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by Andrew Lawson, David Booth, Alan Harding, David Hoole & Felix Naschold

GENERAL BUDGET SUPPORT EVALUABILITY STUDY
PHASE I

SYNTHESIS REPORT

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DISCLAIMER

This draft Synthesis Report is the work of a joint team from Oxford Policy Management Limited, UK (OPM) and the Overseas Development Institute, UK (ODI). Work has been funded by the UK Department for International Development (DFID), under commission through the Economists' Resource Centre. The team comprises Andrew Lawson (OPM – Project Director), David Booth (ODI), Alan Harding (OPM), David Hoole (OPM) and Felix Naschold (ODI). Task management has been by Joanne Asquith of the DFID Evaluation Department, East Kilbride but, in its present form, the responsibility for any of the opinions expressed in this report rests with the authors alone.

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ABBREVIATIONS

AP	Andhra Pradesh
BoU	Bank of Uganda
DFID	Department for International Development (formerly ODA)
EC	European Commission
ESIP	Economic Sector Investment Programme
EvD	Evaluation Department, DFID
GBS	General Budget Support
GoAP	Government of Andhra Pradesh
GoI	Government of India
GoM	Government of Mozambique
GoU	Government of Uganda
IFI	International Financial Institutions
IMF	International Monetary Fund
JDP	Joint Donor Programme
MAAIF	Ministry of Agriculture, Animal Industry and Fisheries
MFPED	Ministry of Finance, Planning and Economic Development (Uganda)
MoH	Ministry of Health
MTEF	Medium Term Expenditure Framework
MTFF	Medium Term Fiscal Framework
NGO	Non Governmental Organisation
O&M	Operations and Maintenance
ODA	Overseas Development Administration (now DFID)
ODI	Overseas Development Insitute
OPM	Oxford Policy Management
PAF	Poverty Action Fund
PARPA	Action Plan for the Reduction of Absolute Poverty
PEAP	Poverty Eradication Action Plan
PEM	Public Expenditure Management
PER	Public Expenditure Review
PEWG	Poverty Eradication Working Group
PMAU	Poverty Monitoring and Analysis Unit
PRGF	Poverty Reduction and Growth Facility
PRSC	Poverty Reduction Support Credit
PRSP	Poverty Reduction Strategy Paper
PSIA	Poverty and Social Impact Assessment
Sida	Swedish International Development Cooperation Agency
SISTAFE	System for State Financial Administration
SPA	Special Programme for Africa
SWAps	Sector Wide Approaches
SWGs	Sector Working Groups
TA	Technical Assistance
UK	United Kingdom
UPPAP	Uganda Participatory Poverty Assessment Process
WB	World Bank

PREFACE

Each year the Department for International Development (DFID) commissions, through its Evaluation Department, a number of independent evaluation studies. The purpose of DFID's evaluation programme is to examine rigorously the design, implementation and impact of selected policies, programmes and projects, and to record and share the lessons learned from them so that these can be applied to current and future policies and operations.

DFID's Evaluation Department (EvD) is independent of DFID's spending divisions and reports directly to DFID's Director General (Knowledge Sharing). This report represents the views of its authors, a joint team of consultants from Oxford Policy Management and the Overseas Development Institute.

This is an Evaluability Study which develops an Evaluation Framework for General Budget Support drawing on case study materials from Uganda, Mozambique and the Indian State of Andhra Pradesh. As such, it is not a rigorous evaluation and the case studies provide only early indications of lessons learned. The report has been widely discussed under the OECD DAC Evaluation Network and the framework itself has been further refined as a result of this. The final version is being used for a joint global formative evaluation of General Budget Support. DFID leads this process which is due to report in late 2005. The final version of the framework is being published by DFID on behalf of the 20 donors participating in the joint evaluation as DFID (2004) Joint Evaluation of General Budget Support: Evaluation Framework for country level case studies.

The valuable detail of the 3 case studies conducted during the Evaluability Study and the way this experience has influenced the design of the Evaluation Framework is captured in 2 volumes. The first is a syntheses pulling together the framework and including the detailed findings from Uganda. The second details the findings from Mozambique and Andhra Pradesh. We are very grateful to the participation of partner Governments in Uganda, Mozambique and Andhra Pradesh, without whose assistance these studies would not have been possible.

M.A. Hammond
Head, EvD

EXECUTIVE SUMMARY

Introduction

1. This is a report on the study of country experiences of General Budget Support (GBS) commissioned by DFID Evaluation Department (EvD) in October 2001. The exercise was conceived as an 'evaluability study' – an initial enquiry that aims to settle a number of preliminary questions and to help in the design of an eventual programme of joint evaluation or research.

2. The study focuses on claims made about GBS as an aid modality and its suitability, effectiveness and sustainability as a means of channelling international support to poverty reduction. Central issues are:

- the degree to which the theoretical claims about GBS are reflected in the views that donors and recipient Governments have about the purposes of specific GBS programmes
- the extent to which these claims remain plausible in the light of current programme realities.

3. The present report is a synthesis of findings from work undertaken in Uganda, on the Mozambique GBS programme and in Andhra Pradesh (AP), India. It draws most heavily on the Uganda experience, which is longer and better established than the case of Mozambique, while the AP case is taken principally as an instance of GBS in a low-aid-dependency setting.

The Conceptual Framework

4. The study uses a flow chart of a Logical Framework type to capture the main claims that emerge from literature and trends in operational thinking about the superiority of the GBS modality (see Figure 1 on page 13 of the main report). Those arguments reflect progressive disenchantment with the dominance of the project modality, and with the ex ante policy conditionality that characterised previous forms of programme aid. They include the claim that GBS has an immediate positive effect of empowering a Government in its relations with donors, especially compared with projects and traditional programme aid, but also – to a lesser degree – compared with Sector Budget Support or common-basket funding of sector-wide approaches (SWAps) (§§ 20-34).

5. More particularly, the evaluability study tests the logic that GBS has the following advantages compared to other forms of aid:

- **Reduced transaction costs** – countries with a large number of projects and multiple donors each with their own reporting and accounting requirements face high transaction costs in the delivery of aid. In contrast, GBS can be managed and monitored through a single multi-donor process, allowing senior government officials to devote time to policy making, instead of dealing with a large number of individual project missions.

- **Increased allocative efficiency in public spending –** a multitude of projects, donors with different priorities and a residual tendency to tie procurement to their own suppliers, have combined to make the allocation of government expenditures inefficient, particularly but not only when aid flows are 'off-budget'. With GBS, by contrast, the policy dialogue shifts from particular expenditure items towards improving the overall direction and consistency of budget allocations.
- **Greater predictability of aid flows –** problems in fulfilling project and programme disbursement conditions and implementation requirements have made the timing of aid flows unpredictable. GBS, in contrast, is delivered in one (or a few) instalment and is also conceived as involving longer-term commitments from donors to a Government, which can help to improve the predictability of foreign assistance.
- **Increased effectiveness of the state and public administration –** projects have built up extensive project management structures, that tend to bypass the problems in government systems and thereby contribute to their weakness. Conditionality has proved equally ineffective in promoting sustained reform, particularly in core Government functions. GBS, in contrast, aims to use government systems and work with national stakeholders to strengthen them.
- **Stronger domestic accountability –** with existing aid arrangements, a Government's accountability has tended to be towards donors rather than its own citizens. This has undermined democratic accountability to political and civil society. As GBS focuses on government's own accountability channels, it may be expected also to improve transparency and accountability to the country's parliamentary institutions and electorate.

6. The study makes the assumption that improvements in these areas would be highly likely to enhance a Government's capacity to reduce poverty. That is, they would be liable to produce intermediate outcomes such as high-quality basic services or effective regulation, which, from theory and research, we know to be critical to poverty reduction. We focus, for this and other reasons, on the 'front end of the logframe' – on the credibility of the links from the package of GBS inputs (a greater proportion of budget funding, a changed form of policy dialogue, and a refocusing of technical-assistance and capacity-building efforts) to the expected immediate results and medium-term institutional effects (§§ 10–13).

Application of the Framework to Country Case Studies

7. The first question asked is about 'programme intent' – whether actually existing GBS programmes are seen by Governments, by donors in general and by DFID country staff as having the purposes identified in the conceptual framework/logframe. The position of the Government of Uganda comes closest, with a well-elaborated policy of promoting more GBS (but not more aid in aggregate) as the basis for a better aid partnership, reduced transaction costs and other benefits (§§ 63–72). The position of Mozambique is more ambivalent, with the Ministry of Finance and Planning not having the political capacity to impose hard budget constraints on sectors or bring the plethora of projects on budget (§§ 73–76).

8. In the Indian case, the principal source of projects in the states is the Government of India not external donors, and weak ownership of policy does not figure as a significant problem. The intentions of the Government of Andhra Pradesh (GoAP) in agreeing a GBS package involving DFID and the World Bank relate to accessing additional discretionary funds to bring forward the financial gains from public-sector reforms. Nevertheless, the benefits of this modality include some elements stressed in connection with the high aid-dependency scenario, such as technical assistance (TA) focused on mainstream Government functions and greater political acceptability (§§ 77–85).

9. The positions of donors, other than DFID, are no less diverse. However, three broad generalisations apply:

- The Poverty Reduction Strategy Paper (PRSP) framework and the need to enhance Government ownership are widely accepted.
- While partnership is espoused, the majority come in to the partnership with many conditions attached.
- The objective of financial 'gap filling' is mentioned more often than one would expect (§§ 88–91).

10. As for DFID staff, strikingly clear and coherent views are expressed, and these are generally close to the concept of the logframe. Programme documents, however, do not reflect this, tending to focus – as other donors do – on final results and poverty-reduction goals, not on the institutional transformations expected of GBS as a modality. In all three case studies, considerable agreement within DFID on fundamentals still leaves space for active debate on implementation issues. In Uganda this includes the size of the remaining space for projects and special funds, and the sequencing of SWAps and GBS. In Mozambique and Andhra Pradesh, further advocacy work is needed with central and federal government respectively (§§ 96–107).

To what extent are the inputs in place?

11. The next step in reviewing actual programme realities is to ask, 'Are GBS inputs and activities in place?' They are all in place in Uganda, with a substantial shift in the balance of DFID and donor funding generally to GBS, new forms and forums for dialogue benefiting from strong government steering (with DFID encouragement) and a consequential reorientation of TA. In Mozambique and Andhra Pradesh there is, despite the significance of GBS, no evidence of a rapid shift away from aid delivery through projects. In Andhra Pradesh, TA was concerned with mainstream Government functions before GBS and has not been substantially reoriented. However, GBS has permitted greater involvement in policy dialogue on governance related issues which some of this TA has been supporting ('a seat at the table') (§§ 108–123).

Immediate results: the Government empowered?

12. The immediate results are most perceptible in Uganda. They do include greater Government control over externally-funded activities and resources, with a relative strengthening of the Ministry of Finance (MFPED), the Cabinet and Parliament as drivers of public resource allocation. A key change is in the way line ministries relate to MFPED, as the guardian of the budget process, on the one hand, and to donors on the other.

13. These changes are incomplete. But bringing a much larger proportion of aid fully into the budget process, without separate disbursement conditions (although with 'notional earmarking') is helping public policy and expenditure management to be governed in the manner that might be considered proper in a system of Cabinet and parliamentary government. A lesser degree of government control and legislative overseeing of budget systems exists in Mozambique, where the Ministry of Planning and Finance is judged to be in too weak a position to effectively discipline spending ministries. In Andhra Pradesh, GBS does not increase ownership of the budget and policy process compared to the non-GBS scenario as proposed by the evaluability framework. Ownership was already strong in Andhra Pradesh. There is recognition, however, that GBS shifts the balance of power towards the Department of Finance, which is one of the main drivers of the reform process (§§ 126–136).

Donor coordination?

14. 'Coordinated behaviour by donors around the PRSP/partnership agenda' is the remaining immediate result claimed for GBS. This is rather more problematic, even in Uganda, for three reasons. Firstly, the relationship between Uganda's Poverty Eradication Action Plan (PEAP similar to PRSP) and its Poverty Reduction Support Credit (PRSC) from the World Bank is not entirely satisfactory, although there are different views about why and what might be done about this. Secondly, political conditionality has re-emerged in the last year in dramatic forms, with different donors withdrawing from, delaying or issuing warnings about GBS in response to political events in the region and/or political changes at home. Thirdly, there is ongoing disagreement about the scale and appropriateness of earmarking in a GBS context. The enhancement of bilateral donor coordination is clearly one of the most important benefits of the budget support programme in Mozambique (§§ 137–150).

Evidence of medium-term institutional transformation

15. The medium-term institutional effects are also explored principally with reference to the Uganda experience. This suggests:

- **Transaction costs** may have *increased* in the short run, as donors have become bedded-in to new ways of interacting with each other and with Governments. However, there are at least reasonable prospects of a reduction in the medium term, especially if deliberate attention is given to improving meeting styles and methods, and if donors delegate powers to each other (§§ 152–161).
- **Allocative efficiency** has probably improved significantly, in three ways. Budget allocations reflect Government priorities more closely (with some remaining doubts about whether the overall allocation of resources is significantly more pro-poor); the chances of gross misallocations have been reduced, especially as compared with the heyday of projects (with some remaining doubts about the size of the discretionary element in the budget); and processes have been created that will, in due course, encourage learning from experience about what does and does not produce results (§§ 162–173).

- **Predictability of funding** – a key objective – is not considered to have increased in the Uganda case, and is seen as very remote in Andhra Pradesh. The fact that GBS is both high-profile aid and highly flexible from the donor's perspective makes it in some ways more of a challenge to deliver predictability within this modality. In the case of Uganda, the major uncertainties surrounding the national and regional political situation compound the problem. Uganda has managed donor unpredictability to some degree by building reserves and protecting disbursements to priority sectors; but these are not solutions. Donors and other observers disagree about the appropriateness of 'political conditionality' in a GBS partnership context, but this reflects a wider lack of consensus on the degree and kind of partnership to which the different actors have committed themselves in Uganda (§§ 174–185).
- **On increasing state effectiveness,** there are grounds for both optimism and caution in the Ugandan experience. Once again, we note striking changes in the way sectors and multi-sectoral stakeholder groups are encouraged to make and improve policies within the Medium Term Expenditure Framework (MTEF) process. The fact that the sector-wide strategies that are developing do not benefit from distinct common-basket funding does not seem to be an obstacle to active involvement of donor specialists and non-governmental stakeholders in improving plans. It may also have some benefits in terms of the vigour with which cross-cutting sector governance issues are addressed (e.g. procurement). Improvements in outcomes for poor people are further off, but some of the preconditions have been created (§§ 186–194).
- A similarly up-beat but cautious finding applies to **effects on democratic accountability** in Uganda. This is a matter of relative improvement, as the evidence on aid dependency generally is pessimistic about domestic accountability. However, Ugandan experience suggests that incremental improvements in the role of Parliament, public audit functions and the media are occurring (for reasons that are independent of donor policies); that the absolute weight of Government accountability to donors may well have *increased* as a result of GBS; but that, under GBS, this is not a zero-sum game – external and domestic accountability may be able to improve together (§§ 195–205).
- It is very important that this should happen. Building on the possible synergies between donor dialogue with Government and internal pressures for change is the most promising avenue for addressing the very considerable worries that persist in well-informed quarters about aspects of public accountability in Uganda. For example, the approach to fiduciary safeguards that has been adopted is right, in view of the demonstrated ineffectiveness of conditionality. However, the main instrument selected – the financial tracking survey – will not guarantee, on its own, the elimination of corrupt practices in the use of budget funds (§§ 202–203).
- Again, service-delivery NGOs that are being thrust by the changing balance of aid modalities into the arms of contractors in district government have some reason to be nervous and will be entitled to more than moral support from GBS donors. Even if some of the current NGOs concerns about 'loss of autonomy' are over-blown, their worries about entering a world that, on reliable accounts, is governed by favouritism, black-listing and compulsory kickbacks, need to be taken seriously (§§ 206–209).

Risks and preconditions

16. The risks connected with GBS are obviously large, helping to explain why many informants consider the whole process extremely fragile, even in Uganda. Regarding the high-level political risks, there are different donor views on how serious they are and what the appropriate range of responses should be. This reflects not just different judgements about the situation but also a lack of consensus on the rules of the game. Lower-grade risks are also numerous and important, but a good case can be made for seeing these as internal to the management of budget support. Risks are reckoned to be substantial in Mozambique, at several levels. In Andhra Pradesh, the attitude of the Government of India to donor GBS is a major source of uncertainty, and thus a significant risk (§§ 210–219).

Preliminary Conclusions

17. Three preliminary conclusions are suggested from the evidence presented:

- **Different governments and donors are pursuing quite a variety of objectives through the use of budget support.** If greater consistency could be established over objectives, and hence over management mechanisms, then it seems likely that the impact would be greater. A first step would be for DFID to express its concept of the institutional-change purposes of GBS in both programme documentation and dissemination materials. This might then be the basis of an advocacy programme aimed at constructing a consensus with Governments and other donors (§§ 222–225).
- **Few, if any, of the postulated positive effects of budget support are automatic.** Incentives are changing in the right direction, and agents can be expected to respond to incentives, but complementary measures are surely needed. In DFID, this is generally appreciated, but the implications for resourcing country programmes need to be followed through, in terms of sector work (at least, where DFID is the designated lead agency); cross-cutting administrative issues; and (of rapidly increasing importance) local government effectiveness and probity (§§ 226–230).
- Last but most important, **the 'operating rules' for GBS need to be more explicitly stated and agreed in advance.** A more honest assessment of the operating context is required. For Uganda, it would probably be wrong to describe this as a conditionality framework, but nor is it 'partnership' as commonly described. A better theoretical framework would be that of a *multi-stakeholder club,* drawing on standard concepts from the economic theory of the firm, including a focus on the relations between 'exit', 'voice' and 'loyalty' (§§ 231–239).

'Exit', 'voice' and 'loyalty' in a multi-stakeholder club

18. We would contend that the concepts of 'conditionality' and 'partnership' – at least as currently defined – *both* tend to confuse the understanding of the situation and may be hindering attempts to establish clarity of operating rules. The reality of the operating context is considerably more complex. It is not amenable to analysis as a two-party contract as conditionality is normally presented (with donors and multilaterals on one side and

government on the other). Still less is it a 'one-party contract', as partnership is often depicted (with donors and Government on the same side). We would suggest that the partnership framework that typically surrounds GBS arrangements is probably better understood as *a multi-stakeholder club* (§ 240).

19. In this context, concepts of the economics of organisations can usefully be applied – in particular those of 'exit', 'voice' and 'loyalty'. Analysis in these terms helps to make sense of emergent patterns of behaviour among the different members of the GBS 'club' in the case study countries. This suggests that such a framework may be of more general utility in understanding, and eventually evaluating, GBS programmes. In particular, it provides a good handle on the problematic question of when, and under what conditions, predictable aid funding is likely to be achieved in a GBS regime.

20. Getting this more realistic perspective widely understood and accepted is important for immediate practical reasons, as well as from the point of view of long-term 'evaluability' concerns. The persistence of unreconstructed conditionality thinking among donors arguably has several negative effects. It obviously contributes to a lack of predictability for the recipient. Less obviously and rather importantly, the belief that, if necessary, aid can be withdrawn to force necessary policy changes may be creating a false sense of security among donors entering budget support processes. This may be leading in turn to inadequate initial diagnosis of risks and potential problems.

21. This analysis clearly has wide-ranging implications for budget support arrangements in other countries. Perhaps the least contentious implication is that more analysis is needed of the organisational and incentive structures that shape decision-making within the budget support process. This analysis should aim to enhance understanding of the factors at work and to facilitate progress towards transparent and effective operating rules for budget support (§ 241).

1 INTRODUCTION

1.1 Background

1. In financial year 2000/01, the UK Department for International Development (DFID) made spending commitments in excess of £380 million for general budget support (GBS) to seven African governments. In addition, a further £90 million of general budget support for two Indian states was under consideration. Overall, this comprised more than 15 per cent of total overseas development spending by the UK government in that year.

2. Other European countries are committing significant proportions of their bilateral aid to direct budget support, in particular the Netherlands, Sweden and Denmark. Since the Cotonou Agreement and the declaration of the European Commission (EC) and the Council of Ministers on the Development Policy of the Community (10/11/2000), the EC has also committed itself to allocating an increasing proportion of its development cooperation in the form of budgetary aid.

3. Although the precise disbursement modalities differ, all of these budget support instruments channel relatively large volumes of funds directly to a partner government, using its own allocation, procurement and accounting systems. Even multilateral agencies, such as the World Bank are re-designing their adjustment lending in similar ways, moving away from conditionality-driven balance of payments support to more loosely targeted budget support in the form of Poverty Reduction Support Credits (PRSCs).

4. These programmes mark a radical departure from previous aid arrangements, which have relied either on project-based aid or on forms of programme aid linked directly to the achievement of *ex ante* conditionalities. In recognition of the importance of budgetary aid, EvD decided in October 2001 to examine the feasibility and scope for undertaking, with other donors and national partners, a joint evaluation of general budget support as an aid modality. The ultimate purpose would be to assess whether general budget support is an appropriate, efficient, effective, and sustainable mechanism for poverty reduction.

1.2 Rationale of the study

5. Recognising the inherent difficulties of such an evaluation, it was decided to divide the work into two phases:

- Phase One would be completed during 2002 and would consist of an ‘evaluability study’, developing preliminary conclusions from the experience of DFID, and identifying issues and a possible framework for future work.
- Phase Two would then consist of both research and evaluation work, drawing on the experiences of a range of donors and multilateral agencies, to assess the role of budget support in poverty reduction.

1.3 Objectives of Phase One

6. The specific objectives of Phase One of the evaluability study are:

- To develop a conceptual framework for the analysis of the impact of GBS upon intermediate institutional policy and service-delivery outcomes that have a known relevance to sustainable poverty reduction.[1]
- To test this framework in the light of up to date research literature on the subject and in the context of three cases where GBS arrangements are either in place or at an advanced stage of design. The cases selected were Uganda, Mozambique and the state of Andhra Pradesh in India.
- To discuss and review the results with DFID, a selection of partner countries and other relevant bilateral and multilateral agencies, in order to consider whether further evaluation work would assist in improving programme performance.
- If so, to identify a set of key issues for further analysis and outline a possible approach for a second phase, involving broader multi-country and multi-donor evaluation and research work.

7. A secondary objective is to gather the emerging lessons from GBS in Uganda and other case study countries, and to use these to develop proposals for improved practice in the design and monitoring of GBS within DFID and its partner countries.

8. The initial approach to this evaluation, as set out in the Inception Report, was to consider what information and data should be collected now in order to make budget support evaluable at a future date. The main hypothesis to be tested would be that:

Countries receiving development assistance in the form of GBS perform better with respect to short-term governance improvements and intermediate poverty outcomes than countries receiving an equivalent level of development assistance in projects.
(page 20 of the Inception Report)

9. A logical framework was constructed drawing causal linkages from budget support (inputs) to activities and intermediate outcomes focused on systems of governance (accountability, transparency), resource allocation (medium-term planning, efficiency of public expenditure, administrative reform), and transaction costs. These institutional outcomes or changes were considered to be necessary steps for poverty reduction.

10. However, following discussions with the Evaluation Department at DFID the approach was modified. As described above, the approach was considered too ambitious and highly quantitative, focused at the output–outcome levels of the logical framework, when not enough was known about input and activity levels. It is too early to judge whether or not budget support is more effective than projects in delivering poverty outcomes, or for that

[1] In adopting this formulation, the study accepts that the measurement of a direct relationship between the provision of budget support and poverty reduction outcomes would be a virtually impossible task, with enormous problems of attribution. However, it assumes that there is sufficient consensus over the close association between poverty reduction and given intermediate outcomes to make it useful to restrict the study to linking budget support to those same intermediate results.

matter in delivering interim outcomes such as strengthened institutions. Nor does the study look in detail at macro-economic issues in relation to budget support. These remain live issues, but they are mostly common to all forms of programme aid (and in some cases to all aid) and have been well analysed by others.[2]

11. It was decided therefore that the evaluability assessment would first be undertaken to establish not whether and how budget support can be made evaluable (any programme can be evaluated) but whether further evaluation work appears likely to be useful, and where it might be focused. The approach is summarised in Box 1.

Box 1: Evaluability Assessment

Evaluability assessment is used when there is interest in improving programme performance but policy makers and managers have not yet defined performance in terms of realistic goals and relevant performance criteria or not yet focused their attention on evaluation options and potential use of evaluation information. Evaluation assessment is most useful in large, decentralised programmes where policy making and management responsibilities are dispersed, evaluation criteria are unclear, and programme results are not readily apparent. Evaluability assessment may be conducted as a stand-alone evaluation effort or as part of an initial phase in more extensive evaluation work. It is an appropriate first step in what may become an ongoing programme of investigative activities (evaluation and research) around budget support.

1.4 Purpose and scope of this report

12. This Synthesis Report brings together the main observations and conclusions from Phase One of the study.

13. The report is based on the following inputs:

- A draft Inception Report that laid out a proposed approach to the study and defined a conceptual framework.
- The response to the draft Inception Report by DFID and the External Panel.
- A GBS Literature Review, undertaken by ODI.[3]
- A Mozambique case study, drawing on analysis of documentation and discussions with the DFID country office in Mozambique, as well as an interview with the Mozambican Minister of Planning and Finance.
- A case study of Andhra Pradesh in India based on analysis of documentation and a short field visit to Delhi and Hyderabad for discussions with the DFID country office, and officials from the World Bank and the GoAP.

[2] For example: White & Dijkstra, *Programme aid and development: beyond conditionality*, Routledge 2002; White, H., *Dollars, Dialogue and Development*, Stockholm: Sida Evaluation Report, 1999
[3] Naschold & Booth (2002).

- A draft Uganda case study, based on background documentation and an extensive programme of interviews with DFID staff and other informants in Kampala.

14. Following this introductory chapter, the report is organised into three chapters as follows:

- Chapter Three explains the conceptual framework developed in the Inception Report and subsequently refined, applied and further adjusted during the country work.
- Chapter Four outlines our preliminary findings and conclusions on the appropriateness, effectiveness and efficiency of GBS as a mechanism for poverty reduction.[4] These conclusions are based upon the application of the conceptual framework to all three country case studies. However, the chapter inevitably draws most heavily on the experience of Uganda because this is where the GBS experience is longest and more parts of the logframe are relevant.
- Chapter Five provides a preliminary summary of the early lessons that are emerging.

15. We have not presented in this draft a formal summary of the ODI Literature Review[5] on budget support, although we have drawn upon it at a number of points. Nor have we attempted to identify what might be the content and direction of future research and evaluation work during the proposed Phase Two. However, we hope that the preliminary conclusions presented here will serve to prompt further thinking on these matters.

[4] These findings are not meant to be definitive, nor do they constitute an evaluation. They provide elements that should enable DFID to make informed judgements about the *evaluability* of this form of poverty-oriented development cooperation.
[5] Naschold & Booth 2002

2 THE CONCEPTUAL FRAMEWORK

16. This chapter presents the conceptual framework of the report and outlines its rationale. The conceptual framework is an attempt to systematically set out the principal claims made on behalf of General Budget Support as a modality of poverty-oriented aid, spelling out the implied causal links in Logical-Framework fashion. The framework is summarised as a flow-chart or logframe diagram in Figure 1 (page 29). While the rationale and geometry of the diagram remain as presented in the Inception Report, the language has been refined in the light of further thinking and the country studies.

17. In order to understand how the conceptual framework was developed, it is important to consider first the genesis of GBS as an aid modality – what is the rationale for budget support, what are its objectives. We then need to consider how it is postulated that it might achieve its objectives and from this we derive the conceptual framework.

2.1 The evolution of budget support and its significance

18. There are two general trends in thinking about poverty-focused aid that underlie the particular focus of this study and justify the desire to evaluate the poverty-reduction impacts of budget support. These are:

- a shift away from projects towards 'programmatic' forms of aid[6]
- a move away from policy conditionality towards a more partnership-based approach to the provision of macro-economic support.

19. It is in response to these trends that DFID and other donors have developed the budget support modality. Here, we examine the driving forces behind these trends and attempt to define more precisely the characteristics of modern budget support.

2.1.1 From projects to programmes

20. For most of the post-war period, projects have been the principal vehicle for concessional loan and grant aid to developing countries. The focus on projects as the 'cutting edge of development' (Gittinger, 1982) was driven by a belief that the principal constraint to development was a lack of investment, and that projects were the most efficient way to deliver capital investment. Alongside this lay a conviction that projects, with their own separate accounting and administrative arrangements, provided the best structure for minimising fiduciary risk and thus for reassuring tax-payers that their aid was producing concrete results and not being wasted.

21. However, aid evaluations over the 1980s and 1990s pointed to a litany of problems with projects:

[6] It has been argued that in terms of disbursement levels, the actual shift between these aid modalities has been less than the rhetoric suggests. We do not here contest this view but what does appear indisputable is that the policies of the majority of donor agencies now call explicitly for such a shift and that allocations to non-project instruments can therefore be expected to rise fast over the next five years.

- For countries with large numbers of aid projects and a multitude of donors, each with their own reporting schedules and accounting requirements, the ***transaction costs*** of delivering aid through projects were becoming unacceptably high.
- The ability of donors to force their priorities upon governments and to tie procurement to their own country contractors was leading to ***inefficient spending.***
- The problems in meeting the disbursement conditions and implementation requirements of different projects were leading to great ***unpredictability*** in funding levels.
- The extensive reliance on parallel, non-government project management structures and special staffing arrangements was seriously ***undermining the effectiveness of Government systems,*** with negative effects right across Government.
- The use of donor-specific mechanisms of accountability was ***corroding the normal structures of democratic accountability.***

22. It was these last two problems and their deeply corrosive impact on institutional development that drew most attention in the World Bank's *Aid Effectiveness* report of 1998:

> Aid agencies have a long history of trying to 'cocoon' their projects using free-standing technical assistance, independent project implementation units, and foreign experts – rather than trying to improve the institutional environment for service provision... They have neither improved services in the short run nor led to institutional changes in the long run. (World Bank, 1998)

23. By working outside of normal government systems – in particular the systems of budget planning and execution, accounting, procurement and performance management – aid projects not only missed the opportunity to assist in the strengthening of government systems but also ended up undermining their credibility and reducing their effectiveness, even in areas of government activity completely untouched by aid. Simultaneously, the primacy given to donor demands for accountability was increasingly forcing governments to be accountable to donors rather than to their parliaments and citizens.

24. Moreover, the main justification for separate project structures, namely the need for more reliable project financial management systems was also being questioned. In the first place, the 1980s and 1990s saw many examples of fraud, corruption and rent seeking in the management of donor projects. In addition, in an economic sense it was clear that even where positive development results were achieved in the short term through projects, this might well permit the transfer of recipient government resources into non-developmental uses. So long as aid was *fungible,* there was little point in focusing only on the outcomes of aid projects, while the wider environment for public administration and service delivery remained weak, permitting a consistent waste of resources at the margin.[7]

[7] Not all aid will be fungible: there are worthwhile activities, such as environmental conservation, where partner governments would typically be dedicating only limited public funding; consequently aid projects would not serve to free up resources for other uses. There are also short-term constraints on aid fungibility.

25. Taken together, these arguments provided a devastating critique of projects. Clearly, they applied most completely to the traditional 'enclave approach' to aid projects and to a degree could be addressed by better project design. However, at the heart of the criticisms lay two fundamental problems that seemed difficult to address within the project paradigm:

- aid-financed projects almost by definition would not use government systems and structures
- the use of donor-specific approval and review processes for projects almost inevitably removed government ownership, making it difficult for government choices and priorities to rule over project selection.

26. In common with other donors, DFID in its White Paper of 1997 took a policy decision to support development as far as possible through government actions and institutions:

> ... where we have confidence in the policies and budgetary allocation process and in the capacity for effective implementation in the partner government, we will consider moving away from supporting specific projects to providing resources more strategically in support of sector-wide programmes or the economy as a whole. (DFID, 1997)

27. Thus, the response to problems in 'project-land' has been to promote the use of direct budget support, with substantial efforts devoted initially to the development of SWAp programmes. A key theme of the evaluability study is to assess to what extent GBS has proved in practice to be immune to the main problems that afflicted projects. The distinction that has emerged between supporting SWAps and providing *general* budget support is also discussed.

28. Before that, we consider the other key development of the 1990s: the growing dissatisfaction with aid conditionality as a mode of promoting sustainable policy reform and economic growth.

2.1.2 Experience in the use of policy conditionality

29. Conditionality, by definition, describes actions that the recipient government would not carry out without donor pressure. Conditional programme aid was intended to buy reforms (Collier et al., 1997). Its use originated in the structural adjustment programmes of the IMF and World Bank. Over the 1980s and much of the 1990s, structural adjustment lending was used by the Bretton Woods institutions – often with financial support from DFID and other bilateral donors – to support the balance of payments and promote policy reform. There is thus some twenty years of multi-country experience in the use of conditionality and hence a substantial basis on which to judge its impact.

30. The conclusions of empirical work on this issue are clear: policy conditionality has been fairly ineffective in improving economic policies in recipient countries. Programme aid contributed to macro-economic stabilisation in many countries, and thus may have assisted in the first stages of reform. However, where an effective local constituency in support of reform has not been in evidence, policy reforms have not been sustained, and results have been disappointing.

31. The most recent studies into the experience of policy conditionality (White, 1999; Tarp, and Hjertholm, 2000; Dollar and Svensson, 2000) have created a broad consensus about the factors at work. Firstly, and most importantly, *it is domestic political considerations that are the prime factor in determining economic and political reform.* In general, these domestic considerations have proven immune to donor pressures. This is in large part because *donors are under pressure to disburse funds and, historically, have proven likely to do so even where agreed conditions are not met.* In addition, there are examples where aid has been given with non- developmental objectives in mind. Conditionality has also proved impractical for operational reasons, as too detailed, numerous and unrealistic conditions have been established.

32. This does not mean that donors have no influence on reform. There are examples of policies that have been implemented only due to the insistence of donors, particularly regarding the privatisation of state enterprises. There is also evidence from Zambia that UK ODA's use of the full range of channels for policy dialogue helped to tip the balance of domestic interests towards economic liberalisation (White, 1999). Sweden's long-standing relationship with the Tanzania government is also considered to have been influential in the introduction in 1984 of economic reforms that had long been resisted in negotiations with the IMF. However, this level of influence only arises after a good working relationship with the government has been established and informal channels of influence have been developed.

33. This requires a different approach to conditionality, whereby governments establish an agreed set of reforms in *partnership* with donors. The apparent failure of conditionality to exert a sustainable policy influence in the absence of a working partnership severely weakens the rationale for conditionality-based budget or balance of payments support. This is especially because conditionality in its classic form has generally served to undermine ownership and internal accountability, both by imposing external priorities and by agreeing budgetary and legislative initiatives before these are placed before the legislature for debate. The lack of transparency over the content of adjustment negotiations complicates still further the potential for any input from parties other than a narrow group within the Executive.

2.1.3 The characteristics of 'new' budget support

34. Out of the analysis of experience with project aid and with policy-based lending, a consensus has emerged within DFID and the other like-minded European donors, within the EC and within the World Bank that a new type of budget support is required. The new approach starts from the realisation that sustained poverty reduction requires effective governments that are accountable to their people. Aid should support this objective and should explicitly avoid utilising approaches that undermine accountability and ownership. This realisation creates an agenda for a new partnership, based upon a shared agenda for change with mutual obligations and a structure of mutual accountability. Aid seeks to provide predictable, transparent modalities of financial support – buttressed when requested by high quality technical assistance, informed by international good practice. This supports implementation of a nationally-owned strategy to build an accountable and capable government and hence to implement an effective poverty reduction strategy.

35. National poverty reduction strategies provide the basis for this new partnership. Through these strategies, governments commit themselves to a set of actions aimed at reducing poverty. These are embedded within a PRSP process, which is country-driven, results-oriented, comprehensive yet prioritised, partnership-based and long-term.

36. The characteristics of ‘new’ budget support may therefore be summarised as follows:

- It is partnership-based and provides untied budgetary resources within a medium or long-term perspective.
- It is focused explicitly upon the PRSP process and supports the government’s own poverty reduction strategy.
- It gives prominence to institutional development objectives, specifically to the requirements for creating accountable, capable governments.
- It utilises predictable, transparent methods for external budget finance that minimise transaction costs and work through government systems and processes.

37. Coordination of donor initiatives in support of the budget is a crucial component of the budget-support process – the aim being to reduce transaction costs, improve predictability of funding, protect ownership and strengthen democratic accountability. Participation in policy and programme design by parliamentarians, local governments and civil society is also a prominent characteristic, supported by incorporating participation into the formulation of the PRSP.

38. How far can this model of ‘new’ budget support be said to be the accepted donor policy on how budget support should be designed? In a strict sense, no donor has formally adopted such a policy. The EC’s methodological guide to budgetary aid (2002), however, does promote an approach similar to that described above. One of the recent budgetary aid arrangements agreed by the EC – that for Burkina Faso – has precisely the characteristics of ‘new’ budget support. It was explicitly developed as a model of this type of aid and had a heavy involvement of the Special Porgramme for Africa (SPA) (Zongo et al., 2000). As such, it enjoyed close involvement from a number of donors and can be said to represent a certain level of consensus on the direction for the future.

39. Within DFID, the most recent Project Memoranda for GBS arrangements incorporate most of the characteristics of ‘new’ budget support described above – certainly those for Tanzania, Uganda, Andhra Pradesh and Mozambique. However, this is not an explicit DFID policy and there are still a number of outstanding GBS arrangements that retain elements of more traditional conditionality approaches. It is important to recognise the continued existence of such ‘hybrid’ arrangements. Nevertheless, the claims now being made for the superiority of ‘new’ budget support are sufficiently coherent to justify the construction of a conceptual model that captures their essential implications, and the use of this to explore actual programme realities in different countries.

2.2 Summary of the conceptual framework

40. Figure 1 represents the postulated structure of causality. This is presented in the form of a flow chart, but in the spirit of a Logical Framework.[8] Five levels are distinguished:

- Level One: Inputs/activities.
- Level Two: Immediate results.
- Level Three: Medium-term institutional effects.
- Level Four: Intermediate outcomes.
- Level Five: Final goal.

41. Details about the proposed definitions and the causal relationships postulated at each of the first four levels are given below (2.2.3–2.2.6). An initial question, however, is posed by a causal hypothesis: what is the counterfactual?

2.2.1 What is the counterfactual?

42. This study is intended as a preliminary assessment of the evaluability of General Budget Support *as an aid modality*. It follows from this that the use of GBS to transfer resources to a partner government in order to achieve poverty reduction needs to be compared with alternative ways of transferring an equivalent level of resources in pursuit of the same goal. The relevant counterfactual is not 'no aid' but the same aid by a different modality.

43. Three potential counterfactuals are worth considering:

- An equivalent resource transfer made through traditional, conditionality-based lending or programme aid.
- An equivalent resource transfer made through projects.
- An equivalent resource transfer made through sector programmes financed under SWAp common-funding arrangements, or direct Sector Budget Support (as defined in Box 2).

Box 2: Definitions of General and Sectoral Budget Support

Direct budget support refers to the channelling of donor funds to a partner government using its own allocation, procurement and accounting systems.

Within this overall definition, **General Budget Support** covers financial assistance as a contribution to the overall budget with any conditionality focused on policy measures related to overall budget priorities. Within this category funds may be nominally accounted for against certain sectors but there is no formal limitation on where funds may actually be spent.

Sector Budget Support covers financial aid earmarked to a discrete sector or sectors, with any conditionality relating to these sectors. Additional sector reporting may augment normal government accounting, although the means of disbursement is also based upon government procedures.

(DFID, Terms of Reference for Evaluation of General Budget Support, 30 October, 2001.)

[8] Here we follow Howard White (1999), who also used a logframe approach to analyse programme aid. The diagram could be characterised as an ideal-type model of 'new' GBS.

44. In the context of a full evaluation exercise, with the ambition of testing specific hypotheses in a rigorous and quantified fashion, there might be a case for opting for just one of these alternative scenarios, even though no empirical examples corresponding to the counterfactual are likely to be found. For the purposes of the present exercise, however, a somewhat less tidy solution is necessary. The conceptual framework and the use we have made of it in exploring actual programme realities imply, at different points, comparison with each of the three alternatives above.

45. As a first approximation, Figure 1 may be seen as postulating improved outcomes by reference to a situation in which equivalent resources were transferred through projects. Thus, the hypothesis is that in comparison with such a situation GBS has 1) a more empowering effect on governments, 2) a more positive transformative effect upon governance, 3) a more pronounced impact in enhancing the capability of government to reduce poverty and 4) by implication a greater impact upon poverty reduction.

46. At certain points, however, the implicit comparison is with older forms of conditionality-based programme aid (for example, changed form of policy dialogue, for empowerment of Government). Elsewhere, the effective counterfactual is a free-standing sector programme (for example, GBS funds strengthening of Ministry of Finance). This is no doubt untidy and possibly worrying from a traditional evaluation perspective. However, it suits the purpose of the present exercise.

2.2.2 The project comparison: some further distinctions

47. In order to avoid misunderstandings, it is important to recognise some further limitations of the hypothesis that is being explored. Firstly, the analysis is restricted to the public sector only – no judgements are being made on the relative effectiveness of projects versus general grants in transferring resources to NGOs, community-based organisations or private-sector bodies. Secondly, the hypothesis does not aim to test the usefulness of projects in general. Clearly projects have an important place as a means of organising capital investments, managing the transfer of technology and more broadly as a modality of development cooperation.[9] We are simply testing whether relatively large-scale resource transfers to the public sector are more 'appropriate, effective, efficient and sustainable' when undertaken through GBS rather than through projects.

48. It might be commented that this is an inappropriate comparison from the outset, because projects are not intended as a means of effecting large-scale resource transfers. This may be true but the fact is that projects have been, and in most developing countries continue to be, the major mechanism of resource transfer for development cooperation. Given the problems that have been identified with the large-scale use of projects, it therefore seems a reasonable point of comparison.[10]

[9] Also, governments themselves may find it useful in certain sectors to fund projects, either exclusively within the public sector or in some form of public-private partnership. Whether projects are a good way of organising public action in this general sense is not a concern here.

[10] It is also worth noting that in the case study of Andhra Pradesh, where GBS is being given to provide financing during a process of public sector reform, the project modality was actually considered. DFID and the World Bank discussed with GoAP the option of providing project support to finance all or part of the short-term costs of public sector rationalisation. The case study has provided an opportunity to investigate why a budget support modality was chosen instead.

2.2.3 Level One: inputs and activities

49. The first level of our stylised logframe or conceptual framework concerns inputs and activities. The DFID definition of GBS as presented above obviously provides a starting point for defining the 'inputs' of such support but possibly does not go far enough in identifying its individual sub-components. Nor does it capture the comparative dimension of the study.

50. This conceptual framework postulates improved results at subsequent levels of the logframe when:

- an increased proportion of external funding is provided to government through GBS (rather than through projects or other modalities)[11]
- the form of the policy dialogue has changed (by reference to a 'conditionality situation'), so that it is focused on the PRSP and other nationally-led processes
- TA and capacity-building efforts are increasingly being re-oriented so as to focus on mainstream activities of government (rather than project management and administration).

51. The reason for including these three inputs or sub-components of GBS is that they are normally all present in those countries where GBS is being actively promoted. This, of course raises the question of how significant each of the sub-components is and whether one could work effectively without the other two. These are important questions for the evaluability study and are to an extent explored in the country case studies. The conceptual framework effectively presents GBS as one integrated package, comprising three necessary sub-components.

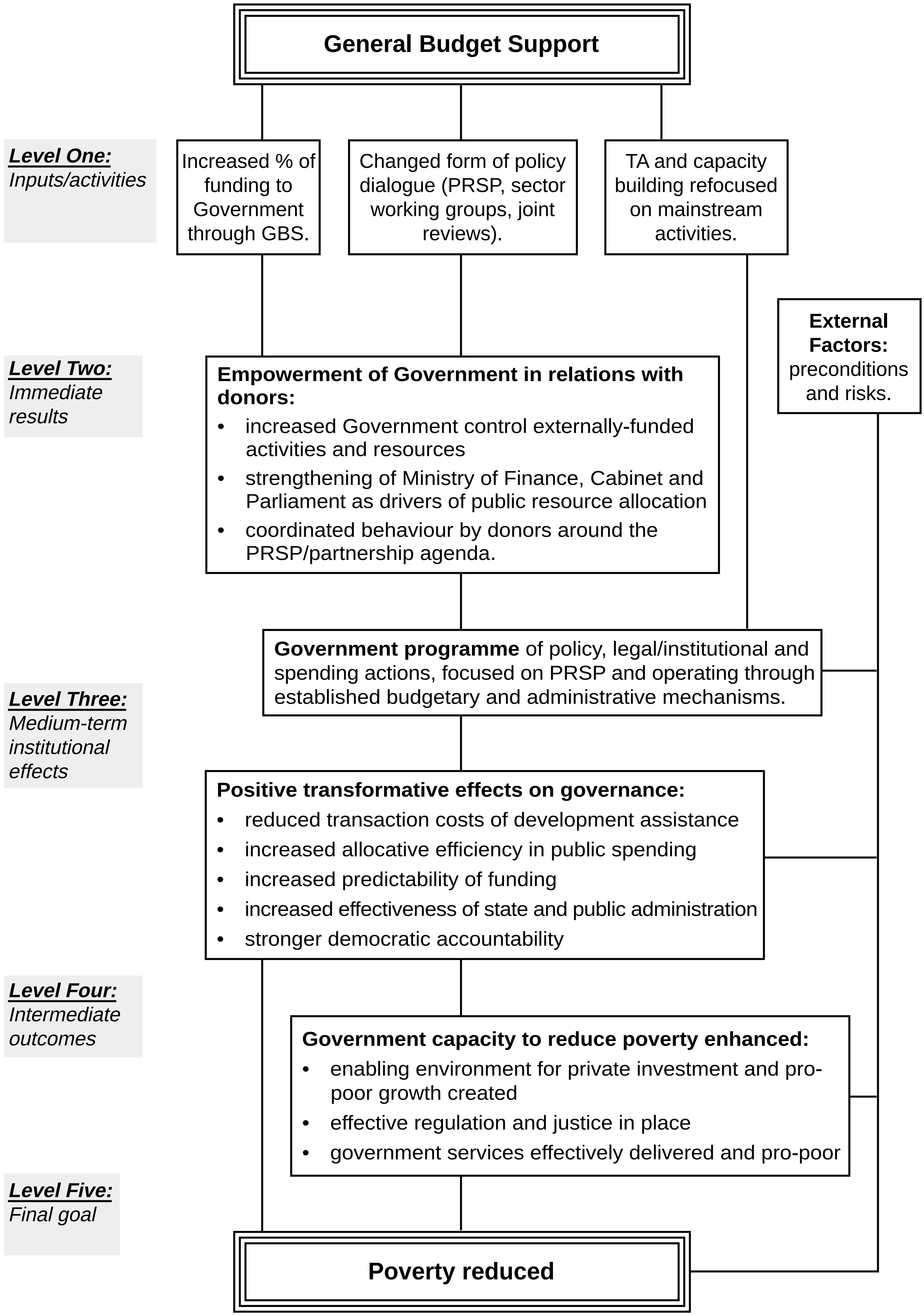
2.2.4 Level Two: immediate results

52. Level Two postulates that when there is a GBS situation characterised by the inputs described above then there will be an immediate empowering effect on a Government in its relations with donors. This effect will manifest itself through:

- greater Government control over externally-funded activities and resources
- a relative strengthening of the Ministry of Finance, the Cabinet and Parliament as drivers of public resource allocation
- more coordinated behaviour by donors around the PRSP and partnership agenda.

[11] In Mozambique, this trend is less clear-cut. Despite the existence of a budget support programme involving ten bilateral donors since 2000, the proportion of non-project aid to total external assistance is estimated to have remained constant at between 40–44% of the total over the period 1999 – 2001.

Figure 1: Logical framework analysis of General Budget Support



2.2.5 Level Three: medium-term institutional effects

53. Over the medium term, it is postulated that the combination of the relative shift to budget support financing, the changed form of the policy dialogue and the new focus of technical assistance and capacity building, will have a positive transformative effect on the country's governance. It is suggested that this will manifest itself in five particular ways: 1) through reduced transaction costs associated with development assistance, 2) through increased allocative efficiency in public spending, 3) through increased predictability of external resource flows, 4) through increased effectiveness of the state and public administration, and 5) through a strengthening of structures and processes of democratic accountability.

54. None of these hypothesised effects are straightforward to measure in an unequivocal manner. The Literature Review of this study contains a section on some of the governance indicators that have been developed internationally and presented a summary of their main advantages and disadvantages. The Inception Report also presented some indicative proposals on quantitative indicators for Levels Three and Four. However, detailed thinking about measurement was considered premature. For the purposes of the country case studies and this synthesis, analysis at this level was based predominantly on a qualitative assessment of these factors, drawing upon interviews with relevant stakeholders in Government, academia, NGOs and the donor community.

2.2.6 Level Four: intermediate outcomes

55. The intermediate outcomes postulated in the logframe relate to the enhancement of Government capacity to reduce poverty, through, in particular:

- the creation of an enabling environment for private investment and pro-poor growth
- effective assumption by Government of its role as a regulator of private initiative, and provision of a framework ensuring justice, law and order
- efficient, pro-poor service delivery.

56. The assumption is that much is known, on research-based theoretical grounds, about the causal linkages between Levels Three, Four and Five. Therefore, it may be assumed that if significant positive changes occur at Level Three (transformative effects on governance), it is highly likely that there will be improvements at Level Four (Government capacity to reduce poverty) and that the Level-Five goal will be likely to be achieved – that is, poverty will be reduced.

3 APPLICATION OF THE FRAMEWORK TO COUNTRY CASE STUDIES

3.1 Introduction

57. Here we present the results of the application of our conceptual framework to the country case studies. The chapter draws most heavily on the experience of Uganda, where the GBS experience is longest and more parts of the logframe are relevant. It also makes reference where appropriate to conclusions drawn from the deskwork and interviews on the Mozambique programme. The Andhra Pradesh GBS Programme was approved less than a year ago and it is in many respects, therefore, too early to assess whether the programme will achieve its objectives. Despite the very different conditions in which DFID is embarking on GBS in Andhra Pradesh, it has nevertheless been possible to discuss the findings of the Andhra Pradesh case study, too, in relation to the framework.

58. This chapter is organised around five questions:

- To what extent does the conceptual framework capture the intentions of the instigators and managers of budget support in the case-study countries?
- To what extent are the Level One inputs and activities in place?
- Are there any indications of the immediate results postulated at Level Two?
- How far are the Level-Three medium-term institutional effects discernable and are some of these effects more prominent then others?
- To what extent are external factors creating risks or opportunities for the budget support process?

3.2 Assessment of programme intent

59. The very first question to ask is whether the objectives and outcomes identified in the conceptual framework correspond to the stated objectives of direct budget support in the country case studies. This is not such a straightforward question as it might at first appear. The conceptual framework formalises the rationale for budget support as an *aid modality* and expresses what might be the objectives and intended outputs of a relative shift in funding towards budget support combined with a structured shift in the nature of policy dialogue and a re-focusing of the use of technical assistance and capacity building.

60. By contrast, the objectives stated in the documentation of the individual budget support arrangements in each country (funded by DFID and other external agencies) relate to the expected impacts of the individual programmes. They refer to co-financing of a joint Government-donor programme but they do not include explicit targets relating to the institutional impact of these programmes in aggregate. Nor do they explicitly consider the effects that will arise out of the particular choice of aid modality.

61. When donor officials are asked what objectives they are pursuing through budget support, they will generally quote their project documents. In most cases these will show consistency only with the Level Four and Level Five outcomes of the logframe, which refer to intermediate and final poverty reduction goals. They make little or no reference to the

immediate empowerment results, nor do they identify the medium-term institutional effects that are so crucial to the structure of causality as we have postulated it. This is less true of the DFID budget support submissions but even with DFID most of the attention is upon goals and intermediate outcomes.

62. Thus, in order to ascertain programme intent, the study team was compelled to probe further through interviews and discussions. We found some striking disparities in objectives and in the perception of the means by which they would be achieved.

3.2.1 Underlying programme intentions: Governments

Uganda

63. The most clearly articulated set of government objectives with respect to budget support was in Uganda. The 'partnership principles' included in Volume III of the Poverty Eradication Action Plan present a clear statement of Government's intention to move to budget support and to adopt mechanisms that protect Government ownership and control over resource use. These principles have been developed through a structured process of dialogue with donors that has been actively managed by the Government of Uganda (GoU) over a number of years, starting with a statement to the 1999 Stockholm conference on 'Making Partnerships Work'.

64. PEAP Vol. III is a landmark document in international terms, providing one of the clearest statements to be found anywhere of the standards of partnership now expected in development cooperation. However, it is not only an impressive document. In discussions with different Government officials, the researchers found that the policy towards budget support and the objectives of the policy were always consistently and clearly presented. These objectives are in turn closely consistent with the conceptual framework in this report.

65. An aspect of GoU policy on the use of budget support that is striking is that it is not seen as vehicle for increasing the volume of external funding. The current MTEF anticipates a reduction in the relative level of external funding over the next few years. Within this, it is planned that a higher proportion of funding should be provided in the form of budget support, but with no overall additionality. The reasons are three-fold:[12]

- external funding is considered to have reached a level where 'Dutch Disease effects' arising from the overvaluation of the exchange rate are now noticeable
- the difficulties of sterilising[13] foreign exchange inflows from official transfers are now becoming acute
- the level of externally financed expenditure is considered unsustainable given the persistently low levels of domestic revenue collections.

66. While it is not about securing additional aid, PEAP Vol. III is definitely concerned to shift the balance of aid modalities away from projects and towards GBS. It is about ways

[12] These are well summarised in Uganda (2002a).
[13] Withdrawing an equivalent amount of domestic currency to avoid expansion of the money supply.

of increasing the total volume of resources committed to PEAP goals, while enhancing the *flexibility* and reducing the *transaction costs* associated with donor flows.[14]

67. As the Executive Summary states, the project approach 'causes some problems', and there is a 'general consensus that the way forward is to move towards an increased volume of budget support, with improved modalities for project assistance for donors who cannot follow this course'.[15] The Government believes that PEAP objectives would be most easily achieved if all resources were available on the basis of full flexibility, so that allocations could be made on the basis of sector-wide strategies within a fully unified budget/MTEF process. However, recognising that full flexibility is not yet acceptable to many donors, it sets out a range of second-best solutions and transitional arrangements for minimising the disruption caused by projectised assistance and sectoral earmarking.

68. We discuss further on, the headway that has been made in these respects, and why the issues are complex in practice. Here the important question is just how close GoU's vision is to the model in Figure 1.

69. A general observation, supported by both a close reading of PEAP Vol. III and by the public statements of senior officials, is that the GoU vision is about as close to the ideal model as it is possible to be. This implies two things:

- The vision inhabits a post-conditionality, post-project world in quite a strong sense. Reasons why donors might wish to impose conditions, earmark funds, tie or projectise their aid are recognised but are seen as principally a matter of restrictions imposed for legal, administrative or political reasons by headquarters' offices. There is little remaining sense of external funders needing to lever changes in policy or improvements in implementation. The possible reasons why a donor might insist on project funding are seen to include taking a fundamentally different view on strategy in a sector, but not a fundamental distrust in government systems.[16]
- The vision does not imply that it is automatic that the changes at Levels One and Two will feed through into changes at Levels Three and Four, and that these will improve poverty outcomes. However, the main obstacles are seen as arising from insufficient vigour and consistency in implementing the partnership principles.

70. Thus, the focus is principally on changing donor behaviour. On the other hand, there are some important nuances that would prevent an over-simple reading of GoU beliefs and intentions about GBS:

- There is a strong aspiration to reduce inefficiencies and transaction costs associated with the project modality, yet the participation of donors, especially locally-based staff, in the MTEF and sector-wide strategy processes is viewed very positively.
- Performance indicators, monitoring arrangements and joint-review processes are given a central place, in a way that suggests that problems at Levels Three and Four need to be recognised and addressed jointly

[14] Uganda (2001: 4).
[15] Ibid: iv.
[16] Ibid: 78.

- There is some recognition that certain of the constraints on de-projectising donor support arise from inadequate progress with key reforms on the GoU side – e.g. pay reform in the civil service that is seen as a precondition for the eliminating the topping up of salaries by means of projects.[17]

71. A final, important proviso needs to be added to this account of the Uganda Government's objectives in promoting GBS. It is that this is most clearly the vision of the central economic ministry, the Ministry of Finance, Planning and Economic Development, and its senior officials and advisers. MFPED has been extraordinarily successful in getting its vision widely accepted across government. However, it is not clear that there is yet full consensus. In other words, the factors that, in other countries, generate entrenched support for project aid and large project-style sector loans are not yet absent in Uganda.

72. PEAP Vol. III is aware of this issue. What is most significant in this sense is the recognition in Uganda of the way a sector's appetite for project funding is affected by the presence or absence of a hard budget constraint, and whether MTEF ceilings are able to encompass all forms of assistance to the public sector. GoU's 'second best' solution to this problem involves a two-tier approach to MTEF ceilings, which sets one limit for Government budget allocations and another for donor grants.[18] This reflects the reality that building consensus around the GBS vision is a process that involves not only intellectual persuasion but also a progressive re-jigging of the effective incentives to which different sections of government respond.

Mozambique

73. The Mozambican Government has also expressed concern about the sustainability of current levels of external funding. They have not, as in Uganda, taken the deliberate step of controlling the growth in external funding but it remains a significant topic of political discussion. It is also interesting to note that in the recent DFID-supported Poverty and Social Impact Assessment (PSIA) of the IMF Poverty reduction and Growth Facility (PRGF) programme, the Government of Mozambique (GoM) explicitly requested an examination of the potential for increasing petroleum tax, with a view to enhancing the sustainability of budget expenditures.

74. With respect to budget support, the Mozambican Government's position is somewhat ambivalent. On the one hand, the 2001 Public Expenditure Review stated that 'increasing the share of external assistance that is disbursed and used through the normal budgetary procedures, and avoiding the proliferation of parallel donor-driven arrangements' has been GoM policy for some years.[19] Also, the need to provide greater accountability to donors in the use of budget support has been one of the reasons why GoM has decided to accelerate current reforms in the fiscal management system.

75. On the other hand, the political weight behind these commitments is not comparable to the case of Uganda. Fiscal management reforms may in due course make a difference but in the meantime sector ministries pursue opportunities for external project financing

[17] Ibid: 86.
[18] Ibid: 27-28.
[19] Mozambique (2001: 85).

relentlessly, with little active effort[20] by the Ministry of Planning and Finance either to control this process or to bring aid projects on budget.[21]

76. Perhaps the clearest statement of the government's current thinking are comments made by the Mozambican Minister of Finance when interviewed for this study. A shortened version of the Minister's comments appears in Box 3.

Box 3 Comments by Luisa Diogo, Mozambican Minister of Planning and Finance on the Budget Support Programme, London 21 September 2002

Budget support is very necessary in order to allow the government to meet its obligations under the PARPA and to effectively implement its expenditure programme. However there is a need to be clear about the objectives of budget support. It should allow both government and donors to spend more time looking at outputs from the government's programmes, rather than focusing upon implementation arrangements. There have been cases where we have received 30 missions per year from various donors wishing to evaluate and discuss their specific projects and programmes, which is a waste of resources and does not lead to better results.

Some bilateral donors are against the idea of budget support and I understand the reasons for this. They need to discuss and get approval from their national parliaments first; it is our responsibility to give them the instruments that they need in order to convince sceptics that Mozambique is fully prepared for budget support and will utilise these funds effectively and transparently. We have to modernise our financial management systems in order to achieve this. In Mozambique this is currently being implemented through a fundamental reform of the financial administration systems of the government – which will come into effect on 1st January 2003. This is the main transmission mechanism which will ensure that the objectives laid down in the PARPA can be effectively implemented and monitored.

The main issue for me regarding budget support is the need for long-term commitment from donors. If donors promise funding and then change their minds, this is a big problem for us. Sometimes procedural problems arise and short-term targets are not achieved. The problem is that if one donor is not happy and decides to stop its programme, all of the others tend to follow. If there are persistent problems and it is clear that the government is not committed to its agreed reform strategy then of course donors should re-evaluate their strategy, but this should not be necessary in the case of short-term problems. Here, it is an issue of confidence and dialogue. Donors have to have confidence in the government and its commitment to reform and the best way to establish this confidence is through dialogue with donors.

Regarding conditionality, in the case of budget support we feel the conditionality more than when donors were supporting their own projects. In fact, we are now having to face two sets of conditionality – one from the World Bank and IMF as part of the PRGF process and one from the bilateral donors connected to budget support. In many cases these two sets of conditions overlap – it is possible to compare the two sets and say that this condition on, for example, outcomes in the education sector is the same as this one, just that the wording is different. But there are cases where the bilateral donors are asking for extra conditions. In the case of Mozambique, we receive approximately US$ 140 million per annum from bilateral donors and US$ 120 million from the World Bank and IMF, so obviously we have to pay careful attention to the needs of both sets of donors. But I believe that more effort needs to be made amongst Mozambique's various partners to integrate their requirements, so that we are clear on what we are trying to achieve and again so that we can focus more of our discussions on outcomes rather than procedures.

[20] The lack of active effort does not necessarily mean there is no desire within the MPF to bring off-budget project funding under control. It may reflect a simple acceptance of their relative powerlessness to achieve this – particularly given the strong political position of sector Ministers in relation to the Minister of Finance.
[21] There are actually two significant sources of off-budget items in Mozambique: donor-financed investment projects – around two-thirds of total capital expenditure are externally financed and mainly implemented outside the normal budget system; and ministries' own revenues (user fees) and associated expenditures, which are substantial in some sectors.

Andhra Pradesh

77. Within the State Government of Andhra Pradesh and the Government of India more broadly, the characterisation of aid projects as a major source of institutional dysfunctionality is not the received view. For the most part, projects remain the preferred modality for the use of external funding.

78. There are two important reasons for this. Firstly, India is a low aid-dependency country and has probably not yet experienced the negative costs of large numbers of externally-funded projects. Secondly, there remains a strong interest in public investment as a vehicle of economic growth and the project structure (whether for Government of India (GoI) or externally funded investments) is considered the best way of organising capital investment. Many GoI officials see the project modality as a good way of 'ring-fencing' funding to the states and controlling its use.[22]

79. So why then did the GoAP respond positively to DFID's proposed budget support arrangement? It helps to assess this decision in two stages: firstly, the justification for additional amounts of development assistance (since in Andhra Pradesh budget support is currently seen as additional to DFID's portfolio), and secondly, the justification for the additional development assistance to come in the form of general budget support:

80. The rationale for additional development assistance in Andhra Pradesh derives from:

- The need to protect priority development expenditures through the period of reform. These expenditures (non-wage O&M, capital outlay, primary health, primary education) would otherwise face substantial forced cuts if the power sector were to be restructured within the constraints of the state's Medium Term Fiscal Framework.
- Budgetary support to the power sector while the sector reforms. The experience of other states is that if support is not provided reforming power utilities are forced to run large arrears and enter into expensive short term borrowing arrangements detrimental to the long-term health of the sector. The power-sector financing requirement is projected to decline only over the medium term since there is a limit to the rate at which tariffs can be increased and efficiency improved without provoking a backlash.
- The need to fund other elements of the state's reform programme that are generating transitional costs and extra demands of the state budget, in particular voluntary retirement payments related to privatisation and the closure or restructuring of public enterprises.

81. The first of these items has not been quantified. The second and third are estimated at US$670m in 2001/02. The combined DFID/WB assistance through GBS of US$350m amounts to less than 5 per cent of the government budget and less than 1 per cent of Gross Sustainable Development Product (GSDP) in 2001/02.

[22] About 40% of the GoAP capital budget is centrally funded through a series of projects. Anecdotal evidence suggests that the fact that GoI is the source does not prevent the project modality from having several of the features associated elsewhere with donor projects – underprovision for recurrent costs, roll-over of much of the project portfolio from one period to the next, limited linkage to the state Government's agenda, etc.

82. The rationale for significant levels of financial assistance is that such amounts allow the *pace of implementation* of the government's reforms to be increased (over and above what would otherwise have been the case) while protecting priority development expenditures. The main institutional and fiscal objectives supported by the programme are expected to have been achieved by the end of 2005/06. At this point the GBS programme is expected to cease and GBS funds will be replaced by those domestic fiscal resources that have been released as a result of the reform programme (i.e. the resources presently allocated to power sector subsidies will become available for developmental purposes).

83. GoAP's intentions in approving GBS as the means of disbursing these additional funds rest on the following three arguments:

- *The need for additional discretionary resources that could be used in a flexible manner to support the economic reform programme.* GBS allows for flexibility in allocating resources between and within the three main areas of reform that are generating transitional costs – power-sector restructuring, allocations to priority social sectors, and public enterprise restructuring. As long as the overall annual cost of reform in these areas has not been underestimated, GBS avoids the need to resort to unplanned borrowing or build-up of arrears in any one area of reform if the costs of reform deviate from plan. The cost of power sector reform is the most significant reform cost in Andhra Pradesh and has proved difficult to forecast in the past despite external TA. The provision of untied budgetary resources allows GoAP to pursue power sector and other reforms and maintain its Medium Term Fiscal Framework (MTFF).
- *To provide additional discretionary resources that the Department of Finance might begin to use to influence aggregate resource allocation and the efficiency and effectiveness of public resource use.* A rough calculation suggests that in the short term the GoAP Finance Department has full discretion over only about 10 per cent of its annual budget, of which about half currently has to go to power sector subsidies. At US$350m in one year, GBS represents about 5 per cent of the Andhra Pradesh budget. According to the above argument it doubles the amount of discretionary resources available to Finance Department. In the context of a reforming government that is trying to maximise the benefits of additional expenditure at the margin, this amount and the flexibility associated with it is significant. That portion of the GoAP budget that is in effect 'non-discretionary' (i.e. the remaining 90 per cent) is allocated to salaries, wages, pensions, debt interest, and counterpart funding for centrally sponsored schemes and donor projects. This portion of the budget is relatively fixed and, in the short term, is not available in significant amount for reallocation within or between sectors.[23] In the longer term, the reduction of subsidies to the power sector should release resources for this purpose. By providing GBS in the short-to-medium term, GBS aims to bring forward one of the anticipated benefits of reform (i.e. resource reallocation) by perhaps three or four years. An additional attraction is the possibility of creating positive demonstration effects, thereby promoting other reforms within the state and more widely.

[23] This argument only makes sense as long as the focus is short term (say, 2–3 years). In the medium to long term all budget resources are available for reallocation within or between sectors.

- *GBS provides the possibility of funding and technical advice in support of the Government's governance reform objectives.* In the short term, this governance reform agenda is difficult to 'projectise' because in large part the strategies by which governance objectives will be met have not been decided or developed in any detail. GoAP recognises that DFID and other donors have a good track record of supporting governance reforms in India and elsewhere and are a useful source of advice on reform. Donors have therefore been 'let in' on the Government's discussions of governance reform and GBS allows for rapid funding for any initiatives that are developed in these discussions and are not covered by existing projects. In a low aid-dependency environment, this type of policy influence is important for DFID. Influence over governance reforms at state level will improve the enabling environment for other DFID interventions in the state. More significantly, it may also influence the effectiveness of that portion of the state budget that is not financed by external donors (in Andhra Pradesh, some 95 per cent).[24]

84. In summary, the rationale for GBS – from the Government point of view – is different in this low aid-dependency case. GoAP ownership of its reform programme is already strong. Projects pose problems but not principally because of their association with external donors. GBS is to support the Government's existing reform efforts in ways that would not be otherwise feasible and, if possible, bring forward their benefits, to help maintain reform momentum, technically and politically.

85. A more subtle point to note is that GBS, with its lack of explicit conditionality, makes it politically easier for GoAP to accept external funding. Context is important here – GBS is implicitly supporting a politically difficult power-sector reform programme and GoAP would find it difficult to be seen to be doing the World Bank's bidding. Of course, the Opposition already accuse the Government of being the Bank's 'lapdog', but the nature of the aid modality can be used by the Government to give themselves some protection from these accusations.

In summary

86. Of the three governments we are considering, therefore, only one has a decisive position in favour of using budget support to enhance Government control over externally-provided resources and strengthen national governance. The example of Andhra Pradesh in India suggests that this is likely not to be the rationale for budget support in a low aid-dependency country, although there may be other rationales that are equally compelling.

87. In Mozambique, the Government position may in the future swing more decisively towards the vision expressed in the 2001 PER and regularly endorsed in the joint Government-donor review meetings on budget support. On the other hand, the interests that are gaining from the lack of a tight budget constraint and from the continued ease with which off-budget project funding can be obtained are powerful ones that enjoy some political support. In contrast to Uganda, there is not yet a firm consensus at the senior echelons of power that the medium-term gains of bringing external resources on-budget will offset the short-term losses.

[24] There may not be much impact on centrally funded programmes. Here interaction with GoI may be more relevant.

3.2.2 Underlying programme intentions: other donors

88. Are the positions of the external agencies other than DFID any clearer or any more consistent with the conceptual framework? In responding to this question, it is important to note that we are mainly summarising here the responses of field staff.

89. At headquarters' level, there are several external funding agencies – notably the European Commission and the World Bank but also many of the bilaterals – that have internalised much of the thinking associated with *Assessing Aid* and that have explicit policies to increase the use of budget support as part of a new PRSP-based partnership. At the field level, these policies appear to be interpreted in a rather more ambiguous manner. In part, this may be because the budget support arrangements we are considering derive from old polices. But it also appears to reflect the difficulties of ensuring that training and briefing processes keep up with policy developments at headquarters. It may also reflect ambiguities that persist at headquarters level.

90. Our findings here draw principally on the cases of Uganda and Mozambique, and we express them in terms that are appropriate for an aid-dependent PRSP country. Nevertheless, the Andhra Pradesh case study supports these statements, at least as broad generalisations about the state of donor opinion.

91. Three broad statements can be made about the positions of other donors:

- *The need to work within the partnership framework of the PRSP has been internalised and the need to protect and enhance government ownership is well understood.* In Uganda, this process enjoys a strong lead from government. In Mozambique, where this is not the case, there is much less appreciation amongst the donor group of the mechanisms by which ownership might be enhanced – of the principles of donor coordination which need to be established and of the specific budgetary systems and structures that need to be protected and promoted. Nor is there much sensitivity to the potential contradiction between the espousal of a partnership framework and the continued desire to push 'pet interests' at sector level and to persist with off-budget funding of projects and SWAp common funds.[25]
- *Although partnership is espoused, most donors come into the partnership with a large number of conditions attached.* This does not necessarily mean that a mechanism of conditionality is being applied (in the specific sense of a process by which policy change is 'bought', i.e. where resources are promised in support of policy actions which governments would not otherwise take).[26] For the most part, the conditions attached to budget support are prior conditions and refer to policy actions, which, while not always palatable, are generally understood by GoU and GoM to be necessary. However, the mechanisms by which these prior conditions are negotiated do not differ drastically from the mechanisms of old-fashioned conditionality. Moreover,

[25] In Mozambique, several bilateral donors expressed an unwillingness to put 'all of their eggs in one basket' given the relative weakness of existing public financial management systems and hence intend to retain a mix of projects and sector programmes, while also participating in the Joint Donor Programme for budget support.

[26] See Collier et al. (1997) and the discussion in this report, section 3.1.2.

several bilateral donors in both Mozambique and Uganda expressed the view that their role in 'forcing' government to adopt reforms was important and that the threat of stopping budget support was an important one to retain. [27]

- *The objective of 'gap-filling' is frequently mentioned by bilaterals and by staff of the World Bank as a key driver of the budget support process.* In Mozambique, the point is explicitly made that to meet Millennium Development Targets, a higher level of public spending is needed than can be financed by domestic revenues and that, by filling this gap, donors make an important contribution to poverty reduction.[28]

92. The objective of 'gap-filling' is perfectly consistent with the structure of causality postulated in the conceptual framework. However, the frequency with which this was mentioned as an objective suggested a degree of self-delusion about the processes that are in reality at work. As we have noted above, GoU has adopted an explicit position that the relative level of external funding should be reduced – in short, if there is a gap to be filled, the government has stated clearly that it does *not* want it filled by external finance. In so far as additional budget support to Uganda might be made available in the future, this could only be to replace financing through projects and other modalities.

93. This is not yet the case in Mozambique but the macro-economic constraints to increased external funding that have been noted in Uganda are also at play in Mozambique. With a thin financial sector and a narrow range of monetary instruments available to the Central Bank, these could begin to bite at a lower level of per capita GDP than in Uganda. Of course, these are not absolute constraints but more precisely constraints on the relative rate of expansion of external funding. Nevertheless, they do mean that the gap-filling role is probably more limited than is generally supposed.

94. Moreover, from the perspective of the GoM, if the key objective for budget support were to fill an external funding gap, would it really make sense to invite ten donors to work together to fill what is in international finance terms a very small gap? Clearly not – the gap could more efficiently be filled by a smaller group of donors providing larger individual amounts. The rationale for a wider donor input is more probably that it permits a larger number of stakeholders to be brought into the partnership process and to engage with government in tackling the problems of macro-economic management, service delivery and poverty reduction. From government's perspective, it is an opportunity to stop donors operating as free electrons in a vacuum and more as partners in a structured process. The logical next step, which has been taken in Uganda but not Mozambique, is to ask donors to halt off-budget funding and to restrict project financing, so as to work with rather than outside Government systems.

95. It is not wrong to see gap-filling as a primary objective in Andhra Pradesh but this function is time-limited there. It applies only for a period of three to four years, until the power sector has been restructured and can release resources (currently tied up in

[27] This was also a feature of donor behaviour in relation to budget support in Andhra Pradesh.
[28] In AP, the budget support programme has been designed to make a substantial contribution to closing the projected three to four year fiscal gap created by the transitional costs of power sector reform. This is seen to contribute to poverty reduction by maintaining the delivery of essential public services while the power sector reforms.

subsidies) back into the budget. The macro-economic arguments against increased funding do not apply, GBS is only 5 per cent of the GoAP budget, and the institutional issues are, as we have explained, different.

3.2.3 Underlying programme intentions: DFID

Uganda and Mozambique

96. How far can DFID's intentions be said to be firstly clear and secondly consistent with the conceptual framework? In relation to Mozambique and Uganda, the answers are on both counts resoundingly positive. In both Uganda and Mozambique, DFID has been a leading promoter and supporter of budget support and building Government-donor partnership around the PEAP. All DFID staff in both country offices appear to have a clear sense of the underlying institutional processes being promoted through the shift to budget support and of the relationship between these processes and the capacity of governments to reduce poverty. Active processes of internal debate as well as semi-formal seminars and training activities have promoted this broad understanding. In both offices, these activities embraced programming and accounting staff in addition to technical advisers.

97. This is not to suggest that there exists unanimity of opinion, in either DFID-Uganda or DFID-Mozambique, about either the extent or the speed of the shift towards budget support. On the contrary, this is a matter of lively debate in both offices. Topics of debate include important issues of implementation that are not settled even if there is complete consensus on moving decisively into GBS. For example:

- It is clear that giving priority to the GBS modality does not mean having no more projects or off-budget funds, if only for the reasons indicated below (civil service salaries are prohibitively low). It is a question, rather, of using these minor forms of support to enhance the effectiveness of the main form of support. But then what range of ancillary efforts is permissible? Should funds continue to be set aside to assist ministries to overcome transitional bottlenecks that for one reason or another cannot immediately be solved through the relevant Government systems? What limits of time or scope should be placed on 'transitional' arrangements of this sort?
- Transitional bottlenecks apart, do projects have a place at all in the DFID Uganda programme, and if so where? A conventional approach is to restrict projects to areas where innovation is required, and Government is unlikely to be able to innovate for itself. Is limiting new projects to areas of 'innovation' either too restrictive (there are likely to be other ways in which government plans are imperfect in the medium term: e.g. total neglect of legal education, or reconstruction in the North) or too permissive (why shouldn't government innovate for itself?).

98. Another key implementation issue that has not been entirely settled within DFID concerns when and how to treat GBS as an alternative to SWAps. In the Uganda programme, the issue has been largely settled or rendered redundant, but different views on the principle are still heard:

- One view says the moment to move from SWAps to GBS is when sectors have strategic plans and review processes, and attention needs to shift to the cross-cutting governance issues that can only be tackled through *general* budget support. This suggests *a sequence:* first support a cluster of SWAps in key sectors, then build a GBS programme on that firm foundation.

- But there is another view, which gets considerable support from the actual process in Uganda. If the basic problems of defining sectoral policies have not yet been tackled then that means there is a reason for donor engagement in sectoral dialogue and support. But that does not necessarily imply the funding modality of a SWAp (a sectoral common basket). Uganda had an ESIP before the move to GBS, but health-sector policy was sorted out without any degree of sectoral common basket funding. This tends to support the view that GBS is *an alternative* to supporting free-standing SWAps, and not a second stage following sectoral budget support.

99. These remain live issues in the Kampala office. However, the debate is firmly based on a shared understanding of the theory of GBS. The view was frequently expressed to us in both Uganda and Mozambique that the conceptual framework in Figure 1 presents a clear and accurate summary of the intended linkages and factors at work.

100. It is unfortunate, perhaps, that these underlying factors are not well captured in the relevant DFID Project Memoranda, although this could be remedied relatively easily at the next iteration. More important and more challenging is the fact that the vision as a whole is not reflected in the mechanisms for monitoring budget support that have been agreed with governments and other donors. If the shift towards budget support is to progress further in each of these countries, a broader and firmer consensus needs to be built about what GBS is meant to achieve and what should count as success.

101. There is a corresponding task of clarification and persuasion for DFID to undertake jointly with other donors. This is especially true in Mozambique where, in contrast to Uganda, advocacy is needed also with Government. However, in order for this to be effective, it is important for DFID staff themselves to be able to marshal the relevant arguments clearly and consistently. A revision of DFID’s own programme documentation (and monitoring indicators) would not be a bad place to start this process.

Andhra Pradesh

102. DFID-India is clear in its understanding of the objectives of GBS in Andhra Pradesh and these objectives are basically consistent with our conceptual framework. However, none of this is adequately captured in programme documentation.

103. DFID has a history of engagement with GoAP in several sectors over a number of years. However, by 2000 it was recognised that while these programmes had succeeded in meeting some targets, such as increased social sector spending, these achievements were overshadowed by problems with the fiscal framework that went seriously off-track as a result of rising power sector subsidies, food subsidies, and a 25 per cent increase in civil service salaries. Together with the World Bank, DFID therefore began to explore alternative means of supporting the GoAP reforms. For both agencies, there is recognition that (as with other states in India) resolving the fiscal crisis in Andhra Pradesh, and the associated governance problems, is a prerequisite for sustainable poverty reduction. Discussions

have centred on details of the MTFF to be supported through GBS and the policy matrix of reforms that would be the basis for successive tranches of budget support over a three to four year period.

104. It is clear that the 'projects or GBS' debate does not apply in Andhra Pradesh, where budget support is largely additional to DFID's project portfolio. The DFID India office regards GBS as a means to meet development goals not easily met by other forms of assistance. The key feature frequently mentioned is the flexibility GBS gives GoAP to use funds between the three short-medium term development goals mentioned above – namely fiscal stabilisation, PEM reform, and governance reform. Flexibility is necessary because of the difficulty in making ex-ante assessments of the politically sustainable rate of power sector reform in Andhra Pradesh and the associated funding requirement, which in the short term is a significant driver of the state's MTFF.

105. Generally, in Andhra Pradesh budget support has enabled DFID to begin discussions with GoAP on a range of governance reform issues for which it previously had no effective platform. In the opinion of many close observers it has given DFID 'a seat at the policy table'. This finding is likely be different to the findings of budget support operations in Africa, where donors are already at every significant policy table by virtue of their overall financial contribution to the budget. In particular, GBS appears to have allowed for the possibility of gradual expansion by donors of the concept of governance – in effect it enables them to 'put difficult issues on the table', or as one observer put it, to 'deal with many of the issues that were traditionally considered external to project world'. Here, the long-standing bilateral relationship between DFID and GoAP is an important factor.

106. GBS is therefore succeeding in having a positive impact in terms of facilitating dialogue on the government's reform agenda. In a low aid-dependency environment, this type of policy influence is important for DFID. Influence over governance reforms at state level will improve the enabling environment for other DFID interventions in the state. More significantly, it may influence the effectiveness of that portion of the state budget that is not financed by external donors (as mentioned, in Andhra Pradesh some 95 per cent).

107. Interestingly, DFID are aware that, as currently designed, GBS in Andhra Pradesh does not promote predictability of funding. This is partly because of the significant elements of old-fashioned conditionality in the agreements, with correspondingly detailed attention, in partnership with the World Bank, to compliance issues. Partly – and perhaps more importantly – it is because GoI's position on GBS per se is unclear. At the time of the fieldwork for the case study the big area of uncertainty was the GoI policy stance on GBS. The need to step up joint discussion and advocacy with GoI on the whole issue of GBS has been recognised but discussions appeared to be at a much earlier stage than at state level.

3.3 Level One: are GBS inputs and activities in place?

3.3.1 The redirection of funding

108. Uganda[29] is almost certainly the country where the role of budget support has increased most dramatically in the last three years. The significance of budget support as a proportion of all concessional and grant financing increased from 19.2 per cent of total inflows in 1998/99 to 40.9 per cent in 2000/01. In 2001/ 02, the percentage is projected to reach 56.4 per cent, stabilising in the subsequent year at approximately 60 per cent.[30] Thus, Uganda most certainly has witnessed a shift in the relative proportion of funding provided through GBS.

109. The shift in DFID's own portfolio has been a significant contributor to this overall trend. However, the budget support process is clearly a multi-donor phenomenon with International Development Association (IDA) DFID, Ireland Aid, the European Commission, the African Development Bank, the Netherlands and Sida all providing funding through budget support.

110. In Mozambique, approximately 40 per cent of all bilateral aid in the 1999–2000 period fell under the twin headings of 'programme assistance' (which we interpret as being primarily budget support) as well as 'action related to debt relief' (which is indirectly part of the budget support programme). This proportion appears to be relatively stable. The most recent IMF evaluation shows that the proportion of non-project aid to total external assistance has remained constant at between 40 and 44 per cent of the total over the period 1999–2001.[31] Hence, there is no evidence at the aggregate level of a rapid shift away from aid delivery through projects, some of which are integrated into sector-wide programmes in areas such as agricultural development, health and education. DFID's contribution to the jointly-funded budget support programme was worth 30 million pounds sterling over 2000–2002 (which is about one-third of total DFID assistance to Mozambique) and is scheduled to increase to 70 million pounds sterling over 2003–2005.

111. There has also been a substantial shift in funding towards budget support in Andhra Pradesh.[32]

[29] This section and the two that follow (3.4 and 3.5) necessarily draw rather heavily on the case of Uganda.
[30] Data supplied in June 2002 by the Ministry of Finance, Planning and Economic Development, Kampala. In the mid-1990s, the proportion of budget support fell from a peak of 35.8 per cent in 1993/94 to a low of 16.3 per cent in 1995/96, reflecting the rise and subsequent decline of programme aid in support of macro-economic stabilisation. See Annex 1 Table A2.
[31] MF Staff Report for 2002 Article 4 consultation, June 2002.
[32] Although precise figures have yet to be provided by DFID India

3.3.2 New form of policy dialogue?

Uganda

112. Uganda was the first country to have a workable PRSP (the Poverty Eradication Action Plan, PEAP). The PEAP is a broadly-owned poverty reduction strategy that has already been updated once and is informed by an ongoing Participatory Poverty Assessment (PPA) process. The PEAP is implemented through the budget in a MTEF, with priority expenditures protected by a ring-fenced Poverty Action Fund. These innovations in Uganda influenced the development of the PRSP concept. They have also helped shape international thinking on donor coordination in a context where Government is strongly committed to poverty-reduction efforts.

113. In this framework, donors generally and DFID in particular have been able to focus much of their dialogue with Government not on specific aid-funded interventions and the conditions of their effectiveness but on ways and means of implementing the PEAP. Much of the content of policy dialogue remains the same (e.g. How can the conditions for growth be improved? Why isn't quality primary health care being delivered?). However, its form has changed in two ways. Firstly, it is directly concerned with improving the quality of what government does in following up its commitments under the PEAP. Secondly, the relevant conversations tend to take place in or around joint forums, convened by Government. These include the sector working groups, including the cross-cutting Poverty Eradication Working Group, convened as part of the MTEF process, and the joint review missions organised around the emerging sector strategic plans.

114. Uganda was also the first country to have a World Bank Poverty Reduction Support Credit (PRSC). This has been utilised by government and partner donors to identify government actions to improve service delivery via the budget process. It is anticipated that the PRSC will be broadened over time to cover all poverty-related activities. The key point, though, is that the PRSC matrix represents a unified framework of agreed reform measures. These have been developed and monitored through an explicitly agreed set of 'Donor Partnership Principles' which in turn derive from the wider partnership principles included in the PEAP Vol. III and are fully in keeping with the Organisation for Economic Cooperation and Development/Development Assistance Committee (OECD/DAC) guidelines for poverty reduction.

Andhra Pradesh

115. Nationally, Andhra Pradesh is seen as a pace setter for reform. It was the first Indian state to articulate a comprehensive vision when it released 'Vision 2020' in 1999. Vision 2020 is an ambitious statement of intent to pursue economic growth, social development and poverty reduction. The programme of reforms supported by GBS aims to strengthen the efforts of Andhra Pradesh to operationalise Vision 2020 and is consistent with efforts by the Government of India to stimulate fiscal reform in the states. In India, the Government of India is a key player in the process of fiscal reform and must be a party to any agreement between donors and state governments on fiscal adjustment. The states derive a large proportion of their revenues (50–60 per cent in some cases) through federal transfers. In

addition, their ability to borrow is determined by the centre. Since GoI is in effect the lender of last resort to state governments it has an interest in the progress of fiscal adjustment reforms at state level at a time when fiscal sustainability is by far the most serious macroeconomic issue facing the country.

116. The policy matrix associated with the Andhra Pradesh GBS Programme is not regarded by GoAP as a summary of conditionalities. Indeed, the term ‘conditionality’ in relation to GBS is unacceptable to the state government, reflecting the very strong domestic ownership of the reform agenda from which the matrix is drawn. The reform actions against which progress is monitored and GBS tranches are released needs to be seen in this light. All stakeholders refer to the matrix as a means of focussing on the key reforms that need to be undertaken. However, the political difficulty of many of the reform measures being considered in Andhra Pradesh indicate the extent to which the reforms, and the decision to enter into discussions about GBS-type financing, have been crisis driven. The main incentive to engage with the World Bank and DFID in GBS discussions is clearly fiscal crisis and the increasing difficulty of meeting recurrent commitments. Contributing to this, the harder line now being taken by GoI on state finances has reduced the prospects of unconditional bailout by the centre. In relation to the cash flow difficulties being faced by the state government the financing now on offer by DFID/WB through GBS is therefore significant.

117. As with Uganda, the nature of dialogue associated with GBS in Andhra Pradesh has shifted away from specific aid-funded interventions towards cross-cutting issues of public sector management and ways and means of implementing Vision 2020. What is different is that this takes place around an agreed agenda and list of priorities (the policy matrix) and in shared forums rather than on a bilateral basis with each donor.

3.3.3 Refocusing capacity building and technical assistance

Uganda

118. With the reduction in the number of projects, the level of technical assistance (TA) and capacity building dedicated purely to project management and coordination has declined in Uganda. Compared with the situation of five years ago, technical assistance is now dedicated to a much greater extent reinforcing and building capacity for mainstream activities of government, such as macro-economic management or sector planning. There remains a relatively high level of technical assistance – particularly in MFPED – but government closely and effectively manages this, so that, in the best cases, it genuinely supplements the knowledge, skills and energies at the disposal of senior policy makers.

119. To a substantial extent, TA is still subject to distinct funding arrangements, that is, it is not funded through ordinary budget allocations to the relevant ministries or departments. This is not only the case of expatriate staff contracted directly by donors and seconded to ministries, it also applies to activities and staffing that require salaries to be paid that exceed civil-service limits, and are projectised to allow this to happen. Important cases in point are the Poverty Monitoring and Analysis Unit (PMAU) that has added significantly to capacity in the Economic Affairs Directorate of the Ministry of Finance, and the management of the Uganda Participatory Poverty Assessment Process (UPPAP).

120. This is a recognised issue, and an aspect of the current GBS arrangements that is clearly out of line with principles but recognised as inevitable during a transition period. The duration of this period will depend on the progress that is made with civil-service pay reforms to permit competitive salaries to be paid in key areas.

121. In short, the inputs and activities identified in Level One are most clearly in place in Uganda, making it an important test case for the linkages that follow in the GBS concept.

Andhra Pradesh

122. As has already been noted, in Andhra Pradesh the ‘projects or GBS’ debate does not apply. There is not the expectation, as a result of GBS, that the nature of donor TA or the number of projects will alter significantly. The level and kind of TA provided by DFID to Andhra Pradesh has therefore not changed significantly as a result of GBS. This is perhaps because it was already substantially focused on strengthening mainstream activities.

123. An additional £0.5 million of DFID technical assistance was approved to support preliminary analysis, design work and one-off studies on key elements of the programme to complement an already substantial portfolio of existing DFID TA in support of the GoAP reform programme (e.g. power sector reform, public enterprise reform, revenue reforms, governance reforms and the strengthening of poverty analysis and monitoring). However, the existing TA portfolio is seen as being largely complementary to the objectives of the GBS programme (this is particularly the case of the Centre for Good Governance in Hyderabad). This also explains why the overall financial amount allocated to additional TA within the GBS programme is relatively small.

3.4 Level Two: what have been the immediate results of budget support?

124. The GBS conceptual framework postulates that budget support should empower government in its relations with donors and that this should be manifested through:

- greater Government control over externally-funded activities and resources
- a relative strengthening of the Ministry of Finance, the Cabinet and Parliament as drivers of public resource allocation
- coordinated behaviour by donors around the PRSP and partnership agenda.

125. It seems clear there has been progress in each of these areas, at least in Uganda. We take the first two issues together, principally as they apply to Uganda, and then deal with the third.

3.4.1 Is Government in control?

126. As compared with the situation prevailing in 1998/99, the coverage of the Uganda budget is wider. Fewer externally-funded activities are off-budget, and fewer of the funds passing through the budget are subject to separate disbursement conditions (as opposed to ‘notional’ earmarking). Therefore, external flows are being governed to a greater extent by the Government’s own resource-allocation process presided over by the Ministry of Finance, subject to decision making by Cabinet and approval by Parliament.

127. Some of the most notable changes are in what happens at the sector level, where the debate over resources is now firmly situated within the budget process. Previously, outcomes tended to be determined by a combination of two dialogues, one between sector ministries and donors, and another between sector ministries and MFPED. Now, it is not just formally the case that MFPED must approve all donor financing,[33] but MFPED takes quite an active and substantive interest in the fit between a particular offer of donor funding and the overall plans of the sector.

128. MFPED and Cabinet factor-in the availability of external funding when setting sectoral ceilings within the MTEF. Having done so, they can – and do – refuse additional offers of grant funding that would exceed the corresponding ceilings.[34] Allocations within these sector ceilings are decided by Sector Working Groups, in which donors, civil society groups and parliamentarians are formally represented. Hence, donors have a voice over resource allocation but it is a voice that is formally integrated within the budget process and circumscribed by a clear set of documented partnership principles.

129. That this has empowered GoU in a significant way seems beyond dispute. Some comments heard in Kampala, taken at face value, might suggest otherwise. These begin with the correct observation that GoU is not a single, fully-coordinated actor. GBS has given an impetus to a particular dynamic that is strongly owned by certain parts of Government and not others. This dynamic has the effect of making certain ways of acting within the Government system less attractive and even impossible – notably the free-wheeling approach to project funding that some line ministries have traditionally adopted.

130. In this process, some official actors may feel significantly disempowered, and in particular instances they may indeed have been so in the short run. A good example would be the position of the Ministry of Agriculture, Animal Industry and Fisheries (MAAIF) during and immediately after the formulation of the Plan for the Modernisation of Agriculture – in which MFPED took a very strong hand. However, this is not a zero-sum game, and arguably all government actors stand to gain in the medium term, as they learn to operate within the new rules. In any case, empowerment of Government can only be sensibly understood as enabling public policy and expenditure-management processes to operate as they are supposed to do within a parliamentary democracy with a Cabinet system of government. Thus, the objection should not be taken at face value, but more as a sly commentary on the perils of words like empowerment and ownership.

131. The results that have been achieved in the above areas are substantial. But they have been achieved over a relatively short time. Not surprisingly, the extent of change is limited in some respects, and there are some significant short-term constraints to further progress. Some of these have to do with shortcomings of the mechanisms that have been put in place to deliver on the basic vision. We signal those here. Others have to do with donor behaviour, and are discussed in section 4.4.2.

[33] The Development Committee within MFPED has been formally required to approve all projects, whatever their level of inclusion in the budget process.

[34] This is moderated by the transitional, 'two-tier' approach to MTEF ceilings described in section 2.2. Even moderated in this way, however, the policy is quite controversial, as witness the debate in the Ugandan media at the time of the O'Neill/Bono visit in May 2002 about the treatment of grants from the Global Fund and other potential gifts by external sources in money or kind.

132. The issues about mechanisms fall into two groups:

- Some remaining limitations of the instruments by which MFPED engages line ministries (and, now, district councils) in the implementation and further elaboration of the PEAP, using the levers provided by the MTEF, the budget and the PAF.
- Ongoing challenges concerning the way Government relates to the wider constituency of PEAP stakeholders as it reviews and elaborates the policies encompassed by the strategy, and the effects this has on the level of policy ownership outside GoU circles.

133. The details on these snags and challenges do not need to detain us.[35] The important point is that they exist – that building commitments across Government and among other national stakeholders to poverty reduction goals is not instantaneous. The immediate results of GBS include giving a stimulus to promising processes of change that begin to put decisions in their rightful place within Government. But it is very much a matter of beginning; these are ongoing processes, not one-shot gains.

134. As has already been noted the degrees of government control and legislative oversight over budget systems are both weaker in Mozambique. The Mozambican Ministry of Planning and Finance is judged to be in a relatively weak position to effectively discipline spending ministries. The view that budget ceilings are not hard constraints over ministerial spending patterns is widespread, both among donors and government officials. Off-budget expenditures and revenues represent a significant proportion of total resource flows, partly as the result of continued donor support for project-related capital expenditures. There is also currently little effective oversight of budget implementation, either by the Mozambican parliament or by the judicial body responsible for monitoring budget execution, the Administrative Tribunal. The main problems are capacity constraints and a poor financial information system.

135. In Andhra Pradesh, GBS does not increase ownership of the budget and policy process compared to the non-GBS scenario as proposed by the evaluability framework. Ownership was already strong in Andhra Pradesh. There is recognition, however, that GBS shifts the balance of power towards the Department of Finance that is one of the main drivers of the reform process. It is recognised among observers that in empowering the Department of Finance GBS could disempower line departments, but donor TA and ongoing projects are seen as helping to address this issue (e.g. the DFID-funded Centre for Good Governance, which is currently supporting a functional review and Medium Term Expenditure Framework for the Department of Education). More importantly, it needs to be recognised that in Andhra Pradesh, GBS is enabling the restoration to the Department of Finance of its rightful ‘challenge’ role in relation to policy making and resource allocation.

136. In short, GBS promotes coordinated behaviour around Vision 2020. However, there are fewer donors active in each state in India compared to other countries where DFID operates so the benefits of cooperation may not be significant. Nonetheless, through GBS there is the possibility of increasing DFID’s policy influence through association with larger World Bank financing. The extent to which this benefit will actually materialise is difficult to say. Attribution is generally recognised as a difficult issue.

[35] They are discussed at some length in the Uganda PSIA demonstration exercise draft report (Booth et al., 2002: Appendix 1).

3.4.2 Donor coordination and partnership

137. On donor behaviour, there are three particular sources of concern. The first is whether the World Bank's PRSP-oriented lending instrument, the Poverty Reduction Support Credit (PRSC) is functioning in the most appropriate way. The second concerns the strong element of de facto conditionality remaining in GBS provided by bilaterals. The third is about the role of earmarking within GBS.

The PEAP/PRSC relationship

138. According to some observers, the PRSC and its related Policy Matrix and associated review processes differ little from the structures of adjustment lending of the 1980s and early 1990s, despite being linked to the PEAP. In this assessment, the level of detail in which policy commitments are specified is far greater than would appear to be consistent with a PEAP-based partnership, which ought to focus on the results of government actions, rather than on the details of their design and implementation.[36]

139. There are different views on whether this is the case, and if so what is driving it. Some suggest it reflects a 'business as usual' attitude at the World Bank, with either staff attitudes or ingrained mission styles preventing adoption of the more hands-off approach espoused by senior management. However, other commentators suggest that it would be a mistake to see the level of specification as an external imposition. They see it as, just as much, a reflection of the interests of the 'hard-core reformers' within MFPED, who wish to use the PRSC as a method for ensuring firm government commitment to the reforms they believe are needed.

140. This can be put a slightly different way. Several donor and GoU commentators (within and outside the central agencies) described the PRSC simply as the implementation plan for the PEAP.[37] In this view, the root of the problem lies in the combination of a relatively general poverty reduction strategy with a detailed and specific PRSC. The level of detail of the PRSC derives directly from its function, with its narrow ownership being an unfortunate but virtually inevitable consequence.

141. Whatever is driving the trend, many commentators agree that it is not conducive to broad-based ownership of reforms within government nor to arm's length partnership by the International Financial Institutions (IFIs). These same commentators see the current situation as operationally stable only because of the close alliance of interests between MFPED, Bank of Uganda (BoU) and the IFIs (closely supported by DFID). This narrow base of ownership is seen as vulnerable both to significant rifts between MFPED/BoU and other parts of government – notably the President's office – and to large-scale personnel changes amongst the senior officials in MFPED.

[36] These observations (on the functioning of the PRSC in Uganda) apply equally to the functioning of the World Bank PSAL in AP and the way in which it has determined the process of the design and monitoring of budget support in AP.
[37] In AP, the Policy Matrix is considered to be simply (the salient parts of) an implementation plan for the relevant Government policy statement, *Vision 2020.*

142. A possible way forward would be to sharpen up the PEAP so as to make it more explicit about the process and pace of reforms necessary to achieve poverty reduction. It might not be easy for such a programme to gain approval through the same broad-based participation process from which the current PEAP emerged but that risk might be worth taking, as it would provide a way of broadening ownership of the policy field currently occupied by the PRSC. That in turn might result in the commitments in the PRSC policy matrix being treated with greater urgency than has been the case, and being associated less with irritating aspects of World Bank mission style.

143. The enhancement of bilateral donor coordination is clearly one of the most important benefits of the budget support programme in Mozambique. Earlier informal attempts to promote donor coordination in the provision of other forms of programme aid in Mozambique were formalised in 2000 with the establishment of the Joint Donor Programme (JDP) for Macro-Financial Support. The donors currently involved in this programme (the 'G10') are the UK, Belgium, Denmark, the European Commission, France, Ireland, the Netherlands, Norway, Sweden and Switzerland. Two bilaterals participate in meetings as observers, namely Portugal and Germany. The IMF and the World Bank are also actively involved.[38] The agreement setting up the JDP recognises that donors should attempt to reach multi-year agreements on macro-financial support and that this should be channelled through the state budget. A specific objective of the programme is to support the government's poverty reduction programme, as articulated in the PARPA (Action Plan for the Reduction of Absolute Poverty, which is Mozambique's PRSP). The government clearly recognises the practical and political advantages of being able to negotiate with a group of donors over future resource flows (see comments of Minister of Planning and Finance in Box 3).

The re-emergence of political conditionality

144. Bilateral and EC budget support is linked in a less problematic way to the PEAP but is not thereby wholly controlled by the government. In particular, it has been shown to be subject to strong informal conditions that go well beyond the requirement to remain on-track with the Bank and the Fund. These conditions have related in particular to political factors, specifically the continued involvement of Ugandan troops in the Democratic Republic of Congo and the southern Sudan as well as concerns over the delay in ratification of the new Leadership Code.

145. These are all issues that for various reasons have raised concerns amongst development NGOs and opposition parties in Denmark, Ireland and other parts of Europe. These concerns have in turn placed under scrutiny the high level of financial support currently provided to the Ugandan Government. As a result of these concerns the Government of Denmark declined to join the budget support arrangement and specific tranche releases by the European Commission and by Ireland Aid have been delayed.

[38] The World Bank's involvement is likely to be further enhanced in 2003/04 when it begins to implement its own form of direct budget support linked to the implementation of a Poverty Reduction Support Credit that will support both cross-cutting reforms and sector spending. Closer involvement by the World Bank is regarded by other proponents of budget support as an important factor in gaining further leverage over the government's reform programme.

146. It is not our role to question the wisdom or otherwise of these decisions. The key point at issue is that decisions on budget support financing were taken as a result of developments *outside* of the framework of the PEAP, the PRSC and the partnership principles. The GoU rightly points out that by opening up the range of conditions which might justify delaying or stopping financing, government control of the process is lost and a structure of potentially arbitrary conditions is created.

Earmarking within GBS: whether and what for?

147. The third point of concern relates to constraints over government ownership arising from the earmarking of budget allocations. Strictly speaking, this is notional earmarking, in that resources are all channelled through the government treasury and accounting system and are not subject to disbursement controls. However, there is a wide range of agreements related to the levels of resources to be allocated to the Poverty Action Fund (PAF) and to the use of resources within the PAF.

148. The intensity of this earmarking places strict limits on the level of discretion held by the Budget Director and, as such, infringes ownership. Moreover, it could well be argued that such earmarking restricts the allocation of public resources unnecessarily, with potential efficiency losses, and should not be required in a framework where there is genuine agreement over objectives and priorities.

149. It can be argued, however, that earmarking, even if notional, has several advantages from the donor's point of view. Notably, it provides some limited political back-covering in donor countries (limited because of fungibility). For example, the development Minister of country X can claim, and expect to be believed up to a point, that country X supports the education sector of country Y, while recent procurement scandals in country Y are in the health sector and therefore nothing to do with country X. Secondly, sectoral earmarking is said to provide sector specialists in donor offices with a 'mandate' that would otherwise be lacking to get engaged in policy work and monitoring in the corresponding sectors or cross-cutting areas.

150. The first argument may have some force. However, the second is not very convincing in the Uganda context. PEAP Vol. III recognises that donors sometimes earmark notionally in order to be able to participate in sector reviews, but deflates this by committing GoU to the principle that 'all donors who are providing fully flexible budget support, or flexible PAF support, should be invited to participate in the review of any sectors where they can contribute useful expertise'.[39]

3.5 Level Three: what have been the medium term institutional effects?

151. In the conceptual framework, it is postulated that GBS will have a 'positive transformative effect' upon governance. It is further suggested that this will be manifested in 1) reduced transaction costs in financing spending through development assistance, 2) increased allocative efficiency in public spending, 3) increased predictability of budget funding, 4) increased effectiveness of the state and public administration, and 5) strengthening of democratic accountability. We examine each of these issues in turn and consider their plausibility in relation to current programme realities.

[39] Uganda (2001: 72).

3.5.1 Have transaction costs fallen?

152. The concept of 'transaction costs' is of crucial importance in development assistance and, more broadly, in the economics of contracts (and hence of markets, trade and the whole process of growth). Reducing the transaction costs of aid has a particularly prominent place in the Government of Uganda's vision of the shift from projects to budget support. However, they are notoriously difficult to measure. Box 4 summarises the conclusions of what appears to be the only study that has attempted to measure the transaction costs of aid delivery.

153. Notwithstanding these obvious difficulties, this seems to be an issue of considerable importance in judging the impact of GBS. Essentially, the concept aims to capture the aggregate cost of the administrative activities involved in providing development assistance, which have no value either to the recipient government or to the donor other than to permit an aid transaction to take place (some donor-recipient interactions may, of course, have substantial value in themselves). Clearly, all development assistance will have some transaction costs and in most cases donors and the recipient government will share these. In postulating that GBS will 'reduce the transaction costs of financing spending through development assistance', we are therefore stating that the move from projects (or sector programmes) to budget support will either reduce the sum total of transaction costs or will alter the way these costs are shared in favour of the Government.

Box 4: Can we measure transaction costs? At what cost?

Brown *et al.* (2000) seems to be the only study that has attempted to measure transaction costs of aid delivery in order to test the hypothesis that these costs fall as foreign assistance moves away from projects. It tries to document what happens to transaction costs as aid delivery mechanisms switch from projects to more programmatic forms of support.

In the relevant theory, four characteristics of transactions are seen as important in influencing costs: frequency, complexity, uncertainty and specificity (Doan and Lestrange, 1998; Williamson, 1998). In order to capture these characteristics, Brown *et al.* (2000) developed surveys and carried out interviews. These covered:

- the number of (non-TA) projects,
- the number of reports (review, progress, final, evaluation),
- the number of meetings,
- the number of steering committees; and
- the total time key civil servants spent on aid administration vs. policy making.

While these indicators appeared to make intuitive sense, it proved to be very difficult to gather quantitative information on them.

Difficulties arose partly from the fact that there is no tested methodology for measuring them, and partly from problems of availability of data. In Vietnam, some respondents were unwilling to take part, and all found it very time-consuming to complete the questionnaire. Government respondents found the quantitative questions impossible to answer, as none were able to break down or cost their time according to the distinct activities identified. This experience suggests that monitoring transaction costs quantitatively is unlikely to be cost-effective, or even meaningful.

Reproduced from Naschold (2002).

154. In the course of brief field visits drawing evidence predominantly from interviews, it was of course not possible to make any measurement of the change in transaction costs. The issue of how best these costs might be measured remains an important one to be resolved in any future evaluation work. However, in both Uganda and Mozambique it was virtually the unanimous view of the Government and donor staff interviewed that transaction costs *had* fallen with the shift to budget support. They pointed in particular to the significant reduction in project-related missions (design, monitoring, evaluation) and related reporting, to the closure of significant numbers of project implementation units and to the strengthening of planning units that has resulted from the consequent reassignment of staff.

155. On the other hand, in Uganda the point was also made that a whole new structure of sector working groups and associated scrutiny processes has been created instead, and that these have also proved to have relatively high transaction costs. In the two years of their existence, there had been 'almost an excessive interest in consultation without attention to the costs of this process'.[40]

156. In Uganda, no person interviewed disputed that the ways in which these meetings are managed and information distributed are considerably less efficient than they should be and that improvements are needed. However, the general view was that most are in the process of becoming more efficient. For example, in the sectors where such processes are most advanced (education and health), sector reviews are now annual rather than six-monthly, agendas are prepared well in advance and the meetings are well focused. Also, there was some recognition (also reflected in PEAP Vol. III) that involvement of donor personnel in sector working groups and joint reviews can have significant benefits, in terms of improved policy making, which outweigh the associated costs.

157. It is of some interest that, within the donor group for Uganda, it has been explicitly recognised that it is in large part the sheer number of donors that keeps transaction costs at a high level. Accordingly, several donors have started to adopt shared responsibility for portfolios.[41] For example, in the education sector, DFID has been representing the Netherlands over the last two years and, as of August 2002, both DFID and the Netherlands will be represented in the Education Sector Working Group by the education adviser of the European Commission. Similar arrangements are at work in the health and law and order sectors involving other donors too.[42]

[40] Some observers would say this applies without reservation to the Andhra Pradesh GBS process. Little attention appears to have been given to making changes in donor (WB/DFID) operating procedures (essentially, how they collaborate and how they interact with GoI and GoAP). There is a strong flavour of DFID following the Bank, which is in turn following standard Bank mission practice. As a result, the effectiveness of donor cooperation is said to be highly dependent on the personalities involved, and GoAP is considered by more than one source to be visibly tired of the lack of coordination, method and structure to the GBS design/monitoring process.

[41] The Mozambican Minister of Planning and Finance placed particular emphasis, in her interview, on a) reducing the number of external donor missions with which officials had to be concerned – which she expected to happen as a result of the Joint Donor Programme – and b) that too little emphasis was still being placed on evaluating the results of the Government's programme, as opposed to reviewing inputs and mechanisms.

[42] If they contribute to the next tranche of GBS in AP, the Dutch are considering delegating some of their dialogue/monitoring responsibilities to DFID.

158. In Andhra Pradesh, channelling donor funds through the state treasury system does not address any significant issue of transactions costs associated with donor financing. This argument applies more in countries with large numbers of aid projects and a multitude of donors each with their own reporting schedules and accounting requirements – leading to excessive transactions costs. As mentioned above, in Andhra Pradesh project and sector aid is seen as having a number of advantages that may help counter some of the problems of the Andhra Pradesh budget system.

159. However, it was the view within DFID-India that the new structure of working with the World Bank, which now involved a much wider group of DFID advisers, was generating transactions costs (see footnote) which in the early years of GBS were likely to be high. The Dutch who are co-funding a budget support programme in Kerala with the Asian Development Bank reported similar 'start-up' difficulties. The formal agreement of coordination and joint working arrangements between donors involved in budget support arrangements would seem to be the obvious solution. These learning effects aside, it was generally perceived that the transactions costs in relation to the level of financing provided through GBS was likely to be much lower in the long run compared to the same amount of funding provided through projects.

160. Overall, then, the situation on the ground does not give strong reasons to doubt the conclusions of earlier research work which argued that 'transaction costs are generally higher for programme than for project aid – at least in the first few years of a sector programme' (Foster *et al.,* 2000). However, the conclusions of this earlier work arose principally from the comparison of traditional projects with free-standing Sector Programmes (or SWAPs). The comparison was not with GBS, of which there was too little experience to report at the time. On the evidence from Uganda today, it does remain plausible that the relative shift in funding towards budget support will eventually reduce transaction costs, if it has not done so already.

161. Three further observations emerge from the Uganda experience, which are consistent with the conclusions of Foster's earlier work:

- The form of policy dialogue that requires partners to have an appropriate level of input at both central and sectoral levels is in most cases a new process that will generate transactions costs of its own. In the early years of budget support, these transaction costs are likely to be high.
- If the number of projects is not simultaneously falling then in aggregate there will be an increase in transaction costs.
- Finally, it is important to recognise that transaction costs do not fall automatically: deliberate attention is needed to how consultation processes are organised, how information is distributed and how decisions are organised. Efforts by donors to 'team up' in their use of sectoral advisers will also help to reduce transaction costs.

3.5.2 Has the efficiency of resource allocation improved?

162. The conceptual framework postulates that a shift towards budget support will promote improvements in the efficiency of resource allocation. There are three principal reasons why this might occur.

Government priorities

163. Most importantly, the re-establishment of the national budget process as the dominant system of resource allocation should ensure that resources are allocated more closely in line with government priorities. National priorities will thus override donor priorities and the influence of tied aid policies (formal or informal)[43] will be reduced.

Reducing gross misallocations of resources

164. A second positive allocative effect arises from the fact that fungibility in resource allocation is considerably higher in the national budget than in donor project structures. This means that there is greater flexibility to address allocative efficiency questions both in initial allocations, and through re-allocations during budget execution.

165. The restrictions on fungibility in a project structure generate allocative inefficiencies even where donors' priorities are fully consistent with Government's. For example, the allocation of aid resources through project structures tends to favour allocations for capital investment, and results in under-funding of the recurrent costs necessary to realise the benefits (at the extreme for example, roads with no maintenance, etc.). Such misallocation would only arise out of a deliberate choice when using the national budget system.

166. Additionally, resources channelled through a donor project structure cannot easily be redirected in the event that the projects are delayed or stopped for any reason. Within the national budget system, all that would be required to redirect these resources would be a virement order or a re-allocation warrant.

Process improvements

167. *Ex ante,* it is impossible to specifiy what is likely to be the optimal allocation of budget resources for meeting an objective such as poverty reduction.[44] However, a good budget process can help to identify gross misallocations and build experience on what does and does not seem to work. Thus, it will be important if GBS inputs can be shown to be supporting ongoing improvements in the national budget process. This is plausible. GBS should result in improved and more structured dialogue on policies and spending priorities, better focused technical assistance and increased importance being given to the national budget process. Where the budget is the 'only show in town', public sector managers, ministers and parliamentarians will focus upon it. As a result, there is more scrutiny and more debate and this should over time have an impact on the efficiency of resource allocation.[45]

[43] Most bilateral donors have renounced the formal tying of aid to own country procurement. However, casual observation suggests that informal links must remain relatively strong. Moreover, several donors refer to their 'comparative advantage' as a criterion in the inter-sectoral allocation of aid resources. If donors' comparative advantages correspond to Government needs, this presents no problem, but in most circumstances it is likely to lead to a supply-driven allocation of resources.

[44] Fozzard (2001).

[45] It will be interesting to monitor the relative performance of Uganda and Mozambique in terms of allocative efficiency. In Mozambique, budget support is quite clearly not 'the only game in town' and there is potentially a far wider set of influences over total resource flows to key poverty-related sectors such as health and education. This is an issue that deserves to be analysed more fully in the second phase of this study.

168. In summary, budget support should give greater prominence to Government priorities, enhance the degree of flexibility over resource allocation and strengthen the budget process itself. All of these changes should serve to improve the efficiency of resource allocation. This improvement may be measured both by the consistency of inter-sectoral allocations with stated priorities and by improvements in the composition of the budget, in terms of the economic classification of expenditures.

Evidence for Uganda

169. Tables A3 and A4 and Figures A1 and A2 in Appendix 1 examine changes in the inter-sectoral allocation and in the composition of spending by economic classification in Uganda before and during the recent expansion of budget support. The data presented there are strongly suggestive of improvements in the efficiency of resource allocation. The absolute and relative level of resources utilised on activities covered by the Poverty Action Fund has consistently increased over the period, suggesting clearly that stated national priorities, and recognised areas of previous under-spending, are getting budgetary priority.[46] The shares of spending allocated to basic health and basic education in particular have risen continuously, although this is now slowing.

170. In terms of the economic composition, the relative balance of capital and recurrent spending is broadly constant, with the share of Development Expenditure rising gently over the last five years. However, the share of Salaries and Wages in recurrent spending has also tended to increase, with the effect that the shortfall in operations and maintenance expenditures that was continuously reported in Public Expenditure Reviews of the early 1990s may remain a problem.

171. Some care is required in interpreting these data. For example, it is in principle possible that with an increasing level of resources coming on-budget, what is being witnessed is an improved recording of an underlying structure of allocations that may not have changed. In other words, it may be that health and education expenditures that were off-budget at the beginning of the period are now financed through the budget, with no change in inter-sectoral allocations.[47]

172. Nevertheless, these data would seem to support the conclusions of Foster and Mijumbi (2002), which point to significant improvements in the management of public expenditure and in the level of budgetary priority accorded to poverty-reducing expenditures.

[46] In Mozambique, a shift in expenditure to priority sectors identified in the PARPA (equivalent of PRSP) can also be seen – see Vol II: Country Case Studies Table 2. Expenditure on priority sectors as a proportion of total expenditure rose from 55.2% in 1999 to 66.2% in 2001, and the share of the education and health sectors rose from 26.4% in 1999 to 34.2% in 2001. However, the extent to which these shifts can be attributed to the move towards direct budget support, rather than to the more general commitment to the implementation of the PARPA, is not clear.

[47] The Ministry of Health estimates that overall funding for the health sector has been static at around $15 per capita from all funding sources. This contrasts with the $28 per capita needed to finance a basic package of health-care services through Government and NGO units (Uganda, 2002b: Chapter 5). The Ministry's planners nevertheless argue convincingly that the increased Health budget has made possible significant improvements in allocative and operational efficiency, and in equity, in the last few years (Uganda, 2002c).

Evidence for Andhra Pradesh

173. In the case of Andhra Pradesh, it is important to recognise that GBS will not have an effect on that portion of the GoAP budget whose content is determined by GoI. Some 40 per cent of the GoAP development (capital) budget is accounted for by 'State Plan Schemes' – i.e. vertical programmes run by the centre.[48] In the low-aid dependency and federal environment of India, DFID needs to interact simultaneously at state and central level if it is to influence the *overall composition* of the GoAP budget. This issue is not discussed at all in the Andhra Pradesh programme document. However, there is evidence that the *processes* associated with GBS may be able to help in this regard. DFID advisers and staff have pointed out that GBS negotiations with GoI (on the consistency between the Policy Matrix supported by GBS and the Government of India's Fiscal Reform Programme) have, for the first time, given them significant access to those GoI officials involved with the GoI-funded portion of the GoAP budget. This has reportedly permitted some entry to discussions around the effectiveness of central resource allocation and monitoring.

3.5.3 Has the predictability of funding increased?

174. Increased predictability of funding flows has a central place in the logframe of 'new' GBS for two reasons. Firstly, the critique of project aid and conditionality-based programme aid includes the claim that, for different reasons, these previously dominant modalities are bad at delivering funds to recipients in a predicable way. Secondly, non-predictability of funding is generally recognised as one of the principal factors undermining the seriousness of public planning efforts at all levels in poor countries. While some of the sources of unpredictability are domestic and are being tackled by the MTEF and arrangements such as Uganda's PAF, recipients continue to complain that one of the major sources of unpredictability is the donors.

175. Is it clear that GBS is delivering greater predictability in Uganda? Unfortunately, not. At least, this is one of the more problematic of the predicted changes within the logframe box on transformative effects on governance. A wide consensus of opinion in Kampala is that increased predictability is not something that GBS is delivering, or should be expected to deliver, under current conditions. The reasons have to do partly with technical characteristics that GBS shares with earlier forms of programme aid, and partly with the theme discussed earlier in connection with 'the re-emergence of political conditionality'.

The problematic relationship of GBS to predictability

176. It is clear that increased predictability of donor flows is not something that GBS guarantees per se. The fact that GBS providers now enter into three-year commitments that can be accommodated within the MTEF is highly beneficial in principle to the recipient. However, these commitments are not binding, even within-year. Moreover, GBS shares with other general programme aid some characteristics that can easily generate greater unpredictability than in the case of project or sector-programme funding. Because fungibility

[48] 2001/02 Budget Estimates. In Appendix III - Capital Receipts of Individual States – State Finances, *a study of state budgets 2001/02,* Reserve Bank of India, January 2002.

is greater, the donor's political exposure is considerably higher. At the same time, disbursement remains very flexible, so that it is administratively simple to 'turn off the tap' or restrict the flow in time or quantity. On these grounds, delivering predictability is in some ways *more* of a challenge when GBS is the dominant aid modality.

177. Whether the benefits are realised depends, therefore, on the willingness of donors to restrain themselves (or each other) from halting or delaying disbursements. This will be affected by the degree to which donors have broken with the conditionality mind-set and entered into a partnership relationship in which influence can be exercised without resort to explicit or implicit threats to turn off the tap. However, it seems unlikely, to most observers that the necessary degree of restraint will be able to be exercised, or the mind-set transformation completed. Part of the problem lies with current and expected conditions in Uganda and its region.

178. The sensitivity of GBS funding is obviously greater than it would otherwise be where political conditions in the recipient country and/or in the neighbouring regions are unstable. The combination of events in the recipient country that donors disapprove of with a change of government on the donor side is a particularly disruptive one, as decisions by Denmark illustrate. But even in the case of donor agencies whose policies have remained entirely stable – such as DFID or Ireland Aid – commitments are unlikely to be maintained without qualification under the impact of events such as the fighting between Ugandan and Rwandan troops in Kinsangani in 2001, not to mention other possible scenarios that informed observers consider quite realistic.[49]

179. Some donor opinion (and some Ugandan opinion) in Kampala tends towards the view that it is actually a beneficial feature of budget support, whether old or 'new', that it permits some leverage that can be used in a crisis to restrain the recipient government from dangerous decisions with potentially serious implications for the whole region. Those who take this view point to the successes of the UK Secretary of State in moderating Uganda/Rwanda tensions and getting Ugandan security issues into a healthier consultative framework.

180. Some observers add that these examples contradict the generalisation that political conditionality does not work. However, there is an alternative, subtler interpretation, which says, in effect, that they are the exceptions that confirm the rule. Disbursement delays were unquestionably involved, in both cases. However, it is arguable that the reason the UK Government's interventions were persuasive is that they were made in the context of a medium-term partnership in which ex ante conditionality was no longer a prominent feature and other important relationships had been built up.

[49] By contrast, in Mozambique the main concerns of donors contributing to the budget support programme since 2000 have been over domestic governance issues, such as corruption and financial sector scandals. Several donors explicitly wish to retain their ability to discipline government behaviour by retaining their right to withhold or delay funding.

181. If that is true, the difficulty of increasing predictability needs to be seen as one of several specific challenges in the current phase of GBS, reflecting its intermediate or transitional character – no longer conditionality-based, but not yet pure 'partnership' either. This theme is taken up in section 4.4.[50]

Managing lack of predictability in Uganda

182. The risk of events that provoke some or all donors to revert to a pure conditionality paradigm seems unlikely to be eliminated in the near future under the conditions prevailing in the Great Lakes region. Donors need to consider how to handle this risk, as argued in the next section. On the recipient side, governments are not entirely dependent on donor disbursement decisions, even under Ugandan-type conditions. For various reasons, GoU has accumulated substantial foreign reserves, which can be used to cushion any curtailment of budgetary support, as well as generally to smooth out fluctuations in disbursements. However, this is only a relative benefit. As Bank of Uganda officials point out, drawing on reserves can mitigate the impact of GBS shortfalls but does not replace the lost resources. It is also not in any way a prevention strategy.

183. The other way in which Uganda has managed the damaging effects of unpredictability (arising from domestic revenue variability as well as donor disbursement decisions) is with the PAF. By ring-fencing government and donor funds destined to priority sub-sectors and giving them priority when considering cash-limited disbursements within the budget year, the PAF mechanism has served to enhance predictability where (arguably) it most matters. From the beginning, PAF budget lines were accorded 100 per cent protection against in-year budget cuts; they now get a less rigid 95 per cent.[51] This is not an absolute guarantee of timely disbursement, as administrative delays still occur, but the large disparities between budget allocations and out-turns that arise under cash-limited budgets in other countries are eliminated.

184. The drawback is that recipients of PAF funds get their greater predictability at the expense of very low predictability for non-PAF budget lines – because actually available resources do often fall below expectations. This is increasingly recognised as a problem in Uganda, especially as the criteria for deciding the eligibility of budget lines for PAF protection have been quite simple and crude (a virtue, from a practical point of view) and therefore fallible.

185. Thus, it is possible to take the view that the PAF has been highly successful in bringing resource allocation into line with the Government's stated priorities but has been in aggregate bad for predictability, and possibly also for allocative efficiency. It may well have hampered improvements in the systems of ministries and departments that have generally

[50] GBS has not increased the predictability of budget funding in AP. While the programme has been designed within the context of a medium-term adjustment programme, approval of tranche release is annual. GoI has only given approval for one year's release of GBS to AP. Given GoI's concern about the allocation of aid at the national level to a few 'partnership' states, delivering predictability is likely to be more of a challenge with GBS compared to other aid modalities – at least in the present climate. GoAP is therefore vulnerable to adverse GoI or donor assessments of GBS and subsequent decisions to reduce or cease this type of funding from one year to the next.
[51] Uganda (2001: 25).

been excluded from PAF funding, as discussed in the next sub-section. In this sense, the PAF experience takes away nothing from the importance and urgency of improving the predictability of the funds flowing into the budget.

3.5.4 Have the state and public administration become more effective?

186. One of the strongest and most attractive claims made on behalf of 'new' budget support is that, by using national systems, it contributes to making these stronger – both more effective and more accountable. To what extent does this claim remain plausible in the light of Ugandan experience, becoming in this way a candidate for closer attention from evaluation studies, in due course? We feel able to give a generally up-beat response to this question, with the proviso that none of the linkages in the bottom half of the GBS logframe are automatic. All require additional conditions to be satisfied, or risks to be avoided. GBS provides a generally enabling environment but specific actions by a range of actors are likely to be required, and those providing GBS have a duty to spell these out.

187. The key lever of change is the focus on the national budget process, and the corresponding reduction in off-budget project financing. Because line ministries and districts no longer have the option of seeking direct funding from donors, or have it within a strict ceiling agreed in the MTEF process, they have a much stronger incentive to comply with budget directives. These now call for a more structured approach to policy development, the lynchpin of which is what are being called in Uganda sector-wide strategies. Sector-wide strategies become in turn the basis of Budget Framework Papers, which are the sector working groups' submissions within the MTEF, and ultimately for resource-allocation decisions in the budget. In respect of performance monitoring, these arrangements are in their infancy. But the potential is there for Government departments not only to be rewarded for raising their game, in terms of policy development and effective implementation, but also to be held to account for failing to do so.

188. As we have already indicated, some of the most notable institutional effects of moving to budget support concern the way sectors are managed. An important interim achievement that strikes many observers is the way effective lines of accountability within government have shifted. Increasingly, senior sector officials are answering to MFPED in the first instance, and only secondarily to sector donors, even in sectors with heavy donor involvement. Within sectors, programme officers are responding more to their formal ministry line managers, and less exclusively to external funders. These changes are said to be observable in the way individuals behave in meetings when both donors and Ministry of Finance officials are present.

189. By all accounts, this is not preventing effective involvement of donor sector specialists in the development of the sector-wide strategies. Without the need for the original type of SWAp common funding basket (and without some of the distortions arising from over-funding of SWAp sectors) donor-assisted planning units are raising their game significantly in a number of sectors and multi-sectoral areas. It is too early in most cases to record noticeable improvements in intermediate or final outcomes, and both survey data and the second-round Participatory Poverty Assessment suggest that conditions on the ground continue to be abysmal in many respects. Nevertheless, sector insiders claim improvements

in efficiency and expect further results despite what they acknowledge to be grossly insufficient funding.[52] The policies, at least, are notably improved in most opinions, in at least the areas of health, education, justice, law and order, water, roads and social development.

190. An important stepping-stone in improving sector performance is addressing cross-cutting governance issues affecting all forms of public service delivery. For example, within the health and education-sector working groups, improving the efficiency of procurement is now a hot topic. It seems that extra impetus to change in this area is gained when donors not only agree to only use the national systems, as would be the case in a traditional SWAP, but also try to address the big issues in a cross-cutting way.

191. The issue of procurement is one example among many of a difficult issue that still needs to be vigorously tackled if the medium-term institutional improvements promised by GBS are to be realised. The, until now, rather slow implementation of the results-based system of performance management in the civil service would be another. An important linked issue is the degree to which the sharpness and specificity of the PRSC matrix could be adopted into the PEAP, as a means of driving these kinds of changes forward in a more effective (because more consensual and less mission-driven) way.

192. Changes of this sort are very far from automatic. The argument expressed in the GBS logframe is not that the financial element of GBS alone makes them happen. It is only that it creates conditions in which active and intelligent use of the other GBS inputs (new policy dialogue and refocused TA and capacity building) can be effective. However, at present little has been written or formally articulated on what exactly works, what doesn't and why, when combining and recombining the different elements of the GBS package. Thinking through and spelling out what kinds of actions of this sort are both appropriate and effective will be an important part of the process of articulating the GBS vision.

193. In contrast to the Uganda case, actual evidence of improved management of the public finance system since 2000 in Mozambique is harder to identify. The most recent Public Expenditure Review in 2001 documents a wide range of fundamental reforms that are required, many of which have been incorporated into the new System for State Financial Administration (SISTAFE) that will be implemented from early 2003. As donors devote an increasing proportion of their aid budget to GBS they have become more concerned with systems of public financial management and with implementing reforms to strengthen these systems (which they previously effectively side-stepped by establishing their own project implementation mechanisms). It is too early to say whether the current programme of reforms will be successful in improving the effectiveness of public administration in Mozambique, but it is undoubtedly a step in the right direction and the fact that this issue is now nearer to the top of discussions between government and donors is a breakthrough in its own right.

[52] Indicative of possibilities in the health sector are MoH figures for 2001/02 showing a 40% increase in outpatient attendances, and DPT3 immunisation rates up from 40–63% in one year (Rob Yates, pers. comm.).

194. It is too early to make any judgements on whether GBS has led to improvements in public administration in Andhra Pradesh. However, there is some evidence that the Department of Finance is starting to implement the type of *process improvements* that are the necessary precursors of improvements to the efficiency of resource allocation. For example, in the education and health sectors the Department of Finance is demanding evidence, as part of the budget process, of the efficiency and effectiveness of existing programmes before approving the increases in budget allocations that are now possible as a result of GBS.

3.5.5 Has democratic accountability become stronger?

195. It may well be the case that the ways GBS helps to improve governance are initially most noticeable within the Executive branch of government. Changes affecting broader relationships of accountability, including those between the Executive and Parliament, may be slower to come. There is, nevertheless, a strong interdependence between the two types of change. Big-picture democratic accountability is very unlikely to improve if there is no line-management reporting and accountability within the Executive. The one thing is a precondition for the other. Improving intra-Government accountability may therefore be the most important thing to monitor even if one is ultimately aiming at a broader and more substantial change in the way political and civil society interacts with Government.

196. Let us consider, all the same, whether or not the experience of Uganda supports the notion that GBS is more or less conducive to domestic democratic accountability than projects and sector programmes. This calls for two preliminary observations.

Approaching the question

197. Firstly, we pose the question quite deliberately in relative terms. There are solid grounds for thinking that aid dependency generally creates perverse incentives that reduce government effectiveness (Moore, 1998; Moore et al., 1999). To some degree, these effects may be unavoidable, whatever the modality, supporting the policy position of countries like India and South Africa of avoiding aid dependence. But we postulate (as Moore, 1998, does) that they are likely to be worse where disbursement arrangements fragment fiscal sovereignty and undermine budget accountability.[53]

198. Secondly, the interactions between external and domestic accountability are probably not a zero-sum game. Depending on its form, an increase in accountability to donors might be quite favourable to a growing domestic accountability, helping this to become strengthened at the same time.

199. The second point is highly relevant to the Uganda case, because most observers seem to think that the weight of external accountability has increased as a result of GBS. Donor representatives are present in large numbers in a host of different policy forums, and some play highly influential roles as advisers or collaborators of key ministries. In

[53] For further details, see GBS literature review (Naschold, 2002: 28-29).

aggregate, the donor voice is listened to and taken more seriously than when it took the form of a series of bilateral dialogues about projects or programme aid conditionalities.[54]

200. However, it does seem that domestic accountability is improving at the same time. Some of the relevant changes are long, slow processes with their origins in the Constitution-making process of the early 1990s. In spite of its formal constitutional powers, Parliament has not until recently played a very effective part in scrutinising the budget and monitoring its implementation. However, MFPED has tabled a new Finance Bill to implement Constitutional commitments. It has also initiated a capacity-building programme to provide the Budget Committee with the technical back-up it lacks. When these changes feed through, it is likely that parliamentarians will become more actively and effectively involved in the results-oriented debates in MTEF sector working groups, as well as in the formal process of approving the budget, than they have been in the past.

201. Auditor General's reports, too, are said to be improving. The Public Accounts Committee is becoming more active in following up cases of misappropriation highlighted in them, and a new parliamentary committee – the Local Government Accounts Committee – is now performing similar functions in relation to districts. The press, even though partly government-owned, is increasingly open in criticising public corruption and the insufficiency of action to curb it. These are all promising, if not yet decisive, developments. Moreover, while they have independent origins, they undoubtedly gain strength from the fact that a greater share of total public expenditure is captured in the budget and is subject to a common system for monitoring execution and results.[55]

Reasons for caution

202. Obviously, it is not possible to consider the prospects of substantive improvements in democratic accountability in Uganda in the coming years apart from the different scenarios that can be entertained about the Museveni succession and the debate about multi-partyism. There is much to play for and there are many risks. In the best of conditions, Uganda is likely to enjoy a limited, neo-patrimonial form of democracy (van de Walle, 2001); that is, one in which the legal and illegal spoils of office continue to be used systematically to buy votes and reward followers. Corruption is likely to remain for some time yet a near-universal feature of the interaction between government, the private sector and the citizenry, as informed observers say it is now.

[54] A similar process of change in levels of external accountability can be seen in Mozambique, where the Joint Donor Programme for budget support is beginning to result in more effective bilateral donor engagement with the Government over the policy agenda, as recognised by the Mozambican Minister of Planning and Finance.

[55] These arguments may also apply in AP, but to a much lesser degree. Generally, the accountability gains proposed in the evaluability framework do not apply in India as they do in more aid-dependent countries. Unlike many countries in which DFID works, the problems of accountability in India do not derive primarily from excessive off-budget donor support.

203. It is good not to have illusions about these things, or about the ability of either donor-promoted safeguards or democratic pressures to eliminate them quickly. A relevant example is that of the regular expenditure tracking studies that have a central place in the package of fiduciary safeguards agreed by GoU, DFID and other GBS donors. We would not say that it is wrong under Ugandan conditions to agree to a limited set of fiduciary monitoring instruments, or that tracking studies are a bad choice of instrument. However, insiders who know 'how things work' within GoU tend to doubt the robustness of conventional tracking exercises. They do not accept that tracing disbursed funds to their intended destination provides assurance that monies are actually being spent as agreed, even with the active transparency that has been adopted by MFPED (publishing disbursements in newspapers, etc.). The possibility needs to be considered that funds have means of trickling back up the chain of intermediaries as a means of repaying the favour of disbursement.

204. The main message from all this is to confirm that, while the benign effects of GBS are quite genuine, they are no means automatic. Not only are there upcoming political risks (and opportunities, as some of our informants were keen to add) that will affect the actual level of democratic accountability greatly. There is also huge scope for donors, by utilising fully the complementary GBS inputs, to reinforce actions by national stakeholders to influence the outcome for the better.

205. On the whole, we think this is less likely to work if it rests on a more complex set of fiduciary requirements. In the final analysis, fiduciary rules are subject to the same objections as other forms of conditionality: that if domestic political constituencies support them, they do not need to be externally imposed, and where they do not, they will not be effective.

NGO concerns

206. We deliberately began with Parliament in discussing democratic accountability. We would generally want to see any evaluation of democratic accountability paying attention to political as well as civil society, and not restricting the latter to NGOs. Nevertheless, there is a place in this discussion for the role of national and international NGOs. In Uganda, NGOs have played and continue to play an important role in debating the PEAP and keeping the Government's eye on the ball when it comes to PEAP implementation. The Government-NGO partnership that has been responsible for UPPAP, and the influence this has acquired, is one of the most successful features of the set-up around the PEAP.

207. It is relevant, therefore, that some and perhaps most NGOs in Uganda are currently very concerned about the trend of thinking and practice among bilateral donors, particularly DFID.[56] They argue that the limited capacity to call the Government to account that they have enjoyed in the past has been based on their position as major service providers that are not dependent on Government funding. They maintain that, as official donors move funds from projects, including NGO projects, into GBS, they will be obliged to become contractors to Government – mostly local government, which has a probably justified reputation for being the most corrupt and arbitrary. (It is assumed that there is limited space for NGOs devoted entirely to advocacy, and that authority to participate in policy

[56] This was picked up in discussions with a handful of NGO informants. However, for a particularly clear written presentation based on a much wider range of interviews, see Lister and Nyamugasira (2003).

development comes from knowing sectoral realities first-hand.) In this process, they will lose the autonomy vis-à-vis Government that makes them effective as interlocutors and critics.

208. NGOs are making a compelling case for thinking there might be a downside to the GBS-accountability relationship. Particularly, there is a genuine concern about getting fatally enmired in the kickback culture of district government. There is another view. This accepts that policy influence comes from knowing a sector and having experience on the ground, but questions the importance of 'autonomy'. The NGO view as summarised above involves some self-delusion about the actual level of independence and power enjoyed by NGOs in the past, and the fixation on autonomy reflects a mechanical and mistaken view of how influence is exercised. The way to influence Government is to work with it, and to be there at the right moment with good policy ideas, not to distance oneself deliberately and shout louder. This is persuasive except that it does not address the kickback problem.

209. This, of course, is a new rendering of an old debate in the NGO world. It remains to be seen whether NGOs in Uganda will find ways of handling their changed roles, by building new alliances, in the GBS context. GBS may and may not affect negatively the relationship between Government and NGOs. This is another issue where the outcome is not automatic, and deliberate action by GBS stakeholders is called for.

3.6 Risks and other external factors

210. As the above analysis demonstrates, across a variety of sectors and at different levels of the logical framework, the shift towards budget support in Uganda appears to be having a positive impact of broadly the expected sort. There remain gaps. The shift from conditionality to partnership is only just beginning, if it is genuinely present at all, with little progress on predictability. However, on the other hand there are signs of an increasing empowerment of government in relations with donors. It also seems plausible to expect a variety of positive transformative effects on the quality of governance. Although we have not discussed the bottom of the logframe, a continuation of those trends seems certain on theoretical grounds to produce in due course some enhancement of government capacity to reduce poverty.

211. Given these apparent successes, and the considerable efforts made by government and donors to achieve them, one of the most striking features of the Uganda situation is how fragile the whole GBS process appears, in the opinion of many close observers. At a variety of levels, there appear to be serious risks to the continuity and continued success of the GBS process.

3.6.1 High-level political risks (Uganda)

212. The most obvious of these relate to the potential suspension of GBS payments, in response to the deployment by GoU of military forces in neighbouring countries or as a result of continuing concerns over corruption. As we have already noted, it was for reasons of this kind that Denmark declined to start a budget support operation in 2002. Similar events have also been the cause of temporary suspensions of payments by Ireland and

by the European Commission in the recent past and have also been the source of warnings by the UK Government.

213. There are a variety of views among different commentators over the gravity of these risks. Officials of Ireland Aid, the Netherlands, Denmark and the European Commission all expressed serious concerns over these risks, noting that they derive not only from the potential for 'unacceptable' actions by GoU but also from the instability of donor policies due to their vulnerability to pressure from parliaments and NGOs. As we have said, GBS is a high-profile form of aid especially since it is perceived as much more fungible than project aid and hence easily subject to misuse. The fungibility of project aid is generally not perceived by parliaments and NGOs and, by and large, there is limited awareness of the negative institutional effects of projects. In these circumstances, it is difficult for development agencies to defend the provision of direct financial support to governments that are not perceived as exemplary.

214. Staff interviewed at DFID and the World Bank expressed a broadly more positive view of the situation, pointing out that many differences over policies have been satisfactorily resolved through negotiation and diplomatic actions. They also said that the track record of GoU in relation to both economic and political governance was strong. Some GoU commentators agreed with this position but argued that the problem of inconsistency in donor behaviour remains.

3.6.2 Lower-grade risks (Uganda)

215. The judgement of the study team is that the risks discussed above are serious. However, they are by no means the only concerns that would need to be identified in the right-hand column of a fully-fledged logframe matrix for Uganda GBS. This is what we mean by saying that the changes identified in the conceptual framework are non-automatic.

216. For the most part, however, the risks that are present at different levels of the logframe can be 'internalised' in the planning and management of budget support. That is, it is possible to develop appropriate response strategies that would substantially reduce the probability of these risks occurring.

217. Table 1 illustrates this suggestion. It lists the key risks identified by the study team, outlines their likely consequences, assesses the potential for a response and makes some suggestions as to what the response strategies might be. Clearly, it is a superficial analysis of risks that are inherently complex but it does serve to illustrate that by identifying risks in advance and seeking actively to internalise them in the planning of budget support the vulnerability of GBS arrangements can be reduced.[57]

[57] It also suggests that some further analysis of the 'External Factors' box presented in our conceptual framework would be warranted.

Table 1: Risks to the budget support process in Uganda and possible responses

Nature of risk	Consequences and potential for response	Possible response strategy
Level One: Inputs		
Political Risks: Funds not disbursed because of actions by GoU unacceptable to donors. Funds not disbursed because of change of policy by Donor governments. *Managerial Risks:* Policy dialogue breaks down because of changes in personnel on donor or government side. Technical Assistance for capacity building proves ineffective.	If short gap in disbursements, climate of distrust is created; if longer, whole GBS policy would come into question. Limited potential for response in current structure because political risks are not pre-identified and discussed. Honest policy dialogue is essential to the GBS process and systems would quickly breakdown in its absence. Clear potential to improve breadth of dialogue. TA plays important role at present but probably not essential in GoU case.	Advance clarification or discussion of areas of concern and of uncrossable 'red lines'. This may clarify risks and reduce the potential for apparently arbitrary ex post conditions. Give clearer briefing to domestic parliaments and civic groups on risks and implications of GBS. Broadening of the range of participants in policy dialogue, building on success of Sector Working Groups and PEWG. Broadening of ownership of PRSC through integration into updated PEAP Attention to quality of TA and to Govt control over use of TA.
Level Two: Immediate Results		
Donors adopt increasingly un-coordinated positions on GBS. Differences of focus/ level of detail between PRSC and PEAP lead to breakdown of donor support for PEAP.	Consequences would depend upon number of donors involved and their importance but possible 'domino effect'. Neither GoU nor DFID are well geared up to respond. PEAP is the core of GBS process and must continue to be respected and supported. DFID and IMF may have some influence over GoU and WB in relation to PRSC.	More coherence must be promoted in donor objectives and approaches on GBS: DFID (possibly with EC) needs to gear itself up for this advocacy role. Updating of the PEAP (to include more detail) may help to prevent perceived divergence between PEAP and PRSC.

Nature of risk	Consequences and potential for response	Possible response strategy
Level Three: Medium-term institutional effects		
Presidential initiatives are introduced outside of budgetary framework. Leakages of funds are documented through fiduciary system and not acted upon.	Obvious breaches of the structures of democratic accountability would receive high attention, despite ongoing improvements in other areas. Would almost certainly lead to breakdown of GBS process. Response is crucially dependent on maintenance of influential position of MoFPED and BoU	The consequences of breaches of democratic accountability appear to be well understood by the President and his advisors (including advisers in MFPED and BoU). Some broadening of this understanding would be wise, through Cabinet retreats, Parliamentary briefings, etc. This can only be initiated by GoU.
Levels Four and Five: Intermediate and final poverty outcomes		
Coffee prices remain low Dutch-disease effects harm export terms Poor private sector investment response, due to low confidence. Civil service performance fails to improve because of continued incentive problems. Service delivery does not improve because of continued governance problems at Local Government level.	Negative impact on growth & rural poverty. Very difficult to respond. Potential negative impact on growth & rural poverty. May help relative reduction in external financing. Negative short and long term impact on growth. Difficult to address directly. Will impact on service delivery and quality of public administration. Has proven an intractable problem. Poor service delivery means bad services for the poor. Needs continuous attention from a variety of fronts.	Opportunities for diversification need to be created – not straightforward. Current MTEF already plans for relative reduction in external financing of budget. Improved coherence in GoU policies for trade & private sector development. More active attention to corruption. Requires combination of pay reform, improved performance management and improved mechanisms of accountability. Strengthening of local-level incentives, performance management structures & accountability systems. Concerted actions across line ministries, local gvts., civil society and Auditor General.

3.6.3 Risks in Mozambique

218. There are considerable concerns in Mozambique, too, regarding risks to the sustainability of budget support. On the donor side, these currently seem to spring from two main sources:

- short-term concerns about government liabilities in the domestic banking sector, where two previously state-owned banks have run into serious problems due to unrecoverable loans and will require recapitalisation – these are linked to broader and longer-term concerns regarding governance and high-level corruption
- concerns about the extremely weak financial management system (particularly at sub-national levels) and whether current reform efforts will be successful within the time-scale envisaged – and hence the merits of channelling increased resources through an untried and untested new budgetary process.

3.6.4 Risks in Andhra Pradesh

219. There are a number of issues that could affect the longer-term success of the GBS programme in Andhra Pradesh. The main issues that became apparent during the case study were as follows:

- Predictability. No agreement over levels of medium-term funding has been reached with GoI. GBS effectively has a one year time horizon and has to be negotiated with GoI each year. Donors describe this annual tranching of budget support as a risk mitigation strategy. However, it is in reality dictated by GoI who have not yet permitted donors to make multi-year GBS commitments. For GoAP, the predictability of budget support in these circumstances depends on GoI's policy stance on GBS, the content of the policy matrix and associated monitoring indicators, and the process of programme review by stakeholders against the matrix. We discuss these latter two points, in turn, below.
- Monitoring. GBS funds over the medium term are predictable only to the extent that performance and reforms at state level are assessed as being 'on-track'. Although the main monitoring tool is said to be the programme policy matrix, it is not clear how this will be applied in practice. It is not reflected in any programme documentation. Given that performance across the policy matrix is likely to be asymmetric and some targets are likely to be more significant than others, there is need for greater clarity in the way in which the programme will be monitored.
- The sequencing of programme review, tranche processing and dialogue needs revisiting. In Andhra Pradesh the current process involves (1) reviewing progress on policy matrix targets for Year One about six months into it (2) making an assessment about whether or not to release GBS and processing that tranche during the remainder of Year One. This is an extremely tight timetable and probably one that is unsustainable both in terms of what it is possible to review at the six-month point and in the time it allows for dialogue with government. The process needs stretching out.

4 PRELIMINARY CONCLUSIONS ON LESSONS LEARNED

4.1 Introduction

220. The three case studies have, as expected, proved to be quite different. Nevertheless, the framework has proven quite robust in the face of the ‘programme realities’ of GBS in Uganda, Mozambique and Andhra Pradesh.

- In Uganda, not only does it capture in a coherent way the objective that GoU, DFID and other donors are pursuing; it has also proved a useful tool for identifying and explaining the pattern of change. Most of the suggested linkages remain plausible, and thus are candidates for more thoroughgoing evaluation. This is not to say that they are yet fully functioning, and predictability remains a particular challenge.
- Mozambique is arguably travelling the same road as Uganda, but is a good deal further from even the intermediate destinations, meaning that there is little scope for probing the plausibility of the linkages further down the logframe diagram.
- Both the rationale and the reality of GBS in the low aid-dependency scenario of Andhra Pradesh are distinct. Nonetheless, the Andhra Pradesh case study did find the framework useful and relevant in several respects. Predictability is also a problem in Andhra Pradesh. Some of the reasons are the same (old-style conditionality thinking still very much in evidence), while others are particular to State–Centre relations in the Indian case.

221. What have we learned from all of this? Three particular lessons stand out. They are supported mainly but not exclusively by the analysis of the most advanced experience, that of Uganda:

- Firstly, ***different governments and donors are pursuing quite a variety of objectives through the use of budget support.*** This is understandable but probably has some opportunity costs. If greater consistency could be established over objectives and hence over management mechanisms then it seems likely that the impact would be greater. This calls for more clarity in the presentation of objectives, more discussion over apparent differences and more active efforts to establish common objectives.
- Secondly, the Uganda experience shows ***that few, if any, of the postulated positive effects of budget support are automatic.*** Incentives are changing in the right direction, and agents can be expected to respond to incentives, but complementary measures are surely needed. The more attention that can be given to coordinating, management and monitoring structures (the careful use of TA and capacity building to support endogenous changes), the more likely it is that these positive effects will be realised to the maximum.
- Finally, ***the ‘operating rules’ for general budget support need to be more explicitly stated and agreed in advance.*** A prior condition for completing this exercise would be a more honest assessment of the operating context – the Uganda experience suggests that it would probably be wrong to describe this as a conditionality framework but nor is it ‘partnership’ as commonly described.

4.2 Objectives need to be more clearly stated and more widely shared

222. GBS processes must necessarily be pursued on a multi-donor basis. This is still more true when partner governments are aiming to use GBS as a way of changing the composition of aid financing, establishing common structures for policy dialogue and promoting institutional development processes to enhance government capacity to reduce poverty. In short, if the objectives of budget support are those presented in our Logical Framework, then these can only be achieved when they are shared by the recipient government and its main external funding agencies.

223. We noted in section 4.2 that, even in Uganda, where the government holds a clear and well-articulated policy on the use of budget support, there is some ambiguity over the precise objectives of different donors. In the absence of such a clear lead from government, we would not expect even this degree of clarity among donors about the purposes of moving to GBS and about what is new about 'new' GBS. Outside Uganda, budget support continues to be seen very largely as a 'macro-economic' tool – as a mechanism for transferring large-scale resources and for reaching agreement over economic and fiscal policy objectives. This view of budget support is not in any sense wrong but it is certainly very partial. In particular, it ignores the many opportunities which the shift to budget support presents for promoting positive institutional development processes.

224. Uganda presents a concrete example of the operation of these institutional development processes. Although we have argued that the Ugandan GBS process remains relatively fragile, it seems reasonable to predict that, if it survives and develops further, the long-term benefits of the resulting institutional changes would be of considerably greater significance to Uganda than the immediate macro-economic impacts.

225. Promoting awareness of the empowerment and institutional development impacts of budget support ought therefore to be given higher priority by DFID and other development agencies. We would recommend three elements of a strategy to achieve this:

- Firstly, ensure that institutional development objectives are properly captured and presented in DFID's own Project Memoranda for GBS arrangements.
- Secondly, Governments need to take on board the positive institutional benefits that GBS can bring. DFID might assist this by engaging with partner governments – within PRSP review processes, for example – to establish indicative targets for the key result areas where change is being pursued and by jointly monitoring progress over time.
- Thirdly, an active advocacy programme is needed with other donors. This would probably be best pursued in conjunction with the European Commission, which has some status as a coordinating body for the main European bilaterals and largely shares the DFID perception of the role and potential opportunities for budget support.

4.3 Results are not automatic: attention to detail is required

226. The second lesson which emerges from Uganda may appear as a contradiction of our assertion that the shift to GBS should be seen as an institutional development process,

which changes power relations between Government and donors and changes institutional incentives. We have no doubt that this is true but an appreciation of the historical context is also needed.

227. Aid dependency is not a recent phenomenon in most developing countries. Thus, the perverse incentives that aid dependency creates have been operating for a long time and often in contexts of weak state capacity and fragile, neo-patrimonial political institutions. To reverse these incentives and (re-)create capable states is a long process and there is nothing inevitable about it. The positive incentives that GBS may create can be easily blunted or perverted. Our analysis of the risks confronting the GBS process at various levels illustrates some of these possibilities.

228. Nor is it simply a case of dusting off old government systems and procedures to make them operational again. There are some developing countries that have never been characterised by good governance. Even when there is a legacy of good governance, this may well have been in a context of a less globalised economy, a smaller population, and an intrinsically simpler Government agenda. Moreover, GBS itself creates a need for new institutional structures – in particular structures for consultation and for performance monitoring.

229. Political and institutional context is important. The institutional challenge which is implicit in the GBS process – the challenge of creating capable states which can manage external and domestic resources effectively to reduce poverty – is a very difficult one, for which new skills, ideas and paradigms are needed. Our work does not provide a real basis for making judgements on this issue both because the sample is too small and because Uganda is the only case out of the three where each of the three ‘inputs’ of the budget support process could be said to be fully in place. However, the three case studies in their own way illustrate very powerfully the importance of institutional context. Thus, realising the benefits of budget support requires focused and coordinated government and donor actions across a number of areas, and a close attention to the detail of institutional structures and procedures.[58]

230. There are three specific aspects of the Uganda experience that illustrate how much attention to detail is required, whilst also demonstrating the benefits this can bring.

- Given that budget support is so commonly perceived as a ‘macro-economic phenomenon’, it is interesting to note that ***the most striking example of the improvements resulting from GBS is probably at the sector level.*** The sharp reduction in off-budget spending brought about by the GBS process combined with the creation of Sector Working Groups (SWGs) has permitted rapid advances in the quality of policy and spending. This is especially true in the education and health sectors where these processes are most advanced but is also noticeable in other

[58] Does this introduce the risk of misinterpreting the direction of causality – i.e. that reforming governments transform their systems of governance, thereby attracting budget support, and that ongoing improvements in governance should not be attributed to GBS? Potentially yes, but we are not postulating that the shift to GBS is any more than a facilitating factor in promoting capable, accountable governments. The challenge in taking this work further in Phase 2 will be to find ways of taking account of the effects of differing institutional environments, so that the direct impact of the change in aid modalities can be assessed.

sectors. What is also interesting is how quickly the agenda of the SWGs has evolved. Policy dilemmas have been essentially resolved, consensus has quickly been reached over the appropriate intra-sector resource allocations and the agenda now is about service delivery. How can procurement be improved to speed up delivery of medicines? How can classroom utilisation be most effectively increased? How can school building costs be reduced? However, these successes have been built upon hard work by government and other partners – attention to the detail of the Memoranda of Understanding governing how sector groups operate, careful attention to information and how it is analysed, presented and circulated; and a willingness to confront problems – for example, over raising expenditure allocations to the facility level.

- ***Attention to service delivery questions has highlighted the significance of cross-cutting administrative issues –*** recruitment and staff posting systems, pay and performance monitoring, procurement. SWGs could only partly address these and they have not been well catered for by the PRSC design and monitoring process, or by the Poverty Eradication Working Group (PEWG). At the time of writing GoU and donors are still working to find an appropriate mechanism for leading a 'joined-up' process of improvements in these areas.
- To a significant extent, ***the front line of service delivery in Uganda is at local-government level and there has been a continuous process of reforms to raise the accountability, efficiency and effectiveness of local government.*** This began with an ambitious decentralisation of powers, which then needed to be partly reversed in recognition of the gaps in capacity and in accountability at local level. Major attention is now being given to the application of 'readiness criteria' for the decentralisation of authority over staff and resources.[59]

4.4 Operating rules need to be clearer: not conditionality but not 'partnership'

231. The final lesson that emerges powerfully from the Uganda experience is the need to clarify as honestly and transparently as possible what the operating rules for the provision of general budget support should be. Once these rules are clarified and agreed, it is then necessary to respect them in order to establish some consistency in the relations between government and donors and as a result some predictability in the provision of funding. We noted in section 3.4.1 that the GBS process in Uganda has failed to create a situation that could be accurately described as 'coordinated behaviour by donors around the PRSP and the partnership agenda' and we argued in section 3.5.3 that one significant consequence of this was a continued lack of predictability over funding levels. Our analysis of risks in section 3.6 hinted at some of the causes of this situation.

[59] A similar concern about the impact of budget support on the centralisation/decentralisation of public expenditure decision-making processes is evident in Mozambique. This is an issue of particular concern due to (a) the strong evidence of significant disparities in the regional/ provincial distribution of poverty in Mozambique, (b) concerns about the political will of the central government to respond to local needs in areas of the country which are opposition strongholds and (c) additional concerns about the lack of effective public expenditure management systems to ensure that budgeted resources actually reach intended local beneficiaries. The ways in which a concerted move towards centralised budget support might impact upon current distributional outcomes are complicated (both at a conceptual level and also in terms of measurement) but are nonetheless a potentially important factor in determining whether this form of aid will be more effective in reducing poverty than other modalities. This aspect of budget support might be of concern in other geographically large countries, where the government's ability to deliver services effectively is poor.

4.4.1 The reality of the partnership model in Uganda

232. Ostensibly, budget support is provided according to a pre-defined schedule in support of a Government-led PEAP and following a set of agreed partnership principles. In practice, there are significant differences from this idealised ‘partnership model’:

- Firstly, most external funding agencies want a greater influence over the definition of policies and spending programmes than this model implies. This is manifested in particular by the detailed specification of the PRSC – theoretically the implementation plan for the PEAP, but actually more hard-hitting in many respects – and the heavy involvement of the World Bank and other agencies in this process.
- It is also manifested by the active involvement of donors in sector working groups and in the PEWG.
- For the most part, this detailed involvement by donors is welcomed both by GoU and by civil society stakeholders. The former emphasise the value of the technical inputs provided by donors, the latter speak of the value of the additional checks and balances which donors can bring.[60]
- In addition to this detailed involvement, there has been considerable concern expressed by the European Commission and by the European bilateral donors over ‘political actions’ related to deployment of armed forces and action on corruption. These ‘political actions’ fall outside of the agenda of the PEAP and the partnership principles. Despite this, they have been the basis for withholding of budget support (Danish Government), delaying of payments (Ireland and European Commission) and threats to delay or withhold budget support (UK Government).
- To a significant extent, the response to these political actions by the European Commission and the bilateral donors has been driven by domestic parliamentary pressures and/or by media or pressure group actions in Europe.

233. Clearly then, the de facto operating rules are not those of the ‘partnership’ which has been defined. Some commentators suggest that this could be characterised as a return to old-fashioned conditionality. Our judgement is that such a description is not accurate either. In relation to the detailed bargaining over the PRSC matrix, it should be noted firstly that many GoU and civil society commentators describe this as a helpful and necessary process. Secondly, it should be stressed that, although releases of funds for the PRSC tend to happen after the negotiation of an updated Policy Matrix, they are in fact based upon prior conditions. So there is not the one-to-one ‘buying of policy change’ which is a characteristic of conditionality.

234. In relation to the actions taken by the EC and the European bilaterals, these have not been justified by the failure to comply with conditions specified *ex ante* but in general in response to actions which were not part of the original financing agreements. It is certainly true that in subsequent negotiations new conditions have been agreed and have generally been followed – the completion of the Security Sector Review being a significant example.

[60] The reasons for the GoU and civil society support to detailed donor involvement in policy and budget processes are clearly more complex than this. We acknowledge this whilst not pretending to understand the stakeholders or their motivations.

However, when conditions are established after the suspension of budget support, there is the possibility of choosing conditions over which agreement can be easily reached and where compliance is virtually assured. An alternative interpretation is that these conditions have been introduced not to force changes in Uganda that would not otherwise have happened (the classic definition of conditionality) but rather to appease domestic constituencies in Europe.

4.4.2 Understanding the organisational rules and incentives

235. We would contend that the concepts of 'conditionality' and 'partnership' – at least as currently defined – *both* tend to confuse the understanding of the situation and may be hindering attempts to establish clarity over operating rules. The reality of the operating context is considerably more complex. It is not amenable to analysis as a two-party contract as conditionality is normally presented (with donors and multilaterals on one side and government on the other). Still less is it a 'one-party contract', as partnership is often depicted (with donors and Government on the same side).

236. We would suggest that the partnership framework that typically surrounds GBS arrangements is probably better understood as a *multi-stakeholder club.* In this context, the concepts of the economics of organisations can usefully be applied – in particular the concepts of 'exit', 'voice' and 'loyalty' (Hirschmann, 1970; Arrow, 1974).[61] In addition, it is important to take explicit cognisance of the role of donors' domestic constituencies, which in the case of Uganda have proven that they can play a powerful role. Thus, the key features of the Ugandan Budget Support 'club' might be described as follows:

- Just as in the case of an organisation, club or firm, the boundaries of the agenda that need to be embraced in joining a budget support arrangement are too broad to be fully captured in a contract. It may help to try to specify the agenda more fully but there will always be unpredictable elements. Hence, 'loyalty' must be based on shared aspirations and shared objectives. It seems unlikely that a framework could be found which might condition this loyalty *ex ante.*
- In such a setting, loyalty is influenced by the extent to which members are able to actually influence the agenda – hence 'voice' becomes important. In Uganda, this is well catered for in principle by the structures that exist for the definition of the PRSC and by the sector working groups and PEWG.
- Members always retain the potential for 'exit', but this clearly has its costs. For GoU, costs are especially high but for the agencies providing the largest amounts of budget support – notably the World Bank and DFID – they are also considerable. For those contributing smaller amounts, the exit costs are likely to be smaller because the impact of their withdrawal on the Government's economic programme will be less, because the investment already made in developing budget support arrangements is smaller and because the consequent loss of face from withdrawing is lower. The predictability of the budget support arrangement depends in large part on increasing the costs of exit. The extent to which partners will accept this will in turn depend on the extent to which they are convinced that objectives are shared – not just at a

[61] There are also many more recent applications of these concepts within the participation literature in the theory of the firm.

general level but also in detail, and the extent to which they believe they have a real voice over the evolving agenda.

- The existence of influential (Northern) domestic constituencies presents a significant problem to this sort of organisation. Clearly, these constituencies can only be considered reluctant partners, if they are partners at all. Certainly, their loyalty is quite limited. The response must therefore be to either make them more active members of the process – through improved information and through advocacy – or to create a more arms' length relationship, so that they have less influence over the exit capacity of their development agencies.

237. This is of course a simplification of a complicated organisational framework. For example, it does not provide an easy way of analysing the relative roles of different GoU stakeholders within the budget support club. Clearly the analysis requires some adaptation and development. However, we would contend that it is a more useful framework than the idealised partnership model and the classic conditionality model.

238. We would also contend that the Uganda experience supports the view, now well established in the literature, that conditionality does not work as a method of buying policy change.[62] Specifically, there is nothing to suggest that the threat of withholding budget support (or the actual act of withholding it) has forced the GoU to undertake policy reforms that it would not otherwise have taken. Certainly, donors have been influential in determining both the pace and content of reforms. But this influence has not been bought: rather it is the manifestation of the voice that has been granted to donors and other stakeholders by GoU. A voice over policy and budgets has been willingly granted by the GoU because of its recognition of the strength of mutual interests and of the value of encouraging donors to buy into the GoU agenda, through the joint venture that we have described as the budget support 'club'.

239. The previous point (section 4.3) on the importance of political and institutional analysis bears repetition in relation to the loyalty/exit/voice approach to conditionality. The agenda of budget support is necessarily broader than can be specified in a contract and must therefore be based on as thorough an analysis as possible of the economic, institutional and political situation. Table 2 summarises the key issues that need to be considered in the design of an operating framework of a multi-stakeholder club for budget support.

Table 2: Clarifying the operating framework – the multi-stakeholder club

Loyalty	GBS implies support for an agenda that cannot be fully specified	Understand partners better – motivations, constraints, risks
Voice	If agenda cannot be fully specified then consultation and influence should be guaranteed	Comprehensive structures for consultation need to be developed. Uganda = good model
Exit	In return for voice, some limitations on exit should be in place	Controls on exit are needed to protect predictability, which is crucial to poverty reduction

[62] See Chapter 3. Also Naschold (2002).

4.4.3 Implications for Uganda and for GBS arrangements elsewhere

240. This analysis clearly has wide-ranging implications, not only for Uganda but also for budget support arrangements in other aid dependent countries. Perhaps the least contentious implication is that more analysis is needed of the organisational and incentive structures that shape decision-making within the budget support process. This analysis should aim to enhance understanding of the factors at work and to facilitate progress towards transparent and effective operating rules for budget support.

241. Beyond this, there are a number of further implications we would draw which are more contentious and, at this stage, inadequately researched. Nevertheless, we present them by way of a contribution to the debate that, without doubt, is urgently needed.

- Firstly, it is time to leave the conditionality paradigm behind. Many donors enter into budget support arrangements in the belief that the threat of their withdrawal would be sufficient to force necessary policy changes, if so required. History does not suggest that there is much basis for this belief. So long as donors continue to hang onto it, the chances of moving to genuinely predictable budget support arrangements are undermined. Moreover, ***it may create a false level of security amongst donors entering into budget support processes, leading in turn to an inadequate initial diagnosis of risks and potential problems.***[63]
- Secondly, we would argue that some refinement of the partnership paradigm is required to capture the complexity of the process. ***This should explicitly capture the fact that partnership embraces many actors, who must have a minimum level of loyalty to a shared agenda; that some voice over the agenda is required and some restrictions over the potential for exit.***
- In this process, the nature of the shared agenda is too complex to be fully specified in a contract or agreed matrix of actions. By lending their loyalty to a budget support process, partners are effectively lending support to a Government as a whole and, by implication, to its entire agenda. It is better that this should be fully recognised. Governments must realise that the more fully their agenda can be specified, the more confidence there will be to support it. Moreover, where it cannot be specified, support can still be maintained so long as there is voice – an open channel of communication.
- On the other hand, donors need to realise that there will probably be aspects of the Government agenda that they will find unacceptable. They need to be prepared for this and to have a clear sense of what an appropriate response would be in these circumstances. They also need to let Government know in advance of diplomatic, legal and/or fiduciary concerns which would limit their ability to support the Government programme.
- The role of domestic parliaments and pressure groups needs to be explicitly recognised by donors and factored into their GBS processes.

[63] This would appear to be the case in Mozambique, where the extent of analysis of the public finance system by the G10 donors does not seem commensurate with the level of risk of GBS. It applies also to AP, where only a preliminary state financial accountability assessment (PSFAA) was made prior to GBS. This was undertaken by, and its circulation largely restricted to, the World Bank.

- In Uganda, the structures by which partners in the GBS process may express their voice are exceedingly strong. For other aid-dependent countries moving into budget support, it is important to take note of how valuable to the budget support process these mechanisms of voice are but also how difficult they are to create and develop.
- ***There is an implicit trade-off between the capacity to influence the government agenda (voice) and the ease of exit from the process.*** In Uganda, the time has probably arrived for Government to place more explicit restrictions on exit – for example, requiring annual GBS disbursements to be guaranteed six months in advance of the fiscal year and to be subject to suspension within-year only under the most exceptional circumstances, if at all. Some partners may choose not to participate in such an arrangement but the gains in predictability would probably offset the costs of some early exits from the GBS process.
- In other countries, where GBS is less advanced than in Uganda, further improvements in voice would probably have to precede additional restrictions on exit.

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APPENDIX

Statistical data for Uganda

Table A1: Uganda data sheet

Land area	sq. km.	197,096
Population, 2002	million (projection)	23.4
Urban population, 2002	%	17.2
GDP at factor cost, 2000/01	million USh, 1991 prices	3,725,835
Av. annual growth, 1996/97–2000/01	%	5.46
Av. annual growth per capita	%	2.8
Annual inflation, 2000/01	%	4.5
Gross reserves, 2001	months of imports	4.4
Coffee in total exports, 1999	% of value	58.91
Coffee in total exports, 2000	% of value (provisional)	31.20
Non-traditional exports, 1999	% of value	28.09
Non-traditional exports, 2000	% of value	47.38
Poverty headcount, Uganda, 1992	%	56
Poverty headcount, Uganda, 1997	%	44
Poverty headcount, Uganda, 2000	%	35
Poverty headcount, North, 1992	%	72
Poverty headcount, North, 1997	%	60
Poverty headcount, North, 2000	%	66
Stunting in children, 1992	%	51
Stunting in children, 2000	%	40
HIV prevalence rate, 2000	%	6.1
Total fertility rate, 2000	children	6.9
Adult literacy, 2000	%	65
Female adult literacy, 2000	%	57

Sources: MFPED, *Uganda Poverty Status Report, 2001;* MFPED, *Background to the Budget, 2001/02;* MFPED, *Summary of Background to the Budget 2002/03/Uganda PRSP Progress Report 2002.*

Table A2: Budget support and project support, Uganda 1992/93 – 2002/03 ($m)

	1992/93	*1993/94*	*1994/95*	*1995/96*	*1996/97*	*1997/98*	*1998/99*	*1999/2000*	*2000/01*	*2001/02 projection*	*2002/03 projection*
Budget Support											
Grants	81.20	35.63	54.54	36.25	65.55	129.54	63.96	165.99	227.16	246.98	179.44
Loans	83.94	119.19	124.43	49.87	45.24	44.95	63.84	38.51	83.40	198.71	261.47
Sub-total	165.14	154.82	178.97	86.12	110.79	174.49	127.80	204.50	310.56	445.69	440.91
Project Support											
Grants	214.11	160	251.5	246	296.9	371.4	351.2	215.84	268.9	207	205.8
Loans	93.73	118	194.4	195	159.7	207	186.9	215.84	179.27	138	137.2
Sub-total	307.84	278	445.9	441	456.6	576.4	538.1	431.68	448.17	345	343.0
Total	472.98	432.82	624.87	527.12	567.39	752.69	665.9	636.18	758.73	790.69	783.91
Budget support as % of total	34.9	35.8	28.6	16.3	19.5	23.2	19.2	32.1	40.9	56.4	56.2

Source: Ministry of Finance, Planning and Economic Development, June 2002

Table A3: Trends in spending by sector and Poverty Action Fund, Uganda.
(% of Government Expenditure)

	1994/95 Out-turn	*1997/98 Out-turn*	*1998/99 Out-turn*	*1999/00 Out-turn*	*2000/01 Budget*	*2001/02 MTEF*	*2002/03 MTEF*
Roads and Works		4.9	6.2	8.2	9.2	8.9	8.6
o.w.PAF		1.0	1.98	1.99	2.03	2.00	1.97
PAF %		(21)	(32)	(24)	(22)	(22)	(23)
Agriculture		1.1	1.0	1.4	1.6	1.6	1.5
o.w.PAF		0.1	0.0	0.3	0.5	0.6	0.5
PAF %		(6)	(2)	(24)	(34)	(35)	(35)
Education		26.0	26.9	26.0	26.8	26.3	26.6
o.w.PAF		14.7	16.6	17.1	18.3	17.6	17.8
PAF %		(57)	(62)	(66)	(68)	(67)	(67)
Health		6.6	6.7	6.3	7.6	8.4	10.0
o.w.PAF		0.5	2.0	1.7	4.1	5.0	6.7
PAF %		(8)	(30)	(27)	(53)	(59)	(67)
Economic and Social		4.6	4.0	5.9	8.7	8.6	8.7
o.w.PAF		0.5	1.3	2.2	4.4	4.9	5.3
PAF %		(11)	(32)	(37)	(51)	(58)	(61)
Total PAF Share (%)		17.3	22.7	24.4	30.5	31.0	33.2

Notes: Total expenditure excludes externally financed development expenditures (i.e. project support), arrears, and promissory notes. PAF figures are for all categories of spending which were subsequently absorbed in the PAF, and are therefore consistent across time. Total PAF share includes categories of PAF spending not covered in the sectoral breakdown, and therefore exceeds the sum of the sector shares.

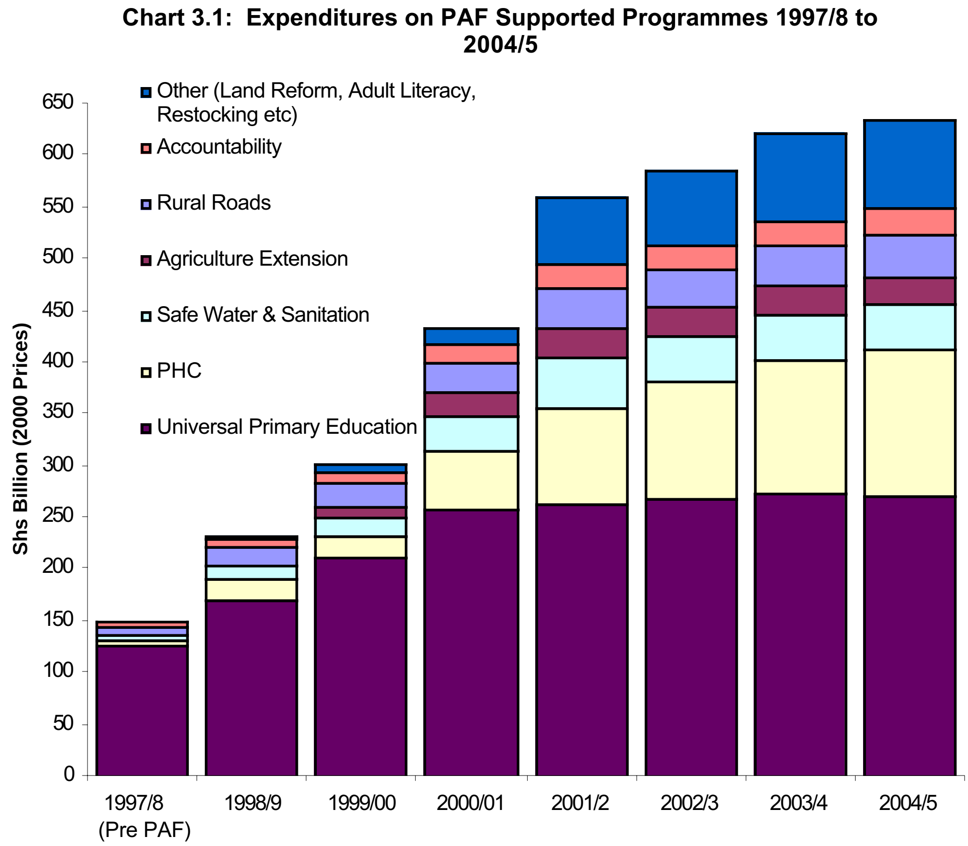
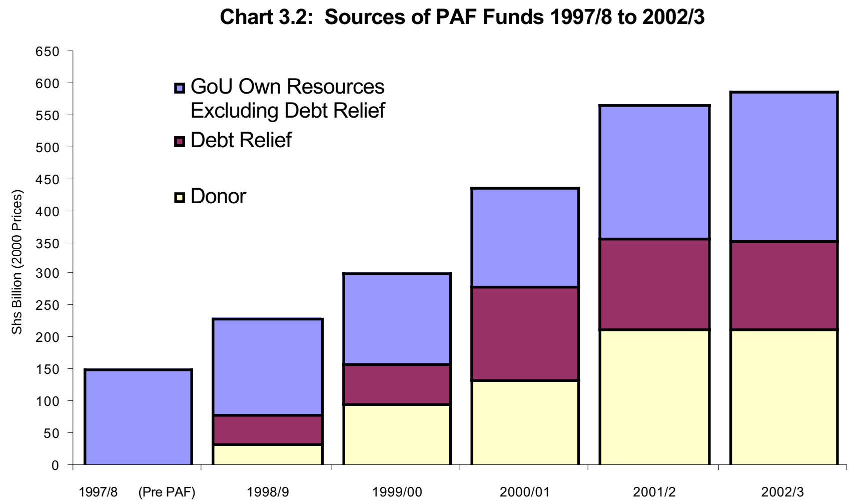


Figure A1: Expenditure trends on PAF-supported programmes, Uganda

Source: Reproduced from Mohoro Ndungu and Tim Williamson, *Financing Poverty Reduction in Uganda: A Study Reviewing the Poverty Action Fund,* Kampala: MFPED, May 2002.

Figure A2: Sources of PAF funds, Uganda



Source: Reproduced from Mohoro Ndungu and Tim Williamson, *Financing Poverty Reduction in Uganda: A Study Reviewing the Poverty Action Fund,* Kampala: MFPED, May 2002.

Table A4: Economic composition of budgetary spending, Uganda

(Budget out-turns, million USh)

	1996/97	*1997/98*	*1998/99*	*1999/2000*	*2000/01*
Total expenditure	1,102,212	1,220,387	1,501,173	1,870,280	2,119,090
Development expenditure	442,035	494,460	635,067	814,320	1,001,380
% of total	40.1	40.5	42.3	43.5	47.3
Recurrent expenditure	658,177	722,927	863,786	957,360	1,143,520
% of total	59.7	59.2	57.5	51.2	54.0
Salaries and wages	227,000	255,753	341,163	373,890	436,600
% of recurrent	34.5	35.4	39.5	39.1	38.2

Source: MFPED, *Background to the Budget, 2001/02,* Table 15

DEPARTMENT FOR INTERNATIONAL DEVELOPMENT

The Department for International Development (DFID) is the UK Government department responsible for promoting sustainable development and reducing poverty. The central focus of the Government's policy, based on the 1997 and 2000 White Papers on International Development, is a commitment to the internationally agreed Millennium Development Goals, to be achieved by 2015. These seek to:

- Eradicate extreme poverty and hunger
- Achieve universal primary education
- Promote gender equality and empower women
- Reduce child mortality
- Improve maternal health
- Combat HIV/AIDS, malaria and other diseases
- Ensure environmental sustainability
- Develop a global partnership for development

DFID's assistance is concentrated in the poorest countries of sub-Saharan Africa and Asia, but also contributes to poverty reduction and sustainable development in middle-income countries, including those in Latin America and Eastern Europe.

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