-energy project approvals (Models 3a-4b). This finding is consistent across models using both cross-sectoral environmental performance (Models 3a/3b) and performance specific to clean-energy targets (Models 4a/4b). As a robustness check, I estimated the same model using the ADB's own listing of clean-energy projects, which includes many large hydropower project and efficient fossil-fuel power generation projects. In this case, borrowers with high emission levels and low

environmental performance are most likely to receive clean-energy projects, indicating an response that is opposite to performance-based allocation.

Table 8: Approval of Clean-Energy Projects (Random-Intercept Probit)

Model	(1a)	(1b)	(2a)	(2b)
MDB	World	World	World	World
ENVIRONMENT SUCCESS	0.69* (0.41)	0.47* (0.27)		
ENVIRONMENT SUCCESS * CO2.GT	-1.06 (0.78)	-1.49 (0.96)		
CLEAN ENERGY SUCCESS			-0.25 (0.54)	-0.06 (0.41)
CO2.GT	2.26** (1.03)	2.05** (0.86)	1.58* (0.84)	1.07** (0.45)
OVERALL SUCCESS	0.08 (0.37)	-0.16 (0.25)	0.30 (0.32)	-0.05 (0.25)
CLEAN ENERGY INITIATIVE	0.34 (0.28)	-0.05 (0.51)	0.40 (0.28)	0.12 (0.49)
GOVT.EFFECTIVE	-0.05 (0.43)	0.08 (0.31)	-0.05 (0.42)	0.07 (0.30)
CONCESSIONAL	-0.97* (0.50)	-0.30 (0.30)	-0.98** (0.50)	-0.32 (0.29)
NO. PROJECTS	0.15** (0.04)	0.02 (0.04)	0.16** (0.04)	0.03 (0.04)
TIME DUMMIES	4+ year gap positive, sig.**		4+ year gap positive, sig.**	
Random Intercept Variance	2.109	0.000	2.049	0.000
Data Subset	Allocation Years	Allocation Years Covered by Evaluation	Allocation Years	Allocation Years Covered by Evaluation
Observations (Countries)	1346 (134)	338 (73)	1346 (134)	338 (73)
Residual Deviance	317.1	136.1	320.9	140.3
Null Deviance	355.4	154.7	355.4	154.7

Table 8 cont.

Model	(3a)	(3b)	(4a)	(4b)
MDB	Asian	Asian	Asian	Asian
ENVIRONMENT SUCCESS	-0.09 (0.40)	-0.06 (0.47)		
ENVIRONMENT SUCCESS * CO2.GT				
CLEAN ENERGY SUCCESS			-0.03 (0.56)	-0.06 (0.66)
CO2.GT	0.87* (0.48)	1.23* (0.69)	0.84* (0.48)	1.22* (0.70)
OVERALL SUCCESS	0.34 (0.31)	0.33 (0.39)	0.33 (0.31)	0.32 (0.40)
CLEAN ENERGY INITIATIVE	0.04 (0.37)	0.05 (0.44)	0.03 (0.37)	0.06 (0.46)
GOVT.EFFECTIVE	0.12 (0.40)	-0.21 (0.70)	0.12 (0.40)	-0.19 (0.72)
CONCESSIONAL	-0.53 (0.44)	-1.64* (0.97)	-0.53 (0.44)	-1.66* (0.99)
NO. PROJECTS	0.07* (0.04)	0.08 (0.05)	0.07* (0.04)	0.08 (0.05)
TIME DUMMIES	4+ year gap negative, sig.*		4+ year gap negative, sig.*	
Random Intercept Variance	0.000	0.315	0.000	0.345
Data Subset	Allocation Years	Allocation Years Covered by Evaluation	Allocation Years	Allocation Years Covered by Evaluation
Observations (Countries)	296 (36)	195 (27)	296 (36)	195 (27)
Residual Deviance	97.1	82.4	97.1	82.4
Null Deviance	111.3	97.3	111.3	97.3

Statistical significance levels: ** p < 0.05, * p < 0.1

Null Deviance is calculated using country random intercept and time dummies if present in regression

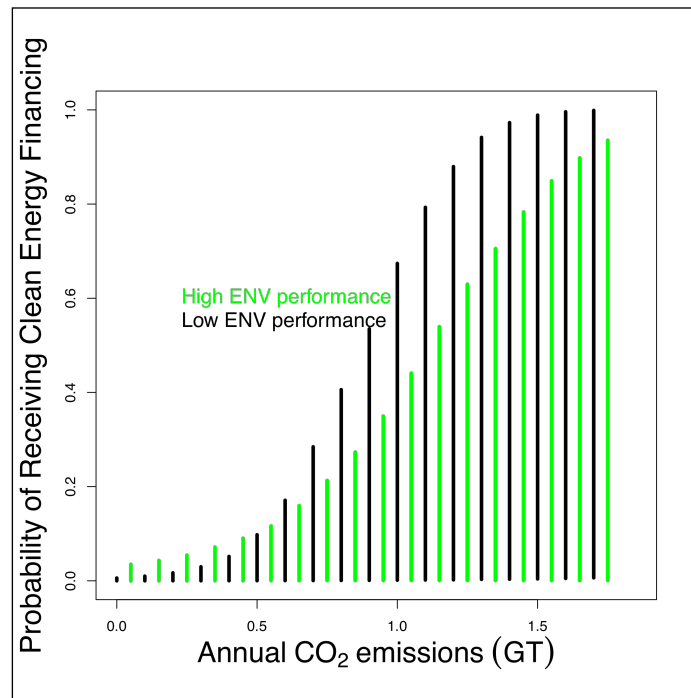


Figure 11: Probability of Receiving World Bank Clean-Energy Financing (Model 1a)

For urban environment-improving projects, the results between the World Bank and the Asian Development Bank are different (Table 9). As expected, cross-sectoral environmental performance predicts higher probabilities of urban project approval (Models 5a/5b). When using past performance with urban environmental project as the predictor variable, an interesting result emerges. For borrowing countries that have very low levels of per capita air pollution damage, there is no difference between high and low performing countries. However, as the pollution burden increases, high performance borrowers are more likely to receive an urban environment project, as predicted in Implication 2 (Models 6a/6b). In both cases, for the World Bank countries that are receiving concessional IDA lending and countries that have fewer total number of projects are less likely to receive urban environment projects. This supports the

preposition that countries primarily select into environment projects that deal with local outcomes.

Table 9: Approval of Urban Environment Projects (Random-Intercept Probit)

Model	(5a)	(5b)	(6a)	(6b)
MDB	World	World	World	World
ENVIRONMENT SUCCESS	0.46** (0.23)	0.49** (0.24)		
URBAN.ENV SUCCESS			-0.76 (0.86)	-1.26 (0.93)
URBAN.ENV SUCCESS * POLLUTION BURDEN			0.13* (0.07)	0.17** (0.08)
POLLUTION BURDEN	0.00 (0.00)	-0.01 (0.01)	0.00 (0.00)	-0.01 (0.01)
OVERALL SUCCESS	-0.15 (0.21)	-0.24 (0.24)	-0.07 (0.19)	-0.25 (0.25)
GOVT.EFFECTIVE	0.11 (0.15)	-0.36 (0.33)	0.15 (0.15)	-0.25 (0.35)
CONCESSIONAL	-0.85** (0.18)	-1.11** (0.30)	-0.79** (0.17)	-1.02** (0.32)
NO. PROJECTS	0.14** (0.02)	0.10** (0.04)	0.14** (0.02)	0.12** (0.04)
TIME DUMMIES	mixed signed, n.s.	mixed signed, n.s.	mixed signed, n.s.	mixed signed, n.s.
Random Intercept Variance	0.145	0.152	0.124	0.223
Data sub-set	Allocation Years	Allocation Years Covered by Evaluation	Allocation Years	Allocation Years Covered by Evaluation
Observations (Countries)	1294 (127)	333 (72)	1294 (127)	333 (72)
Residual Deviance	618.8	205.7	615.3	198.7
Null Deviance	698.1	232.6	698.1	232.6

Table 9 cont.

Model	(7a)	(7b)	(8a)	(8b)
MDB	Asian	Asian	Asian	Asian
ENVIRONMENT SUCCESS	-0.07 (0.32)	-0.08 (0.33)		
URBAN.ENV SUCCESS			0.23 (0.43)	0.19 (0.42)
URBAN.ENV SUCCESS * POLLUTION BURDEN				
POLLUTION BURDEN	0.01 (0.02)	0.01 (0.02)	0.01 (0.02)	0.01 (0.02)
OVERALL SUCCESS	0.37 (0.25)	0.57* (0.30)	0.35 (0.25)	0.56* (0.29)
GOVT.EFFECTIVE	0.51* (0.31)	0.45 (0.41)	0.51 (0.31)	0.44 (0.40)
CONCESSIONAL	-0.44 (0.34)	-0.84* (0.45)	-0.42 (0.34)	-0.80* (0.45)
NO. PROJECTS	0.11** (0.03)	0.10** (0.04)	0.11** (0.03)	0.10** (0.04)
TIME DUMMIES	mixed signed, n.s.	mixed signed, n.s.	mixed signed, n.s.	mixed signed, n.s.
Random Intercept Variance	0.066	0.028	0.073	0.026
Data sub-set	Allocation Years	Allocation Years Covered by Evaluation	Allocation Years	Allocation Years Covered by Evaluation
Observations (Countries)	267 (28)	187 (23)	267 (28)	187 (23)
Residual Deviance	150.3	110.8	148.7	110.6
Null Deviance	195.0	133.6	195.0	133.6

Statistical significance levels: ** p < 0.05, * p < 0.1

Null Deviance is calculated using country random intercept and time dummies.

By contrast for the Asian Development Bank, past environmental performance, either cross-sector or as relate to past urban environment operations, in no case predicted the approval of urban environment projects (Models 7a-8b). When I specify the same models using the ADB self-defined list of environmental projects as the dependent variable, I obtain the same results. As expected, borrowers that receive a greater number of total project are more likely to receive an urban environment project in any given year. When examining the subset of the panel covered by at least one

project evaluation during the last five years, I also find that overall success in achieving project outcomes predicts recipient of urban environment projects (Models 7b/8b). Thus, given the limited size of the ADB lending portfolio and the decreased opportunity to look for specific instances of repeated performance, the planning cycle might be more responsive to general performance and governance information.

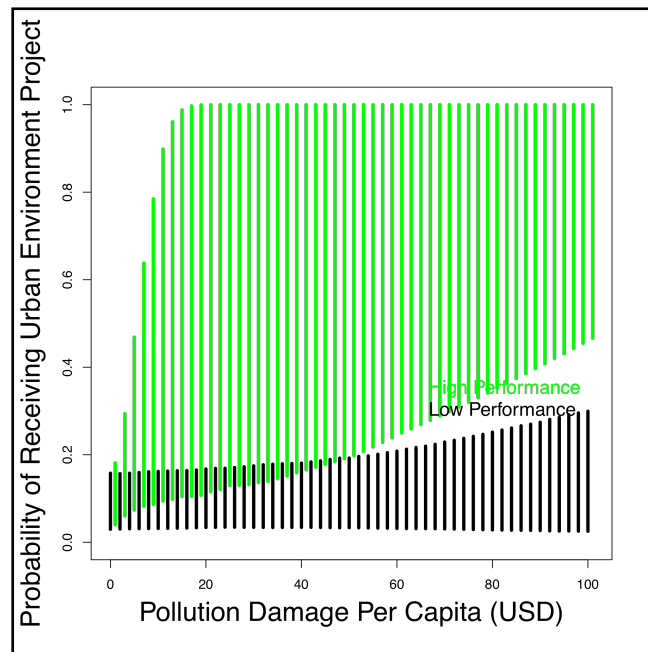


Figure 12: Probability of Receiving World Bank Urban Environment Project (Model 6a)

As with clean energy projects, there are no significant predictors of when African Development Bank borrowers receive urban environment projects. No measure of past environmental performance, including the self-assigned “environmental” scores that are assessed in every project evaluation, predict future approval decisions. Indeed, in the 15-year panel that included 52 borrowing countries, there were only 9 countries that received an urban environment project, and eight of which received only one project over the entire panel. In no case was an urban environment project approved when a country was classified as a borrower with high environmental performance.

5.6.1 Allocation Amounts for Environmental Projects

While the approval of environmental projects in a particular country-year is a part of allocation decisions made by the development banks, it is also necessary to account for the amount of financing that is allocated to achieve environmental goals. Indeed, it may be the case that performance information is not reflected in *whether* to approve an environmental project, but rather *how much financing* to allocate for environmental projects once the decision has been made to move forward with projects, with more successful countries allocated larger projects due to both lending supply pressures and borrower demand. In order to examine this dynamic, I re-specified the models presented above with the amount of financing allocated to a particular purpose as the outcome variable, conditional on a country having received any clean-energy or urban environment financing during that time period.

However, in no case across the different MDBs considered here did I find that past environmental performance predicted the size of environment-improving projects. For the World Bank, the overall portfolio size of a particular borrowing country during a given year was the only significant predictor of project size for both clean-energy and urban environment projects. However, countries with larger portfolio sizes receive less environment-improving financing as a proportion of their total portfolio allocation, indicating that increasing borrowing does not fundamentally alter development priorities among middle-income countries. For the Asian Development Bank, there are no significant predictors of environment-improving project size among the countries that received either clean-energy or urban environment projects.

At first glance these results are puzzling. It might be expected that high-performing borrowers not only receive more environment-improving operations, but that they also receive higher amounts of environment-improving finance relative to their

total portfolio size. What the combined results of the approval and allocation models show is that high-performing countries *do* receive more environment-improving financing in certain circumstances (see approval models), but that this effect is primarily observed in “go or no go” decisions about these projects. Among countries that receive environment-improving projects, there is no *additional* effect of high performance in the size of projects that are received, controlling for portfolio size. This result reflects how decisions are made about projects. Several operational staff that I spoke with indicated that project size decisions are made in reference to project goals, rather than past performance. In no case did I find examples of projects that were explicitly made larger or smaller because of past performance. Instead, decision-making focused on whether to pursue similar projects in future periods given past outcomes.

5.7 Extending Model Results with MDB Staff Interviews

The models presented above reveal several findings: (1) borrowing countries with higher carbon emissions are more likely to receive clean-energy projects; (2) past environmental performance is not a robust predictor of clean-energy project approvals, and it only appears to influence World Bank approvals for countries with low emissions; (3) past environmental performance predicts World Bank approvals of urban environment projects, especially for countries facing high levels of urban pollution; (4) past environmental performance does not predict Asian Development Bank approvals for urban environment projects; (5) in no case does past environmental performance predict the size of environment-improving projects, given that a country receives a relevant project.

In order to probe these findings, I completed interviews with 54 MDB staff and managers in evaluation, policy, and operations across the four MDBs involved in sovereign lending. While the model results present above can tell us that there is not a

systematic response to performance information as contained in project evaluations, these models do not provide insight into the reasons why responding to environmental performance information is so difficult for MDBs as a matter of the decision-making process. In general, I sought to interview the widest possible range of operational and evaluation staff in order to capture the full variation in observations about MDB practices. My interviews were often based on “snowball sampling,” with interviewees suggesting additional contacts in order to capture a wider variation in observations (Goldstein, 2002). In each interview, I utilized a semi-structured interview template and asked about how external pressures, internal processes, and staff incentives influence approval and allocation decisions about environment-improving projects.

5.7.1 Mechanisms to Respond to Environmental Performance in Project Evaluations

The interviews that I conducted confirmed the general conclusion that it is difficult for MDBs to practice performance-based allocation by responding to environmental performance information contained in project evaluations. For all three MDBs considered here, the formal procedures to respond to environmental performance are weak or non-existent. At all three of the MDBs, evaluation staff reported that the most significant way that they influenced decision-making at the project level was through inter-departmental comment periods during project design. Over the last decade, it has become standard practice to circulate project information and appraisal documents to relevant departments for comment. Evaluators frequently use this process to bring up lessons from past projects, especially when there are environmental targets in the projects or operations being considered. Evaluators reported that project design will often be altered in response to comments on achieving environmental targets. While

such comments might give evaluation some influence, they rarely affect project approval decisions.

In addition, the MDBs have all adopted “quality-at-entry” standards that are required of all projects. Both the World Bank and the African Development Bank have Quality Assurance Groups that conduct desk reviews of projects during their design phase to ensure that best-practice procedures are carried out, one of which is documenting how the project design responds to the lessons of past evaluations. However, staff members in quality assurance readily admit that there is nothing systematic about the review of past lessons. To the extent that the MDBs produce hundreds of assessments and evaluations each year, all with multiple lessons and recommendations, operational staff are likely to pick up on a few easy recommendations that are relatively easy to reconcile with the project being designed so that approval decisions are not delayed. Operational management across the MDBs indicated that it is primarily the responsibility of the relevant task leader to complete a due diligence search of past operational lessons, with very little in the way of formalize procedure to ensure that this search is systematic. One possible exception is the Management Action Record tracking system of the Asian Development Bank, in which management is supposed to track its actions acting on evaluation recommendations. However, since very few recommendations advise dropping future projects in unsuccessful areas, this system is not likely to bear directly on approval and allocation decisions.

Both inter-departmental comment and quality-at-entry reviews involve influencing project design rather than approval and allocation decisions. Projects that are formally part of the design pipeline are almost always approved, making this kind of influence unobservable in the models presented above. Decisions about whether to pursue a project are often made informally as part of ongoing country strategic planning

and dialogue. In the case of concessional lending, there is an approved lending amount that must be roughly adhered to on a rolling year-to-year basis. This often leaves little room to expand environment-improving lending even when there is very good performance, unless the borrowing country is willing to forego other development priorities to do so. For example, an operational staff member at the African Development Bank indicated that even after a very successful first round sewerage project in the Gambia, the government was unwilling to expand urban environment investments at the expense of other priorities. This is a likely reason why borrowing countries with concessional lending are significantly less likely to receive environment-improving projects of all types. Furthermore, even though the Asian Development Bank has become more selective in the sectors that it will pursue in any given country, environmental targets remain a cross-cutting goal to be integrated into all development projects, making it unlikely that high performance will trigger increased investment, as was found in the model results. Indeed, operational staff at the management level across the three organizations report significant pressure from donor country executive directors to address environmental issues of all types in their projects, but especially for clean-energy investments. Asian Development Bank energy staff report that this is one area of the portfolio where investments are still primarily “donor-driven,” with pressure to demonstrate the “do something” approach to donors as part of the replenishment of concessional lending resources.

It is also very difficult for project evaluations to set the tone for high-level strategic decisions taken at the Board level. Indeed, it is uncommon for the Board or the subset of the Board delegated authority to deal with development effectiveness (e.g., World Bank Committee of Development Effectiveness) to consider individual project evaluations. An Executive Director at the Asian Development Bank reported that only

project evaluations dealing with very high profile operations are considered at the Board level. This means that there is not a significant audience among donors for the kinds of detailed information that I collected from project evaluations. This issue is further compounded by the fact that only the African Development Bank has a standardized score for environmental performance within its project evaluations. None of the MDBs use a consistent set of environmental performance indicators, which has been recognized as an impediment to responding to environmental performance (Independent Evaluation Group [IEG], 2008b). In addition, because membership in CODE has significant turn-over, there is little opportunity for CODE members to accumulate knowledge that is necessary to synthesize repeated performance issues within particular borrowing countries. Senior management and Board members report having greater ability to respond to high-level, synthesizing, or thematic evaluations. Indeed, when I asked operational staff about influential evaluations, they often reported high-level, thematic evaluations, for example rural water supply and sanitation with the African Development Bank and clean energy with the Asian Development Bank.

In general, the “loan approval culture” still dominates the approval and allocation decision context at the development banks. While traumatic experiences can cause MDBs to avoid environment-improving projects in a certain country (e.g., Bangladesh Biodiversity project), in most cases priorities for a particular country or programs have shifted since the decade when a project was first designed. Indeed, many mid and low-level operational staff across the different banks could not point to a project evaluation they had read that subsequently influenced their decision-making, especially as related to approval and allocation decisions, in any meaningful way. Senior operational staff at both the World Bank and African Development Bank reported that their primary purpose is to lend money and that they are evaluated on their ability to

shepherd loans through the pipeline process. An Asian Development Bank staff member called this the “path of least resistance” logic to approval and allocation decisions, as described above.

In addition, several operational staff reported that the culture inside the MDBs tends to view poor performance, especially as related to environmental targets, as a capacity issue. Thus, the solution to poor performance may in some cases be to approve more environment-improving projects, or at least more technical assistance related to environmental management. This is apparently the norm, especially at the Asian Development Bank. In addition, many operational staff see development investments as a long-term process. For example, energy investments in Pakistan have been planned as part of a 10-year strategy, first building up the policy environment through traditional investments so that clean-energy investments can be successful.

5.7.2 Demand-Induced Borrowing Decisions Mimicking Performance-Based Allocation

Unlike approval decisions for clean-energy projects, the models presented above do find that the World Bank responds to past environmental performance when approving urban environment projects, especially for borrowing countries with high per capita pollution burdens. Staff members that I interviewed indicate that this dynamic can be generated by borrower demand for environment-improving projects that have mainly domestic benefits. Operations that address local environmental issues at the MDBs, especially as they relate to sanitation and sewerage, receive less lending pressure from donor countries. Instead, countries that are facing significant pollution burdens oftentimes turn to the MDBs for assistance because it can be difficult to borrow for environment-improving projects from other sources. In these cases, when the borrowing country in question is invested in the success of the project, they oftentimes seek

subsequent projects in the same sector after instances of success. For example, the Asian Development Bank has supported a string of small-scale water resource management projects in Bangladesh that have proved very successful.⁹

In addition, for local environment improving projects, specifically those that relate to the urban environment, there is likely to be a correlation between the demand and the capacity to implement them well as countries move from low to middle-income. It is often countries that experienced rapid industrialization that have the greatest need for urban environment projects, but also the resources to achieve better environmental management (Bai & Imura, 2000). In addition, middle-income countries also borrow from commercially-competitive financing sources, leaving them room to expand borrowing for urban environment projects when they experience successful outcomes. Indeed, staff in the water supply and sanitation sector report that large-middle, income countries are the easiest to convince about taking on water quality projects.

5.8 Conclusions

The model results presented here cast doubt that the provisioning of environmental performance information through project evaluations is capable of producing performance-based allocation outcomes. For clean-energy projects, the models presented here only found a response to past performance in one instance and only for countries with low emissions levels. This finding conforms to the notion that the “power to destroy” is an important driver of the relationship between international organizations working in the environment sector and developing countries (Darst, 2001). Because previous work has shown environmental projects must align with borrower

⁹ For more information, see the Asian Development Bank project database for Bangladesh water projects, available at: <http://www.adb.org/projects/summaries.asp?query=&browse=1&mode=1&ctry=BAN&sctr=3800&year=ALL> (Accessed April 2011).

policy priorities in order to be successful (Connolly, 1996), it is uncertain that focusing on large countries without a history of environmental achievement will achieve cost-effective results.

Indeed, it is somewhat puzzling that donor countries continue to push a rapid expansion of clean-energy lending in large countries with poor performance records. Rational choice logic would dictate that they attempt to achieve cost effective emissions reductions with their scarce environmental financing. It is likely the case that because they large countries will largely determine global environmental outcomes, they form a cartel of sort, which must be dealt with regardless of performance. Recent research has explored how emerging economies have maintained a unified bargaining position on climate change in order to induce increased financing from donor countries (Kasa, Gullberg, & Heggelund, 2008). To the extent that large emitters are able to maintain this coalition, donor countries may have no choice but to continue financing large emitters with poor performance records.

Current development bank practices do not include a formal mechanism to decide how to allocate projects within individual functional sectors, like the environment. This system may have the benefit of flexibility, as country lending portfolios can be tailored to the needs and capacity of the borrower. However, it is also possible that the lack of a formal performance-based allocation system by sector decreases the ability of development banks to resist approving global environmental projects in countries with a record of poor performance. The results of the analysis presented here suggests that development banks face incentives that detract from effectiveness, so far as past performance on environmental projects predicts future performance.

A number of questions about optimal allocation are raised by this study that cannot be addressed here. In many cases, development banks attempt to leverage small investments that can have a significant influence on the policies and practices of borrowing countries, known to staff as the “demonstration effect.” Thus, it may be the case that steering investments to large countries regardless of performance is justified because of the increased potential for diffusion of good environmental practices in those countries. Indeed, this is an important question to address when considering whether to extend performance-based decision criteria to individual functional sectors. Other scholars have addressed the need to think more critically about the marginal benefits of development assistance projects, taking into account performance expectations when designing formal decision frameworks based on past performance (Amprou, Guillaumont, & Jeanneney, 2007). Environmental assistance is likely to become an even more important part of development bank operations in the coming years – it will be important to think critically about the decision practices that can lead to the best possible outcomes in terms of securing both local environmental quality and global environmental goods.

Because the findings from project evaluations do not appear to have a large impact on decisions about environment-improving projects across the multilateral development bank, it was suggested to me by interviewees that I examine the effect of country program evaluations. These evaluations are written to feed directly into the process of planning country portfolios and because they are considered by high-level decision-makers and state representatives, they may have more of an effect. Thus, in the next chapter I turn to the question of whether the provisioning of performance information in a formal decision process that involved state shareholders can induce responses to past performance.

6 Country Program Evaluations and Environment-Improving Lending Decisions

6.1 Introduction

Every three to five years, the multilateral development banks plan their lending strategies for each borrowing country. As part of this process, management at the MDBs negotiates with borrowing country ministries about the sectors and types of projects that will best address development needs, accounting for emerging opportunities and past lessons. Recognizing that broad level allocation decisions were made as part of this process, the MDB evaluation departments began producing multi-year country evaluations to directly inform and shape the country assistance strategies. In 1995, the Operations Evaluation Department at the World Bank completed the first in a series of these “new style” evaluations – an evaluation that reviewed “the relevance and efficacy of the Bank’s overall country assistance strategy and the effectiveness of various lending and nonlending instruments of Bank assistance” (Operations Evaluation Department [OED], 1995, memorandum). This new style of evaluation, which I will call a *country program evaluation* for consistency across MDBs, was “a performance audit report on the Bank’s total assistance program” (Operations Evaluation Department [OED], 1995, p. 7). Whereas project evaluations were narrowly focused on single operations, this new style of evaluation directly addressed portfolio composition decisions.

This new type of evaluation reflected an emerging recognition among evaluation scholars that influential evaluations clearly addressed the needs of their audience and were integrated into decision-making processes (Patton, 2008). The country program evaluation is well positioned in terms of both audience and process, given that they are formally considered in the context of country planning, included as part of sub-Board meetings about country program evaluations, considered during Board reviews of draft

country assistance strategies, and brought up during final Board discussion about country assistance strategies (World Bank, 2009b).¹ In addition, country program evaluations aggregate information from project evaluations, completion reports, and other types of monitoring information. Thus, unlike project evaluations, they present a systematic analysis about how different lending priorities in the country portfolio were achieved and how *portfolio composition* decisions might be improved to better achieve prioritized development goals with scarce resources.

A recent example that demonstrated how such an evaluation could influence portfolio composition decisions is available in the *Country Assistance Program Evaluation for Pakistan* that the Asian Development Bank completed in 2007. This evaluation chronicled the achievements of lending and technical assistance projects to the country since 1985. This was the first “whole-program” evaluation for Pakistan, and it sought to examine whether portfolio composition decisions were properly aligned with identified development targets. The findings and recommendations indicated that portfolio composition decisions were not organized to achieve maximum development impact (Operations Evaluation Department [OED], 2007c, p. vii):

“ADB has too many loans in its Pakistan portfolio, spread across too many sectors and subsectors... since resources are unlikely to increase significantly, the number of loans must be reduced... ADB should reduce the number of sectors and subsectors in which it is involved.”

Particular to environment-improving lending, the same evaluation found that investments in water supply, sanitation, and waste management were largely

¹ Project evaluations, which were the focus of previous chapters, are weak with respect to audience in several ways. State shareholders acting through the MDB Boards are rarely in a position to formally review individual project evaluations, unless a project has become high-profile due to publicized poor performance. In general, the Board is responsible for setting higher-level, strategic directions for the MDBs, and given the breadth of operations that come before the Board for consideration, the shareholder states do not have the capacity to process implementation issues that come up in the context of individual projects. Because performance outcomes in the context of single country programs are often variable, project evaluations do not give state shareholders the ability to separate noise from more systematic performance issues that can be dealt with by higher-level decisions, such as when adopting a new country assistance strategy.

unsuccessful (ibid., p. v). In its conclusion, the evaluation recommended that portfolio composition decisions should focus on other sectors (ibid., p. 41):

“Under this [proposed] scenario, ADB would move out of the health, water supply and sanitation, and urban development sectors... urban development, which has a prominent place in the pipeline portfolio, does not feature under the scenario because of past poor performance in this area... clear evidence would be needed that the approach proposed, and/or changed context, would increase significantly the chances of success [in this sector].”

Responding to this evaluation, ADB management developed a new country assistance strategy that focused on four investment areas. From January 2007 to August 2008, the number of active loans was reduced from 80 to 58 (Asian Development Bank [ADB], 2009b). This process showed the potential for *country program evaluations* to influence portfolio composition decisions in ways that are not possible with project evaluations, which are necessarily limited to single operations and are not able to directly engage with the broader process of making allocation decisions, most importantly the making of country assistance strategies.

The purpose of this chapter is to test whether the provision of aggregated, country-level performance information in the context of country portfolio planning creates sufficient incentives for operational staff to practice performance-based allocation. As described below, MDB operational staff that I interviewed often stated that the country program evaluation was the evaluation product most likely to exert direct influence on allocation decisions. This expectation derived from observations that country program evaluations have distinct advantages over project evaluations in terms of audience, process, and information aggregation. However, within the MDBs, there are no formal requirements that recommendations from country program evaluations are implemented. Instead, the most important feature of the country planning procedures is that decision-makers are forced to confront evaluation information. Operational decision-makers must write management responses addressing the recommendations in

country program evaluations, but do not necessarily have to agree with the recommendations.

By examining whether recommendations in these evaluations impact future lending decisions, I test whether the provision and synthesis of performance information within a formalized decision processes creates sufficient incentives to adjust lending decisions. By answering this question, I will be able to more carefully parse out the impact of performance information from the impact of operational policies and administrative procedures that incentivize the use of performance information. This distinction will answer important questions about whether evaluation must be coupled with operational policies that provide “hard incentives” to use performance information (see Pollack & Hafner-Burton, 2010).

This chapter proceeds by first examining the theoretical reasons why country program evaluations are likely to have a direct effect on lending decisions, owing to their audience, process, and information-aggregation advantages. I draw heavily from MDB staff interviews to derive my theoretical expectations and testable hypotheses. I then examine the extent to which country program evaluations address environmental performance and make recommendations about future environmental operations. Using panel models, I examine the impact of relevant findings and recommendations on lending decisions. Despite the strong position of many MDB staff that country evaluations should be the single most important evaluation product in terms of their influence on lending decisions, I do not find any such influence in panel models. In order to explain this puzzling finding, I examine how the current country evaluation process has not effectively addressed environmental performance and has created limited “hard incentives” to actively use performance information or respond to recommendations.

6.2 Audience, Process, and Information-Aggregation Effects: Evidence from MDB Staff Interviews

Decision-makers at the MDBs are likely to respond to recommendations contained in country program evaluations for a combination of three reasons. First, recommendations contained in country program evaluations are likely to be more influential because of an *audience effect*, that is the significant involvement of donor state shareholders in assessing past performance in the context of designing new country assistance strategies. Second, unlike project evaluations, country program evaluations are well-integrated into the process of designing country strategies, likely making them more influential because of a *process effect*. Third, performance information about lending outcomes is scattered among a variety of different reports and evaluation products, especially environmental performance that is often a sub-component in larger project evaluations. Country program evaluations synthesize dispersed information, making it more accessible to decision-makers who cannot monitor the myriad of information on performance that is produced each year, which I term the *information aggregation effect*. The combination of these effects, explained in greater detail below, suggest that performance information and recommendations contained in country program evaluations are more likely to have a direct influence on lending decisions than was found with project evaluations.²

Indeed, during the course of conducting interviews with 54 staff at the headquarters of the World Bank, Asian Development Bank, Inter-American Development Bank, and African Development Bank, I was repeatedly told by both

² For the most part, results from project evaluations fall below the level of oversight that state shareholders are able to conduct with regards to the MDBs. Because state shareholders do not directly consider the vast majority of project evaluations and are involved in approval decisions about individual projects mostly in an “advise and consent” capacity, project evaluations themselves have limited direct impact on lending decisions. As argued in the previous chapter, approval and allocation decisions about environment-improving projects that appear to respond to environmental performance likely do so because borrowers with high environmental performance choose to pursue environment-improving projects.

evaluation and operational staff that country program evaluation should have the most direct impact on lending decisions among evaluation products. Thus, while it was not my original intention to examine aggregated evaluations, it became important to do so because they can be used to parse out whether the evaluation process itself provides sufficient incentives to use performance information. Thus, in the following section, I report on the expectation of MDB staff members about the influence of country program evaluations, which I use to derive hypotheses about the ways they should affect environment-improving programming.

6.2.1 Audience Effect

State shareholders of the MDBs are involved primarily in high-level and strategic decisions that in turn affect a broad range of day-to-day operational practices. Indeed, given the size and complexity of MDB operations, member states have very limited ability to monitor project-level decisions and performance outcomes, unless they are forced into the spotlight through the Inspection process (see Chapter 4). Explaining the source of slack between state preferences and World Bank behavior, Ascher comments that “the proliferation and increasing complexity of projects has reduced the capacity of the Executive Board to oversee the Bank’s operations with any mastery” (1983, p. 422). More broadly, states’ lack of ability to monitor the day-to-day operations at IOs has been cited as a key source of slack between state preferences and IO behavior (Lyne, et al., 2006).

Both operational and evaluation staff at the MDBs reported that country program evaluations are likely to have a larger influence over allocation decisions than project evaluations because they appeal directly to an audience of donor states, which at the World Bank and Asian Development Bank have a majority on the Board. Donor state shareholders have shown increasing interest both in promoting accountability for

performance. In addition, donor countries have typically been interested in increasing the supply of environment-improving lending. Recommendations to emphasize environment-improving operations in country program evaluations give donor countries a source of leverage in discussions with management and borrowing countries as part of the process for planning a country portfolio. One operational staff member at the World Bank comments that the country planning process is “where the action takes place” in terms of donor state shareholders expressing preferences about country lending portfolios.³ Thus, country program evaluations benefit from an engaged audiences that is capable of steering allocation decisions.

In practice, state shareholders most directly engage country program evaluations as part of the development effectiveness sub-Board committees that exist to oversee and improve the performance of bank operations. At both the World Bank and Asian Development Bank, the Development Effectiveness Committee meets to discuss all country program evaluations and is tasked with ensuring that recommendations are properly addressed before a final country assistance strategy come to the full Board for final approval. For each country program evaluation, high-level meetings are held between state representatives to the committee, vice-presidential level operational staff, and evaluation directors to discuss and address evaluation findings. At the Inter-American Development Bank the similar sub-Board committee is the Policy and Evaluation Committee. Thus, unlike project evaluations, state shareholders are well-appraised of the content and recommendations in country program evaluations. A recent World Bank assessment found that state representatives most often look at the recommendations in country program evaluations and the management’s plan to

³ For example, see the World Bank’s Operational Manual, Section BP 2.11 for Board involvement in development of the country assistance strategy.

address them in preparation for Board meetings where country assistance strategies are discussed and approved (Operations Evaluation Department [OED], 2005a).⁴

Other studies of influential evaluations have also found that accessing high-level decision-makers is important if evaluations are to have an influence on organizational practices. Scientific reports and evaluations that are influential at the international level almost always have the attention of key state decision-makers (Bamberger, 2000). Mitchell (2006) find that the influence of global environmental assessments must be understood in “relational” terms, that is the extent to which they are relevant, timely, and credible to a particular decision-making audience, rather than the specific content contained within assessments. In the context of the International Monetary Fund, Weaver (2010) finds that higher-level, cross-cutting evaluations, such as those on the process for conducting technical assistance work, often have the greatest influence on the organization because the Board is actually involved in those kinds of high-level strategic decisions. Selin (2006, p. 178) examine scientific assessments related to persistent organic pollutants and found that assessments that were push into “higher-level political agendas” were the most influential. Thus, because country program evaluations more effectively engage state shareholders with recommendations about performance, they should impact decisions about lending strategies more directly than project evaluations.

6.2.2 *Process Effect*

Country program evaluations are likely to have a more direct influence on allocation decisions than project evaluations because they are formally integrated into

⁴ The Development Effectiveness Committees are composed of a subset of Executive Directors that are tasked with considering evaluations and improving practices that contribute to development effectiveness at the MDBs. For more information about the formal structuring of the sub-Board committees at the World Bank Group, see: “Boards at World,” available at: <http://go.worldbank.org/R39ZLBTU10> (Accessed April 2011).

the process of designing new country assistance strategies, which in turn steer lending decisions (see Picciotto, 2002, p. 10). At several points in this process, the findings and recommendations in country program evaluations are considered by both member states and operational staff tasked with designing the country assistance evaluation. In contrast, when I spoke with evaluation staff at the MDBs, they could not identify a specific process that required bank management or state shareholders to actively address the recommendations in project evaluations. The common components of the country assistance strategy process across the MDBs are:

1. Evaluation department drafts country program evaluation.
2. Operational staff comment on country program evaluation draft.
3. Evaluation department finalizes country program evaluation.
4. Management issues a response to the recommendations in country program evaluation.
5. Evaluation department, sub-Board development effectiveness committee, and senior operational management meet to discuss the country program evaluation and management response.
6. Country team drafts concept note for country assistance strategy.
7. Evaluation department provides inter-departmental comment on concept note.
8. Country team drafts country assistance strategy.
9. Evaluation department provides inter-departmental comment on strategy draft.
10. Board members provide comments on strategy draft.
11. Country team prepares final country assistance strategy.
12. Board considers final country assistance strategy for approval.

Importantly, this process requires both the Board and operational staff to deal with the findings and recommendations of country program evaluations at several points. The country teams that are responsible for writing country assistance strategies pass drafts around to relevant technical and evaluation department for comments, both when the strategy is in a concept phase and when a full draft of the country assistance strategy is available. When evaluation staff comment on draft country assistance strategies, they use the finding and recommendations in country program evaluations as the basis for their comments. One evaluation staff member at the ADB reported that these comments are taken seriously by the team drafting the country assistance strategy,

because delays can be encountered if inter-departmental comments are not addressed properly in the opinion of Board members or senior operational management. In addition, operational management must also justify their response to the recommendations in country program evaluations to Board members, and the degree to which that properly addressed such recommendations are often critical parts of final Board discussions of country assistance strategies.⁵ To the extent that recommendations are incorporated into the strategy, they will influence lending decisions, since new projects must reference how they support the overall country assistance strategy.⁶

Institutional processes constrain the ways that information is used within organizations. Accordingly, most research on the utilization of evaluations has found that the integration of evaluations into decision-making processes is more important than evaluation content. For instance, Clark and colleagues (2006, p. 14) find that global environmental assessments become influential not by containing certain types of content, but rather that they are well integrated into “the social process of assessment.” Information in the form of assessments, analysis, and evaluation are often most influential when they have a clear and institutionalized role in some specific decision (Hansson, 2006). Patton (2008), a pioneer in utilization focused evaluation, argues that useful evaluation recommendations must be formulated in ways that directly address the context of decision-making, recognizing possible constraints in carrying out recommendations in collaboration with a specific decision-making audience. Thus, influential evaluations must focus not only on the credibility and validity of findings,

⁵ Many country program evaluations contain an actual “management response,” which is the formal place where management indicates how it will act on recommendations contained in country program evaluations. An analysis of the use of country program evaluations indicated that this management response often figure prominently in Board discussion of country assistance strategies (Operations Evaluation Department [OED], 2005a).

⁶ Operational staff at the Inter-American Development Bank have been less constrained by planning documents according to interviews, which often leads to a higher “improvisation rate.” This is the proportion of project that were not planned, but are eventually approved.

but must be designed back on the identified decisions they intend to influence. This arguments echoes much of the evaluation literature that has thought of influential evaluations as a collaborative process between decision-makers and evaluators (Mathison, 1994; Torres & Preskill, 2001; Weiss, 1998).

6.2.3 *Information Aggregation Effect*

Decision-makers in large organizations must often account for dispersed sources of information when making strategic decisions, and establishing a country assistance strategy is no exception. Research on strategic decision-making has focused on the ability of decision-makers to easily access synthesized information as being key to making good decisions in high information environments (Hardy, 1982; O'Reilly, 1982). Indeed, one of the primary challenges is not so much the lack of information, but the organization of information into forms that are usable to decision-makers. As one evaluator at the World Bank stated, country program evaluations have the advantages of driving operational changes because they address issues that cut across multiple projects. Most systematic operational changes at the MDBs occur in response to the development of new policies or lending strategies.

This point has not gone unnoticed by scholars who are interested in the utilization of evaluations within organizations. As Feinstein (2002, p. 436) writes, "evaluation use capacity involves a capacity to search for relevant information." Even if state shareholders wanted to seek out environmental performance information in the context of advising the adoption of country lending strategies, they would face extremely high transaction costs in processing diverse streams of performance information that accumulate within the MDBs. Indeed, Weaver (2008, p. 70) is skeptical that the Board can provide oversight for the MDBs because "supervision of policies and programs requires extensive time and expert resources." Thus, to the extent that country

program evaluations aggregate performance information and utilize more macro-level metrics of evaluation (Gutner & Thompson, 2010), they solve information problems for the principals of the MDBs in ways that project evaluations cannot. Indeed, scholars have argued that the primary reason donor countries have push to establish independent evaluations at IOs is “to reduce information asymmetries to enable donors to better hold Fund staff and management to account for process and outcome performance” (Weaver, 2010, p. 378). Indeed, many operational staff that I spoke with at the MDBs identified high-level, thematic evaluations are more influential because they were able to synthesize highly dispersed performance information across programs to identify operational practices in need of attention.

It is not only through appealing to donor countries with synthesized information that evaluations are likely to be more influential. Evaluation offices also view MDB management and staff as important stakeholders, and they must also search out diverse sources of dispersed information when making decisions about individual projects and designing longer-term strategies. Thus, country program evaluations might also help MDB staff to organize performance information in ways that can lead to better decisions. A recent OED assessment found influential evaluations tend to aggregate findings across projects (Operations Evaluation Department [OED], 2004). A similar review at the Asian Development Bank also found that aggregate evaluations were most influential (Operations Evaluation Department [OED], 2007e, sec. 7). A review of the IMF Independent Evaluation Office finds that senior staff found synthesizing reports most useful for reflecting on broad strategic issues (Lissakers, Husain, & Woods, 2006, p. 23). Thus, country program evaluations may also be useful to state shareholders and operational staff alike, since they both work under information rich conditions.

6.2.4 *Hypotheses*

The MDB staff that I interviewed expected that the findings and recommendations contained in country program evaluations should have more of a direct effect on lending decisions than the findings contained in project evaluations. As I found in the previous chapter, there appears to be only limited responses to performance information contained in project evaluations, and those responses are likely to reflect the underlying incentives of the MDB bureaucracies, rather than being a direct response to evaluation findings. Given the audience, process, and information aggregation effects that should accompany country program evaluations, I test whether the provisioning of information within a formalized decision process can create sufficient incentives for the MDBs to alter their allocation decisions. In particular, I expect that donor state representatives will use recommendations suggesting a focus on environment-improving operations to establish environmental operations as a strategic priority in the associated country assistance strategy.

However, unlike environmental safeguard policies, there is no “hard incentive” for MDB operational departments to agree with country program evaluation recommendations. Indeed, the formal management responses to such recommendations often take issue with the premise of the recommendations. As one former country director at the World Bank stated, the management response is where operational units “give the [evaluation department] actual facts.” Given the lack of uniform incentives to respond to evaluation recommendations, I am able to test whether evaluation can have a direct impact of allocation decisions. Like the previous chapter, I test whether clean-energy and urban environment operations are more likely in countries that have country program evaluation recommendations suggesting a focus in these areas. Given that MDB operational staff might respond to such recommendations by adding

environment-improving project components to larger development projects, I also test the influence of recommendations for both project with primary environment-improving purposes and projects with smaller environment-improving activities:

Hypothesis 1a: Borrowing countries that receive a recommendation to focus on clean-energy operations will receive more projects with a primary clean-energy purpose.

Hypothesis 1b: Borrowing countries that receive a recommendation to focus on clean-energy operations will receive more projects of any type that have clean-energy components.

Hypothesis 2a: Borrowing countries that receive a recommendation to focus on urban environmental operations will receive more projects with a primary urban environment purpose.

Hypothesis 2b: Borrowing countries that receive a recommendation to focus on urban environmental operations will receive more projects of any type that have urban-environment components.

6.3 Data

Country program evaluations are more recent products, with the first official evaluation conducted by the World Bank Operations Evaluation Department in 1995 for

Ghana.⁷ The Asian Development Bank soon followed suit, completing its first country program evaluation for China in 1998. In 2001, the African Development Bank and Inter-American Development Bank evaluation departments completed their first country program evaluations (Figure 13). However, since that time, the country program evaluation has grown into being a primary product of each of the evaluation offices, rising in numbers each period, with the exception of the World Bank Independent Evaluation Group.⁸

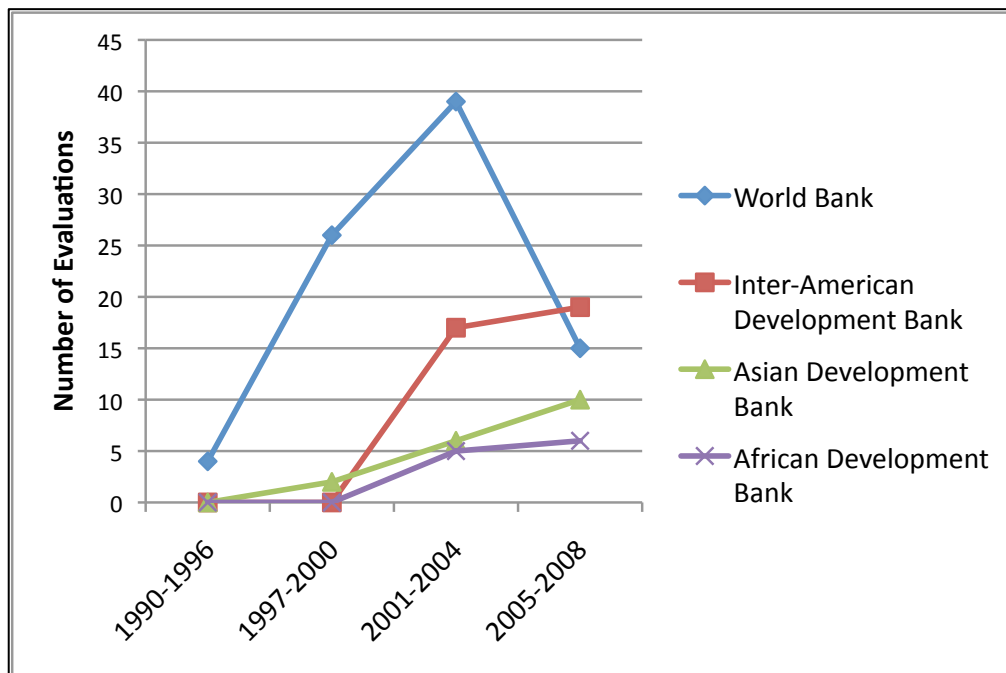


Figure 13: Number of Country Program Evaluations, 1990-2008

Country program evaluations are intended to sum up the performance lessons that have been realized through the implementation of projects over the course of several years. Within country program evaluations, a wide variety of sectors are

⁷ The World Bank conducted very similar evaluations since 1990 that were not officially designation country program evaluations, but are included in the database of country program evaluation documents. Those prior evaluations are included in the analysis presented here.

⁸ In recent years, the Independent Evaluation Work program has focused on special evaluation studies of particular importance to the Board of Executive Directors.

evaluated for general operational lessons. Environmental performance information does not enjoy any special emphasis. Thus, the inclusion of environmental performance information in country program evaluations is dependent on the emphasis with which evaluators believe environmental performance is to achieving broad, country-level economic and institutional outcomes. Indeed, across the different MDBs, there is substantial variation in the extent to which environmental performance information appears in evaluations.

In order to examine whether environmental performance and relevant recommendations in country program evaluations influenced lending decisions, I assembled a team to code whether 21 binary items related to environmental performance appear in each of the country evaluations that have been completed since 1990 by each of the four MDBs considered in this section. Rather than attempting to code performance on ordinal scale, as with project evaluations, we found it more reliable to code whether specific pieces of information were present in the different sections of the country program evaluations. This was important for the analysis presented below because I am able to understand how environmental performance information becomes part of different sections of country program evaluations (e.g., executive summary or recommendations), which are likely to receive different levels of attention from both MDB operational staff and also donor countries through the Board.

The coding procedure (described in greater detail in Appendix 1), focuses on four main sections of the country program evaluations. First, it is often the executive summary that receives the most attention by higher-level decision makers, thus we coded whether the country evaluation recognized environmental programs as a priority within a particular borrowing country and whether environmental performance information was contained in the executive summary. Second, it is important to note

whether evaluators considered environmental issues to be an important area of concern for a particular borrower, thus we coded a variety of items on whether background information identified environmental degradation as a development constraint. Third, we coded whether both negative and positive environmental performance information was included in the analytical section of country programs that document and synthesize program outcomes. Finally, we coded whether final recommendations were made to emphasize environmental project or institutional development in future periods, given that the MDB management must formally respond to the recommendations that are part of country program evaluations in many instances. **Table 10** contains descriptive information for the coded items that will be important for the analysis presented below. The percentages show the proportion of evaluations that were positive on a particular coding item.⁹

⁹ The environmental performance variables are not mutually exclusive.

Table 10: Descriptive Data on Selected Items Coded from Country Program Evaluations, 1990-2008

MDB	World	IADB	ASDB	AFDB
Total Country Evaluations	84	36	18	11
Environment identified as programmatic priority (ES)	14%	24%	33%	0%
Concern over degradation of global environmental resources (B)	8%	9%	28%	0%
Concern over environmental degradation for local well-being (B)	42%	28%	61%	27%
Specific evaluation section dealing with environmental performance (PP)	40%	25%	78%	45%
Unsatisfactory environmental outcomes (PP)	40%	41%	72%	9%
Unsatisfactory borrower environmental implementation (PP)	24%	19%	44%	0%
Satisfactory environmental outcomes (PP)	45%	38%	61%	45%
Satisfactory borrower environmental implementation (PP)	15%	0%	5%	0%
Emphasize any environmental goals in future lending (R)	20%	8%	33%	9%
Emphasize clean-energy goals in future lending (R)	4%	0%	11%	0%
Emphasize urban environment goals in future lending (R)	6%	3%	17%	0%

Percentage is present, divided by total where the relevant section was present. The following abbreviations are used to identify which sections of the country evaluations is coded for each item: Executive Summary (ES); Background (B); Project Performance (PP); Recommendations (R).

The World Bank and the Asian Development Bank have higher densities of environmental performance information and environmentally relevant recommendations than the Inter-American and African Development Banks. This reflects prevailing wisdom that the IADB and AFDB have places less emphasis on environment improving operations, perhaps owing to the fact that borrowing countries

enjoy majorities on their Boards. One of the other striking findings in the descriptive data is despite the IADB focus on environmental performance in country program evaluations, recommendations about future environment-improving operations are almost never made. Because the IADB and AFDB do not make many recommendations based on environmental performance, it could not be expected that they will have an additional effect on future lending decisions.

6.4 Modeling the Influence of Country Program Evaluation Recommendations

This section tests whether the findings and recommendations that come out of country program evaluations have a discernable influence on lending decisions, both for stand-alone clean energy and urban environment projects, and any project that has components in these areas. To understand whether recommendations have independent impacts on lending decisions beyond performance, I control for environmental performance as reported by each country program evaluation in the body of the evaluation text. Because internal studies of evaluation use have indicated that Board members rarely use information from the body of evaluation texts in their discussions of country strategies (Operations Evaluation Department [OED], 2005a, Annexes C-D), this empirical strategy controls for background performance information that is likely available to operational staff. As a result, any additional effect from recommendations indicates that evaluations exert a direct influence on lending decisions.

As was presented in Chapter 5, I examine approval decisions made about clean-energy and urban-environment project, allowing me to confirm responsiveness to performance information from a different data source. In all of the models reported below, I employed a random-intercept probit model as in previous chapters, unless otherwise noted. The unit of analysis is the country-year. In most cases, I examine the

effect of evaluation findings and recommendations on both the full panel and within the subset of years covered by a country program evaluation to control for possible selection bias of being subjected to country program evaluations and to examine whether recommendations contribute to a “treatment effect” for any country that receives one.

In this chapter, I introduce several new binary variables that were coded from country program evaluations as described above. POOR ENV. PERFORMANCE and GOOD ENV. PERFORMANCE are positive when unsatisfactory or satisfactory achievement of environmental goals are noted to be the results of borrowing country performance. At some of the MDBs, particularly the Asian Development Bank, identifying poor borrower country performance is not a norm, thus only satisfactory environmental outcomes (GOOD ENV. OUTCOME) and unsatisfactory environmental outcomes (POOR ENV. OUTCOME) were available to be coded.

I split recommendations into three separate variables in order to examine the impact of recommendations on lending decisions. First, ENV. RECOMMENDATION indicates that a recommendation was made to increase lending emphasis on any environment-improving target. By contrast, CLEAN ENERGY RECOMMENDATION and UEI RECOMMENDATION are subsets that indicate a recommendation was made specifically about clean energy or urban environment-improving lending. Lending responses to these variables are the primary outcomes of interest. In all cases, the binary variables from the country program evaluations become positive beginning the year after the evaluation is completed and discussed by the Board.

6.4.1 Clean Energy Projects and Project Components

Table 11 displays regression results for the approval of clean-energy projects by the World Bank and Asian Development Bank. The Inter-American Development Bank had only one clean-energy project approved during a year covered by a country

program evaluation and the African Development Bank does not have a portfolio of clean energy projects. For this reason, it was not possible to specify models for these MDBs. For the World Bank, it was possible to examine both the effect of clean energy recommendations and general environmental recommendations. For stand alone clean-energy, in no case did either specific or general environmental recommendations increase the probability of receiving clean-energy projects in future years. For the World Bank, there was no discernable effect of clean-energy recommendations on clean-energy lending (Models 1a/1c). In both the full panel and the subset, countries that have higher carbon emissions were more likely to receive clean energy recommendations and this colinearity made estimates of the effect of emissions insignificant. If the clean-energy recommendation is omitted from the regression then carbon emissions becomes strongly significant, but not vice versa. This indicates that clean-energy recommendations do not influence future lending decisions. Instead it seems likely that recommendations follow the perceived donor need to be involved in clean energy project in countries that substantially influence climate outcomes.

For country programs that received recommendations to emphasize any environmental targets, there was actually a decrease in clean-energy lending during future years (Models 1b/1d). Given that more World Bank recommendations focused on natural resource management and urban environmental improvements, this result suggests that countries in need of financing for basic natural resource management activities were not likely to receive clean energy financing, likely because they are not significant global emitters. For the Asian Development Bank, I find no evidence that environmental recommendations increase clean energy financing in future years (Models 2a). In fact, for country-years that are covered by country program evaluations

and environmental recommendations in any sector never receive clean energy projects in this sample (Model 2b).

Table 11: Approval Decisions About Clean-Energy Projects

Model	1a	1b	1c	1d	2a	2b
MDB	World	World	World	World	Asian	Asian
CLEAN ENERGY RECOMMENDATION	0.13 (0.74)		-2.37 (2.83)			
ENV. RECOMMENDATION		-1.12* (0.63)		-2.48* (1.49)	-0.09 (0.08)	<u>0 7</u> 9 30
POOR ENV. PERFORMANCE	0.22 (0.34)	0.34 (0.35)	0.08 (0.33)	0.14 (0.35)		
GOOD ENV. PERFORMANCE	0.22 (0.42)	0.60 (0.46)	0.11 (0.40)	0.17 (0.44)		
POOR ENV. OUTCOME					-0.01 (0.06)	<u>7 0</u> 22 17
GOOD ENV. OUTCOME					0.10 (0.07)	<u>7 0</u> 16 23
BANK PRIORITY			0.55* (0.33)	0.90** (0.38)		<u>7 0</u> 16 23
GLOBAL IMPORTANCE			-0.76 (0.61)	-0.67 (0.60)		<u>6 1</u> 10 29
CO2.GT	0.95 (0.69)	1.46** (0.63)	2.66 (1.87)	2.24** (1.08)	0.38** (0.07)	
CONCESSIONAL	-0.60** (0.26)	-0.59** (0.26)	-0.18 (0.29)	-0.25 (0.29)	-0.04 (0.03)	
No. PROJECT	0.11** (0.03)	0.10** (0.03)	0.08* (0.05)	0.11** (0.05)	0.01** (0.00)	
Random Intercept Variance	0.457	0.481	0.000	0.000	0.000	
Data Subset	fp	fp	cce	cce	fp	cce
Model Type	rip	rip	rip	rip	rilpm	Cross-tabs (DV +) (DV 0)
Observations (Countries)	1347 (134)	1347 (134)	381 (68)	381 (68)	285 (38)	46 (12)
Residual Deviance	337.5	332.9	118.9	109.4	86.79	
Null Deviance	371.9	371.9	140.5	140.5	275.6	

Statistical significance: * p < 0.1, ** p < 0.05

Data subsets: fp – full panel; cce – covered by country evaluation.

Model Type: rip – random-intercept probit; rilpm – random intercept linear probability model.

Confirming results from the previous chapter, environmental performance reported in country program evaluations does not influence clean-energy lending.

Instead, the level of carbon emissions of a borrowing country is a consistent and strong predictor about whether clean-energy projects are approved (Models 1a-2b). As expected, countries that received more total numbers of projects are more likely to receive clean energy projects. In addition, for the World Bank, when a country program evaluation identifies the environment as an existing lending priority, a borrowing country is more likely to receive a clean energy project following a country program evaluation (Models 1c/1d).

It may be the case that recommendations to pursue environmental or clean-energy goals in future lending does not influence the allocation of stand alone projects, but rather whether clean energy activities are incorporated into other types of projects. Indeed, the type of “environmental mainstreaming” has been one of the primary ways that the MDBs have met commitments to increasing their emphasis on environmental sustainability (Findley, et al., 2009). In order to identify which projects have clean-energy activities, I utilized activity codes from AidData and included any project with renewable energy activities (excluding large hydropower) and/or energy conservation activities (Findley, et al., 2009).

Similar to the results reported above, I do not find evidence that recommendations or performance information contained in country program evaluations exert a discernable effect on lending decisions about projects with clean energy components (**Table 12**, Models 3a-4b). Instead, the level of carbon emissions from a particular borrowing country continues to be the primary predictor of whether projects with clean-energy components are approved. The only case where carbon emissions is not a statistically significant predictor (Model 3b), occurs because having a clean energy recommendation is collinear with carbon emissions. For purposes of consistent exposition, both variables are included in Table 12.

Table 12: Approval Decisions About Projects with Clean-Energy Components

Model	3a	3b	4a	4b
MDB	World	World	Asian	Asian
CLEAN ENERGY RECOMMENDATION	-0.87 (0.78)	-1.02 (1.33)		
ENV. RECOMMENDATION			0.53 (0.76)	0.25 (0.79)
POOR ENV. PERFORMANCE	-0.12 (0.24)	-0.13 (0.25)		
GOOD ENV. PERFORMANCE	0.41 (0.28)	0.38 (0.29)		
POOR ENV. OUTCOME			-0.25 (0.56)	0.13 (0.74)
GOOD ENV. OUTCOME			-0.44 (0.65)	0.02 (0.82)
CO2.GT	1.21** (0.40)	1.43 (0.94)	3.23** (0.84)	2.24** (1.12)
CONCESSIONAL	-0.01 (0.12)	0.13 (0.22)	0.06 (0.30)	-0.24 (1.24)
No. PROJECT	0.08** (0.02)	0.05 (0.04)	0.07** (0.03)	0.02 (0.07)
Random Intercept Variance	0.000	0.000	0.130	0.000
Data Subset	Full Panel	Covered by Country Evaluation	Full Panel	Covered by Country Evaluation
Model Type	Random-Intercept Probit	Random-Intercept Probit	Random-Intercept Probit	Random-Intercept Probit
Observations (Countries)	1347 (134)	381 (68)	285 (38)	44 (12)
Residual Deviance	610.4	209.8	172.9	25.1
Null Deviance	653.0	224.5	199.7	38.5

Statistical significance: * $p < 0.1$, ** $p < 0.05$
All models are random-intercept probit

For the Inter-American Development Bank, in no case was a project with a clean-energy component approved following a recommendation to emphasize environmental targets in future lending strategies. While the lack of recommendations makes it impossible to model a response to recommendations, this offers further support that the content of country program evaluations are not driving lending decisions related to clean-energy. Taken together, the results in this section do not support the proposition that country program evaluations influence lending decisions related to clean energy. In

many cases, recommendations related to clean energy are not available and when they are, they do not exert a discernable influence on project approval decisions. This suggests that having to respond to evaluation content alone does not produce sufficient incentives for the MDBs to pursue performance-based allocation decisions.

6.4.2 Urban Environment Projects and Project Components

More recommendations were made in the country program evaluation considered here about achieving urban environment-improving goals than about clean-energy investments. Thus, examining recommendations related to urban environment investments may offer a better test of the direct influence exerted by the country evaluation process. However, as displayed in **Table 13**, recommendations in country program evaluations did not have a discernable influence on urban environmental projects at any of the development banks (Models 5a-7b). At the Inter-American Development Bank, a sufficient amount of recommendations were not available to enable modeling of the influence of recommendations. Likewise for the African Development Bank, an urban environment projects was approved for only one year covered by a country program evaluation, making modeling impossible.

**Table 13: Approval Decisions About Urban Environment-Improving Projects
(Random-Intercept Probit)**

Model	5a	5b	6a	6b	7a	7b
MDB	World	World	Asian	Asian	IADB	IADB
UEI RECOMMENDATION	0.14 (0.49)	0.17 (0.45)				
ENV. RECOMMENDATION			-0.11 (0.70)	2.06 (1.86)		
POOR ENV. PERFORMANCE	-0.43 (0.30)	-0.58** (0.29)				
GOOD ENV. PERFORMANCE	0.46 (0.31)	0.50* (0.29)				
POOR ENV. OUTCOME			0.23 (0.48)	1.14 (2.62)	-0.13 (0.48)	1.45 (1.46)
GOOD ENV. OUTCOME			0.34 (0.54)	0.97 (0.92)	0.09 (0.56)	0.75 (0.70)
POLLUTION BURDEN	0.00 (0.00)	-0.00 (0.01)	-0.18 (0.34)	1.46 (1.59)	-0.00 (0.01)	0.04 (0.03)
CONCESSIONAL	-0.90** (0.16)	-0.57** (0.24)	-0.62* (0.35)	-2.65 (1.81)		
K.GDP PER CAPITA					0.00 (0.06)	-0.16 (0.19)
No. PROJECT	0.14** (0.02)	0.16** (0.03)	0.12** (0.04)	0.30* (0.15)	0.16** (0.03)	0.08 (0.06)
Random Intercept Variance	0.133	0.000	0.147	0.000	0.000	0.000
Data Subset	fp	cce	fp	cce	fp	cce
Observations (Countries)	1294 (127)	380 (68)	254 (29)	44 (12)	348 (25)	58 (19)
Residual Deviance	621.0	214.4	154.3	18.8	191.8	28.8
Null Deviance	699.8	260.8	173.0	34.5	223.0	38.6

Statistical significance: * p < 0.1, ** p < 0.05

Data subsets: fp – full panel; cce – covered by country evaluation.

Confirming what I found in the previous chapter, World Bank borrowing countries that have poor environmental performance will receive fewer urban environment projects in future years and borrowing countries with good environmental performance receive more of these projects for years covered by country evaluations (Model 5b). However, this result is not statistically significant when examining the full panel, indicating that the identification of performance by the country program evaluation does not function as a “treatment” that directly causes this response. For both

the World Bank and Asian Development Bank, more urban environment projects are approved for middle-income countries that have access to market-rate lending resources (Models 5a-6a).

Like above, it is possible that environmental recommendations in country program evaluations primarily cause the “mainstreaming” of urban environment project components into traditional projects, such as including a sewerage components in a water supply project. Thus, I used AidData activity codes to identify all projects with urban environment components, including all activity codes related to waste management, sewerage, and urban pollution abatement. Thus, the dependent variable becomes a project with any component in these areas.

As displayed in **Table 14**, both general environment recommendations and recommendations specific to urban environmental project fail to have a discernable influence on decisions to include environmental components in urban projects (Models 8a-9b). This again indicates that country program evaluations do not have a direct impact on lending decisions despite their audience, process, and information aggregation advantages. What is remarkable, however, is that across the MDBs there appears to be performance-based allocation happening with regards to performance findings. For the World Bank, while there does not appear to be a “treatment effect” of having environmental performance noticed in a country program evaluation (Model 8a), among country-years covered by country program evaluations, poor environmental performers are significantly less likely to receive projects with urban environment-improving components (Model 8b). For the Asian Development Bank, it does appear that recognition of good environmental outcomes in a country program evaluation is associated with increased probability of receiving a project with an environmental component in future years (Model 9a). However, due to extremely low coverage of

country program evaluations, I was not able to confirm this effect within the country years covered by evaluations (Model 9b). For the Inter-American Development Bank, borrowing countries that are noted as achieving poor environmental outcomes are less likely to receive projects with urban environment components in future periods (Model 10a). Again, this result cannot be confirmed in the subset of country-years covered by evaluations (Model 10b).

Table 14: Approval Decisions About Projects with Urban Environment-Improving Components

Model	8a	8b	9a	9b	10a	10b
MDB	World	World	Asian	Asian	IADB	IADB
UEI RECOMMENDATION	0.13 (0.40)	0.13 (0.38)				
ENV. RECOMMENDATION			-0.36 (0.58)	-0.46 (1.12)		
POOR ENV. PERFORMANCE	-0.25 (0.21)	-0.35* (0.21)				
GOOD ENV. PERFORMANCE	0.35 (0.26)	0.34 (0.25)				
POOR ENV. OUTCOME			0.04 (0.41)	-0.63 (1.06)	-0.81* (0.45)	-0.36 (0.55)
GOOD ENV. OUTCOME			0.95** (0.47)	0.75 (0.88)	0.08 (0.51)	0.52 (0.62)
POLLUTION BURDEN	0.00 (0.00)	-0.00 (0.00)	-0.44 (0.30)	0.13 (1.18)	0.01 (0.00)	0.01 (0.02)
CONCESSIONAL	-0.41** (0.11)	-0.29 (0.19)	-0.55** (0.27)	-0.74 (1.16)		
K.GDP PER CAPITA					-0.08* (0.05)	-0.21 (0.17)
No. PROJECT	0.14** (0.02)	0.16** (0.03)	0.12** (0.03)	0.15 (0.12)	0.18** (0.03)	0.18** (0.08)
Random Intercept Variance	0.065	0.000	0.085	0.341	0.028	0.000
Data Subset	Full Panel	Covered by Country Evaluation	Full Panel	Covered by Country Evaluation	Full Panel	Covered by Country Evaluation
Observations (Countries)	1294 (127)	380 (68)	254 (29)	44 (12)	348 (25)	58 (19)
Residual Deviance	1122	355.7	215.6	39.9	321.9	45.8
Null Deviance	1196	391.2	238.5	44.2	364.5	56.3

Statistical significance: * p < 0.1, ** p < 0.05

For the African Development Bank, countries that received projects with urban environment components were never identified as having the environment as a bank priority or poor environmental outcomes, making modeling impossible. Taken together, the results of these models do not support any of the hypotheses that the country program evaluations process has a direct effect on lending decisions in future periods.

Instead, the results confirm that clean-energy project mainly respond to the global importance of borrower countries as emitters and the urban environmental project decisions respond to performance, rather than recommendations. These findings suggest that evaluations are not a direct cause of lending decisions. An explanation of this finding is contained below.

6.5 Why Do Country Program Evaluations Lack Influence On Lending Decisions?

In the models presented above, I find no evidence that the findings and recommendations present in country evaluations influence lending decisions about environment-improving projects, other than in ways that I observed previously. Instead, I continue to find that other factors are better predictors of whether particular countries receive clean energy or urban environment projects, including the level of carbon emissions, whether environmental programming was already a priority in a given country, and the size of the country project portfolio. This is a puzzling result, given the belief of several MDB staff that country program evaluations would have a direct effect on country strategies, and thus lending decisions. From this finding, it appears that the formalized process of creating country assistance strategies has not created sufficient “hard incentives” for operational management to respond to recommendations. In this section, I address reasons why the recommendations in country program evaluations appear to have such a limited impact.

In particular, there are several impediments to the *direct* use of evaluation information in decisions about country strategies and portfolio composition decisions. First, environmental performance information in country program evaluations is not perceived as being credible. Second, many country evaluations do not analyze and make recommendations about environmental performance, thereby limiting any effect they

might have on future project approval decisions. When recommendations are made, they often address implementation concerns, rather than advocate for selectivity. Third, although the country program evaluations are formally considered in the process of country strategy planning, the systems in place to monitor the *implementation* of recommendations are weak in many cases. Forth, the ability of operational staff to follow the recommendations of coming out of country program evaluations, especially those advocating greater focus on environmental activities, are constrained by the lack of borrowing country demand for increased environment-improving investments.

6.5.1 Lack of Credible Connection Between Environmental Performance and Recommendations

One of the key advantages of country program evaluations over project evaluations is that they are able to compile dispersed performance information and present that information to important decision-making audiences. However, given that MDB management has the opportunity to respond to country program evaluations through management comments and present those views to the Board, it is important that the country program evaluations present credible performance information in order to have influence in higher level decisions about environment-improving lending. Indeed, interviews that I conducted with operational staff suggest that a perceived lack of credibility is often a key reason evaluation findings and recommendations are discounted in management responses.

There is significant variation in the degree to which country program evaluations at the different MDBs effectively compile environmental performance information from project evaluations. In Figure 14, the country program evaluations of each MDB are divided into three columns: (1) a light green column that indicates no project evaluation during the five years prior to the country program evaluation documenting satisfactory

environmental performance; (2) a green column that indicates one project evaluation during the previous five years documenting satisfactory environmental performance; and (3) a dark green column that indicates multiple project evaluations during the previous five years documented satisfactory environmental performance. Each of those columns is divided between the country evaluations that document satisfactory environmental performance on the part of the borrowing country (shaded) and those that do not (white).

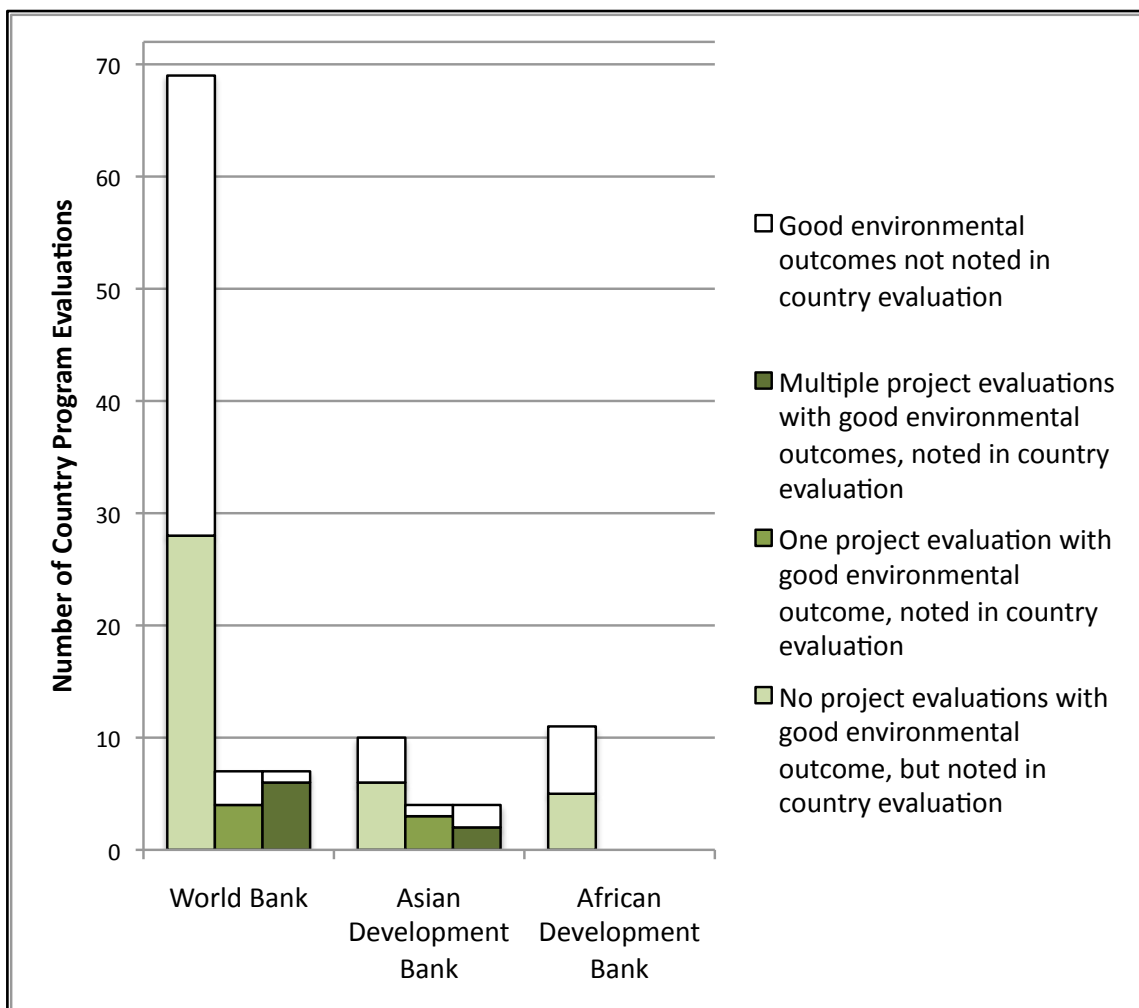


Figure 14: From good environmental performance in project evaluations to similar finding in country program evaluations

As displayed in Figure 2, the World Bank is the only one of the MDBs where strength of environmental performance information reflected in project evaluations is related to the probability that a country program evaluation will include information about satisfactory environmental outcomes. Less than half of country program evaluations for countries document satisfactory environmental performance when corresponding project evaluations are not available. All but one country program evaluation where the borrowing country has multiple project evaluations documenting

good environmental performance contain this information. Thus, from descriptive data it appears that the World Bank does a reasonable job of compiling environmental performance information in a credible way. This relationship does not hold for the Asian Development Bank, which has a higher proportion of country evaluations without relevant project evaluations documenting good environmental performance than it does for country evaluations that have multiple project evaluations documenting good performance. The African Development Bank did not have a sufficient number of country evaluations with multiple project evaluations to examine this trend.

I find a very similar pattern when examining whether findings of marginal or unsatisfactory environmental performance as documented in project evaluations are compiled in country program evaluations (Figure 15). For the World Bank, the number of available project evaluations that document poor environmental performance is a good predictor about whether a country program evaluation will raise concerns about poor achievement of environmental goals at the programmatic level. This relationship does not hold for the Asian Development Bank. For the African Development Bank, when available project evaluations document poor environmental performance, this information does not become part of the findings of country program evaluations.

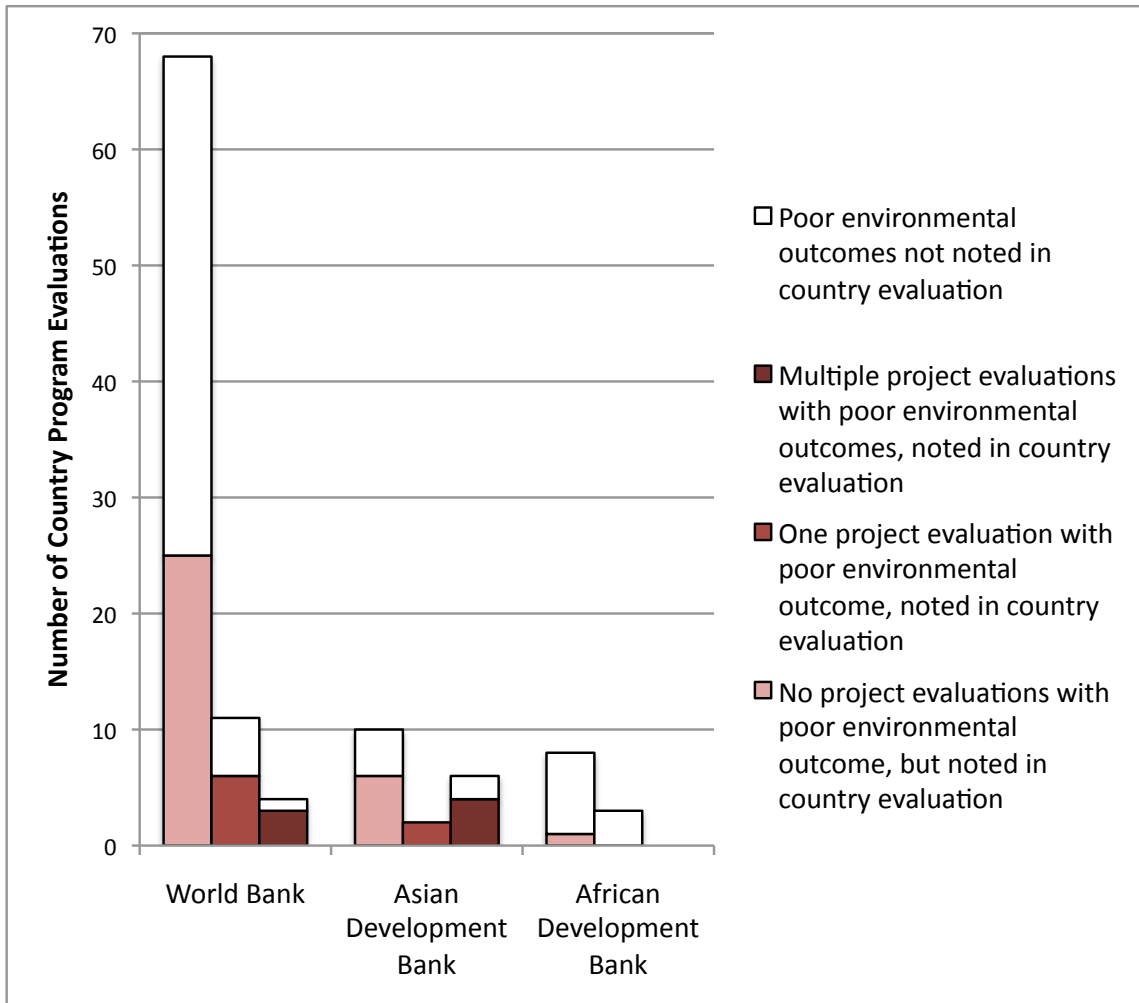


Figure 15: From Poor Environmental Performance in Project Evaluations to Similar Findings in Country Program Evaluations

These data speak to difficulty of aggregating dispersed performance information in ways that could be considered credible to operational staff. If evaluators that are tasked with compiling this information find it difficult to do so (other than for the World Bank, it seems), then there is further evidence that organizations should be less likely to respond to project-level evaluations because of difficulties aggregating information in credible ways. In that case, country program evaluations might prove to be less influential for environmental operations than was expected by MDB staff.

Given that country program evaluations draw performance information from a variety of sources, including project evaluations, thematic evaluations, project completion reports, and project supervision data, it may be the case that they represent a more holistic picture of environmental performance. However, if findings about environmental performance do not become recommendations, there is less opportunity for country program evaluations to leverage audience and process effects, and thereby promote performance-based allocation. Formally, the MDB management must respond to the recommendations contained in country program evaluations, including the operational steps that will be taken to address the recommendations. Thus, before examining whether the content of country program evaluations influence environment-improving lending decisions, it is important to understand how the different evaluation offices turn findings into recommendations.

As displayed in Figure 16, there is significant variation between the MDBs in how findings about environmental performance become operational recommendations for the Board and management to consider when designing a multi-year lending program. Both the World Bank and Asian Development Bank produce more environment related recommendations. Thus, their country program evaluations should have a higher probability of influencing lending decisions because of requirements for a management response. The Inter-American Development Bank and African Development Bank only turn findings about operational outcomes into operational recommendations on rare occasions, leaving little room to influence lending decisions.

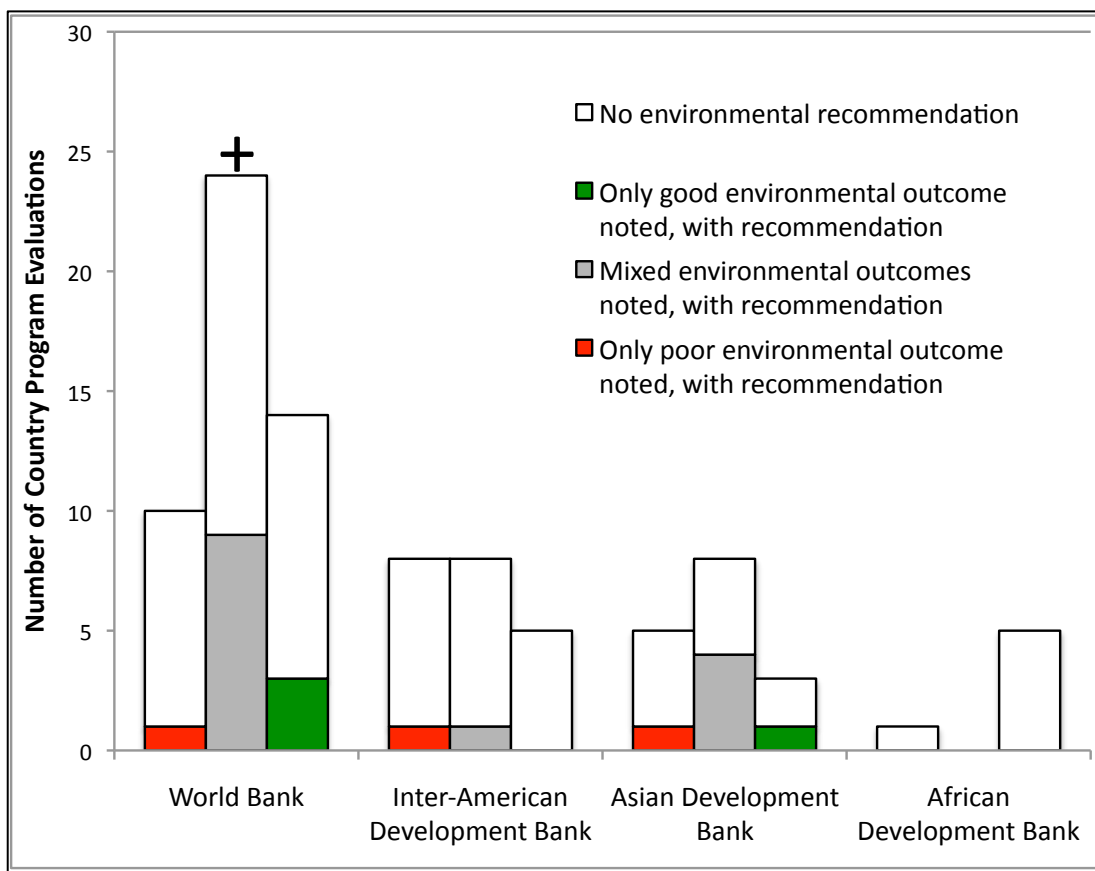


Figure 16: From country program evaluation findings to recommendations

However, it is interesting to note that for both the World Bank and the Asian Development Bank, recommendations to emphasize environment-improving lending tend to be for countries that have a mixed environmental performance record. Thus, even if these recommendations were followed, it would not necessarily lead to the observation of performance-based decision-making. Instead, recommendations might be more fruitfully viewed as addressing design issues in countries where environmental operations have room for improvement.

6.5.2 *Lack of Selectivity Inducing Recommendations*

Although staff of all types highlighted the country program evaluation as the key product that should influence lending decisions, due to process, audience, and information aggregation effects, those expectations do not hold related to decisions about environment improving projects. While it may be possible that the country program evaluations are highly influential for other sectors or project types, the data collected as part of this project shows that these evaluations either do not emphasize or have not engaged with future environmental lending decisions. In the case of the Inter-American Development Bank and African Development Bank, recommendations about environment-improving operations rarely appear. For the Inter-American Development Bank, I found that only two of 36 evaluations that made any sort of environment related recommendation, and in those cases neither clean energy or urban environmental projects were the subject matter. For the African Development Bank, only one of 11 evaluations included an environment related recommendation, and it was highly general in nature and did not pertain specifically to urban environmental projects. Thus, given the lack of focus these country evaluations paid to environmental performance, it is no surprise that they did not influence future lending decisions about environmental operations.

The lack of engagement with environmental performance was further evidenced by the interviews I completed at these MDBs. At the Inter-American Development Bank, one operational staff that was involved in country-level planning indicated that Country Environmental Assessments are the primary mechanism through which environmental considerations are introduced into the country planning process. These assessments tend to be forward looking and identify the “need” for environment improving projects, rather than focusing retrospectively on what operations were successful or unsuccessful.

This approach to environmental planning mirrors donor pressures to mainstream environmental considerations through increased investment, rather than focusing on selectivity. Furthermore, IADB policy staff emphasized that evaluations had little ability to generate robust lesson because environment performance information is still generally unavailable, not being a part of project monitoring until very recently. Indeed, when I met with policy staff in 2009, which is after the conclusion of the data considered here, I was told that the IADB is still trying to set up a formalized way to monitor environmental performance in the course of normal project activities. Given the lack of baseline data or environmental monitoring, evaluators have not been in a position to engage seriously with environmental performance at the IADB.

The African Development Bank evaluation department is in a similarly weak position in terms of engagement with environmental performance issues. Until very recently, there was little review of the quality of country strategies, and a “pilot quality review” process for country strategies was met with significant opposition from operational staff, according to interviews with policy staff. Evaluation staff reported on the severe limitation that they faced in engaging seriously with environmental performance. Because environmental performance has only recently become a larger concern at the AFDB, most projects that were completed and evaluated in time to be included in the sample considered here have very limited environmental ambitions. This means that evaluators must reformulate project goals and engage in “loose, post-hoc analysis rather than rigorous evaluation” in order to address environmental performance. Given that internal documents (e.g., project design documents, internal supervision reports, etc.) are often not available even for evaluators, it is difficult to carry out rigorous evaluations of all types. As evaluators reported, it is difficult enough to evaluate primary and secondary performance concerns at the country level, let

alone environmental goals and targets that are rarely formalized in the context of project planning. These limitations are clearly evidenced by the lack of environmental recommendations in African Development Bank country program evaluations.

The World Bank and the Asian Development Bank do have several country program evaluations that recommend environmental targets be emphasized in future lending decisions. I find little evidence that these recommendations influence lending decisions about either clean energy or environment improving projects or project components. Part of the lack of effect may be due to the fact when breaking down environmental recommendations by sector, I find very few recommendations in these areas. Given this low coverage, it is not surprising that I do not find statistical support for organizational responses to country program evaluation findings. I find a much stronger series of recommendations made about natural resource management issues, perhaps owing to the fact that these types of goals have longer been part of MDB portfolios.

Although the World Bank and Asian Development Bank have not produced many recommendations about specific operational areas considered, there are reasons to believe that they are similarly constrained in producing *selectivity-inducing* recommendations. As one ADB evaluator reported, country program evaluation are not really in the business of “picking winners” among different sectors and project types. Instead, they focus on the planning and operational *processes* that can be improved to enhance the effectiveness of a country portfolio. While several country evaluations considered here advocated for increased selectivity, they did so generally and in terms of the planning process, rather than specifically in terms of sectors. As one World Bank evaluator reported, the evaluation department is not intended to be a “policy shop” and once it begins to make specific operational recommendations, its independence and

primary function of evaluation is compromised. Given that including environmental components in lending projects is already an organizational priority, there may be little influence in restating this as a country goal in the context of a country program evaluation. Indeed, given that evaluators act strategically by including recommendations on a few, actionable items, several evaluators indicated that it was often not possible to engage seriously with environmental performance in the context of summary evaluation recommendations, since MDB policies already instruct operations in these areas.

6.5.3 Lack of Processes to Ensure Implementation of Recommendations

Even though the MDBs have formal procedures for the consideration of recommendations that are made in country program evaluations, they mostly lack management systems to ensure that recommendations are carried out in future implementation activities. At each of the four MDBs considered here, the management must provide a response to the recommendations in country program evaluations. This “management response” provides an operational perspective on the recommendations and includes a set of operational steps that will be taken in response to the recommendations. However, aside from external oversight, internal staff incentives, and borrower demand that drive responsiveness to past performance discussed in previous chapters, there are few systems in place to ensure that management commitments are diligently implemented. Simply put, given the wide range of mandates facing high level management at the MDBs, there is little capacity to follow-up on the literally dozens or hundreds of recommendations that come out of evaluations each year in a centralized fashion.

At the World Bank, for example, although country program evaluation are discussed at the sub-Board level within the Committee of Development Effectiveness,

the planning of a country strategy still very much rests with the country director and the country team. One country director that I spoke with indicated that evaluators that are part of producing a country program evaluation rarely have knowledge of the country at a level similar to operational staff. Thus, this country director viewed the process of responding to country program evaluations as a chance to “give the Independent Evaluation Group actual facts.” Thus, although a country program evaluation is considered in the process of designing a country strategy (if available), other forms of analysis often take precedent. In particular, country planning teams often assemble both internal and external sectoral experts in a team to analyze the conditions that are likely to foster an effective lending program going forward. Furthermore, once the country strategy is adopted, implementation realities mean that evaluation recommendations are not a high priority, unless they receive considerable attention and oversight at the Board level and are thus made a priority at the divisional level, which is rare given the myriad of projects and strategies that come up for consideration at the Board level each year. Furthermore, in many cases through the 1990s and early-2000s, country program evaluations were completed affect initial drafts of country strategies at the World Bank, further limiting their influence.

At the IADB, operational staff that I interviewed were skeptical that the *country strategy* process had much of an effect on eventual lending decisions. Unlike the World Bank, operational staff at the IADB reported following a more borrower-driven, “practical” approach to lending decisions that allows the borrower country to change the projects that are being prepared in the pipeline on a year to year basis. There was reported to be great variation in the degree to which country strategies drive lending at the country level, which one evaluation staff going so far as saying they “have no influence on lending.” In specific country program evaluations, this is known as the

“improvisation rate,” and indicates the degree to which approved projects are not those envisioned during the country strategy process.¹⁰ Thus, given the weak nature of the country planning process, there is little opportunity for country program evaluations that are one step further removed to influence lending decisions about environment-improving projects. Furthermore, evaluation staff express reservation that they were “completely out of the process” in terms of project level lending decisions, and skeptical that their findings had much influence under prevailing organizational policy. Because there is no tracking system for evaluation recommendations, evaluation staff were unable to report whether operational management were following their recommendations.

Similarly at the African Development Bank, there is no formal process to track whether operational management follows through on recommendations made as part of the country program evaluation. Given that the first AFDB country program evaluation was not completed until 2001 and there are limited resources available for evaluation, there have been no repeated evaluations that have allowed the evaluation department to examine whether its past recommendations have been followed in future operations. Evaluators, however, are pessimistic about the prospect to have direct influence over lending decisions. Evaluators highlighted how operational management are pulled in many directions, particularly by borrowing and donor country demands, that attempting to respond to past performance is perceived to be a lower priority. Like the other MDBs, management must issue a formal response to country program evaluations, but that is the final formal step to be followed in the country program evaluation process, effectively closing off that evaluation.

¹⁰ For example, see the recent country program evaluation of the Dominican Republic, which indicates that 33% of operations were never programmed. Available at: <http://www.iadb.org/ove/Documents/uploads/cache/35398366.pdf> (Accessed April 2011).

The Asian Development Bank is the only MDB considered here that has a formalized way to track the implementation of recommendations made within evaluations. Since 1982, the evaluation office has been tracking the implementation of recommendations. In 2008, the Board approved an electronic tracking system to increase the ability to provide oversight for implementation issues that come up in country program evaluations. Furthermore, responses to recommendations made in country program evaluations must be formally included in new country strategies, making the Asian Development Bank an important test case for the importance of high-level evaluations as part of future research. An initial evaluation of this system indicates that it is producing significant responsiveness from operational management (Independent Evaluation Department [IED], 2009). However, despite the institutional means of following recommendations, functioning of the Management Tracking System depends entirely on the self-reporting of operational staff, and evaluators indicated that they have very limited means to undertake independent monitoring of the implementation. Furthermore, when the ADB evaluation department comments on future operational documents by evaluating whether findings and recommendations are taken into account, they “check what the plan says,” rather than check actual implementation. Indeed, one operational staff that I spoke with indicated that unless a particular recommendation received attention from high-level management (VPs or Director-Generals), there was little systematic responsiveness to recommendations prior to the establishment of the Management Tracking System.

6.5.4 Implementation of Recommendations Constrained by Borrower Demand

As was introduced in previous chapters, borrowing countries have tended to give less priority to stand-alone environmental projects, especially those countries that have a specific allocated window of concessional lending available. Both evaluators and

operational staff across the MDBs reported that the lack of borrower demand constrains their ability to implement recommendations coming out of country program evaluations. Although evaluators have tried in recent years to broaden their audience to include borrowing country government ministries, fundamentally evaluation departments still report to the Boards and thus produce evaluation content based on interests expressed at the Board level (Operations Evaluation Department [OED], 2005a). Thus, the findings of country program evaluations are likely to play a secondary role in the country planning process to other factors, such as borrower lending demands, prevailing MDB lending strategies, and the resources that the MDBs have available to finance projects in specific sectors.

At the country level, operational staff are often able to distinguish between borrowing countries that are interested in environment-improving financing and those that are not. For example, operational staff members at the Inter-American Development Bank reported that while Brazil and Peru have generally been interested in “greened” portfolios, environment-improving lending has not been a priority for Argentina. Even when recommendations might exist, through country program evaluations or country environmental assessments, the country director in question must work within the limits set by the borrowing government. This may mean “mainstreaming” environmental components into traditional development projects or finding grant resources to address environmental issues. Some countries show much more willingness to pursue such negotiations than others.

The larger the size of the borrowing country and the greater the development level, the more constrained the MDBs will be in pursuing operational recommendations that do not have borrower support. At the Inter-American Development Bank, the majority of lending is directed to just four countries. At the Asian Development Bank,

the majority of lending is directed to just six countries. These large countries often have very specific ideas about how their portfolios should be managed. For example, one operational staff reported that China generally approaches the ADB with projects that are almost fully designed, leaving little room for a direct influence of evaluations. In recent years across the MDBs, more emphasis has been placed on having countries develop their own development strategies that frame lending negotiations. As the lending process has become more borrower-driven, there may be less room for recommendations in country evaluations to have a large influence within bank-driven planning processes.

Perhaps the one clear area of responsiveness to country program evaluations reported by MDB staff has been the drive toward greater sector selectivity at the Asian Development Bank. In recent years, country program evaluations for Pakistan, Cambodia, and Laos have all recommended greater intra-sector selectivity and a lending portfolio that focuses on at most 2-3 sectors within the country.¹¹ Operational staff have reported that these evaluations have caused the closing of many projects that were identified to be underperforming (47 in Pakistan) and subsequent country strategies with greater focus (Asian Development Bank [ADB]). Furthermore, recommendations about sector selectivity fed into the development of Strategy 2020, which set ADB priorities for the coming ten years. This example shows that even when evaluations are influential, they tend to be at the level of overall organizational processes and priorities, rather than for specific lending decisions that are affected by a host of other factors.

Given that the implementation of recommendations coming out of country program evaluations are constrained by borrower country lending demand, it will make

¹¹ Asian Development Bank country program evaluations are available at: <http://www.adb.org/Evaluation/resources-list.asp?type=5&p=evalcape> (Accessed April 2011).

sense in future periods for evaluators to expand their sense of audience to include borrowing country stakeholders. While this has happened in some evaluations, with recommendations directed at borrowing countries, this has not been a priority and will likely constrain the direct influence of country program evaluations in future periods unless reformed.

Although country program evaluations are the primary product that is likely to have an influence on allocation decisions at the MDBs, it is clear from the descriptive data presented above (Table 1) that environmental performance information and recommendations are not always highlighted in country program evaluations. When country program evaluations do a poor job at compiling environmental performance information and do not make recommendations based on environmental performance information, they are unlikely to influence allocation decisions about environment-improving projects.

6.6 Conclusions and Implications

The primary finding of this chapter is that the country program evaluation process does not create sufficient incentives for operational staff to respond to recommendations about environment-improving operations. This is an important finding in the context of the larger project presented in these chapters, indicating that evaluations are unlikely to have a *direct* effect on lending decisions in the absence of operational policies that incentivize their use. If the evaluation process itself was driving lending decisions, I would expect to find that most clearly in the context of country program evaluation recommendations because of audience, process, and information aggregation effects.

This result echoes the broader evaluation literature about the importance of indirect evaluation effects rather than instrumental evaluation effects. Several authors

that have written about the ways that evaluations influence both general decisions (Patton, 2008) and international environment decision-making (Mitchell, et al., 2006), have emphasized how evaluation content rarely drives decision-making. This line of reasoning runs counter to the corpus of program evaluation research that focuses on reaching better and more robust conclusions. Indeed, the findings presented here confirm a more pessimistic view that evaluations are seldom used in direct, instrumental ways within complex organizations (Torres & Preskill, 2001).

Recent attempts to understand when evaluations are influential find that incentives to respond to performance information need to be in place. In the case of the previous chapters, I have argued that donor lending preferences, borrower demand, and operational policy can cause noticeable responses to environmental performance information in certain circumstances. The data presented here suggest that evaluations do not play a decisive role in providing the performance information, but rather capture knowledge about environmental performance that is available within the MDBs from a variety of sources. Within such large organizations, it is impossible to track exactly where performance information originates, and operational staff are generally skeptical that evaluations contribute new information. Indeed, the arguments of the previous chapters speak more generally to IO decision-making incentives than they do the particular role that evaluation plays in provisioning information about performance. Instead, the evaluations considered in this project serve as snapshots of performance information that is available to decision-makers. This conclusion is stronger, given that recommendations in country program evaluations have no discernable effect on future lending decisions.

In the future, this suggests a need to look to other avenues of evaluation influence when delineating the organizational value of evaluation. For example, several

evaluation staff reported that one of the primary effects of evaluation at the MDBs is to induce more candid self-evaluations (e.g., completion reports) that are completed for every project by operational staff, since operational staff know that such reports might come up for evaluation review. Other evaluators reported that carrying out diligent evaluations gave them credibility to engage in conversations about performance with both MDB management and member states through the Board, thus widening the review *process* when approving new operations. Operational management reported that the opportunity to respond to evaluations induces reflection among operational staff about performance that might not occur otherwise. Similar avenues of evaluation influence are well-documented and even emphasized within the evaluation literature (Kirkhart, 2000). This chapter suggests that future work that seeks to understand evaluation influence must look deeper into how it affects the process of decision-making within organizations.

The models presented in this chapter several support the findings of previous chapters with new data. For clean energy projects, borrowing countries that are globally important to climate change continue to receive the bulk of climate change financing, with no discernable effect of past performance. For urban environment projects, I confirmed that the World Bank approvals reflect past borrower performance, likely induced by varying levels of borrower demand. This result also extends to the Asian Development Bank and Inter-American Development Bank in relation to urban environmental activities that are integrated into larger development projects. Operational policies that incentivize the use of evaluation and borrower-driven lending continue to be the primary ways to induce selectivity in allocation decisions based on performance.

Finally, I have not sought to understand how evaluation findings have induced better findings in future periods by improving the *design* of projects and strategies. Rather than inducing selectivity, it is possible that the primary way that evaluations can improve organizational performance is by highlight the planning, design, supervision, and implementation processes that lead to more successful outcomes. Indeed, the findings and recommendations that are part of country program evaluations rarely speak to selectivity, but rather the improvement of process for effectiveness. In the future, it will be important to test whether countries or sectors that have been subjected to evaluations, including country program evaluations, are likely to have more successful outcomes. Given that MDB management does have incentives to produce successful projects, in order to capture a greater share of development resources during replenishments and capital increases, it is possible that evaluation has been part of a process to improve performance since the 1990s. This proposition could be tested directly using the data collected in this project and will be important, given that this chapter shows evaluation content and recommendations do not directly drive performance-based lending.

7 Conclusions

7.1 Getting the Incentives Right

We enter the 21st century facing transboundary environmental problems of growing scale and scope. Yet, no clear solutions are in sight. States are still struggling to establish cooperative mechanisms that effectively address climate change, deforestation, and a host of domestic environmental problems. Many of the most severe environmental problems occur in less-developed countries, where donor assistance is necessary to address them. For the last two decades, international attempts to address environmental problems have revolved around financing mechanisms. Beginning with Agenda 21 and the 1992 Rio Earth Summit, donor countries pledged \$2 billion and established the Global Environment Facility to finance environmental programs in less-developed countries. At the 2009 Copenhagen Climate meeting, donor countries pledged to mobilize an additional \$100 billion annually to address the climate change mitigation and adaptation needs of less-developed countries. Yet, despite the continued focus on mobilizing ever more financing for environmental activities, the organizations used to deliver this financing are the same today as they were two decades earlier. If the same multilateral development banks are to play an ever more important role in the delivery of environmental financing, it is essential that they have incentives to allocate it in effective ways.

Despite the international “results agenda” that has been adopted by development organizations around the world, the core incentives that drive MDB allocation decisions have remained relatively unchanged. MDB staff are still rewarded for successfully steering new projects through the pipeline to Board approval. At the departmental level, the ability to hire new staff and gain control of additional administrative and lending resources likewise depends on securing new lending. Thus,

the problem of performance at the MDBs remains rooted in an approval culture to this day. Whenever the MDBs prioritize new lending over effective lending, the outcomes of their operations are likely to suffer.

While the core incentives of MDB staff have not changed substantially, what has changed is the pipeline process that they must navigate to secure new lending. Nowhere is this more evident than with the project types examined in this dissertation. For environmentally-risky projects, MDB staff must now prepare detailed environmental impact assessments and environmental management plans prior to Board approval. These requirements must be approved by separate environmental departments. In addition, staff must show that allocation decisions align with higher level strategies, which often mandate a focus on environment-improving operations. Projects must also be designed with clear and measurable objectives, monitoring frameworks, and are likely to face independent evaluation. Staff must also consult with civil society groups about projects prior to approval to ensure that complaints will not arise during implementation. All of these requirements have been put in place to deal with the problem of performance at the MDBs. All of these requirements also change the costs of preparing and seeking approval for projects. Have these new pipeline requirements helped make project approval decisions responsive to performance?

I have shown that when these policies and administrative requirements change the costs of approving new projects in line with past performance, the MDBs practice performance-based allocation. Since prevailing allocation arrangements have remained relatively stable at the MDBs, the practice of performance-based allocation depends on making it difficult to approve projects that are not likely to achieve satisfactory results. Given that member states to the Board of Executive Directors very rarely make it difficult to approve projects by casting negative votes, the future of performance-based

allocation hinges on finding administrative policies and preparation requirements that can do so.

This argument is most clearly supported by results that show how the MDBs respond to borrower performance implementing environmental safeguards. Environmental safeguard policies have created strong incentives for staff to respond to past performance because they make it difficult to approve environmentally-risky projects in countries that implement safeguard requirements poorly. Operational staff, who are under tremendous pressure to meet lending targets, have a tendency to avoid environmentally-risky projects in low-performing countries. At both the World Bank and Asian Development Bank, special safeguard units exist to ensure safeguard requirements are met prior to Board approval, which decreases the ability of operational staff to shirk these requirements. For environmentally-risky projects, the approval culture is channeled in a way that results in performance-based allocation.

In contrast, the Inspection Panel process does not make it more costly to approve environmentally-risky projects in low-performing countries. Instead, it increase the costs of approving environmentally-risky projects in countries that have active environmental civil societies, which does not correspond to past safeguard performance. As I demonstrated in Chapter 4, Inspection Panel requests tend to target *high-performing* countries that have a portfolio with many environmentally-risky projects. Thus, past performance implementing safeguard procedures does not indicate the likely costs that staff will face through the Inspection process. As a result, MDB staff approve more environmentally-risky projects in countries that have low levels of civil liberties. While there is evidence that the MDBs improve their performance in borrowing countries with previous Inspection requests, the Inspection process does not induce performance-based

allocation because it does not create uniform incentives across different country portfolios that vary by past performance.

In the future, incentivizing performance-based allocation will hinge on establishing policies and requirements at the MDBs that make it more difficult to approve new projects when similar projects have been ineffective in the past. To do so, the pipeline process at the MDBs needs to require more intensive planning in countries that have demonstrated poor performance in the past. Indeed, the literature on domestic bureaucratic design and governance has recognized that institutional “checks” are an important way that principals can constrain the activities of bureaucratic agencies (Kiewiet & McCubbins, 1991). Principals can design executive agencies in ways that lead to competing interests within or across agencies. For example, executive agencies can be audited by specialized units whose sole responsibility is to monitor performance, which essentially amounts to delegating oversight (Norton & Smith, 2008). In addition, principals can mandate certain administrative practices that make it easier to monitor that agencies are acting in desired ways (McCubbins, et al., 1987).

This same logic extends to international organizations, where donor countries can mandate “checks” as part of the project approval process. For example, Pollack and Hafner-Burton (2010) found that environmental considerations were not effectively mainstreamed into European Commission through informal socialization, but rather administrative procedures that universally required “impact assessments” prior to new operations. Similar procedures could be put in place for performance at the MDBs. Whereas current project appraisal documents at the MDBs require a short account (1-2 paragraph) about how the project in question responds to past lessons, a more complete performance assessment could be automatically required for particular countries when past operations in the same sector did not achieve satisfactory results. This extra

preparation requirement would incentivize staff to choose project types that have been successful, and when they must continue to engage in a low-performing sector, to at least spend more time designing a project for strong performance.

This type of incentives might also be created in the opposite way. Both the World Bank and Asian Development Bank are currently in the process of certifying that the domestic environmental safeguard policies of certain countries are equivalent to bank policies in stringency. In essence, by allowing “country systems” to move forward, the MDBs are allowing high-performing countries to implement their own safeguard processes and forego bank administrative procedures, thereby decreasing the design and administrative costs of environmentally-risky projects in those countries. By allowing high-performing countries the ability to streamline the project approval pipeline, countries that do not currently have good performance records may be incentivized to improve in order to access the “country systems” planning process.

It may be possible to extend streamlined processes to other parts of the project design stage. For example, bank staff still must write up project proposals and information documents according to a standardized bank format. It may be possible to have high-performing borrowing countries take the lead on producing such documents according to domestic planning systems, in order to decrease the time that projects spend in the planning pipeline.

Regardless of the way the incentives are created, the implication of this research is that approval processes at the MDBs must be designed carefully and deliberately in order to constrain the “approval culture” and incentivize performance-based allocation. There are indications, however, that the MDBs are moving in the opposite direction. For example, the Asian Development Bank recently approved a strategy to halve the time that projects spend in preparation (Asian Development Bank [ADB], 2009a). Borrowing

countries, which are increasingly making their voices heard at the Board level of the MDBs, describe current pipeline requirements as onerous and often seek alternative forms of financing when they are likely to face significant delays during project preparation.

This trend raises serious doubts about the ability of the MDBs to respond to their performance in the future. As one staff member I interviewed put it, safeguard policies are what make the MDBs “different from Citibank.” The MDBs have struggled to stay relevant in an era when many countries, especially their largest borrowers, can turn to private capital markets in order to avoid the delays associated with MDB planning requirements. But, it is unclear why the MDBs should seek to compete with private capital markets. If borrowing countries have good enough policy and economic environments that they no longer need the MDBs, they should be graduated from MDB lending. Doing so would allow the MDBs to refocus their efforts on implementing programs in places where strong planning requirements are needed to implement programs well.

7.2 Donor-Driven Environmental Programs Will Result in Waste

In this research, I also questioned how the push for new and additional environment-improving lending can be reconciled with the practice of performance-based allocation. As expected, this is not easy for the MDBs to accomplish. The push for more environment-improving lending reinforces the approval culture at the MDBs. Donor countries have set targets for the amount of environmental lending that needs to be transferred, which places MDB staff under considerable pressure to demonstrate that they are doing something about this mandate. Under these pressures, MDB staff have incentives to approve environment-improving projects and integrate environmental activities into standard development projects regardless of their likely performance.

The consequences of these incentives are predictable. For projects that deal with global environmental resources, projects tend to be directed towards countries with significant amounts of the resource in question, irrespective of past performance with similar projects. Staff report that these types of projects are among the most “donor-driven” in the portfolio. This may be one of the primary reasons that global environmental projects consistently rank as one of the lowest performing components of MDB portfolios (Operations Evaluation Department [OED], 2005b). It is quite clear that if prevailing allocation practices continue, a great deal of resources that could otherwise be directed toward global environmental concerns will be wasted.

Donor countries must recognize the overwhelming evidence that “donor push” is likely to lead to ineffective outcomes in the delivery of development assistance. There is evidence to support this argument across many different sectors, including environment, democracy promotion, economic adjustment, and civil society promotion projects (Easterly, 2005; Goldsmith, 2008; Knack, 2004). While the goals of such projects might be desirable, the research presented here confirms experiences elsewhere that show scarce financing will be wasted in pursuing “donor-driven” projects. This suggests that other mechanism should be used to manage financing for global environmental targets, as will be discussed below.

This same problem does not exist for environment-improving projects that have primarily domestic targets. High-performing borrowers are more likely to pursue environment-improving projects that involve domestic environmental issues than low-performing borrowers. This result indicates that high-performing countries are often able to select projects that will be both successful and address prioritized environmental needs. It may be possible, therefore, to make additional environmental financing available to high-performing countries and allow them to select their own projects. Low-

performing countries tend to avoid environment-improving projects, and it is likely better for the MDBs to focus on areas that are higher priorities and where they can have a more significant development impact.

7.3 Favoring Performance or Favoring Need?

The practice of performance-based allocation can be at odds with the desire to address environment and development needs in countries that are poor, have low governance capacity, and are politically or economically unstable. Indeed, this is the fundamental paradox of development assistance: the countries that need aid the most are also the countries that are least likely to benefit from aid, since they are unable to use it effectively. Although the MDBs oversee grant and lending projects, borrowing countries are still responsible for implementing them. Thus, if the MDBs were only to allocate infrastructure projects or environment-improving projects to borrowing countries with strong performance records or high governance capacity, it is likely that they would be working almost exclusively in middle-income countries. These middle-income countries often have access to commercial lending markets and do not “need” MDB assistance. Indeed, several MDB staff that I interviewed suggested that performance-based allocation runs counter to their role as “lender of last resort” to the countries that have nowhere else to turn for their development financing needs.

Despite the sentiment that borrowing country need should drive allocation decisions at the MDBs, waste is still waste no matter where it occurs. Projects that are likely to fail in reaching their objectives have no defensible place in the portfolios of development organizations. Failing projects decrease the public’s general support for development assistance in donor countries, which may have more serious long term impacts on the availability of development assistance (Diven & Constantelos, 2009; Paxton & Knack, 2008). In addition, there is evidence that aid can actually harm

institutional development in countries that are unable to use it effectively (Easterly, 2006). Financing for environmental and development concerns is well below international target levels, with very few donor countries reaching 0.7% GDP targets set as part of the Millennium Development Goals. Given the magnitude of needs around the world, little good is served by allocating scarce development assistance to places where it is likely to be wasted.

However, shifting focus from performance-based allocation practiced through aggregate allocation decisions to performance-based allocation practiced through portfolio composition decisions offers a way to reconcile the paradox of development assistance. Development assistance is an exceptionally broad umbrella terms for financing that can be delivered through different modalities, directed to a wide variety of sectors, and implemented by a number of different actors. Portfolios can be structured to emphasize project versus multi-tranche program lending, projects for infrastructure versus projects for institutional capacity building, and even official development assistance implemented by civil society groups instead of centralized government agencies. The MDBs have the advantage of working under broad mandates, which allow them to structure lending portfolios in unique ways for individual borrowing countries.

Whereas the institutionalized performance-based allocation frameworks at the MDBs deal with aggregate lending amounts, there is substantial leeway for the banks to customize portfolios in even the poorest countries in ways that respond to past performance. Often times that will involve being more selective and focused on the types of projects that can be implemented well, rather than trying to be all things to all countries. Based on evaluations, for example, the regional development banks have attempted to focus their portfolios in a limited number of sectors where they have comparative advantages in managing successful projects (see Asian Development Bank

[ADB], 2009b; Operations Evaluation Department [OED], 2007c). This type of shift is highly complementary to performance-based allocation practiced through portfolio composition decisions, and should be prioritized by donor countries.

The ability to practice performance-based allocation through portfolio composition decisions comes down to whether donor countries are trying to induce specific outputs or support broader development goals. One example of a specific output that I deal with in this dissertation is reductions to greenhouse gas emissions. For this output, it does not matter where in the world emissions reductions are carried out, just that they actually occur. In this case, it makes very little sense to send clean energy projects to all large emitters. To achieve the largest reductions possible with scarce financing, clean energy projects should be allocated to the borrowing countries that can successfully implement such projects. Thus, instead of requiring climate change activities to be implemented across all countries, as is presently required by MDB climate strategies, a certain amount of financing should be set aside for climate projects and be allocated based on performance-based eligibility criteria. If donor countries are trying to induce specific outcomes, then allocation systems need to be based on specific eligibility requirements.

On the other hand, if financing is intended to solve the most pressing development problems where it can be most useful, then performance-based allocation can be accomplished through flexibility within specific country portfolios. The MDBs should be incentivized to move in and out of sectors as performance dictates. One of the obstacles to this type of flexibility is that staffing creates inertia to continue financing programs based on the present mix of expertise. Thus, to truly use their flexibility to practice performance-based allocation, the MDBs might need to adopt more flexible

staffing policies and continue their reliance on contractors where technical expertise is required.

There is something to be said, however, for building the capacity of a borrowing country over time in a particular sector. Operational staff I spoke with at the Asian Development Bank, for example, described how a series of technical assistance and traditional energy projects are being implemented in Pakistan to build capacity for future clean energy investments. While this is certainly a part of MDB mandates, when borrowing countries perform poorly on initial projects in a capacity building series, it calls into question the likelihood of success in building capacity over time in that sector. Many operational staff state that they begin with “easy” projects and then scale up size and complexity as particular borrowing countries gain more capacity. If borrowing countries fail to implement these easy projects well, then it is difficult to maintain that they will be able to progress. This situation calls for either choosing a different way to build capacity or to focus on those sectors where the MDBs can be successful.

What is clear from this research is that when development banks pursue specific, donor-driven targets in all countries, results will be at best mixed and financing will be wasted. When donor countries in essence want to purchase certain results, they should do just that. Indeed, the future of financing for global environmental goods is not likely to be as effective as possible under prevailing MDB allocation decisions.

7.4 Climate Change and the Future of International Environmental Finance

International environmental finance will arguably be the most dynamic area of development assistance over the coming decades. Current climate negotiations have centered around drastically increasing the availability of environmental financing in order to secure global environmental goods. At the 15th Conference of the Parties to the

United Nations Convention on Climate Change in Copenhagen during 2009, Secretary of State Hillary Clinton announced that the US would aim to mobilize \$100 billion of climate financing annually to be used to address mitigation and adaptation in less-developed countries. At the current time, several new international financing mechanisms are being established to manage initial resources that have been pledged towards this commitment, including the Climate Investment Funds and the Green Climate Fund, both of which are slated to be managed by multilateral development banks. In addition, the private sector lending divisions of the multilateral banks have scaled up climate-related financing more than any other type of investment. The research presented here suggests several issues that will be critical to the successful management and allocation of this climate-related financing.

First, and perhaps most importantly, financing mechanisms for climate change must avoid being driven solely by donor supply preferences. Given that most of the recent negotiations about climate change financing have centered around drastically increasing the *supply* of climate financing, the results here suggest that unless mechanisms are put in place to direct the bulk of this financing to high-performing countries, a great deal of resources will be wasted. In my interviews with MDB staff, it was often commented that projects related to climate change continue to be one of the most “donor-driven” areas of the financing portfolio. As was seen in models of MDB decisions related to clean-energy projects in Chapter 5, the bulk of climate financing tends to be directed towards large emitters, without reference to past performance. This suggests that increasing the *supply* of climate-related financing and managing it as traditional public-sector project lending will result in the inefficient use of scarce financing.

At the very least, allocation mechanisms should be put in place that incentivize donor organizations to direct financing to high-performing countries related to emissions mitigation, since donor countries are essentially contracted to secure global environmental goods. Two possibilities immediately follow from this suggestion. First, recipient countries must be incentivized to implement climate mitigation projects well. Climate mitigation financing institutions like the Clean Development Mechanism incentivize such performance because only verified emissions reductions are eventually purchased (Streck, 2004). Likewise, a recent proposal for “cash on delivery” development financing would provide recipient countries incentives to achieve certain outcomes in order to receive the cost of projects plus extra development dividends (Birdsall, Savedoff, Mahgoub, & Vyborny, 2011). Related to this approach, recent climate negotiations have included the possibility that less-developed countries would undertake specific climate mitigation commitments in exchange for financing to meet such goals. All of these mechanisms would provide host countries the incentives necessary to actually reduce climate emissions, and allow those that could not produce successful outcomes to opt out for other types of development financing.

Likewise, incentivizing private sector actors to invest in clean-energy technologies in less-developed countries will be key to addressing climate mitigation targets internationally. Already, significant portion of MDB private sector lending is directed towards clean-energy investments. In related work, I find that private sector operations are very responsive to the past performance record of borrowing countries.¹ This suggests that ramping up private sector investment in mitigation activities would offer a way to spend scarce financing efficiently.

¹ Projects allocated to private sectors actors by the World Bank’s Carbon Finance Unit tend to be directed to countries that have strong environmental performance records as revealed in evaluations.

On the other hand, climate adaptation financing, which is used to prepare less-developed countries for the changes associate with climate change, might fruitfully be managed as standard public-sector project financing. As I demonstrate in Chapter 5, when an environment-improving project is primarily intended to meet domestic environmental needs and does not face strong donor supply pressures, high-performing countries with strong environmental management needs tend to select into available financing. Thus, while the multilateral development banks might be wise to build up the expertise necessary to administer climate adaptation projects and have the availability of financing on hand for these directives, borrower requests should drive lending in these areas. Given that climate change mitigation is a long term process, it may be several years or decades before such demand fully materializes. However, because the spatial effects of climate changes are expected to be highly heterogeneous (Intergovernmental Panel on Climate Change [IPCC], 1998), climate adaptation financing has the potential to be substantially borrower-driven and thus more effective.

7.5 Outsourcing Monitoring to Civil Society

Civil society groups have long led the charge for sustainable development and environmental protection at both domestic and international levels. The environmental practices of the MDBs first came under scrutiny because of the persistent efforts and protests of civil society groups in the late-1980s and early-1990s. To this day, civil society groups continue to be leading advocates of good environmental practices at the MDBs. Several civil society groups, like the Bank Information Center or Action Aid, exist for the primary purpose of monitoring MDB practices. They provide free performance monitoring to states and often bring together political constituencies to press donor countries to demand better environmental performance at the MDBs.

Today more than ever, it is easier for civil society groups to perform monitoring and advocacy functions. With the advent of communication technologies, it is easier to monitor and disseminate information about the environmental consequences of MDB projects that are implemented in even remotest locations. The MDBs are now required to consult relevant civil society groups as projects are prepared. MDB project teams can now be subjected to Inspection requests if they do not respond to the concerns of civil society groups that come up during project implementation. These new roles and tools raise the possibility that civil society groups can play an important role in prompting performance-based allocation and improved environmental performance at the MDBs.

Indeed, related research has explored how non-state actors might play a crucial role in inducing good performance at international organizations, since they can provide state principals with performance information that would otherwise be difficult for states to attain (Dai, 2007; Lake & McCubbins, 2006; Raustiala, 1997). More directly, civil society groups may be able to influence the cost-benefit calculations of international organizations at the individual, department, and organizational levels. They might do so by effectively blocking certain activities, which is particularly relevant in the case of MDBs, given their direct role in on-the-ground activities throughout the world.

This research clarifies that civil society monitoring and advocacy, while potentially important, is applied unevenly. Thus, it is not a substitute for monitoring and evaluation that is applied consistently across MDB portfolios. I showed that both the World Bank and the Asian Development Bank practiced performance-based allocation as related to environmentally-risky projects across the portfolio in response to the past performance of borrowing countries. However, civil society groups tend to file complaints about the environmental performance of *high-performing* countries. While I have shown that this caused better implementation in the high-performing countries

over time, civil society complaints did not tend to target the places where monitoring and advocacy is needed most.

There are hazards in this approach to monitoring and evaluation. For example, civil society groups have been so vehemently opposed to MDB hydroelectric projects in southeast Asia, that the banks have basically exited from the sector (Khagram, 2004). In response to persistent civil society criticism, the World Bank and Asian Development Bank jointly financed the Nam Theun II project in Laos, with best practice environmental safeguards and resettlement procedures. The project has taken years to plan and implement in a responsible manner.² When I spoke with Asian Development Bank staff about the project, they indicated that there is little willingness either from the MDBs or borrowing countries themselves to pursue similar projects in the future, owing to the persistent delays caused by civil society monitoring.

At the same time, China has financed hundreds of dams throughout southeast Asia without stringent environmental safeguards. The countries of southeast Asia have turned almost entirely to the Chinese for financing of these projects. Civil society groups are unable to effectively target Chinese hydropower companies or southeast Asian governments for better environmental practices in the numerous projects that are currently being constructed (Hirsch, 2011). With these outcomes in mind, it seems that civil society groups have won one battle, but lost the broader war. The multilateral development banks are a convenient target for monitoring and advocacy, owing to their centralized administrative structure and their relation to donor countries that are sympathetic to the claims of civil society groups (Keck & Sikkink). By pushing them out

² For example, see the frequently asked questions about the project at: <http://go.worldbank.org/NXRZK3DX20> (Accessed June 2011).

of certain sectors like hydropower, civil society groups may have actually caused outcomes that are worse than would be the case if the MDBs were still engaged.

This does not yet appear to be happening for environmentally-risky projects more generally at the MDBs. I showed that countries that are subjected to Inspection requests are more likely to receive environmentally-risky projects than countries that have not been targeted, conditional on the level of civil society organization within a borrowing country. Civil society groups are able to push the MDBs away from risky projects, but not because of their voice at the international level. Instead, the results indicate that domestic action and influence on borrower demand may be a greater source of influence for civil society groups.

Civil society groups would do well to think about their broader impacts, however. While focusing on individual cases may be an effective fund raising strategy, it does not ensure that the MDBs are more responsible overall. Since the MDBs are responsive to safeguard policies, this indicates that the higher stakes decisions are made at the policy and strategy level. It is unclear whether local civil society groups are able to participate effectively in such processes.

One interesting possibility that might be explored in the future is whether independent evaluation is an avenue for greater civil society participation in MDB decisions. Civil society groups have seized on the findings of independent evaluations to press their own agendas. Indeed, civil society groups may also have information disadvantages as related to MDB activities and publicly available evaluations may allow them to connect their local issues to broader performance issues at the MDBs. Currently, evaluation practices do not include debriefing sessions with civil society groups. Perhaps a civil society working group could ensure that the results of evaluations are better disseminated within advocacy networks.

7.6 The Broader Role of Monitoring and Evaluation

While this research has elucidated reasons why MDBs respond to their measured performance when allocating projects, it has raised additional questions that will be important to address in future research. Primary among these questions is whether monitoring and evaluation can improve performance by prompting better design of projects and programs. While some of the evaluations considered here recommend increased selectivity in decisions about the allocation of projects, a greater number of evaluations address issues that can be dealt with through planning, design, and implementation decisions. Indeed, many thematic evaluations dealing with both environmental safeguards and environmental targets are primarily concerned with *improving* similar operations in future periods (e.g., Independent Evaluation Group [IEG], 2008b, 2010b; Operations Evaluation Department [OED], 2006). MDB evaluations often deal with questions like what types of safeguard planning procedures improve environmental mitigation outcomes? How can emerging best practices in environmental mitigation be reflected in project implementation policies? How can environmental targets be effectively incorporated into broader development programs? What types of lending modalities have the greatest impact in terms of climate change mitigation and adaptation?

It may be the case that MDB staff respond to evaluation findings, but do so by altering decisions that do not pertain to allocation. Indeed, evaluation scholars have identified a number of other ways evaluations can influence organizations (Kirkhart, 2000). For example, the process of conducting evaluations may give decision-makers the space to critically consider their decisions, thereby contributing to an open culture of critically addressing performance issues (Mathison, 1994; Torres & Preskill, 2001). Evaluations can also contribute to the generation of better information among non-

evaluators, since operational staff know that self-assessments are likely to be challenged by evaluators. Indeed, one operational staff member at the World Bank believed that the primary impact of project evaluations was to improve the quality of post-project self-evaluations that project staff complete. Furthermore, by making evaluation a regular part of operations within organizations, all types of non-evaluators may be incentivized to carry out better monitoring of performance through the integration of evaluation systems into operations (A. J. Love, 1991). In other words, the process of developing robust evaluation functions within organizations can have important *indirect* effects that enhance performance.

Interviews that I conducted during visits to the headquarters of the MDBs suggest that these types of indirect effect may be occurring within the MDBs. Evaluation departments have played a direct role in building monitoring frameworks and performance indicators into project designs, especially during the past decade. By requiring operational staff to clearly state their goals during project design and develop frameworks to measure their performance in achieving those goals, evaluation broadly conceived may have prompted design practices that improve performance. In addition, because evaluations often make recommendations about design issues and identify systematic implementation problems that might be fixed through project design decisions, the “quality at entry” of MDB projects has been improved (Asian Development Bank [ADB], 2011). In the future, it will be important to examine the broader impacts of monitoring and evaluation at the MDBs.

The data collected as part of this research can be used to address these issues. In particular, it would be possible to examine whether projects, sectors, and country programs that have been subjected to evaluation become more effective over time. I have created reliable indices of environmental performance that are consistent across

time and organizations, which has been a major limiting factor for research on IO performance (Gutner & Thompson, 2010). Given limited resources for evaluation, the practice of evaluating performance has not been applied uniformly across time, countries, and sectors, which might provide leverage to understand the influence of evaluation on organizational performance in a time-series context.

It is also possible that evaluation has had deleterious impacts on performance. For example, strong external oversight can decrease the space for innovative administrative practices that enhance performance at public agencies (Jos & Tompkins, 2004). At international organizations, it is unclear whether evaluation and the external accountability that it has entailed have pushed the MDBs to be involved in projects that have easily quantified targets, but lower development impacts. While conducting interviews, I found instances where evaluations created incentives for operational staff to be less candid about problems encountered during project implementation, because doing so would subject them to external oversight.³ Facing evaluation, staff may make it harder to access information about their decisions and project outcomes.

Another issue that will clearly be important to the future of studies on IO performance is how the rising tide of borrower-driven lending will interact with evaluation. To this point, evaluation departments see their primary audience as the Board of the MDBs, which is largely dominated by donor countries in practice. However, recent organizational reforms at the MDBs have placed a higher burden on borrowing countries to develop their own poverty alleviation strategies, project lending requests, and project implementation systems. As the MDB lending processes move towards a partnership model, it will be important to reassess whether evaluation

³ For example, one evaluation staff member at the World Bank reported that an operational staff member had recently stated they will never again be candid in the self-evaluation completion report, since this was used as the basis for the evaluation department to give the project an unfavorable rating.

departments as currently operating effectively serve to improve the effectiveness of development assistance, or whether they are misaligned in terms of audience. As allocation and design decisions are driven more and more by borrower demand, evaluations will need to shift and recognize this new locus of decision-making authority. For a practical perspective, trials of joint evaluations with national audit authorities might be a useful way to improve domestic evaluation capacity.

As the international community presses forward with attempts to address a number of entrenched environmental problems, it will be necessary to design effective mechanisms for financing environmental improvements. I have shown that monitoring and evaluation does not provide a silver bullet for the problem of performance at the MDBs. Instead, member states must effectively channel the approval culture in ways that promote effectiveness.

Appendix I: Data Collection Procedures

Coding Procedure for Project Evaluations

Our team coded several items from project evaluations completed by the World Bank, Asian Development Bank, and African Development Bank from 1990-2008. I first recruited and trained research assistants on the coding items. Based on initial practice coding sets, I iteratively revised the coding criteria in order to increase reliability.

Following the adoption of final coding criteria, all research assistants were required to pass a 20-evaluation practice set at 90% coding reliability before they were allowed to move onto the final coding stage that produced the data for this dissertation.

Two research assistants independently coded each project evaluation in the sample. In all cases, the research assistants made note of the evaluation section that they used to determine their coding result. When the two coding results matched, the coded value was entered into the final dataset without further review. When the two coding results were different, I referenced the sections that the research assistants noted in their coding sheets and made a decision about the final coding value. All of the coding was completed before I specified any of the models contained in this dissertation.

Item 1. Environmental Target Performance. The purpose of this item is to assess the quality of implementation for environmental *targets*. Environmental targets are any project goals that attempt to make some environmental condition *better* than it was before the project. In other words, environmental targets are project components that are designed to “do good,” and they are not “do no harm” items (which is safeguard performance, Item 2). Environmental targets should be an attempt to improve the *quality or extent* of some environmental resource (e.g., water, forest, land, soil, etc.).

Environmental targets do not have to be the primary purpose of the project in order to be coded on this item. However, if environment targets are the primary purpose of the project, an aggregate summary of their achievement should be coded according to the criteria indicated below. There must be some information or indication of performance in order to code this item. The intention to address environmental issues is not sufficient, unless there is information on the actual outcomes.

A goal to improve the environment-related institutions or to improve management/policy related to the environment are considered to be environmental targets for the purpose of this item if the implied goal of such improvements is to support environmental management.

Any mention of project implementation that either discusses targets achievement generally or in terms of borrower performance should be coded. If it is specifically mentioned that achievement of environmental targets was the result of Bank actions (design, monitoring, etc.), the item should not be coded in this category, and instead in the Design category (Item 3). It is possible for both this item and the design item (Item 3) to be coded for the same evaluation. The following criteria should be used when assigning an environmental target code:

Items related to *water supply/quantity* that should be coded as an environmental target: (1) more efficient use of water resources; (2) improved management of water extraction; (3) decreased extraction of water resources from surface or groundwater. Flood control is not a target, unless it involves improved natural resource management or restoration of wetlands. Agriculture targets are not considered environmental targets unless they involve the improvement of some environmental resource, such as decreasing soil erosion, improving water use efficiency, restoring upper watershed areas, etc.

For projects that have multiple environmental targets, the score should be the aggregate of all components that best meets the criteria below.

Project Evaluation Item 1. Coding criteria for environmental target performance

Coding	Meaning	Criteria
4	Highly Satisfactory	Exceeds environmental goals or targets; specifically mentioned for outstanding environmental performance; Efforts significantly improve environmental outcomes as compared to pre-approval expectations; fairly detailed description of excellent performance with no room for improvement
3	Satisfactory	Meets all environmental goals or with only minor exceptions observed; summary statement of performance is positive ; any negatives are minor and easy to fix; summary statement of satisfactory performance without detail outlining strengths or weaknesses
2	Partly Satisfactory	Meets some environmental goals or conditions with significant deficiencies observed; summary statement of performance is negative ;
1	Unsatisfactory	Does not meet most environmental goals or targets with major deficiencies observed in most areas; Non-achievement of targets and mentions of failure and unsatisfactory performance;
NA	Not Available	Project has no environmental aspects OR insufficient information is available in evaluation report to assess environmental target implementation performance.

Item 1b: Environmental Target Sector. If environmental target performance is coded, the sector to which that performance applies should also be coded, according the following sectors:

- 1: Climate change, clean energy, climate adaptation projects (excluding dams)
- 2: Conservation: biodiversity, forestry conservation, forestry management
- 3: Rural sector: sustainable agriculture, water management, erosion control, soil conservation; community resource management
- 4: Local/urban environmental issues: water pollution, sanitation, sewerage, urban improvement

Item 2. Environmental Safeguard Performance. Each of the development banks has adopted environmental safeguard policies that are meant to ensure projects “do no harm” to the environment. In most cases, evaluations will contain safeguard performance information for projects with substantial physical components, such as dams, large infrastructure, roads, urban improvements, etc. As opposed to environmental targets, environmental safeguards attempt to maintain environmental quality measures as they existed before the project. Words that are typically associated with safeguard performance include, “loan covenants,” “safeguards,” “environmental compliance,” “environmental impact,” etc.

Items related to *water supply/quantity* that should be coded as an environmental safeguards are: (1) depletion of surface or groundwater sources; (2) conversion of wetlands to other uses; (3) extraction of water from natural areas.

Any mention of project implementation that either discusses safeguard performance generally or in terms of borrower performance should be coded to this item. Safeguard performance must relate to *project activities*, rather than general environmental issues surrounding a project. If it is specifically mentioned, that achievement of environmental targets was the result of Bank actions or a design decisions, the item should not be coded in this category, and instead in the Design category (Item 3). If a borrower either properly or poorly responds to unexpected safeguard issues, that should be recorded here, with an additional positive coding in Item 3 for design issues.

For projects that have multiple safeguards or sub-projects, the score should be the aggregate of all components that best meets the criteria below:

Project Evaluation Item 2. Coding criteria for environmental safeguard performance

Coding	Meaning	Criteria
4	Highly Satisfactory	Exceeds environmental conditions in terms of monitoring plans and mitigation activities; specifically mentioned for outstanding remediation efforts; environment is maintain in high quality despite risks posed by project design;
3	Satisfactory	Meets all environmental safeguards and conditions with only minor exceptions observed; summary statement of performance is positive;
2	Partly Satisfactory	Meets some safeguard goals met with significant deficiencies observed; Does not meet monitoring or evaluation standards in projects with no discernable environmental impacts; Does not meet safeguard standards with no discernable environmental impacts; summary statement of performance is negative or indicates that major improvements are required;
1	Unsatisfactory	Does not meet most environmental goals or conditions with major deficiencies observed in most areas; Outright non-compliance with environmental loan conditions; failure to address the project environmental impacts during implementation;
NA	Not Available	Project has no environmental aspects OR insufficient information is available in evaluation report to assess recipient performance;

Item 3. Design Issues Impair Environmental Performance. In many early projects, full consideration of the environmental issues was not completed during project preparation. Some evaluations state that environmental performance was low because environmental issues were not fully appraised, which is the content this coding item collects for each project. If a borrowing country fails to conduct monitoring or planning that is agreed to, the performance is coded in the appropriate performance item above. In order to code this item, environmental outcomes of the project need to be less satisfactory than would otherwise be expected.

In addition, many projects experience problems meeting environmental targets or adhering to safeguards because of issues that were not recognized at the project design phase, to no fault of the borrowing country. In such cases, Item 3 is coded for

design issues. In the case that the project or borrower failed to respond to unexpected challenges, the appropriate performance rating should be coded in either Item 1 or 2.

The design issue should be coded as follows:

1: Mentioned that no environmental planning was considered by the bank; failed to anticipate environmental problems; failed to anticipate factors that affect environmental performance.

0: none of the above issues apply and no-design issues are mentioned in an evaluation that contains some information about the environmental aspects of a project.

NA: the evaluation contains no information about the environment.

Item 4: Environmental Targets Mentioned in Lessons/Recommendations. For both items 4 & 5, information should only be coded from the final forward looking sections, not from recommendations that come up in the body of the evaluation. Different development banks have various names for these sections, including Conclusions, Lessons, Recommendations, Key Issues, Follow-up Actions, etc.

The end of each evaluation will normally contain a section on lessons learned and recommendations for future implementation and follow-up. This item should be coded if either the lessons or recommendation section contain information about the achievement of *environmental targets*, as defined in Item 1. Having a coding for Item 1, does not mean that this item will necessarily be coded and vice versa.

1: The lessons/recommendations sections contains a statement about the achievement of *environmental targets* in either the current or future project.

0: No mention of *environmental targets* in the lessons/recommendation section.

Item 5: Environmental Safeguards Mentioned in Lessons/Recommendations. This item should be coded if either the lessons or recommendation section contain

information about the achievement of *environmental safeguards*, as defined in Item 2.

Having a coding for Item 1, does not necessarily imply that this item will be coded and vice versa.

1: The lessons / recommendations sections contains a statement about the achievement of *environmental safeguards* in either the current or future project.

0: No mention of *environmental safeguards* in the lessons / recommendation section.

Additional items compiled from project evaluations. In addition to producing the original coded data described in this section, our team also compiled performance ratings that were already assigned in the project evaluations. All project evaluation assign an *overall performance rating* to each project, which we compiled. In addition, project evaluations often included a rating for *borrower performance*, which we compiled.

Coding Procedure for Country Program Evaluations

Our team coded 21 binary items from every available country program evaluation completed by the World Bank, Asian Development Bank, Inter-American Development Bank, and African Development Bank from 1990-2008. Similar to the coding procedure for the project evaluations, I recruited and trained research assistants on the binary coding items described below. I worked with the first group of research assistants to revise the coding items in order to increase reliability. In particular, I assigned paired research assistants and had them independently code 5-evaluation practice sets. In an iterative fashion, we closely scrutinized any item that was coded differently across more than one of the evaluations. Once we finalized the coding criteria, research assistants we assigned to 5-evaluation practice sets, which they had to code at 90% reliability before they were allowed to move onto the final coding stage.

Two research assistants independently coded every country program evaluation in the sample. In all cases, the research assistants made note of the evaluation section that they used to determine their coding result. When the two coding results matched, the coded value was entered into the final dataset without further review. When the two coding results were different, I referenced the sections that the research assistants noted in their coding sheets and made a decision about the final coding value. All of the coding was completed before I specified any of the models contained in this dissertation. We coded the following items according to the guidance listed below.

Executive Summary Item 1. *Is the environment (sustainability, degradation, sanitation, deforestation, etc.) mentioned as a Bank priority / area for emphasis? In the case that there is no executive summary, a memorandum to the Board can be used to for this and all executive summary items. All executive summary items can only be coded from an executive summary or memorandum to the Board.*

Executive Summary Item 2. *Are the general (not project related) environmental practices or lack of appropriate environmental management in the recipient country mentioned as a concern? This item is coded if environmental problems are identified and either environmental practices are noted as deficient or if there is no mention of any actions taken to address the problems.*

Executive Summary Item 3. *Are improvements to the general (not project related) environmental practices (policy, monitoring, implementation) of the recipient country during the period under evaluation mentioned? This item is coded if there is any mention of government actions that positively address environmental problems that are unrelated to the MDB's projects and programs. This item it coded unless the environmental practices are mentioned as being specifically tied to a project/program. This item is not mutually exclusive with ES2.*

Executive Summary Item 4. *Are environmental safeguard issues in any of the projects that are evaluated mentioned as a concern?* For a definition of environmental safeguard issues, see project evaluation coding item 2 above.

Executive Summary Item 5. *Is the implementation of environment-improving activities in the evaluated projects mentioned as less than satisfactory?* For a definition of environment-improving activities, see project evaluation coding item 1 above.

Executive Summary Item 6. *Is the implementation of environment-improving activities in the evaluated projects mentioned as satisfactory?*

Executive Summary Item 7. *Is there an unsatisfactory summary assessment of Bank programs?* Keywords used to make this determination include: major / many problems; poor execution / implementation; not been effective; fallen short of expectations; shortcomings; below par / average; systematic shortcomings; fraught with challenges; persistent problems; disappointing; ineffectual. The summary assessment is the success of the *entire* bank lending program, including projects that are unrelated to the environment. This coding item should account for performance information over the entire period being evaluation. When overall performance has been mixed, neither ES7 / ES8 should be coded.

Executive Summary Item 8. *Is there a satisfactory summary assessment of Bank programs?* Keywords used to make this determination include: effective; successful; positive outcome; highly favorable; good level of performance; significant gains; above average. If the overall performance is qualified by numerous shortcoming, this item should not be coded.

Background Item 1. *Are global environmental resources (i.e. biodiversity, tropical forests, deforestation, climate, global fisheries) in the recipient country described as having notable importance/abundance?* All background coding items are related to general, non-

project conditions and practices that are in place in the country (all other sections relate to bank activities). Items in this section capture the context in which the MDB operates. Background items are primarily coded primarily from the background section of country program evaluations, but are allowed to be coded from other relevant areas, including the executive summary. Global environmental resources concern environmental resources that cross international borders and are often subject of international treaties.

Background Item 2. *Is the degradation of global environmental resources without a link to local well-being listed as a concern?* This item should be coded if the degradation of environmental resources is not linked to human well-being, but rather for the existence value (e.g., biodiversity preservation). This item is only coded when a specific environmental issue is listed or at least two sentences about general environmental concerns are present.

Background Item 3. *Is the degradation of the environmental resources described and also linked to development and human well-being in the borrowing country?* This item is only coded when a specific environmental issue is listed or at least two sentences about general environmental concerns are present.

Background Item 4. *Are the general (not project related) environmental practices or lack of appropriate environmental management in the borrowing country mentioned as a concern?* This item relates to the institutional and policy response of the borrowing government. This item is coded positively if significant environmental problems are identified and are not being addressed, or getting worse despite being addressed. This item is only coded when a specific environmental management concern is listed or at least two sentences about general environmental concerns are present.

Background Item 5. *Are improvements to the general (not project related) environmental practices (e.g., policy, monitoring, implementation) of the borrowing country during the period under evaluation mentioned? This item relates to the institutional and policy response of the borrowing government. This item is coded if there is any mention of government actions unrelated to bank projects that positively address environmental problems. This item is coded positively if improvements are being made to general environmental conditions, even if problems remain. Policy changes that are influenced by dialogue with the MDB, but that do not result from a specific project or program are coded for this item.*

Project Performance Item 1. *Is there a sub-section (at least one paragraph) that deals primarily with environmental implementation performance? All project performance items relate to the implementation of specific MDB projects. Information from any section of the country program evaluation is coded, so long as it refers to the performance of specific MDB projects or programs.*

Project Performance Item 2. *Are the environmental impacts of development projects (a.k.a “safeguards”) during the period under evaluation mentioned as a concern? This item is only coded when a specific environmental mitigation concern is listed or at least two sentences about general environmental mitigation concerns are present.*

Project Performance Item 3. *Are the goals or targets of MDB development projects said to be at risk because of general (not project specific) environmental concerns? This item should be coded if environmental degradation negatively impacts other development goals. This item is only coded when a specific environmental concern is listed or at least two sentences about general environmental concerns related to development goals are present.*

Project Performance Item 4. *Are concerns mentioned about the achievement of environmental goals or targets in Bank projects?* This item is only coded when a specific project performance concern is listed or at least two sentences about general project performance concerns are present.

Project Performance Item 5. *Are unsatisfactory borrowing country environmental practices (e.g., policy, monitoring, implementation, ownership) listed as a reason unsatisfactory achievement of environmental goals or targets in Bank projects?* This item is coded only when PP4 is positive and the evaluation attributes concerns about environmental targets performance in bank projects to the borrowing country. PP4 and PP5 are not mutually exclusive with PP6 and PP7, and both can be coded when mixed performance is noted in the evaluation.

Project Performance Item 6. *Is the satisfactory achievement of environmental goals or targets in bank projects noted?* This item is only coded when a achievement of environmental goals in specific bank project(s) is noted or at least two sentences about general environmental performance in bank projects is present.

Project Performance Item 7. *Are good borrowing country environmental practices (e.g., policy, monitoring, implementation, ownership) listed as a reason for the achievement of environmental goals or targets in bank projects?* This item is coded only when PP6 is positive and the evaluation attributes the achievement of environmental targets performance in bank projects to borrowing country actions.

Recommendations Item 1. *Is mitigating the negative environmental impacts (a.k.a "safeguards") that result from Bank projects recommended?* All items in the recommendations section are only coded from the recommendations section at the end of the country program evaluation or from the concluding recommendations lists that is set aside in some other part of the evaluation. In the case that a recommendations

section only exist as part of the executive summary, these items can be coded from that section.

Recommendations Item 2. *Is future action on environmental goals or targets recommended?* This item is coded for project activities that directly and tangibly improve environmental resources. For a definition of environment-improving operations, see project evaluation coding item 1.

Recommendations Item 3. *Is a focus on environmental capacity building recommended?* This item is coded for actions to improve institutions related to environmental management in future periods, without directly and tangibly improving the condition of environmental resources.

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Biography

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