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Affinity or effectiveness? Donors' preferences for bypass aid

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ABSTRACT


Western donors have progressively increased the amount of foreign aid allocated through bypass channels, particularly for recipients with weak domestic institutions. Rather than giving money directly to recipient governments, aid is given to non-governmental organizations working on the ground in those countries. Explanations for this shift range from increased donor attention to effectiveness, a desire to deliver assistance directly to those in need, and enhanced legitimacy by working with local civil society partners. Donors, however, face a trade-off when deciding whether or not to allocate aid through bypass channels. Because bypass aid is not given directly to the recipient government, the donor has less leverage to prop up friendly regimes or buy policy concessions. We argue that as donors balance competing motivations, geo-strategic incentives can, at times, trump concerns regarding best practices of poverty alleviation. Using data on bypass aid from 2004 to 2019, we find that donor's commitment to good governance is ameliorated in strategically important recipient states. Strategic partners who improve their domestic governance are rewarded with less bypass aid (more government-to-government aid) at higher rates than less strategic recipients. These results highlight potential limitations of the good governance movement in foreign aid.

KEYWORDS

bypass aid; foreign assistance; NGOs

Los donantes occidentales han aumentado progresivamente la cantidad de ayuda extranjera asignada a través de canales de derivación, sobre todo para aquellos receptores que cuentan con instituciones nacionales débiles. En lugar de dar dinero de forma directa a los Gobiernos receptores, la ayuda se da a las organizaciones no gubernamentales que trabajan sobre el terreno en esos países. Las explicaciones a este cambio comprenden: una mayor atención de los donantes con respecto a la eficacia, el deseo de prestar asistencia directamente a los necesitados y una mayor legitimidad mediante el trabajo con los asociados locales de la sociedad civil. Sin embargo, los donantes se enfrentan a una disyuntiva a la hora de decidir si asignan o no la ayuda a través de los canales de derivación. Debido a que esta ayuda derivada no se entrega directamente al Gobierno receptor, el donante tiene menos influencia para apuntalar regímenes amistosos o para comprar concesiones políticas. Argumentamos que, a medida que los donantes

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equilibran las motivaciones contrapuestas, los incentivos geoestratégicos pueden, a veces, superar las preocupaciones en materia de las mejores prácticas de alivio de la pobreza. Concluimos, mediante el uso de datos sobre la ayuda derivada llevada a cabo entre 2004 y 2019, que el compromiso de los donantes con la buena gobernanza mejora en aquellos Estados receptores de importancia estratégica. Los socios estratégicos que mejoran su gobernanza interna son recompensados con menos ayuda derivada (más ayuda de Gobierno a Gobierno) a tasas más altas que los receptores menos estratégicos. Estos resultados ponen de relieve las posibles limitaciones del movimiento de buena gobernanza en el ámbito de la ayuda exterior.

Les donateurs occidentaux ont progressivement augmenté le montant des aides étrangères attribuées en contournant le gouvernement, notamment pour les bénéficiaires aux faibles institutions nationales. Plutôt que de donner directement l'argent aux gouvernements bénéficiaires, l'aide est donnée à des organisations non gouvernementales qui agissent sur le terrain dans ces pays. On explique aussi bien ce changement par une attention accrue à l'efficacité de la part des donateurs, par un désir d'apporter l'assistance directement aux personnes en ayant besoin et par l'augmentation de la légitimité conférée par le travail avec des partenaires de la société civile locale. Cependant, les donateurs sont confrontés à un compromis quand ils doivent décider s'ils attribuent leurs aides en contournant le gouvernement ou non. S'ils choisissent de contourner le gouvernement, ils auront moins de poids pour soutenir des régimes amis ou obtenir des concessions politiques. Nous affirmons que lorsque les donateurs soupèsent des motivations contradictoires, les incitations géostratégiques peuvent, par moment, prendre le dessus sur les inquiétudes relatives aux bonnes pratiques en matière de réduction de la pauvreté. À l'aide de données sur les aides attribuées en contournant le gouvernement entre 2004 et 2019, nous observons que l'engagement des donateurs en faveur d'une bonne gouvernance s'améliore dans les États bénéficiaires d'importance stratégique. Les partenaires stratégiques qui améliorent leur gouvernance nationale sont récompensés par davantage d'attributions directes d'aides (de gouvernement à gouvernement) plus fréquentes que les bénéficiaires moins stratégiques. Ces résultats mettent en lumière des limites potentielles du mouvement de bonne gouvernance en matière d'aide étrangère.

Introduction

Foreign aid has been and continues to be an important tool for donor states to enhance their political influence. During the Cold War, Western donors used foreign aid to support friendly, anti-communist regimes (Alesina and Dollar 2000; Schraeder, Hook, and Taylor 1998). As part of the efforts to conduct a War on Terror, the United States increased aid to

Iraq, Afghanistan, and Pakistan, at the cost of decreasing the share of aid allocated to the poorest nations in the international system (Fleck and Kilby 2010). Today, US policymakers and scholars debate the best ways to use foreign aid as a tool of soft power to combat the rising influence of China (Blair, Marty, and Roessler 2022).

While strategic interests have changed over time, the aid regime has also undergone a remarkable shift in aid-giving practices since the end of the Cold War (Bearce and Tirone 2010; Bermeo 2016; Dunning 2004). Donors (and scholars) have paid greater attention to aid effectiveness and how recipient governments use aid money to enhance the well-being of their citizens. Recognizing that aid can be used most effectively by recipient governments with good policies and high-quality governance, donors have encouraged selectivity (Burnside and Dollar 2000; Dollar and Levin 2006). To varying degrees, donors now take the domestic institutions of potential recipients into account when deciding *whom* to give aid.

Domestic institutions in recipient countries also affect *how* aid is given (Winters 2010). Development efforts have progressed from bilateral aid, given from one government to another, to project aid, whereby aid monies are tied to particular projects. More recently, donors have turned to alternative forms of aid delivery. To enhance aid effectiveness, donors increasingly opt for strategies that bypass weak or corrupt recipient governments in favor of delivering aid through non-governmental organizations (NGOs). Over time, this practice has gained popularity, and greater proportions of foreign aid are being delivered through non-state development channels, with the hope that bypass aid diminishes the consequences of aid capture in recipient states (Acht, Mahmoud, and Thiele 2015; Dietrich 2013; Knack 2013, 2014). The expectation is that by using NGOs to bypass corrupt governments (who might use the aid to their own benefit) or weak governments (who might be unable to effectively deliver services), more of the aid can get to those in need.

While bypass aid efforts are aimed at increasing effectiveness, there is growing evidence that it is not apolitical. Donors' decision to bypass recipient governments is strategic (Allen and Flynn 2017; Dietrich 2016). Foreign aid bypassing also affects public opinion (Shammama 2022), civil unrest (DiLorenzo 2018), and leader tenure (Allen, Ferry, and Shammama 2023) in recipient countries. While aid effectiveness has risen in importance, the political significance of foreign aid has not disappeared. In this paper, we begin from the assumption that donors perceive non-state actors, and NGOs in particular, to be more effective in reaching the poor in recipient states. Therefore, bypass aid should be allocated in greater proportions where recipient domestic capacity is lacking (Dietrich 2013). However, bypass aid is also less suitable for foreign policy manipulation (Bermeo 2016) and less

fungible for office-motivated recipients. It is a less enticing “carrot” than government-to-government aid¹ and should be a lesser preferred tool in strategic situations. Therefore, not only do donors’ strategic interests impact *how* aid is given, but at times donors’ strategic interests can trump their commitment to aid effectiveness. Good governance should impact the choice of aid modality differently based on the strategic importance of the recipient to the donor country.

We test this idea using data on bilateral aid flows from 2004 to 2019 for OECD donor-recipient pairs. Our results highlight that donors are considering strategic tradeoffs when deciding how aid will be delivered. Donors allocate more bypass aid to countries with weak domestic governance, suggesting that they are concerned about effective aid delivery. However, the importance of good governance wanes faster for strategic partners. Even as the foreign aid landscape changes, donors must still balance the oftentimes competing goals of poverty alleviation and political influence. Our primary contribution is to highlight that this calculus not only affects who gets aid, but also how they get it.

The evolution of foreign aid delivery

Following World War II, the foreign aid regime was largely characterized by the geopolitics of the Cold War. The United States provided millions of dollars in foreign aid to countries like Zaire (now the Democratic Republic of Congo), who were willing to fight against communism, albeit with poor domestic institutions and a lack of attention to the population’s well-being. The Soviet Union’s aid strategy mirrored the US approach, and both superpowers used aid to gain support for their political agendas.

These aid practices raised two primary concerns in the development community. First, critics pointed to the pattern of aid donation. Repeated studies found that donors’ strategic interests trumped humanitarian needs or recipient policies in determining aid flows (Alesina and Dollar 2000; Maizels and Nissanke 1984; McKinley and Little 1977; Schraeder, Hook, and Taylor 1998). While each donor had their own unique pathology—the United States gave more than 30% of total aid to Egypt and Israel; France skewed strongly towards former colonies; and Japan rewarded recipients with similar foreign policy preferences—all of these tendencies diluted the effectiveness of foreign aid (Alesina and Dollar 2000). Second, even when aid was given to those who needed it, critics questioned whether recipient states had the institutional capacity to implement prescribed policy and convert foreign aid into economic growth. As early as 1969, the Pearson

¹This term indicates development assistance channeled through (and implemented through) recipient government institutions

Commission on International Development identified that foreign aid should be more closely linked to recipient policies and performance.

Following the collapse of the Soviet Union, the aid regime underwent a fundamental shift. First, economic connections increased. With growing interdependence, donors recognized that poverty and conflict in less developed countries had spillover implications. Underdevelopment writ large, posed (and continues to pose) significant challenges in attaining common economic and security goals (Bermeo 2017; Cammack et al. 2006; Denney, Mallett, and Benson 2017). Thus, aid allocation patterns in the post-Cold War period are characterized by donors' pursuit of self-interested development to mitigate the negative externalities of poverty and instability that transcend recipient states' national borders (Bermeo 2017). Second, a focus on state-building emerged—as a stepping stone for maintaining peace and stability in conflict-affected and politically fragile contexts.

This did not immediately translate into development and stability for recipients; a majority of these states lacked the capacity to effectively transform foreign assistance into intended outcomes. Because aid is fungible, it provides opportunities for aid capture (Bräutigam and Knack 2004; Svensson 2000). In countries with poor quality of governance, corrupt elites and public officials can use aid monies for patronage benefits and rent-seeking (Briggs 2012, 2014; Jablonski 2014), notwithstanding aid appropriation at the top by elites and rent-seeking behavior by different factions at the bottom (Djankov, Montalvo, and Reynal-Querol 2008). In such settings, the extent to which aid can encourage economic growth is limited. While it is now widely acknowledged that foreign aid effectiveness relies significantly on the quality of governance in recipient states, the observation that “corruption severely weakens an aid program” represented a paradigmatic shift (Collier and Dollar 2004, 263).

Against the bleak prospects for aid effectiveness in poorly governed recipients, development practitioners and scholars began to advocate for curtailing foreign assistance to countries with weak institutions (Dollar and Pritchett 1998; Radelet 2004). The selectivity approach gradually became a dominant element in the development aid paradigm (Collier 2006; Dollar and Levin 2006; Winters and Martinez 2015), with changing economic and political implications for foreign aid in recipient states (Bearce and Tirone 2010; Bermeo 2016; Dunning 2004). Managing total aid flows with a strong focus on institutional quality can be detrimental to the development prospects of the poorest states, who also happen to be poorly governed. States that require the greatest external assistance may be discounted in favor of better-governed, but less needy, recipients (Dietrich 2013; McGillivray 2006).

For recipients with weak institutions, donors have further diversified aid practices by focusing on the modality of aid provision.² The emphasis has shifted from general budget support to project-specific aid, where funds are earmarked for specific development projects (Jelovac and Vandeninden 2014). However, when the implementing agency is the recipient government, there is still a high degree of leakage (Reinikka and Svensson 2004). Continued misuse and wasting of aid funds have led to a growing belief among donors that foreign aid can be provided more efficiently through NGOs, essentially circumventing or “bypassing” recipient government institutions.

The logic behind bypass aid is that foreign aid can be outsourced to NGOs as a way to supplement the provision of public goods by the state. NGOs are touted as efficient social service providers, who are functionally suited to bypass the hierarchical structure of state bureaucracies and assist in poverty alleviation by directly working with poor populations on the ground (Edwards and Hulme 1998; Tender 1982). For example, a significant portion of bilateral development assistance that bypasses recipient governments is used in basic service delivery in the social sector (Figure 1) to compensate for limited state capacity and gaps in service provision (Mcloughlin 2015; Winters, Dietrich, and Mahmud 2018). Correspondingly, there has been a remarkable growth in the number and size of operation of externally funded service delivery NGOs in recipient states, vis-à-vis advocacy NGOs (Kabeer, Mahmud, and Castro 2012; Lewis 2017). While NGOs vary in funding, size, and location decisions (Barr, Fafchamps, and Owens 2005; Brass 2012; Fruttero and Gauri 2005), in settings where the risk of aid misimplementation is high, they serve as crucial intermediaries between donors and the recipient public.

Thus, aid modality should also vary with the institutional quality of recipient states. Recipient governance impacts donor choices of programmatic versus project aid and technical assistance (Winters 2010; Winters and Martinez 2015). Donors also allocate more aid to sectors with high non-state actor engagement, for instance, humanitarian assistance as opposed to infrastructure aid, when institutional quality is low (Bermeo 2017; Winters and Martinez 2015). Overall, donor countries outsource higher proportions of foreign aid to non-state actors in aid-receiving countries with lower quality of governance (Dietrich 2013; Knack 2014).

The increased emphasis on aid effectiveness does not imply that the strategic elements of foreign aid have disappeared. Rather, the broader point is that the balance between geopolitics and development has waxed and

²Bermeo (2017) highlights another shift in aid practices whereby donors may be more selective about the economic sectors they target for assistance. As Figure 1 shows, donors may also be making strategic or at least selective choices about the sectors where bypass aid is targeted.

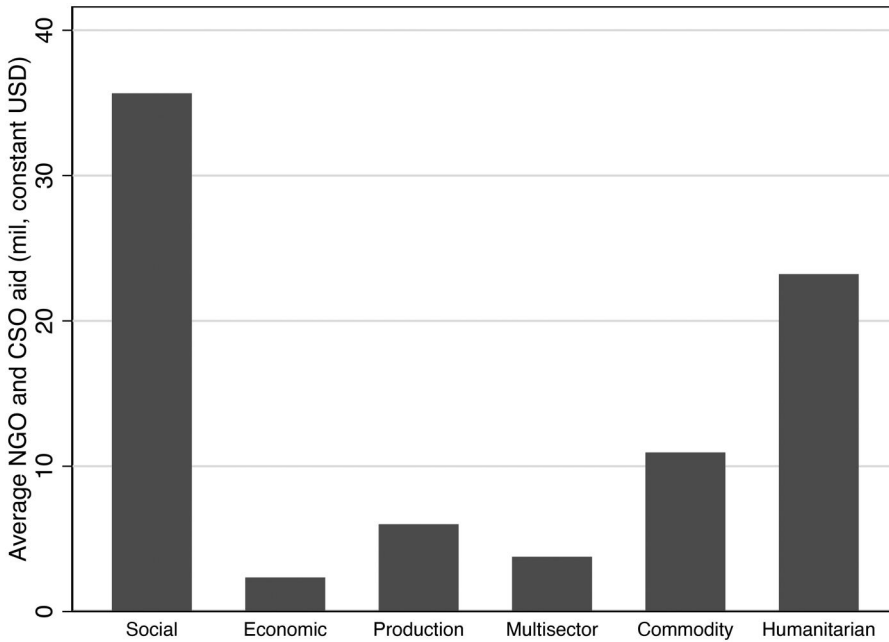


Figure 1. Average bypass aid by sectors, 2010–2018.

waned across time and recipients. While there is generally more selectivity (in both to whom and how aid is allocated) in the 21st century, this didn't stop the United States from shifting aid towards its allies in the War on Terror (Fleck and Kilby 2010). Nor does it negate the fact that these strategically important recipients were held to less stringent development criteria (Girod 2019). In the 2010s, evidence suggests that good governance may also have taken a backseat to the US and China's competition for influence over developing countries (Blair, Marty, and Roessler 2022; Kilama 2016; Vadlamannati et al. 2019). Where donors seek leverage over recipients, development gains have typically been lowest (Bearce and Tirone 2010).

Donor interests: effectiveness or affinity?

One of our contributions is to call attention to the fact that bypass aid is not apolitical. The decision to bypass is shaped by both donors' political economies and their partisanship (Dietrich 2016; Allen and Flynn 2017). It also has political implications for recipient states. Incumbent politicians may still claim credit for NGO-delivered projects (Cruz and Schneider 2017). In autocracies, NGO-delivered aid may also act as a subsidy on government transfers, lowering domestic unrest (DiLorenzo 2018). Bypass aid impacts citizens' perceptions of state legitimacy and support for local officials (Dietrich and Winters 2015; Dietrich, Mahmud, and Winters 2018;

Winters, Dietrich, and Mahmud 2018). Ultimately, the lower fungibility of bypass aid can undermine leaders' tenure in recipient countries (Allen, Ferry, and Shammama 2023). Therefore, while NGO-delivered aid can augment aid effectiveness, the choice of aid modality is likely to have political consequences that both recipients *and donors* care about.

The political consequences of aid modality largely stem from fungibility. The canonical understanding of foreign aid is implementation through recipient state institutions, which relaxes the recipient government's budget constraints, freeing up additional resources to augment the support of the winning coalition (Bueno de Mesquita and Smith 2007, 2009; McDonald 2011). In other words, foreign aid administered by the recipient government can abet leaders' office-seeking motivations (Kono and Montinola 2009; Licht 2010). However, in reality, the extent to which leaders in recipient countries are able to translate aid receipts into domestic support hinges on how foreign aid is provided. When foreign aid is provided through bypass channels like NGOs, the implementation of aid projects is generally outside of the government's control.

Donors care about how fungibility conditions aid's impact on development. The historical evolution of aid generally assumes that contemporary donors value poverty reduction, as a goal in and of itself, to achieve other global public goods, or to limit negative externalities (Acht, Mahmoud, and Thiele 2015; Bermeo 2017; Dietrich 2013). Yet, when aid is allocated through the recipient government, even in the form of program aid, money still passes through the government's hands with the potential for mismanagement (Jelovac and Vandeninden 2014). Under sound political institutions, particularly democratic institutions, the threat of opportunism is constrained by regulations, checks and balances, etc. However, in low-quality institutional settings, the threat of aid capture increases, hence donors' concern about fungibility. For example, Hodler and Raschky (2011) find that increased foreign aid disproportionately increases light emissions in leaders' birth regions, but only in countries with poor governance. Therefore, especially under weak institutions, bypassing the recipient government in favor of NGO implementation is most likely to deliver aid to those who need it (Boulding et al. 2012; Nancy and Yontcheva 2006).

National aid agencies like the US Agency for International Development (USAID) herald NGOs as partners who can enhance aid effectiveness due to their years of on-the-ground experience, which enables NGOs to deliver assistance to a wider range of beneficiaries (United States General Accounting Office 2002). According to USAID's website, "Non-governmental organizations (NGOs) are critical change agents in promoting economic growth, human rights and social progress" (US AID 2023). Additionally, when a recipient government has taken actions contrary to development

objectives, “Congress has specified that assistance to that government be prohibited or limited, while not affecting overall assistance to the country” (Morgenstern and Brown 2022, 19). Given the shortcomings of direct government assistance, international organizations like the UN and World Bank have also touted the fact that NGOs can deliver aid more effectively under difficult conditions (Bank 1998; Sachs 2005). With a smaller bureaucratic footprint, NGOs are often more nimble in service provision (Koch 2009). Their local embeddedness provides these organizations with enhanced legitimacy among the recipient public (Nancy and Yontcheva 2006), promoting better outcomes of development interventions.

While scholarship on the effectiveness of NGOs has focused on certain geographic regions or sectors, rather than cross-national samples (Brass et al. 2018), policymakers in donor states and aid agencies make clear that NGOs’ contextual knowledge, capacity, and innovative practices set them apart as implementing partners. At the level of the individual policymaker, Dietrich (2021) finds that there is a significant preference for bypass aid when the recipient is corrupt. The effect is strongest among officials from aid organizations that require more immediate verification of “effectiveness.” According to one US official, “when we learn of severe corruption in government we turn to NGOs to deliver our assistance... we need to make sure that people get our help. If we continued working with the government, we would not get anywhere,” (as quoted in Dietrich (2021, 60)).

The desire for aid effectiveness, particularly in poorly governed recipient states, is also shared by donor publics who influence the aid decisions donor governments make (Baker 2015, Milner 2006). While foreign aid can be misunderstood (Milner and Tingley 2013), taxpayers in donor countries are generally supportive of aid for development and humanitarian purposes. However, they are also consistently against sending aid to poorly governed countries because of the fear that a percentage of that aid is stolen off at the top (Knecht 2010; Paxton and Knack 2012). Aid allocated through NGOs allows governments to bypass offending actors, while still serving their development goals. For example, Dietrich and Murdie (2017) argue that donor governments turn to bypass aid after a recipient government has been named and shamed for human rights violations as a way of minimizing domestic backlash. Dietrich (2021) shows more directly that citizens in the US and Germany are more supportive of providing aid through non-state actors when recipient countries are poorly governed. Because non-state actors sidestep unsavory domestic practices, they can, according to the Swedish International Development Cooperation Agency (SIDA) “operate independently and act with legitimacy” (Löfven and Lövin 2016). This micro-level evidence underlies the more general argument that

where donors care about aid effectiveness, greater proportions of foreign aid should be delivered through bypass channels (Dietrich 2013) or allocated to sectors with lesser recipient government involvement (Bermeo 2017) when domestic capacity is lacking.

While aid effectiveness matters, we argue that donors have not forsaken their geopolitical ambitions. The development community pressed hard to minimize strategic aid donations after the Cold War, but the War on Terror and the rise of China have made some developing country governments strategically important in new ways. Donors prioritize certain relationships, and while previous work has investigated how this affects the amount of foreign aid donors give, we focus on how this affects the channel through which assistance is provided. For example, Dietrich (2013, 700) states that “donors have a baseline preference for government-to-government aid as direct relations with the recipient government will strengthen bilateral ties in general and carry pay-offs in non-development issue areas as well.” This accords with Bueno de Mesquita and Smith (2007)’s argument that foreign aid is a means for donor governments to gain influence over recipient states and extract policy concessions. Yet, the ability to achieve payoffs in areas outside of development hinges on foreign aid being provided to, or at least implemented through, the recipient government. It is hard for donors to exchange favors with their recipients when the aid they provide is not flowing to the recipient government. Thus, if donors want to use foreign aid to extract concessions on other dimensions, then the proportion of fungible aid to non-fungible aid should be higher (Bermeo 2016). Even if donors’ goals are less ambitious than policy change, for example propping up friendly regimes, the proportion of fungible aid should still be higher as it assists leader’s ability to stay in office (Allen, Ferry, and Shammama 2023). According to Bueno de Mesquita and Smith (2011), “Aid is given to thieving governments exactly because they will sell out their people for their own political security. Donors give them that security in exchange for policies that make donors more secure too...” (Bueno de Mesquita and Smith 2011, 226).

Thus, donors value both efficacy and political affinity. Donors want to minimize aid capture at the same time as they want to maximize payoffs in areas outside of development. For example, the 2019 BUILD Act in the United States combines the goals of promoting development with shifting developing countries’ allegiances away from China (Girod 2019).³ In some cases, these objectives are compatible; for example, in well-governed recipients, donors can provide government-to-government aid as strategic influence without worrying about fungibility because the recipient government

³Better Utilization of Investments Leading to Development Act

has domestic institutions in place to better ensure that aid benefits development. However, in other cases, for example in poorly governed recipients, “the two goals will tend to work at cross-purposes” (Girod 2019, 99). Using bypass channels to increase the probability that aid money reaches those in need comes at the cost of using aid for political leverage. How do donors choose their method of aid allocation when development and influence are in conflict?

In any period there will be variation in the “importance” of potential recipients (Bermeo 2016). The political economy of foreign aid literature has identified a plethora of pathways through which some aid recipients might matter more to their donors than others. Scholars have focused on factors like colonial history, voting patterns in the UN, military alliances, military spending, trade openness, etc. They have also demonstrated that donors have their own unique pathologies for biased allocation (Alesina and Dollar 2000; Lundborg 1998; Schraeder, Hook, and Taylor 1998).

Going back to Morgenthau (1962), one argument is that certain recipient states should be important for states’ security goals. Noting that the United States had international interests that could not be guaranteed by military means alone, Morgenthau (1962) saw foreign aid as an essential way of supporting allies and signaling interest to partner nations. In a more globalized world, even the most powerful states’ security is dependent on others. Interdependencies like alliances, the location of military bases, etc. imply that donors receive lucrative benefits from keeping the right “friends” in office. In the early post-Cold War period, military alliances played a key role in determining how much aid countries received (Lai 2003). More recently, Girod (2012) cites military alliances as a key variable in their index of strategic importance.

A similar argument centers around donors’ political goals. Aid can increase support in multilateral negotiations or lead to specific policy changes in the recipient state, like democratization, that advance donors’ international objectives. Beginning with Alesina and Dollar (2000), many scholars have argued that foreign aid may be used to influence voting in the UN General Assembly.⁴ For example, the Reagan administration directly tied US foreign aid to recipient voting in the UN General Assembly (Kegley and Hook 1991). More recently, the Trump administration called to strengthen the US commitment to this approach (Natsios 2020).

Finally, certain recipients can play an outsized role in the donors’ economy. Foreign aid can strengthen donors’ export markets, support new opportunities for donor firms in recipient countries, and protect donors’ access to essential imports (Lundsgaarde, Breunig, and Prakash 2010).

⁴For a review of the literature see Carter and Stone (2015).

Aid can also be important in ensuring the economic stability of partners, so that profitable economic patterns are not disrupted. Additionally, as Bermeo (2017) notes, economic goals and development goals might go hand-in-hand if development minimizes negative spillovers that could be spread through economic networks. Numerous works find that foreign aid is biased towards achieving commercial interests (Lundsgaarde, Breunig, and Prakash 2010; Neumayer 2003; Schraeder, Hook, and Taylor 1998) and Bermeo (2017) finds that this is not an artifact of the Cold War. These three dimensions are neither exhaustive nor mutually exclusive. Empirically, measures of security, political, and economic importance are all associated with higher levels of foreign aid (Alesina and Dollar 2000; Maizels and Nissanke 1984; McKinley and Little 1977; Schraeder, Hook, and Taylor 1998).

Conditioning the tradeoff between aid effectiveness and payoffs in other areas on recipients' strategic importance implies two testable hypotheses for aid modality. The first is unsurprising. Donors should allocate less bypass aid (more government-to-government aid) to countries that are important to their commercial or strategic objectives. A lower proportion of bypass aid (a higher proportion of government-to-government aid) is more likely to extract concessions or ensure the stability of a donor's "friends". While this idea of aid flows being determined by donors' strategic interests isn't new, establishing that this also affects the choice of aid modality is a logical advancement.

H₁: Strategically important recipient states will receive a lower proportion of bypass aid, as compared to non-strategic recipients.

Our central hypothesis is that donors' concern for aid effectiveness should not apply equally. Rather, the role of good governance in donors' choice of aid modality varies based on the relationship between the donor and recipient. Where recipients are strategic to donors' objectives, concerns about development should take a backseat. In other words, bad governance is more of a deterrent for government-to-government aid in less important states. This points to important limitations in the good governance movement, and the role of bypass in particular for meeting its goals.

H₂: Strategically important recipient states will see a larger decrease in the proportion of bypass aid as governance improves, as compared to non-strategic recipients.

For example, when the United States wanted Pakistan's assistance in the War on Terror, more of that aid was distributed through government channels to ensure strategic assistance. Holding Musharraf's government's feet to the fire on economic policies was not the US' foremost concern (Howell 2006).

Similarly, Girod, Krasner, and Stoner-Weiss (2009) and Girod (2019) highlight how donors without strategic interests in Uganda (e.g. the UK and Sweden) cut budget support to the Museveni administration in 2005/2006 after the government removed term limits and imprisoned the opposition. They redirected most of this aid through humanitarian projects and UN organizations. In contrast, the United States perceived Uganda as strategic in its fight against terrorism and was therefore less responsive in adjusting their method of aid allocation following these concerns.

Data and Research Design

Dependent variable

To test our theoretical argument, we conduct a quantitative analysis using data on bypass aid from 2004 to 2019.⁵ We rely on data from the OECD's Credit Reporting Service (CRS) to construct our main dependent variable (Organization for Economic Cooperation and Development 2017). Data on foreign aid commitments are available in donor–recipient dyads of aid allocation to recipient country i in donor country j in year t beginning in 2004. We rely on the CRS's reporting by channel, which includes the following categories: the public sector (i.e. traditional government-to-government aid), NGOs and civil society organizations, multilateral organizations, public–private partnerships, teaching and research activities, private institutions, and an “other” category of official development assistance. Because we are interested in donors' decision to provide aid through NGOs versus recipient governments, we follow Dietrich (2021) and Dietrich and Murdie (2017) and construct our dependent variable as follows. The variable *Bypass Ratio* is the ratio of aid provided to recipient j from donor i in year t through non-state actors relative to the total amount of aid provided in the same donor–recipient-year dyad. The numerator thus represents the sum of aid provided through NGOs and CSOs, multilaterals, public–private partnerships, private institutions and teaching/research activities.⁶ The average ratio of bypass aid to total aid is approximately 40%.

However, proportional outcomes are inherently constrained. In this case, the sum of the aid channels cannot be greater than 100%. Therefore, we follow the literature and log-transform the aid ratio. This leaves the measure unconstrained and addresses the right skew of the data. The resulting coefficients reveal how the log ratio of bypass aid changes with respect to total aid.

⁵The temporal sample is defined by data availability, which limits our ability to test our argument across the full range of strategic interests in the post-WWII era.

⁶See Appendix A for the distribution of aid across implementation channels. The “other” category is unidentifiable in the CRS database so we do not code it as bypass aid.

$$\begin{aligned} \text{Bypass ratio}_{ijt} &= \ln(\text{ratio})_{ijt} \\ &= \left(\frac{\text{Aid implemented through non-state actors}_{ijt}}{\text{Total aid}_{ijt}} \right) \end{aligned}$$

Independent variables

We begin from the assumption that if donors value aid effectiveness, either as a means or an end, aid modality will vary with the institutional quality of recipient states. Donors are wary of aid capture and therefore increase aid provision through non-state actors when recipients are poorly governed. We model Governance Quality with data from the World Bank's World Governance Indicators (WGI) (Kaufman and Kray 2019), which defines governance as "the traditions and institutions by which authority in a country is executed." This includes processes of government selection and monitoring, policy implementation, and citizen-state relations. We follow Dietrich (2013) and construct our primary measure of governance by combining all six of the WGI indicators (voice and accountability, political stability, government effectiveness, regulatory quality, rule of law, and control of corruption). We standardize all indicators onto the same 0–1 scale, before creating an additive index. The resulting index ranges from 0 to 6 with higher values representing higher quality governance.

We argue that good governance is not the whole story. Significant variation remains, in part, because a commitment to aid effectiveness can limit opportunities for payoffs in non-development issue areas. Figure 2 plots the log *Bypass Ratio* by OECD donor where recipients are below the mean level of governance. Even among the pool of recipients that are vulnerable to aid capture, there remains variation within and across donors' preference for bypass.

We hypothesize that part of this variation is explained by a recipient's importance in non-development issue areas. But recipients can be important on different dimensions and donors have their own unique pathologies. Therefore, we include measures of recipients' military, economic, and political importance from the existing aid literature. First, to capture the relationship between aid and security, we include a dichotomous indicator for an *Alliance* between the donor and recipient from the Alliance Treaty Obligations and Provisions (ATOP) project (Leeds et al. 2002). Second, we capture economic ties by focusing on donors' exports to recipient countries. Specifically, we measure logged *Exports* from donor to recipient with data from the IMF's Direction of Trade Statistics (DOTS). For both of these

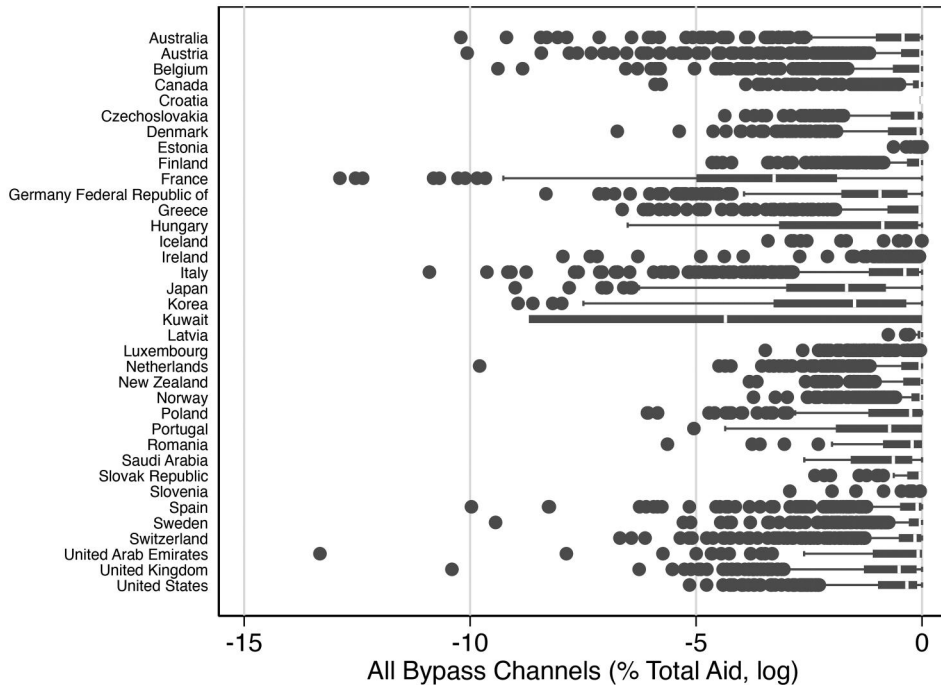


Figure 2. Bypass aid (% Total aid, log) by donor, low-quality government recipients only.

measures, **H1** implies that donors will allocate less bypass aid to countries that are allies or important trade partners.

To proxy for political interests, we include a measure of *Ideal Point Distance* in the United Nations General Assembly from Bailey, Strezhnev, and Voeten (2017). Here, the application of **H1** is theoretically ambiguous. Donors may give less bypass aid to already aligned recipients as a reward. They also might give less bypass aid to more divergent recipients as a way to influence or “buy” their future alignment (Dreher, Nunnenkamp, and Thiele 2008). While the direction is unclear, certain states should be more important to achieving donors’ political interests.

Because our main hypothesis, **H2**, is not about strategic interests per se, but the role of strategic interests in watering down donors’ commitment to good governance, we interact each of our interest variables with recipients’ WGI Index. Recipient governance should constrain the choice of modality less when recipients are important to donors’ interests. In other words, strategically important states should see a larger decrease in bypass aid as their governance improves. This implies a negative coefficient on the interaction term for *Alliance* and *Exports*. The expectation for *Ideal Point Distance* is again ambiguous. A negative interaction would imply that as recipients’ governance improves, they would be rewarded with less bypass aid at a faster rate *if* they are politically distant from the donor.

Empirical specification

Our outcome measure, the log transformation of *Bypass Ratio*, allows for a straightforward estimation through OLS regression. To account for temporal variation, we include a linear time trend.⁷ Because across-dyad comparisons are theoretically relevant in our temporal sample, which has relatively stable geopolitical relations, we opt to include donor and recipient fixed effects and cluster our standard errors at the dyad level to account for dependence over time within dyads.

Our empirical strategy also relies on controlling for economic and political factors that might confound the hypothesized relationship. First, we account for characteristics of the donor state. We control for GDP growth in the donor state (*Growth (%)*), with the assumption that countries experiencing greater economic growth are more likely to provide foreign aid abroad. Data come from the World Bank's World Development Indicators. We also include measures of *Social Expenditures (% GDP)*, to capture donors' predisposition towards public sector intervention, and total official development assistance (*Total Aid (% GDP)*) provided by each donor, to control for donor size. Data on social expenditures and aid come from the OECD. Lastly, we control for the domestic political considerations of donor states by introducing a measure of partisanship (Allen and Flynn 2017) (*Leftist*). A dichotomous coding of leftist governments comes from the Database of Political Institutions (DPI).

Second, we include a series of recipient-level variables. Larger or needier countries may be more likely to receive bypass aid if donors assume that bypass aid produces more efficient or equitable results. Therefore, we control for recipient *GDP per capita* and *Population* (log) with data from the World Development Indicators. We also want to ensure that our focus on governance is not conflated with other metrics of political institutions, specifically democracy. While democracy does imply constraints on officials, which might impact aid capture, our argument is broader and focused on recipient countries' capacity to use aid money as an effective tool for development. We therefore include the recipient country's liberal *Democracy* score from the Varieties of Democracy (V-Dem), normalized on a 0 to 1 scale (Coppedge et al. 2020). Similarly, differentiating governance from other political institutions, we control for the recipient state's *Respect for Human Rights* with data from Fariss (2014). The government's ability to provide social services is likely to be diminished in conflict situations, so we include an additional dummy variable for *Civil War* from the Correlates of War project (Sarkees and Wayman, 2010). Finally, we control for the geographic *Distance* between donor and recipient country capitals

⁷Results are robust to controlling for year-fixed effects. See [Appendix B](#).

(in kilometers). To ensure that our explanatory variables precede the decision to bypass, we lag all independent and control variables by one year.

Our primary estimation approach thus takes the following form, in which we estimate the effect of recipient governance (WGI), donor strategic interests (SI) and their interaction at time $t-1$ on the logged proportion of bypass aid in year t . We include our strategic interest variables (*Alliance*, *Exports*, *Ideal Point Distance*) separately and in a combined model. We include a vector of controls (X_{ijt-1}), recipient (μ_i) and donor (η_j) fixed effects and a linear time trend (αt). ϵ_{ijt-1} represents the error term.

$$\text{Bypass Ratio}_{ijt} = \beta_0 + \beta_1 \text{WGI}_{it-1} + \beta_2 \text{SI}_{ijt-1} + \beta_3 \text{WGI} * \text{SI}_{ijt-1} + \beta_4 X_{ijt-1} \\ + \mu_i + \eta_j + \alpha t + \epsilon_{ijt}$$

Results

As a test of **H1**, [Table 1](#) presents our unconditional results. Models 1–3 capture the role of security, commercial, and political concerns, respectively. Model 4 introduces all three indicators into a common model.

Table 1. Unconditional results.

	(1) Security	(2) Commercial	(3) Political	(4) All
WGI index	−0.299*** (0.0775)	−0.283*** (0.0774)	−0.298*** (0.0776)	−0.284*** (0.0776)
Alliance	0.0262 (0.0534)			0.0492 (0.0537)
Exports (log)		−0.0506*** (0.0117)		−0.0517*** (0.0118)
Ideal point distance			−0.00997 (0.0422)	−0.0144 (0.0424)
Donor growth (%)	−0.0205*** (0.00355)	−0.0208*** (0.00356)	−0.0204*** (0.00354)	−0.0209*** (0.00356)
Donor social expenditure (% GDP)	0.0206*** (0.00612)	0.0202*** (0.00618)	0.0209*** (0.00611)	0.0198*** (0.00622)
Donor total aid (% GDP)	524850.5 (10033913.6)	−417504.8 (10037319.1)	719925.3 (10030806.2)	−365198.4 (10049103.4)
Donor Leftist	0.0283 (0.0218)	0.0258 (0.0219)	0.0275 (0.0219)	0.0245 (0.0221)
Recipient GDP per capita	0.0000840*** (0.0000286)	0.0000885*** (0.0000285)	0.0000844*** (0.0000287)	0.0000887*** (0.0000286)
Recipient population (log)	0.279 (0.277)	0.287 (0.277)	0.288 (0.277)	0.281 (0.278)
Recipient democracy	0.161 (0.228)	0.179 (0.227)	0.155 (0.228)	0.176 (0.227)
Recipient civil war	0.0531* (0.0308)	0.0529* (0.0309)	0.0531* (0.0308)	0.0531* (0.0309)
Recipient respect for human rights	−0.0728*** (0.0275)	−0.0736*** (0.0275)	−0.0721*** (0.0275)	−0.0739*** (0.0276)
Distance	0.0000364*** (0.00000693)	0.0000240*** (0.00000735)	0.0000355*** (0.00000676)	0.0000255*** (0.00000743)
Year	0.0623*** (0.00665)	0.0642*** (0.00667)	0.0622*** (0.00665)	0.0644*** (0.00668)
Observations	24581	24314	24581	24314

Standard errors in parentheses.

* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

Several findings emerge. Across all models, the coefficients for governance align with previous findings. The *WGI* Index has a negative and significant effect. Substantively, based on Model 4 and holding all other variables constant, a one-unit increase in a recipient's *WGI* score decreases the proportion of bypass aid by approximately 25%. When institutional quality is problematic for aid effectiveness, donors opt for bypass through non-state actors. When institutional quality is not a concern for donors, they opt for increased proportions of government-to-government aid, which has a greater potential to generate positive payoffs in other areas.

Our unconditional results still provide additional nuance to previous findings – albeit not as uniformly as expected. Only one dimension of strategic importance is consistently significant; more *Exports* are associated with less bypass aid. This suggests two things. First, commercial interests play an important role in aid modality, although their substantive effect is smaller than recipient governance. For every 1% increase in donor exports, the proportion of bypass aid falls by 0.05%, *ceteris paribus*. Economic ties not only affect the level of aid, but also the delivery channel through which aid is provided. Second, contrary to our expectations, *Alliances* and *Ideal Point Distance* are not significant predictors of aid modality. This may be because development provided through bypass aid can have positive externalities in the security or foreign policy realm; it may also be because the importance of security ties has weakened over time.

Regarding our control variables, both donor and recipient characteristics are important. Donors with larger social expenditures provide more bypass aid, while donors with higher levels of economic growth provide less bypass aid. Countries engaged in a civil war receive more bypass aid. Recipients with greater respect for human rights receive less bypass aid. At the dyadic level, donors consistently provide more bypass aid to geographically distant countries.

Given previous research, the results so far are unsurprising. Robust findings about the role of strategic interests on the *level* of aid allocation make our findings on the *channel* of aid allocation highly intuitive. [Table 2](#) thus presents results for our second hypothesis (**H2**) about the conditional nature of good governance criteria. Where recipients are deemed important in other issue areas, bad governance should be less of a deterrent for government-to-government aid. Commitments to aid effectiveness should be watered down. Again, we present results for security, economic and political importance separately before combining all three measures in the same model.

We find that strategic relationships between the recipient and donor play an important mediating role in how donors channel foreign aid. For all three measures, the interaction between recipient importance and

Table 2. Main results.

	(5) Security	(6) Commercial	(7) Political	(8) All
WGI index	−0.281*** (0.0780)	0.576*** (0.164)	−0.108 (0.0914)	0.585*** (0.165)
Alliance	0.313 (0.194)			0.102 (0.201)
Alliance interaction	−0.111 (0.0701)			−0.0159 (0.0724)
Exports (log)		0.0710*** (0.0229)		0.0527** (0.0246)
Exports (log) interaction		−0.0507*** (0.00921)		−0.0440*** (0.0100)
Ideal point distance			0.263*** (0.0789)	0.158* (0.0852)
Ideal point distance interaction			−0.118*** (0.0301)	−0.0737** (0.0334)
Donor growth (%)	−0.0205*** (0.00354)	−0.0207*** (0.00355)	−0.0201*** (0.00355)	−0.0206*** (0.00356)
Donor social expenditure (% GDP)	0.0207*** (0.00612)	0.0203*** (0.00619)	0.0211*** (0.00611)	0.0200*** (0.00622)
Donor total aid (% GDP)	425675.9 (10035174.9)	−558315.4 (10005016.2)	764334.2 (10032440.1)	−564861.6 (10018703.3)
Donor Leftist	0.0286 (0.0218)	0.0262 (0.0219)	0.0271 (0.0219)	0.0248 (0.0220)
Recipient GDP per capita	0.0000825*** (0.0000286)	0.0000886*** (0.0000283)	0.0000899*** (0.0000289)	0.0000920*** (0.0000285)
Recipient population (log)	0.252 (0.277)	0.279 (0.276)	0.291 (0.277)	0.269 (0.278)
Recipient democracy	0.164 (0.227)	0.175 (0.225)	0.156 (0.228)	0.173 (0.226)
Recipient civil war	0.0524* (0.0308)	0.0447 (0.0308)	0.0515* (0.0308)	0.0451 (0.0308)
Recipient respect for human rights	−0.0742*** (0.0275)	−0.0755*** (0.0276)	−0.0728*** (0.0275)	−0.0764*** (0.0277)
Distance	0.0000359*** (0.00000691)	0.0000208*** (0.00000737)	0.0000334*** (0.00000682)	0.0000214*** (0.00000748)
Year	0.0632*** (0.00667)	0.0647*** (0.00665)	0.0618*** (0.00665)	0.0648*** (0.00669)
Observations	24581	24314	24581	24314

Standard errors in parentheses

* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$

governance is negative and significant (although the conditional effect of *Alliances* loses significance in the combined model). Improvements in governance are rewarded with a decline in bypass aid, and bypass aid decreases more quickly for “important” recipients. In other words, the reward for an improvement in governance quality is higher for important partners.

To better understand these conditional effects, [Figure 3](#) plots marginal effects from Models 5, 6, and 7. The top panel graphs the effect of good governance (*WGI*) for allied and non-allied dyads, along with their 95% confidence intervals. The difference between allied and non-allied dyads is only significant at intermediate levels of governance. For example, a country with median levels of governance (i.e. Vietnam) can expect the proportion of bypass aid to be greater (32%) from a non-allied donor (i.e. Italy). The predicted proportion of bypass aid (24%) is smaller when the donation

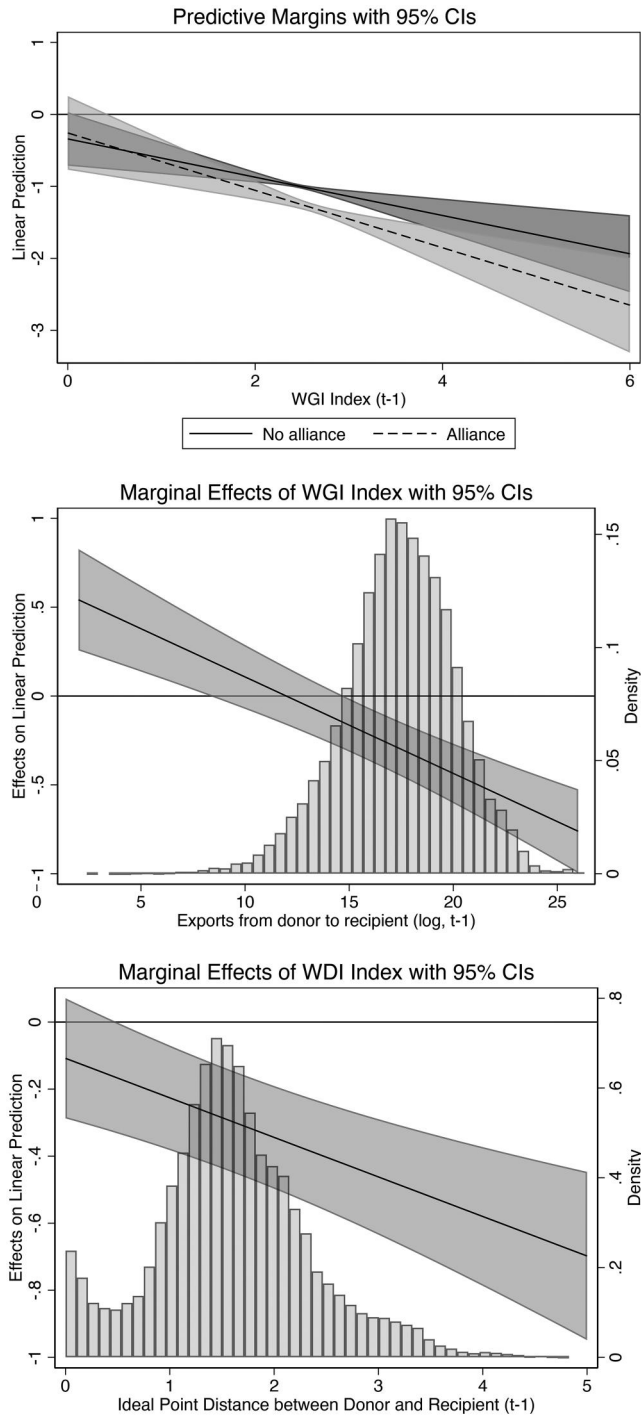


Figure 3. Marginal effect of WGI index for allied and non-allied dyads (top), average marginal effect of WGI index across levels of export dependence (middle), average marginal effect of WGI index across levels of ideal point distance (bottom).

comes from an allied donor (i.e. Japan). This suggests that concerns over aid capture are likely to dominate geopolitics in the most unsavory recipients. Concerns over aid capture are also likely to be minimal in well-governed recipients, allowing governments to revert to their baseline preference of government-to-government aid for everyone. Therefore, security concerns may trump governance in only a subsection of recipients.

The middle and bottom panels graph the effect of good governance (*WGI*) across different levels of donor *Exports* and *Ideal Point Distance*, respectively. More specifically, in the middle panel, larger export markets receive greater rewards for increases in government quality. Based on the average marginal effects, at the 25% percentile of export dependence (i.e. South Korean exports to Belize), a one unit increase in governance is associated with a 17% decrease in the ratio of bypass. As export dependence approaches the 75% percentile (i.e. American exports to Belize), a one unit increase in governance is associated with a 35% decrease in bypass ratio. In the bottom panel, the results for foreign policy priorities are similar. For dyads with low ideal point distance in UNGA voting, i.e. the ideal point distance between donor and recipient is in the 25% percentile (Portugal and Thailand), the average marginal effect of a one-unit increase in governance is associated with a slight decline in the proportion of bypass aid to total aid (approximately 20%). For dyads where there is more distance between UNGA ideal points, i.e. the distance between donor and recipient is in the 75% percentile (The United Kingdom and Thailand), a one-unit increase in governance quality is rewarded with a larger decline in bypass aid (approximately 30%). Combined with earlier results, this implies that donors use government-to-government aid as a potential bribe for dissimilar states whose preferences they most want to change. This suggests that there may not just be an aid-for-policy change bargain but also an aid modality-for-policy change bargain.

To ensure that our results are not dependent on empirical modeling choices, we perform several sensitivity analyses, which we describe here and report in full in the appendix. For succinctness, we present results for aggregate models combining military, economic, and political interests. [Appendix B](#) focuses on specification. It's possible that aid delivery through non-state actors is the only viable option in "failed" states. To account for this, we follow Dietrich (2013) and reanalyze our results removing the top 15 failed states each year according to the Fragile States Index. Similarly, it's possible that the decision to bypass is driven by recipient governments' control over NGO operations within their border. If some governments impose tighter restrictions on NGO activities, then this could limit the opportunities for donors to choose bypass. To ensure that this is not driving our results, we control for Dupuy, Ron, and Prakash (2016)'s measure

of NGO finance laws (0,1) and V-Dem's measure of CSO repression. Our results are robust in both specifications. Alternatively, including a lagged dependent variable and year-fixed effects, in lieu of a year-time trend, the results don't change.

Appendices C, D and E probe our conditional findings by using alternative measures of key variables. In [Appendix C](#), we focus on the dependent variable, bypass aid. Results are robust to using the unlogged form of *Bypass Ratio*. As NGOs/CSOs and multilateral organizations represent the most popular non-state implementation channels, we also replicate our analyses for both types of aid separately as a percentage of total aid. Our findings for the interaction of *Exports* and *Ideal Point Distance* with the *WGI* Index do not change. Finally, we look at the logged *Amount of Bypass Aid* (in millions of constant USD). While the conditional effect of *Exports* is less significant, recipient countries whose policy positions donors are trying to manipulate receive greater rewards (less bypass aid) as governance improves. Interestingly, there is also evidence of a negative interaction effect for *Alliances*.

[Appendix D](#) turns to alternate measures of governance. Results hold when focusing on an index of *WGI*'s economic indicators.⁸ They are also robust when using the State Fragility Index and Fragile States Index.⁹ [Appendix E](#) presents unconditional and conditional results for alternative measures of recipient importance. While previous work points out that donors favor their former colonies as a means of maintaining their sphere of influence (Schraeder, Hook, and Taylor 1998), we do not include colonial relationship as one of our main measures because it possesses military, economic and political dimensions. Here, we demonstrate that former colonies receive less bypass aid and witness a larger decrease in bypass aid as governance improves. We also use principal components analysis (PCA) to reduce the dimensionality of our data by determining whether the information from our set of strategic variables (*Alliances*, *Exports* and *Ideal Point Distance*) can be summarized by a smaller set of latent variables. While not directly interpretable, we include the first eigenvector and its interaction with the *WGI* Index and find that our results are unchanged.

Finally, we acknowledge that donors are heterogeneous in their preference for bypass. Major powers should be more likely to use government channels for strategic considerations. Empirically, this translates to major powers being more attuned to voting in international organizations and less attuned to human rights violations when considering the modality of

⁸Corruption control, government effectiveness, regulatory quality, and rule of law.

⁹The State Fragility Index comes from Marshall and Elzinga-Marshall (2020) and the Fragile States Index is taken from Fund for Peace (2020). The results with the Fragile States Index point to an additional positive effect of alliances on bypass aid, which is counter to our expectations.

aid provision (Adhikari 2019, Dietrich and Murdie 2017). Therefore, we present unconditional and conditional results for samples of minor power donors, major power donors, and Scandinavian donors in [Appendix F](#).¹⁰ While minor powers are generally considered to be less “geopolitical” in their aid policy, our results suggest that even minor power donors provide less bypass aid to larger export markets and that this effect is heightened as recipient countries improve their governance. Major powers on the other hand give less bypass aid to politically distant states, but their focus is not conditional on a recipient’s political institutions. Finally, even the Scandinavian donors, often cited as the most “development-oriented” have their own pathologies. This is consistent with Schraeder, Hook, and Taylor (1998)’s conclusion that rather than donors being more or less strategic than others, they are driven by different strategic biases.

We take this analysis one step further in [Appendix G](#). We present additional results by individual donor, which allows us to speak to more specific patterns in the data. Overall, results are consistent with our finding that some donors are more strategic than others, but each has their own unique pathologies. Due to space constraints, we highlight three takeaways. First, many of the major power donors bias their implementation of aid away from non-state actors when the recipient is a major export market. Similar to results pooled by donor grouping, the biases of major power donors are largely unconditional on recipient governance. Second, while individual analyses of the Scandinavian donors imply fewer strategic incentives, the results suggest that the negative interaction between *WGI* and *Ideal Point Distance* is a largely Swedish phenomenon. Finally, minor powers appear to have the most heterogeneous preferences; the results are the most mixed. Some countries (e.g. Austria) decrease their level of bypass aid to allied recipients at a faster rate as the quality of governance increases. Others (e.g. South Korea) react the same way for politically distant states. A third set of countries (e.g. Canada and Switzerland) demonstrate no strategic biases in their choice of implementation channel. We take these results as a starting point and encourage future scholars to develop more specific arguments about diversity in donor preferences for bypass aid.

Conclusion

The allocation of foreign aid is based on donors’ preferences, which vary over time as the geopolitical climate and aid regime evolve. Foreign aid was an essential tool of international influence during the Cold War. Allies

¹⁰Major powers are considered the United States, The United Kingdom, France, Germany, and Japan. Sweden, Norway, and Finland represent the Scandinavian donors.

were rewarded with more aid, regardless of their degree of need. Parallel with the shift in political tensions following the end of the Cold War, donors shifted more attention to aid effectiveness as a tool of poverty reduction. Yet, the heightened focus on selectivity, primarily based on recipients' domestic political institutions, does not negate the importance of foreign aid as a tool of soft power in the contemporary era. Donors' preferences for effectiveness may at times, conflict with their preference for strategic affinity.

In this paper, we explore whether donor states have become more sophisticated in the way they balance competing preferences. Traditionally, the expectation has been that donors give more aid to allies or give no aid to non-allies. The global emphasis on aid effectiveness should make donors' choices more complex, shifting their calculus from the *level* of aid to the *channel* of aid implementation. As donors have increasingly turned to NGO partners to bypass weak or corrupt governments, political and economic relationships may still affect donors' choice of aid modality.

Importantly, our results highlight cracks in the facade of the good governance approach to foreign aid. If donors are only concerned about rewarding recipients whose state capacity is higher or improving, then their geo-strategic relevance should be of no importance. Our results suggest that good governance affects decisions about aid modalities less for important recipients. Countries with weak state capacity that are strategically insignificant will receive a greater proportion of their aid through bypass channels than comparable states with strategic importance.

While others have focused on the reinvigoration of strategic aid allocation in the War on Terror (Fleck and Kilby 2010; Girod 2019), we note the relevance of our findings in an era where the United States and China are engaged in strategic aid competition (Blair, Marty, and Roessler 2022; Kilama 2016). With the rise of China and their efforts to gain influence in Asia, Africa, and Latin America, Western donors may increase their efforts to use aid strategically, but when they do so, the choice will not be whether or not to give aid, but how to give it.

More importantly, extreme global poverty has decreased over time. UN efforts like the Sustainable Development Goals continue to emphasize the international importance of improving the well-being of all citizens of the world. NGOs play an important role in this global effort. While significant scholarship argues that NGO service provision plays a uniquely positive role in alleviating poverty (Boulding et al. 2012; Faye and Niehaus 2012; Nancy and Yontcheva 2006), there remains debate (Dreher, Mölders, and Nunnenkamp 2010). Our findings suggest that deciphering the effects of NGO-provided aid is more challenging; the decision to bypass is nonrandom. If more bypass aid is directed at non-strategic recipients, then

research may be capturing upward bias given previous findings that aid is most effective at alleviating poverty when it is given with non-strategic objectives (Bearce and Tirone 2010).

Finally, our results provide important fodder for future research. For example, our findings focus on the good governance movement as a broad concept. They also reaffirm the specific biases of different bilateral donors. But how do donors (either similarly or heterogeneously) evaluate good governance? Which criteria are the most important in their allocation decisions? It's likely that some donors are most concerned with aid capture and thus give less government-to-government assistance to regimes that score high on corruption, but other donors are most concerned with democratic values like voice and accountability. Similarly, we know little about the non-state actors through which donors are choosing to implement aid projects. Who are the NGOs, and how do donors choose them? Donor governments likely maintain closer ties to some NGOs (i.e. large, international organizations) than others (i.e. local organizations). Different NGOs are also likely to be suited to working in different environments. While our findings suggest a heightened focus on the method of aid allocation, many parts of the bypass process still remain a blackbox. How donors decide to bypass and who they decide to bypass to are unanswered questions.

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