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Structural Incentives and the Performance of International Relief and Development NGOs

Scott Bennett
Washington University in St. Louis

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WASHINGTON UNIVERSITY
Center in Political Economy
Political Economy & Public Policy

STRUCTURAL INCENTIVES AND THE PERFORMANCE OF INTERNATIONAL RELIEF AND DEVELOPMENT NGOs

by
Scott Andrew Bennett

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Graduate School of Arts and Sciences
of Washington University in
partial fulfillment of the
requirements for the
degree of Master of Arts

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Abstract

Current measures of evaluating NGO effectiveness do not actually capture what they claim. While some researchers and “watchdog” associations seek to develop better measurements, this paper offers an alternative hypothesis that the search for better metrics is a red herring—the lack of accountability is a rational outcome of the structural incentives within the NGO system. This paper begins by outlining some of the existing organizational evaluation methods. Next, the incentives of each powerful actor within the system are explored, revealing that all are motivated by factors other than effectiveness. Lastly, some emerging alternative approaches to the current NGO system are identified, providing a possible glimpse into the future of international development.
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1) Introduction

While any measure of global poverty is inherently difficult and imprecise (see Deaton, 2010) the World Bank defines extreme poverty as living on less than $1.25 a day and estimates that it is currently endured by 1.4 billion people in the developing world (Chen and Ravallion, 2008). Often, the effects of global poverty are also the causes, as poor sanitation, poor nutrition, insufficient health care and limited formal education all hinder the world’s poor from seizing whatever opportunities exist to lift themselves and their families out of poverty.

Each year, the rich nations of the world spend billions of dollars to combat these issues. In 2009, the Organization for Economic Cooperation and Development (OECD) reported that the total amount of aid disbursed by the governments of its 32 member states—known as official development assistance, or ODA—was $119.8 billion. Additionally, the OECD reported private donations from its member’s citizens of another $23.8 billion (OECD, 2008, 2010). The Center for Global Prosperity (CGP), an American policy institute, has developed what it claims is a more accurate calculation of private giving. While this new metric has not yet been applied to all OECD countries, estimates for the United States and the United Kingdom, at $34.8 billion and $1.61 billion respectively, are both three times higher than OECD-reported amounts (2008). In terms of private giving in both real and per capita amounts, the U.S. is by far the most beneficent. Moreover, it is the only country in the CGP’s dataset with private donations greater than official aid in real terms.

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1 All dollar amounts herein are expressed in U.S. dollars.
Much of these funds—both ODA and private donations—are channeled to non-governmental organizations (NGOs). As of 2002, NGOs were officially receiving six percent of ODA (Agg, 2006). If extrapolated to 2008 data, that would amount to $7.19 billion. However, Hulme and Edwards (1997, p.6) point out that the official figure grossly underestimates the true volume of official aid sent to NGOs, since it only accounts for direct grants and not funds channeled through NGOs by governmental and multilateral agencies for the implementation of projects. In 2001, USAID alone issued $7 billion in contracts to NGOs (Werker and Ahmed, 2007). By 2008, USAID’s budget had grown by another 40 percent (“Overseas Loans and Grants”, 2008). In all, NGOs manage funds equivalent to one-third the amount of ODA (Riddell, 2007).

For decades, these numbers have been steadily increasing; in fact, ODA has more than doubled in the past ten years alone (OECD, 2010). Over the past fifty years, the amount of aid transferred from rich countries to poorer countries has amounted to $2 trillion (Moyo, 2009, p.28). Yet despite the enormity of the resources used, positive results are not always apparent; the scourge of poverty remains a reality for so many. Given the large scale of their projects and public profiles, bilateral and multilateral development agencies such as the World Bank and USAID have been targets of persistent criticism, facing allegations of poor fiscal management and insufficient results (see, for example Moyo, 2009 and Easterly, 2006).

NGOs on the other hand, have portrayed themselves as apolitical and serving the interests of their beneficiaries. A 2003 Gallop poll conducted in advance of the annual World Economic Forum found NGOs the second-most trustworthy of
seventeen institutions (the first was the military, multinational corporations and national legislatures placed last). This positive image has aided NGOs in avoiding the scrutiny that has dogged the larger agencies. But as their presence has grown, concomitant with a rise in public funding, researchers and the media have begun regarding NGOs more critically.

This paper will discuss the current methods for evaluating NGOs and explain why they are insufficient. Next, it will describe how, in the absence of fair and accurate evaluation, the powerful actors in the system—that is, all except the beneficiaries—are able to pursue incentives other than effectiveness with impunity. Lastly, a sample of emerging alternatives to the current NGO system is presented. These alternatives seek to address the shortcomings inherent in the current system. Preceding these sections, however, is a further elaboration of the current NGO sector.

1.1) NGO Typology

NGOs comprise a specific subset of the larger non-profit sector. Often called the “third sector,” these are societal organizations that operate apart from the government and the commercial sectors. While non-profit organizations can include trade unions, religious orders and educational institutions, NGOs in the context of this paper refer only to non-profit organizations that are concerned with improving the lives of people in developing and crisis-affected countries. This definition includes a wide range of activities, including education, health care provision, water and sanitation improvement, humanitarian relief, economic development and advocacy.
Further, NGOs herein only refer to those organizations which operate internationally, as opposed to locally-based non-profit organizations, or community-based organizations. Often this distinction is drawn using the terms northern NGOs (NNGOs) and southern NGOs, with northern and southern being euphemisms for rich and poor, respectively.

The Union of International Associations, a research institute, maintains a directory of international organizations. Currently, the number of registered international NGOs is listed at 63,866 (2010). However, despite these large numbers, the spheres of international development and humanitarian assistance more closely resemble oligopolies. Simmons (1998) pointed out that half of the contracts issued for humanitarian relief operations are awarded to only eight NGO federations. Similarly, Harmer and Macrae note that in 2000, “one-quarter of the U.S. government funding for relief and development aid went to just four NGOs: CARE, Catholic Relief Services (CRS), Save the Children, and World Vision” (2003, p. 26). In addition to each other, these NGOs also compete with for-profit contractors for donor agency contracts. From 1996 to 2005, the proportion of USAID funds awarded to for-profit contractors increased from 33 percent to 58 percent (McCleary, 2009).

On the whole, donor agency funds account for an average of 27 percent of revenue among U.S.-registered NGOs (ibid.). However, for the largest NGOs, this figure is considerably greater. CRS, Save the Children and World Vision all rely on

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2 Another commonly used label for NGOs is private voluntary organizations (PVOs)—this is the official terminology used by the United States Agency for International Development (USAID).

3 An NGO federation is a network of affiliated national offices that work under the same name and mission but with varying degrees of autonomy. Simmons’ list is as follows: CARE, World Vision International, Oxfam Federation, Médecins Sans Frontières, Save the Children Federation, Eurostep, CIDSE (International Co-operation for Development and Solidarity), APDOVE (Association of Protestant Development Organizations in Europe).

2) Current Evaluation Methods

In a sense, non-profit organizations are victims of their own past successes. It was the nonprofit sector that spearheaded the push for greater transparency in both the public and private sectors. As expectations of transparency and accountability have become more common, this pressure has since expanded to include the non-profit sector.

As competition for private and government funds has increased there has been an attendant rise in non-profit sector watchdog organizations angling to help steer their charitable giving. Additionally, the concept of “venture philanthropy” has arisen, whereby large-sum donors take a more active role in the way their money is used. While evaluation methods have been developed, accurately capturing the effect of a non-profit organization remains elusive. The reasons for this are two-fold: First, the outcomes of non-profit organizations are difficult to measure. Second, the organizational diversity within the sector makes comparisons difficult. Below, three common methods are discussed in detail.
2.1) Social Return on Investment (SROI)

A common approach to evaluating a nonprofit organization is to attempt to capture and quantify the social benefits it created. One example of this is the social return on investment (SROI). Based on the common “return on investment” metric used in the private sector, SROI is the ratio of the monetized value of an organization’s social impact divided by the amount of capital spent, or “invested.” The appeal of this method is that it distills the benefits of an organization’s various outputs into an easily digestible figure. With the input and output variables both expressed in financial units, gauging the overall effect of the organization’s activities becomes easier.

The process of compiling an SROI begins with identifying the non-financial impacts of an organization’s operations in a per-unit basis. These impacts can include both benefits created, such as the number of new jobs, as well as costs avoided, such as people no longer using welfare programs. These benefits are then translated into dollar terms. At this point, some SROI practitioners (see Ralser, 2007) subject these amounts to spending multipliers to capture positive spillovers within a community. Once all amounts are computed, they are summed for a specified time period, say five or ten years, and discounted to their present value. This total present value amount then becomes the numerator of the SROI calculation. Figure 1 gives an example of a calculated SROI statement.
While SROI has an undeniable intuitive appeal, as a method of evaluating an NGO’s effectiveness it leaves much wanting. Since unlike financial accounting, no standardized method exists, calculations can vary considerably depending on the variables and assumptions used. This makes SROI calculations susceptible to manipulation.

Being a ratio, SROI’s value is only apparent in a relative context. One might presume that SROI could be useful to a donor when deciding which organizations to support. However, given the lack of methodological rigor, SROIs developed by different organizations are incomparable. Olsen adds: “Differences in outcomes
measured, measurement methods, and data sets used can significantly affect the SROI calculation, and if not standardized, could result in comparisons that are of little value (2003, p.12-13).”

SROI, therefore, is not an effective method for assessing the effectiveness of organizations. Its value rather, is in its ability to demonstrate to donors how their contributions can spread throughout a community. In other words, SROI is a fundraising tool that borrows concepts from finance (ROI, net present value) and economics (spending multipliers) to convey a false sense of precision.

2.2) “Efficiency”

Another commonly used method for evaluating NGOs is the so-called “efficiency” measurement. This method takes the proportion of an organization’s expenditures that are allocated to programs and compares it to the proportion used for non-program expenditures, such as administrative and fundraising costs. Because non-program expenditures are not directly reaching beneficiaries, these expenses are condemned by donors and the media.

Analyzing expenditures is a seductive metric for a number of reasons. First, these data are easily available since all non-profit organizations must include them in their public tax filings. Second, because “efficiency” measurements constitute a straightforward ratio, they allow for easy comparisons between organizations engaged in widely varying activities. For example, according to Charity Navigator’s online data, the Doctors without Borders (MSF) USA, which delivers emergency medical aid to victims of humanitarian disasters, reports spending 86.8 percent of its outlays
toward programs. AmeriCares, which provides donated supplies to similar crises, reports channeling 99 percent to programs (ibid.). Using this method, AmeriCares would therefore be regarded as the superior organization.

A third reason why the use of efficiency measures is so common is because they appeal to a public unsatisfied with how they perceive non-profit organizations spend their donations. A 2004 Brookings Institution survey in which only eleven percent of respondents reported that they believe that charities do a good job of spending their money wisely (as cited in Pallota, 2008, p.4). Similarly, “seventy percent of people surveyed in a 2008 NYU study said that charities waste a ‘great deal’ or a ‘fair amount’ of money (ibid.).”

For these reasons, this measure has been adopted by non-profit “watchdog” organizations such as Charity Navigator and GuideStar. These organizations give credence to the metric and call it to the media’s attention. Forbes magazine is but one media outlet that reports on the figure. Every year the publication issues an annual list of the 200 largest U.S. charities. This list ranks each organization in five categories, all pertaining exclusively to revenues and expenditures.

The problems with evaluating NGOs in this way are many. First, Maren (1997, p.141) points out that this figure tracks the proportion of expenditures, not the proportion of donations. It is not uncommon for the larger NGOs to receive over half of their revenue from government and multilateral agencies. Maren gives the example of Save the Children, whose expenditures are nearly three times larger than donations, so “even if Save spent none of the sponsors' money on programs, they could still find
a way to claim that 75 percent of the money they spend is going to program services (ibid.).”

Additionally, there does not exist any clear definition of what constitutes program expenditures. With increasing pressure from the media and the public over how organizations allocate their resources, many NGOs have been pressured into less transparent and more creative accounting procedures (Jacobs, 2006, p.266). One such example in the domestic non-profit sphere was brought to light in 2006 when Mothers Against Drunk Driving (MADD) Canada was found to be spending 81 percent of their donations on administration and fundraising rather than the 83.6 percent they publicly claimed. According to the Toronto Star article:

MADD counts the words in each fundraising request and apportions expenses based on that: when the telemarketer or paid door-knocker gives prospective donors a "victim's story" that is public awareness and part of the charity's mission — not fundraising — even though the story is told to get a donation. The charity uses the same method of accounting for its mail fundraising drive.

In [a telemarketing script], the paid fundraiser begins with a statistical overview of drunk driving in Canada, then describes volunteer-based services the charity provides. At this point, the fundraiser asks for a minimum donation of $50. If the prospective donor agrees, the telemarketer asks for a credit card number. If the donor says "no" then the fundraiser launches into a description of how MADD is pushing for tougher court penalties. Again, the fundraiser asks for a donation. If the prospective donor agrees, a credit card number is requested. If the answer is "no" more statistics are provided followed by one final pitch for money. [MADD’s CEO] said this is the charity's public awareness and education campaign. Ironically, the Star found, the person who does not donate gets the most "public awareness" because the fundraiser continues providing information.
Yet more problematic than any discussion of an organization’s expenditure accounting is that criteria based on an organization’s spending (i.e., outputs) completely ignore any discussion about what the organization is achieving (i.e., outcomes). The impact of an NGO does not lie in its balance sheet, but rather in the quality and scope of the services it provides to its beneficiaries.

Maren (1997, p.269) points out that because one hundred percent of in-kind donations are usually passed on to beneficiaries, NGOs, such as AmeriCares, who deal explicitly on this type of donation, are able to claim that 99 percent of their donations go to the needy. It does not necessarily follow, however, that those contributions are always appropriate. Easterly (2006, p.338) explains that donors give based on what they have, not what is needed. This can especially be the case for the in-kind donations that AmeriCares manages, since firms can benefit from reducing surplus inventory and reducing their tax burden. Indeed, Maren (1997, p.264-265) mentions examples of AmeriCares donating Gatorade, Mars candy bars, Pop Tarts and bras to disaster-stricken areas.

2.3) Project-level Evaluation.

Most development activities are conducted in the form of discrete projects. The most common method of managing development projects is through a logical framework approach (LFA) (Roche, 2004). This approach was first devised by USAID in the late 1960s (“The Logical Framework Approach”, 1999). Soon other bilateral and multilateral agencies followed suit. Because these agencies were requiring its use among grantees, LFA quickly spread among NGOs.
LFA is designed to be used throughout the project management process, from planning to monitoring and ultimately to evaluation. The main characteristics of LFA are causality, bounded timeframes and objectively verifiable indicators (ibid.). After identifying a desired goal, LFA uses backward induction to identify a series of causally linked events that, if achieved (under several identified assumptions), would contribute toward that goal. Over the years, various aid agencies have developed their own idiosyncratic variations of LFA, with slightly differing terminology (see Rugh, 2005). Figure 2 provides an example of the logical framework used by the United Nations’ Food and Agriculture Organization.

<table>
<thead>
<tr>
<th>Project Structure</th>
<th>Objectively Verifiable Indicators</th>
<th>Means of Verification</th>
<th>Important Assumptions</th>
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</thead>
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<td>Goal</td>
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<tr>
<td>Purpose</td>
<td>if</td>
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<td></td>
<td>then</td>
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<tr>
<td>Outputs</td>
<td>if</td>
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<td></td>
<td>then</td>
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<tr>
<td>Activities</td>
<td>if</td>
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*Figure 2: The Logical Framework (Source: FAO, 2010)*
LFA’s reliance on causal logic is its greatest appeal to donors and the fiercest point of contention among critics. Critics assert that the local developing country context is too complex to correspond to simple charts. Poverty, as Easterly points out, is a “complicated tangle of political, social, historical, institutional, and technological factors” (2006, p.6). Edwards and Hulme sight evidence that “when donors finance service delivery they expect contracted outputs to be achieved and do not see themselves involved in a learning process” (1995, p.852). This challenges the practical insight that development work is essentially experimental (Easterly, 2006; Duflo, 2006; Riddell, 2007).

When LFA is too rigid to reflect the local reality, NGO’s resort to a pro forma attitude toward the process, cynically filling in necessary boxes to appease donors and receive funding (Bakewell and Garbutt, 2005). Similarly, donors’ preferences for short timeframes and measurable outputs can lead to NGOs becoming more risk averse, shying away from potentially innovative projects with more uncertain outcomes (Hulme and Edwards, 1997; Wenar, 2006).

LFA acknowledges that achieving a project’s intended goal is subject to many environmental factors beyond the control of the practitioners and participants. Evaluation therefore is limited to checking whether predefined output indicators have been met (Jacobs, 2006). Duflo (2006) responds to this disconnect by identifying two separate types of evaluation: process evaluation and impact evaluation. Process evaluation makes sure that the implementing organization has used grant funds as promised and conducted the activities stipulated in the contract. Impact evaluation is determining what the long-term effect of those activities was. Since processes are
considerably easier to assess, most projects are evaluated exclusively in this manner—the causal design of the project allows implementers to simply assume that goals are gradually coming to fruition.

As meeting predefined project indicators becomes the measure of a project’s success, NGOs and evaluators risk myopia, losing sight of the larger development context (Bakewell and Garbutt, 2005). Additionally, foreign NGO staff may not be able to recognize the ancillary impacts of their work. Riddell elaborates: “changes that appear marginal to the outside observer can often provide a crucial catalyst galvanize poor people (2007, p.271). This raises the important issue of who conducts a project’s evaluation. Most evaluations are conducted in-house (Easterly, 2006, p.193). This immediately threatens the credibility of any results. Consider the case where a project is based upon a renewable contract. These renewals are contingent upon a positive evaluation; being too truthful about a project could threaten the organization’s chances for renewal (Cooley and Ron, 2006). Even when an independent evaluator is used, objectivity is still not ensured since an evaluators’ future employment may depend upon a favorable review of the project of the organization which has hired him or her (Wenar, 2006).

In addition to claims of bias, critiques of evaluations have been leveled on methodological grounds, since even with the inclusion of baseline data most evaluations ignore the counterfactual question of what would have resulted in the absence of any intervention (Riddell, 2007). Several development economists, such as those from MIT’s Abdul Latif Jameel Poverty Action Lab have sought to rectify this issue by incorporating randomization into evaluations.
2.3.1) **Randomization.** Similar in design to drug trials, randomized evaluations begin with a pool of potential beneficiaries which is then randomly divided into control and treatment groups. Both groups undergo baseline evaluations. Next, the treatment group participates in the intervention being evaluated. Upon the project’s conclusion, both groups are again evaluated in order to determine the existence and extent of any effects.

Part of the appeal of randomized trials is their easily understandable results, which can be as simple as a comparison between two means and their distributions (Duflo, 2006). Additionally, randomized evaluations do a better job of addressing the counterfactual issue than simple before-after evaluations because they control for temporal factors. For example, children, on the whole, will improve academically after a year regardless of whether they receive a new textbook (ibid.).

Randomization is however, not without its critics. The greatest concern deals with the extent of a trial’s generalizability—how much can be extrapolated from the results of a randomized evaluation? Rodrik elaborates:

> The typical evaluation will have been carried out in a specific locale on a specific group and under specific conditions. Its generalizability to other settings—its "external validity"—is never assured—and it is certainly not established by the evaluation itself (2009, p. 26).

Certainly the results of a randomized trial in Kenya’s Kibera slum would not be wholly applicable to a program in an Andes village. Still, by controlling for more variables, randomized evaluations do further overall understanding of in a systematic manner. Over time, these experiments could lead to increasingly effective
development programs. A practical concern is that randomized evaluations are very resource intensive—institutional donors have heretofore not even been willing to devote the necessary resources to non-randomized evaluations (Smilie, 1996).

While randomization does promise to improve service delivery of various programs, project performance is not currently a practical method for evaluating organizational effectiveness. Evaluation data is dispersed among various donor agencies, each using its own evaluation methods. There is not sufficient political pressure to develop universal measures, to aggregate data, or to make evaluation data freely accessible to the public. NGOs have no obligation and little incentive to make project evaluations public (Edwards and Hulme, 1996). Add Werker and Ahmed:

[T]he paucity of clear, objective evaluations should not be particularly surprising. It is in neither the interests of the NGOs nor the official donor agency, complicit as a funder, to publicize less-than-stellar results. In addition, public opinion of NGOs is generally very high in rich countries and poor countries alike, so the demand for rigorous evaluation is correspondingly low (2008, p.22).

2.4) Conclusion

NGO performance on the whole is widely viewed as variable (Jabobs, 2006, p.247). Individual NGO performance however, is not currently being accurately assessed. The effectiveness of an NGO cannot be captured in the fulfillment of short-term outputs. A true evaluation of an NGO’s effectiveness must consider the long-term outcomes of activities and relate them to each organization’s specific mission (Collins, 2005). NGO missions, however, can be aspirational or overly vague (Jacobs, 2006). It does not necessarily follow that the successful implementation of a project
serves an NGO’s mission. Aid agency-funded projects are designed first and foremost to serve the agency’s objectives.

The lack of counterfactual data causes problems of attribution and the diversity of program areas complicates meaningful comparisons (Riddell, 2007, Ahmed and Potter, 2006). To date, no method exists that can accurately evaluate NGO performance (Collins, 2005; Pallotta, 2008).

2.5) Accountability

With evaluation limited to aspects of process, not impact, NGOs are accountable to their donors based on their ability to keep records rather than any impact they might effect. With respect to their beneficiaries, whose needs are ostensibly the organizations’ raison d’être, NGOs are entirely unaccountable. As Werner (2006) notes, accountability goes beyond responsibility to include the possibility of sanction. Beneficiaries have no power to hold NGOs accountable (Easterly, 2006, p.17). Indeed, the NGO sector exists in a unique system where their performance is not subject to a feedback system in which viability depends upon performance. This is a stark contrast to both the private and public sectors. For-profit firms rely upon the patronage of customers; elected officials must maintain the support of voters.

Considering the growing size and importance of the NGO sector to international relief and development, one might presume that the pressure would arise to find a more meaningful evaluation metric. Instead, the current system persists in a stable equilibrium. The lack of accountability does not constitute a coordination
problem because as empirical evidence demonstrates, leaders and subordinates of both public and private organizations seek to avoid accountability (Fox, 1992). In fact, save for the beneficiaries, all of the actors in the international development system harbor motivations other than effectiveness. To better understand what those motivations are, each actor is discussed in greater depth in the next section.

3) The Motivations of Actors within the System

The sphere of NGO activity is complex. NGOs operate primarily outside of their home country. Funding derives from multiple sources. NGOs engage in multiple activities and interact with multiple constituencies. Within this system, different actors enjoy varying degrees of power. Home and host-country governments exercise de jure power over NGO activity. Conversely, donors exercise de facto power by their ability to threaten “exit,” or withdrawn future funding from financially dependent NGOs. Beneficiaries don’t have any real power in this relationship; they are encouraged to participate in the development process, but no real discretion is conferred to them. If development is a matter of delivering goods and services, Martens (2004) notes that simply sending a check and allowing beneficiaries to fill their needs on the open market would suffice. Werker and Ahmed (2007) explain that instead, aid agencies prefer channeling their funds through Western NGOs because those organizations ostensibly ensure that funds are used as donors intend. As a result, assistance is offered to beneficiaries on “take it or leave it” terms. The incentives of each powerful actor are discussed in detail below.
3.1) NGOs

The staff working within an NGO’s headquarters face separate incentives than those working overseas in the organization’s field projects. This is reflected in the pay structures of each group—headquarter staff are full-time employees (though often supplemented by volunteers) tasked with bringing in donations and winning agency contracts, field workers are hired to implement projects and are therefore commonly employed on a project-to-project basis.

3.1.1) NGO Headquarters. Lofty rhetoric aside, NGOs, just as with for-profit firms, are motivated to maintain their long-term viability. To do this, NGOs must continue to attract money to sustain and expand operations. For NGOs, revenue comes from two main sources: private donors and aid agency contracts. The increasing number of international development NGOs has driven up the competitiveness for funding. Neither private donations nor government contracts are rewarded strictly on merit and NGOs strive to appeal to both constituencies.

When appealing to the public, decades of experience have taught NGOs how to mobilize their supporters—Smillie and Minear (2004, p.193) note one experiment in which an Irish charity created two different public appeals, one based on development and another based on a more simplified, alarmist message. The alarmist message garnered ten times more in donations. Knowing how heartstrings can affect purse strings, NGOs will often play up their roles in humanitarian relief efforts despite the
fact that these represent a small portion of their total activities (McCleary, 2009, p.138). In addition, NGOs that began by sponsoring children but have branched out to other activities continue to promote this image in order to retain supporters (ibid., p.139).

NGOs have also adapted to increase their odds of winning government contracts. Many NGOs have moved beyond their traditional area of expertise, becoming active in myriad aspects of aid and development. World Vision USA’s website, for example, lists operations in nearly 100 countries and over fourteen areas of focus, spanning such disparate activities as water sanitation to economic development to advocating against child trafficking. With this drive to become development “jacks of all trades,” comes a pressure not to turn down any opportunity. Within NGOs there exists the sentiment that choosing not to participate in a program of high government importance could harm the chances of winning future government contracts (Smillie and Minear, 2004, p.192). Additionally, the high levels of competition ensure that any attempt to boycott a particular intervention would be futile, as plenty of other NGOs would be waiting in the wings to fill in the gap.

As government contracts become an increasingly important source of funding, often accounting for over half of total revenue, NGOs have been forced to alter the relationship they have traditionally kept with governments. Representing the “third sector,” NGOs originally posed as an alternative to government, often challenging government policies and offering services as a supplement in areas where government was negligent. Greater reliance on government contracts has pushed NGOs to becoming agents of the government, incorporating government reporting techniques,
appropriating government terminology and executing government foreign policy objectives. As government contractors, NGOs must focus on producing the agreed-upon outputs within the agreed-upon time period. The result is that organizations are less able to conduct experimental approaches and pay less attention to organizational learning (Edwards and Hulme, 1996). Additionally, this increased dependency on government funding threatens NGOs’ credibility when speaking on behalf of beneficiaries (Clark, 1995).

Many observers have claimed that increased government reliance has compromised NGO autonomy. NGO leaders are less inclined to speak out against controversial government policies and will agree to carry out projects that they know will have little chance of success (Edwards and Hulme, 1996). The reliance on private donors and government for continued funding means that those groups are able to hold NGOs accountable.

3.1.2) NGO Field Staff. The pool of aid and development workers has been steadily professionalizing over the decades, moving away from the early stereotype that Maren (1997, p.33) refers to as “good-hearted, globe trotting, draft-dodging hippie types,” to more ambitious professionals with specialized advanced training. It is safe to assume that the majority of those employed with international NGOs are drawn by the motivation to “make a difference”—at least initially—and contemporary development practitioners with degrees from institutions such as Harvard’s Kennedy School of Government and Columbia’s School of International Public Affairs forgo substantial earnings over a lifetime for the opportunity (Werker and Ahmed, 2008).
Yet it would be too simplistic to attribute this opportunity cost entirely to altruism. In a series of interviews with newly-recruited aid workers awaiting deployment, Berjneld (2009) offers a more nuanced perspective of personal motivations. In addition to creating a positive impact, aid workers were motivated by a desire to develop both personally and professionally, an interest in gathering new and challenging experiences, the prospect of working closely with like-minded people, and feelings of curiosity and wanderlust. Once drawn into the milieu, aid workers often become disillusioned, contributing to large staff turnover rates within the sector.

Others aid workers however, are drawn in by the levels of authority they possess that are greater than they would otherwise command in their home countries (Stirrat, 2008; Maren, 1997). Perhaps one of the most egregious recent cases of power differentials afforded to workers on account of their “Westerness”—though admittedly not a true “development” context—occurred in the early reconstruction of Iraq in the wake of the 2003 U.S.-led invasion. Young professionals, most below the age of thirty and some recent graduates, were hired by the Coalition Provisional Authority despite their lack of relevant experience. In time these workers were presiding over a $13 billion budget and making decisions that affected millions of Iraqis (Cha, 2004). When asked what prompted them to take such demanding positions despite their inexperience, professional advancement was commonly cited as a motive (ibid.).

With a clearer understanding of the incentives that allow aid workers to part with their families, accept reductions in remuneration and expose themselves to difficult living conditions, it can be said that aid workers, while still being well-intentioned, are motivated by more than improving the lives of beneficiaries.
3.2 Donor Governments

Government’s involvement in foreign aid is steered primarily by two main interests: foreign policy and domestic interest groups. Alesina and Dollar (2000) point out there is no direct correlation between the degree of a country’s need and its foreign aid receipts. Instead, governments use aid funds in order to influence both the leaders and constituents of foreign countries. In general, OECD-members use aid programs to promote democratic societies and free markets. Simultaneously, donor countries use aid to influence regimes or citizens of strategically important countries. These two foreign policy objectives can come into conflict, such as when a nondemocratic country controls an important resource, is located in a geostrategic location, or is succumbing to the influence of an ideological or military rival.

Governments are also influenced by interest groups. Large diaspora populations can affect foreign aid allocations (Werker and Ahmed, 2008). Domestically, powerful industries have influenced how aid programs are designed. This has led to what is called “tied-aid”—a system in which certain goods or services are required to be provided by domestic suppliers. In the U.S., food aid is a prime example of tied-aid. Under U.S. Public Law 480, also known as PL 480 or the “Food for Peace” program, the U.S. government purchases agricultural surpluses from American farmers to be donated overseas. Seventy-five percent of this food is then required to be shipped using American carriers (Wenar, 2006). Because surpluses are dependent upon world food prices rather than humanitarian need, their availability tends to decrease as prices rise, which can be food security is most threatened (Farzin,
Additionally, much of the food that the U.S. donates is monetized, both by recipient governments and by NGOs in-country. When levels of monetization are sufficiently high, they can drive down the price of food and threaten the livelihoods of local producers (Maren, 1997, p.170).

Other examples of tied-aid include stipulating the use of national contractors, computer manufacturers, automakers and air carriers. About three-fourths of official U.S. aid is tied to American companies (OECD, 2001). By restricting the number of available suppliers, costs increased, choices are limited and quality is compromised (Easterly, 2006, p.192). This causes a direct negative effect on aid effectiveness.

Within donor countries there does exist a domestic constituency who believe in a moral obligation to assist those who are less fortunate. Sadly, even this pressure does not guarantee that aid is made effective. As Easterly (2006, p.253) points out, this can cause a bias towards observable actions. Easterly provides the example of PEPFAR—the President’s Emergency Plan for AIDS Relief. Under this initiative, the majority of resources—55 percent— are allocated for the treatment of existing cases, while the prevention of future cases was only 20 percent. Easterly explains: “If money spent on treatment went instead to effective prevention, between three and seventy-five new HIV infections could be averted for every extra year of life given to an AIDS patient” (ibid.). Treating patients, however, is an easier and more observable than changing people’s behavior. Sadly, it is also less effective in the fight against HIV and AIDS.

Taken together, these policies demonstrate that effectiveness is not the primary concern of government aid. If it were, then countries would receive aid based upon
need and laws would encourage the allocation of resources towards their most cost-effective uses.

3.3) Private Donors

3.3.1) Individuals. Funds from private individuals account for seventy-five percent of all charitable donations (McCleary, 2009, p.22). Dollar-for-dollar these contributions are more valuable than government funds because NGOs have more discretion over how they are spent (Smillie and Minear, 2004, p.197). Fierce competition among NGOs for these funds have led NGOs—as well as researchers—to seek a better understanding of what motivates people to part with their money for the sake of charity. Harbaugh (1998) suggested that donors are primarily motivated by two factors: private satisfaction and public prestige—later studies have corroborated both theories. Harbaugh et al. (2007) used brain imaging to show that charitable contributions activate the areas of the brain associated with pleasure. Similarly, in 2009, a study by Sieg and Zhang revealed that well-heeled donors are attracted to high-profile fundraising events that convey social status and create an opportunity to mingle with other affluent and influential individuals. NGOs respond to these different motivations by offering a mix of ways to donate. Sponsorship and gift donation catalogs allow donors to acquire a sense of satisfaction at varying price points. Gala-type fundraising events, on the other hand play more to donors’ desire for attention.

What is interesting is that the utility derived by the donor is independent of the actual output of the NGO. Vesterlund explains:
Researchers typically rely on the predictions of the classical model of charitable giving when determining whether the benefits from giving have private or public characteristics. The vast majority of the empirical research on this topic has found that private benefits are the primary motive for giving. As a result most researchers agree that there is limited evidence to support the common belief that donors give because they care about the nonprofit’s output (2006, p.43).

In the market for charitable contributions, donors remain rationally ignorant to the true performance of the organizations they support, relying instead on proxy measures such as the strength and ubiquity of an organization’s image and the deftness of its donor relations (Jacobs 2006). Regardless of actual performance, all NGOs tend to exaggerate the extent of their successes and downplay or conceal any failures (Smillie, 1996).

Private donors are neither fully-informed nor fully altruistic. A charitable donation is still a financial transaction and donors must still derive sufficient satisfaction to be induced to give. Because donors receive their satisfaction at the point of transaction, their benefit occurs independently of the activities they fund.

3.3.2) Foundations. In addition to private individuals, NGOs also receive funds from private, grant-making foundations. Under U.S. law, these entities are obligated to spend at least five percent of their assets each year on charitable activities (Doucette, 1999). Additionally, foundations must direct their contributions towards charitable or educational purposes and avoid political activities (Yunus, 2010, p.128). Aside from aligning these grants with the foundation’s mission, private foundations have no further obligations. It is worth noting that foundations too can be subject to less-than
purely altruistic motives. Consider the Bill and Melinda Gates Foundation, which in 2002 donated $100 million over ten years to fight HIV in India. Concurrently, Bill Gates’ own Microsoft Corporation invested over $400 million towards fighting the Linux operating system in the lucrative emerging Indian software market (Greene, 2002). Commentators have speculated that the foundation’s donation, which garnered plaudits for Gates, served as a smokescreen for Microsoft, a company notorious for its aggressiveness toward its competition. (ibid.).

3.4) Local Governments

Local governments are not motivated to support the effectiveness of NGOs. The presence of NGOs creates opportunities for local officials to profit. It is in the interests of these officials, therefore, not that NGOs’ activities succeed, but that they continue. Local leaders understand that any meaningful improvement in their economy could lead to a reduction of official development assistance—free money to which they often become reliant (Easterly, 2001, p.116). Occasionally, perverse incentives can arise; as a case in point, in Somalia in the late 1990s the Minister of Agriculture was personally profiting from the sale of US food aid. By successfully performing his duties promoting and improving the nation’s agriculture his personal earnings would have decreased (Maren, 1997, p.168).

Every transaction between the government and NGOs represents an opportunity for a monetary transaction, either officially through fees and taxes or unofficially through bribes. Resources diverted to government officials can support unpopular leaders while reducing the impact of programs (Wenar, 2006). In the case
where local leaders are elected democratically, foreign aid conditional upon enacting certain policy prescriptions can threaten the leader’s ability to represent the interests of his or her constituents (ibid.).

In addition to ceding resources to the local government, NGOs must strike a precarious balance between empowering beneficiaries without seriously challenging local power structures. NGOs’ foreign funding and staffing arouse suspicion among local officials. Similarly, higher wages, higher quality resources and opportunities for international travel can evoke feelings of jealousy (Clark, 1995). NGOs, therefore must be cautious not to clash too directly with the local government. Since government policies are usually partially responsible for the poor conditions of beneficiaries in the first place, placating the government can render certain development objectives impotent.

With NGOs needing to tread lightly, government officials are able to claim credit for foreign aid programs. As long as these programs continue, beneficiaries remain dependent and grateful to local leaders. But if any program were to actually achieve self-sufficiency among beneficiaries, their gratitude to political leaders would no longer be certain (Maren, 1997, p.69).

3.5) Multilateral Aid Agencies

At less than ten percent of total revenues on average, multilateral agencies account for considerably less NGO funding than government agencies and private sources (McCleary, 2009). Multilateral agencies, such as the World Bank, European Union, and the agencies of the United Nations are similar to government aid agencies
in that they are funded with public tax revenues and face incentives to demonstrate positive results. However, multilaterals are further shielded from the scrutiny of their tax-paying constituents—there is no multilateral equivalent to the United States’ Freedom of Information Act, for example, to support transparency (Maren, 1997, p.120). Their increased isolation has allowed multilateral agencies to become more internally driven.

Within the agency staff face pressure to disburse ever larger sums of money (Chambers, 1996). While the majority of multilateral outflows are in the form of loans, it can be implied that this pressure to disburse funds extends to NGO grants and contracts. Easterly elaborates on this pressure thus:

Most donor institutions are set up with a separate department for each country or group of countries. The budget for this department is determined by the amount of resources it disburses to recipients. A department that does not disburse its loan budget will likely receive a smaller budget the following year. Larger budgets are associated with more prestige and more career advancement...” (2006, p.116).

Conversely, shrinking departments can threaten the organizational standing of staff (Moyo, 2009, p.54). This push to keep funds flowing, coupled with minimal external accountability creates a system were the agency is disassociated from the repercussions of its activities. The “absorptive capacity” of an NGO is of greater importance to multilateral agencies than its professional capacity the project’s likelihood of success.

3.6) Conclusion

Even if an NGO were highly effective, no measure exists for that organization to objectively prove itself. Organizational sustainability is independent of
effectiveness. Rather, NGO sustainability depends upon satisfying those who pay their bills. For aid agencies, this means meeting agreed-upon output indicators and maintaining sound financial records. For private donors, this means maintaining a strong organizational public image and hosting fundraising events that appeal to donors. Executing these activities well requires considerable resources—resources no longer available for programs. Scarcity dictates that allocation decisions must incur opportunity costs. Given the nature of certain NGO activities, the consequences to beneficiaries may be critical.

Yet no amount of resources will suffice if beneficiaries remain powerless. The broken feedback loop must be fixed so that the opinions and needs of beneficiaries can affect the types of services provided and the manner in which they are offered. The powerful actors have no reason to change the system and no incentive to devolve power. Expecting changes to occur is therefore futile.

5) Potential Alternative Approaches

To those familiar with the NGO system, its shortcomings are apparent. Alternative methods of alleviating poverty and improving the lives of the world’s poor have been emerging. What follows is a brief summary of some notable alternatives receiving attention. The purpose of this section is to highlight potential new directions; a thorough analysis of each method is beyond the scope of this paper.
5.1) Social Businesses

Hailed by Forbes in 2010 as one of “twenty-five ideas to change the world,” social business is the newest brainchild of Muhammad Yunus, one of the pioneers of the global microfinance movement. According to Yunnus, a social business provides a socially-beneficial good or service to a community through free market exchanges. The advantage of this business model is that it shifts the focus of the organization from continually courting donors to meeting the needs and preferences of the beneficiaries. Since, like a traditional business, the organization’s sustainability depends upon maintaining and expanding revenue, a social business must be nimble.

What separates Yunus’ concept of social business from a traditional business is that social businesses do not generate any profits for their owners and investors. Once the business is able to make enough revenue to cover its costs, it begins to repay its investors their investments—without interest. Any further financial “surpluses” are retained within the business to aid expansion and hedge against contingencies.

Currently no county’s legal framework is setup to accommodate this type of business. Because of their tax-exempt status, non-profit organizations face strict laws governing the extent to which they can engage in commercial activities. For-profit businesses on the other hand entrust directors with a legal obligation to maximize profits on behalf of shareholders. Directors of social businesses operating under the for-profit business framework would face the possibility of being sued by owners for diverting earnings to socially beneficial purposes (Yunus, 2009, p.119).

Relaxing Yunus’ definition, we find that some new organizational models of a similar vein. In 2005 the U.K. introduced the community interest company (CIC).
CICs are organizations that pursue government-approved social objectives. They generate profits and pay taxes. Dividends paid out to owners however are limited by law to 35 percent of the company’s profits (Yunus, 2009, p.126-127).

Similarly, several U.S. states have allowed for the creation of low-profit limited liability companies (L3Cs). Like CICs, L3Cs are tax-paying companies. They are directed toward pursuing a social purpose while still generating profits. However, as the name suggests, social aims trump profit maximization. The unique appeal of L3Cs is that they are designed to qualify for financial support from charitable foundations—something typical businesses are excluded from under the current U.S. federal tax code (Yunus, 2009, p.127-128).

The success of a social business depends on its ability to continually induce low-income customers to part with precious funds. Importantly, recent randomized evaluations of user fees in education and health suggest that even small fees can affect significant decreases in participation (Holla and Kremer, 2009). Coupled with a more volatile business environment typical of poorer countries suggests that behind the elegant concept, operating a successful, financially sustainable social business could prove exceptionally difficult.

5.2) Patient Capital Investing

Another market-based alternative to the current NGO system is patient capital investing. This investing strategy aims to tackle poverty by providing long-term capital—either loans or equity—to fund new businesses in developing countries. At the vanguard of this movement is Acumen Fund, established in 2001. What sets
patient capital and Acumen apart from traditional business investment is that it seeks to support businesses that earn both financial and social returns. Acumen Fund operates as a non-profit foundation that channels philanthropic funds to socially beneficial for-profit businesses. Because these businesses employ untested models in difficult business environments they are frequently passed over by traditional investors. Patient capital investors are therefore characterized by a greater risk tolerance (Alexander, 2009).

Acumen looks for innovative, locally-conceived business ideas that address issues of water, health, housing, energy and agriculture. In order to qualify for funding businesses must be designed to be become wholly sustainable through sales revenue. In addition to generating financial and social returns, businesses selected for funding must be scalable so that their impact can spread to a wide range of customers.

All Acumen Fund investments are interest-baring and come with the full expectation of repayment, usually within five to seven years. Since Acumen itself is a charitable foundation, all repayments and dividends are recycled into new investments (ibid.). One of the most significant aspects of Acumen’s approach is that in addition to money, businesses receive professional management support to improve the chances of success. In this manner, patient capital investment is closer to traditional venture capital than to other models of development financing like microcredit.

5.3) Kiva Microfunds

Founded in 2005, Kiva Microfunds has received accolades for its innovative approach of using the internet to bring together microloan borrowers and lenders from
around the world. Kiva’s website maintains a database of borrower profiles, from which lenders can choose to whose loan they wish to contribute. The unique prospect of contributing directly to the financing of specific loans has helped Kiva attract over $158 million within five years, originating from 479,000 lenders and nearly as many borrowers among 204 different countries (“Facts and History”, 2010).

In 2009, more information of Kiva’s model emerged, revealing that loans had in fact already been issued by local microfinance partner organizations which then used Kiva funds to “backfill” these loans (Strom, 2009). While this method is more cost-effective than an actual peer-to-peer lending model, it was the subject of a sizable backlash from lenders upset to learn that any connection between their funds and their borrower’s loan was mostly fictional.

In light of these revelations, Kiva’s model is decidedly less innovative than once assumed. By offering personal stories but pooling resources, Kiva’s service is a slightly different take on decades-old approaches like child sponsorships and donor “gift catalogs.” Moreover, studies are beginning to call into question the extent to which microfinance can have on reducing poverty (see: Banerjee et al., 2009 and Karlan and Zinman, 2009). Therefore, it seems that Kiva—at least in its present iteration—does not present practical alternative to the current system.

5.4) Conditional Cash Transfers

Called “the world’s favorite new anti-poverty device” by the Economist magazine (2010), conditional cash transfer programs (CCTs) provide stipends to poor households if they meet certain conditions, such as school attendance or vaccinations
for children. As the Economists notes, more important to poor families than the amount of the payment, is the payment’s reliability, which can be a godsend to households earning uneven incomes. According to the World Bank (Rawlings and Rubio, 2005) evaluations of CCT programs in Columbia, Mexico and Nicaragua have all proven to be effective in improving school enrollment rates, improving preventative health care and raising household consumption. While the positive research is encouraging, CCTs are no panacea. While CCTs do a better job at incentivizing the poor, they remain prescriptive in that their behavior is still guided by others.

One provocative extension of CCT programs was proposed by economist William Easterly in his 2006 book *The White Man’s Burden*. Easterly’s idea was to provide the poor with “development vouchers” which can be used for any number of purposes, such as health and education services, however their recipients they see fit. Vouchers could be brought to local NGOs and exchanged for services, after which they would be sent redeemed by the issuing agency for cash. The idea is that beneficiaries would be able to exercise more control over their lives while simultaneously forcing NGOs compete for beneficiaries.

6) Conclusion

The current NGO system reflects outmoded mindsets and power structures. Most of today’s prominent NGOs arose in the early twentieth century, a time marked by the beginnings of the American missionary movement (Bays, 2010). While an American belief in divine providence traces back it to the country’s beginnings, the
emergence from the Second World War as the world’s lone superpower, followed by
the success of the Marshall Plan only served to reinforce the conviction in American
exceptionalism. With the dawning of the Cold War and increasing government use of
NGOs as agents of foreign policy, the scope of NGO activity expanded significantly.
Since these organizations emerged from a sense of Western superiority and
righteousness, the NGO approach was by design prescriptive rather than
collaborative—rare is the NGO that was invited by its beneficiaries.

Decades of development projects have proved this dominant approach to be
ineffective and on occasion, destructive. The fact is that development work is highly
experimental. The context of every problem is complex, combining common and
unique elements. The difficulty lies in recognizing which is which.

While it remains to be seen precisely which new models will gain prominence,
those that are sensitive to local contexts and capacities, that embrace new
technologies, and that adapt to beneficiary feedback present promise. After all, under
the current system there is much room for improvement.
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