

International assistance, donor interests, and state capture in the Western Balkans

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Abstract

Despite the enormous inflow of international assistance to the Western Balkans over the last twenty-five years, the intended state-building efforts have only had partial success and great concerns have been raised over the problems of state capture, weak governance, poor rule of law and widespread corruption at a high level throughout the region. The paper identifies the patterns of international assistance and examines the extent to which donor aid allocations have been driven by concerns for recipients' need and merit, or by donor self-interest. The analysis reveals that while donor allocations have on the whole reflected need, they have not reflected merit to the same extent, suggesting that international assistance may have facilitated domestic political elites' engagement in practices of rent-seeking and state capture. With a few exceptions, EU donors and EU Institutions have not allocated their aid to motivate adherence to EU norms in candidate and potential candidate states in the region. The paper concludes that the "Samaritans dilemma" is alive and well in the Western Balkans, and that donors have chosen to mostly overlook poor governance behaviour among recipients in order to prioritise assistance to the neediest countries while pursuing their own foreign policy concerns.

Key words: International aid, state capture, corruption, Western Balkans, EU enlargement

1. Introduction

Over the last three decades the countries of the Western Balkan region have received an enormous inflow of concessional official development assistance (ODA), amounting to about \$62 billion¹ over the whole period from 1993-2018, supplemented by inflows of non-concessional “other official finance” (OOF) from international development banks. In recent years, the EU has provided almost half of total foreign aid to the region as part of its pre-accession process, supporting a large effort of institutional reform in the candidate countries motivated through a carrot and stick approach. The carrot has been eventual EU membership backed up by an enormous inflow of technical and financial assistance, while the stick has been the threat of delay in opening and conducting accession negotiations, and withdrawing or reducing assistance programmes. Progress with meeting the EU conditions for membership has been closely monitored, providing a signal for varying the speed of accession. This process has been extensively studied in the literature on EU enlargement. Schimmelfennig and Sedelmeier (2004) identified an “external incentives” model of enlargement governance under which speedy compliance with EU accession conditionality is rewarded by faster integration, while failure to comply is punished by a slowing down of the accession process. Anastasakis (2008) argued that state weakness in the region was likely to require more rigorous conditionality to avoid the danger of fake compliance which was a likely outcome of the accession process. The debate was extended by Noutcheva (2009, 2012) who identified gradations of compliance with EU conditionality on the part of the accession states: genuine, rationality-based, fake and imposed modes of compliance.² She claimed that the path followed would depend on the perceived legitimacy of the EU conditionality and reform requirements. In view of these considerations, the EU has reinforced its conditionality requirements by requiring accession states to draw up Economic Reform Programmes, which set out agreed policies for macroeconomic stabilisation and structural reforms. It also supports the required reforms through its financial and technical assistance programmes, which are the focus of this paper.

Yet, despite this assistance, the candidate and potential candidate countries of the Western Balkans are not yet judged to be functioning market economies (European Commission, 2019). Their political economies are based upon close interlinkages between political and economic elites, with leading parties achieving power on the basis of widespread clientelism and strong influence over mainstream media outlets, all of which have led to the widespread phenomenon of state capture as an entrenched characteristic of the political economy of the Western Balkans (Keil, 2018). State capture has been linked to the reversal of democratic reforms that has taken place over recent years, and a reversion

¹ Source: OECD International Development Statistics database; see Table 1 below.

² Genuine compliance is a form of social learning in which accession states internalise EU norms and wish to undertake reforms on their own behalf because they see them as valuable policy orientations in themselves. Rationality-based compliance reflects the external incentives model, in which accession states do not internalise EU norms but comply with them so long as they see positive net benefits in doing so. Fake compliance reflects a situation in which accession states tick the boxes and meet the formal conditions set down but fail to implement the policies in an effective way. Imposed compliance concerns the case of semi-protectorates such as Kosovo where the EU has extensive influence over the reform process.

to more authoritarian modes of governance (Bieber, 2020; Lavrič and Bieber, 2020; Stojarova, 2020; Pavlović, 2019). The phenomenon of state capture has gone hand in hand with the processes of political backsliding, the emergence of competitive authoritarianism as a defining feature of the political culture (Bieber, 2018) and the emergence of illiberal democracy as a zeitgeist in the region, reflecting and to some extent leading broader trends within Europe (Kapidžić, 2020). The justice systems lack effective independence (Gomes, 2017) and the media have become less and less independent of political influence (Kmezić, 2020). Alongside its 2018 Enlargement Strategy, the Commission recognized that state capture has become a widespread phenomenon in the region. It claimed that

“...the investment climate continues to be hampered by signs of state capture, in particular as regards the lack of independent and efficient court systems and the uneven enforcement of competition rules. State influence in the economy is strong in the region, exacerbating the risk of corruption through weak public financial management and frequent changes in permits and taxes.” (EC 2018: 6).

Corruption and clientelism have become systematic strategies adopted by political elites in captured states in the region (Sotiropoulos, 2018). Typical corrupt practices include offering plum contracts to favoured companies who give kickbacks to the dominant party in power, and the placement of party loyalists in prime positions in state agencies and public enterprises at both national and local level. The practice of clientelism involves the provision of resources in the form of jobs and favourable access to credit to party members or supporters or, as mentioned above, welfare payments to favoured groups of supporters of the ruling party. The numerous examples of clientelism and its systematic use by ruling parties to attract votes and retain a hold on power have been well documented in the cases of Serbia and Kosovo by Cvejić (2016a, 2016b). Political elites engage in rent-seeking activities as a result of which public procurement is riddled with corrupt practices, and large politically-connected companies maintain quasi-monopoly positions, stifling entrepreneurial start-ups, innovation, and the growth of small businesses (Bartlett, 2012). As Stefano Bianchini observed “the [EU] aid strategy has failed” (Bianchini, 2014: 360).

What has gone wrong? It is the contention of this paper that the EU and international assistance itself has itself been a major factor in explaining the lack of progress with democratisation and economic development of the region. Instead of promoting productive entrepreneurship, donor programmes have enabled rent-seeking elites to support unproductive or destructive entrepreneurship³; in the field of public expenditure, they have turned a blind eye and facilitated corrupt practices around public procurement; in the field of democratisation, the EU has in practice allocated relatively small proportion of funds to promoting good governance (Grimm and Mathis, 2015). I argue that international assistance has suffered from the moral hazard effect known as the “Samaritan’s dilemma” (Gibson et al. 2005). This posits that the provision of aid to countries governed by rent-seeking elites simply perpetuates elite rent-seeking behaviour. The Samaritan’s dilemma is whether to withdraw aid if recipient governments fail to follow a donor’s recommended policy reforms, or to

³ I use these terms in the sense of Baumol (1990).

continue supplying aid conditional on the implementation of reforms despite the likelihood that this may weaken fiscal constraints on rent-seeking behaviour.

In section 2, I analyse the dimensions of donor assistance, setting out the empirical data on EU and bilateral donor activities in the region. In section 3, I analyse the distribution of international aid by donors and recipients and identify the patterns of donor assistance. In section 4, I analyse whether EU and other international development assistance has promoted good governance or instead facilitated rent-seeking behaviour in the Western Balkans. In section 5, I draw some conclusions from the analysis.

2. The contours of international assistance in the Western Balkans

In addition to control over the accession policy agenda and its timing, the main instrument in the EU's arsenal to manipulate accession states' compliance is the enormous programme of financial and technical assistance, known as the Instrument for Pre-Accession (IPA). Through this instrument the EU has become the largest provider of donor-funded assistance to the Western Balkans. EU financial and technical assistance is a key element of the external incentives approach to enlargement, but one that has been the subject of little research scrutiny.

Over the last thirty years the EU approach to the countries of the Western Balkans has gone through at least three identifiable phases. In the 1990s, the EU was preoccupied with the transition and subsequent accession of the countries of Central and Eastern Europe and failed to engage successfully with the countries of South East Europe which were riven by war and conflicts (Lavdas, 1996; Dover, 2005). The second phase of engagement followed the Kosovo war of 1999, following which the EU became more focused on the region, developing a Stabilisation and Association Process in 1999 which led to the negotiation of a set of Stabilisation and Association Agreements (SAAs) with the countries of the region (Bartlett and Samardžija, 2000). This ushered in a second phase of enlargement based on "member-state building" (Keil, 2013) in which the EU began to support widespread institutional change to prepare the candidate and prospective candidate countries for eventual EU membership, an ambition that was set out by the European Council in the Thessaloniki Declaration of 2003. Based on the concept of external incentives, the EU conditioned its assistance on progress with democratisation, rule of law, control of corruption, and "good" economic development policies based around privatisation, economic liberalism and control of government budget deficits and public debt (Huliaras, 2011).

The third phase of EU engagement followed the global financial crisis of 2008 and the subsequent eurozone crisis beginning in 2009 which caused a fundamental rethink of enlargement policy. This phase was informed by growing "enlargement fatigue" among the EU member states, involving scepticism towards further enlargement of the EU (O'Brennan, 2014). Reflecting this development, the EU Enlargement Strategy was fundamentally changed in 2015 by introducing tougher conditionality and through a renewed emphasis on fundamental reforms in the rule of law, democracy

and economic governance (Dimitrova, 2016). This raised the costs of compliance while at the same time reducing the credibility of the incentive of eventual EU membership (Schimmelfennig and Sedelmeier, 2019). Through this new approach the EU Commission aimed to synchronise its state building activities with the EU enlargement policy agenda. It involved a steep increase in the financial assistance provided by the EU Institutions just as bilateral assistance from the EU member states began to diminish.

Donor assistance did not really get off the ground in the former Yugoslavia until after the end of the first phase of the wars of Yugoslav succession in 1995.⁴ EU assistance began with the PHARE programme, succeeded by the CARDS programme, and then the IPA and IPA-II assistance programmes.⁵ The focus of these programmes has been on institutional reform, while economic development actions have been left largely to the World Bank and budgetary assistance to the IMF. Numerous bilateral donors, some of whom are EU member states, have also been involved in providing aid to the Western Balkans. More recently, several “new actors” have entered the region with their own financial and technical assistance programmes (Bieber and Tzifakis, 2019).

Official Development Assistance (ODA) is provided by many different donors, including the EU Institutions, individual countries, and multilateral agencies.⁶ The EU Institutions include grants from the pre-accession assistance programmes as well as concessional loans from the European Investment Bank (EIB), which provides infrastructure investment in transport and other sectors. The individual donor countries are “bilateral donors”, both EU member states and non-EU member states. The bilateral donor group can also be broken down into those who are members of the OECD’s Development Assistance Committee (DAC) which sets certain standards for the provision of aid, and aid-providing countries from outside this club. The DAC donors include both EU member states and others, principally the USA, Switzerland, Norway and Japan. Finally, there are the multilateral agencies, the largest of which are the World Banks’ International Development Association, the Organisation for Security and Cooperation in Europe (OSCE), the Council of Europe Development Bank and the Global Fund.

The total ODA flowing to the Western Balkans has varied over time in response to specific crises. In the 1990s, the DAC bilateral donors were responsible for most aid disbursements to the region (see Figure 1). Immediately after the Kosovo war of 1999 the flow of aid increased dramatically, reaching \$4.5 billion in 2002 (in 2017 prices). Contributions from the EU Institutions peaked at this time, briefly exceeding the contributions from EU bilateral agencies. Total donor involvement declined after 2002

⁴ Substantial assistance was provided to Albania in the early 1990s at the start of the transition process.

⁵ Going forward, the European Commission has proposed merging IPA into a single instrument for global external assistance to be known as the Neighbourhood, Development and International Cooperation Instrument (NDICI) in the next Multi-annual Financial Framework budget for 2021-2028.

See: https://eeas.europa.eu/sites/eeas/files/eu_global_strategy_2019.pdf

⁶ In the account that follows, the contributions of IMF loans are excluded, since although they are often concessional, they amount to general budget support which responds to different drivers than conventional ODA flows, i.e. to balance of payments difficulties rather than to pre-accession needs or developmental aims.

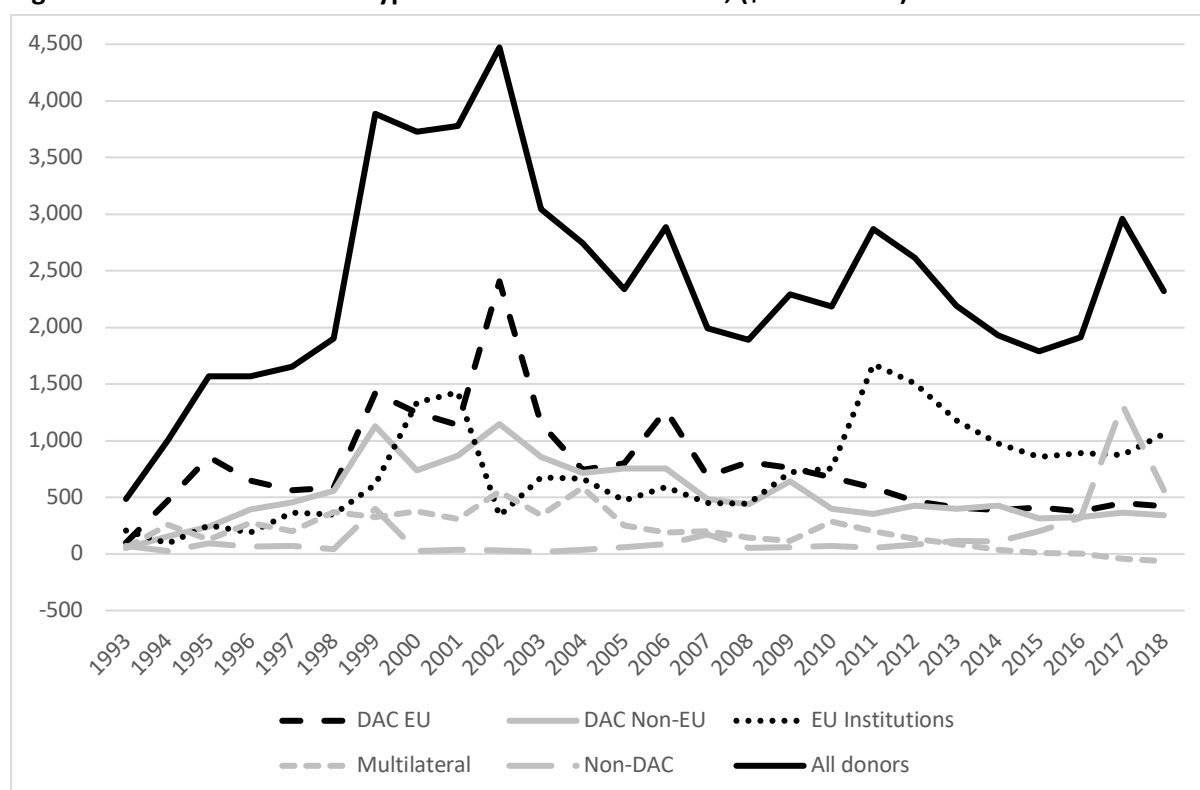
until the onset of the global financial and eurozone crises which hit the region hard. In response, total aid increased once again, reaching \$2.9 billion in 2011. Since then, the DAC bilateral donors have steadily reduced their contributions as they too were badly affected by the economic crisis, while the contributions from the EU Institutions have taken the leading role.

The main increase in contributions after 2008 came from the EU Institutions, both in response to the economic crisis and following the launch of the IPA programme in 2007. The IPA II programme, which ran from 2014-2020, targeted reforms on a sectoral basis covering specific areas set out in the EU Enlargement Strategy, including democracy and governance, rule of law, and economic growth and competitiveness. The sector approach aimed to promote structural reform in each sector alongside a more systematic use of sector budget support. As an instrument of EU foreign policy, the accession funds must comply with the general principles of the EU common aid policy set out in the EU Code of Conduct on Complementarity and Division of Labour in Development Policy. This aims to achieve harmonisation among donor activities by overcoming donor fragmentation and increasing the effectiveness of assistance. The IPA II Regulation follows these principles.⁷

The multilateral agencies briefly increased their contribution in 2010 before drawing down their presence until their net contribution became negative after 2016 as repayment of previous concessional loans exceeded new inflows. From 2016, the non-DAC donors became more involved and in 2017 briefly became the largest donor group with a \$1 billion concessional loan from UAE to Serbia. They are now the second largest donor group, at a level similar to that of the DAC-EU and DAC non-EU bilateral donors, generating a widespread concern about the influence of these new actors in the Western Balkans (Bieber and Tzifakis, 2019).

⁷ Article 5.4 states that “The Commission and the Member States and the EIB shall ensure coordination of their respective assistance programmes to increase effectiveness and efficiency in the delivery of assistance ... in line with established principles for strengthening operational coordination in the field of external assistance ... in particular the international principles on aid effectiveness”. Article 5.5 further states that “In order to increase the effectiveness and efficiency in the delivery of assistance ... the Commission, in liaison with the Member States, shall take the necessary steps to ensure better coordination and complementarity with multilateral and regional organisations and entities, such as international financial institutions, United Nations agencies, funds and programmes, and non-Union donors”.

Figure 1: ODA from all donor types to the Western Balkans, (\$m constant)



Source: OECD International Development Statistics database.

In summary, for the first two decades of transition up to the onset of the global financial crisis, DAC bilateral donors contributed over three fifths of total ODA funding; in the post- crisis period from 2009 to 2018 their contribution fell to under two fifths of total ODA (see Table 1). Correspondingly, after the crisis, the contribution from the EU institutions rose significantly to almost one half of total ODA to the region, the share of non-DAC bilateral donors rose to more than one tenth, while the contribution of the multilateral agencies became relatively trivial.

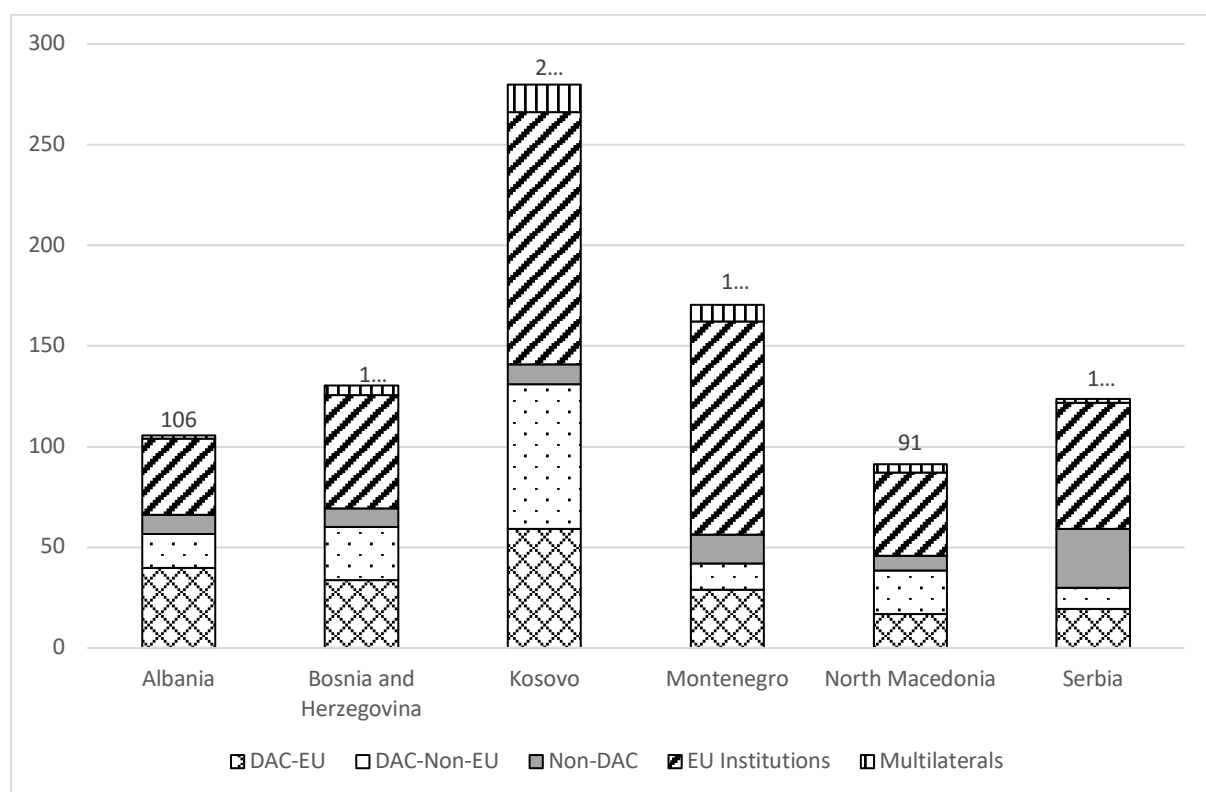
Table 1: ODA to the Western Balkans and shares of donor groupings by time periods

| | 1993-1999 | 2000-2008 | 2009-2018 | 1993-2018 |
|-----------------------|-----------|-----------|-----------|-----------|
| EU Institutions | 17.1% | 23.8% | 45.5% | 30.6% |
| DAC EU | 38.4% | 38.1% | 21.4% | 32.0% |
| DAC Non-EU | 24.7% | 25.2% | 17.3% | 22.1% |
| Non-DAC | 6.4% | 1.9% | 12.5% | 6.7% |
| Multilateral agencies | 13.3% | 11.0% | 3.3% | 8.6% |
| All donors | 100.0% | 100.0% | 100.0% | 100.0% |
| Total (\$bn) | 12.1 | 26.9 | 23.1 | 62.0 |
| Annual average (\$bn) | 1.8 | 3.1 | 2.5 | 2.3 |

Source: OECD International Development Statistics database.

International assistance has made a considerable contribution to the economies of the region. Over the whole period from 1993-2018, the Western Balkan countries received an inflow of ODA equivalent to an (unweighted) average of 4.2% of their GNI. This varied from a massive 10.9% of GNI in the case of Bosnia and Herzegovina, to a more modest 1.2% of GNI in the case of Montenegro. The contribution of international aid has gradually fallen over time from 6.4% of GNI in 1993-1999 to 3.1% between 2009-2018. In the former period, international assistance contributed 26.7% to the GNI of Bosnia and Herzegovina reflecting the huge reconstruction needs of the country. In the period 2000-2008, Serbia attracted a large inflow of ODA amounting to 6.9% of its GNI. In its post-independence period from 2009-2018, Kosovo has been highly reliant on inflows of international assistance, equivalent to 7.5% of its GNI.

Figure 2: ODA per capita by type of donor, \$, average 2009-2018



Source: OECD International Development Statistics database.

Equivalently, ODA per capita from the donors has been relatively generous. In Bosnia and Herzegovina, average ODA per capita over the entire period from 1993-2018 amounted to \$148 (in current prices), with the greatest disbursement in the period following the end of the Bosnian war in 1995 (the average over the period 1993-1999 reached \$187 per capita). Figure 2 shows that during the post-crisis period from 2009-2018, Kosovo received the most ODA per capita from all donors, equivalent to about \$280 per annum, due to its high needs for donor assistance following its unilateral declaration of independence in 2008. This was followed by Montenegro due to its status as a leader in the region in the accession process, as the opening of negotiations for EU membership triggered a large inflow

of EU funds. The other four countries have received relatively lower, but still substantial, amounts of ODA per capita over this more recent period.

3. Distribution of donor assistance across the region

Donor proliferation, defined as a multiplicity of donors in a beneficiary country, has been a concern to policy makers. Following the agreed principles of international aid set out in several international declarations,⁸ the EU Code of Conduct adopted in 2007 emphasised the potentially negative effects of donor proliferation, and the importance of donor coordination and donor complementarity.⁹ The Code recommends that donors should designate a limited number of countries of intervention. Overcrowding of donors in a country is thought to have a number of negative effects on aid effectiveness by imposing significant administrative burdens and high transaction costs on the recipient countries, diffusing policy dialogue, reducing transparency and increasing the risk of corruption.

These issues have been explored in a number of studies of international aid effectiveness. For example, Djankov et al. (2009) demonstrated that the presence of multiple donors makes aid less effective, while Anderson (2012) identified the high donor transaction costs resulting from the fragmentation of bilateral aid across recipient countries. Donor proliferation may also lead to higher transaction costs for aid recipients due to competition between donors for skilled personnel, poaching of skilled personnel from government agencies and ministries, and the tendency of some donors to indulge in excessive amounts of training (Acharya et al., 2006; Kilby, 2011). Donor proliferation and fragmentation is also visible in the Western Balkans, as demonstrated in this section.

Table 2: Recipient aid shares by donor (2009-2018)

| <i>Donor</i> | Albania | Bosnia and Herzegovina | Kosovo | Montenegro | North Macedonia | Serbia | Western Balkans |
|--------------------------------|----------------|-------------------------------|---------------|-------------------|------------------------|---------------|------------------------|
| <i>EU Institutions</i> | 36.6% | 42.7% | 43.7% | 62.7% | 45.4% | 49.6% | 45.7% |
| <i>EU bilateral donors</i> | | | | | | | |
| <i>Germany</i> | 13.3% | 7.9% | 7.5% | 8.2% | 9.1% | 9.7% | 9.2% |
| <i>Sweden</i> | 3.7% | 5.3% | 3.5% | 0.6% | 1.5% | 1.8% | 3.0% |
| <i>Austria</i> | 3.2% | 5.5% | 2.4% | 1.4% | 1.4% | 1.4% | 2.6% |
| <i>Italy</i> | 8.1% | 0.8% | 0.3% | 1.2% | -0.2% | -0.3% | 1.1% |
| <i>Greece</i> | 6.0% | 0.1% | 0.6% | 0.2% | 0.2% | 0.3% | 1.0% |
| <i>Non-EU bilateral donors</i> | | | | | | | |
| <i>United States</i> | 8.5% | 9.7% | 15.3% | 5.1% | 13.1% | 4.3% | 8.8% |
| <i>Switzerland</i> | 6.5% | 5.2% | 9.2% | 0.1% | 8.1% | 2.2% | 5.1% |
| <i>Norway</i> | 0.4% | 2.3% | 2.2% | 1.7% | 2.1% | 1.1% | 1.6% |

⁸ These stem from the Paris Declaration on Aid Effectiveness (2005) and the Accra Agenda for Action (2008), see: <https://www.oecd.org/dac/effectiveness/parisdeclarationandaccraagendaforaction.htm>

⁹ The EU Code of Conduct on Complementarity and the Division of Labour in Development Policy is available at: http://europa.eu/legislation_summaries/development/general_development_framework/r13003_en.htm

| | | | | | | | |
|---|------|------|------|------|------|-------|-------|
| Japan | 2.4% | 2.4% | 0.6% | 1.0% | 1.4% | 1.2% | 1.4% |
| <i>Non-DAC bilateral donors and multilateral agencies</i> | | | | | | | |
| Non-DAC | 8.8% | 6.4% | 3.1% | 7.7% | 7.1% | 24.3% | 12.6% |
| OSCE | 1.0% | 2.8% | 4.0% | 2.0% | 3.6% | 0.8% | 2.1% |
| Other | 1.4% | 8.8% | 7.8% | 8.3% | 7.1% | 3.7% | 5.7% |
| Total | 100% | 100% | 100% | 100% | 100% | 100% | 100% |

Source: OECD International Development Statistics database. The flows reported cover 95% of all ODA flows to the Western Balkans. Note: Highlighted percentages are more than 5 percentage points above each donor's average ODA share to all recipients (last column). Data are based on net disbursements in constant dollars over the period 2009-2018.

From the recipient perspective, while international assistance from the EU Institutions has been the major source of ODA to the Western Balkans providing almost half of the total from 2009-2018, recipients have attracted aid from many other donors including Germany, which provided 9.2% of total ODA and the USA, which provided 8.8% (see Table 2). Despite attempts at aid coordination, especially among the EU Institutions and EU bilateral donors, the proliferation of donors has enabled aid recipients to cherry pick the best offers from a variety of donors. Recently, recipients have attracted new international actors from outside the DAC club, including China, Russia, Turkey, the UAE and others. With the entry of these donors, aid recipients have a viable alternative source of assistance that is not subject to EU conditionality and which has had the effect of undermining the soft power influence of the EU in the region.

Comparing aid flows from specific donors across recipients (the horizontal rows in Table 2) it can be seen that some recipients have been favoured by a greater proportion of ODA inflow than others (indicated by highlighted cells). Thus, Albania is a favoured recipient of aid from Italy and Greece, reflecting historical ties and current trade relationships, while Kosovo is a favoured recipient of the USA reflecting its continuing foreign policy linkage to that donor. The EU Institutions have favoured Montenegro due to its leading position in the EU accession process. The non-DAC donors have favoured Serbia, providing double the average share of aid that they provide to the Western Balkan countries as a whole.

Table 3: Donor aid shares by recipient (2009-2018)

| Donor | Albani a | Bosnia and Herzegovi na | Kosov o | Monteneg ro | North Macedon ia | Serbi a | All recipien ts | SD |
|---|-------------|-------------------------------|------------|----------------|------------------------|------------|-----------------------|-----------|
| EU Institution s | 9.7% | 17.5% | 19.9% | 5.9% | 7.7% | 39.3 % | 100.0% | 12.4 % |
| EU bilateral donors | | | | | | | | |
| Germany | 17.5% | 16.1% | 16.9% | 3.8% | 7.7% | 37.9 % | 100.0% | 11.8 % |
| Sweden | 15.3% | 33.7% | 24.1% | 0.8% | 3.8% | 22.3 % | 100.0% | 12.6 % |
| Austria | 15.1% | 40.0% | 19.3% | 2.3% | 4.3% | 19.1 % | 100.0% | 13.5 % |
| Greece | 73.2% | 1.9% | 11.6% | 0.8% | 1.8% | 10.7 % | 100.0% | 28.1 % |
| Italy | 87.2% | 13.5% | 4.7% | 4.5% | -1.2% | -8.8% | 100.0% | 35.3 % |
| Non-EU bilateral donors | | | | | | | | |
| United States | 11.7% | 20.7% | 36.0% | 2.5% | 11.5% | 17.7 % | 100.0% | 11.3 % |
| Norway | 3.2% | 27.4% | 28.7% | 4.6% | 10.3% | 25.8 % | 100.0% | 11.9 % |
| Switzerlan d | 15.6% | 19.0% | 37.3% | 0.1% | 12.4% | 15.5 % | 100.0% | 12.1 % |
| Japan | 20.6% | 31.4% | 8.0% | 3.1% | 7.6% | 29.3 % | 100.0% | 12.1 % |
| Non-DAC bilateral donors and multilateral agencies | | | | | | | | |
| Non-DAC | 8.5% | 9.5% | 5.1% | 2.6% | 4.4% | 69.9 % | 100.0% | 26.2 % |
| OSCE | 5.8% | 25.0% | 38.7% | 4.1% | 13.1% | 13.2 % | 100.0% | 13.1 % |
| All donors | 12.2% | 18.8% | 20.8% | 4.3% | 7.8% | 36.2 % | 100.0% | 11.4 % |

Source: OECD International Development Statistics database. The flows reported cover 95% of all ODA flows to the Western Balkans. Note: Highlighted cells show cases where donor ODA shares to a specific recipient country are more than 10 percentage points above the recipient share of all donor ODA (bottom row). SD=Standard deviation. Data are based on net disbursements in constant dollars over the period 2009-2018.

From the donor perspective, Table 3 shows the percentage variation of each donor's ODA flow across recipients. The final column shows the standard deviation (SD); a lower SD reflects a more equally spread distribution of a donor's ODA across recipient countries. Among the EU member state donors, only Germany has aligned its pattern of assistance with that of the EU Institutions; other donors have adopted a less even-handed distribution of assistance across recipients. Non-DAC donors, and smaller donors such as Greece and Italy have the least balanced spread of ODA across beneficiaries, having at

least one recipient to which they allocated aid at a level more than 10 percentage points above the average share of ODA by recipient (indicated by highlighted cells of the Table).

A pattern of specialisation emerges in which most donors focus their efforts on particular recipient countries. Each donor brings to the table its own specific interests and policy concerns. As noted by Ker-Lindsay et al. (2017) EU member states have a variety of motivations to support or resist enlargement towards the Western Balkans, including support for traditional allies, promotion of commercial advantage, or concerns over migration. These motivations are reflected in the distribution of international aid by individual donors across recipient countries. Greece and Italy focus their ODA on Albania for mainly historical and geographical reasons. Austria focuses on Bosnia and Herzegovina due to its strong links as the former colonial ruler; Sweden and Japan also focus their efforts on that country. Switzerland and the USA have championed Kosovo, for reasons mentioned above. The new non-DAC donors have focused their attention largely on Serbia; they generally appear to have less concern for recipient needs than the traditional donors (Dreher, et al., 2011; Bieber and Tzifakis, 2019).¹⁰ It is noticeable that Montenegro and North Macedonia lack specific donor champions. Although there has been some degree of specialisation by donors in the Western Balkans, this seems to have been led more by foreign policy considerations of donors rather than by a serious attempt at donor coordination aimed at reducing the administrative burden on beneficiaries or to coordinate around the priorities of the EU Institutions, let alone by the domestic needs of the recipients.

Overall, there is strong evidence of donor proliferation in the Western Balkans. While some donors are relatively even-handed, the data demonstrate that several donors allocate aid on a basis of foreign policy considerations and are less than even-handed across the beneficiary countries. In addition, a range of new and emerging donors are increasingly active in the region with more relaxed conditionality than the EU Institutions or bilateral donors that support the EU Enlargement process. There is a risk that these new donors may reduce the effectiveness and “transformative power” of EU conditionality. Yet there is an even stronger threat to the EU’s transformative power that derives from the activities of the donor community as a whole, and the way in which international assistance interacts with the evolution of domestic political cultures. As will be shown in the next section, this relates to the development of what has come to be called the “state capture” of the regional political economies, and the role of international assistance in facilitating this process.

4. International aid and state capture in the Western Balkans

In the 1990s a number of studies questioned the beneficial impact of international assistance in poor countries. They appeared to show that there was little relationship between inflows of aid and economic growth of a country (Boone, 1996). The explanation was that aid flows were being used for consumption, rather than being channelled into productive investment. Burnside and Dollar (2000) argued that aid is less effective when governance is weak, and so should be targeted to countries with

¹⁰ On the motives for Chinese aid flows see Woods (2008).

a record of “good governance”. They proposed that aid has a positive effect on growth in countries with “good” fiscal, monetary and trade policies. However, good policies are not necessarily an exogenous factor, as policies can themselves be influenced by aid flows, and there may be a causality between aid and the quality of governance. Svensson (2000) argued forcefully that aid diminishes the pressure on governments to reduce wasteful public spending from their own revenues, and may also facilitate rent-seeking behaviour by politicians who are able to use public funds to maintain their positions of power through clientelistic practices. A study by Knack (2001) provided evidence that higher levels of aid erode the quality of governance, as measured by indices of bureaucratic quality, corruption, and the rule of law. Combined with evidence that more corrupt governments receive more foreign aid (Alesina and Weder, 2002) this implies a negative feedback loop between aid and governance. In empirically investigating such effects in a sample of over one hundred countries, Djankov et al. (2008) provided support for the existence of such effects, finding that that foreign aid has an overall negative impact on political institutions. On the other hand, Jones and Tarp (2016) provided contrary evidence that aid does not have a systematic negative effect on political institutions, while others find no significant relationship between aid and corruption (Tavares, 2003; Menard and Weill, 2016). In relation specifically to EU assistance, in the case of the Czech Republic, Fazekas and King (2019) found a strong relationship between aid and corruption, and specifically that EU funds increased corruption risk by up to 34 percent. The negative effects were largely attributable to overly formalistic compliance with EU Funds overriding domestic accountability mechanisms in public organisations.

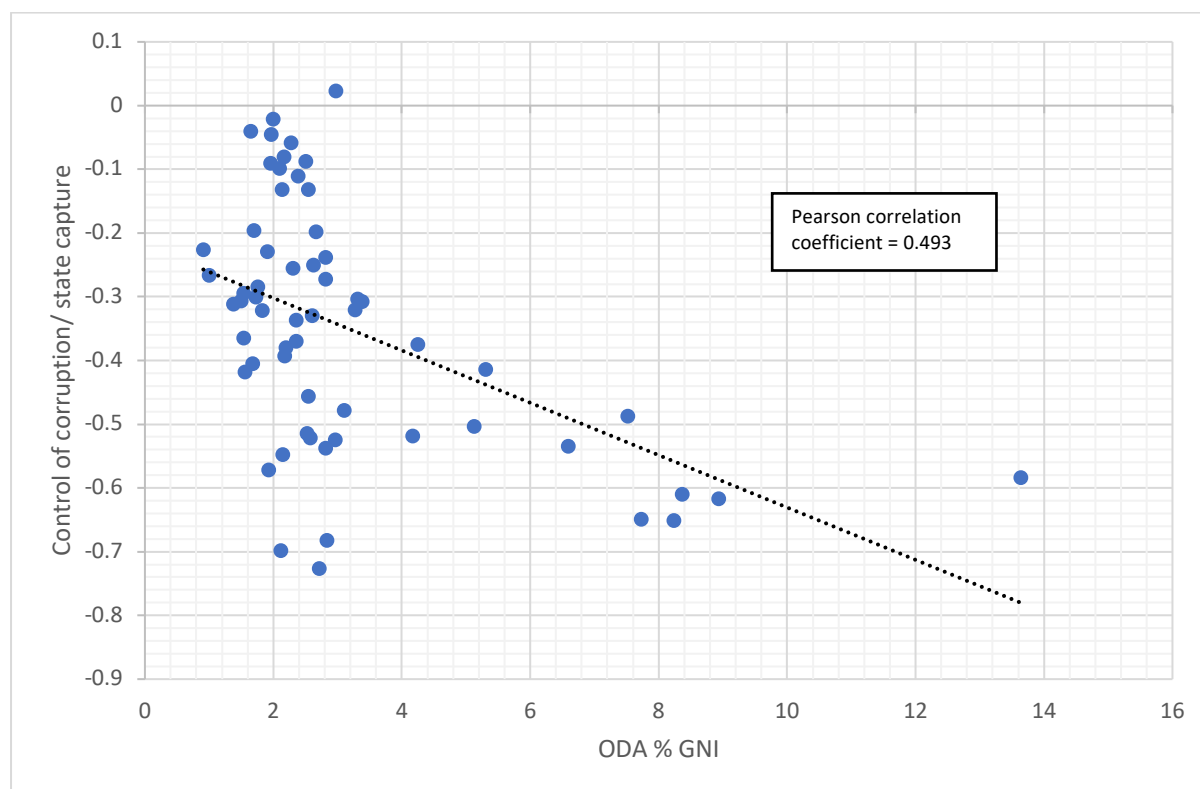
The debate on aid effectiveness raises concerns that international aid to the Western Balkans may be implicated in the development of more authoritarian modes of governance, and may support rather than diminish rent-seeking behaviour by ruling elites. As argued by Richter and Wunsch (2019: 51) “the prevalence of clientelism [in the Western Balkans] suggests that external funding serves as a displacement, freeing up local sources to nurture informal networks.” As elsewhere, aid flows may be used to support unproductive consumption by ruling elites and may facilitate rather than suppress corrupt and clientelistic practices. By directly or indirectly funding established elites, inflows of international assistance may facilitate the process of state capture rather than foster democratic consolidation.

In order to examine the relationship between international aid and state capture, I make use of the World Governance Indicators dataset produced by the World Bank. This has a variable “control of corruption” which measures the strength of public governance and reflects “perceptions of the extent to which public power is exercised for private gain, including both petty and grand forms of corruption, as well as “capture” of the state by elites and private interests”. This therefore seems ideally suited to an examination of the relationship between state capture and the flow of international aid to the region. It is a continuous variable which has a range from -2.5 (weak governance performance) to +2.5

(strong governance performance). It summarises the views on the quality of governance provided by numerous enterprise, citizen and expert survey respondents.¹¹

Based on this data, Figure 3 shows the negative relationship between the share of ODA as a proportion of GNI of the recipient countries and the WGI control of corruption variable. The correlation coefficient between the two variables over the period 2009-2018 is -0.493 (statistically significant at the 1% level); equivalently this can be interpreted as a positive relationship between the flow of international assistance and the extent of state capture. There is a similarly significant negative correlation between the flow of international ODA in per capita terms and the control of corruption variable of -0.301 (significant at the 5% level). For aid flows from EU Institutions alone, the correlation coefficient between recipient ODA/GNI and the control of corruption variable is -0.320, lower than the overall correlation but still substantial and significant at the 5% level, while for all donors other than EU Institutions the correlation coefficient is -0.566 (significant at 1%). This suggests that ODA flows, rather than supporting the adoption of EU norms in the region may actually contribute to the ability of ruling elites to sidestep such norms and the EU accession conditionalities relating to them.

Figure 3: Flow of international aid (ODA) and state capture in the Western Balkans



Source: OECD International Development Statistics database and WGI online database. Data cover the period from 2009-2018.

¹¹ The data are gathered from a number of survey institutes, think tanks, non-governmental organizations, international organizations, and private sector firms.

Of course, correlation does not imply causation, and it may equally be the case that there is some other intervening variable that is driving the flow of ODA. One obvious candidate for such an intervening variable is the level of development, proxied by GDP per capita, i.e. donor countries can be expected to allocate a larger flow of international assistance to countries with lower levels of development. In this I follow the work of scholars who have examined the determinants of the allocation of international aid, such as Dollar and Levin (2006). The key question is whether aid is allocated according to recipient “needs” and “merit”, or donor self-interest. Recipient needs are often proxied by a measure of the level of development, while recipient merit is often proxied by a measure of adherence to principles of good governance such as control over corruption (Hoeffler and Outram, 2011). As shown above, the “merit” aspect of recipient governance performance has become an increasing concern of donors, especially the EU through its accession conditionality. We might therefore expect that donors would reward countries with better governance processes and especially with greater control of corruption and a lower level of state capture than others, by allocating a greater flow of aid to them. If this effect is present, we should expect to find a positive relationship between the allocation of aid and merit as proxied by the WGI control of corruption index. On the other hand, if international assistance facilitates the adoption of rent-seeking strategies and state capture by ruling elites we would expect to find a negative relationship between the allocation of aid and the control of corruption (a proxy for control over state capture and rent-seeking).

Donor self-interest is often measured by the strength of the economic relationship between donor and recipient. One such measure is the trade openness of recipients, on the grounds that more open recipient countries are more likely to engage in trade with donors, which may in turn incentivise aid allocation to recipients. For example, Frot et al. (2014) found that trade flows were a predictor of aid allocation by donors to the early transition countries of the CIS and Central and Eastern Europe in the 1990s.¹² Among OECD countries, donor aid allocations have been shown to reflect trade flows to recipient countries (Younas, 2008). Both general trade openness and the specific direction of trade may influence the flow of ODA from donor to recipient. Furthermore, in the context of the enlargement process, the status of countries as either candidates or potential candidates may be expected to influence aid flows. This variable will be both place and time specific as countries of the Western Balkans have become candidates for EU membership at different points in time.

In analysing these channels of causation of donor aid allocation, I perform a panel data regression analysis of the determinants of aid flows over the period from 2009-2018. Not only is this a period for which more comprehensive data are available for the variables of interest, but it also encompasses the post-crisis period following the global financial crisis and the eruption of the Eurozone crisis, and so relates to a period with a more consistent policy regime (i.e. the third phase of EU enlargement policy identified above). This encompasses the period of IPA programme flows, and policy conditionalities that have emphasised the rule of law and the control of corruption as main aims of

¹² For evidence that individual donor’s aid allocations may be driven by trade policies see for example Martinez-Zarzoso et al. (2009)

EU conditionality. The dependent variable is ODA as a proportion of recipient’s Gross National Income (ODA/GNI), which normalises aid flows by the size of the recipient economy.¹³ In the regression model, these aid flows are determined by a set of independent variables including the recipient’s level of development, proxied by its GDP per capita (“GDPpc”). A negative relationship is expected, reflecting a larger allocation of aid flows to less developed countries. Aid flows are also thought to be related to the degree of recipient economic openness as explained above, which is proxied by (half) the sum of exports and imports as a share of recipient GDP (“Openness”). Aid is also thought to be incentivised by specific direction of trade flows such as those between the EU and the Western Balkans, which is represented by the share of Western Balkan imports from the EU (“EU import share”). The flow of aid is also modelled as being sensitive to the EU candidate status of recipients, represented by a dummy variable which takes the value of 1 for years in and after which a recipient become an EU candidate and zero otherwise (“EU candidate”). The key variable of state capture is represented by the WGI indicator for control of corruption (CC). As this is expected to vary across recipients this is interacted with a set of recipient country dummy variables (“[country]*CC”). The independent variables are entered in the regression model with a one-year lag to allow for prior recipient behaviour to influence donor decisions in the current year.

Table 3 sets out the panel data regression model explaining the allocation of ODA by different donor groups. The coefficients on GDP per capita reveal that both DAC bilateral donors, both EU and non-EU, along with the multilateral organisations allocate aid, at least in part, according to recipient need. Somewhat surprisingly the EU Institutions do not follow this pattern and tend to allocate more aid to less needy recipients. This is likely due to the inclusion of the European Investment Bank among the EU institutions. This organisation provides commercial loans with a grant element, and these may be more likely to be affordable by the more developed and more prosperous recipients. The non-DAC donors, sometimes referred to as “new actors”, are shown not to allocate their aid on the basis of recipient level of development (since their coefficient on GDP per capita is statistically insignificant).

Table 2: Determinants of aid allocation by donor group

| Dependent variable ODA/GNI (%) | DAC EU bilateral donors (e.g. Germany, Austria, Sweden, Italy) | DAC Non-EU bilateral donors (e.g. USA, Norway, Switzerland) | Non-DAC bilateral donors (e.g. UAE, Russia, China, Turkey) | EU Institutions (e.g. EU aid programmes, European Investment Bank) | Multilateral organisations (e.g. regional development banks, UN organisations) |
|---|---|--|---|---|---|
| GDPpc | -0.0008*** (-6.45) | -0.0001* (-1.63) | -0.0001 (-0.61) | 0.0004* (1.75) | -0.0001** (-2.52) |
| Openness | 0.0259*** (3.05) | 0.004 (0.48) | 0.039** (2.57) | -0.027 (-1.16) | 0.006** (2.53) |
| EU import share | -0.000 (-0.00) | 0.001 (0.08) | -0.021 (-0.85) | 0.027 (0.71) | 0.005 (1.29) |
| EU candidate | -0.168 | 0.109 | 0.212 | -0.317 | -0.140*** |

¹³ An alternative would be to specify the dependent variable as ODA per capita, which would normalise by the population size; doing this yields similar results. The adopted approach is more relevant as ODA is a financial flow.

| | | | | | |
|--------------------|---------------------|----------------------|----------------------|----------------------|-------------------|
| | (-1.53) | (1.00) | (1.05) | (-1.01) | (-4.24) |
| AL*CC | 1.338** (2.36) | -0.185 (-0.65) | -1.227** (-2.32) | 1.226 (1.50) | 0.103 (1.20) |
| Bosnia*CC | -1.966** (-2.41) | -0.997** (-2.27) | -1.466* (-1.80) | 1.915 (1.52) | 0.034 (0.26) |
| Kosovo*CC | -0.476 (-0.59) | -2.397*** (-4.92) | -0.632 (-0.70) | -4.028*** (-2.88) | -0.106 (-0.72) |
| Montenegro*CC | 1.540 (1.57) | -0.911 (-0.99) | 0.794 (0.46) | 0.827 (0.31) | -4.07 (-0.72) |
| North Macedonia*CC | 0.169 (0.28) | -0.462 (-0.71) | 0.856 (0.71) | 1.448 (0.78) | 0.124 (0.63) |
| Serbia*CC | -1.849 (-1.25) | 0.193 (-0.39) | -2.531*** (-2.74) | 2.573* (1.80) | 0.124 (0.82) |
| Constant | 3.409*** (3.99) | 0.570 (0.60) | -0.365 (-0.21) | -0.642 (-0.24) | 0.571 (1.99) |
| N | 54 | 54 | 54 | 54 | 54 |
| R-squared | 0.3466 | 0.8893 | 0.3067 | 0.7092 | 0.8499 |
| Wald Chi2 | (F) 7.25*** | 345.40*** | 19.2** | 104.84*** | 243.55*** |
| Estimation method | Fixed effects | Random effects | Random effects | Random effects | Random effects |

Source: Data are derived from WGI online database, OECD international aid online database and Eurostat online data. Note: GDP per capita is measured in Euro. Control of corruption ranges from -2.5 (weak control) to +2.5 (strong control). CC= control of corruption; Dummy variables: BA= Bosnia and Herzegovina, XK=Kosovo, ME=Montenegro, MK=North Macedonia, RS=Serbia. Independent variables have a one-year lag. The model is a panel data regression model estimated using the STATA xtreg command using random effects, apart from DAC EU bilateral donors which uses fixed effects. The choice between random effects and fixed effects is taken on the basis of a Hausman specification test. Parentheses show z-statistics for random effects estimation, t-statistics for fixed effects estimation.

As discussed above, some research on international aid effectiveness has suggested that aid allocations follow trade relations. In the Western Balkans, the general level of trade openness is an influential factor in determining aid allocations from both DAC donor groups and the multilateral organisations (positive coefficients - significant at 1% or 5% level). The positive relationships between ODA flows and trade openness could be considered as an indication that donors are interested in rewarding recipients who adopt more liberalising policies in general. However, it is unlikely to be an explanation of the influence of openness of the aid flows of the non-DAC new actors, who may be mainly influenced by the commercial opportunities related to recipient economic openness *per se*. In contrast, there is no evidence of a specifically locational basis to this effect as the coefficients on the share of recipient imports from the EU are all insignificant.

Whether a recipient is formally accepted as a candidate for EU membership is revealed to be only important for the multilateral organisations, for whom there is a negative relationship between aid flows and EU candidacy status. The relationship is strong and significant at the 1% level. This suggests that the multilateral organisations begin to withdraw their international assistance to countries when they become candidates for EU membership, most likely in the expectation that aid from other sources (such as EU Institutions and EU country donors) will increase following achievement of candidate status. However, the lack of any significant observable relationship between ODA flows and

EU membership status from the EU donors demonstrates that unfortunately such an expectation is unfounded. This is somewhat surprising in the case of the EU Institutions and the EU bilateral donors, and may be related to delays between the acceptance of countries as candidates for EU membership and the commencement of real engagement in the EU accession process through the opening and speed of negotiations.

The regression model interacts the control of corruption variable with individual recipient countries. It shows that in six cases control of corruption has a statistically significant inverse relationship with ODA flows, supporting the counterfactual that international assistance facilitates rent-seeking behaviour by political elites; however, there are a couple of exceptions to this general trend. Taking the DAC EU donors first it can be seen that they make different allocation decisions in regard to this variable. For Albania, ODA flows from this donor group respond positively to an improved control of corruption, while the reverse is true for Bosnia and Herzegovina. For the other four recipient countries there is no observable effect on donor allocations in relation to control of corruption.

Secondly, aid allocations from the DAC non-EU donors have a negative relationship with the control of corruption in two cases: Bosnia and Herzegovina, and Kosovo. The effect is especially strong in the latter case. These donors seemingly not only turn a blind eye to state capture in these countries, but positively reward such performance with increased aid flows. This should be interpreted in the context of the aid concentrations of these donors shown in Table 2 and Table 3 above. For example, the USA focuses much of its international assistance in the region on Kosovo, seemingly oblivious to the governance outcomes there. A similar effect is observable for aid flows from the EU Institutions to Kosovo, which bear a similar inverse relationship to control of corruption. This suggests that ODA flows from some donors strongly facilitate rent-seeking behaviour in countries that have been under international protection following periods of severe conflict. This might be expected, since these countries have the weakest governance arrangements and have made least progress with post-conflict member state building (Keil and Arkan, 2015). They are also the only countries in the region that have not as yet become candidate members for EU accession.

Thirdly, international assistance from the non-DAC donors, the new actors, is shown to facilitate state capture and a reduced control of corruption in Albania, Bosnia and Herzegovina, and Serbia, more strongly and more significantly in the latter. The role of the UAE in this respect can be highlighted as its involvement in the development of the Belgrade Waterfront project has been notably intertwined with an increased incidence of state capture, and led to a vocal opposition protest organised around the civil society movement “Ne davimo Beograd” (Bartlett and Prelec, 2018). However, aid allocations from the EU Institutions to Serbia offset this influence to some extent by rewarding contrary trends towards improved control of corruption. The equal and opposite effects of this variable on aid flows to Serbia from the non-DAC donors and the EU Institutions reflects the trade-offs that the Serbian state makes in balancing external incentives from different donor groups. Finally, ODA flows from the multilaterals are neutral with respect to governance performance, as shown by the lack of any

significant coefficients for this group of donors in relation to the control of corruption variable across recipients.

5. Conclusions

Despite the enormous inflow of international assistance to the Western Balkans over the last twenty-five years, the EU member state-building efforts have only been partially successful. None of the countries of the region are considered to be functioning market economies, and great concerns have been raised by both researchers and the European Commission over the problems of state capture, weak governance, poor rule of law and widespread corruption at a high level throughout the region. EU assistance has been conditional on improvements in these governance indicators but has had little success in achieving this aim. From a policy perspective, starting out from a first phase in the 1990s in which EU involvement was relatively insubstantial, a second phase of EU involvement in the 2000s adopted a more hands-on approach based on carrot and stick conditionality to prepare countries for eventual EU membership. The eurozone crisis ushered in a third phase of involvement in the 2010s in which enlargement fatigue was addressed through a toughening of the EU's conditionality and a large increase in international assistance from the EU Institutions. The EU's external incentives were strengthened, to encourage greater compliance from the candidate and potential candidate states in relation to governance issues. At the same time, a range of new actors entered the scene in competition with EU soft power in the region.

These three phases of policy involvement have been mirrored in the patterns of EU and international aid to the Western Balkans. Surges in aid flows have, not surprisingly, followed the end of armed conflicts (in Bosnia and Herzegovina after 1995, in Kosovo after 1999) and the global financial and eurozone crises from 2009 to the present day. The recent increase in the relative importance of EU Institutions and of new providers of international assistance compared to aid from more traditional bilateral donors and multilateral agencies has also been documented. Analysis of the patterns of international assistance in the post-crisis period has shown that although some donors have pursued an even-handed approach across the region, others have pursued self-interested foreign policy aims that favour certain recipient countries over others. At the same time, there is little evidence that donors have followed the international efforts to promote donor coordination. The proliferation of donor assistance has enabled recipient countries to play donors off against each other, weakening the force of EU conditionality and undermining the EU's soft power in the region.

The paper has provided empirical evidence that addresses the question whether international assistance promotes good governance in the region by examining the extent to which donor allocations have been driven by concerns for recipient need and merit, or rather by donor self-interest. The analysis has revealed that donors have allocated more aid to countries that have greater needs as proxied by (lower) levels of GDP per capita, but have largely failed to allocate aid on the basis of merit, as proxied by control over corruption. Neither EU donors nor EU Institutions have applied the "financial stick" as means of motivating adherence to EU norms in candidate and potential candidate

states in the region (with the notable exceptions of DAC EU donors' aid to Albania and EU Institutions' aid to Serbia). This suggests that international aid may have facilitated domestic political elites' practices of rent-seeking and state capture. The analysis has also provided evidence of donor self-interest in so far as aid flows have followed trade openness, and may therefore reflect a pursuit of commercial advantage or ideological orientation rather than altruistic purposes, although this phenomenon has a general nature and is not reflected in geographically directed trade linkages (e.g. trade with the EU). Overall, the analysis suggests that the "Samaritans dilemma" is alive and well in the Western Balkans, and that donors have chosen to mostly overlook poor governance performance among recipients in order to prioritise assistance to the neediest countries and to pursue their own foreign policy concerns.

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