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Strengthening budget practices in Africa

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Acronyms and abbreviations

ADB	African Development Bank
CABRI	Collaborative Africa Budget Reform Initiative
CAEMC	Central African Economic and Monetary Community
CBA	Central Budget Authority
CEPEX	Central Public Investment and External Finance Bureau
CSO	civil society organisation
CSP	Country Strategy Paper
CSRP	Civil Service Reform Programme
DAD	Development Assistance Database
EFU	External Finance Unit
EMCP	Expenditure Management and Control Programme
ETCA	Economic and Technical Co-operation Agreement
EXIM Bank	Chinese Export Import Bank
FDI	foreign direct investment
FOCAC	Forum for China-Africa Co-operation
GEMAP	Governance and Economic Management Assistance Programme
GPRA	Government Performance and Results Act
HIPC	Heavily Indebted Poor Countries
IDA	International Development Association
IMF	International Monetary Fund
IPRSP	Interim Poverty Reduction Strategy Paper
KDI	Korea Development Institute
MINECOFIN	Ministry of Economy and Finance
MSF	Ministry of Strategy and Finance
MPB	Ministry of Planning and Budget
MTEF	medium-term expenditure framework
NFMP	National Fiscal Management Plan
NIS	National Investment System
OBL	Organic Budget Law (Organic Law on State Finances and Property)
ODA	official development assistance
OECD	Organisation for Economic Co-operation and Development
PAGAM/GEF	Governmental Action Plan to Improve and Modernise Public Financial Management
PEFA	Public Expenditure and Financial Accountability Secretariat
PFM	public financial management

PRC	People's Republic of China
PRS	poverty reduction strategy
PRSP	Poverty Reduction Strategy Paper
PSCAP	Public Sector Capacity Building Support Programme
PSIP	Performance and Service Delivery Improvement Policy
SABP	Self-Assessment of the Budgetary Programme
SEZ	Special Economic Zone
SFPR	Strategic Framework of Poverty Reduction
SOE	state-owned enterprise
SPA	Strategic Partnership for Africa
UA	units of account
WAEMU	West African Economic and Monetary Union

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Strengthening budget practices in Africa: An overview of CABRI's 5th Annual Seminar

Alta Fölscher

In previous years, CABRI seminars evolved around a budgeting theme of importance to member states. However, with the introduction of other focused events such as sector dialogues and policy seminars, the decision was made to allow the annual seminar to cover a selection of themes that are related to CABRI's ongoing work and/or of immediate interest to participating countries. The 5th Annual Seminar, held between 7 and 9 April in Dakar, Senegal, was the first seminar in the new format. The seminar programme and copies of key presentations can be found on the CABRI web site (www.cabri-sbo.org).

The themes covered in the seminar picked up on the work undertaken by CABRI in the preceding year (the budget practices and reform priorities, and the aid on budget sessions), on future work (the performance budgeting, and the budgeting for large capital projects sessions), and on issues that were pertinent in budget management at the time of the seminar (the session on fiscal responses to the global economic slowdown).

This chapter provides an overview of the seminar proceedings, linked to the papers and notes arising from the seminar that are presented in this volume. As in previous years, the papers published here include short notes reflecting the presentations developed for the seminar, the source papers that underpinned seminar presentations on work undertaken by CABRI, and papers prepared for this volume that build on or reflect the themes covered at the seminar. The volume is intended as a reference and a resource for CABRI countries.

Budget practices and procedures in Africa

CABRI's participation in 2008 in the Organisation for Economic Co-operation and Development (OECD) Survey on Budget Practices and Procedures created an opportunity for the analysis of similarities and differences in the budget practices of participating countries. The survey, which involved 24 CABRI participating countries, was the first time that substantial standardised information became available on budget systems of African countries. Early in 2009, the network published its *Report on Budget Practices and Procedures in Africa*. A session of the 5th Annual Seminar was dedicated to sharing the findings of the report with members. Chapter 2 of this volume provides a summary of the findings.

The findings in respect of key aspects of the budget process showed that African budget systems balance various aspects of the budget process differently. In addition, the findings showed the extent of progress towards achieving commonly accepted principles of good budgeting. As reported by Paolo de Renzio and Joachim Wehner in Chapter 2:

- The start of the executive drafting stage of the budget process varies between 11 and four months before the beginning of the fiscal year.
- The tabling of the budget in the legislature varies between three months prior to the start of the fiscal year and one month thereafter.
- Only two out of 26 countries publish their accounts within six months of the fiscal year having ended. In nine countries, audited accounts take longer than 12 months to be published, and some countries do not make accounts publicly available at all.
- Fourteen countries impose comprehensive ceilings at lower levels of the budget structure at the start of the budget process, three countries impose only partial ceilings on certain types of expenditure, five countries impose indicative limits, and two impose no limits at all.
- In 12 countries, the finance minister resolves high-level disputes within the allocative budget process, in two countries this role falls to the prime minister or president, in ten countries high-level disputes are settled in Cabinet, and two countries refer such issues to a subgroup of ministers.
- Eleven countries do not include multi-year estimates in the budget documents sent to Parliament for approval. Five countries provide detailed estimates at individual line-item level, while the remaining ten countries provide estimates at some level. For all but one of the countries, the forward estimates cover three years and are updated on an annual basis.
- The use of multi-year expenditure targets or ceilings that are not submitted to the legislature is common. Only three countries reported not using such forward targets internally.
- Five countries indicated that once approved, the executive cannot cancel spending. In 14 countries, spending can be cancelled, but subject to restrictions, and in six there are no restrictions on spending.
- Seven countries reported that overspending without prior approval is not allowed, 16 countries indicated that this is only possible with limitations, and three responded that there are no limits.

The report includes an extensive analysis of the relative strengths of countries' legislatures, how different countries perform against internationally promoted principles of good budgeting, such as transparency and discipline in budget implementation and the inclusion of aid on budget.

De Renzio and Wehner conclude that the results of the 2008 CABRI/OECD Africa Budget Survey in many ways confirm a number of recent strands of CABRI work. For example, the contribution of legislatures to sound management of public finances,

transparency and off-budget spending are areas in which the results show weaknesses. In many cases, country responses reveal lack of availability or inadequate coverage of budget information. The absence of clear policies, poor institutional co-ordination and quality of information flows in aid management, and weaknesses in medium-term budgeting frameworks, reveal further serious shortcomings. Especially for those governments that depend heavily on donor funding, a more proactive management of aid flows should bring about significant benefits in terms of 'putting aid on budget', and should improve the capacity of the government to adopt a medium-term perspective. Finally, budget execution and audit procedures show room for improvement.

In order to reflect on how current reform initiatives might address some of these challenges, the CABRI seminar included group sessions on current reform priorities. Chapter 2 of this volume includes a series of six short inputs representing the case studies considered in these sessions and subsequent discussions. The case studies were: Mali, presented by Abdoulaye Touré, Budget Director; Liberia, presented by Anthony G Meyers, special assistant to the Minister of Finance; and Ethiopia, presented by Demelash Megersa and Desu Gebre of the Ministry of Finance and Economic Development. The groups were structured according to countries that had a long history of public finance management reforms, countries that had more recently started on a reform path, and countries whose reforms occurred in the context of their membership of the West African Economic and Monetary Union and the Central African Economic Union.

Despite differences in circumstances, the discussions revealed commonalities in the concerns that countries face and the reforms undertaken. A common theme was the wide spectrum of reforms that countries were dealing with simultaneously: from reform of procurement institutions and processes, to the introduction and strengthening of internal audit, to the development of public finance management information systems, to strategies to make budget processes more responsive to citizens, to the introduction of medium-term budgeting, new budget structures and programme performance budgeting. Despite the breadth of the reforms, countries reported a common concern about continued lack of discipline in budgeting and budget execution and an ongoing need to develop approaches at country level that are country-specific and appropriate.

Moves towards a performance orientation in budgeting were reported across all countries and, even in the advanced reformers group (where the discussion was almost exclusively about the various initiatives to introduce programme performance budgeting), all countries reported significant challenges in making it effective.

Programme performance budgeting

The challenges of programme performance budgeting emerged as a theme across different seminar sessions, with the session on Korea's experience with programme performance budgeting, presented by Youngsun Koh of the Korea Development Institute, offering a focal point. This session was developed in collaboration with the OECD.

Across the sessions, it was clear that although many countries are looking at implementing a performance orientation, countries do customise approaches to suit their needs. Some countries are more formal in their use of performance information, some are less formal; some countries add a programme structure to their budget information, but retain the legislative instruments authorising expenditure by economic or line-item classification; some allocate to programmes, while some countries implement across the board, while others prefer piloting in selected sectors followed by gradual implementation. Despite the differences in approach, challenges were shared.

Countries commonly experience difficulty in defining appropriate programmes and indicators across the government sector. For some sectors, such as education and health, programme structures and performance measures are more obvious. For other sectors, such as administrative departments, the task is much more challenging. A second common challenge is the management of performance information. Even if a country succeeds in establishing a good programme structure and in selecting appropriate performance measures, the systematic, reliable and timely collection of data and its storage is challenging. The third challenge is to use the performance information effectively. A move towards a performance orientation does not only entail establishing a performance information framework, collecting information and reporting against the identified performance measures, it also requires a paradigm change in how policies, organisations and programmes are managed. Effective programme performance budgeting requires a change in approach to leadership and management, and different support capacities for management processes at all levels of government. It is telling, therefore, that many countries reported difficulties with regard to the ownership and acceptance of programme budgeting reforms. A key conclusion of the seminar was that budgeting and managing spending effectiveness according to programmes, with a performance orientation, takes a long time to implement. It is not simply a one- or three-year programme; it requires continuous development and improvement over a much longer period.

The discussion of Korea's experience in implementing programme performance budgeting provided a timely input for participating countries on how performance

budgeting can be systematised, institutionalised and incentivised. The two papers in Chapter 6 of this volume (one of which is a note on Mr Koh's presentation) provide an overview of the context, institutional arrangements and detailed mechanisms of the evolving performance budgeting system in Korea.

The discussions on programme performance budgeting at the seminar provide useful information for the network as it starts preparing for its research work on programme performance budgeting.

Fiscal response to the global economic slowdown

African countries escaped the first-round effects of the global financial crisis, as their banking sectors were not exposed to high-risk debt instruments. However, they are severely affected by the second round of the global economic slowdown. As reported in Chapter 4, the African Development Bank has described the impact of the global slowdown as a 'growth crisis' for Africa, which is leading towards worsening fiscal constraints. The crisis has struck the key drivers of African growth; lower demand and lower prices for Africa's commodities, reduced trade flows, reduced capital inflows and tighter credit have worsened the economic outlook for Africa significantly.

The seminar introduced the theme with a Zambia Case Study (discussed in more detail in the country case study note in Chapter 4) presented by Danies Chisenda, Director of Budget, showed how the Zambian economy is facing a steep increase in inflation and the cost of capital, currency depreciation and a weak growth outlook. The public finances are affected through reduced revenue as a result of falling copper production levels and higher demand for expenditure.

The session provided participating countries with an opportunity to share the key impacts on their economies and to discuss their priorities in response to the presentation by Zambia. Common lessons and intervention choices emerged.

While the discussion mostly concerned appropriate responses, a key theme was that countries that had used the accelerated economic growth in the years prior to the crisis to achieve positive primary fiscal balances had given themselves a cushion against the shocks and a means to counter the effects of the global slowdown on their economies. Another important lesson arising from the crisis is the vulnerability of African economies that are not sufficiently diversified and too dependent on global demand for their commodities.

Looking forward, participating countries emphasised that ill-considered short-term measures to address the immediate effects of the slowdown – such as excessive borrowing on internal capital markets to sustain existing and often unproductive recurrent spending – without taking into account the potential long-term damage

of such measures must be avoided. While the impact of the global crisis is affecting development progress in Africa, it may be seen as an opportunity to put in place key internal drivers of growth. Countries' fiscal and budget choices are pivotal in ensuring that the impact of the global crisis is minimised and in facilitating future economic development in Africa.

For example, participants agreed that increased public spending may be required to counter local economic downturn, but warned that the quality of spending is the important variable in determining whether this response will have the desired effect. Even for countries for which the fiscal position prior to the slowdown does not allow significant space to increase spending, the allocation of their available funding matters. Key thoughts were that:

- Countries should resist the short-term measure of cutting capital spending or investment in infrastructure to allow recurrent spending to continue. At the very least, capital spending should be sustained, if not increased. Using available public money to increase spending on infrastructure has immediate economic spin-offs through employment and demand for material, but also supports the medium- to long-term growth prospects of the economy.
- To protect the population against job losses as a result of the global slowdown, countries should look at the use of labour-intensive methods in the development of infrastructure and the delivery of public services.
- Steps should be taken to adjust the distribution of public resources to protect the vulnerable. Countries should identify which sections of their population are particularly vulnerable to the slowdown and most in need of assistance, and develop appropriate responses, such as social assistance programmes.

In addition to a careful fiscal response and a considered allocation of public resources, a key priority for countries is to use the pressure of the growth slowdown to improve the efficiency of revenue collection. Together with these fiscal and budget policy responses, the participants emphasised the need for an economic policy response around two key aspects: the diversification of the local economy and the need to enhance long-term economic competitiveness. In addition to improving the quality of spending, policies to diversify the economy and regulatory reform to lower the cost of doing business are important interventions that will determine a country's ability to resume a higher growth path as the global economic outlook improves.

Aid on budget

Bringing aid on budget has been a CABRI focus for more than two years. The cross-country research undertaken jointly in 2007 with the Strategic Partnership for Africa (SPA) on how aid-receiving countries can improve the integration of aid flows into their budget process led to the publication by CABRI and SPA in 2008 of the *Putting Aid on Budget Synthesis Report* and *Good Practice Note*, which has been influential in how the global aid-effectiveness community thinks about the use of country systems. The use of country systems, in turn, is a key commitment of the 2005 Paris Declaration on Aid Effectiveness and, more recently, of the 2008 Accra Agenda for Action.

The work done to unpack the use of country systems systematically into the phases of the budget process in the 2007 research has put CABRI in a position to assist its member countries in investigating, and making progress towards resolving, key bottlenecks to improving the integration of aid on budget. The process undertaken with the Ministry of Economy and Finance in Rwanda in this regard was presented at the seminar and is summarised in Chapter 3 in the paper by Clement Ncuti, from the Ministry of Finance and Economy in Rwanda, and CABRI researcher Mailan Chiche. This work, together with CABRI's interaction with member states and the ten country case studies of the 2007 CABRI/SPA research, has developed CABRI's insight into the practical constraints against the use of country systems, the risks thereof and the possible unintended consequences for aid-receiving countries.

In principle, CABRI agrees that using country systems to manage aid is essential not only for improving aid effectiveness and building effective state capacity, but also for improving the effectiveness of domestic expenditure. However, the use of country systems remains a means towards these ends and should not be enforced as an end in itself, without taking into account whether it is likely to lead to the desired improvements. A more nuanced approach during implementation should reflect developing country choices about how they wish to manage their own fiduciary and development risks. Key considerations are the sequencing of how countries wish to strengthen their systems, and when aid should be on budget in any dimension and when it should not.

While the existing documentation with regard to the use of country system speaks extensively of the fiduciary, development and reputational risk for donors in using country systems, little attention is paid to the risks faced by aid-receiving countries and how to address these. CABRI has emphasised that the debate around the use of country systems is far too focused on the use of downstream elements of the budget cycle; the upstream elements – planning, budgeting and parliamentary approval – are equally if not more critical for the effectiveness of aid and domestic

resource expenditure. Finally, CABRI has reminded the international community that developing countries have a much stronger role to play in determining whether and where aid should be integrated into the various dimensions of a country's policy and budgeting cycle, and this determination is the key focus of CABRI's in-country work on aid on budget.

The two sessions at the seminar dedicated to these issues – the reflection on the reforms undertaken by Rwanda and the discussion with CABRI participating countries on CABRI's formal response to the Accra Agenda for Action (presented in the paper in Chapter 3 by Aarti Shah from the CABRI Secretariat) – evoked strong discussion. A central theme was that the use of country systems and the integration of aid on budget are country-specific issues: while the underlying principles may be universal, their application is not. Aid management reforms, like budget reforms, are not one-size-fits-all. Progress can be made only at country level, in response to country circumstances, and will lead to success only if appropriate to the country concerned. Attempts to apply uniform approaches in pursuit of global targets will not succeed and can do more damage than good. Country-level reforms should be led by the recipient country, with an eye on the integration of aid into its budget process. The reforms in practice will be step-by-step, donor-by-donor and modality-by-modality.

The session reconfirmed that the aim and underlying principles of CABRI's work on aid on budget are about the effectiveness, transparency and accountability of aid and domestic resource expenditure. A key forward priority is a closer interface between aid management reforms and public finance management reforms.

Budgeting for capital projects

The fifth theme in the 2009 Annual Seminar revolved around the development of systematic approaches to budgeting for capital projects, and how the source of external financing affects the potential development of a comprehensive government-wide system to appraise, plan and manage capital projects.

The Chilean experience, covered in the first session on this theme, represented an important case study of the utilisation of technical project appraisal in a centralised fashion. As set out in Chapter 5 of this volume, the Chilean government has developed a National Investment System (NIS), linked to the budget process, which manages the appraisal, planning and implementation management of public investment. Key themes covered were the processes for appraising investment projects and the benefit to the quality of investment and decision-making of running thorough *ex ante* appraisal processes, the institutional arrangements for effectively monitoring the implementation of investment projects, the influence of politics on final project

decisions, and building capacity to appraise projects. Key lessons from this session were the importance of robust appraisal in cutting ill-considered projects as early as possible in the cycle, before they gain momentum, and the benefits of a systematic, comprehensive, integrated and capacitated country system for managing the project cycle from cradle to grave.

The second session on budgeting for capital projects was built around how different external sources of funds force African countries away from the development of centralised systems where trade-offs between projects and approaches can be made systematically. The presentation of the Sierra Leone case study in Chapter 5 (written up by Tasima Jah and Abdul Rhaman Conteh from the Finance Ministry of Sierra Leone) was followed by a presentation by Martyn Davies from the Centre of Chinese Studies at the University of Stellenbosch, South Africa on China's involvement in the public infrastructure sector in Africa (represented in this volume by the paper in Chapter 5, which draws on the presentation and other outputs of the Centre).

Key themes from this session were that countries that receive concessional support for the development of infrastructure should undertake careful analysis and weighing of the conditionalities that accompany the support. External concessional support for infrastructure development should not drive the development. Rather, countries should develop stronger approaches to planning for the systematic and sequenced development of their infrastructure, together with strong central capacity to appraise proposed projects early in the project cycle and to develop and consider financing options for approved projects.

In current practice, the link between externally financed projects and the budget cycle is far too weak; budget officers are poorly informed of the demand placed by externally financed projects on domestic resource, both during project implementation and subsequently when the infrastructure comes into operation and needs to be maintained. This, too, is symptomatic of poor central infrastructure planning, appraisal and financing capacity. However, the provision of timely and comprehensive information on the immediate and long-term impacts of an infrastructure project on the budget is a first necessary step, even in the absence of such capacity.

The seminar session concluded with discussion on the difficulties for country infrastructure development systems caused by the high-level political contact that often precedes Chinese-based support for infrastructure projects in Africa. The emphasis in the presentation on China's involvement was on the mutual benefit that underlies China's increasing presence in African economies and the responsibility that rests on African countries to ensure that the terms of China's engagement are appropriately balanced in their favour. There is an urgent need for African policy-

makers to understand China's interest in Africa and to negotiate far more robustly in the interests of their countries' long-term growth and development.

The infrastructure sessions at the 5th Annual Seminar underscored CABRI's interest in continuing work in this area, and highlighted the potential value of its planned December 2009 seminar on the appraisal, financing and management of large infrastructure projects.

2

Budget practices in Africa

2.1 Introduction

During 2008, CABRI joined up with the Organisation for Economic Co-operation and Development (OECD) to conduct its extended survey on budget practices and procedures in participating countries. This was the first time that a substantial amount of standardised information has been made available on the budget systems of countries in Africa. The database – which provides information on 26 CABRI participating countries and a further 71 countries across the world – provides a unique and comprehensive resource for government practitioners, legislatures, academics and non-governmental organisations.

In addition, CABRI commissioned an analysis of the results for the 26 participating states, focusing on topics such as the timeline of the budget process, budget formulation issues, the role of the legislature and budget execution practices. For the Africa survey, an additional set of questions concerned aid management, the results of which were analysed as well. The main paper in this chapter, by Paolo de Renzio and Joachim Wehner from the London School of Economics, presents the findings in a summarised form. The original report can be found on the CABRI website (www.cabri-sbo.org).

The report on budget practices and procedures provided an opportunity for an update on reform priorities in participating CABRI countries. The third session at the Dakar seminar, therefore, was dedicated to the discussion of country-specific reform efforts. This took place in three groups: (a) early reformers, (b) advanced reformers, and (c) participating countries belonging to the West African Economic and Monetary Union (WAEMU) and the Central African Economic and Monetary Community (CAEMC), in which reforms take place in the context of convergence criteria and the 1959 Ordinance on public financial management.

In each group, a participating country was asked to initiate discussion by sharing its reform experience, followed by inputs by other group members. The group discussion then focused on commonalities and differences between reform programmes. The six short inputs that accompany the paper on budget practices and procedures in this chapter provide an overview of the group discussions. For the early reform group, the note on the overall discussion by Dr Bode Oyetunde from Nigeria is accompanied by a note on the Liberian experience by Caroline Mulliez, an intern in the CABRI Secretariat. The note by Yacine Bio-Tchané from the CABRI Secretariat on the experience of the WAEMU and CAEMC countries is accompanied by a summary of the Mali presentation and experience. Finally, the note on reforms in Ethiopia sits alongside a summary of the discussion on programme performance budgeting amongst the advanced reformers.

2.2 Budget practices and procedures in Africa: Results from the 2008 Africa Budget Survey

Paolo de Renzio and Joachim Wehner

Introduction

A key factor for the ability of the Collaborative Africa Budget Reform Initiative (CABRI) to achieve its objectives is the availability of comparative information on how budget systems work across the African continent. Therefore, CABRI decided to take advantage of the opportunity to participate in the extension of the already established Survey on Budget Practices and Procedures, promoted by the Organisation for Economic Co-operation and Development (OECD) and based on a questionnaire that captures key features of the budget process during its various stages.[1]

1 In 2007, the OECD carried out a Survey on Budget Practices and Procedures, which yielded results for 30 OECD member states, as well as eight additional countries. An extension of the survey in 2008 was targeted specifically at non-OECD countries, and yielded results for a further 59 countries, bringing the total number of countries included in the database to 97.

The African component of the 2008 survey was carried out in collaboration with CABRI, and yielded results for 26 countries.[2] This is the first time that a substantial amount of standardised information has been available on the budget systems of countries in Africa. The database provides a unique and comprehensive resource for government practitioners, legislatures, academics and non-government organisations, providing these groups with data to undertake analyses, and enabling them to compare and contrast national practices. The data collected allows CABRI, as well as other interested parties, to make substantial analyses and to publish research on current practices in budgeting. The resulting report documents the analysis undertaken and points out possibilities for further work that could be undertaken in subsequent phases.[3] This chapter presents the material in the report in a summarised version, focusing on a number of substantive topics linked to the different phases of the budget cycle and to some key cross-cutting features of the budget process.

Timelines of the budget process

The budget process can be divided into four distinct stages: (1) executive drafting, (2) legislative approval, (3) execution, and (4) audit and evaluation (Lee, Johnson & Joyce 2004). The timing of the budget process is likely to reflect country-specific factors, such as administrative heritage and capacity, the balance of power between the different branches of government, and the macroeconomic context.

There are no firm international guidelines on the precise duration of the executive drafting (or budget formulation) process, for good reasons. As Wildavsky (1975) notes, the nature of budgeting reflects, amongst others, the degree of uncertainty in planning. In countries with a volatile macroeconomic environment (for instance, when revenues are highly dependent on a few commodity exports with fluctuating prices), it is very difficult to plan ahead over an extended time period. Even planning for a single year can be impossible with high uncertainty, and budgets may have to be remade almost continuously (Caiden & Wildavsky 1974). More stable economies,

2 The countries are: Benin, Botswana, Burkina Faso, Congo (Brazzaville), Ethiopia, Ghana, Guinea, Kenya, Lesotho, Liberia, Madagascar, Malawi, Mali, Mauritius, Morocco, Mozambique, Namibia, Nigeria, Rwanda, Sierra Leone, South Africa, Swaziland, Tunisia, Uganda, Zambia and Zimbabwe. Financial support for the survey was provided by the UK Department for International Development (DFID). An additional 35 countries from various regions were covered with funding from the World Bank, including two North African countries, Morocco and Tunisia.

3 See CABRI/ADB (2009). The appendices to the report include tables detailing the coding and the construction of the composite indices used throughout the report, as well as short profiles of all participating countries, bringing together some basic information and the responses to the survey questions covered in the report. In some cases, survey responses were re-coded, based on comments included in the survey or following a workshop held in Pretoria in December 2008. Details of all changes are included in the report.

on the other hand, can plan ahead more easily within an expanded time horizon, sometimes involving fiscal frameworks that are fixed over a number of years (Tarschys 2002). Hence, diverse patterns are likely in cross-national data.

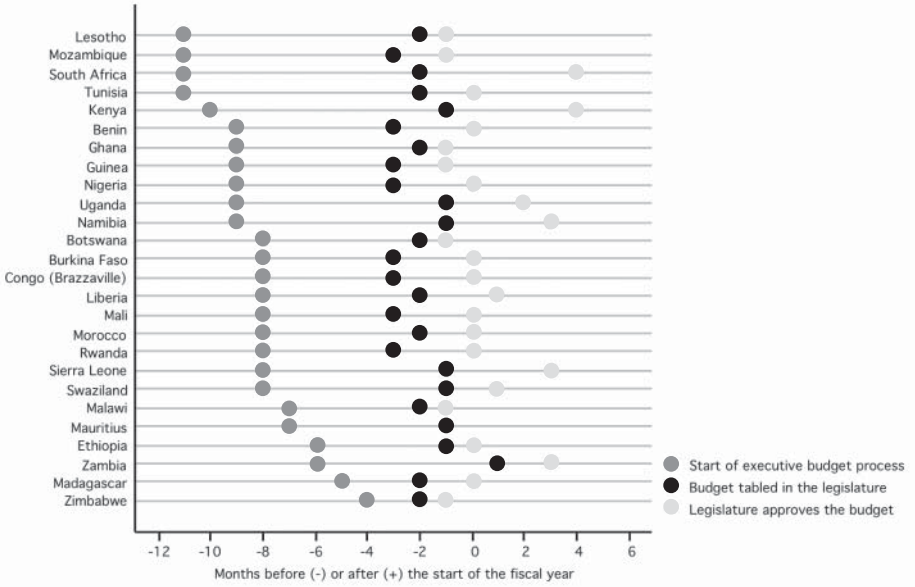
Figure 2.2.1 is a dot plot that tracks the beginning of the executive drafting stage, and the timing of the tabling of the budget in the legislature and its approval. Countries are sorted by the beginning of the executive drafting process, in descending order on the vertical axis. The figure shows that the beginning of the annual budget process varies between 11 months (Lesotho, Mozambique, South Africa and Tunisia) and four months (Zimbabwe) prior to the beginning of the relevant fiscal year. The median is eight months. Taking into consideration the timing of the tabling of the budget in the legislature does not reduce these differences: there remains a difference of seven months between the longest executive drafting processes in the sample (nine months in Kenya, Lesotho, South Africa and Tunisia) and the shortest (two months in Zimbabwe). The median executive drafting process lasts six months.

International standards on budget transparency require that legislatures have sufficient time to review the draft budget. Notably, the OECD Best Practices for Budget Transparency recommend the tabling of the budget at least three months prior to the start of the fiscal year and its approval before the fiscal year commences (OECD 2002: 8). The Public Financial Management Performance Measurement Framework is less demanding, and gives countries a high score if the budget is tabled at least two months prior to the beginning of the fiscal year (PEFA Secretariat 2005: PI–27). The IMF Code of Good Practices on Fiscal Transparency also demands 'adequate time' for the legislative review of the draft budget (IMF 2007a: 2.1.1). In sum, while all of these standards recognise the importance of legislative review of the draft budget, there is no agreement on an exact minimum requirement.

According to Figure 2.2.1, the timing of the tabling of the budget in the legislature varies between three months prior to the start of the fiscal year (in eight countries) and one month after (Zambia). The median is two months prior to the commencement of the fiscal year. Hence, most countries in the sample meet the Public Expenditure and Financial Accountability (PEFA) Secretariat requirement, but not the OECD's more demanding standard.

The timing of legislative approval varies slightly more. It takes place between one month before the start of the fiscal year (in seven countries) and four months into the fiscal year (Kenya and South Africa). The median is zero months prior to the beginning of the fiscal year. Overall, the median timeline for the legislative process is more compact than the OECD recommends. This suggests a relatively weak role for the legislature in many African countries (see also Lienert 2003).

Figure 2.2.1: The timeline for budget formulation



Note: Based on Q25 ('In practice what is the timeframe for the budget drafting process?') and Q39 ('In practice what is the timeframe for the following stages of the budget approval?').

Following the end of the financial year, the audit of accounts is a fundamental requirement for government accountability (INTOSAI 1998). According to the OECD Best Practices, audited government accounts should be available within six months of the end of the fiscal year (OECD 2002: 10). This is a tight deadline that even several industrialised democracies do not meet in practice. The IMF Code is more generous: 'Audited final accounts and audit reports, including reconciliation with the approved budget, should be presented to the legislature and published within a year' (IMF 2007a: 2.2.4). The PEFA framework gives countries the highest score when they produce annual financial statements within six months of the end of the fiscal year and when these are audited within another four months (PEFA Secretariat 2005: PI–25 and PI–26). The OECD, IMF and PEFA standards all require the publication of audited accounts (OECD 2002: 14; PEFA Secretariat 2005: PI–10; IMF 2007a: 4.3.2).

Most countries in the sample do not meet the OECD's standard; only two of the 26 countries (Mauritius and South Africa) publish their accounts six months after the end of the fiscal year or earlier. Half of the countries in the sample meet the IMF's more generous deadline, but the median for the publication of audited accounts is

beyond 12 months. In nine countries, audited accounts take longer than 12 months to publish; Tunisia does not make audited accounts publicly available at all, and the Supreme Audit Institutions in Congo (Brazzaville) and Liberia were set up only recently and, at the time of the survey, had yet to complete audits.

In several countries, the timeliness of external audit has improved in recent years. A comparative study of five African countries published in 2002 found that, on average, audit reports were tabled in the legislature about two years or more after the end of the relevant financial year, whereas the legally stipulated deadlines varied between six and 11 months (Fölscher 2002: 42). For instance, when democracy returned to Nigeria in 1999, financial statements had not been produced since 1993; hence, they could not be audited either. Nigeria now reports that audited accounts are publicly available within eight months. The rebuilding of the external audit function in Congo (Brazzaville) and Liberia also represents an important step in the right direction. Thus, although the quality of accounting and auditing does not yet meet international standards in a number of African countries, the overall trend is more positive.

Issues in budget formulation

As highlighted in the previous section, the budget formulation stage is dedicated to the drafting of budget documents by the executive, in order to translate policy initiatives into resource allocation decisions across the numerous activities and units of government. This process is guided by the Central Budget Authority (CBA), usually based in the Ministry of Finance, which sets the guidelines, formulates the macroeconomic framework, and negotiates with spending ministries and agencies their respective allocation for the following budget year. While practice varies greatly across countries, Schiavo-Campo (2007: 236) identifies three prerequisites for budget formulation to ensure that the resulting budget is 'both technically sound and faithful to political directions'. These are: (a) making early decisions on budget priorities; (b) setting hard constraints to ensure aggregate fiscal discipline; and (c) taking a medium-term perspective. The first two fall broadly within what have been termed 'top-down budgeting' practices (Kim & Park 2006), while the third is linked to the introduction of multi-year budgeting frameworks. This section uses selected survey findings to analyse these aspects of budget formulation, and to describe existing practices across the African continent.

Top-down budgeting

The emphasis on top-down budgeting arose from the observation that allowing budgets to be formulated according to a 'bottom-up' approach, where line ministries

submit unconstrained budget requests, which are then aggregated by the CBA, can lead to overspending and unsustainable fiscal deficits. Institutional arrangements that attribute strategic powers to central actors such as the finance minister, prime minister or president are elements of a 'top-down' approach that is more likely to promote aggregate fiscal discipline (Von Hagen & Harden 1995; Alesina & Perotti 1996). Alesina et al. (1999), for example, looked at the design of the budget process across Latin American countries. They distinguished procedures that are 'hierarchical' (top-down) from those that are 'collegial' (bottom-up). Hierarchical procedures impose a hard budget constraint and concentrate decision-making authority in the hands of the finance minister, while collegial procedures disperse decision-making authority. They found that, indeed, hierarchical procedures were associated with lower deficits.

One of the potential benefits of top-down procedures is the protection of fiscal discipline. However, case study evidence suggests that there can be a trade-off between fiscal discipline and allocative as well as operational efficiency (Stasavage & Moyo 2000; Campos & Pradhan 1996). Therefore, no judgement is made on whether top-down or bottom-up practices are more desirable and effective; the items selected here capture the degree to which the process imposes a hard budget constraint and concentrates decision-making authority in the hands of the finance minister.

Question 23 in the survey asked whether the CBA imposes limits or ceilings on the initial spending requests by line ministries during the drafting stage of the budget process, and at what level of detail, if applicable. The answers are presented in Table 2.2.1. The CBAs in South Africa and Zimbabwe impose no limits,[4] and in a further five cases there are only indicative limits. In three countries, there are only partial ceilings on certain types of expenditure, while in 14 countries the CBA imposes comprehensive ceilings at the chapter level and in a further two countries at the line item level.

Question 26 considered high-level dispute resolution (see Table 2.2.2). In most budget processes, there will be issues that cannot be settled by civil servants, and on which a political decision is required. The survey captured whether a single individual at the centre of government makes final decisions in such cases, or whether this involves a more collegial forum. Twelve countries indicated that the finance minister generally resolves high-level disputes, and another two indicated that this role falls to the prime minister or president. Ten countries have a collegiate approach,

4 In the case of South Africa, however, the lack of limits/ceilings on initial spending requests does not imply that top-down budgeting practices are not in place. Fölscher and Cole (2005: 118) explain how 'all bids competing for the same envelope of available funds are considered together within an overall hard budget constraint, forcing hard choices'.

Table 2.2.1: Limits/ceilings on initial spending requests

Q23: Does the CBA impose limits (ceilings) for each ministry's initial spending request?	Countries
No, there are no such limits	South Africa, Zimbabwe
No, there are only suggested/indicative limits	Congo (Brazzaville), Botswana, Ethiopia, Swaziland, Tunisia
Yes, but only for some types of expenditure (e.g. salaries) on a chapter level	Benin, Liberia, Uganda
Yes, but only for some types of expenditure (e.g. salaries) at a line-item level	None
Yes, for all types of expenditure at a chapter level	Guinea, Kenya, Lesotho, Madagascar, Malawi, Mali, Mauritius, Morocco, Mozambique, Namibia, Nigeria, Rwanda, Sierra Leone, Zambia
Yes, for all types of expenditure at a line-item level	Ghana, Burkina Faso

Table 2.2.2: Dispute resolution

Q26: In practice, how are disputes between line ministries and the Central Budget Authority in the budget preparation process generally resolved, i.e. issues not resolved at civil servant level?	Countries
The issue is resolved by the minister of finance	Benin, Burkina Faso, Kenya, Lesotho, Madagascar, Malawi, Mauritius, Morocco, Sierra Leone, Tunisia, Uganda, Zimbabwe
The issue is resolved by the prime minister	Mali
The issue is resolved by the president	Congo (Brazzaville)
The issue is resolved by the Cabinet	Botswana, Ethiopia, Ghana, Guinea, Mozambique, Namibia, Rwanda, South Africa, Swaziland, Zambia
The issue is sent to a ministerial committee	Liberia, Nigeria

where high-level disputes are settled in the Cabinet, and two countries refer such issues to a subgroup of ministers in the form of a ministerial committee.

Multi-year frameworks

While government budgeting almost universally follows a yearly cycle, managing public finances inevitably requires a more extended time horizon, as fiscal policy decisions have economic and budgetary implications that go well beyond a single fiscal year. Medium-term budgeting frameworks are meant to ensure aggregate fiscal discipline while, at the same time, allocating resources to policy priorities (World Bank 1998; Le Houerou & Taliercio 2002). Moreover, such frameworks help increase budget transparency and improve the link between the capital and recurrent budgets (IMF 2007b).

Medium-term expenditure frameworks (MTEFs) have been promoted across Africa as a 'best practice' approach to bridge the gap between the goals and objectives of

medium-term country development strategies and the yearly budget process. Given the challenges inherent in embedding a medium-term perspective in budgeting, in 2007 CABRI devoted its entire Annual Seminar to this theme, exploring some of the specific building blocks of MTEFs, such as existing budgeting rules, forecasting, projections and estimates both on the revenue and on the expenditure side, capital budgeting and the integration of aid flows in the budget process (CABRI 2007).

The survey questionnaire focuses on two main aspects of medium-term budgeting, distinguishing between the forward-looking estimates that are included in budget documents in order to describe the medium-term fiscal outlook, and the multi-year targets/ceilings that might be imposed on aggregate or sector-specific spending. For instance, Table 2.2.3 shows which countries include multi-year estimates in the budget documents that are sent to Parliament for approval. Eleven of them do not include such estimates, while the others present different levels of detail. Five countries include very detailed estimates that cover individual line items. In all countries that include multi-year estimates, these cover a period of three years including the upcoming budget (except for Madagascar which reports having five-year estimates), and are updated on an annual basis (except for Rwanda and South Africa, where they are updated twice a year).

Table 2.2.3: Multi-year estimates

Q16: Does the annual budget documentation submitted to the legislature contain multi-year expenditure estimates?	Countries
No	Botswana, Burkina Faso, Congo (Brazzaville), Ethiopia, Guinea, Liberia, Mozambique, Swaziland, Tunisia, Zambia, Zimbabwe
Yes, at the aggregate level	Uganda
Yes, at the ministry level	Benin, Ghana, Lesotho, Madagascar, Mali, Mauritius, Namibia, Nigeria, Sierra Leone
Yes, at the line-item level	Kenya, Malawi, Morocco, Rwanda, South Africa

Note: For a number of francophone countries, it should be noted that budget legislation prevents the inclusion of multi-year estimates in the annual budget document.

As reported in Table 2.2.4, multi-year expenditure targets or ceilings that are not submitted to the legislature for approval are much more common. Only three countries report not using such targets, while all the other countries apply them either at ministry or at line-item level. In this case, as well, all countries report having targets that are set for a three-year period, except for Madagascar and Uganda (both five years) and Botswana (six years). All countries revise their targets annually, except for Botswana where they are updated every three years.

Table 2.2.4: Multi-year targets or ceilings

Q20: Are there multi-year expenditure targets or ceilings?	Countries
No	Guinea, Liberia, Zimbabwe
Yes, at the aggregate level	Congo (Brazzaville), Mozambique, Swaziland
Yes, at the ministry level	Benin, Botswana, Burkina Faso, Ethiopia, Ghana, Kenya, Lesotho, Madagascar, Mali, Mauritius, Namibia, Nigeria, Sierra Leone, Zambia
Yes, at the line-item level	Malawi, Morocco, Rwanda, South Africa, Tunisia, Uganda

These results seem to indicate that medium-term budgeting frameworks in Africa are instruments for ensuring fiscal discipline, which executives use in a flexible manner. The survey, however, sheds little light on the 'quality' of these instruments and on the impact they actually have on fiscal discipline and budget policies and processes more generally. Previous studies on MTEFs in developing countries (including Le Houerou & Taliercio 2002; Holmes & Evans 2003) have highlighted a number of challenges that African countries face when introducing medium-term frameworks. These include the introduction of these instruments without taking into account the broader budgeting environment and existing capacity, the lack of medium-term projections for more predictable aid flows, and the existence of different legal and administrative traditions that might influence the feasibility of introducing a medium-term framework (see chapter by Lienert in CABRI 2007).

Only two of the survey questions reveal potentially interesting aspects of medium-term budgeting in Africa. The first is Question 19, which asks about the basis on which multi-year estimates are extrapolated. Responses for most countries show that estimates are simply adjusted on the basis of official macroeconomic forecasts, with little attention given to expected policy changes or other variables. In OECD countries, for example, several additional criteria are usually utilised in generating multi-year estimates. The second is Question 27, which shows that 11 out of the 26 countries included in the survey have separate capital and operating budgets (see Table 2.2.5). There are good reasons to distinguish the nature of these two kinds of spending, recognising, for example, that capital budgeting often requires distinct processes. However, when the existence of two separate budget documents corresponds to two separate budget formulation processes and a lack of adequate integration mechanisms, this can constitute an obstacle for credible and comprehensive medium-term budgeting.[5]

5 The opposite is also true, of course. One of the key objectives of an effective medium-term budget process is bringing together capital and operational budgeting into a joint and integrated planning process.

Table 2.2.5: Dual budgeting

Q27: Is your central government budget split into a separate capital and operating budget?	Countries
No	Benin, Congo (Brazzaville), Ethiopia, Ghana, Guinea, Lesotho, Liberia, Madagascar, Mali, Mozambique, Rwanda, South Africa, Uganda, Zambia, Zimbabwe
Yes	Botswana, Burkina Faso, Kenya, Malawi, Mauritius*, Morocco, Namibia, Nigeria, Sierra Leone, Swaziland, Tunisia

*Note: *From fiscal year 2008/09, however, the two budgets have been integrated.*

The role of legislatures in the budget process

The role of Parliament in the budget process is one of the distinguishing features of any public financial management system (Lienert 2005). Amongst others, Schick (2002) and Coombes (1976) have explored the evolution of legislative control of the budget in a small number of OECD countries, mainly highlighting a decline in parliamentary influence. However, little is known about the 'power of the purse' elsewhere (Oppenheimer 1983), with the exception of some case studies (e.g. Stapenhurst et al. 2008). Recent cross-national surveys have shown that the role of legislatures in the budget varies greatly between countries (Lienert 2005; Wehner 2006). In addition, several legislatures have initiated reforms to strengthen financial scrutiny (Stapenhurst et al. 2008). The survey provides a unique opportunity to assess, for the first time, the budgetary role of African legislatures.

Legislative budget capacity can be conceptualised in different ways (Meyers 2001). Wehner (2006) adopts an institutional capacity perspective and surveys six variables that affect legislative control of the budget process, which are coded between zero (the least favourable from a legislative perspective) and ten (most favourable). Legislatures obtain a high score when: (a) they have unfettered amendment powers; (b) spending is disallowed without legislative approval; (c) the executive cannot unilaterally adjust the budget during implementation; (d) the budget is tabled well in advance of the start of the fiscal year; (e) a budget committee as well as sectoral committees are involved in the scrutiny of the budget; and (f) Parliament has access to budget research capacity. The six indicators are then combined into an index of legislative budget institutions (Wehner 2006: 774–776; see also Alesina et al. 1999: 260). The index scores are standardised to range between zero (no legislative budget capacity) and one (full capacity). Full details are provided in the main report.

Question 40 asked about the amendment powers of the legislature in budgetary matters (see Table 2.2.6). There are several legal restrictions in the African context, which are shaped noticeably by colonial heritage. Many francophone countries have

adopted provisions that do not allow the legislature to increase the deficit, whereas many Anglophone countries allow legislatures to make cuts to existing items only. In total, 21 of the 26 countries in the sample circumscribe parliamentary changes, including two where legislatures can only accept or reject the budget without any amendments. For the index, legislatures receive higher scores the more permissive their powers to amend the budget proposal.

Table 2.2.6: Amendment powers

Q40: What are the formal powers of the legislature to amend the budget proposed by the executive?	Countries
The legislature has unrestricted powers to amend the budget	Ethiopia, Liberia, Mozambique, Namibia, Nigeria
The legislature may make amendments but only if it does not change the total deficit/surplus proposed by the executive	Benin, Congo (Brazzaville), Guinea, Madagascar, Mali, Rwanda, Sierra Leone
The legislature may only decrease existing expenditures/ revenues (i.e. the legislature cannot increase existing items nor create new ones)	Botswana, Burkina Faso, Ghana, Kenya, Lesotho, Mauritius, Swaziland, Tunisia, Uganda, Zambia, Zimbabwe
The legislature may not make any changes; it can only approve or reject the budget as a whole	Malawi, South Africa*
Other: The legislature may not increase spending or decrease revenues	Morocco

*Note: *In early 2009 the South African Parliament passed the Money Bills Amendment Procedure and Related Matters Bill, which outlines a procedure for amending the budget.*

Next, 'reversionary budgets' are those that take effect should legislative approval happen only after the start of the fiscal year. Country responses are summarised in Table 2.2.7. In nine countries, the executive proposal takes effect if the budget is not voted by the start of the fiscal year. In another 13 countries, spending reverts to the previously authorised budget on an interim basis. In three countries, the legislature has to vote interim measures, and in Liberia expenditure without legislative approval is not allowed. The latter is an outlier and resembles the USA system in this regard (see Williams & Jubb 1996). The coding scheme assigns high scores to countries that do not allow spending unless authorised by the legislature, and lower scores where arrangements are more favourable to the executive.

The survey also considers the extent to which the executive has flexibility during budget execution in the form of powers to vire or impound, or has access to a contingency reserve. These items are presented in detail in the following section, on budget execution, but it is important to note their importance in the context of legislative oversight. If the executive has extensive powers to adjust the budget unilaterally during execution, this means that in-year adjustments can bring about a large gap between the budget approved by the legislature and actual spending, which makes legislative approval less meaningful. As an indicator of legislative control over

Table 2.2.7: Reversionary budgets

Q43: If the budget is not approved by the legislature before the start of the fiscal year, which of the following describes the consequences?	Countries
The executive's budget proposal takes effect	Botswana, Madagascar, Morocco, Sierra Leone, Tunisia, Zambia
The executive's budget proposal takes effect on an interim basis, i.e. for a limited period	Lesotho, South Africa, Uganda
Last year's budget takes effect on an interim basis, i.e. for a limited period	Benin, Ethiopia, Guinea, Malawi, Mali, Mauritius, Mozambique, Namibia, Nigeria, Swaziland, Zimbabwe, Congo (Brazzaville), Rwanda
Other interim measures are voted on by the legislature	Burkina Faso, Ghana, Kenya
Expenditure without legislative approval is not allowed	Liberia

Table 2.2.8: Committee structures

Q33: Thinking about the following types of committee structures for dealing with the budget, please indicate which arrangement applies to the lower house.	Countries
A single budget committee formally considers all budget-related matters. Sectoral committees may make recommendations, but the budget committee does not have to follow them	Burkina Faso, Congo (Brazzaville), Guinea, Kenya, Malawi, Mali, Mozambique, Rwanda, Zimbabwe
A single budget committee formally considers the budget, but members from sectoral committees attend meetings of the budget committee when expenditures in their specific areas are discussed	Benin, Ethiopia, Liberia, Madagascar, Nigeria
A single budget committee formally considers budget aggregates (total level of revenue and spending and their allocation to each sector) and sectoral committees formally consider spending for sector-specific appropriations	Morocco, Sierra Leone, South Africa, Swaziland, Uganda
Sectoral committees formally consider appropriations for each respective sector. No budget committee is in place, or it provides technical assistance only	Ghana, Tunisia
No formal committee involvement, but committees may choose to consider aspects of the budget	Botswana, Lesotho, Mauritius, Namibia, Zambia

execution, the index gives a high score to countries that do not allow cuts (see Table 2.2.10), shifts (see Table 2.2.12) or emergency spending from a contingency fund (see Table 2.2.13) without prior legislative approval.

The other three items relate to the organisation of the legislative budget process. First, the report considers the time available for scrutiny of the budget prior to the beginning of the fiscal year. As explained in the previous section, several international standards recognise the importance for thorough scrutiny of tabling the budget sufficiently in advance of the fiscal year. Data on the timing of the tabling of the budget is reported in Figure 2.2.1. For the index, legislatures receive higher scores the earlier the budget is tabled.

Question 33 asked countries to indicate the committee structure for dealing with the budget. Here, the focus is on the results for the lower house (or unicameral parliament). In 14 countries, the process centres on a single budget committee, whereas five countries report that they involve both a budget committee and sectoral committees. In two cases (Ghana and Tunisia), there is no budget committee, but sectoral committees deliberate on the budget, whereas five legislatures debate the budget on the floor of the house. Since committees are crucial for the development of parliamentary expertise and division of labour, the index assigns a high score to legislatures that have extensive committee involvement.

Finally, the analysis includes legislative access to a specialised budget research unit. Several legislatures are considering the establishment of, or are in the process of establishing, legislative budget offices (Johnson & Stapenhurst 2008). At the time of the survey, five of the 26 countries reported that their parliaments have access to specialised research capacity in the form of such units. The largest by far is in Uganda, with a total staff of 27, and there are smaller units in Benin, Kenya, Morocco and Zimbabwe. In Liberia, a Legislative Budget Office had been enacted at the time of the survey, but had not yet been activated, and the South African Parliament, at the time of writing, was in the process of passing legislation that would establish a budget office. The index gives higher scores to countries with large units, and zero to countries without any such units. In this sample, Uganda receives the highest score (0.75), the remaining four countries with legislative budget offices a lower score (0.25), and all others zero.

Table 2.2.9: Legislative budget offices

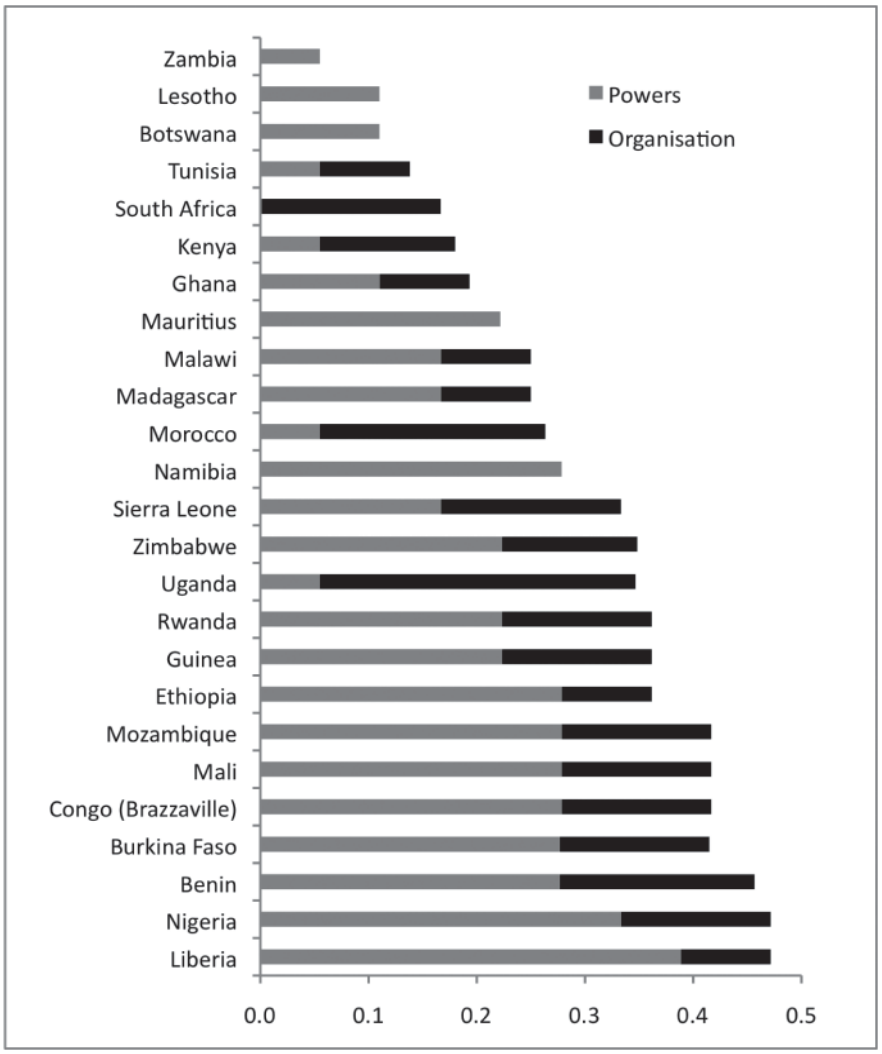
Q34: Is there a specialised budget research office/unit attached to the legislature to conduct analyses of the budget?	Countries
No	Botswana, Burkina Faso, Congo (Brazzaville), Ethiopia, Ghana, Guinea, Lesotho, Liberia*, Madagascar, Malawi, Mali, Mauritius, Mozambique, Namibia, Nigeria, Rwanda, Sierra Leone, South Africa**, Swaziland, Tunisia, Zambia
Yes, there is a specialised budget research office/unit (number of full-time staff)	Benin (5), Kenya (6), Morocco (3), Uganda (27), Zimbabwe (5)

*Notes: *A Legislative Budget Office has been enacted, but not activated. **In October 2008, the National Assembly passed the Money Bills Amendment Procedure and Related Matters Bill, according to which Parliament will establish its own Budget Office.*

Figure 2.2.2 summarises the results for the index of legislative institutions. Total scores range between 0.47 (Liberia and Nigeria) and 0.06 (Zambia). The median is 0.33. It is noteworthy that not a single legislature in this sample obtains a score

of 0.5 or higher. These findings contrast with the results for 27 out of 30 OECD countries reported in Wehner (2006), where scores range between 0.89 (USA) and 0.17 (Ireland), with a median of 0.42. Unlike in this sample of African legislatures, more than one third of the OECD country legislatures (ten out of 27) obtained a score of 0.5 or higher. This suggests that the role of legislatures in the budget process varies more in the industrialised democracies than in African countries. Moreover, African legislatures have, on average, less institutional capacity for financial scrutiny than their counterparts in the OECD.

Figure 2.2.2: Index of legislative budget institutions



Note: Refer to the main report for full details about the coding scheme.

The comparison between these two groups of countries also reveals commonalities. In particular, a pattern that is similar across both the Africa and OECD samples is that countries with a Westminster heritage tend to have weaker legislative bodies. In the sample of 27 OECD countries, all five legislatures with a Westminster heritage (Australia, Canada, Ireland, New Zealand and the United Kingdom) are in the bottom third of the distribution. In Figure 2.2.2, the bottom third of the ranking is also dominated by legislatures from Anglophone Africa that retain features of the Westminster system (Botswana, Ghana, Kenya, Lesotho, Malawi, South Africa and Zambia). Also, Nigeria and Liberia, both of which have a constitutional inheritance influenced by the USA arrangements, obtain the highest scores in the African sample. These results suggest that there are clusters of legislatures with particular patterns of institutional features that are partly determined by colonial heritage or other constitutional influences.

Figure 2.2.2 also distinguishes two sets of features that are captured by the index. Three of the variables (amendment powers, reversionary budgets and executive flexibility during execution) relate to the formal powers of the legislature. A second set of variables (the timing of the budget process, committee capacity and research capacity) relate to the organisational capacity of the legislature. This distinction yields a further interesting result: in most of the countries in the sample, formal powers exceed organisational capacity. For only five of the 23 African legislatures assessed here do the scores for the organisational variables exceed those for formal powers (Uganda, Morocco, Kenya, South Africa and Tunisia). The formal powers of legislatures are typically much more time invariant, or durable, than organisational features such as committee systems or legislative budget offices. This suggests that, where legislative strengthening is considered desirable, the latter features are often very suitable for capacity-building initiatives.

Budget execution

A major challenge faced by many African countries is to enhance the credibility of the budget by reducing the gap between planned and actual spending. According to the PEFA framework, a well-performing public financial management system ensures that the budget is 'implemented in an orderly and predictable manner and there are arrangements for the exercise of control and stewardship in the use of public funds' (PEFA 2005: 2). Poor budget execution can undermine fiscal policy, distort allocations and undermine operational efficiency (Ablo & Reinikka 1998; Stasavage & Moyo 2000). At the same time, however, overly rigid execution rules can be detrimental to performance (Campos & Pradhan 1996; Blöndal 2003). This section presents data on

several key institutional features that affect the degree of executive flexibility during budget implementation, and on the extent of in-year adjustments.

One of the principal ways in which the budget can be changed during the course of the fiscal year involves the cancellation or rescission of spending approved by the legislature. In-year cuts can help the government to ensure that aggregate spending remains within planned and prudent levels, but they can also distort budget priorities. Question 52 asked whether the government has the authority to make such in-year cuts, and to what extent. According to the results shown in Table 2.2.10, five countries indicated that the government cannot cancel spending and another 14 responded that this is only possible subject to restrictions. In six countries there are no restrictions on the cancellation of spending.

Table 2.2.10: In-year cuts

Q52: Does the government have the authority to cut/cancel/rescind spending once the budget has been approved by the legislature?	Countries
No	Benin, Lesotho, Madagascar, Malawi, Namibia
Yes, with restriction	Burkina Faso, Congo (Brazzaville), Ethiopia, Ghana, Guinea, Kenya, Liberia, Mali, Mauritius, Morocco, Rwanda, South Africa, Tunisia, Uganda
Yes, without restriction	Botswana, Mozambique, Nigeria, Sierra Leone, Zambia, Zimbabwe
No data	Swaziland

Budget execution can also undermine fiscal management when there is no effective control of overspending. The survey probed how easy it is to spend money in excess of the amount authorised by Parliament. Question 57 asked about the possibility of overspending prior to the approval of a supplementary appropriation by the legislature. Seven countries responded that overspending without prior approval is not allowed, 16 countries indicated that this is only possible up to a certain limit or for mandatory spending, while three responded that there are no limits on overspending without legislative approval. However, it should be noted that these answers might understate the *de facto* extent of overspending, as in many countries line ministries circumvent spending controls by accumulating arrears, which in some cases amount to a substantial share of public spending.

Table 2.2.11: Overspending

Q57: Can overspending occur before a supplementary appropriation law/budget is approved by the legislature?	Countries
No	Ethiopia, Ghana, Liberia, Morocco, Mozambique, Nigeria, Rwanda
Yes, but only up to a certain limit	Guinea, Kenya, Lesotho, Malawi, Mali, Mauritius, Tunisia, Uganda, Zimbabwe
Yes, but only for mandatory spending	Benin, Botswana, Congo (Brazzaville), Madagascar, Namibia, South Africa, Swaziland
Yes, there are no limits on overspending without legislative approval	Burkina Faso, Sierra Leone, Zambia

Some in-year changes do not affect the aggregate level of expenditures, but do alter their composition. Table 2.2.12 reports answers to Question 53, which asked countries whether ministers are allowed to vire or reallocate funds between line items. After adjusting the results on the basis of country comments, no country in this sample prohibits shifts outright. Four countries allow unrestricted reallocation and 18 indicate that restrictions apply. For example, ministers in Ethiopia are not allowed to vire from operation and maintenance to salary expenditures, or from the capital budget to the recurrent budget. In Rwanda, the minister of finance, after approval by Cabinet, can authorise transfers between some items within the same category of an agency's current budget, subject to a 20% limit. In South Africa, virement is subject to parliamentary approval if the amount involved exceeds 8% of the allocation for a programme, while in 13 countries it requires the approval of the finance minister. The need for virement depends partly on the level of detail at which Parliament approves the budget.

Table 2.2.12: Virement

Q53: Are ministers allowed to reallocate/vire funds between line items within their responsibility?	Countries
No	None
Yes, without restrictions	Botswana, Swaziland, Zambia, Zimbabwe
Yes, with restrictions	Benin, Burkina Faso, Ethiopia, Ghana, Guinea, Kenya, Lesotho, Liberia, Madagascar, Malawi, Mali, Mauritius, Mozambique, Namibia, Rwanda, South Africa, Tunisia, Uganda
With the approval of the legislature	South Africa
With the approval of the finance minister	Burkina Faso, Congo (Brazzaville), Ethiopia, Ghana, Guinea, Lesotho, Malawi, Mauritius, Morocco, Nigeria, Sierra Leone, South Africa, Tunisia

In exceptional circumstances, it may also be necessary to allow spending on items that are not included in the approved budget, for example to respond quickly and effectively to natural disasters such as floods or droughts. Question 61 asked about

the use of contingency reserves, which provide flexibility to address such urgent spending needs. As shown in Table 2.2.13, most countries' budgets include a central reserve fund for such purposes; only nine of the 26 countries have no contingency reserve. The use of contingency reserves should be fully transparent, so that this mechanism is not abused, for instance to finance spending that was not included in the budget and which was foreseeable.

Table 2.2.13: Contingency reserves

Q61: Did the budget for the last fiscal year include any central reserve funds to meet unforeseen expenditures?	Countries
No	Benin, Botswana, Burkina Faso, Liberia, Mali, Nigeria, Sierra Leone, Swaziland, Uganda
Yes	Congo (Brazzaville), Ethiopia, Ghana, Guinea, Kenya, Lesotho, Madagascar, Malawi, Mauritius, Morocco, Mozambique, Namibia, Rwanda, South Africa, Tunisia, Zambia, Zimbabwe

Table 2.2.14 presents some basic data on the frequency of supplementary budgets. A large number of supplementary or adjustment budgets may be an indicator of poor budget planning, although this also depends on how detailed the budget is and at what level of detail it is approved. Moreover, it is possible that a country has very permissive rules for in-year adjustments that allow the executive to make a large number of changes without having to ask for parliamentary approval. Hence, the mere number of supplementary budgets does not necessarily indicate the extent of in-year adjustments. While a few countries report that they have not submitted any supplementary budgets in the past two fiscal years, the majority of countries report that they submit one supplementary budget per year. No country reports more than four supplementary budgets.

Table 2.2.14: Supplementary budgets

Q58: How many supplementary budgets were submitted?	a) Last fiscal year	b) Previous to last fiscal year
None	Guinea, Morocco, Namibia, Sierra Leone	Congo (Brazzaville), Morocco, Namibia, Nigeria, Sierra Leone
One	Benin, Congo (Brazzaville), Ethiopia, Kenya, Lesotho, Liberia, Madagascar, Malawi, Mali, Mauritius, Mozambique, Nigeria, Rwanda, Zimbabwe	Benin, Burkina Faso, Ghana, Guinea, Kenya, Lesotho, Liberia, Malawi, Mali, Mauritius, Rwanda, South Africa, Zambia, Zimbabwe
Two	Burkina Faso, Ghana, South Africa, Uganda, Zambia	Swaziland
Three	Botswana	Botswana, Uganda
Four	Swaziland	None
No data	Tunisia	Ethiopia, Madagascar, Mozambique, Tunisia

Internal audit plays an important role in ensuring the effectiveness of internal control, which underpins sound budget execution (Diamond 2002). All sample countries, with the single exception of Swaziland, report that line ministries have internal audit units (Question 66). However, there is probably substantial variation in the quality and coverage of internal audit.

While these results once again highlight the great variation in existing practice across the African continent, they also point to weaknesses in budget execution and expenditure control. The extensive use of supplementary budgets, and the opportunities that exist for overspending and reallocations, can easily undermine the overall integrity of control mechanisms in the budget process. On the other hand, as highlighted at the beginning of this section, some of these mechanisms allow space for the flexibility that many African countries need as they budget with scarce resources and are subject to numerous uncertainties and shocks.

Cross-cutting issues

Fiscal transparency

Transparency in government finances implies 'openness about policy intentions, formulation and implementation' (OECD 2002: 7; see also Kopits & Craig 1998). Several studies have found that fiscal transparency is associated with improved fiscal discipline, better credit ratings and reduced corruption (see Alesina & Perotti 1996; Hameed 2005; Alt & Lassen 2006). Others argue that citizens and taxpayers are entitled to full disclosure with regard to the management of public money to ensure participation and accountability in policy processes (Fölscher 2002). As a result of this increased focus on the provision and quality of budgetary information, several organisations have developed international guidelines and measurement frameworks. The OECD has developed a non-prescriptive reference tool, Best Practices for Budget Transparency (OECD 2002). Other initiatives include the IMF's Code of Good Practices for Fiscal Transparency (IMF 2007a), which is used for formal country assessments, and the International Budget Project's Open Budget Initiative, which develops an index of budget transparency to compare countries across the world (IBP 2006).

It is difficult to define precisely how much and what kinds of information governments should make publicly available. While a general case can be made in favour of publicising as much budget information as possible, two caveats should be kept in mind. Firstly, the quantity of information released to the public should not come at the cost of its quality. For example, the OECD Best Practices indicate that all countries should produce monthly reports with updated revenue and expenditure

figures during budget execution. In some cases, however, less frequent reports based on more reliable data might be a better option when capacity to produce high quality data is limited. Secondly, in cases where capacity to use available information is limited, for example within civil society, published information may allow other players, such as donor agencies or lobbying groups with a narrow base to distort overall accountability processes.

In this section, survey items that provide an initial overview of the degree to which African countries provide 'full disclosure of all relevant fiscal information in a timely and systematic manner' (OECD 2002:7) are drawn together. Transparency is assessed in three areas that are broadly linked to the different phases of the budget cycle: (a) the information included in budget documents presented to the legislature (Question 35); (b) the frequency with which data on actual revenues and expenditures is reported during budget execution (Question 56); and (c) whether audit reports are made publicly available (Question 69) and with what delay (Question 70). An index of fiscal transparency is then developed, which allows for a comparative assessment of the coverage, timeliness and public availability of key budget information at different stages of the budget process.

Question 35 targets 12 types of information, highlighted in both the OECD and IMF guidelines, which should be included in the budget documentation sent to the legislature. All or most countries reported that they include information on macroeconomic assumptions, budget priorities, fiscal policy objectives for the medium-term, clearly defined appropriations to be voted by the legislature, and a linkage of appropriations to administrative units (e.g. ministry, agency). Disclosure of off-budget expenditures and extra-budgetary funds, tax expenditures, comprehensive annual financial plans and reporting on non-financial performance targets were more scattered across countries, while no country claimed to include a long-term perspective on total revenue and expenditure (ten or more years) in the documentation sent to the legislature. While countries like Burkina Faso, Lesotho, Madagascar and Nigeria report providing only limited types of information to the legislature, budget documents in countries like Ghana, Malawi and South Africa are much more comprehensive.

The frequency of reporting on actual revenues and expenditures is also crucial, in that it allows governments to measure progress on the implemented budget during the fiscal year. In-year reporting also gives practitioners and the general public the information necessary to assess the accuracy of budget projections and to hold the government to account for delivery. Question 56 records how often respondent countries publish information on revenues and expenditures during the course of the fiscal year. The responses are reported in Table 2.2.15. Nine of 25 countries report

producing either weekly or monthly information, nine publish this information quarterly and three every six months. More worryingly, four countries only publish such information annually, preventing any significant monitoring during the course of budget execution.

Table 2.2.15: Frequency of in-year reporting

Q56: How frequently do you publish information on actual revenues and expenditures during the fiscal year?	Countries
Weekly	Burkina Faso
Monthly	Botswana, Ethiopia, Liberia, Malawi, Morocco, South Africa, Tunisia, Zimbabwe
Quarterly	Benin, Congo (Brazzaville), Kenya, Madagascar, Mali, Mozambique, Rwanda, Sierra Leone, Zambia
Every six months	Ghana, Guinea, Uganda
Annually	Lesotho, Mauritius, Namibia, Nigeria
On an ad-hoc basis	None
Not at all	None
No data	Swaziland

Finally, Question 69 looks at the public availability of audit reports. According to the results presented in Table 2.2.16, 15 of the 26 countries always publish reports, while six countries never or rarely do. Amongst the latter group are countries like Congo (Brazzaville) and Liberia, where the external audit function has recently been reconfigured, or like Guinea and Sierra Leone, where they are experiencing serious constraints and backlogs. The practices that emerge in these countries over the next few years will be crucial in defining the contribution of these audit reforms to fiscal transparency.

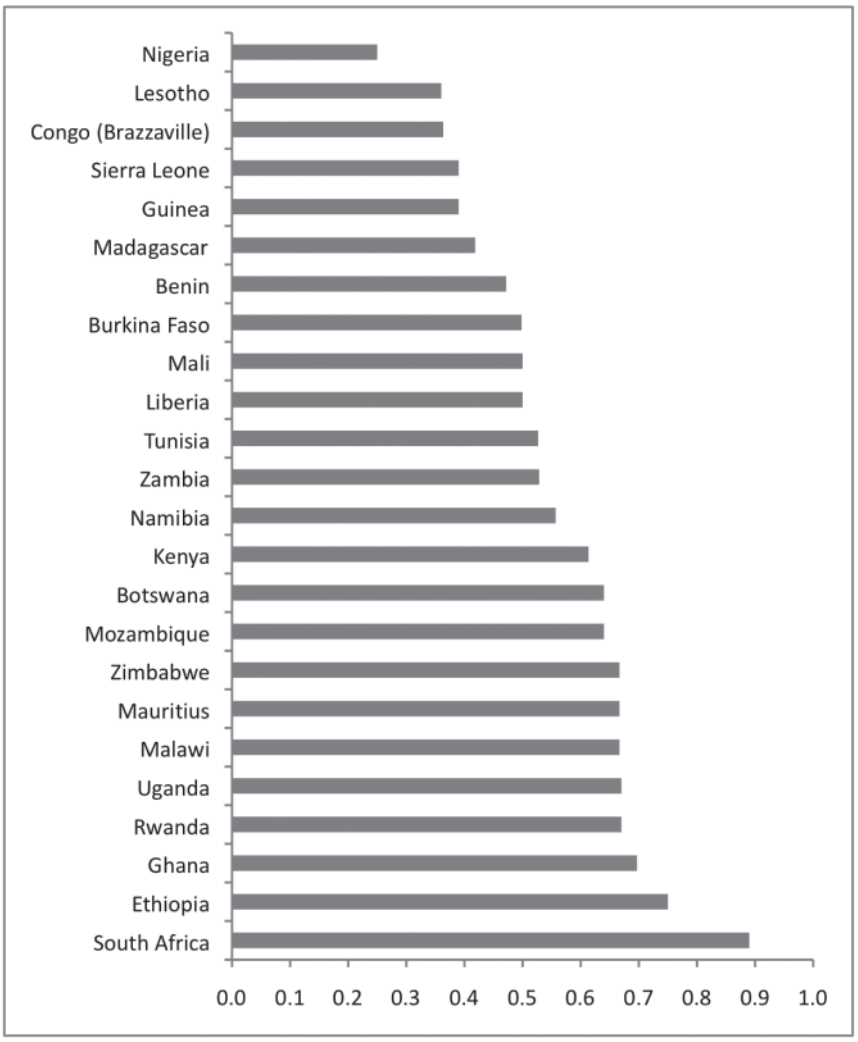
Table 2.2.16: Public availability of audit findings

Q69: Are the findings of the supreme audit institution available to the public?	Countries
Never	Congo (Brazzaville), Liberia, Tunisia
Rarely	Guinea, Nigeria, Sierra Leone
Yes, in most cases with some exceptions (e.g. audits of the military)	Benin, Botswana, Burkina Faso, Madagascar, Zambia
Yes, always	Ethiopia, Ghana, Kenya, Lesotho, Malawi, Mali, Mauritius, Morocco, Mozambique, Namibia, Rwanda, South Africa, Swaziland, Uganda, Zimbabwe

In order to provide an overall comparative assessment of the level of fiscal transparency across the African countries involved in the survey, Figure 2.2.3 presents a summary index based on the questions presented above. To account for the

timeliness of reporting, the availability of audit reports is weighted by the delay with which these are made public. Country scores on the fiscal transparency index range between a maximum of 0.89 for South Africa and a minimum of 0.25 for Nigeria, with a median of 0.54.

Figure 2.2.3: Fiscal transparency index



Note: Refer to the main report for full details about the coding scheme.

What the survey results show is that there remains substantial variation in fiscal transparency across African countries, although several countries appear to publish

substantial amounts of fiscal information. While this clearly should be valued positively, it should also encourage countries that are lagging behind to focus on both producing and publishing more and better quality budget information, in formats that promote broad access and understanding.

Off-budget spending

Linked to the principle of transparency is that of comprehensiveness, which requires that all government revenues and expenditures should be subject to budgetary mechanisms and procedures, as recognised already by the early budgeting theorists (Sundelson 1935) and more recently by assessment tools such as the PEFA framework (PEFA 2005). Comprehensiveness is a prerequisite for transparency, which, in turn, allows for better accountability (CABRI & SPA 2008). Yet, there are categories of government expenditure that often are not subject to normal budgetary procedures and are not included in budget documentation, thereby reducing the degree of transparency of fiscal operations, while at the same time creating potential liabilities that can undermine fiscal sustainability. Such categories of expenditure include, among others, social security funds, loan guarantees, public sector pensions and donor funds.

The survey questionnaire attempted to gauge the extent and importance of off-budget spending across the participating African countries. The results suggest that there are several challenges to address in integrating off-budget spending into the budget process. Even though a majority of countries report that most categories of off-budget spending do not exist in their system, in the applicable cases (i.e. where off-budget spending exists), its nature is often neither accountable nor transparent, given that in about half of the cases it does not require legislative authorisation and information is not included in the budget documentation. Another thing to note is that many countries report very few categories of off-budget spending, even though some of them are quite common. Countries such as Burkina Faso and Mali, for example, state that there are no off-budget donor funds.

For many African countries, however, donor funds are a particularly important category of spending, which is often kept off-budget and implemented directly through donor-managed projects or other parallel systems. Question 99 in the survey asked respondent countries to attempt an assessment of the extent to which aid flows are captured in different budget documents. While Ghana, Kenya, Ethiopia, Mali and Uganda claim to have medium-high coverage of aid flows at different stages of the budget process, in countries like Burkina Faso, Sierra Leone and Mozambique coverage is much less consistent and comprehensive. Moreover, not only do more countries report coverage at earlier stages of the budget process than during

execution, but also coverage values are higher for budget formulation documents. Some of the comments provided by respondent countries are interesting and point to the difficulties that governments face in capturing aid data in budget systems, mostly due to donor fragmentation and lack of transparency and predictability in aid flows. In many cases, coverage is limited mostly to loans and to aid that is channelled through direct budget support, while project aid often remains off-budget.

The data reported are likely to be both incomplete and potentially unreliable, being based on subjective estimates provided by officials within the finance ministry who may not have had all the necessary information available at the time of filling in the survey questionnaire. Recently, CABRI completed a cross-country study of 'putting aid on budget' (CABRI & SPA 2008), which highlights not only the challenges that African governments and their donor counterparts face when trying to ensure that aid flows are captured in country budgets, but also the difficulty of clearly defining what 'on-budget' actually means, in order to pursue the joint objectives of better comprehensiveness, transparency and accountability in budget processes. The data reported in the CABRI study only partially confirm our survey responses. While in both reports countries such as Ghana, Kenya and Uganda manage to capture higher percentages of aid in their budgets, data for Rwanda and Mozambique, for example, are not consistent across the two sources (CABRI & SPA 2008: 21–24). This points to the fact that this area is one where more work is needed in order to come to a better and more complete picture of the inclusion of aid flows in country budget processes and documents.

Aid management

When external development assistance represents a sizable share of public spending, the ways in which foreign aid flows are managed are an important factor affecting the quality of policy and budget processes across Africa. In recent years, an international consensus has formed on aid effectiveness, highlighting the importance of aid being channelled through government systems, and in support of policies and interventions defined by the recipient government (OECD 2005). While much of the emphasis has been put on changing donor practices, effective aid management systems within the recipient government are key to ensuring an effective use of aid flows. In recognition of this, an additional section on aid management was added to the survey questionnaire, to gather information on how African governments organise themselves to deal with donor-funded programmes and projects and incorporate them in their policy and budget processes. CABRI has also carried out a series of case studies to look at how governments in sub-Saharan Africa can properly capture aid flows in the different stages of the budget process (CABRI 2007: 160–184).

From a recipient government perspective, there are three fundamental issues shaping the government's capacity to manage foreign aid flows effectively: the first relates to the structure of government *institutions* that have responsibility for dealing with the donor community; the second deals with the *policies* that governments put in place to manage and co-ordinate donor activities; and the third is based on the *information* that allows the government to capture aid flows better at different stages of the budget process. More effective aid management systems help uphold key budgeting principles such as comprehensiveness, transparency and accountability. These three dimensions are combined in an index, which is based on a number of survey questions on aid management (Questions 90 to 99).

As far as institutions are concerned, Question 90 (see Table 2.2.17) looks at who is responsible for the aid management function. Responses reveal a great degree of fragmentation, with 16 of the 26 countries reporting that two or more government units are jointly responsible for aid management. Most frequently, responsibilities are divided between various ministries (finance, planning, foreign affairs) and sometimes between those and the president's office. This inevitably makes the task of ensuring the adequate integration of all aid flows into the budget process more complex. For the seven countries that responded that their aid management responsibilities are all within the ministry of finance (or the CBA), the task will be somewhat easier. An additional important institutional characteristic relates to how negotiations with donor agencies are carried out when designing new aid projects/programmes. In some countries, line ministries are given more freedom to negotiate directly with donors without involving the ministry of finance. Once again, the more freedom they have, the more difficult it is to ensure the full integration of all aid flows in the budget.

Table 2.2.17: Location of the aid management function

Q90: Where is the aid management function located?	Countries
There is no specific unit responsible for aid management	None
In a single unit within the CBA	Botswana, Ethiopia, Lesotho, Madagascar, Mauritius, Rwanda, South Africa
In a single unit separate from the CBA	Kenya, Malawi, Namibia
It is split between two or more units	Benin, Burkina Faso, Congo (Brazzaville), Ghana, Guinea-Conakry, Liberia, Mali, Morocco, Mozambique, Nigeria, Sierra Leone, Swaziland, Tunisia, Uganda, Zambia, Zimbabwe

Looking at aid management policies, Table 2.2.18 shows how such policy statements have been adopted by a majority of countries. There are two shared characteristics. Firstly, in the countries that took part in the survey, legislatures are never involved in

their approval. Secondly, more often than not aid management policies are subsumed within other documents, typically a Poverty Reduction Strategy Paper or similar policy statement. While these are not necessarily problems, they point to the fact that aid management is not seen as a key policy area that deserves specific attention, not only by the executive, but also by oversight institutions that ensure budget accountability.

Table 2.2.18: Aid management policies

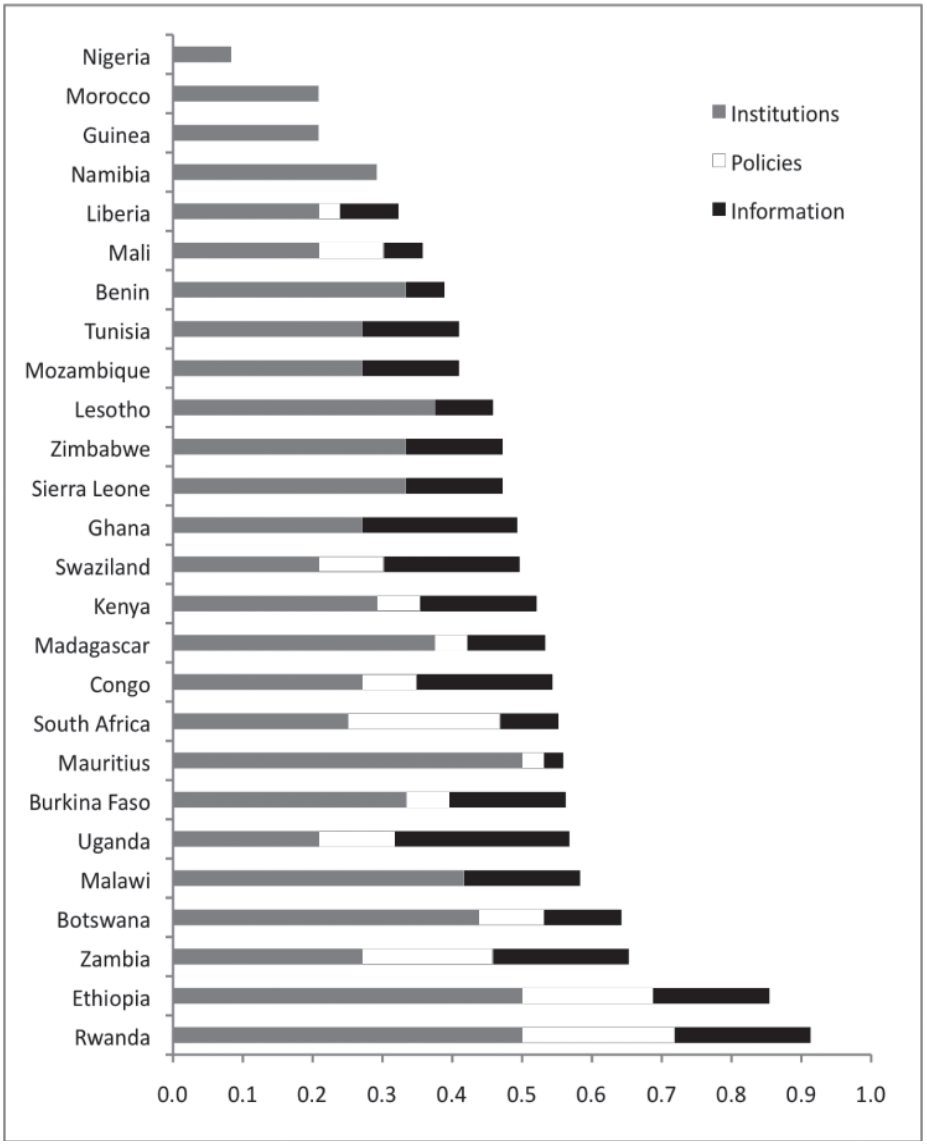
Q91: Does your government have an explicit aid management policy?	Countries
No, there is no such policy	Benin*, Ghana*, Guinea-Conakry, Lesotho, Malawi*, Mozambique, Namibia, Nigeria, Sierra Leone*, Tunisia*, Zimbabwe
Yes, in a specific document approved by the legislature and Cabinet	None
Yes, in a specific document approved by the legislature only	None
Yes, in a specific document approved by the Cabinet only	Ethiopia, Mauritius, Rwanda, South Africa, Swaziland, Zambia
Yes, as part of another document	Botswana, Burkina Faso, Congo (Brazzaville), Kenya, Liberia, Madagascar, Mali, Morocco, Uganda

*Note: *Aid management policies are currently being drafted in these countries, or exist but have not been approved by either Cabinet or the legislature.*

Finally, in terms of information flows, Question 94 asked whether the aid management unit keeps a database of incoming aid flows, which allows it to effectively track donor-financed activities and integrate them into the budget. Most countries (23 of the 26) report the existence of such a database, but with a coverage that varies and hovers around 60–80% of total aid flows. Similarly to the issue of off-budget spending, estimating the coverage of such databases can be tricky, however. Loan-financed activities have better coverage, given the recipient government's responsibility for repayment, but responses on grant coverage need to be viewed more carefully, as they are often limited to programme aid modalities like direct budget support.

The information obtained from the survey questions above, plus others included in the section on aid management, which give more detail on the contents of aid policies and aid databases, can be summarised in an index that highlights how each country has taken steps to put in place a more effective aid management system. The aid management index presented in Figure 2.2.4 gives a higher score to countries that have a centralised aid management function, including not allowing line ministries to directly negotiate donor funding, and that have a comprehensive aid management policy and aid flows database. Scores range from a maximum of 0.91 (Rwanda) to a minimum of 0.08 (Nigeria), with a median value of 0.49.

Figure 2.2.4: Aid management index



Note: Refer to the main report for full details about the coding scheme.

Clearly, for countries whose dependence on foreign assistance is limited, like Nigeria, Namibia and South Africa, aid management systems are not as important as they are for countries where a large percentage of public spending is externally financed. In general, as is evident from the Index, survey results seem to indicate that countries are

reasonably well placed in terms of the necessary institutions, and to a lesser degree as far as information flows are concerned. The main missing ingredient seems to be a clear policy statement that guides the overall relationship between the government and the donor community.

Conclusions

This analysis of the results of the 2008 CABRI/OECD Africa Budget Survey in many ways confirms a number of recent strands of CABRI work. First of all, the survey highlights the variety of practices and procedures that characterise African countries; for example, with respect to budget timelines, to the adoption of 'top-down' budgeting approaches, and to the role of parliaments. These differences are the consequence of several factors, from administrative traditions to ongoing reform efforts, to past and current political and economic realities. An important consequence of this is the fact that it might be difficult to identify ready-made recipes that can contribute to improving budget practices across the continent, as improvements will depend on tailor-made interventions that are designed to address specific issues within each country's budget system. Past CABRI activities and annual seminars have highlighted this issue numerous times.

Secondly, and more substantively, the results identify a number of significant challenges for African countries. The need to increase transparency and address the issue of off-budget spending, for example, is one area clearly in need of attention. In many cases, country responses reveal the lack of availability and comprehensiveness of budget information, which, in turn, can have a severe impact on accountability and the 'challenge function' in the budget process (CABRI 2006), and can undermine coherence and co-ordination in policy-making (CABRI 2005). The lack of clear policies, better institutional co-ordination and quality of information flows in aid management, and the weak basis of medium-term budgeting frameworks, are additional areas where there are serious shortcomings. Especially for those governments that depend heavily on donor funding, a more proactive management of aid flows could bring about significant benefits in terms of 'putting aid on budget', and improve the capacity of the government to adopt a medium-term perspective (CABRI & SPA 2008). Finally, budget execution and audit procedures show room for improvement and possibly deserve more attention in future CABRI activities.

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2.3 Experiences of Anglophone early reformers

Dr Bode Oyetunde[1]

Introduction

Even where circumstances are similar, and similar reforms are attempted, a country can face unique problems in managing its reform path. Country-level uniqueness should be heeded more when reform packages are designed. This was one of the conclusions reached during a discussion on the budget reform experiences of eight countries with Anglophone-type systems, which participated in the Dakar seminar and which may be described as 'early reformers' with respect to their level of development in public financial management, in general, and budgeting reforms, in particular.[2] Some of the participating states (for instance, Liberia, Sierra Leone

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2 Namely, the Gambia, Lesotho, Liberia, Nigeria, Rwanda, Sierra Leone, Swaziland and Zambia.

and Rwanda) are post-conflict states. Others (such as Nigeria and Swaziland) have embarked only recently on systematic and modern budget reforms.

The discussion within the group of 'early reformers' was aimed at sharing and learning from the various countries' experiences on their unique journeys. A presentation by the delegation from Liberia on their country's experiences served as the precursor for further discussion (see elsewhere in this chapter). The discussion continued with brief presentations and contributions from each country, drawing out common themes, issues and experiences.

This process identified inimitable issues, experiences, reform priorities and approaches that characterised each country's distinctive and unique path to reform, despite fairly common objectives. The group's discussion converged on key points of note that applied to each country, but raised applications and implications for all.

Common themes and issues

Several common issues arose during Group III's discussions. *Enhancing budget transparency, credibility and comprehensiveness* was one common reform objective. By allowing greater participation by the public, media and legislature in the executive budget preparation process, countries such as Nigeria and Zambia sought to increase budget transparency, lending greater credibility to the outcomes of the process. Also, for the many countries that received relatively high levels of donor aid or had significant sub-national expenditures at the local government level (like Rwanda and Sierra Leone), improving the comprehensiveness of budget information by putting aid on budget and channelling aid flows through local budgeting systems was a priority.

Given the focus of the Group III countries on commencing budget reforms, it was not surprising that a common issue was how best to initiate, accelerate and *deepen public financial management reforms*. Many of the countries within the group were in the process of undertaking diverse reforms towards implementing medium-term expenditure frameworks (MTEFs), introducing performance-based budgeting systems and improving efficiency, transparency and value for money in their public procurement systems. Lesotho, Nigeria, Sierra Leone and Swaziland all shared experiences in grappling with this issue and the related challenges.

For those countries that received high levels of donor aid, *improving aid co-ordination and management* presented common challenges. Lesotho, Sierra Leone, Swaziland and Zambia all related experiences of seeking to channel aid flows through local budgeting systems and managing the efforts of donor countries and organisations to support their public financial priorities.

A final common thread woven through the countries' experiences was that of *managing off-budget spending, particularly sub-national spending and tax expenditures*. This issue was accentuated in countries with federal structures like Nigeria. Rwanda, Sierra Leone and Swaziland also shared their views on their experiences with this common issue, with a particular focus on how to channel all public expenditure through the budget and how to enhance central co-ordination of information on tax and other fiscal incentives provided by various tiers of government.

Unique experiences and issues

During the conversations among the countries of Group III, issues unique to each country cropped up: these were related to underlying problems – sometimes structural – in the public finance management system that had to be resolved sooner rather than later for other reforms to succeed. Alternatively, they were related to unique tools or approaches for improving budgeting, which countries have prioritised, or to short-term country-specific circumstances that affected budgeting.

For the *Gambia*, the idiosyncratic issue was enhancing budget formulation and monitoring based on poverty reduction initiatives, which also influenced the set budget ceilings. *Lesotho* struggled with challenges in advancing procurement reforms and, particularly, the decentralisation of processes from the central tender board to the procuring ministries, departments and agencies of government. *Liberia* had the peculiar predicament of trying to reconcile the balanced budget requirements of the Heavily Indebted Poor Countries (HIPC) initiative with the need to repeatedly prepare and present supplementary budgets for legislative appropriation of new donor aid required to bridge fiscal deficits.

Nigeria faced the atypical challenge to increasing budget comprehensiveness and transparency of coping with constraints imposed by the constitutionally guaranteed fiscal autonomy of sub-national governments in the federal system. These legal and political conditions impeded efforts to compile, analyse and disseminate information on consolidated national accounts, public finances and tax expenditures. *Rwanda* was the only country that ranked its gender-responsive budgeting programme very highly and sought to introduce a gender budget statement by the 2010/11 fiscal year. On the other hand, *Sierra Leone* was facing acute fiscal constraints and shortfalls, due to the severe decline in donor aid precipitated by the global economic slowdown. *Swaziland* was in the singular position of having to recommence key public financial management reforms (such as transitioning to a MTEF) after a false start. Finally, while all countries were coping with the reality of the global economic downturn, copper-

reliant *Zambia* was dealing with a mélange of reduced revenue from commodity exports, increased capital flight and rapid currency depreciation.

Key points of note

After exploring the similarities and differences evident in each country's experiences, the workshop concluded with three important key points of note. Firstly, to succeed in their efforts, *countries had to prioritise and focus on the most pressing areas of reform* (by basically asking, 'What are we trying to achieve?'). Countries often end up with very ambitious and wide-ranging reform agendas and a high risk of doing everything but achieving little. However, being circumspect and closely examining what they were trying to achieve depended on the next direction of inquiry: *countries needed to understand why these issues were pressing priorities*. Articulating rationales in this way was a prerequisite for determining the nature and sequence of the next steps required to resolve current challenges and advance ongoing efforts at reform. Finally, it became apparent that *despite the similarities in the various countries' reform experiences, country circumstances were often unique and non-comparable, requiring appropriately individualised approaches, strategies and interventions*. A clear example of this was the varying degree of dependency on donor aid. For Liberia, this source amounted to 68% of the funds committed to the country's US$1.6 billion Poverty Reduction Strategy. Conversely, in the case of Nigeria, donor aid flows amounted to less than 1% of the aggregate funds appropriated by the federal budget. How these two countries approached putting aid on budget would need to be different. Consequently, the countries in the group recognised that home-grown, country-specific reforms were imperative as, clearly, one size did not fit the circumstances of all.

Future policy priorities and rationale

Armed with these new insights and perspectives, each country considered its own path towards reform, drawing lessons from the experiences and examples of other countries, which could shape and inform reform priorities and rationales. For the *Gambia, Lesotho, Sierra Leone* and *Swaziland*, the paramount priority was enhancing aid co-ordination and management, recognising the importance of aid to their public financial management agendas and the need to implement and consolidate on best practices. However, the secondary priorities of these countries varied. The Gambia needed to develop sectoral capacity to implement its MTEF. Similarly, Lesotho was focused on ongoing public financial management reforms, but these extended beyond the MTEF to encompass audit processes, reporting procedures and procurement

reforms. Swaziland's secondary reform imperative was to upgrade its budget processes, particularly by improving the timeliness of budget preparation and by implementing an MTEF over the next two to three years. However, Sierra Leone's secondary focus was rather different and concerned the need to better manage off-budget spending and so improve the level of budget comprehensiveness.

For *Nigeria* and *Rwanda*, deepening public financial management reforms ranked equally high on their respective agendas. However, whereas Nigeria prioritised deepening public financial management reforms over increasing budget openness, transparency and credibility, Rwanda did the opposite. Nigeria was intensifying efforts to consolidate early gains from its MTEF and the rolling Medium-Term Sector Strategy programme, which underpinned the capital budgeting process. The country was also preparing for the introduction of a programme variant of the performance-based budgeting system in the near future. Nigeria's secondary reform priority was to learn from recent experiences to ensure better engagement with the legislature and other key stakeholders to improve the budget process, public participation, budget transparency and credibility. However, for Rwanda, this emphasis on improving budget openness and transparency was the number one priority, given the need to address past lapses. Deepening public financial management reforms was an important, though secondary concern, as the country accelerated enhancements to its MTEF, Integrated Financial and Economic Management Information System, chart of accounts classification and budget comprehensiveness, placed greater emphasis on tracking deliverables by the ministries, departments and agencies, and increased the linkages between the planning and budgeting functions.

Similarly, *Zambia* ranked deepening public financial management reforms as its primary reform concern by focusing on the provision of an appropriate legal and regulatory framework to institutionalise these efforts. Due to the importance of aid to the Zambian fiscus, improving aid management processes and procedures was a close secondary reform imperative.

Liberia had three reform priorities that preoccupied its reform agenda. The first was capacity-building for the executive and legislative arms of government to help the executive ministries, departments and agencies to highlight outputs as well as to improve the organisational capacity of the legislature to manage its responsibilities in the budgeting process. The secondary reform imperative was to develop a more open and accountable budget process. Finally, given circumstances similar to those pertaining in the Gambia, Lesotho, Sierra Leone and Swaziland, the Liberian delegation identified improving aid co-ordination and management as a key (though tertiary) priority, given the unquestionable importance of aid in its fiscal management strategy.

Conclusion

In précis, the recent experiences of the countries in Group III in advancing public financial management reforms may be likened to Mandela's proverbial long walk,[3] in that after climbing many a great hill on the road to reform, each country found that there were indeed many more hills, some great, some not so great, to climb. Happily, these countries discovered each other, out and about on these hills, engaged in similar, though not identical, pursuits. These countries also found that by resting and lingering for a moment among the rich, varied and shared experiences of other fellow travellers, each country was inspired and encouraged to make a success of their individual, though common, trek.

3 Mandela N (1994) *Long walk to freedom: The autobiography of Nelson Mandela*. New York: Little, Brown & Co.

2.4 Liberia: An early reformer perspective

Anthony Meyers
Note compiled by Caroline Mulliez

Since the end of the civil war in 2003, Liberia has had to face the task of rebuilding its public institutions. An important aspect of this, post-2006, has been the establishment of effective budgeting and Public Financial Management (PFM) systems. Through the reshaping of the policy and administrative framework, hard expenditure ceilings, clear linkages between spending and outputs, strict cash-flow management, an accountable and time-bound procurement system, and the establishment of frameworks to increase budget resources, some success has been experienced.

Table 2.4.1: Liberia at a glance

Population	3.6 million
GDP per capita (US$2 000)	134
Central government revenue (as % of GDP)	5.4
External debt (as % of GDP)	102.4
Net aid (as % of GDP)	43.8

Source: World Bank (2008)

The reforms

The civil war in Liberia had a devastating impact on the capacity of the public sector to deliver basic public services. Collapse of government revenues, lack of human resources, as well as a breakdown of systems and procedures for public management, contributed to the deterioration of the financial management system of Liberia. As such, the budget process before 2006 was characterised by a weak or non-existent administrative and policy framework. There was no real linkage between the resource outlay and the final output: what was prescribed in the budget was hardly a reflection of the real allocation of money. This collapse of the system of financial management, a sign of poor governance, provided opportunities for revenue leakages and damaged relations with donors. Accountability and transparency were very limited: the government, the legislature and civil society were unable to trace, monitor and explain the differences between the approved and the executed budget. Finally, the unsustainable debt burden (US$1bn internal and US$4bn external) prevented Liberia from accessing multilateral sources of finance.

A new government, headed by President Ellen Johnson Sirleaf, took office in 2006 and implemented a series of reforms, including the development of a poverty reduction strategy (PRS). Restoring good governance and sound financial management were key objectives of this initiative.

Liberia started its reforms by strengthening the policy and administrative framework of the budget process. Internally, these reforms were driven by a clear recognition of the importance of an open and disciplined budget process. This resulted in a drive to improve the quality of the budget process between the finance ministry and spending agencies by making it more consultative and its processes and decision-making more transparent. Greater discipline was introduced into the processes through establishing clear budget regulations and enforcing them. A budget law was enacted and a prescriptive budget calendar was established. Budget guidelines and budget circulars now regulate the interaction between the finance ministry and spending agencies, and budget implementation is governed by a series of financial rules and ordinances. The finance ministry recognised the value of a budget process that is open to external stakeholders; consequently, the process includes key points for information sharing and public participation.

These internal reforms were complemented by the efforts of Liberia's development partners. The Liberia Governance and Economic Management Assistance Programme (GEMAP), which was initiated in late 2005, is a core partnership in economic governance between the government of Liberia and the international community. With regard to the reform of policies and the administrative framework for PFM,

it supported reforms in financial management and accountability and in budgeting and expenditure management, including the establishment of a commitment control system, the development of the Liberia Expenditure Control and Accounting Programme software, the elaboration of a cash management system and the development of an Integrated Financial Management Information System. In the area of procurement and concessions practices, it supported the enactment of a new procurement law and the establishment of institutions to ensure transparent and fair procurement. GEMAP is an important vehicle for donor co-ordination in the PFM area, and includes support for the development of systems, vital institutions and capacity building. Key donor programmes, such as the Poverty Reduction and Growth Facility of the International Monetary Fund, are linked to the GEMAP.

The Heavily Indebted Poor Countries (HIPC) Initiative in Liberia can be linked to important policy and administrative reforms; for example, the establishment of a medium-term fiscal framework, reform of the tax code, the undertaking of periodic audits and the enactment of PFM legislation. The HIPC Initiative also triggered the integration of the Bureau of the Budget into the Ministry of Finance, a key institutional reform. The HIPC Initiative, in turn, is linked to the PRS, the implementation of which is a key condition for debt relief.

A second aspect of the Liberian reforms was resource maximisation; this part of the reforms rested on two legs, namely the clear linking of spending proposals with policy and the enforcement of hard expenditure ceilings. Clear linkages are now made between spending and expected outputs: every item on which expenditure has been incurred has to serve one of the objectives expressed in the policies. There is also a strategic prioritisation of the policies and of the budget dedicated to them, in line with the PRS. For example, high importance has been given to the HIPC programme and the Kimberley Process, which was a key priority towards achieving good economic governance and macroeconomic and revenue stability for the Liberian government.[1]

The ceiling system makes appropriate distinctions during budget preparation and budget execution between recurrent and non-recurrent expenditures over a multi-year period, and between essential and non-essential programmes. Allocations aim to achieve appropriate trade-offs between recurrent and non-recurrent spending within hard spending ceilings over the medium term, taking into account short- and long-term spending rigidities. In the allocation of funds, precedence is given to the

1 After being certified under the Kimberley Process Certification Scheme as being able to control the production and import and export of diamonds, Liberia is now able to export its rough diamonds into the legal diamond trade. This was a consequence of improvements in the financial management of, and governance in, the mining sector resulting from the programme.

essential programmes for spending, thereby sharpening the alignment of spending with priorities.

A third key aspect of the Liberian reforms concerns cash management and budget execution control. Liberia has had to ensure that the improved allocation of available resources through the budget is translated efficiently into spending.

A significant problem faced in this regard was matching available cash from revenue collection and donor disbursements with spending demand. Like many other CABRI countries, mismatches between cash flow and spending demand led all too easily to service disruptions, stop-start project implementation, expensive procurement and costs associated with the late payment of bills. In response, Liberia has strengthened the functioning of the cash management committee that controls the match between available cash and spending agencies' expenditure plans, and has instituted a system of rolling cash plans and dynamic spending plans, which allow for the identification of more flexible spending, and which can be rolled over forwards and backwards in order to create greater alignment without interrupting the funding of core activities.

The second leg of Liberia's drive for improved efficiency is tighter governance of procurement. The Public Procurements and Concessions Act, which came into effect in January 2006 and which is considered Liberia's first significant step towards improved transparency, provides a framework for sound, time-bound and accountable procurement. It also links the initiation of procurement processes more tightly to the availability of funds through budget approval processes.

Finally, Liberia has had to increase its revenue resources to reduce the debt burden and provide better public services. This was achieved through two means. First, efforts were made to modernise domestic tax and customs systems, supported by clear legislation and regulations, modern procedures and automated systems. In the administration of revenue, revenue accounts are now consolidated for centrally generated revenues and for the dispersed administrative charges and fees, allowing for better support to the budgeting and revenue forecasting functions of the finance ministry. In customs, for example, a strict and modern pre-shipment and destination inspection regime is enforced. There has also been a great move towards automation through the implementation of the computerised Integrated Tax Administration Software and the Automated System for Customs Data. In addition, Liberia is trying to integrate as much aid as possible into its budget, to be able to account for off-budget aid and to channel funds to growth sectors and sectors that are critical for social development.

Gains

Liberia has achieved successes in six areas, by virtue of these numerous reforms to its PFM system. First, there is now a visible link between the resources engaged and the goals Liberia is trying to achieve. Budgets are underpinned by policies: the budget of the financial year 2005/06 has been recast to reflect the policy of the new government, and the PRS has anchored the budgets of the financial years 2006/07 and 2007/08 and will determine budget policy from July 2008 to June 2011.

Second, general adherence to the legal framework has been observed. The OECD International Budget Practices and Procedures Database also reveals the great legislative 'power of the purse' now in place in Liberia. For example, the legislature has unrestricted powers to amend the budget, a supplementary appropriation law/budget has to be approved by the legislature before any overspending can occur, and ministers are restricted in their power to reallocate funds between items within their responsibility. These measures make the government more accountable to citizens.

In recent budgets, the appropriation law has been followed more scrupulously, signalling the effective application of the new legal framework established under the reform programme. Also, the new Standards for Audit Institution required by the Constitution is now functional; the General Auditing Commission, created as an independent and autonomous government body in 2005, started its work in 2007. Prior to 2005, the Auditor General reported to the President, but that compromised the ability to monitor the executive branch of the government and there was no formal mechanism for the legislature to monitor the effective use of budgetary resources. Nowadays, the General Auditing Commission is still appointed by the President, but with the consent of the Senate and it reports to the legislature. Its powers and duties have been better defined in the new regulations.

Third, expenditure inputs and programme outputs are now linked. Ministers have to justify their requests for funds in the budget preparation forms, and the relevance of the spending of each organisational unit is measured against the objectives stated in the PRS programme. The approved budget also links appropriation with deliverables. There is, thus, a tight control of spending, ensuring efficiency in budget utilisation.

Fourth, the budget process has become more structured, predictable and open. Estimates are issued regularly, as required by the budget guidelines and calendar. As a consequence, increased participation by non-governmental and governmental stakeholders has been observed. The publication of draft and approved budgets and periodic out-turns also creates the necessary transparency, contributes to accountability and is instrumental in generating higher public awareness of budget issues.

Fifth, the growth in revenue and budget expenditure has been phenomenal. Budget expenditure – without taking on crippling debt burdens – grew from US$80m in 2005 to US$199m in 2007; the projection for 2009 is US$293m. This will allow better provision of public services and increased capacity of the public sector in general.

Sixth, relationships with donors have improved greatly. Liberia has received over US$20m of direct budget support since 2007, and donors have committed to financing 68% of the US$1.6m necessary to carry on the PRS plan. In addition, there has been some concerted support for completing the process towards Liberia's debt relief.

Ongoing challenges

Despite successes, Liberia still faces some challenges. For example, it needs to increase capacity at the budget authority and ministry, department and agency (MDA) levels to fully benefit from the improved systems that have been put in place. Some of the reforms have also created new challenges; for example, the implementation of the new procurement legislation creates difficulties for smooth, timely budget implementation. As with many other CABRI countries that receive significant support from development partners, the accounting/reporting of off-budget aid and its alignment with budget priorities present budget management issues. However, the improvement of this aspect is not entirely under Liberia's control. Liberia also faces challenges – particularly in the current economic climate – in managing the fiscal constraints under its programmes with multilateral institutions. The challenge of managing the demands placed on it by its development partners and internal stakeholders, and the different pressures on the budget in different directions, is a constant reality for budget managers in Liberia.

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2.5 Reforms in francophone Africa

Yacine Bio-Tchané

Background

On the eve of independence from France, francophone African countries' budget systems were replicas of the French system. These countries retained their coloniser's laws and practices relating to budgeting. The 1959 ordinance on public financial management remains the primary law that defines the legal budgetary framework of francophone African countries. This legacy and legal framework have resulted in similarities between the budget reform issues faced by francophone participants in the seminar: these issues, common reform paths and solutions were discussed in a parallel group session. The group participants – Mali, Benin, Burkina Faso, Congo and the Central African Republic – provided an overview of their reforms in response to the main presentation by Mali (see elsewhere in this chapter).

In 1994, regional economic and monetary unions were created, and francophone African countries were divided into two blocs: the West African Economic and Monetary Union (WAEMU) and the Economic and Monetary Community of Central

Africa (CEMAC).[1] These two regional economic communities were constructed to reform fiscal, budget, procurement, accounting and auditing institutions, laws and practices. Additionally, they have established convergence procedures aimed at harmonising economic and budgetary policies between countries. WAEMU countries have established a multilateral monitoring process that co-ordinates and harmonises public finance policies.

In addition to regional harmonisation efforts in public finances, it is a prerogative of WAEMU governments to transpose the guidelines on the finance law, public accounting regulations, the budget nomenclature and the table of financial operations agreed upon in the Union into their respective national laws. CEMAC countries have elaborated 20 measures to be implemented so as to consolidate public finances and reinforce regional integration, monetary policy and financial reforms.

While WAEMU countries have made significant strides in convergence, CEMAC countries are at less advanced stages, due mainly to political instability in some of the member countries.

Priorities in public financial management reform in WAEMU

Prior to 1994, the public financial management systems in WAEMU countries were weak and inefficient. The systems were characterised by delays in the budget process, centralised payment-authorisation powers, inadequate budget classification and nomenclature and fractured aid modalities (project aid, programme aid and budget support), among other things.

Thus, WAEMU countries have been revising their guidelines on the harmonised framework for public finances. Countries believe reforms are needed to: (a) take into account the new tools developed at international level; (b) rectify deficiencies and inaccuracies in the initial directives; (c) ensure more transparency and optimal allocations; and (d) improve comparability.

The focus of the reform programme is on the following areas:

- a transparency code for managing public finances;
- a table of financial operations;
- finance law;
- the regulation of public accounting;
- accounting; and
- budget nomenclature.

1 WAEMU member states are: Benin, Burkina Faso, Côte d'Ivoire, Guinea Bissau, Mali, Niger, Senegal and Togo. CEMAC member states are: Cameroon, Central African Republic, Chad, Congo, Gabon and Equatorial Guinea.

Heads of state have declared that governments should endeavour to converge by 31 December 2013. This leaves enough time to adjust to the various crises (food, financial and political) that have affected the region.

Budget practices and procedures

Reforms to guidelines for the finance law are pertinent to the expansion of the power of Parliament to be included in reviewing the macroeconomic framework and budgetary policy, specifically for the medium-term expenditure framework (MTEF), and to participate in budgetary debates. In addition, the finance law should include all expenditures covered by internal revenues, and the regulation act must be tabled at the opening of the budget session for the upcoming fiscal year. Furthermore, the budget nomenclature should be amended to take into account new norms of classification stipulated through the Heavily Indebted Poor Countries (HIPC) Initiative.

WAEMU countries are also giving priority to tools that are promoted internationally as being essential to strengthening and improving the quality of public finance systems. These tools are: programme budgeting, MTEFs and strategic frameworks for the fight against poverty. Additionally, governments are looking into incorporating into their systems the IMF's new prescriptions in the *Government Finance Statistics Manual*. They also seek to introduce an analytical framework that aims to assess the durability of budgetary and financial policies of all public administrations. This framework is to include a consolidated table of financial operations (of central and regional governments), assets and liabilities, and current economic and treasury flows.

Accounting

WAEMU countries are changing regulations on public accounting as well as other accounting practices. Firstly, they are emphasising de-concentration of budget execution so that every minister becomes an *ordonnateur principal* (or a payment-authorising officer) and enters into contracts with sector ministries that ensure they apply results-based budgeting. Secondly, they have decided that only accountants be permitted to reduce the complementary period or the lag allowed for completing the revenue and expenditure operations of a given budget year, which are executed at the end of the calendar year. Thirdly, they are introducing accrual accounting and reorganising the different classifications of accounts.

Transparency

A transparency code has been established. It defines the principles and obligations that member states have to respect in their legislation and practices, at both the central and regional level. These principles apply to the entire budget cycle, to the information in the budget documentation (integrity and dissemination to the public) and to assigning clear roles and responsibilities to all actors and institutions involved.

Significant reforms are being undertaken regionally in public financial management, specifically to improve the efficiency of budget practices and procedures, to strengthen accounting practices and to ensure transparency. WAEMU countries acknowledge that reforms can be successful and fulfil their objectives only if a monitoring system is in place, which produces periodical update reports, and if there is an increase in public awareness about the reform programme.

Budget tools

Medium-term expenditure framework

Most francophone African countries adopted MTEFs in the late 1990s. This framework projects government expenditures on a medium-term time frame of three or five years, given the macroeconomic context. Multi-year budgets enable governments to plan sector priorities better and in accordance with available internal and external resources. This is challenging for aid-dependent countries, since official development aid tends to be unpredictable.

Mali, Benin and Burkina Faso were pioneers in the region, and have reached more advanced levels of implementation than have Guinea Bissau, Côte d'Ivoire and Togo, which have been delayed and have experienced setbacks in public finance management due to political instability.

In the more advanced countries, most ministries and some parastatals have elaborated MTEFs. The Ministry of Economy and Finance is in charge of the global MTEF, which includes sector allocations used to finalise sector ministries' MTEFs and their budget programmes. The latter documents are annexed to the finance law; therefore, they are not tabled in Parliament, and are used for information purposes rather than as policy documents. Also, ministries report only on executing the annual budget or finance law.

The use of MTEFs has proved to be far from simple for francophone countries. Improvements have been made, and the budget process has been rendered more participatory: ministries play a more active role in budget execution; the role of the budget office as advisor and technical assistant has been strengthened; and the

ministry of economy and finance has signed performance agreements with some sector ministries.

However, important challenges remain. The first one was explored during the 4th Annual CABRI Seminar in an article entitled 'Burkina Faso: Multi-year budgeting and francophone systems', and is pertinent to the lack of compatibility between WAEMU's legal framework on public finances and multi-year budgeting. The second challenge relates to the weak link between second- and third-year sectoral allocations of the MTEF and the annual budgets of these years. In other words, multi-year planning is not indicative of annual expenditures, and this erodes budget credibility.

The third challenge is related to the second one. Sector ministries' MTEFs, which incorporate sector strategies, and the global MTEF, which incorporates appropriations, are divergent. Again, this shows that the finance law is not a translation of multi-year priorities.

Finally, the global MTEF is not discussed during Cabinet meetings and is not tabled in Parliament.

Consequently, the classical annual budget remains at the forefront of budget practices. Furthermore, regional guidelines, time and capacity prevent budget officials from fully implementing results-based budgeting.

These challenges have been acknowledged by WAEMU and will be addressed through amended guidelines, which will give more prominence to multi-annual documents, change the institutional framework of the budget office, redefine the role of key stakeholders and decentralise human resource management in ministries.

Programme budgeting

Programme budgeting has been introduced more recently in francophone countries. For the past three years, countries have compiled budget programmes that stipulate ministries' objectives and activities over a medium-term period. These budgets are annexed to the finance law in the initial year of the multi-year expenditure framework.

Central to programme budgeting are the design of programmes, the use of performance indicators relating to programme objectives, and the monitoring and evaluation of programmes during their implementation as well as thereafter. Francophone countries are still getting acquainted with the principles and methodology of this budget tool. Budget officers are learning how to ensure effectiveness and sound performance.

Francophone countries are grappling with defining performance indicators, which tend to measure outputs, thus not assessing effectiveness or impact. Also, since each ministry prepares its own programmes, which are then not presented in the finance

law because of the current WAEMU guidelines on budget nomenclature, cross-sector programmes are not taken into account. As a result, budget officers are accountable for executing the budget on a line-item basis and not according to identified programmes or sector priorities. Additionally, the information contained in programme budgets is not consistent with that in line-item budgets.

As francophone countries build the capacity and find ways to adopt guidelines that are more in line with a medium-term framework based on performance, they will have to enhance credibility by ensuring that the finance law is a numerical representation of line ministries' priorities and strategic plans over a medium-term period.

National reform programmes

WAEMU countries' national reforms are in line with their strategic framework for the fight against poverty.

Benin

The government of Benin has undertaken a series of reforms that ensures harmonisation and convergence with WAEMU countries and that places greater accountability on budget officials. Spending ministries are now responsible for the payment-authorisation of their budgets, whereas previously it was the sole responsibility of the budget director. This increases ministries' responsibilities, enhances allocation of funds and renders ministries more accountable during budget execution. Also, a computerised, integrated system for budget preparation has been established to ensure that budgetary data are reliable and that the budget is executed in accordance with the budget calendar. Moreover, budget documentation is harmonised with WAEMU guidelines. Finally, efforts are made to strengthen internal audit institutions so that *ex-post* control is better organised.

Burkina Faso

In 2002, the government of Burkina Faso adopted an action plan for reform in budget management, which initially focused on public expenditures but was revised in 2004 to include state revenues. The action plan was consolidated through a participative process across different departments in the Ministry of Finance and Budget as well as in other ministries, and included recommendations made in the public expenditures review and the report on the observance of standards and codes, as well as WAEMU guidelines. Its objective is to improve transparency and effectiveness in budget management. An institutional framework has been put in place and priorities have been defined on a rolling triennial time horizon. As a result, the calendar for budget

preparation was formalised and the budget circular was sent out in a more timely fashion. Also, the budget nomenclature was adapted to the legal and regulatory framework of WAEMU. The government of Burkina Faso has also de-concentrated payment-authorisation powers so as to give greater budget responsibility to government agencies. In terms of transparency, the government has begun publishing the table of financial operations on a monthly basis and has carried out public expenditure reviews at the global level and for two sectoral ministries. Efforts have also been made to reduce delays in producing end-of-year reports. Finally, an information and communications technology (ICT) strategy has been put in place to computerise accounting tools such as the state's integrated accounting system.

In 2007, the government decided to pursue its reform programme by launching a long-term (until 2015) strategy to strengthen public finances. The strategy covers resource mobilisation (internal and external), results-based resource allocation, effective and transparent public expenditures, timely and exhaustive data on budget execution, and audit systems that are coherent, effective and comply with international standards. The strategy does not neglect the ministry's institutional abilities to fulfil these objectives or the capacity of all actors at all phases of the budget cycle.

CEMAC countries' reform programmes are less advanced and slower in implementation.

Central African Republic

The government of the Central African Republic prioritised good governance in its reforms of public administration in the 1990s. The emphasis is on respecting basic principles of budgeting such as transparency, accountability, participatory practices, effectiveness and efficiency. As a result, current reforms highlight strategies for developing a new culture based on ethics and merit, as well as systematic monitoring, accountability and results.

Congo

The government's reform process in public financial management was triggered by weak human and financial resources, lack of co-ordination and functional links between different actors, the worsening of corruption and fraud, and bad governance in general. As a result, the government has focused its reforms on adapting its budget nomenclature to pro-poor expenditures, requesting that sector ministries develop sector strategies, improving the expenditure chain so as to limit off-budget spending, managing public investments to ensure an effective selection of projects and quality monitoring and evaluation frameworks. Additionally, in 2004, the government

adopted an action plan for the fight against corruption and fraud. Similarly, the government has created a working group, comprising the main national stakeholders in public financial management, to conduct a fiduciary review and to auto-evaluate public finance systems and public service management. Unfortunately, concrete actions have yet to be taken.

Conclusion

In conclusion, it can be said that francophone African countries have embarked on an ambitious reform programme in public financial management, endeavouring to prioritise good financial governance. Several laws have been passed, action plans have been adopted, budget tools have been introduced, budget actors have been trained and institutions have been strengthened. As a result, progress has been made in participatory processes, more frequent in-year reporting of budget execution, wider dissemination of budget documentation and a stronger 'challenge function' played by Parliament. However, the objectives of budget credibility, effectiveness and transparency have not yet been attained. Greater efforts will have to be made to ensure that the legislation and budget tools that are used fulfil their role and that governments benefit from stronger systems and allocative efficiency.

2.6 Mali: A francophone perspective

Abdoulaye Touré
Note by Yacine Bio-Tchané

Mali's budget practices and procedures are legislated by the Constitution, national laws, regional guidelines and criteria of convergence from the West African Economic and Monetary Union (WAEMU). Its reforms have been guided by recommendations of the Bretton Woods institutions as to best practices for budgeting; however, as with other WAEMU countries, it is Ordinance 59 of 2 January 1959 that remains the basis for public financial legislation and the legal framework.

Since 1994, when the CFA franc was devalued and WAEMU was created, several laws have been enacted and reforms adopted for the effective management of public finances. The overall aim of these reforms is to improve the quality and reach of basic social services and to improve the financial systems, with the goal of achieving poverty alleviation. For this purpose, budget reforms were targeted to ensure the efficient allocation of resources, as well as greater transparency in the budget process and accessibility of budget documents.

Table 2.6.1: Mali at a glance

Population	12 million
GDP per capita (US$2 000)	290
Central government revenue (as % of GDP)	16.40
External debt (as % of GDP)	24.50
Net aid (as % of GDP)	14.10

Source: World Bank (2008)

The reforms

Budgeting in Mali is informed mainly by laws and decrees, the President's economic and social development project, the Prime Minister's general policy statement and the strategic framework for growth and poverty. The laws and decrees that were passed to complement the 1959 ordinance and to modernise public finances are as follows:

- In 1998, the Budget Act (*Loi 96-060 du 4 novembre 1996*) entered into force and aimed at adapting financial regulations to current circumstances in the country. The law defines the principles that govern public financial management, specifically state revenues and expenditures, the treasury's operations, accounting, tabling and voting/appropriations of projects in the finance law, and regulatory measures for executing the finance law.
- The Basic Principles of Public Accounting Act (*Loi 96-061 du 4 novembre 1996*) covers the main principles for public accounting (personnel's responsibilities for managing public finances and the process for executing the budget).
- Two decrees complement these laws by determining the rules for public accounting and the general code for procurement.

Thus, the legal and regulatory framework and institutions' responsibilities are clear and well enunciated. There also exist clear rules and procedures for the budget calendar and the presentation and adoption of the finance law.

Budgeting remains the government's prerogative, and while it is most directly informed by legislation, it also evolves from the reform programmes needed to fulfil the objective of improved allocation of resources and transparency, as well as using those budget tools that are considered to be international best practice.

The budget process in Mali

Mali's budget process begins more than six months before the start of the fiscal year to which the budget relates. The timeline is as follows:

- *May*: Budget circulars.
- *May/June*: Period of four to six weeks for secondary authorising officers to prepare budget drafts.
- *July/August*: Technical and ministerial budget arbitrations.
- *Early September*: Budget passed through the Council of the Prime Minister's Cabinet.
- *Mid-September*: Review and adoption of the Finance Draft Bill by Cabinet.
- *End September*: Submission of Draft Finance Bill and the Budget Execution Bill for the previous year to Parliament.

If Parliament does not authorise the budget by the beginning of the fiscal year to which it relates, the government may undertake spending of one-twelfth of the budget, on the basis of the recurrent expenditures of the previous year.

Source: Abdoulaye Touré, Budget Director Mali, presentation to the 2009 CABRI Annual Seminar

In the area of public expenditures, Mali has introduced a new budgetary nomenclature and public expenditure reviews, and has adopted programme budgeting and a medium-term expenditure framework (MTEF). The new budget nomenclature enables: (a) various budget reforms linked to programme budgeting; (b) allocations related to poverty reduction; (c) expenditures made with Heavily Indebted Poor Countries (HIPC) funds; and (d) internal versus external resources used for public expenditures.

Mali was a pioneer in the sub-region when, in 1995, it launched results-based budgeting. In 1998, Mali became the first francophone African country to implement programme budgeting and present a five-year expenditure framework.

The MTEF is a mechanism that allocates resources according to strategic and sector priorities and that renders the budget process more coherent, realistic, predictable and efficient, as it is done on a multi-year basis. All ministries have used MTEFs since 1996, although they still only execute and account for the finance law.

Programme budgeting was adopted in order to improve coherence between budget allocations and policies, to achieve a better appreciation of strategic allocations, especially in social sectors, and to strengthen monitoring and evaluation throughout the budget process. Multi-annual budget programmes are added as an annex to the yearly finance law. The Ministry of Economy and Finance of Mali has commissioned two diagnostic studies with development partners in order to review the structure

and content of ministries' and institutions' programme budgets and to conduct an overall review of programme budgeting. Principal recommendations from the study included: strengthening budget officials' capacity; simplifying the content of the budget document for it to be more accessible and to encourage its use as a strategic tool and as an instrument of consultation, reference and decision; setting up a monitoring system; and integrating programme budgeting into the legal framework of public financial management.

In addition, an annual review of programmes is conducted in every ministerial department and institution. This review is integrated into the budget cycle and aims at taking stock of the activities undertaken in each programme during the course of the year and at analysing the outcomes and perspectives. This is done in terms of the Strategic Framework of Poverty Reduction (SFPR) and the government's policy statements.

Finally, in the area of control or audit, the government has developed tools to reinforce the legitimacy and credibility of audit and to align national practices with international ones. Similarly, a manual on budget execution is published by the government so as to improve budget monitoring.

In 2005, the government of Mali launched an action plan to improve and modernise public financial management (PAGAM/GEF), in order to consolidate the efficiency, transparency and reliability of public financial management. In 2007, PAGAM/GEF was adjusted following the results of a public expenditure and financial accountability study. PAGAM/GEF is built on five pillars: (a) improving the quality of budget preparation and execution; (b) rendering fiscal and financial administration more efficient; (c) integrating external financing into national budget procedures; (d) increasing the efficiency and transparency of procurement; and (e) strengthening good governance and transparency.

In addition, the government of Mali, along with its development partners, has elaborated an action plan for aid management, which specifies actions, indicators, relevant stakeholders and an implementation calendar for the five principles of the Paris Declaration: ownership, alignment, harmonisation, managing of results and mutual accountability.

Transparency and the budget in Mali

Since 2008, the Finance Act has been published in all the principal national languages. Appendices to the Act provide rich additional information, including:

- a report defining the financial balance, the results of the execution of the Finance Act of the previous year, and the results of the execution of the in-year Finance Act as of 30 of June;
- an annex introducing, per chapter and item, the voted services costs and new measures to be funded;
- an annex regarding the phasing out of payments for future years resulting from the authorisation of programmes;
- a list of Treasury special accounts;
- a full list and value of all forms of tax;
- investment operations funded by external resources for which money does not pass through the Treasury;
- all capital expenditure;
- the projected monthly Treasury plan;
- a statement of outstanding payments and of outstanding state debt; and
- any other annex intended for the National Assembly, for information and scrutiny purposes, including the programme budget.

Source: Abdoulaye Touré, Budget Director Mali, presentation to the 2009 CABRI Annual Seminar

Gains

Mali has undertaken an extensive programme of reforms, which has been reviewed and adjusted in terms of performance and which aims to improve the efficiency, transparency and credibility of the budget process: from implementing new budget systems and issuing manuals to explain how these systems operate, to training budget officials and attempting to harmonise development partners' reviews with the country's budget calendar. The country has made great strides in public financial management with enhanced revenue generation, a better command of expenditures and lower debt ratios.

Challenges

However, despite the extensive reforms in public financial management and the progress made, systems fail to achieve the set objectives and remain weak.

First, budget programmes are seen as limited and far from achieving the goal of improving public financial management. For instance, the amounts corresponding with programmed expenditures do not correspond consistently with the amounts that appear in the Finance Act tabled in and approved by Parliament. In other words, budget programmes are compiled parallel to the national budget; it is still not an integrated process. Furthermore, each programme is a description of a department's responsibilities and objectives, with indicators to measure these objectives; and the cost of programmes is based on departmental budgets, not on the programmes' objectives.

Second, the adoption of the MTEF in 2000 coincided with the country's SFPR. While the MTEF enables the assessment of each ministry's budget allocation in future years, it does not allow for verification of the correlation between public expenditures and set indicators. Thus, effectiveness is not assessed. Also, multi-year estimates tend to be unrealistic and incremental rather than based on programme performance. Furthermore, monitoring and evaluation is weak, due to poor staffing of the chambers of account and its personnel's lack of training in analysing public expenditure performance.

Third, the budget process needs to be improved at various points in the cycle (preparation, execution and monitoring and evaluation), and it needs to be more inclusive of all government ministries and institutions. Similarly, the budget timeline has been problematic; delays have occurred and budget officials have had little time to perform their duties. This is particularly problematic when reforms are introduced, and a new results-based culture has to be adopted by civil servants.

Finally, while there is no law that prevents the publication of budget information, it is not generally available in a timely fashion and in a format and language accessible to the general public.

In conclusion, the government of Mali is committed to improving its budget process and making the necessary trade-offs that have the most value for money and that translate into appropriate and effective service delivery. While several laws have been passed, budget reforms have been introduced (mainly the MTEF and programme budgeting), assessment studies have been commissioned and action plans have been undertaken, systems remain weak at the planning, execution and monitoring and evaluation stages. Additionally, some of the reforms are implemented in parallel with the regular budget process, duplicating efforts and undermining principles of multi-annual budgeting and results-based budgeting. Furthermore, civil servants remain untrained and unable to grasp all the new budgeting practices, especially given the limited time available during the budget cycle. Finally, monitoring and evaluation frameworks barely exist and function.

Further challenges to modernising Mali's budget process

Mr Abdoulaye Touré, Budget Director of Mali, highlighted the following challenges specific to the modernisation of the budget process at the 5th Annual CABRI Seminar:

- improve participation in budget preparation, execution, monitoring and evaluation, and accountability;
- improve the budget timeline, thereby giving more time to the secondary authorising officials and the credit administrators;
- establish results-based management with programme budgeting (specific issues discussed alongside) and strengthen the multi-year estimates;
- broaden the deconcentration and decentralisation of the budget;
- finalise the entire spending chain, in order to make budget information available as soon as possible; and
- strengthen the alignment of partners on the budget management system through the harmonisation of the calendar of reviews with the budget cycle.

Nevertheless, the government of Mali pursues its efforts to improve public finances; and through training, stronger systems and budget reforms that are implemented more effectively, it will achieve its objectives of better service delivery and poverty alleviation.

Reference

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2.7 Advanced reformers identify common programme performance budgeting issues

Note by Alta Fölscher

A current priority budget reform for countries with a longer reform track record is the introduction or strengthening of programme performance budgeting. The presentation by Ethiopia emphasised the role of performance budgeting as a leading reform, catalysing changes in how state institutions are structured and the capacity requirements of the system. Consequently, the group discussion in the advanced reformers group was oriented towards the challenges presented by programme performance budgeting. This note is intended to reflect the main themes discussed in the session, rather than being a comprehensive review of programme performance budgeting.

An initial issue concerned the definition of programme performance budgeting. The term 'programme budgeting' was first used in the 1960s to refer to the allocation of funds to programmes that funded priority objectives across government, notwithstanding their organisational location. A water sector programme would fund

water-related expenditure in the water affairs, agriculture and rural development ministry, for example. In this usage, the term was associated also with the identification of objectives and performance measures for the programme, and the monitoring thereof through implementation.

Some of the comments in this session – for example, that of Botswana concerning the difficulties of allocating funds to a water programme across ministries, that of South Africa explaining that it did not undertake programme budgeting but merely performance budgeting, and queries to Ethiopia with regard to how it assigns accountability under programme budgeting – relate to equating the use of the term 'programme budgeting' with the identification of, allocation of funds to, and results-based management of cross-government programmes.

Nowadays, however, the term 'programme performance budgeting' is often used interchangeably with performance budgeting. It refers to the use of performance information in budgets that are classified in (and preferably allocated to) programmes that do not span ministries, but are a dimension of the budget structure by ministry. In other words, programme performance budgeting refers to systems that budget by programme and which link – more or less formally – the funding of public institutions to their performance or their results. When programmes do not span organisations and serve as budget allocation, implementation and monitoring instruments within ministries, departments and agencies, there is no breakdown in the accountability for funds.

Even where cross-government programmes are used, the performance measures framework that goes with the programme can be constructed to assign responsibility for specific outcomes or outputs to specific organisations. While funds are allocated to the programme as a whole, lower levels of allocation within the programme can map cleanly to organisations against the assigned outcomes or outputs. In some ways, such a structure is no different from allocating a transfer payment to an agency from within a ministry's budget against a mandate to fulfil specific objectives or undertake specific activities. These types of mechanism for cross-government programme management, however, critically depend on the quality of the budget classification system: it is only possible to manage such a programme across organisations if the budget and chart of account classification is aligned and multi-dimensional. Therefore, assuring clarity on lower-level political and managerial accountability for cross-government programmes is not impossible; overall political accountability for the degree to which the programme and the combination of outcomes and outputs contribute to the programme's ultimate goals, however, often remains opaque.

A second issue concerned the criteria for defining a programme and the control over programme structures. Participants commented that frequently when the

criteria for what counts as a programme are not clear, programmes can proliferate. When programmes are first introduced into the budget classification, the programme structures are discussed extensively with the finance ministry and technical assistance is available. This results in a relatively neat programme structure. However, three to five years down the line, many additional programmes can be in place which do not group objectives or activities at the same level or according to the same criteria as the first set. This undermines a programme-based budget process. Thus, it is important that ministries of finance approve changes to programme structures.

It is equally important that ministries of finance do not determine line ministry programme structures without extensive consultation. As was emphasised in the responses provided by Ethiopia to queries, the individual institutions should define their own programme structures, as they are responsible for the delivery of services and have better knowledge of how best to structure their programmes as funding, delivery and monitoring and reporting vehicles. Approval by the ministry of finance, however, remains necessary.

The discussion also highlighted that programme performance budgeting is more likely to be successful if countries change the structure of the budget that their parliaments approve. Some countries introduce programme performance budgeting, but the programme budget structure is parallel to a traditional administrative/line-item budget, which remains the form in which the budget is approved. In these cases, programme budgeting processes carry little weight and largely are ignored or undertaken as compliance drafting of documentation. The real focus remains on ensuring that administrative/line-item budget proposals are successful. Participants warned that in such cases the performance targets set in the programme performance budget documentation become wish lists, with weak institutions supporting their realisation.

A related issue is the degree of discretion that is given to ministries to allocate funds within a programme to personnel, goods and services or capital expenditure. Participants pointed out that accountability for performance is weakened when the finance ministry still controls lower levels of allocations. The functionality of programme budgeting depends on ministries having the discretion to cut or increase funding within their overall ceiling to activities, groups of activities, sub-programmes or even programmes, depending on which activities will deliver on their priority objectives. Traditionally, finance ministries have controlled spending by administrative units and line items, such as personnel, transport, communication and consultants. Line ministries, however, know how these line items combine to deliver activities: when budget cuts (or increases) are made by line item, they affect priority and non-priority activities equally and, consequently, the capacity of a ministry to

perform optimally against its priorities within its budget. Any increases in discretion, however, need to be tightly linked to increased accountability for performance to ensure that the incentives that drive allocations are about programme performance.

Another factor that weakens the implementation of programme performance budgeting is when there is a disjunction between budget programme and administrative structures. The Ethiopian presentation set out how the introduction of programme performance budgeting has resulted in realignment of ministries and structures within ministries. If there is a clear mapping between programmes and organisational structure, managerial and expenditure accountability coincide and the performance information used for organisational performance management equals the information used for programme performance management. Participants agreed that resistance to, and the organisational upheaval associated with, changing organisational structures can hinder the effective implementation of programme performance budgeting. At the very least, it can make it a very long process.

Finally, discussants emphasised that programme performance budgeting reforms are not a short-term undertaking. It takes many years to develop programme performance information frameworks and the systems to ensure that the information used to manage programme performance is comprehensive, accurate, reliable, relevant and timely. While it is easier for delivery-type programmes to implement a performance orientation, the process is much more difficult for programmes that provide policy, regulatory or administrative services. For all programme types, however, organisations usually learn through trial and error whether the indicators and methods of interpreting indicators (for example, benchmarking, rating, grading and target setting) provide relevant information for decision-making. Often, just the availability of programme performance information is not sufficient to ensure programme performance: indicators effectively signal past or future success or failure, but do not necessarily tell programme managers and oversight agencies much about the reasons for success and failure. This requires the addition of some form of programme evaluation. Overall, the capacity to use programme performance information to make decisions in the budget process takes time to develop. It also takes time to realign organisational and decision-making structures to a programme budget.

It is against these factors that participants emphasised the need for both a clear vision of how a programme performance budgeting system should develop and a strategy to systematically ensure its development along the selected lines. In the short term, the reform is costly and cumbersome, and the drive to implement it can falter as the benefits are slow to emerge. A key factor is the ownership of the reform: while the ministry of finance might direct and support the reform and reform standards,

the highest chance of success emerges if line ministries need, own and direct its implementation within their domains.

The discussion in the advanced reformers group highlighted the relevance of CABRI's upcoming programme to research and provide guidance on emerging operational practice in Africa relating to the introduction of programme performance budgeting. While the approach to programme performance budgeting is diverse, common challenges remain.

2.8 Ethiopia

Desu Gebre
Note by Alta Fölscher

The budget system in Ethiopia caters for national government, nine regional governments and two city administrations. It is a federal system, with the central government budget including transfers to the regions.

Table 2.8.1: Ethiopia at a glance

Population	77 million
GDP per capita (US$2 000)	161
Central government revenue (as % of GDP)	14.8%
External debt (as % of GDP)	15.3%
Net aid (as % of GDP)	12.8%

Source: World Bank (2008)

Public sector reform in Ethiopia is undertaken through an integrated Civil Service Reform Programme (CSRP), which was introduced in 1996.

The introduction of the reform followed on the realisation by the government that core civil service functions, such as policy-making, financial management and service

delivery, were hampered by a legacy of institutional systems. Key problems were: outdated civil service legislation and working systems; the absence of a medium-term planning and budgeting framework; ineffective financial and personnel management controls; inadequate civil service wages and inappropriate grading systems; poor capacity for strategic and cabinet-level decision-making; and insufficient focus on modern managerial approaches to service delivery (Mengesha & Common 2006).

The programme works in five reform areas: human resources management, senior management, service delivery, ethics and public financial management. In September 2001, the government launched the Public Sector Capacity Building Support Programme (PSCAP), building on the CSRP. At this point, key achievements of the CSRP included the development of new legislation (for example, a financial management proclamation, a civil service law, a code of ethics, complaints-handling procedures and a service delivery policy) and operating systems for budgeting, procurement and some aspects of personnel management (such as salary surveys and records management).

An important part of the PSCAP was to deploy the gains made already under the CSRP to all regions and levels of government. The new programme worked from pilot studies in selected ministries, departments and agencies. Specific steps taken to support the programme were: the establishment of focal points responsible for reform implementation across tiers of government; a series of workshops undertaken to sensitise political leadership and civil servants across the country; and the launch of a 'special programme' designed to deepen the implementation of performance management in priority ministries, departments and agencies – the Performance and Service Delivery Improvement Policy (PSIP) (Mengesha & Common 2006).

Within these programmes, the public finance management reforms are encapsulated in the Expenditure Management and Control Programme (EMCP). The vision of this sub-programme is to create an efficient, effective, accountable and transparent financial management system that will contribute to the economic development efforts of the government.

The EMCP, in turn, consists of eight projects: reform of the legal framework; the government procurement reform project; budget reform; cash management reform; accounts reform; internal audit reform; government property management reform; and a project to develop an integrated financial information management system.

The objectives of the budget reform project were multiple:

- reforming the chart of accounts and developing a new single series of expenditure codes, with the view to replacing the previous three series of codes;

- introducing a financial calendar with detailed steps for the expenditure planning and budgeting processes;
- introducing cost-centre budgeting through budget classification, and integrating the preparation of the recurrent and capital budgets; and
- introducing a new system of budget classification that maps the budget to organisations more consistently and in more detail.

The budget reforms are being implemented at the federal, regional and sub-regional levels of government. Given the difficulty that different budget structures created in the past for the integrated management of resources across levels of government, the establishment of a new budget structure that offers uniformity across regions under the budget reform project is a major achievement. In federal institutions the project has also upgraded budgeting to an electronic platform – the IBEX.

However, there are still shortcomings in current budgeting practices: while the framework within which budgeting is undertaken has been standardised across levels of government and the federal platform has been upgraded, budgeting (as a whole) still occurs under an incremental line-item approach within a one-year horizon. The budget is decided largely by inputs and provides very little information about what resources will be spent on and what achievements can be expected.

One way of addressing this shortcoming is to reform the budget calendar and process to allow for greater emphasis on the discussion of priorities and budget allocations. In addition, the Ethiopian government has opted to introduce programme budgeting. Instead of laying out the budget primarily by line item, the government will move towards a programme-based budget that sets out activities and their associated expenditures by the intended outputs. The aim is to improve the allocation of resources to the government's strategic priorities and to manage expenditure in order to achieve these priorities.

Programme budgeting requires not only a reformatting of the budget, it requires a changed approach in spending ministries, departments and agencies, and changed processes to integrate budgeting more effectively into the management of institutions and programmes. Programme budgeting requires, at the very least, the introduction or strengthening of strategic planning, including the formulation of a vision, mission and objectives for each public body, as well as the definition of programmes with objectives and outputs for each public body.

The intention is that through a programme-budgeting approach, ministries, departments and agencies will be able to present their budgets against more useful information on service delivery. At the same time, the government will be able to present its spending plans together with systematic information on what resources

will be used for. In this way, a programme budget allows for transparency and accountability in service delivery.

The government expects that programme budgeting will allow it and its stakeholders to determine better whether allocations reflect priorities. In addition, it will be able to plan better for the delivery of services and the monitoring of resource use within each programme. Areas in which savings can be made or where more funds are needed will also no longer be identified in terms of inputs – with little understanding of how inadequate (or excess) funds affect service delivery – but by lower and higher priority activities, outputs and programmes.

The implementation of programme budgeting is just starting. Initially, it will be rolled out only at the federal level, where 20 ministries have been selected to pilot the new approach. In preparation for the next budget cycle, training has been provided to the target ministries. The training was focused on raising awareness of approach; it included building ministries' understanding of what programme budgeting entails, comparing the approach with traditional line-item budgets and budgeting, and investigating the advantages and disadvantages of each approach. Finalisation of the programme-budgeting procedural manual and preparation of a technical training module are in progress. The next step will be training staff to implement programme budgeting fully at federal level.

The ministry expects the effective use of programme budgeting to be a long-term project. It anticipates confusion and much trial and error in the short term. Since the reform also means changes in the responsibility of managers, it will entail changes in the long term in how ministries, departments and agencies are managed. Also, while its implementation and annual process burden are cumbersome and time-consuming, and the approach is information intensive, costly and requires a large initial investment in systems and data development, the expectation is that the benefit will outweigh the cost in the long run.

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3

Aid on budget

3.1 Introduction

The effective use of aid resources is an important priority for CABRI participating countries. This interest underpins CABRI's ongoing work with regard to bringing aid on budget. Following on the 2007 joint CABRI/SPA *Putting aid on budget* study, the network has engaged internally and externally through processes surrounding the implementation of the Paris Declaration on the use of country systems and the integration of aid on budget.

This chapter reflects the work undertaken since 2007. The first paper is a summary report on the work undertaken by CABRI with the Rwanda Ministry of Economy and Finance. Using the analytical framework developed for the 2007 study, CABRI undertook research into the different criteria and underlying processes that result in aid flows being 'on plan', 'on budget', 'on Parliament' and/or 'on account'. The paper is written by the project researchers, Clement Ncuti of the Rwandan Ministry of Economy and Finance and Mailan Chiche from Mokoro Limited. This research was used in a stakeholder workshop to develop a set of criteria to determine when aid would be reflected in budget documentation (i.e. be 'on budget') and when it would also be approved by Parliament as part of the Finance Law (i.e. be 'on Parliament'). At the same time, the research highlighted institutional and process issues under the

control of the finance ministry, which the ministry has subsequently taken on board to improve the quantity and quality of aid on budget.

The second paper provides CABRI's response to the 2008 Accra Agenda for Action provisions on the use of country systems. The paper, by Aarti Shah from the CABRI Secretariat, highlights that while it is a critical part of improving aid effectiveness, the use of country systems remains a country-specific undertaking that should take local circumstances into account.

3.2 Bringing more aid on budget in Rwanda

Clement Ncuti and Mailan Chiche

Rwanda's consolidated public accounts for 2007 showed that 30.9% of resources used by general government was provided by donors. Therefore, aid constitutes a substantial share of public resources, and the way in which aid is handled in the budget process is important in effective management of public finances overall. Yet, as the CABRI/Ministry of Economy and Finance (MINECOFIN) research set out below found, in 2007 only 16% of projects and programmes were reported consistently in the aid database, on budget and on accounts, indicating significant weaknesses in the systems to manage and integrate aid on budget.

For this reason, Rwanda was eager to participate in the 2007 and 2008 CABRI initiatives to support African states in bringing more aid on budget more effectively. In 2007, Rwanda was one of five in-depth country case studies underlying the ten-country CABRI/Strategic Partnership for Africa (SPA) *Synthesis Report* and *Good Practice Note* on how countries integrate aid on budget. In 2008, Rwanda was the first country to benefit from CABRI assistance in addressing operational shortcomings in integrating aid on budget.

This paper discusses Rwanda's engagement with CABRI, and the outcomes thereof. While it covers the salient points of the work in general, it provides more detail on particular issues that are of interest to all African countries.[1] It consists of four sections: the first section sketches the background to the joint intervention by MINECOFIN and CABRI; the second section discusses the research and research findings; and the third section considers the workshop findings, while the fourth section looks at the outcomes of the intervention and the way forward for the process.

Background

Using country systems to manage aid is a central tenet of international declarations on aid effectiveness. Most recently, this has found expression in the Accra Agenda for Action, in which the commitment to use country systems is prominent. This commitment is based on the conviction that country ownership of strategy and leadership of aid management are important in determining aid effectiveness and that strengthening of country systems is a necessary condition for the development of sustainable state capacity and, therefore, for poverty alleviation and development.

From a country perspective, the commitment means that the budget system, in particular, needs to integrate aid effectively. After all, it is the system through which public resources are allocated, disbursed, used and accounted for and is an important foundation for the delivery of public infrastructure, goods and services.

While the commitment on aid effectiveness is international, bringing aid into the budget process is also important at the country level, not only for effective use of aid, but also for effective use of a country's own resources. Proper trade-offs between different public purposes and activities using own resources are impossible without knowing what will be done with donor resources. While reflecting information on aid expenditure in various budget documents is a first step, the real challenge is to use country systems fully; in other words, to integrate aid into the budget process in such a way that the budget system itself is used for the management of aid.

The 2007 CABRI/SPA study was aimed at empowering African countries to bring more aid on budget more effectively. The study broke up the budget process and the challenge of bringing aid on budget into its successive parts. Bringing aid on budget would mean the integration of aid on plan, on budget, on Parliament, on Treasury, on procurement, on account, on report and on audit. In practice, however, while aid is rarely integrated in all the phases, it is often integrated or reflected in one or more. Aid-funded projects and programmes can be integrated or reflected in any number

1 More detail on the research, research findings, workshop proposals and outcomes is available from MINECOFIN and the CABRI Secretariat.

and combination of phases, depending on the country, the donor and the project or programme itself.

The benefit for Rwanda of unpacking the budget cycle and the management of aid flows like this became clear during the 2007 CABRI research. The Rwanda case study showed that each phase presents different challenges and that progress towards better quality and more coverage of aid also differed. It showed that shortcomings in one phase result in poor integration in a subsequent phase. Rwanda, therefore, requested CABRI's assistance in identifying the phase and/or issue that it could address with the most effect in its efforts to bring more aid on budget, and in formulating strategies in that regard. Such assistance is offered by CABRI to its member states, and involves the joint identification, through a joint scoping exercise, of the key issue the country wants to address, CABRI-led research on the issue and one or a series of working sessions with relevant role-players to resolve the issue and determine a way forward. The involvement of senior budget officials from elsewhere in the CABRI network is an invaluable resource (see box for a more detailed explanation of the process).

CABRI's aid on budget work

Using country systems has been a key theme in the work of CABRI since 2007. Following on the multi-country Aid on Budget study in 2007, the network offered interested member states the option of a more focused single-country research and assistance process, employing the approach developed for the 2007 study.

While the exact process and the focus of the research and assistance will depend on country circumstances, the CABRI approach comprises problem identification (done through a joint scoping exercise), research, country-based assistance by network members and the formulation and negotiation amongst stakeholders of a way forward to resolve key bottlenecks in bringing aid on budget.

The process recognises that bringing aid on budget is a multi-stakeholder issue. Success does not depend only on co-operation between donors and the government, it is also a function of the degree of buy-in to central principles and processes by different government actors, including line ministries and central aid and budget management offices. The CABRI approach, therefore, is to offer independent research and assistance, carried out by CABRI-vetted experts, with the participation of other network members, to unpack problems in an unbiased way. The aim is for this research to provide a shared understanding of issues amongst stakeholders, facilitating the reaching of agreement on the way forward.

Another critical component of CABRI's research and assistance is that it draws on expertise located in participating CABRI countries in investigating country bottlenecks. For example, in the case of Rwanda, senior budget and aid management officials from Mozambique, Ghana, Uganda, Tanzania and South Africa participated in the process.

While benefits from this process accrue in the first place to the particular member country, learning also takes place by officials from other countries who participate in the process. At the same time, working in more depth within countries on aid on budget issues allows the network secretariat to build an ever-richer knowledge base on the use of country systems. Besides this base being available to all participating countries, it also helps inform CABRI's participation in international forums on aid effectiveness on behalf of its members.

Source: CABRI Secretariat

The CABRI/SPA study framework for bringing aid on budget spans the Paris Declaration indicator for using country systems (Indicator 5a: use of country treasury, budget execution and auditing systems) and the indicator for aligning aid flows to national priorities (Indicator 3: aid to government sector on budget). For each phase of the budget cycle, it defines what it would mean if aid were integrated fully on budget. Table 3.2.1 presents the definitions used.

Table 3.2.1: Analytical framework for aid on budget

Term	Definition
On plan	Programme and project aid spending is integrated into spending agencies' strategic planning and supporting documentation for policy intentions behind the budget submissions
On budget	External financing, including programme and project financing, and its intended use are reported in the budget documentation
On Parliament	External financing is included in the revenue and appropriations approved by Parliament
On Treasury	External financing is disbursed into the main revenue funds of the government and managed through the government's systems
On procurement	Externally financed procurement follows government procurement procedures
On accounting	External financing is recorded and accounted for in the government's accounting system, in line with the government's classification system
On audit	External financing is audited by the government's auditing system
On report	External financing is included in *ex post* reports by the government

Source: CABRI/SPA (2008)

A key measure of how well Rwanda has succeeded in bringing aid on budget in each of these phases is the extent to which processes result in *comprehensive*, *transparent* and *accountable* management of aid and own resources in Rwanda. The focus of the work, therefore, related to identifying the key obstacles for each phase in terms of whether:

- comprehensive information is available to the right decisions-makers at the right time;
- the information is accurate and meaningful for budgetary decision-making; and
- aid management institutions build transparency so that decisions with regard to aid are accountable.

Identifying key obstacles to improved management of aid in Rwanda's budget

Early in 2008, the government of Rwanda undertook a comprehensive exercise to compile government accounts for the 2007 financial year. This allowed it to include not only aid flows that used the country's treasury and accounting systems, but all aid that was disbursed to general government and public entities, even if projects were undertaken by project implementation units and used separate bank accounts. Significant discrepancies emerged when the total amount of aid in the resulting accounts was compared to disbursed aid recorded in the Development Assistance Database (DAD) by the External Finance Unit of MINECOFIN and to total aid budgeted in the Finance Law. This pointed to different rules being followed at different points and/or to unsystematic or poor data collection.

At the same time, the government was under pressure from some donors to include aid in budget documents over which it had very little control and for which it did not wish to be held accountable in any way.

It became clear during the joint Budget Office/CABRI scoping exercise that a key issue in the Rwandan context was *which* aid should be included in budget documentation and *how* this should be done. Lack of a common understanding amongst role-players on how to treat different types of aid throughout the budget cycle emerged as an important stumbling block to having the right aid information with the right people at the right time. A vital aspect of improving the common understanding was the formulation of a clear set of rules with regard to how different aid flows should be treated up front. Thus, the focus of the Rwandan work was on the 'on plan', 'on budget' and 'on Parliament' dimensions of the cycle.

There was also an awareness that, in addition to lacking clear guidance on how to treat aid in the budget process, the existing information management mechanisms and processes were complex and fragmented, contributing to inconsistent information on aid flows and use.

The objectives of the CABRI/MINECOFIN intervention, therefore, were to resolve:

- *What* the rules would be in Rwanda for integrating aid on budget. Under which circumstances would Rwanda include external assistance: (a) in its Finance Law or 'on Parliament'; (b) in its budget documentation (or 'on budget') but not in the Finance Law; and (c) in neither its Finance Law nor its budget documentation?
- *How* the rules could be operationalised in order to ensure quality integration of aid on budget. The issue was for the process to look at streamlining procedures to ensure the capture of sufficient, useful and quality external assistance information at relevant points throughout the budget cycle.

The work, undertaken between June and October 2008, was focused on official development assistance (ODA) to the government sector; in other words, it included all grants and loans from development partners that are disbursed on the basis of an agreement with a government agency and which have as their main objective the promotion of the economic development and welfare of Rwanda. Since budget support is already on budget in all respects, the focus of the work excluded budget support. This means that the key questions were by which rules project and programmes flows would be included on budget and on Parliament, and how flows for projects and programmes would be managed to ensure that the inclusion is transparent and meaningful.

After the scoping exercise, terms of reference were prepared for the research team. The working session, held in October, included participation by relevant MINECOFIN units, representatives from key donors to Rwanda and senior budget officials from Mozambique, Ghana, Tanzania, Uganda and South Africa. After the working session, a final output brief on key decisions was prepared, and this has formed the basis for a series of reforms led by MINECOFIN.

Research process

The research process was important in establishing a shared understanding amongst role-players. While there were commonly held opinions on significant obstacles with regard to the under-reporting of aid on budget, there were also key differences. The

research facilitated a mutual understanding of the causes of the problem as a platform for deciding on reforms.

A joint research team was constituted, comprising a senior staff member from the Budget Office in MINECOFIN and the CABRI researcher who undertook the initial Rwandan aid on budget case study. The research was conducted in three phases:

- In phase one, the team analysed the gaps between ODA to the government sector as reported by donors on the DAD (see box below on aid management institutions and databases in Rwanda), ODA on the consolidated accounts, and ODA in the Finance Law and its annexes. The purpose of the analysis was to establish how the nature of aid flows, and/or the processes of managing them, contributed to the gaps. During this phase, interviews on which criteria determine or should determine when aid is on budget and on Parliament were undertaken with key stakeholders in the government.
- During phase two, the team tracked the flow of budget, disbursement and spending information on eight selected projects and programmes. The aim of doing this was to gather information on how aid and budget management institutions affected the timeliness and quality of information on aid and the meaningfulness with which it is integrated into the budget process.
- The third phase involved an analysis of both sets of information to establish when aid should be on budget or on Parliament and why, what the reasons were for it not being on budget or on account when it should be, and the shortcomings of the underlying processes in ensuring the quality of aid integration.

A series of notes was made available to the MINECOFIN prior to the joint CABRI/government of Rwanda/donor working session. A final research paper was distributed to participants, and the findings were presented at the working session.

Research findings

The research findings were focused on the nature of the discrepancies between key documents and databases recording aid flows and on the underlying factors that result in those discrepancies.

Central aid management institutions

Within MINECOFIN, three units are concerned particularly with the management of aid: the External Finance Unit (EFU), the Central Public Investment and External Finance Bureau (CEPEX), and the National Budget and Development Planning Units.

The EFU, established in 2005, is the key government entry point for the oversight and management of external aid. It is supported in the implementation of its mandate by the Aid Co-ordination Unit, and is financed by a basket-fund of six donors. The EFU is specifically in charge of monitoring progress towards the implementation of the Aid Policy and the Paris Declaration. In addition, the EFU has been the promoter of the DAD, and is in charge of ensuring the quality of the data it contains on donor support to Rwanda. Data collection for the DAD is based on donor reporting of aid flows.

As an autonomous agency under MINECOFIN, CEPEX is in charge of offering technical support services to government ministries and institutions in project preparation and appraisal, negotiations, implementation, and monitoring and evaluation. It was established in the late 1990s. CEPEX runs the database that tracks project implementation, and covers a range much wider than only donor-funded projects/programmes. To date, CEPEX reports have been the main source of data on the execution of the development budget.

The National Budget and Development Planning Units are jointly in charge of preparing the medium-term expenditure framework and its capital expenditure component, the Public Investment Plan. Until 2007, the Budget and Planning Units were responsible for putting together the Development Budget. However, this is no longer required as a separate budget; instead, it is integrated into the Finance Law, classified by government programmes through an integrated chart of accounts.

The Public Accounts Unit is responsible for capturing all spending from aid flows to the government in line with the new chart of accounts, together with the government's own spending.

Comparing the three documents

In the budget, accounts and DAD, 283 different externally financed projects and programmes were identified.[2] The total of 283 was arrived at despite there being more projects in sum from each document, because the three documents (the Finance

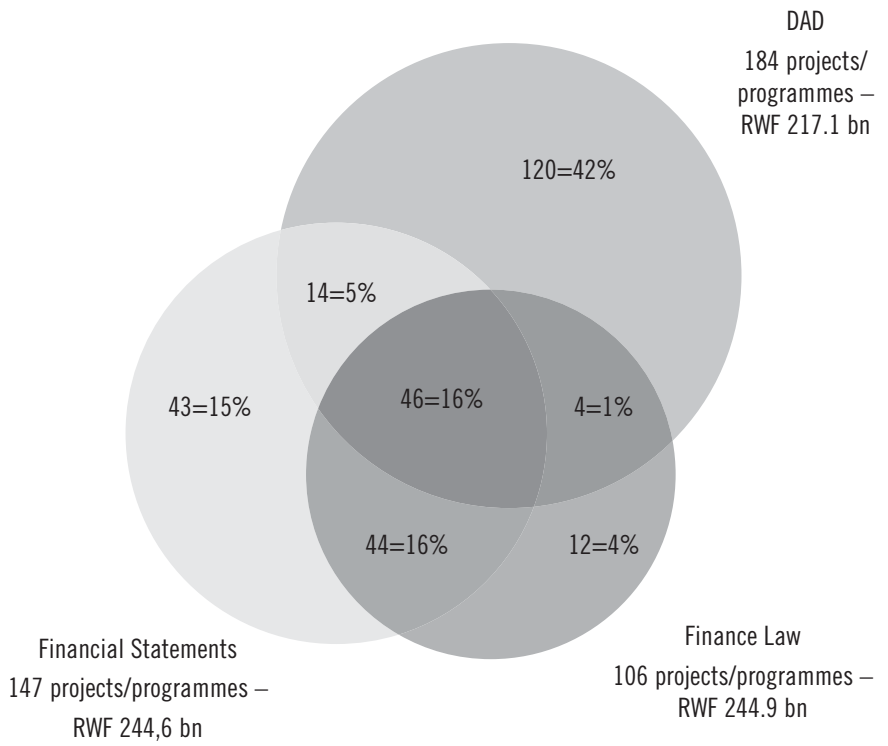
2 Multi-donor projects were counted as single projects.

Law, the 2007 Financial Statements and the Development Assistance Database) overlap partially. Figure 3.2.1 illustrates the overlap between the three documents. The following findings emerged.

Very few projects appear consistently in all three documents:

- only 46 projects/programmes (16% of the total) can be found in all three documents, and these projects/programmes represent approximately 18% of the total amounts associated with the 283 projects;
- a total of 90 projects/programmes (32% of the total) appear both in the budget and in the accounts (there are 147 projects/programmes in the accounts and 106 in the budget);
- 175 projects/programmes (62% of the total) can be found only in one of the three documents; and
- 177 projects/programmes are not on budget.

Figure 3.2.1: Distribution of projects/programmes between DAD, the Finance Law and the Financial Statements



Projects/programmes that are both on account and on budget comprise 61% of the total projects/programmes on account. However, in terms of money value, these projects represent 92% of the amount recorded against all projects/programmes on account. Moreover, although in money terms what is reflected on account roughly equals what is on budget, the difference in the number of projects that are on both compared to what are on each separately (90 projects on both compared to 147 projects on account and 106 on budget) further illustrates the poor quality of capture of projects.

Even for the projects that are on all three bases, there is a difference in the amounts reported. For these 46 projects/programmes, the amount reported in the budget is RWF64.2 billion; however, the amount indicated in the accounts is RWF114.1 billion. Many mismatches contribute to this discrepancy:

- The 2007 budget projected that the programme Rwanda Institutional Support for Economic Management (financed by the European Commission) would spend RWF1.3 billion in 2007; according to the accounts, it spent RWF38.3 billion.
- For a further 10 projects (where the difference between the amount budgeted and the amount accounted for is more than RWF1 billion), the amount budgeted is on average 49% of the amount spent.
- In total, 29 (or 65%) of the 46 projects/programmes that are on all three sources spent more than was budgeted.

The gaps occurred both because the amounts projected for some donors were lower than what was actually spent (or in a few cases higher) and because there were disbursements by additional donors that were not foreseen in the budget document.

Another significant finding was that out of the 177 projects that were not on budget in 2007, 62% incurred disbursements of less than RWF200 million but more than RWF50 million, while a further 33% had disbursements of less than RWF50 million. However, only 5% of projects were budgeted to receive less than RWF50 million and 20% between RWF50 and RWF200 million. Small projects are clearly more difficult to integrate on budget.

Loans do better than grants. Although there were some data problems with the accounts – where direct payments and technical assistance were captured separately from cash loans and grants, without an indication of how they were financed – the discrepancies with regard to loans and projects were lower.

Central ministries and investment ministries fare better. The discrepancies were higher for ministries whose projects and programmes were not investment oriented

and included more recurrent spending. Where the beneficiary institution was a public entity or a district, the discrepancies were higher too.

Multilateral donors performed better. Among donors with a high number of projects/programmes, the African Development Bank (ADB) and International Development Association (IDA) perform well, with 100% and 88% of their projects/programmes on budget, and 76% and 69% of their projects on accounts. On the other side of the spectrum of the donors that have most projects/programmes, UNICEF, UNDP, Canada, DFID and Netherlands have poorer performances (in terms of integrating projects/programmes on budget), while the European Commission and Belgium showed average performance.

Finding the reasons for the gaps

The research team identified a number of key reasons for relatively poor capture of aid information.

The criteria for what should be on Parliament, what on budget but not on Parliament and what on account were not well defined or widely understood. As predicted during the scoping exercise, different understandings of which aid flows should be reported on budget resulted in some aid flows not appearing on budget. Too much discretion on how aid was handled in the budget cycle led to inconsistent reporting of aid. In addition, differences between the DAD and the accounts arose from projects and programmes that were reflected in the DAD but which were not ODA to the government sector and which, therefore, were not included in the consolidated accounts.

Lack of MINECOFIN involvement and poor information sharing in MINECOFIN led to aid flows remaining off budget. Many of the projects that are not on budget appear to have been negotiated directly with the beneficiary entity without clear and systematic MINECOFIN involvement or knowledge. Nevertheless, many other projects, signed by the Minister of Finance, and for which even each disbursement is signed by the Ministry of Finance, are neither on budget nor on account.

A main finding from the tracking exercise is that some of the primary information gaps at the time of budget preparation are within MINECOFIN. The National Budget Unit is not informed of new projects signed or projects terminated. In addition, it is not consistently provided with information on project flows in the appropriate format for budget preparation, despite extensive data collection exercises by various other MINECOFIN units. As a result, for budget preparation, the unit relies solely on budget submissions from line ministries and budget agencies, and carries out no triangulation with information available in other units – consequently, all potential synergies in the work of various MINECOFIN units are lost.

The multiplicity of MINECOFIN databases and data collection exercises result in incomplete and poor information at all stages of the budget cycle. This, combined with poor information sharing in MINECOFIN, leads to inexplicable differences between the amounts provided in each document. These differences may be due, in small part, to the use of different exchange rates and the fact that different entities provide the different reports, which use different stages in the payment process, or that some information is missing in some places, in particular information on direct payments and technical assistance.

Importantly, the number of databases in MINECOFIN may lead to the assumption of actors outside of MINECOFIN, and that once information is communicated to one institution for its database and purposes, it is available in MINECOFIN for all purposes. This is not the case. The assumption that communication with CEPEX, which is charged with project management support, is sufficient for inclusion on budget and on account emerged significantly as a reason for under-reporting of aid in the tracking exercise.

MINECOFIN 'cutting' of project estimates results in under-budgeting. From the comparison of information on donor disbursements on the 46 projects that are in the three documents, it seems that for big investment projects, the budgeted amount is approximately 50% of the actual donor disbursement. This is due largely to systematic cutting of the estimates of likely project spend provided by ministries within the MINECOFIN leg of the budget process. The reason provided for this practice is the International Monetary Fund performance criteria on the primary fiscal deficit,[3] an aggregate fiscal statistics that is driven partly by aid revenue into the budget combined with the expectation that projects habitually overestimate their ability to spend. However, in the case of Rwanda, as evidenced by recorded spending, MINECOFIN imposes a higher adjustment of projected spending than is merited, resulting in under-budgeting and non-transparent aid flows.

Some ministries may be reluctant to provide information. The National Budget Unit relies on ministries to report aid in order to include the information on budget, but not all ministries report aid fully. In addition to under-reporting small projects because of the size of the project (see discussion below), another reason might be that they do not want their national budget allocation to be affected. MINECOFIN is not always involved in processes setting up a project/programme, despite the Aid Policy, which says that it should be.

3 The primary balance is a measure of how deficit- or surplus-creating a government's current policies are. It equals the overall balance (which is called a deficit when negative or a surplus when positive) plus interest spending. The overall balance, in turn, is defined as total revenue minus expenditure and lending minus repayments.

Externally financed projects and programmes that are not investment-driven have no clear place on the budget. Most of the projects/programmes that are not on budget comprise externally financed recurrent activities, for which there are no counterpart funds. Investment projects, which often include counterpart funds, are less often off budget.

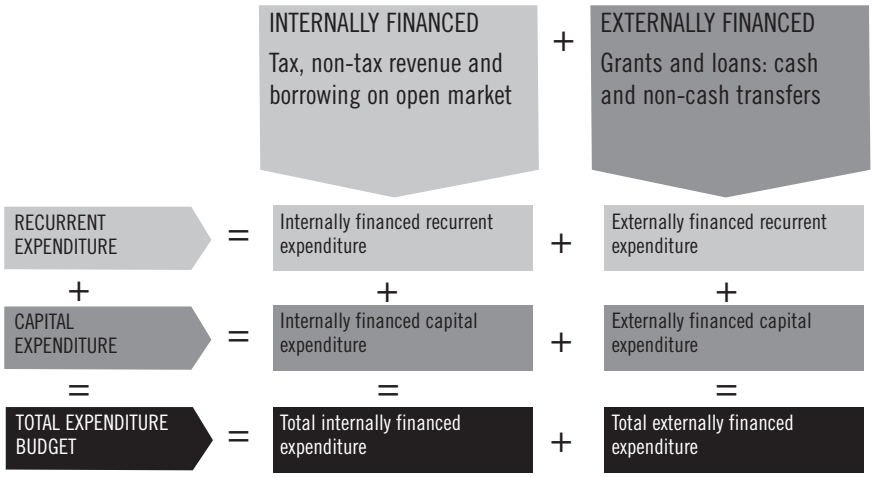
This arises partly from the ambivalence of the development budget in Rwanda, which, on one side, includes all investment expenditures (internally and externally financed), and is derived from the Public Investment Plan, and which, on the other side, should (in theory) encompass all non-budget-support external aid – some of it being of a recurrent nature. The recent steps towards budget integration have not solved the problem entirely, since the development budget still appears separately (2008 Finance Law Annex II-2, II-5, II-6) and is still prepared on a parallel track to the recurrent budget.

Although the development budget should include these externally financed recurrent flows, the dual purpose of the development budget, and its preparation on a parallel track driven by the Public Investment Plan, creates confusion during budget preparation.

In addition, there is inconsistency in how externally funded programmes that comprise recurrent activities are reported on budget: some recurrent activity projects and programmes are not reflected at all, other projects are included in the development budget for specific reasons (for example, donor visibility) and one project (the IDA-financed project on demobilisation and reintegration) appears on the 'recurrent' side of the national budget (i.e. the non-development budget) as a sub-programme and is classified as exceptional expenditure.

Although the new chart of accounts, if properly used, allows the adequate classification of all expenditures, whether internally or externally financed, as recurrent or capital (see Figure 3.2.2), in practice the persistence of a separate process for and separate reporting of the development budget in the Finance Law causes some externally financed recurrent expenditures to remain off budget.

Figure 3.2.2: Chart of account classification of projects/programmes



There is lack of a clear definition of what constitutes a project/programme, and what should be considered sub-components of projects/programmes. Some groups of projects/programmes are reported in one document as one entity, while in another document each sub-component is recorded separately. This results in different counts in different databases for the same project/programme. A significant consequence of this is that it is difficult to track how well aid interventions are implemented. An important step forward would be to attain clarity on when a collection of aid interventions should be counted as one project/programme and when not. Also, the government would need to carefully design how projects/programmes appear in the Finance Law and its annexes, so that a uniform style can assist stakeholders in interacting with the information provided.

Lack of a unique project identification number leads to opaque aid flows. Tracking aid flows from the DAD through budgets to accounts is made very difficult by projects/programmes not being given a unique identification number that would ensure consistent reporting. Projects and programmes have different names in different documents, sometimes different partner ministries or institutions, and sometimes are grouped or split differently.

Lack of clear instructions on aid to public entities leads to inconsistent reporting. A great number of the projects/programmes that are not on budget are in support of autonomous and semi-autonomous agencies. In the central government budget (i.e. the Finance Law), these agencies appear only in terms of the transfers they receive from central government. Articles 39 and 41 of the Organic Law on State Finances and

Property (known as the Organic Budget Law, or OBL) require that a summary of the budget (revenues and expenditures) of these public entities be annexed to the Finance Law and be transmitted to Parliament in the budget documentation, but this has not happened. As a result, there is no clear pattern; while some projects in support of autonomous and semi-autonomous agencies are on the central government budget, under the parent ministry of the institution, most are not. Nor do they yet appear in the annex.

The tracking exercise showed that where aid to public entities was included in the parent ministry's submission to MINECOFIN, it ended up in the central government budget. A key step to resolving the problem and bringing more aid to public entities onto the budget documentation would be clear rules on how this aid should be reflected (by defining the format of the OBL annex), accompanied by clear instructions to ministries with regard to submitting information on such aid.

Aid to districts is also reported inconsistently. The OBL requires that a summary of districts' budgets be annexed to the Finance Law. Therefore, districts should appear in the Finance Law itself only with respect to the transfers they receive from central government. Aid that is agreed upon with and disbursed to districts should appear in the annex as a revenue to districts. Nevertheless, although this annex has been produced since 2008, some donor projects directed at districts still appear in the central government budget. The underlying problem in this case is lack of clarity in the rules for signing aid agreements with districts and/or parent ministries and how different arrangements should be reflected in the budget documentation.

Small projects are omitted too easily from budget information. The vast majority of projects that disbursed less than RWF50 million in 2007 were off budget. These are often not considered worthwhile or necessary to report. While there might be a reason to define a limit above which all projects should be reported – in order to minimise the transaction cost of bringing aid on budget – there is a danger that it would create incentives to break up projects in order to keep the spending under the radar. In addition, it would mean that spending – which in aggregate could be significant in a sector – might not be considered properly in the budget process. A solution might be for MINECOFIN to require reporting of all aid, but with less detail on small projects.

Lack of validation procedures on data provided by donors on the DAD results in incomplete and unreliable information. Entries by donors in the DAD do not always cover all ODA to the government sector, especially when there are many institutions involved. Some donors do not complete the DAD. Unchecked data entry by donors on the DAD, therefore, accounts for some under-reporting on DAD compared to accounts and renders it useless for budgeting purposes.

Data quality is an issue throughout the system. Two sets of information that should be almost identical are the donor disbursements recorded in the accounts and in the DAD. The discrepancies between these sets of information can be explained by multiple reporting lines for donors and projects, resulting in different information, and by the donors directly recording their information on the DAD without quality control or validation.

Other issues

The issues listed above are generally within the capability of the government of Rwanda to address, although often with the co-operation of its development partners. There are, however, other issues which are outside the control of Rwanda. As was evident from the tracking exercise, there are donors whose own requirements and procedures make inclusion in budget processes and appropriate reflection on budget and on Parliament difficult. For these 'difficult donors', the issues can be addressed only through reform of the donors' own practices, often at international level.

A final issue that emerged from the research had to do with the timing of project/programme signature and start-up. In many cases, this is outside the control of the government of Rwanda: the rules for including aid on budget and on Parliament – in the Finance Law or though a later adjustment budget – would need to take this into account.

The way forward: improving the quantity and quality of aid information on budget

The research provided an important input into the joint CABRI/government of Rwanda/Donor workshop held in October 2008. The CABRI/MINECOFIN intervention and workshop was timed in order to influence the preparation of the Rwanda Aid Management Manual and a Budget Process Manual, as well as the next budget preparation cycle.

The Aid on Budget workshop was attended by key donors (the World Bank, the IMF, the ADB, DFID, EC, the Netherlands, KFW, UNDP and USAID, among others), and key staff from MINECOFIN, including the Accountant General and staff from the External Finance Unit, the National Budget Unit, the Development Planning Unit and CEPEX. Senior budget and aid management officials from Mozambique, Ghana, Tanzania and Uganda also attended, in order to bring their experience in addressing some of the key issues identified in Rwanda to the discussion.

A key conclusion from the research findings was that the quantity of aid and the quality of aid information on budget were affected by two types of issues, which can be addressed with system reforms:

- Firstly, the types of aid that should be on budget and how they should be reflected were not clear to all stakeholders, *in other words the rules for putting aid on budget were lacking*. Examples from the discussion of findings above are: the impact of lack of clarity with regard to when aid should be approved by Parliament as part of the central government Finance Law and when it should merely be reflected on budget; how aid to public entities and districts should be reported; and how aid flows for recurrent activities versus investment activities should be processed and recorded.
- Secondly, it was clear that *the processes for capturing aid were not robust enough to deliver accurate information in meaningful formats on time for inclusion on budget*. Examples from the findings include: the impact of multiple databases and data collection processes; poor information sharing in MINECOFIN; donors completing the DAD without validation; insufficient involvement of the MINECOFIN in aid agreements; and lack of unique project and programme identification numbers and consistent classification of projects and programmes that are grouped together throughout the cycle.

A third set of issues concerned the incentives for poor information provision in the budget process; for example, line ministries that might be reluctant to report aid fully, unreliable estimates by donors or project managers on expected spending and unavailable or incomplete information on actual spending. These are more difficult to address, since some are endemic to the dynamics of the aid relationship. However, tightening up rules and processes creates a counter-incentive, which will be strengthened by follow-up and increased efforts to be transparent and to expose under- and over-budgeting (see box on Mozambique's use of the requirement to pay duties and taxes on project imports to discipline reporting on aid).

The workshop task, therefore, was to reach some resolution on the rules by which aid would be put on budget and to make progress towards resolving the process-type issues.

Incentivising internal reporting of all aid flows

One factor that contributed to improved reporting of aid on the Mozambique budget is the centralising of funds to pay duties and taxes for all line ministries. Now, when a line ministry implementation unit needs to import any aid-related goods, it is required to apply to the Finance Ministry for funds to get the goods through customs and other processes. This means that the Finance Ministry has an alternative avenue to register projects, which incentivises reporting of all aid flows in the first place. Mozambique also does not use ceilings inclusive of all aid flows, which minimises the negative incentives to report. For the import of, for example, services that are paid for directly by the donor outside of the country, however, under-reporting is still a problem. For these types of expenditure, the government of Mozambique requires expenditure balance sheets from donors.

Source: Presentation at Aid on Budget Workshop, Rwanda, by Rogério Nkomo, Budget Director, Ministry of Finance Mozambique.

Criteria to determine when aid is on budget, on Parliament and on neither

The workshop focused on the following factors as important in deciding how aid should be treated in the budget process:

- the purpose for which the aid is used;
- the recipient of the aid;
- the timeliness of the information and its integration in the planning/budgeting process; and
- the degree of government control in planning, using and accounting for aid funds.

An important distinction in the Rwandan context (see box on the Ugandan system for a contrasting example) is between aid that is on budget, but not on Parliament, and aid that is on Parliament and, therefore, automatically on budget. The government clearly specified that it would include aid on Parliament only when it has sufficient control over the use of the aid and can be held to account by Parliament. Where such control is lacking, aid to the government sector should still be on budget – to ensure its inclusion on plan and to make its flow transparent to Parliament – but the government is not prepared to be held accountable for its use and effectiveness.

The Ugandan system in brief

The distinction between on budget and on Parliament does not hold equally for all partner countries. In his presentation to the workshop on the Ugandan system, Mbulamuko Laban, Assistant Commissioner for Infrastructure in the Ugandan Ministry of Finance, Planning and Economic Development, pointed out that by law all expenditure in Uganda needs to be included on budget. This includes aid to the government sector.

In Uganda, the finance ministry has implemented a number of rules and processes that have improved the coverage of aid on budget. For example:

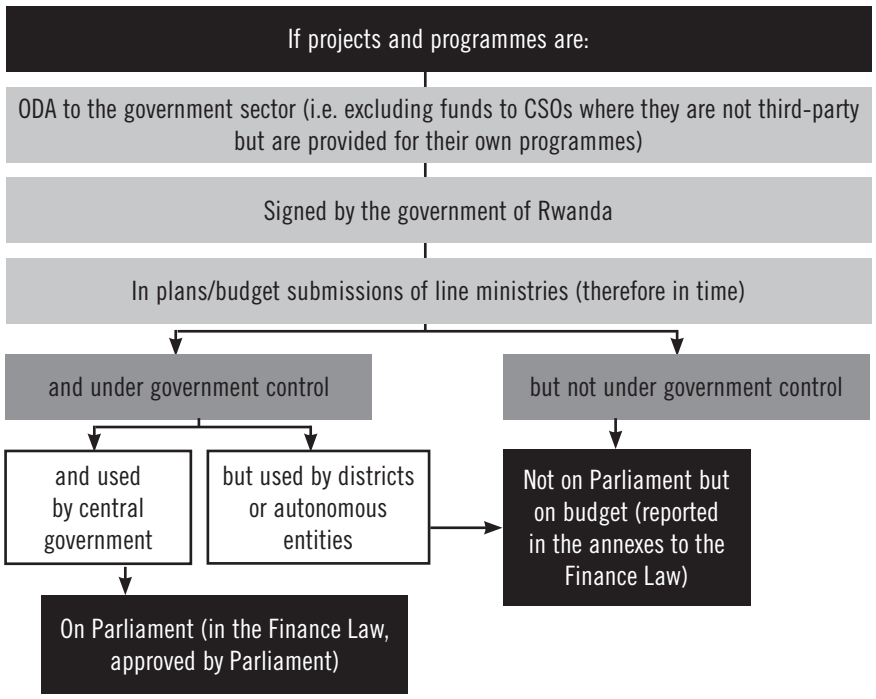
- Bank accounts for aid projects and programmes to the government sector now have to be held at the central bank. This means that the Finance Ministry has an alternative route to accessing information on aid flows.
- The Finance Ministry is party to all aid contracts and all aid flows have to be in line with the government's priorities, as set out in its planning frameworks, its debt strategy and its budget strategy.
- All aid information received from donors is double-checked with the relevant ministries.
- The Ugandan Sector Working Groups have to approve all new projects or programmes before an aid agreement is concluded. This means that aid is integrated into planning and budgeting processes and that the Finance Ministry is aware of aid flows through Working Group documentation.
- A Development Committee approves all project expenditures before 31 December for the fiscal year starting in June. This means another avenue of information. As all disbursements have to go through the Accountant General's office, there is the potential for follow-up.

The key challenge, however, is to enforce compliance with these rules, and to encourage donors to stick to their commitment to provide quality information on time.

Source: Presentation by Mbulamuko Laban, Ugandan Ministry of Finance, Planning and Economic Development, at the Rwanda Aid on Budget Workshop, October 2008.

Figure 3.2.3 illustrates how these factors are sequenced to categorise different projects and programmes.

Figure 3.2.3: Criteria to determine treatment of aid in Rwanda's budget process



The workshop decided on three main criteria to include aid on budget:

- A first exclusion from aid on budget is aid that does not flow to the government sector (i.e. aid that is provided in the country but to which the government is not a party). This would include aid flows to civil society organisations (CSOs), where this aid is the result of an agreement between donors and a CSO itself. However, aid that flows to CSOs as a result of an aid agreement signed with a government agency must be on budget, even if not on Parliament.
- A second exclusion would be aid that flows without an agreement signed by the government of Rwanda. This means that aid would be included on budget and on Parliament only if a full negotiation and contracting process has been completed.
- A third factor is that aid would be included on budget and on Parliament only if it was programmed in time for its integration at the ministry level into planning processes. An indicator at the central level of this is the inclusion of

aid in ministry submissions (with clarification of rules with regard to public entities, districts and recurrent expenditures). Thus, late aid agreements that are reported to MINECOFIN directly by the donor in the final weeks before the budget submission to Parliament would not be included on budget.

In future, all aid that satisfies these three criteria will be on budget, even if some of it might not be on Parliament. The next two layers of factors determine when aid is on budget and on Parliament, and when it would be merely on budget.

The first question is whether the aid flow is under government control. The workshop defined 'under control of government' to mean that *all* of the following five conditions must be satisfied:

1. the responsible budget agency is active in decisions on the allocation of funds for the project;
2. disbursement of the funds is approved by the budget agency's chief budget manager;
3. the project submits its accounts to the responsible budget agency;
4. supporting documents for financial transactions are kept by the responsible budget agency; and
5. if a third party is an implementing partner (NGO, consulting firm, etc.), a contract must be signed between the budget agency, the implementing partner and MINECOFIN.

All aid flows to central government that do not satisfy one or more of these criteria would be reported in an annex to the Finance Law – provided that they fulfil the first three criteria – but would not be approved by Parliament. For example, if a third party is the implementing agent and the contract is still signed with the donor only, the aid flows would be on budget but not on Parliament, since the government of Rwanda cannot be held accountable by Parliament for aid flows over which it has no contractual oversight.

Again, where aid flows comply with the above five criteria in addition to the first three, but constitute support to public entities or districts, where the contracts are signed with these institutions, aid would be on budget and not on Parliament. The reason for this is that the aid flow is then outside of the central budget (i.e. not in the Finance Law and not for the account of central government). It would be reported as revenue on the entity or district budget, and be reflected in the annexes to the Finance Law.

In short then, where aid flows are to the government sector, are as a result of a signed agreement, are on time, satisfy the five criteria of 'under government control' and constitute aid to the central government, it would be on Parliament. If any one of these conditions is breached, aid would be either not on budget at all or reflected only in the annexes to the Finance Law.

Streamlining aid information management for budgeting purposes

The workshop engaged with how aid information is currently collected, processed and distributed in Rwanda. It endorsed the key research finding that whereas clarity on the criteria for when aid should be on budget and on Parliament is necessary for improving the coverage of aid in Rwanda's budget and budget process, it is far from sufficient. There were core problems with existing systems for managing aid information that need to be addressed in order to bring aid on budget meaningfully. The workshop agreed unanimously that *data collection and management should be streamlined as a matter of urgency*, implying amongst other things that *co-ordination of aid information on MINECOFIN should be addressed*.

The workshop recommended that MINECOFIN should undertake the design of a clear set of rules, with accompanying roles and responsibilities, for itself and its various units, line ministries, project managers, districts and public entities and donors to ensure that aid is captured in the budget process and that accurate aid information is available for inclusion on budget, on Parliament and on account.

More specifically, this entails:

- *A unique entry point in MINECOFIN:* Workshop participants agreed that one unit in MINECOFIN should be designated as the unique entry point for all aid information. The unit should be strengthened to manage the subsequent information flows required to ensure that aid is managed well and captured sufficiently and accurately in the budget. This holds for all aid information, including information on new projects, disbursements, project implementation and accounts. The 'unique entry point unit' should provide the National Budget Unit with up-to-date information in the budget process.
- *Co-ordinating/streamlining databases and a unique project identification number:* The multiplicity of databases makes it impossible to co-ordinate aid spending and track aid information. Besides a unique entry point in MINECOFIN, there is also cause to argue for a single primary database, in all likelihood the database used by the National Budget Unit to compile and manage the budget. More importantly, even if different databases are still in use –

hopefully drawing on the central primary database for core information components – projects and programmes should be identified by a unique project identification number that would allow information to be tracked across databases. The purposes of different databases should not overlap, and core information should be shared amongst them.

- *The involvement of MINECOFIN in signing off on aid projects:* Although further work is required to ensure that MINECOFIN is involved in the approval of aid projects without slowing down processes or overloading the ministry, in principle MINECOFIN needs to be aware of and involved in aid project preparation, in order to ensure that all necessary projects are integrated in budget processes and the budget. Furthermore, when the project is signed it should include an assessment by MINECOFIN of how it will be treated in the legislative budget process and in the budget documentation (on budget/on Parliament). There was also consensus at the workshop that the involvement of sector working groups should be highlighted, to ensure that all aid is properly integrated at the sector and ministry levels.
- *MINECOFIN undertaking to triangulate aid information in the budget:* In order to ensure the quality of aid information, part of budget appraisal and preparation in MINECOFIN should be to cross-check with stakeholders the quality of the information it is using for budget planning purposes. This might involve checking with the External Finance Unit and the recipient agency on specific projects and programmes, or with donors themselves.
- *Resolving unrealistic 'cutting' of aid projects and amounts:* MINECOFIN should undertake to resolve conflict between the honest budgeting imperative to reflect aid flows as completely as possible on budget – in terms of number of projects and amounts to be spent – and the requirements of macroeconomic planning and the fiscal framework.
- *Providing aid information in chart-of-accounts format:* Aid information for government use should be classified in line with the budget structure and chart of accounts. It should specify, therefore, which ministry, programme and sub-programme are affected and should provide financial information in line with the chart-of-accounts classifications (as set out in Figure 3.2.2).

Besides these government of Rwanda-centred recommendations, the workshop also resolved that donors should provide comprehensive information on time and in the right formats; in order to bring aid on budget in such a way that aid is integrated into the government's own spending, donors undertook to do so. This includes information on direct payments and technical assistance.

Impact of CABRI/MINECOFIN work and the way forward

The work done by CABRI and the National Budget Unit of MINECOFIN during 2008 was instrumental in setting a reform agenda for aid management. Subsequent to the workshop, a memo of workshop proceedings and recommendations was presented internally in MINECOFIN and to the Minister of Economy and Finance to formalise decisions and determine a way forward.

In November 2008, MINECOFIN senior management approved the recommendations. The National Budget Unit was tasked with preparing the roadmap for further discussion of the recommendations with stakeholders and for their subsequent implementation. A four-step process was agreed to in this regard:

1. To upgrade the Smartgov as a central database and to pilot the proposed changes on a sample of selected projects, thereby testing the feasibility of the reform. The pilot has been completed, and the reform is being implemented in the new financial year, which commenced in July 2009.
2. To hold a meeting with chief budget managers and to agree on the implementation of the recommendations before the commencement of the new financial year (July 2009/10). This meeting was held in March 2009.
3. To discuss the recommendations at the broader meeting of joint budget support donors in April 2009 and to agree on concrete steps on the way forward.
4. To undertake an internal process review at MINECOFIN to streamline management of project information.

The process engaged in by CABRI and MINECOFIN in 2008 – a first for CABRI in country-level support – was instrumental in setting a government-driven reform agenda for aid management, and was also a valuable learning experience for the network on how to use its expertise optimally in supporting individual countries in key CABRI themes.

Reference

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3.3 Use of country systems: Means, not end in itself

Aarti Shah

This article reflects the CABRI position on provisions within the Accra Agenda for Action (AAA) with regard to the use of country systems. While CABRI strongly supports efforts to increase the use of country systems in the delivery of development assistance, it does caution against emphasising the means towards more effective aid and systems – i.e. the use of country systems – without considering carefully whether, in the specific circumstances, this will indeed result in the desired progress in particular countries.

Background

Effective co-operation is premised on shared objectives and mutual interest, relationships of trust, transparent practices and the sharing of information, clear frameworks for responsibility and accountability, and long-term investment by both parties in terms of resources and capacity. The intentions underpinning the Paris

Declaration speak of a mutual partnership in which both developing countries and donors are encouraged to move towards the above ideal.

The commitments in the declaration reflect a consensus that aid effectiveness is critically dependent on countries owning and driving their development agendas and leading the management of official development assistance (ODA). An integral part of ownership is aligning ODA to developing countries' development strategies, institutions, systems and procedures.

The 2008 Survey on Monitoring the Paris Declaration provides us with evidence that only 43% of ODA flows through partner-country systems, suggesting that considerable progress still needs to be made in meeting the 2010 target (85% of aid recorded on budget) set out the declaration. In light of these results, the AAA presents a set of actions for both developing countries and donors in accelerating progress.

The AAA, an outcome of the 3rd High Level Forum held in Accra in September 2008, urges donors to use country systems as a first option, based on mutually agreed diagnostic assessments of the strength of country systems. Where this is not possible, donors must consider safeguards and measures that strengthen rather than undermine these systems. Developing countries are urged to define reform priorities and programmes that will strengthen country systems, while donors are encouraged to develop plans that provide their organisations with guidance on, and incentives for, using country systems. Lastly, donors are required to channel 50% or more of government-to-government assistance through country fiduciary systems, including through the increased use of programme-based approaches.

Since 2007, CABRI has undertaken several exercises that provide depth to the network's thinking on using country systems. Therefore, the network's response to the AAA element on using country systems (encapsulated in this brief) draws on the practical experience of senior budget officials to ensure that using country systems reap the desired benefits.

CABRI's contribution to the debate on using country systems

CABRI's particular contribution to the 3rd High Level Forum's regional consultations on alignment and the use of country systems was the analytical distinctions it has drawn with regard to the management of aid in the budget cycle, and is based on its growing understanding of how these distinctions can contribute towards improved aid effectiveness on the ground. Key inputs into CABRI's contribution are the joint CABRI/SPA (2008) *Putting Aid on budget* study, the proceedings of its 4th Annual Seminar in December 2007, discussions amongst member countries and country-level work conducted by CABRI and the government of Rwanda.[1]

The CABRI/SPA (2008) study presents an analytical framework that depicts six dimensions of putting aid on budget.[2] The dimensions follow the phases of a policy and budgeting cycle, as presented in Table 3.3.1. The study found that different aid programmes or projects make use of country systems in any one or any combination of these budget phases. In practice, therefore, bringing aid on budget does not imply that all country systems should be used at once: countries can make measured progress towards integrating aid on budget as is appropriate and possible.

Table 3.3.1: Different dimensions of on budget capturing of aid

Term	Definition
On plan	Programme and project aid spending is integrated into spending agencies' strategic planning and supporting documentation for policy intentions behind the budget submissions
On budget	External financing, including programme and project financing, and its intended use, are reported in the budget documentation
On Parliament (or 'through budget')	External financing is included in the revenue and appropriations approved by Parliament
On Treasury	External financing is disbursed into the main revenue funds of the government and is managed through the government's systems
On accounting	External financing is recorded and accounted for in the government's accounting system, in line with the government's classification system
On audit	External financing is audited by the government's auditing system
On report	External financing is included in *ex post* reports by the government.

Source: CABRI & SPA (2008)

For CABRI's participating countries, the aid-on-budget framework highlighted the importance of not associating bringing aid on budget with budget support. All forms of aid can and should be brought on budget in one or more of the dimensions; in this respect, CABRI's point of view is in line with the Accra outputs.

Terminology and country-level rules associated with specific terms were an important consideration at CABRI's 4th Annual Seminar. The seminar discussions highlighted that the definition of aid instruments used by certain counties could, in fact, prevent all flows of aid coming on budget and/or misrepresent aid flows. For example, in Mali and Ghana, project support is off-budget by definition. At the same time, Mali's definition of sector budget support consists of funding for specific line items allocated separately to domestic resources. In other countries, such earmarked flows would be viewed as project aid. The session concluded that aid instruments

1 The 3rd High Level Forum consultations included a meeting of the OECD-DAC's Joint Venture on Public Financial Management hosted by CABRI in May 2008.
2 'On procurement' is an additional dimension, which was not included in the scope of the study, but is an important element of using country systems.

should not be designed to be off-budget by nature, given the development risks of separating the planning, budgeting and reporting processes of these flows from those of government programmes. It is possible for all modalities, including project aid, to use different aspects of country systems. One key consideration for putting project aid on Treasury is that government accounts should be able to show comprehensively all sources of funds, as well as all uses of funds. Therefore, systems and processes are needed to integrate aid at the various stages of the budget cycle, notwithstanding specific aid modalities and donor requirements.

CABRI's country-level work further confirmed that clear distinctions between different aid modalities, and how they are treated in the budget cycle, are important. It has shown that developing countries need to consider relevant criteria for determining when aid should be on the various dimensions of the budget cycle. In the case of Rwanda, the government would only include aid on Parliament – i.e. Parliament approves aid as part of the Finance Law – when it has sufficient control over the use of the aid to be held to account. Where that control is lacking, aid to the government sector should only be 'on budget' – i.e. reported in documentation accompanying the Finance Law – which will ensure its inclusion on plan and make its flow transparent to Parliament.

The work in Rwanda also illustrates how important a thoughtful and well-managed interface between country aid and public finance management systems is for the quality of aid information and the integration of aid on budget. Pushing for comprehensive and timely information on the disbursement and use of funds is an important part of putting aid on budget.

A further important distinction is between reporting aid in government documentation and integrating aid properly in government planning and budgeting processes. The CABRI/SPA (2008) study identifies three factors that determine whether reporting on or integrating aid into national budget processes will have the desired effects. These are: (a) the quality of the aid information captured; (b) the ability to make use of the information; and (c) the quality of the information and processes related to non-aid resources. If aid is merely reported in budget planning and reporting documentation in the absence of one or more of these factors, significant development and fiduciary risk still remains for the partner government in question.

CABRI's response to the Accra Agenda for Action

CABRI recognises the important role that development assistance can play in strengthening institutions and systems, building capacity and financing resource needs. These are all means to improving service delivery and, ultimately, the living standards of the poor. Furthermore, CABRI welcomes international efforts to support developing countries in taking the lead and driving their own development agendas. Ownership and alignment are interdependent principles that cannot be divorced in implementation. The long-run benefits of alignment should be seen in the light of reducing aid dependency, increasing domestic revenues and improving debt sustainability positions.

CABRI firmly believes that developing countries must drive the policy-making agenda, based on credible processes. This is our commitment to the mutual partnership. Without credible government planning, budgeting, accounting, auditing and reporting processes, it is difficult for governments to lead inclusive policy dialogues and to make systematic use of donor information.

Essentially, the AAA represents a positive compromise reached between a broad spectrum of donors and developing countries in order to take steps towards improved aid effectiveness. The AAA firmly places the use of country systems on the agenda, thereby re-emphasising that it is a critical part of alignment to partner-country strategies and of ownership. CABRI presents some views below on how the five action areas in using country systems can be applied to achieve maximum impact, drawing on its own learning in this regard.

- *The use of country systems should not be applied as a blanket approach. Not all donors will use all dimensions of all countries' systems in the near future, and it may not be appropriate, realistic or even in the interests of developing countries to expect them to do so.* The use of country systems is a means, not an end. We must be cautious not to encourage thinking that focuses on the means only and blindly pursues procedures aimed at increasing scores on the Paris Declaration commitments. The important question when deciding on how an aid flow should be managed remains: Will channelling this aid through this particular system make it more effective, and/or will it lead to a better allocation and management of public funds (domestic and external) in the medium to longer term? A more nuanced approach during implementation should reflect developing country choices about how developing countries wish to manage their own fiduciary and development risks. Key considerations are the sequencing of

how countries wish to strengthen their systems, and when aid should be on budget in any dimension and when it should not.

- *A developing country also faces risks in integrating aid into country systems.* The report on the use of country systems in public financial management (PFM) speaks only of fiduciary, development and reputational risk for donors in using country systems. Developing countries also face risk, including fiduciary and development risks, when integrating aid into country systems. For example:
  - unreliable and unpredictable aid flows reduce the credibility of a government's budget process. This is a fiduciary risk for developing countries. Increasing in-year and multi-year predictability are important related actions in the AAA;
  - unreliable and incomprehensive donor aid information poses a development risk for developing countries, where it is not possible to track and report accurately on the disbursement and use of aid that flows outside of partner country treasury and procurement systems;
  - the benefits of channelling aid through treasury and procurement systems do not always outweigh its cost, in particular for small, multiple short-term projects; and
  - information not provided in time with a government's planning and budgeting cycles presents both a fiduciary and development risk.
- *Greater emphasis should be placed on the upstream elements of the budget cycle: planning, budgeting and parliamentary approval.* There is a strong emphasis on the downstream elements of the budget cycle when donors are encouraged to channel 50% or more of government-to-government assistance through country fiduciary systems. This is reflected in the way the indicators are separated out and balanced in the Paris Declaration, where indicator 3 refers to aid on budget and indicator 5 to the downstream systems. It is indicator 5 that bears the title 'use of country systems'.

  The use of country systems for planning and budgeting for aid is of immediate developmental interest to countries. Separating out planning and budgeting from fiduciary systems, and focusing on fiduciary systems to make progress, detracts from the importance of the upstream dimensions for partner countries, as well as from the interdependence of different phases in the budget cycle for spending effectiveness. Most damaging, it encourages the use of fiduciary systems over and above planning, budgeting and reporting systems.

To drive the development agenda, governments must determine the allocation of both domestic and external resources on the basis of their priorities. Not reporting on or not integrating aid into countries' planning or budgeting is a development risk. Without a comprehensive view of what is happening in a particular sector, developing countries cannot assess where resources are being targeted or whether domestically financed programmes duplicate or complement aid programmes.

Therefore, aid programmes and projects need to be subject to the same budget scrutiny as government projects, and this may mean that certain aid programmes and projects are redefined or not undertaken.

Putting aid on plan and on budget does not represent any fiduciary risk to donors, but is vital for aid effectiveness and the optimal use of partner countries' own resources.

- *Developing countries have a much stronger role to play in determining whether and where aid should be integrated into the various dimensions of a country's policy and budgeting cycle.* Currently, the AAA places the onus on donors to use country systems. The role of the developing countries is limited to strengthening country systems and engaging in joint assessments of these systems. CABRI proposes the following additional requirements. Developing countries must also manage their fiduciary and development risks by: (a) defining the relevant criteria and terms for including aid into the various dimensions of the budget cycle; and (b) determining which systems they wish to strengthen first.

  The AAA urges countries to strengthen their PFM systems and their aid management systems, but says little about how these are integrated. Mostly, the focus in the AAA is on PFM systems, but alignment requires countries to develop robust systems and processes to integrate aid, not just to manage public resources well.

  The use of country systems is an important element of the aid effectiveness agenda, and is related strongly to the work of senior budget officials in ministries of finance. We have a strong role to play in ensuring that country systems are robust, not only for the management of aid resources but, more importantly, for the sustainable management of our own domestic resources. Understanding the nuances of using country systems will prevent a blanket procedural application of the AAA and will ensure that the benefits outweigh the costs for developing countries.

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4

Fiscal policy in the global economic slowdown

4.1 Introduction

This chapter mirrors the discussion at the Dakar seminar on the challenge to African countries posed by the global economic slowdown. The introductory note to the chapter by Alta Fölscher summarises the effects of the global crisis on African countries and emerging proposals for policy responses. The note draws on recent literature on the impact of the crisis on Africa and looks at how African economies have been affected by the direct and indirect impacts on their financial sectors, trade and exports, domestic economic investment and activity, and on their fiscal, current account and monetary positions. It is accompanied by two short papers reflecting inputs provided for the seminar by Zambia and Egypt on their fiscal policy responses at the time of the seminar. The Zambia presentation, by Danies Chisenda, Director of Budget, Ministry of Finance and National Planning, Zambia, highlighted how the decline in demand and prices for copper has affected the Zambian economy and public finances. The policy response has been to maintain a prudent fiscal policy and to realign expenditure items to cushion the impact of the multiple crises on the domestic economy. In contrast, Egypt's response has been to introduce a fiscal stimulus package, as explained in the note on the presentation prepared by Amgad

Hegazy, Economist in the Micro-fiscal Policy Unit, Ministry of Finance, Egypt. Both notes were prepared by Yacine Bio-Tchané from the CABRI secretariat.

4.2 Africa and the global recession

Alta Fölscher

The global financial crisis and accompanying economic slow-down are affecting African economies, resulting in immediate fiscal policy challenges. The quality of fiscal policy decisions will determine, to some degree, how well African economies weather the downturn. This introductory note to the two country case studies presented in this chapter draws on recent literature on the impact of the global crisis on Africa, and summarises the proposed policy responses.

The impact of the global crisis on African economies

The mid-2000s brought high growth rates to many African economies. In sub-Saharan African countries, growth averaged about 6.5% between 2004 and 2008 (Berg et al. 2009). For some, this high growth was commensurate with sustainable debt burdens and low inflation, bringing macroeconomic stability. The improved macroeconomic conditions were the result of growing exports, debt relief, increased aid and private inflows, and improvements in the terms of trade.

The global economic crisis is hitting exactly these key drivers of growth, especially trade flows, capital inflows, and exports from the natural resource sectors and agriculture. Although African economies were isolated, to some degree, from the first

round of the financial crisis, the second round effects are resulting in a growth crisis in African economies. From the high growth rates before 2008, forecasts of growth for 2009 were at 2.3%, with some economies contracting (ADB 2009). This means that for the first time since 1994, per capita income will contract, with significant implications for Africa's ability to reach its development targets. In September 2009, the United Nations Conference on Trade and Development forecast that Africa's GDP growth in 2009 would be only 1.2%.

Several factors drive the effects of the global crisis on Africa. Going into the global crisis, many African economies had already been severely affected by the 2007/08 sharp increase in global food and fuel prices, which reduced their ability to react to the 2008 financial crisis and its aftermath. Between January 2007 and July 2008, the global food-price shock on low-income countries amounted to almost 1.0% of GDP, and the fuel-price shock to almost 3.5% (IMF 2009a). The price shocks impacted on African countries' balance of payments (for some, reserve cover fell below three months of imports) and on their fiscal position (with support for energy and food security costing central government budgets).

As a result of the fall in global demand, African exports have declined sharply, resulting in the deterioration of current account balances and foreign exchange reserves, and losses of trade tax revenue. Exports from the continent are expected to fall by more than US$250 billion in 2009 (ADB 2009). The impact on commodity exports is felt through both the quantity and the price of commodities.

Trade taxes are declining dramatically as a result of the fall in global demand for oil and minerals. The ADB expects the loss to amount to 4.6% of government revenue in 2009.

The drop in commodity prices is causing a drastic fall in foreign exchange earnings for exporters of oil, minerals and agricultural products. This creates shortages of imported products, including inputs for import-dependent activities such as those of the construction sector (ADB 2009).

Capital inflows are declining. Portfolio and direct foreign investment inflows are expected to decline to below US$30 billion in 2009, from peak inflows in 2007 of just below US$50 billion (Plant 2009). At the same time, the ability of countries to raise funds in the capital markets is declining. Some countries have postponed issuing bonds and are expected to rely more on domestic financing (Berg et al. 2009), with impacts on domestic capital markets and interest rates. The potential for reduced aid flows is of concern to many countries, particularly where they face difficult budgetary conditions and/or are heavily dependent on aid flows.

Country-specific sector impacts

Mineral exporters, Zambia and the DRC together could lose about US$6 billion in 2009.

In Uganda, coffee robusta exports were 34% lower in March 2009 than at the same time the previous year (US$23.9 million compared to US$36.3 million).

Nigeria and Angola alone could experience a combined shortfall of US$76.8 billion in 2009. Nigeria may experience a 34% fall in oil export revenue in 2009 relative to 2007, arising from a 5% decline in production and a 31% decline in oil price. Nigerian foreign reserves declined from a peak of US$61.9 billion in September 2008 to US$50 billion in January 2009 (a 19% fall).

In Ethiopia, coffee exports in March 2009 amounted to US$221 million, only half the target of US$446.7 million, due mainly to the decline in world prices.

Cotton and livestock make up 75% to 80% of Mali's annual exports; in Burundi, coffee and tea represent 70% of exports. The international prices of these commodities declined substantially – by 25% for cotton and 19% for coffee – between the first quarter of 2008 and January 2009.

In Mauritius, where the tourism industry accounts for 15% of the GDP, tourist revenues were 15% lower during the last quarter of 2008 on a year-on-year basis.

In Tanzania, where tourism contributes 17.2% to GDP, safari companies reported a cancellation rate up to 60% in November 2008, and the situation was expected to worsen as the crisis deepened.

Source: ADB (2009)

Revenue flows on account of domestic economic activity are also affected. African stock markets have been hit by the crisis. According to the ADB, African markets have experienced much larger losses than those in developed economies. From the end of July 2008 to 17 April 2009, the All Share Index on the Nigerian stock exchange lost 62.2% of its value, the Cairo CASE 30 Index lost 46.2% of its value, and the Johannesburg All Share Index lost 24.4% of its value. In comparison, the Dow Jones Industrial lost 28.5% and the Paris CAC 40 Index lost 29.6% during the same period (ADB 2009). Company asset values have declined, and low confidence levels constrain domestic investment and production.

The exposure of the banking sector in Africa to the first-round effects of the financial crisis was limited. African banking systems had limited integration with global financial markets, minimal exposure to complex financial instruments, limited reliance on foreign funding, low use of leverage, and relatively high banking liquidity (IMF 2009b). However, the system is experiencing second-round effects,

with a surge in non-performing loans resulting in profit losses. Tighter international credit conditions also mean that lending criteria are stricter and lending margins have widened, putting African banks' ability to access funding at risk. Where African banks are subsidiaries of international banks, there is also a risk of de-leveraging, with parent banks being less willing to provide liquidity to their subsidiaries and, at the same time, trying to repatriate capital (IMF 2009b). These impacts of the global crisis on African banks have resulted in tighter domestic credit conditions, further constraining the growth potential of African economies.

In addition to the impact of the global crisis on the oil, mining and agricultural sectors, the effect on the tourism sector is likely to impact on the short- to medium-term growth of African economies. Tourism has been an important growth driver for African economies such as Cape Verde, Mauritius, Kenya, Uganda and Morocco.

The fiscal impact of the crisis is driven not only by reductions in government revenue due to declining domestic economic activity and a reduction in exports, but also by increased pressure on spending. For example, countries will need to expand safety nets and pro-poor spending to address rising poverty levels. Poor people are disproportionately affected, because they hold vulnerable employment and rely on the deeply affected primary mining and agriculture sectors, and because of a potential decrease in aid and remittance inflows (ADB 2009). With decreasing incomes and increasing food prices, the poor are forced to allocate more income to food and to reduce expenditure on health and education.

A significant contributor to rising poverty levels is the increase in unemployment due to declining production and investment. As reported by the ADB (2009), the International Labour Organisation estimates that the unemployment rate in sub-Saharan Africa could increase to 8.5% in 2009, representing an additional 3 million unemployed. Furthermore, the proportion of vulnerable jobs could increase from 77.4% in 2007 to 82.6% in 2009, implying an additional 28 million vulnerable jobs in Africa.

Rising food insecurity is a major factor, as economic growth declines and unemployment increases. The financial crisis has amplified the impact of the food crisis, especially on the urban poor and the rural population. Besides the impact on the current account deficit for food-importing countries (67% for Lesotho, 82% for Gambia, 32% for Mauritania, 31% for Malawi), government action to stabilise food security for the population has been costly (ADB 2009). Declines in food aid increase the burden on domestic budgets. Out of the US$12.3 billion that had been pledged in June 2008, only US$1 billion had been disbursed by the donors by February 2009 (ADB 2009).

Currency depreciation and rising interest rates will also increase debt servicing cost, which may be counterbalanced by the increased local currency value of aid inflows and trade taxes (Berg et al. 2009).

The various effects are threatening hard-won macroeconomic stability with a widening of current account and fiscal deficits. In February 2009, the ADB projected a budget deficit of 5.4% of GDP for 2009 for the continent as whole. By May, this had already deteriorated to 5.8%, down from a surplus of 2.8% of GDP in 2008. The expectation is that the current account balance will decline from a surplus of 2.7% of GDP in 2008 to a deficit of 5.3% of GDP in 2009, according to the May projections. The widening 'twin deficits' severely limit the ability of African governments to undertake needed crisis response initiatives and to sustain their development programmes (ADB 2009).

The declining current account and fiscal balances will pose a renewed threat to countries' debt positions. Before the crisis, most African countries had made progress in improving their external debt conditions. For example, the debt to GDP ratio of countries that benefited from the heavily indebted poor countries debt initiative declined from 117.6% in 2000 to 35.6% in 2008. Countries that benefited from mineral and oil export windfalls had used the opportunity in the mid-2000s to reduce their foreign liabilities. As fiscal balances improved under better growth conditions, domestic debt situations also greatly improved. However, the declining trade and fiscal balances now threaten to reverse these gains. Many countries will be forced to borrow to cover the widening current account and fiscal deficits as revenues decline and spending pressures increase in efforts to respond to the crisis. While low-income countries are the most exposed to this risk, due to their limited fiscal space, middle-income countries will also be affected through the higher costs of borrowing, as they cannot obtain cheap concessional loans (ADB 2009).

Priority policy responses

African governments have limited scope to formulate fiscal responses to the crisis. Key constraints on governments' ability to meet the rising demands for countervailing public spending and investment are declining public revenues, shrinking capital inflows and expensive external borrowing conditions. Scope for fiscal policy responses is also limited because of the risk of crowding out domestic private demand for capital in the limited domestic financial markets, the limited room for counter-cyclical monetary policy in some countries and weak capacity for increasing spending effectively (Berg et al. 2009). Within the limited fiscal space to respond to the crisis, several priorities have come to the fore.

A key recommendation is to preserve a medium- to long-term outlook in formulating responses. Governments are encouraged to preserve the foundations of growth in Africa (ADB 2009). A first policy focus in this regard is the need to avoid building up unsustainable debt and to continue with the structural reforms required to boost domestic economic investment and attract foreign private capital (ADB 2009).

Key policy focuses for growth generated by domestic investment and consumption are: to sustain levels of public spending; to increase domestic tax and resource mobilisation through tax policy and administration reforms, and the development of domestic and regional bond markets; to pursue reforms to improve the business environment; to increase investment in infrastructure to alleviate supply-side constraints; and to increase access to credit for the domestic private sector (ADB 2009).

African countries with output that is below potential, and with sustainable debt and financing options, have more scope to implement an expansionary fiscal policy in pursuit of these priorities. Almost two-thirds of sub-Saharan African countries have low to moderate levels of debt distress, which does allow some scope for fiscal expansion. These countries also have the option to allow automatic stabilisers to work, to accommodate the decline in commodity revenues and to implement a fiscal stimulus package.

In these countries, however, fiscal stimulus packages should be timely (lags in identifying and implementing suitable measures and weaknesses in public financial systems can result in delayed responses, which would be pro-cyclical rather than anti-cyclical), the interventions should be targeted to maximise the change in economic output relative to the change in the fiscal balance (countries should carefully weigh the impact of tax cuts in relation to the impact of expenditure increases), and the measures chosen should be reversible, in other words not result in permanent increases in fiscal deficits (Berg et al. 2009). To avoid rolling back the gains made pre-crisis in increasing countries' revenue ratios, it is not recommended that tax rates be reduced (Berg et al. 2009). Spending should focus primarily on infrastructure, in particular roads, electricity and telecommunications, and spending should be sustained on health, education, water and sanitation, and social protection (Berg et al. 2009).

Countries that have little fiscal space, few or expensive financing options and a high risk of debt distress need to look at fiscal adjustment in order to weather the effects of the global crisis (Berg et al. 2009). The preservation of macro and debt sustainability is an important imperative that reduces the options available to these countries. For these countries, policies are required to increase revenue and prioritise

spending within the fiscal limitations. Strategies to increase revenue should focus on broadening the tax base and strengthening revenue administration. This would put in place important structural reforms to support long-term growth. Some countries, however, might need to look at temporarily increasing some tax rates to alleviate the immediate impact of the crisis in their short-term adjustment packages. Strategies to rationalise and redirect spending should target generalised subsidies, transfers to loss-making public enterprises and excessive government employment (Berg et al. 2009). Spending increases, if possible, should be directed at productive spending on infrastructure and the reinforcement of social safety nets. The strengthening of public financial management systems to improve spending efficiency should be a continued priority.

The ADB also emphasises the need to use the current circumstances to strengthen banking sector regulation and to pursue prudent capital flow management (ADB 2009). Key measures are better risk assessment and monitoring systems and capital adequacy requirements. In addition, African countries need to pursue prudent capital control strategies to promote private inflows, while reducing the risk of abrupt reversals. The IMF has emphasised the need to strengthen bank supervision and improve contingency planning (IMF 2009c). It is important in this regard to focus on banking system vulnerabilities (identify banks that are most likely to experience difficulties; require frequent data provision from banks; and comprehensively supervise foreign currency risk, bank risk management practices, lending standards and funding reliability).

The IMF Africa Department has emphasised the role of monetary and exchange rate policies. In some countries where inflation has fallen in recent years, monetary easing can provide a stimulus for growth on the back of the slight decline in food and energy prices. Other countries that still experience excessive inflation might need to tighten monetary policy (IMF 2009c). In countries with flexible exchange rate policies, real exchange rates should be allowed to depreciate as an automatic stabiliser. The IMF has advised against introducing new controls on capital outflows and using reserves to support exchange rates.

The ADB has identified several other policy areas that should be emphasised in regional and country-specific responses. These include a focus on investing in information and communications technologies, consolidating political stability and improving governance. A key factor in Africa is likely to be the new trade and development partnerships with India and China, which offer great opportunities for Africa to diversify its export markets, its sources of development financing and private capital inflows.

The scope for African countries to countervail the global crisis, however, remains constrained. African countries are increasingly unable to finance the widening current account deficits. The structural investment-savings gap in many African economies has been worsened by the crisis, and options for fiscal policy responses are constrained. The ADB has estimated that in order to achieve pre-crisis growth rates, African countries would need US$50 billion to finance the investment-savings gap (ADB 2009). To achieve the 7% growth rate required to reach the Millennium Development Goals, the financing requirement increases to US$117 billion. African economies continue to need strong support from their development partners to fill these financing gaps and to support national response strategies. The renewed commitment by international and development finance institutions to pre-empt the crisis from worsening in Africa is important. How these packages are tailored will be crucial in supporting a speedy recovery and providing a base for long-term growth.

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4.3 The global crisis and its effects on the Zambian economy

Danies Chisenda
Note compiled by Yacine Bio-Tchané

The Zambian economy has experienced robust growth over the past few years, thanks to macroeconomic stability supported by prudent fiscal management, and a favourable external economic environment with strong global demand for metal commodities.

Zambia, a copper-rich country, has benefited from high copper prices in recent times. Copper export prices nearly doubled between 2005 and 2008, from US$1.5 per pound to US$2.9 per pound, and the volume of copper exported increased by more than 30% during this period. This resulted in a growing economy, 6.1% growth per annum between 2006 and 2008, curbed inflation to a single digit figure (8.9%) in 2007, a surplus in the balance of payments and stabilised the exchange rate, allowed for the accumulation of comfortable international reserves, which more than doubled (from US$331.1 million in 2005 to US$976 million in 2008), and the expansion of industry by way of sector linkages, thereby creating employment.

Unfortunately, the Zambian economy suffered a slowdown in 2008 due to an unfavourable external economic environment characterised by record increases in world fuel and food prices during the first half of 2008, which had inflationary effects, and falling global demand for copper, leading to lower prices for the commodity in the second half of 2008. Other factors, such as flooding due to heavy rains that destroyed crops and a slowdown in the construction sector, had a negative impact on growth prospects. Also, unexpected events like the larger-than-planned civil service wage award, the need to hold presidential elections, the need to augment resources for the Fertiliser Support Programme and the need to finance the Zambia Electricity Supply Corporation (ZESCO) rehabilitation project exerted significant pressure on expenditure.

As a result, macroeconomic performance in 2008 was weaker, with lower than projected growth rates and higher inflation and interest rates. The Zambian economy is estimated to have grown by 5.8% in 2008 (with a slowdown in key sectors such as mining, tourism and construction); inflation outturn skyrocketed to 16.6% (against a target of 7%) and the Zambian currency, the Kwatcha, depreciated by 27.3% against the US dollar. While growth is projected to be lower (at 5%) in 2009, inflation is expected to fall to 10%. Growth is expected to improve in 2010/11 alongside a global recovery.

Faced with these challenges, the government decided to maintain a prudent fiscal policy and to realign expenditure items to cushion the impact of the multiple crises on the domestic economy. Despite a reduction in projected government revenues as a result of a fall in the production of copper, the government is set to enhance provision for social safety programmes and to reduce excise duties on fuel. Additionally, the government will promote diversification and improve national competitiveness through structural reforms and infrastructure development. Emphasis will be placed on agricultural development, tourism infrastructure development and the promotion of the manufacturing sector. Finally, borrowing will be maintained at sustainable levels and there will be greater investments in human capital.

The government responded to the slowdown of the economy through specific policy interventions, the primary one of which has been to protect key productive sectors from further decline and increasing unemployment by offering tax concessions.

On the revenue side, several sectors have benefited from fiscal incentives. In the mining sector, the windfall tax has been removed, capital allowance has increased by 100%, customs duty has been removed on copper powder, flakes and blisters, and excise duty on heavy fuel oil has been reduced from 30% to 15%. For the manufacturing sector, and particularly for developers and investors in the Multi Facility Economic Zones (MFEZ) and industrial parks, taxes on management and consultancy fees have

been waived, VAT no longer needs to be paid for supplies to the MFEZ and industrial parks, and the necessary equipment and machinery are exempted from tax. Other sectors, such as agriculture, tourism and energy, also receive various forms of tax incentives. Additionally, the government has provided tax relief to workers.

A further policy intervention is geared towards increasing expenditure on infrastructure and social services. To support diversification of the economy, approximately 20% of the budget was allocated to economic affairs, which include: (a) agriculture, forestry and fishing, particularly allocations to the fertiliser support programme, the strategic food reserve and livestock and irrigation development; (b) fuel and energy; (c) mining; (d) transport (mainly roads); (e) communication; and (f) tourism.

In light of constrained revenues, these measures are achieved through a realignment of resources and an increase in borrowing (23.3% of the budget will be financed through foreign assistance, grants and loans from co-operating partners). Grant support has increased from 3.9% to 4.6% of GDP, and external borrowing has increased slightly from 0.5% to 0.8%. The government has also borrowed domestically but has enhanced its efforts to improve the efficiency of revenue collection. Zambia's development partners have not shown signs of reducing their commitment to official development assistance. On the contrary, certain donors, like the Department for International Development (DFID) and the European Union (EU), have increased their support and have pledged to continue supporting Zambia's development agenda.

The global financial crisis has put a strain on the Zambian economy. However, the country's vulnerability has led the government to shift gear and build on the achievements of various economic diversification programmes pursued over the years. It is important that the government places emphasis on stimulating growth through diversification, while ensuring that it has the resources necessary to finance its operations.

The future of the Zambian economy lies in diversification, mainly by: (a) becoming the breadbasket of eastern and southern Africa, and providing energy to countries in these sub-regions; (b) capitalising on the potential of beef as a new export commodity; and (c) offering the right incentives to manufacturers to use Zambia as a strategic location to supply goods to the region.

4.4 Egypt's fiscal policy response to the global economic slowdown

Amgad Hegazy
Note compiled by Yacine Bio-Tchané

During the past few years, the government of Egypt has conducted prudent macroeconomic policies and a supportive monetary policy, which have led to robust growth, job creation and strong external balances.

Growth of the Egyptian economy has increased from 4.1% in 2003/04 to 7.2% in 2007/08, thanks to a boom in key sectors like manufacturing and extractive industries, tourism, retail and construction. During these years, the growing economy led to a surge in the number of jobs created, with 49% more jobs created in 2007/08 than in 2004/05. Thus, unemployment declined from 11.2% in 2004/05 to 8.4% in 2007/08. Furthermore, foreign direct investment (FDI) has more than doubled since 2004/05, and the overall balance of payments has slightly increased since 2005/06.

The 2008 global economic crisis has reversed these tendencies. Egypt's growth decreased steeply from 7.6% in the second quarter of the fiscal year 2007/08 to 4.1% in the second quarter of the fiscal year 2008/09. There has been a retreat in the real economy: despite firm consumption levels, government investment has deteriorated.

Expenditures in key sectors, mainly manufacturing and services, have reduced notably. The external sector has been the most affected. As industrialised nations are experiencing lower growth rates, forecasts for world trade flows are very pessimistic. In Egypt, both current accounts (mostly in tourism) and capital account flows (particularly FDI) have felt the brunt of the crisis.

However, trade flows have been affected to a much lesser extent. While export growth has fallen due to a waning of external demand from Egypt's main trading partners, import growth has retracted amid a drop in international prices. The crisis has also spared the country's tax revenue levels, with the exception of a slight deficit in taxes on international trade and corporate activity. Overall, tax revenue increased by 17% from the fiscal year 2007/08 to 2008/09.

The government of Egypt's response to the slowing economy has been to introduce a fiscal stimulus package. The government intervened with two temporary packages aimed at protecting society and the economy from the effects of the crisis.

The objectives of the interventions are to: (a) sustain growth; (b) boost domestic demand and employment; and (c) maintain social balance while ensuring medium-term fiscal and debt sustainability. It is important to mention that the fiscal stimulus is fully self-financed by the government; thus, it has a neutral deficit and is geared to accelerate the already planned public investments.

The first package was adopted in May 2008, as the government had approved policies to increase social spending on food subsidies and wages. As the country faced high levels of inflation, due to the increase in prices of food and raw materials, the package was structured as a once-off allocation of almost EGP14 billion. However, the government was mindful of maintaining stable deficit and debt ratios, while offering subsidies for food and other commodities essential for the survival of populations with a limited income as well as the poorest segments of society.

The second package was adopted during the fiscal year 2008/09, when the global recession began affecting domestic growth rates. The government presented a bill for an additional provision of EGP13.5 billion to accelerate project implementation in several areas, including potable water and sanitation, the development of roads and other infrastructure, the promotion of exports, domestic trade infrastructure and industrial development. In this regard, the government is implementing a policy that should stimulate demand by boosting spending on public services.

While the focus of the stimulus is on sustaining spending on public investments, as well as supporting industrial zones to maintain export volumes, the government has also taken policy measures on the revenue side, mainly by reducing tariffs on customs for intermediate and capital inputs to support the manufacturing industry and to boost production.

Additional measures were taken by the government to ease the burden of the crisis on the financial sector. The Central Bank of Egypt reduced interest rates by 1.5% in February and March 2009. It has also reduced the required reserve ratio to entice banks to lend more. Finally, a revision of the growth in credit to the private sector and to small and medium enterprises, and a review of the role of companies providing mortgage finance to small and medium enterprises, are underway. Among other policy measures, the government is easing access to land for investors and is developing a coherent investment promotion strategy to attract investors and to keep FDI at sustainable levels.

Overall, the fiscal stimulus packages have enabled public investment expenditures in order to compensate for the reduction in private sector investment and to offset the withdrawal of substantial FDI in the country due to the financial crisis. The Egyptian government pursues its strategy of stimulating effective economic activity and creating jobs to alleviate the repercussions of the crisis on factories and production.

The government's efforts have been relatively effective. The outturns for the fiscal year 2008/09 were not as negative as expected, thanks to the fiscal stimulus package. The budget deficit stood at 6.9% of GDP, while expected revenues increased slightly by 1% (from EGP275.5 billion to EGP278.6 billion) and expected expenditures increased by 2% (from EGP340 billion to EGP347.7 billion). The increase in revenues was due largely to the fiscal stimulus package, which generated demand and pushed the bill of imports. As a result, despite the budget deficit and an increase in public debt and its service burdens, the government has managed to maintain spending levels on priority areas.

However, while the Egyptian economy did not feel the repercussions of the global financial crisis during the fiscal year 2008/09, the government expects to feel the effects of the crisis during the fiscal year 2009/10. First, growth rates are expected to reach only 4% instead of the initially anticipated 7%. Second, the total budget deficit is expected to rise again and reach 8% of GDP, negatively impacting on the government's efforts to maintain social spending and to stimulate economic activity. Also, the budget is smaller compared to the previous year, due to lower levels of state revenues and thus expenditures. The budget deficit will be covered and financed through borrowing.

Despite the negative scenario, the Egyptian government is intent on steering public spending towards the purchase of Egyptian products and commodities, the use of the services of local contractors and suppliers, the employment of the local workforce and the connection of export promotion with the achievement of quantitative and valuable targets, in order to enhance the local economy and to create employment for all Egyptians.

5

Budgeting for infrastructure

5.1 Introduction

Capital budgeting and the financing and management of infrastructure projects are ongoing CABRI themes. This chapter reflects the sessions at the 5th Annual Seminar on different options for financing public infrastructure and on systems to ensure that value for money is achieved in the development of public infrastructure.

The first paper is a note by Yacine Bio-Tchané, from the CABRI Secretariat, on the presentation prepared by Prof. Edgardo S Mimica, from the Adolfo Ibanez University in Chile. The paper sets out the Chilean experience of a centralised project appraisal function, coupled to government-wide budgeting and management of infrastructure. The Chile case study raises a number of issues and lessons for African countries, many of which are experiencing growth in their capital spending. In particular, it illustrates the potential benefit of a comprehensive, government-wide system to appraise, plan and manage capital projects.

The second paper is a note by Alta Fölscher, from the CABRI Secretariat, flowing from the presentation by Dr Davies, Executive Director of the Centre for Chinese Studies at the University of Stellenbosch, South Africa. The paper utilises the presentation and papers by Dr Davies and others published by the Centre to provide

a picture of the involvement of the People's Republic of China, the Chinese EXIM Bank and Chinese construction companies in Africa.

In the third paper, Tasima A. Jah and Abdul Rahman Conteh, respectively Deputy Director of Budget and Senior Budget Management Officer in the Ministry of Finance and Development, Sierra Leone, review Sierra Leone's engagement with China and the African Development Bank. They conclude that urgent attention is required to improve arrangements to plan, finance and manage infrastructure projects in Africa.

5.2 Capital budgeting systems: The Chilean experience

Edgardo S Mimica
Note compiled by Yacine Bio-Tchané

For the optimist, the glass is half full; for the pessimist, the glass is half empty; for the project evaluator, the glass is double the necessary size and we are wasting resources – a project appraisal joke

Introduction

A capital budget reflects a country's investment portfolio. As developing countries are increasingly investing in economic and social infrastructure projects, the level of investment and the quality and effective implementation of these projects are essential for economic and developmental objectives. Different processes and systems have been used to manage investment projects. In Chile, the government plays a strategic role in ensuring that public investments create low transaction costs and are

aligned with the country's social and economic development goals. In the midst of the innumerable needs for investment in various sectors and limited public finances, a system has been established to decide which demands for public investment should be prioritised and which ones need to be postponed or cancelled. The ultimate decision on selected projects is based on social returns and development objectives from a technical, economic and social point of view. This system is called the National Investment System (NIS) or *Sistema Nacional de Inversión Pública*, and ensures a high level of quality in the country's public investments.

This paper explores the Chilean NIS, which established norms and procedures that have improved the government's ability to appraise, plan and manage capital or investment projects.[1] The paper describes: (a) the rationale for the NIS; (b) the processes used to make more cost-effective choices for the planning and budgeting of capital projects; (c) institutionalisation, legitimacy and capacity building of the NIS; and (d) challenges faced by the NIS. A case study on a seaport project is described to illustrate the role that systems such as the NIS play in ensuring that all investment options are explored and the most cost-effective ones are chosen when making public investments. The paper also emphasises the importance of taking into account politics when choosing which projects to invest in, given the annual budget, as well as the importance of capacity building of civil servants who are appraising investment projects.

Rationale for the NIS

The Republic of Chile is a middle-income country (with a GDP per capita of US$9 876) bordering Peru, Bolivia and Argentina in Latin America. The country's territory is divided into 13 regions, which are comprised of 51 provinces and 345 municipalities.

In the 1970s, the government of Chile acknowledged disparities between ministries' budget allocations and the quality of investment projects. As a result, there was a tendency to execute more projects with low or negative social returns to the detriment of those with higher returns due to limited funds. This was due to civil servants' inability to identify, prepare and appraise investment projects. This realisation led to the need to improve the quality and efficiency of public investments and, in 1973, the government launched the NIS.

1 This paper draws generously from a paper prepared by Pilar Contrera G, from the Ministry of Planning in Chile, *Sistema nacional de inversión pública experiencia Chilena*, and from a presentation delivered by Juan Cavada Artugues, also from the Ministry of Planning, *Sistema nacional de inversión pública: notas sobre la experencia de Chile*.

The NIS is a system with norms, procedures and regulations that aims at improving the quality and relevance of public investment projects and at eliminating 'bad' projects. The NIS is located in the Ministry of Planning and is jointly administered by the Ministry of Finance. Provincial and local governments, major municipalities, state enterprises, sector ministries and other state entities formulate and appraise projects they seek investment for according to the regulations established by the Ministry of Planning. The NIS's functions of formulating, presenting and executing investment projects are exercised at the central, regional, provincial and local levels. The Ministry of Planning does not formulate any project; it is responsible for reviewing and monitoring the appraisal of projects that have been submitted by various ministries and public institutions.

This process of project appraisal of public investment is done electronically, through the Integrated Bank of Projects, across all levels of government. E-government has been one of the objectives of the Presidency, and the use of information and technology is mainstreamed among government agencies.

The Integrated Bank of Projects is an up-to-date database that contains each of the projects in need of public funding and records information on every step of the project life cycle. One of the major contributions of the database has been the use of a common jargon for the different processes to identify a project. It is also important to highlight that the database has been updated several times since it was computerised in 1985. It has kept up with technology and has been modernised to improve the system so that entering and processing information is faster and access is simple and easy.

The database is operated by 5 000 registered users who are responsible for formulating and appraising investment projects across the country. These users come from 1 400 public institutions, specifically, ministries, municipalities, provincial governments, governors' offices and public companies.

The database is used to enter and store data relevant to investment projects according to the rules and procedures established by the NIS. It has the capacity to handle an average of 15 000 new initiatives each year. Currently, there are approximately 500 000 projects in the database.

The database exists in three formats:

- The *consultative section* of the database is available to the general public and does not require users to register or to create user IDs. It is a search engine that enables access to any project idea that has been submitted by the government, according to geography, sector, thematic area or keyword. The results of the search are in the form of project typology, project analysis,

financial information and the year in which the investment was sought. This tool enables viewers to analyse information on public investment.

- The *working section* of the database is used only by previously registered public sector users to enter new information on project ideas or to modify existing one.
- The *management section* of the database is restricted to registered users of the working section of the database. It gives access to different tools that enable users to extract information on current and previous processes. It also facilitates the analysis and control of public investment. This database is a shorter and more easily accessible version of the data contained in the working section of the database.

The data on project initiatives or ideas contained in the Integrated Bank of Projects is carefully reviewed and analysed by project appraisal officers who decide through carrying out cost-benefit analyses which projects are viable. Every public investment project idea undergoes the same treatment. That is the role of the NIS. It is neither software nor database, but a system based on rules and procedures that 5 000 professionals apply to prepare and appraise projects. Thus, the Chilean NIS plays the role of a giant sieve, which filters the best projects and allows them to compete for resources in the annual budget. Most investment projects require one or two years to mature (i.e. to be financed) and only the projects with the highest returns and the highest socio-economic impact are included in the budget. Most investment projects must comply with quality standards in terms of elaboration, evaluation and analysis, and they are controlled and monitored according to uniform and transparent rules and with an adequate democratic participation of both public institutions and civil society.

The Chilean law stipulates that only projects within the NIS, which have also been favourably assessed by the Ministry of Planning, can appear on the capital budget that is tabled to Congress.

Thus, the purpose of the NIS is to provide public authorities with a plentiful portfolio of good investment projects, so that they can choose those most suitable for society as a whole.

The NIS is rigorous and even-handed in considering project financing. This systematic appraisal of public investment has been successful in ruling out 'white elephants' and in keeping to the government's policies on growth and development. The bottom line is that the NIS is all about efficiency in the use of scarce public investment funds.

How does the NIS operate?

The NIS established the norms and conditions for the process of public investment, which consists of conducting a socio-economic evaluation of projects using a specific methodology. This process permits the transformation of ideas on projects into investment projects, and it allows differentiating between bankable projects and projects that should not be executed from the point of view of cost effectiveness and impact on society.

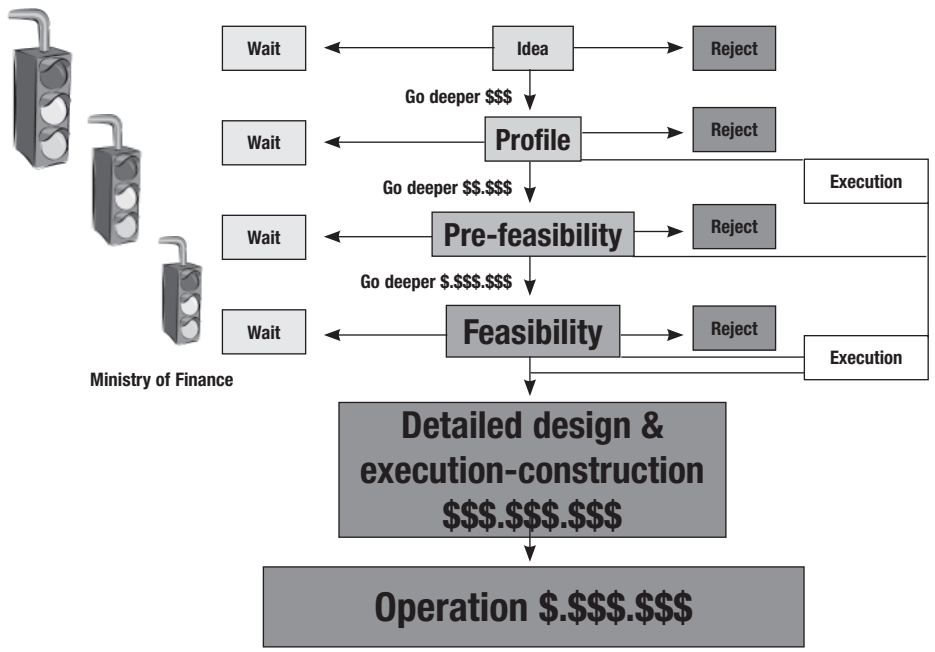
The Ministry of Planning sets the norms, procedures and methodologies for the preparation and evaluation of projects that any public institution, at the national, regional and local level, seeks financing for, and analyses, revises and makes technical recommendations for each of them. Ministries, departments and agencies are responsible for formulating, presenting and appraising all projects in need of public funding according to the established norms. Legally, no project can be executed before the Ministry of Planning has made a positive recommendation on the project.

For the evaluation of investment projects, the NIS uses specific methodologies that take into account the particularities of these projects. The NIS primarily conducts cost-benefit analyses to assess the social benefits yielded by investment projects. In fact, 25 different methodologies are available to agents who appraise the project ideas. The methodologies have improved over time, and new ones have been incorporated in response to changes in the types of project. The methodologies are established jointly by civil servants in the Ministry of Planning and relevant ministries and agencies that seek to carry out public investments.

In the NIS, projects have to follow the natural development cycle to be approved. The process starts with an idea that is officially entered by a ministry or public institution into the NIS and sent to the Ministry of Planning together with a request for financing for the year in which the project would start. It is these institutions' role to formulate and appraise projects according to the Ministry of Planning's regulations.

During the pre-investment stage, the Ministry of Planning creates a profile for the project and analyses the information submitted by conducting pre-feasibility and feasibility studies. Once this is done, the ministry officially informs the institution in charge of investment of the results of the technical-economic analysis. The Ministry of Planning does not formulate projects, it only reviews and monitors the appraisal of projects. Additionally, it verifies whether investment initiatives are attractive by performing economic or social project appraisal (see box below for a detailed description of the pre-investment stage).

Figure 5.2.1: Flux diagram of a project life cycle



Only when the study, programme or project has been favourably recommended as being cost-effective does the Ministry of Finance generate a detailed design of the project and monitor project execution. That is the investment stage.

The operation stage is the final stage of the project life cycle and consists in the operationalisation of the project by the ministry or public institution responsible for the project. The Ministry of Planning conducts an *ex-post* evaluation of the project.

The project development cycle is a continuous and dynamic process with a great deal of overlap, interaction and feedback between the various phases of the project life cycle. Many of the activities are interrelated and cannot be confined to one particular phase. This interrelationship is particularly strong among the phases preceding the implementation of the project. There is considerable interaction between the implementation phase and the evaluation phase as the lessons of *ex-post* evaluation are used constantly to suitably modify the operations of the project.

While this process may seem somewhat technocratic, with several phases and three main institutions involved, politics plays an important role during the entire process. Politics can distort the portfolio of projects that are approved, as the government's incentives to spend on mega-visible projects are high, especially at election time. The government of Chile has attempted to curb this phenomenon by building firewalls

and establishing safeguards before each stage of the project life cycle. It becomes important for effectiveness and transparency purposes to ensure that the NIS (or similar system) is not caught up in the political aspect of public works and focuses on providing the country with the best alternatives in public investment for growth, development and societal welfare.

Thus, the NIS systematically kills bad projects, and does so as soon as possible during the pre-investment stages. When this has been successfully accomplished, politicians and civil society enter discussions on the investment decision or start lobbying only after the NIS pre-investment process has come to an end. Public discussion is only on the portfolio of projects that have been approved by the NIS.

Moreover, the NIS introduces gradualism into the mandatory project life cycle by slowing down the investment decision and ensuring that it is based on sound appraisal. As a result, the NIS becomes the anchor of the financial system; it provides stability, forcing a gradual approach towards the desired end (see Figure 5.2.1 for a flux diagram of a project life cycle).

Components of the NIS project cycle: pre-investment stage

Idea: Identification of an unresolved problem, possible benefits, geographic localisation and objectives.

Profile: Collect additional data and check previous information. Examine technical and institutional alternatives, establish first cost assessments for investment, operation, project life and other requirements. Do a preliminary evaluation.

Pre-feasibility: Obtain all the detailed information needed. Eliminate certain unviable alternatives and evaluate the rest. Prearrange for financing. Study all modules: marketing-demand, technical, environmental, human resources, institutional. Do financial, economic and distributional appraisals. Also conduct a sensitivity and risk analysis. Find the best alternative.

Feasibility: Develop the chosen alternative and reduce the uncertainties to acceptable limits, and define its parameters. Arrange final financing scheme. Go deeper into studying modules with the highest risks, and check all the assumptions you have made.

Design: Detail engineering design, blue prints and specifications. Define all the logistics, make final adjustments prior to execution stage, and draft bidding proposal.

Institutionalisation, legitimacy and capacity building of the NIS

The norms and procedures established by the NIS are embedded in a legal framework. A set of laws has been passed, stipulating: (a) the steps required for public institutions to request public funds for investment projects; (b) the role of the Ministry of Planning in elaborating global and sectoral policies and in maintaining and evaluating public sector projects; (c) the procedure for incorporating new investment projects during budget execution; (d) the requirements for public investment projects that also require external funds; and (e) the type of financial information at the planning and execution phases of the cycle that need to be entered into the Integrated Bank of Projects database. An NIS has to be rooted securely in the national legal system of a country for it to be credible, legitimate and operational. It is even better for it to appear in the Constitution.

The NIS has evolved as a legitimate and valid system in the eyes of the government and society in general. The system has achieved legitimacy at three levels: economic, ethical and political:

- *Economic legitimacy*: efficiency 'creates' important economic resources, which contribute towards resolving a number of problems in the most effective manner. Economic legitimacy has been gained by the NIS's success in filtering the bad and finding the best projects among 0.5 million alternatives that revolve in the database. This gain in efficiency has helped to solve more social demands within the limitations of available public funds.
- *Ethical legitimacy*: ethical legitimacy stems from the increasing transparency and availability of contemporary information regarding the public investment process. Information about all projects in the Integrated Bank of Projects has been made public through the Internet.
- *Political legitimacy*: public efficiency valorises the role of the political system as well as that of authorities. Thus, democracy is enhanced through the co-ordination of government policies and strategies. Moreover, civil society has participated increasingly in discussions on investment-decision processes. Private and non-governmental organisations may also propose and formulate investment projects, but they must be co-ordinated through the provincial or local governments in order for them to apply indirectly for public funding.

The NIS requires a critical mass of professionals qualified in preparing and evaluating social projects across all spheres and levels of government and in public institutions. Thus, it is important that this staff is trained regularly and provided with the necessary tools to enable the system to operate smoothly and efficiently. As a result, the government of Chile has made some tools available to build the capacity of the NIS. These tools include a manual for project preparation and appraisal, methodologies for specific project preparation and appraisal, executive education and training for the public sector and periodic recalculation of shadow prices and national parameters (used to do cost-benefit analyses).

A system that operates according to the established processes and criteria contributes towards the transparent management of public funds for investment.

Some challenges of the NIS

Thus far, the NIS has operated efficiently in allocating public funds for investment and in the welfare of society. Additionally, the government has aimed consistently at improving it and rendering it even more effective. Currently, the system faces several challenges.

The first is related to improving the way the system operates, mainly through simplifying the processes, improving the methodologies and incorporating new ones, strengthening human resources, greater IT support and reduction in the time necessary to process information and to analyse it. Furthermore, maintaining such a system has proven to be more difficult than foreseen, due to the need for sufficient qualified professionals at the central, regional, provincial and local levels. Retaining these professionals has been challenging because of competitive remuneration in the private sector.

Secondly, there seem to be more investment projects recommended than there are funds available for in the capital budget. The quality of some of these projects appears questionable. This situation is created by a lack of co-ordination among the staff in charge of formulating and appraising these projects in relevant institutions.

Thirdly, the system of *ex-post* evaluation of projects remains weak and is incapable of verifying whether financial resources have been allocated efficiently to investment projects.

Finally, decentralisation of project appraisal has not been done with sufficient resources and supervision; externalities and urban impacts of public investment are not assessed, and the considerable increase in the number of small projects has led to re-examining the processes in place.

Case study: evaluation of a seaport project in Chile

The Chilean port had been experiencing congestion problems as ships had to wait for a long time before loading and unloading their cargos. Given that seaports are the biggest and most expensive infrastructure investments of civil engineering, the Chilean government contracted the services of a well-known consulting firm to find a solution to this problem.

Using queuing theory and sophisticated simulation models, the firm measured and valued the cost of one day of waiting time of an average ship. The firm came up with an engineering solution, which was a mega-project for building two new wharfs for the vessels. The economic attractiveness of this project was calculated through the Economic Internal Rate of Return, which was 13%. However, the project seemed more attractive for the mayor, construction firms and engineers than for remedying the issue of congestion.

As a result, the Ministry of Planning hired the department of economics at the Catholic University to suggest alternative investment options. The university team re-evaluated the project at a pre-feasibility level, and determined that an increase in the size of the seaport through the construction of two new wharfs was only one of the alternative projects that could solve the queuing problem. The team arrived at this conclusion through optimisation of the 'base case', using information on the capacity of a seaport (determined by the number of available sites for cargo handling, operational efficiency and the number of hours the port is open for business).

To speed up the transfer of cargo, the university team proposed opening up the seaport operations to private companies to handle the cargo within the port facilities. An increase in warehouse storage prices at the seaport would create the right incentives to push the cargo to inland intermodal terminals ('dry-ports') that were cheaper. This strategy would liberate space at the port site, relieving congestion, but the most important proposal was to open up the seaport to a 24-hour-per-day operation using three working shifts. This proposal would require workers to work overtime; thus, overtime pay would have to be negotiated with the powerful seaport workers union.

The result of this base case optimisation exercise allowed the Chilean government to postpone the enormous investment suggested by the consulting firm for another 15 years. The consulting firm's mistake was not in measuring and valuing the cost of one day of waiting time for the vessels, but in determining the incremental costs and benefits of the project.

The original project was not accepted by the government, and the seaport started working three shifts, 24 hours per day, 365 days per year.

Conclusion

The advent of the NIS in Chile has permitted the timely discovery of deficiencies in project ideas and has allowed a more effective and transparent allocation of resources to public investments. As a result, the system rules out the enormous costs of 'white elephants' to society. It creates conditions for a better co-ordination of public investments, as well as clearer decision-making based on the costs and benefits of demand-based projects in line with limited public funds.

However, what makes the NIS successful is a combination of factors. Continuity in political will and a legal framework constitute the first prerequisite for success. A sufficient number of qualified staff who have benefited from training and have incentives to ensure the effective functioning of the system is a second important element. Third is the use of a database like the Integrated Bank of Projects, which makes the system operational. Fourth, decentralisation or de-concentration, done with the necessary resources, training and supervision, are ways in which the system is made more operationally effective at various levels of government. Last, project appraisal is not an exact science. Thus, time, repeated efforts to review processes and methodologies, a clear understanding of the weaknesses in project ideas and the process of reviewing the appraisal of projects before they reach the feasibility stage are important.

5.3 China's role in infrastructure development in Africa

Martyn Davies
Note compiled by Alta Fölscher

China's growth path over the past three decades has been extraordinary. For 27 years, the average annual growth of China's per capita GDP has been 9.4%, and in the 20 years between 1985 and 2005 the number of people living in absolute poverty (US$85.38 per year) has decreased from 125 million to 24 million (Davies & Jansson 2008).

The policy priority for China has been growth and development. Its foreign policy, in particular in the developing world, has emphasised commercial objectives, including securing access to the commodities required to sustain its economic growth. In this pursuit, it has sought a closer diplomatic and economic coupling to Africa. The relationship between China and African states has grown particularly rapidly over the last decade. All but four African countries now have diplomatic ties with China, there has been a rapid growth in trade, and the flow of aid and loans has expanded greatly.

The impact of the changing relationship can be seen clearly in a comparison of Chinese and African growth statistics (see Figure 5.3.1). After 1999, the impact of

China's New Africa Policy is apparent in the close correlation between growth in the African and Chinese economies (Davies 2009).

Figure 5.3.1: Real GDP growth, China and Africa, 1980–2009 (forecast)

Source: IMF, EIU and Frontier Advisory analysis, in Davies (2009)

Kaplinski identifies three factors through which China affects sub-Saharan Africa: (a) trade flows; (b) foreign direct investment, technology transfer and integration in global value chains; and (c) aid flows (see Davies & Jansson 2008). However, these factors are interwoven, as much Chinese private sector activity in Africa is either state-supported or financed through Chinese concessional loans, which, in turn, are coupled to Chinese trade concessions and guarantees.

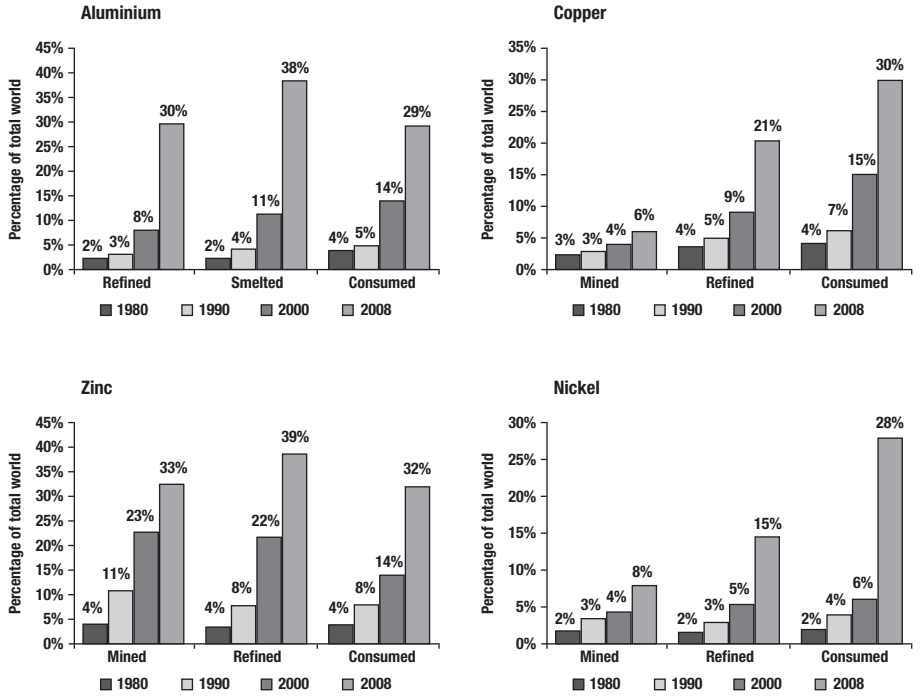
This paper examines the impact of Chinese engagement with Africa on the public infrastructure sector. It looks at the factors that drive this engagement, the kind and distribution of trade interests and infrastructure investment, the typical institutional arrangements that underpin the infrastructure investment, and the implications for African policy and institutional capacity.

Chinese interest in Africa

Several main reasons behind Chinese interest in Africa can be identified. The first concerns the need for raw materials: China has about one-fifth of the world's population and only 7% of its productive land. Hence the oil, timber and mineral resources that China lacks are critical in fuelling its rapid economic growth, modernisation and development (Le Pere 2008). Given that China has an aging population, there is only a limited window of opportunity during which it can take advantage of a large pool of cheap labour to fuel growth and wealth accumulation, and to lay the groundwork for economic restructuring (Kornegay 2008).

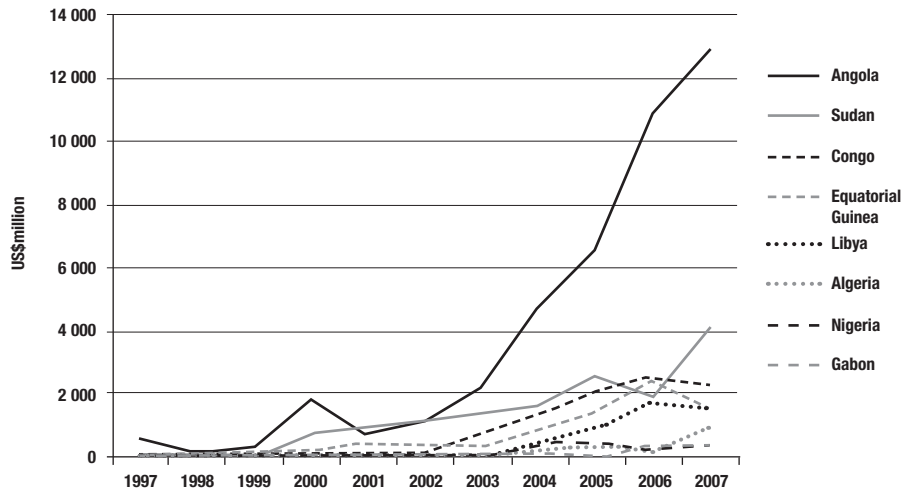
Access to energy and other natural resources, therefore, tops China's list of priorities, and China has secured access at governmental level to Africa's resources (Alves 2008). One aspect of particular importance is energy security, which has driven the choice of African countries with which China has engaged. China's higher demand for resources compared to the rest of the world explains the close coupling of its growth and Africa's (see Figure 5.3.2). Similarly, the impact of its energy demand on the earnings of African states is reflected in Figure 5.3.3.

Figure 5.3.2: China's share in world consumption of key minerals



Source: NBS, ICSG, INSG, ILZSG, China Metals & Macquarie Research, in Davies (2009)

Figure 5.3.3: Top-8 African states exporting oil to China



Source: Davies (2009)

A second important factor is the emerging African consumer market. Markets that ensure continued demand for Chinese-manufactured goods are as important for sustaining the accumulation of wealth in China as is a secure supply of energy, minerals and other natural resources. China views Africa as being at the beginning of its own economic growth trajectory and, consequently, as an ideal market for its goods. In fact, China's trade data reveal that it already exports more to most African economies than it imports (Alves 2008).

A third factor is that engagement in African economies is 'a good incubator' for emerging Chinese state-owned multinational companies (Alves 2008) or, put differently, a commercial learning ground for China Inc (Davies 2009).

China's interest in Africa, however, is not purely commercial: geo-strategic politics are also involved. In addition to its ongoing interest in reducing Taiwan's diplomatic footprint (today only four African countries recognise Taiwan, compared to 14 in 1946), China's closer ties with African states help it to garner support for the positions it takes in international forums. It places great emphasis in its rhetoric on its own status as a developing nation, and on the importance of South-South co-operation and co-development (Alves 2008; Le Pere 2008; Habib 2008).

The nature of Chinese engagement

China has pursued deeper engagement with Africa through various instruments, including trade agreements, loans, aid, debt forgiveness and assistance with infrastructure investments.

Sino-African relations go back several centuries. Chinese mariners visited the east African coast in the 15th century. After the formation of the People's Republic of China (PRC), China established diplomatic relations with many African states as soon as they became independent. The PRC provided financial support, equipment and training to many African liberation movements, including in Angola, Congo, Mozambique, Namibia, South Africa and Zimbabwe (Corkin & Burke 2008). The visit to Africa of Chinese Premier Zhoi En-lai in 1963/64 marked an important point in the articulation of principles for China's engagement in Africa, which underpin friendly relations between Africa and China to this day: to promote friendship and sincerity; to respect the principles of sovereignty and non-intervention; to promote development on the basis of equality and mutual benefit; to establish norms of solidarity and consultation in international affairs; and to co-operate in the creation of a more peaceful, stable and prosperous world.

The death of Mao Zedong marked a period of reduced engagement with Africa. However, in the early 1990s, the PRC resumed its assistance to Africa through projects administered by the Chinese Ministry of Foreign Relations and Trade (Corkin & Burke 2008). The Forum for China-Africa Co-operation (FOCAC) was initiated in 2000, soon after China's adoption of its New Africa Policy, and remains a key locus of discussions on mutual economic benefit, development assistance, political dialogue and international co-operation.

Between 1999 and 2007, trade between China and Africa increased more than tenfold from US$6.5 billion to about US$73.5 billion. Development aid assistance in 2006 was estimated at US$5.7 billion, and by 2004 Chinese companies had invested more than US$1 billion in Africa (Le Pere 2008). The latest Chinese policy tool in its engagement with Africa is the extension of unilateral trade preferences to Africa's least developed countries.

China and investment in public infrastructure in Africa

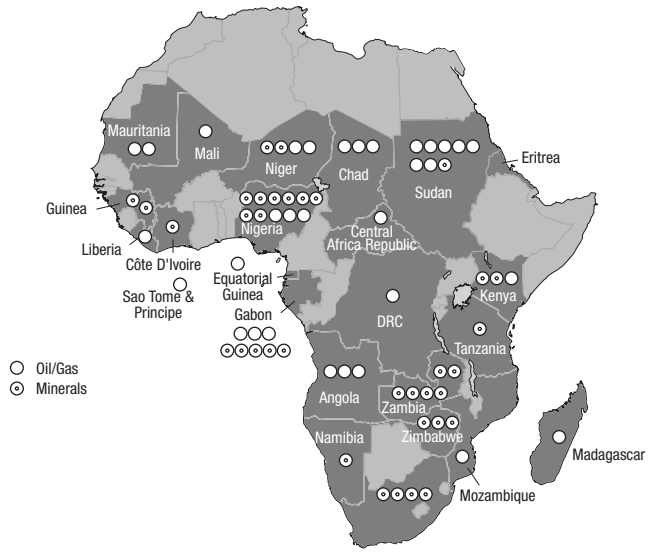
Chinese state-owned enterprises (SOEs) are active in the construction industry in almost every African country. The contracts undertaken can be categorised as follows:

- projects funded through Chinese government loans or financing aid;
- projects funded by loans from multilateral institutions such as the World Bank or the African Development Bank;
- projects obtained through governmental bilateral trade agreements;
- projects won through international bidding;
- projects obtained through local clients; and
- projects obtained through local branch offices of Chinese enterprises. (CCS 2006)

Between 1985 and 2003, the activity of Chinese enterprises worldwide increased from 143 enterprises operating in 45 countries on contracts worth US$170 million to 7 400 enterprises operating in 160 countries on contracts worth US$33.2 billion. The expansion was fuelled by support provided by the Ministry of Foreign Economic Relations and Trade, which became a legal entity in 1990, with capital to assist Chinese enterprises (CCS 2006). Chinese state-owned construction companies were at the forefront of this expansion.

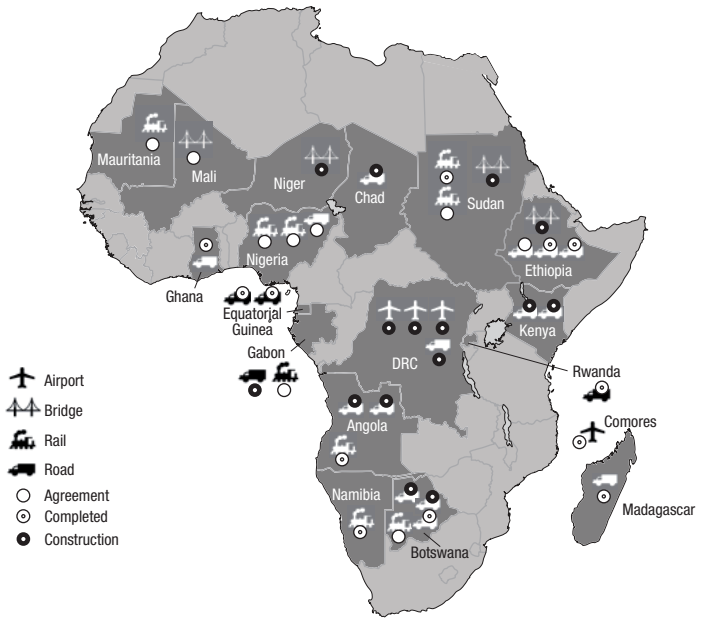
In Africa, China's focus is geared towards resource-rich counties such as Angola, Nigeria, Sudan, the Democratic Republic of Congo, Gabon and Zambia (CCS 2006). Figure 5.3.4 shows the export of natural resources (oil and minerals) to China between 2001 and 2008, while Figures 5.3.5, 5.3.6 and 5.5.7 show the spread across Africa of different types of infrastructure development undertaken with Chinese support. The correlation between investment in infrastructure and the export of minerals and oil is clear.

Figure 5.3.4: Export of natural resources to China, 2001–2008



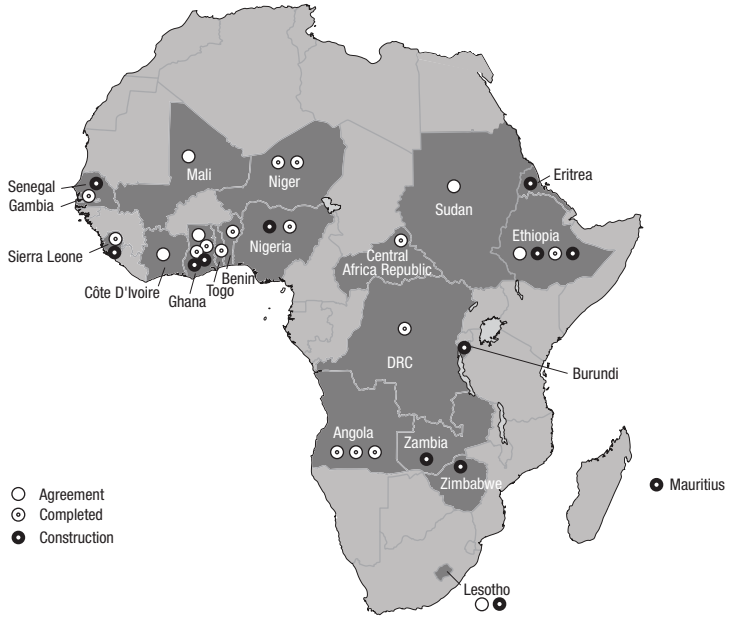
Source: Davies (2009)

Figure 5.3.5: Chinese-supported development of transport infrastructure, 2001–2008



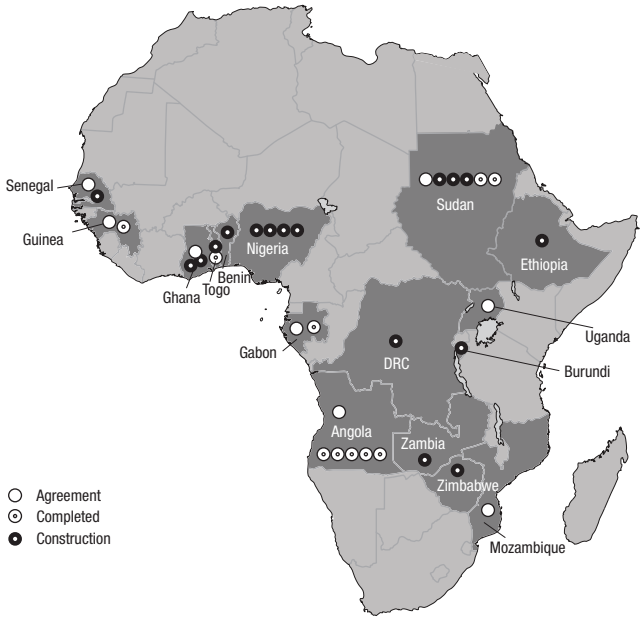
Source: Davies (2009)

Figure 5.3.6: Chinese-supported development of power infrastructure, 2001–2008



Source: Davies (2009)

Figure 5.3.7: Chinese-supported development of ICT infrastructure, 2001–2008



Source: Davies (2009)

With decades of experience in the construction of large-scale infrastructure projects and with access to liquidity, state-owned Chinese construction companies are at the forefront of the PRC's engagement with Africa (Corkin & Burke 2008: 42). The 'state capital' approach to engagement, which includes a long-term view of commercial engagement, allows Chinese companies to compete with traditional players in the construction industry in Africa. Risk is quantified in a different manner, allowing companies to invest in large-scale projects with returns that emerge in the long term, rather than seeking profits over the short term. In addition to the coupling of China's investment in infrastructure and the export of natural resources, the entry of Chinese SOEs into the local construction market spearheads Chinese investment and involvement in the local and neighbouring economies and allows market access for Chinese manufactured goods (Corkin & Burke 2008).

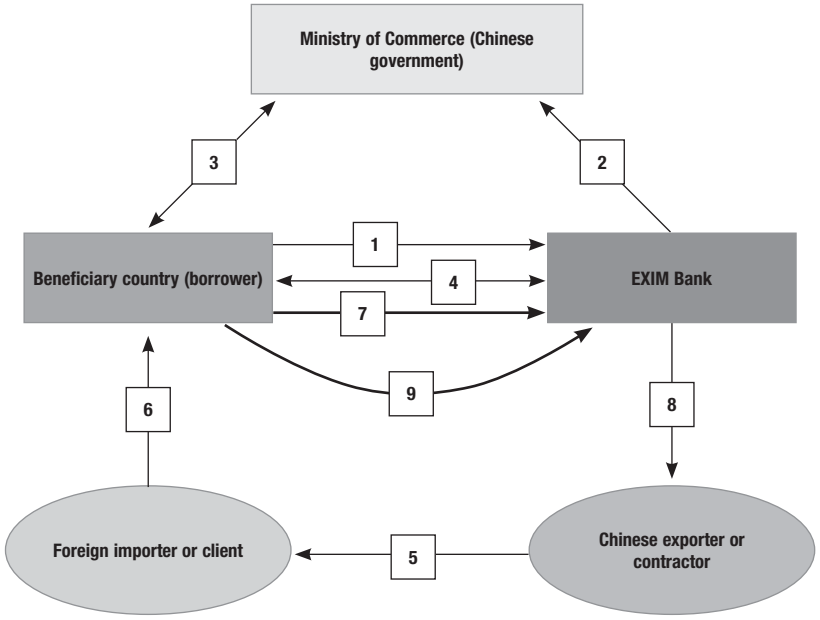
An important instrument in the entry of Chinese construction SOEs into the African market is the Chinese Export Import Bank (EXIM Bank). The bank was established in 1994 as a government policy bank reporting to the State Council. It provides finance to projects that are aligned with China's strategic interests in Africa: in practice, it is the project finance arm of the PRC government (Davies 2009). It provides loans for the export of Chinese products (export buyer's credits) and for investment and

construction projects in foreign countries that are undertaken by Chinese companies. It also provides concessional loans to China's partner governments. This is a key policy instrument facilitating Chinese companies' entry into Africa, as the bank requires that all contractors and exporters linked to a project funded by the bank should be Chinese, and that at least 50% of all procurement should be from China. The Chinese government identifies the Chinese construction companies that are eligible to compete for EXIM Bank business through a competitive process in China: when a loan is agreed, the Chinese government provides quotes for a project on the basis of a pre-approved list from which the borrowing country chooses the successful bidder. To date, this process has been dominated by SOEs, although the size and capacity of privately owned companies is growing rapidly (Corkin & Burke 2008).

According to Li Ruogu (in Davies 2009), up to 40% of EXIM Bank's entire loan book is in Africa, and approximately 80% of the African loans finance infrastructure projects.

Concessional loans from China's EXIM Bank are disbursed in accordance with a standard operating procedure, which means that the funds do not leave China. A typical process is illustrated in Figure 5.3.8.

Figure 5.3.8: Concessional loan process



Source: Davies (2009)

The process, thus, is as follows:

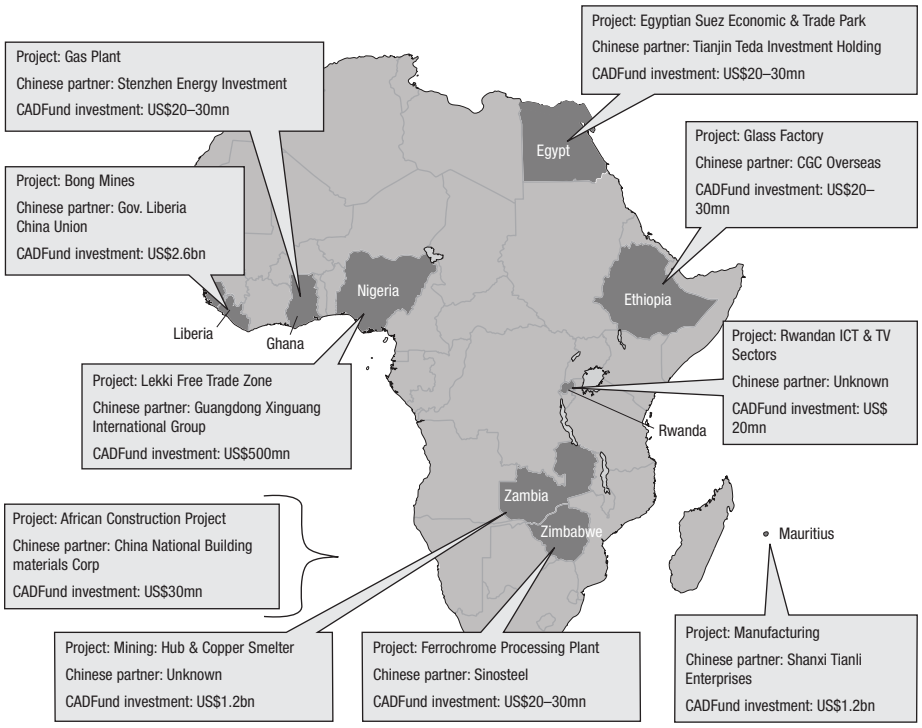
1. the government of the borrowing country (represented by its finance ministry) submits an application to the EXIM Bank for no less than RMB20 million (US$2.4 million);
2. the bank conducts an evaluation in the form of a feasibility assessment, and submits a recommendation to the Ministry of Commerce;
3. the PRC government signs a framework agreement with the borrowing country;
4. a minister of the borrowing country signs a project loan agreement with the EXIM Bank president or vice-president (the loan interest rate and grace period are negotiated separately, with repayment due semi-annually following loan negotiations);
5. according to the terms of the contract, the Chinese contractors and exporters invoice the foreign executing agency requesting payment;
6. the foreign executing agency submits the invoice and progress report to the government of the borrowing country;
7. the government of the borrowing country submits a drawing application, invoice and progress report to the EXIM Bank;
8. the EXIM Bank then disburses the funds to the exporter; and
9. the government of the borrowing country pays the principal debt, interest, fees and loan repayments to the EXIM Bank.

In addition to securing preferential access to large infrastructure projects through EXIM Bank financing, Chinese companies are advantaged by their access to cheap capital from other Chinese banks to finance the start-up phase of large projects. In bids other than on EXIM Bank projects, Chinese companies often can offer not only their experience in undertaking large projects but also cost-effectiveness, supported by their access to good-quality, low-cost skilled labour, low-cost professional services and low-cost materials imported from China (CCS 2006).

More recently, the introduction of the China-Africa Development Fund has provided another instrument for the engagement between China and Africa. The fund, announced at the 2006 meeting of FOCAC, was established in June 2007. Its capitalisation at the time was US$5 billion, provided by the China Development Bank. The purpose of the fund is to encourage Chinese companies to invest in Africa. It has a focus on agricultural projects, power projects and the establishment of industrial parks. It capitalises investments by Chinese companies of between US$5 million and

US$50 million for a period of between five and eight years. In April 2009, 20 projects were earmarked for investment with a total value of US$400 million.

Figure 5.3.9: China-Africa Development Fund projects, April 2009

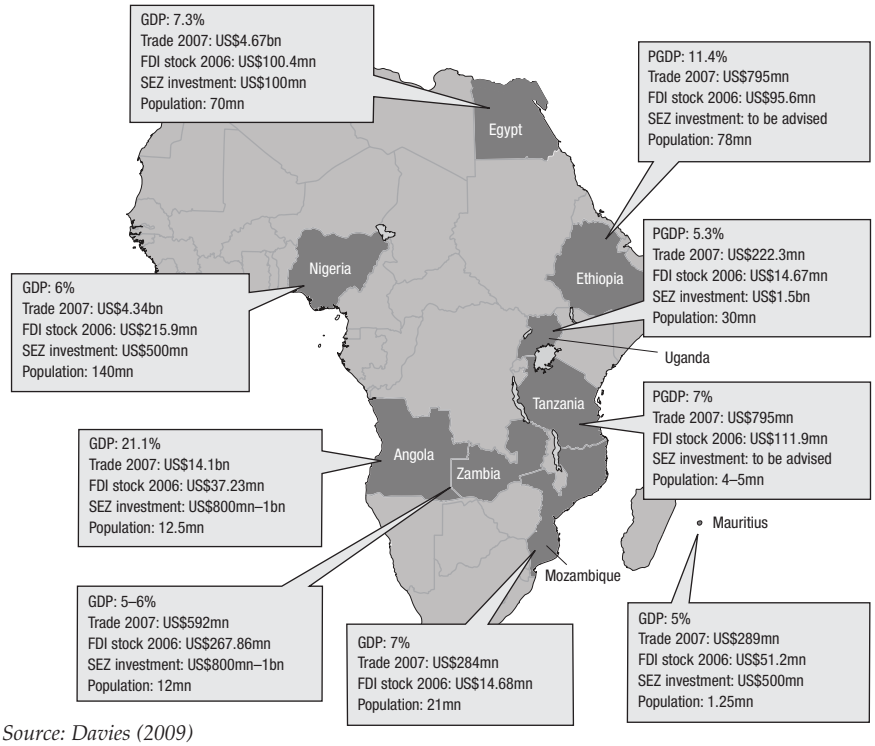


In some cases, the provision of Chinese support for infrastructure investment in Africa accompanies agreements on the export of key natural resources to China, resulting in criticism of China's role on the continent. In Angola, for example, the provision of a US$2 billion loan to the Angolan government, which was later extended to US$4.5 billion when Angola could not secure funds from institutions such as the World Bank, went hand in hand with guarantees on the export of oil to China (CSS 2006).

An additional instrument in China's engagement with Africa is the establishment of Chinese Special Economic Zones (SEZs). A SEZ is intended to form a hub for Chinese companies investing in African states. In mid-2008, the PRC approached various African states to set up SEZs. Preferential investment and trade conditions (for example, exemption from tax and labour market restrictions that apply to other foreign and local companies) are negotiated by the Chinese government for companies setting up in a SEZ. In turn, the country becomes a focal point for Chinese foreign

direct investment and Chinese-spurred economic growth. Figure 5.3.10 provides a picture of SEZ activity in Africa.

Figure 5.3.10: Chinese SEZ investment in Africa, April 2009



Source: Davies (2009)

Benefits to Africa of Chinese engagement

China is an increasingly important player in the financing and construction of public infrastructure in Africa. Its role in Africa is fiercely debated, on the continent and internationally. There are accusations that it is a 'new imperial power' on the continent, that it has a colonial agenda and that, in its own national interest, it will slow down or derail Africa's development through the ruthless exploitation, extraction and destruction of the continent's natural resources and industrial base (Naidu 2008). Alternative views emphasise China's policy commitment to mutual development and note the potential benefit of engagement with China for Africa in achieving its potential.

These debates apply to China's involvement in public infrastructure development in Africa. There are concerns that Chinese companies – whose entry into the African markets is facilitated by the various kinds of direct and indirect support provided by the Chinese government – are contributing to the atrophy of African industry (Corkin & Burke 2008), that the coupling of the financing of infrastructure with the export of minerals is destructive of countries' long-term potential, particularly countries with poor governance, and that the contribution of Chinese-financed infrastructure projects to economic growth and job-creation in African countries is severely limited because of the requirement of using Chinese companies and procuring materials from China.

However, there are also benefits. The projects and services that Chinese companies offer are often significantly less expensive than those of traditional project bidders, allowing cheaper access to infrastructure, which is essential for economic growth (Corkin & Burke 2008). Also, the competitive landscape is changing rapidly, not only in relation to the cost of infrastructure development, but also in the area of development aid. While alternative access to Chinese financing undermines efforts by traditional donors to improve countries' governance records, the entry of China as a donor to Africa also has the potential to provide a new aid-engagement model for Africa, shifting the power relations associated with the delivery of aid. Also, in the current economic downturn, the closer trade relations between China and African countries can be counter-cyclical, through (amongst other considerations) a potential increase in financial flows due to the policy-oriented nature of the Chinese banking sector.

Nevertheless, these benefits are conditional on African governments developing their institutional regulatory frameworks and capacity to monitor and encourage the transfer of technology and skills to African economies. A key difference inherent in China's engagement with Africa, compared to traditional development partners, is that China needs Africa in ways that traditional development partners do not. This should enable African governments to negotiate improved terms and conditions for Chinese involvement in the development of public infrastructure. At the same time, there is a need for greater regional co-ordination of infrastructure spending and Chinese financing. The PRC is involved in a long-term strategic engagement with Africa, a situation that African governments should exploit.

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5.4 Planning and managing capital projects in Africa: Sierra Leone's experience with the People's Republic of China and the African Development Bank

Tasima A Jah and Abdul Rahman Conteh

This paper presents a perspective on how the planning and managing of capital projects in Sierra Leone is carried out by bilateral and multilateral development partners, with particular reference to Chinese and African Development Bank projects.[1] It is a response to a request by CABRI to present a perspective on Sierra Leone's experience in this regard at the CABRI Annual Seminar in Dakar, Senegal, in April 2009. It discusses issues around the planning, financing and managing of

1 The paper reflects the personal view of the authors.

portfolios, as well as factors that influence the effective implementation of projects under the overall public investment received from these two development partners.

Post-war development strategy and relationships with development partners

Over the last seven years, the Sierra Leone government has deemed it necesary to prepare various national policy strategy documents geared towards driving the economy forward in resuscitating the devastated infrastructure and other engines of the economy that were destroyed as a result of the 12-year rebel war. The first policy document prepared immediately after the war was the Interim Poverty Reduction Strategy Paper (IPRSP). This emergency strategy to kick-start the economy was implemented within two years, between 2002 and 2005. After successful implementation of this strategy, a full Poverty Reduction Strategy Paper (PRSP) was prepared in 2005. The broad thrust of these two papers centred on four pillars, namely: good governance, social and human resources development, agriculture, and youth empowerment.

The million-dollar question that many citizens asked at that time was: How is the government going to address all of these pillars of the PRSP? However, it emerged clearly that tackling these challenges would result in heavy dependency on various development partners (bilateral or multilateral). Bilateral partners include the People's Republic of China, the United Kingdom, the United States of America, Nigeria and Libya, while multilateral partners include the World Bank, the African Development Bank, the Islamic Development Bank and the European Commission, to name but few.

The essence of such a move was to generate sufficient funds to support the government's development strategies within the four pillars and to resuscitate the economy.

Types of development partner support

Sierra Leone receives support from development partners as follows:

- *direct budget support* – this finances activities within the national budget and is channelled through the Government Treasury Account;
- *programme/project support* – this finances specific programmes or projects, either within or outside the budget;
- *technical assistance* – this provides human capital in disciplines that are not fully occupied by nationals or that require special technical skills; and

- *direct aid support* – this is in the form of goods that are provided and sold at cost, and which are used for agreed developmental activities.

The above forms of support are either tied or untied. Tied support refers to support geared towards specific activities that the donor and the government agree upon, while untied support is discretionary.

Overview and analysis of the People's Republic of China's support to Sierra Leone

Sierra Leone and the People's Republic of China established formal diplomatic relations in 1971, which was followed by the signing of a broad-based Economic and Technical Co-operation Agreement (ETCA). Within the ETCA framework, China gives grants and interest-free and concessional loans to Sierra Leone for economic, social and infrastructural development programmes and projects. Currently, most of the support received from China is by way of grants, with few interest-free and concessional loans of late. Through their relevant ministries and departments, the two governments identify development projects, which are then considered by the appropriate authorities.

When the programmes or projects are approved by the two governments, the Chinese government (in accordance with its annual foreign aid budget policy) provides the funding. China's support has been focused mainly on infrastructural developments, particularly the construction of buildings and the supply of agricultural inputs. Public investments financed by China prior to the war include the construction of the National Stadium and Hotel, a multi-purpose office building (the Youyi Building), the development of agricultural demonstration fields, and short- and long-term training in various disciplines such a medicine and agriculture.

Some of the post-war projects agreed with China in the spirit of economic recovery (as stated in the PRSP) are:

- a feasibility study on power supply shortages in Freetown and the development of a medium- and long-term Electric Power Development Plan;
- the rehabilitation and design of the expansion of the Parliament building;
- a survey on two small hydroelectric power stations;
- agriculture projects; and
- rehabilitation of public buildings that were destroyed during the war.

Table 5.4.1: Analysis of China's support to Sierra Leone, 2004–2008

Type of support	Total support			Percentage of total support
	RMB	US$	Le (mil.)	
Grant	148 490 000	22 498 485	67 495	42.6
Non-interest loan	70 000 000	43 465 758	107 670	20.1
Concessional loan	130 000 000	19 696 970	13 636	37.3
Total	348 490 000	85 661 212	188 802	100.0

Source: Ministry of Foreign Affairs and International Co-operation, Sierra Leone
Note: The concessional loan was provided for the SERATEL Company

Table 5.4.1 shows estimates of the People's Republic of China's total support to the Republic of Sierra Leone from 2004 to 2008. It is clear that China's support has been largely in the form of grants (accounting for 42.6%), followed by concessional loans (37.3%) and non-interest loans (20.1%).

Further analysis of grant support in line with pillars of the PRSP shows that health and sanitation, which fall within the human resources development pillar, accounts for the largest share of the total grants received from China. This is followed by the governance sector (the first pillar of the PRSP), since governance issues were one of the main factors that led to the outbreak of war.

Even though the agricultural sector has been of high priority to the Sierra Leone government, Chinese grants to this sector accounted for about RMB13 900 000, while the energy and power sector recorded the least grant funding, since only feasibility studies were embarked upon for mini-hydroelectric projects in the country. This allocation is shown in Table 5.4.2.

Table 5.4.2: China's grants for capital investment in Sierra Leone by sector, 2004–2008

Sector	Amount			Percentage share
	RMB	US$	Le (mil.)	
Governance	35 890 000	5 437 879	16 314	24%
Energy & power	1 900 000	287 879	864	1%
Agriculture	13 900 000	2 106 061	6 318	9%
Health & sanitation	78 850 000	11 946 970	35 841	53%
Entertainment	17 950 000	2 719 697	8 159	12%
Total	148 490 000	22 498 485	67 495	100%

Source: Ministry of Foreign Affairs and International Co-operation, Sierra Leone

Disbursement and management of China's support

The disbursement and management of Chinese financial support to Sierra Leone appears very complex to analyse, simply because the support, whether grants or loans, is calculated in the local Chinese currency, which is 'non-convertible'. Furthermore, funds for the various projects, once agreed upon by the two countries, are provided under the ETCA (as gratuitous assistance).

The funds are disbursed into a pool-like account managed by Chinese authorities in China, the Chinese Embassy in Sierra Leone and Sierra Leonean authorities. All grants or loans are made available through this account, and payments for all projects are effected upon request for the buying of goods and services for a particular project through this single account. The costs or values of goods and services are computed in RMB, the only currency in which payments are made, and charged against the particular project's loan or grant. It must be emphasised that only Chinese companies are qualified to compete for all international bidding, and such bids are conducted solely by the Chinese government.

Requirements on the part of the government of Sierra Leone

Chinese support, like much other bilateral support to Sierra Leone, requires government input or responsibility. In the case of the Chinese support, the government of Sierra Leone is required to provide the following for infrastructure projects:

- land with access to water, electricity and telecommunications connections;
- relocation of all residents from the proposed project site;
- duty waiver for all customs charges, taxes, tariffs and duties that would be required by law;
- technical team assistance in the execution of the project by the dispatch of representatives to the site;
- funds, where needed, to purchase local materials such as cement, blocks, tiles, sand, wood and stone;
- technical support in processing all customs clearance, loading and unloading, transportation from quay to site and storage of materials and imported personal belongings and security for project staff; and
- facilitation of all the entry and exit formalities for Chinese experts, among others.

Planning and budgeting implications for Chinese support

As is the case with many other African countries, Sierra Leone encounters some problems regarding bilateral donors' support in investment planning and budgeting.

In the case of Chinese support to Sierra Leone, some of the problems encountered in national planning and budgeting are:

- *lack of adequate information* to include in the formulation of budget estimates, due to sectoral negotiations with little or no involvement of the Ministry of Finance and Economic Development;
- *off-budget operations,* resulting from the fact that grants and loans are channelled and managed outside the consolidated revenue funds by the Chinese government and Chinese Embassy;
- *extra-budgetary requests* at the time of project implementation, resulting from not monetising the Sierra Leone government's responsibilities at the time of conceptualising the project or signing the agreement;
- *loss in domestic revenue* through 100% customs and other tax waivers (also, the employment of technical experts only from China through hiring Chinese companies and providing work permits and income tax concessions);
- *high capital flight*, resulting from the transfer of a large proportion of the Chinese experts' salaries directly to China;
- *reporting problems* arising from the payment for various projects from one pool-like account (this causes many problems in reporting on project execution, as some projects that are executed at a high speed utilise a large proportion of the total funds, leaving the others unimplemented); and
- *relocation costs* of residents at the proposed project sites, which exerts pressure on the budget, especially when compensation requests are considered at the time of budget preparation.

Overview and analysis of the African Development Bank's support to Sierra Leone

The African Development Bank (ADB) commenced its lending operations with Sierra Leone in 1969. The bank's total commitment to Sierra Leone as of February 2007 stood at UA268.25 million for 43 operations. As a post-war country, Sierra Leone gained support from the ADB on the basis of a Country Strategy Paper (CSP) prepared by the bank after wide-ranging consultation with government officials and consideration of national policy papers like the PRSP and sectoral plans to provide national policy guidance. In addition, international policy frameworks such as the Millennium Development Goals (among other donor policy documents) provide guidance in preparing the CSP to avoid duplication of effort and resource allocation.

The most recent CSP for Sierra Leone was approved in July 2005 to cover the period 2005–2009, and aims at assisting in the country's transition from a nation focused primarily on post-conflict emergency needs to a nation poised for long-term sustainable growth and development. The goals and objectives of the CSP were operationalised through three of the PRSP pillars: the promotion of economic growth by improving governance, human resources development, and agriculture.

At the end of 2007, the ADB portfolio for Sierra Leone contained 15 ongoing interventions, with total commitments amounting to UA118.56 million (US$78.95 million), of which UA67.84 million remained undisbursed. The portfolio is diverse in terms of sectoral allocations and lending instruments. This can be seen in Table 5.4.3, with current lending activities concentrated mainly in the social sector (48.5%), agriculture (22.4%), multi-sector (11.4%) and energy and water (11.2%). The finance/governance sector, as computed in Table 5.4.3, reflects 6.5%.

Table 5.4.3: Analysis of ADB support to Sierra Leone by sector, 2007

Sector	Amount			Percentage of total
	UA (mil.)	US$ (mil.)	Le (mil.)	%
Social sector	57.55	38.37	115 110.00	48.54
Agriculture	26.50	17.67	53 010.00	22.36
Multi-sector	13.49	8.99	26 970.00	11.37
Energy & power	13.29	8.86	26 580.00	11.21
Economic/finance	7.72	5.15	15 450.00	6.52
Total	118.55	78.95	37 120.00	100.00

Source: Various policy documents on DDB support to Sierra Leone
Note: Exchange rate: UA1.00 : US$1.50; SLLe3 000.00 : US$1.00

Disbursement and management of ADB support

After the CSP, the ADB looks at the sectors earmarked for intervention and prepares various sector project papers/proposals in accordance with the available grant or loan funds. When the projects/proposals are technically accepted by the two parties, they are submitted to the ADB board for approval, and the loan or grant agreements (LGAs) are prepared by the ADB's legal department for the consent of the government of Sierra Leone. The Law Officer's Department of Sierra Leone, in turn, reviews the LGAs and advises the executive and Parliament by way of the Ministry of Finance and Economic Development. Then, the LGAs are then signed by the Sierra Leone government representative (preferably the Minister of Finance and Economic Development) and the ADB's representative (preferably the President).

The funds for either grants or loans are disbursed into two separate project accounts (the ADB Account and the government of Sierra Leone Counterpart Account), which are managed by the project management team on a consultancy basis but with involvement of Sierra Leone authorities. All biddings for goods, services and works are done by the project management team within the ADB's procurement rules and regulations and the national public procurement law and regulations of Sierra Leone. Contracts are awarded only after receiving no objection from the ADB on the overall procurement process.

In the past, all international contracts were restricted to companies or firms operating within the ADB's member states; but according to recent developments in the ADB, non-member state companies are now allowed to compete for contracts. Payments to international or local contractors for goods, works or services delivered are initiated by the management unit within the implementing ministry through the Ministry of Finance and Economic Planning for onward submission of withdrawer forms to the ADB. As in most other countries, there are four authorised signatories.[2] Category A signatories (the Financial Secretary and Accountant General) are preferred; when they are out of office, the designated alternates (Category B signatories) can sign. It is upon the submission of these documents to the ADB that payment is effected for any contract performed.

Unlike the Chinese payment procedure, ADB currency is convertible to any internationally accepted currency in which contracts are awarded. Payments for all international contracts are made directly to the respective contractors after delivery of the goods and services or after completion of a specified level of work in accordance with the contract. These payments are effected upon submission of all verified supporting documents, along with forms processed at the Ministry of Finance and Economic Development.

Requirements on the part of the government of Sierra Leone

Similar to the arrangements for Chinese-supported projects, the ADB projects require the government of Sierra Leone to commit to certain obligations before any project is approved by the ADB board or the first tranche of funds is disbursed.

2 Category A (two signatories) and Category B (two signatories).

In the case of infrastructural projects, the following, among others, are required on the part of the government of Sierra Leone:

- provision of project counterpart funds of a certain percentage of the total project costs funded by the bank (ranging from 1% and 15%);
- parliamentary approval of project agreements;
- establishment of project implementation units (PIUs);
- recruitment of the PUI or project management staff; and
- opening of project accounts and submission of details of account signatories to the bank.

Planning and budgeting implications of ADB support for infrastructure projects

As with bilateral donor support for public investment in Sierra Leone, multilateral donor investment support has created national planning and budgeting problems over the years. These problems include the following:

- *Provision of counterpart funds* is a serious problem or constraint in national planning and budgeting in Sierra Leone. The national budget is currently about 40% donor-supported. Statutory payments (salaries, interest payments and so forth) account for over 65% of domestic revenue. Combined, these two factors result in high constraints on providing for recurrent services and development counterpart funds.
- *Delays in project implementation* adversely affect planning and budgeting, especially when some projects take over six months to become effective, with the consequence that funds provided for either the first year or the previous year lapse.
- *Exchange rate variation* causes costing problems in planning and budgeting. The projects are budgeted in ADB units of account (UA), which are convertible. However, since the Sierra Leone budget is prepared in a medium-term expenditure framework (MTEF), the exchange rate variation from the time of preparing the planning and budgeting to the time of effecting payments causes some problems in fiscal reporting. Sometimes, local contractors who are paid in local currency but who submitted bids in foreign currencies invoice the additional cost due to exchange rate fluctuations. The change in costing could result from either appreciation or depreciation of the currency, but both distort the budget execution process, especially in medium- to long-term infrastructure projects.

- *Extension of projects*, because of delayed implementation or the project being suspended by the bank for some administrative lapse, affects planning and budgeting, as new projects cannot be accommodated within the limited available resources (for example, the Bumbuna Hydro Project started in the early 1970s and it is only in late 2009 that this project is expected to be completed).
- *The issue of multi-sector projects* results in various sectors requesting counterpart funds for a particular project simply because a component thereof is being implemented by that particular ministry, department of agency. This exerts unnecessary pressure on planning and budgeting to provide funds for the three or more ministries that are implementing a particular project.
- *Extra-budgetary requests* at the time of project implementation, resulting from not monetising the obligations of the government of Sierra Leone at the time of conceptualising the project or signing the agreement, cause serious problem in budget execution when the project starts.
- *Domestic revenue loss* through the hiring of international consultants, who are exempted from paying taxes, to provide services within the PIU. Domestic revenue loss also results from payment to international contractors who deliver goods and services. In most cases, they argue that they should not pay taxes of any nature.
- *Foreign exchange constraints* result from the transfer of a large proportion of the salaries on a project to expatriates or consultants directly to their home countries. This constrains the foreign reserves that are needed to service external transactions such as transfers to foreign missions of the government of Sierra Leone.
- *Subcontracting of procurement management to non-governmental institutions* (such as agencies of the United Nations) also results in high project administration costs and loss of revenue, since most of these agencies are tax-exempt for all activities in Sierra Leone.[3]
- *The Cabinet and Parliament* are not given adequate time to review and debate the merits of project proposals and agreements against budgetary implications within the MTEF framework. The technocrats in line ministries play a critical role in decision-making for the projects, while Parliament only ratifies agreements.

3 In most cases, 10% administration costs are charged on projects budgeted by these and other agencies.

Conclusion and the way forward

It is evident from the above analysis that the identification of projects by multilateral donors (such as the ADB) represents a more policy-based approach than that of some bilateral donors, simply because the multilaterals engage in more consultation with policy advisers than do bilateral donors. In the case of Chinese support to Sierra Leone, the Chinese authorities usually consult with the Sierra Leone political authorities to determine the needs for intervention. In the case of the ADB, however, broader consultation takes place with technocrats, and existing policy documents play a role in determining intervention before political consultation. Hence, bilateral support is more prone to be politically driven, while multilateral institutions focus more on issues that affect the poor.

Multilateral support is easier to manage than some bilateral support; there are difficulties in the management a pool account intended for a series of projects rather than different accounts for various projects. Also, data on multilateral projects are captured easily for the overall national budget, since these funds are disbursed in consultation with the Ministry of Finance and Economic Development. This is the case for the ADB and other donors like the World Bank and the Islamic Development Bank. In the case of the Chinese government's support, disbursements and fund management are executed directly from China, and this causes many problems in capturing data on such projects for budget analysis.

However, bilateral funds for public investment are disbursed easily, since the processing of financial documentation is done by the donors themselves, as in the case of China. Disbursement of funds for multilateral-funded projects is less timely as a result of delays in processing and approving government of Sierra Leone documentation. Hence, projects are likely to suffer delays beyond the initial estimated time.

This paper points to several reasons why African countries, including the Republic of Sierra Leone, need to review the terms and conditions under which all infrastructural project agreements are signed, to take account of all the planning and budgetary implications highlighted in this article. Development partners should make greater efforts to reduce the burden on recipient governments by including most of the requirements in overall project proposals, which would allow for fiscal space in executing nationally driven programmes and projects. African countries should improve their *ex-post* evaluation of projects funded by donors, in order to learn the necessary lessons and to improve planning for new projects. Finally, a major shortcoming of donor support management in Africa is the sidelining of parliaments. Legislators should be given ample time to review project proposals and loan or grant

agreements before approval. As the representatives of the electorate, the ultimate beneficiaries, they should be involved at the project inception stage, with constant consultation throughout the formulation of a particular project.

6

Performance budgeting: A case study of Korea

6.1 Introduction

Many CABRI countries are putting in place programme performance budgeting systems. These can involve the formal allocation of funds to outputs and the formal review of performance against projections, or may refer merely to the allocation of funds against a programme budget structure coupled with the use of performance information in decision-making and reporting. In both cases, the move to performance budgeting is strengthened by a clear vision of what is required to ensure effective performance budgeting and of how non-financial performance information is to be collected, managed and used in the budgeting system.

Korea recently implemented programme performance budgeting reforms. Together, the two papers in this chapter provide an overview of the reforms and the institutional arrangements through which performance information is used in budgeting in Korea. The first paper, by John M Kim and Nowook Park (previously published in the *OECD Journal on Budgeting*) provides the context of the reforms and an overview of the Korean approach, and discusses the challenges that emerged. The second paper is a short note compiled by the CABRI Secretariat based on the presentation on the Korean reforms provided at the 5th Annual Seminar by Youngsun Koh from the Korea Development Institute. The note complements the main paper insofar as it provides detail on the institutional arrangements followed in the Korean process.

6.2 Performance budgeting in Korea[1]

John M Kim and Nowook Park

Korea recently launched a reform to introduce performance-based budgeting into government. What makes the Korean case particularly interesting is the speed with which the government has ushered in a performance management system, and the fact that other budgetary reforms of similar magnitude are being pursued concurrently with equal zeal as part of a comprehensive fiscal reform package known as the Four Major Fiscal Reforms.

One advantage of such a multi-pronged effort is that, if co-ordinated properly, it ensures that an exceptionally favourable background is set for building up an effective performance management system. The downside to such an approach is that it demands a level of commitment in terms of both political willpower and material resources that may not be feasible in many countries.

1 This paper providing the background to performance budgeting reforms in Korea first appeared as Kim JM and Park N (2007) Performance budgeting in Korea, *OECD Journal on Budgeting* 7(4). It is reproduced here with the permission of the OECD.

Background and context

The Korean government's Four Major Fiscal Reforms are designed to:

- establish a medium-term expenditure framework (the National Fiscal Management Plan);
- introduce top-down budgeting;
- establish a performance management system; and
- build a digital budget information system (which includes a transition from the existing line-item structure to a programme budget structure).

The scope and pace of this reform package are quite exceptional. If successful, the Korean budget system will be completely retooled within the space of a few years into one that incorporates virtually all of the best practices.

These ambitious reforms were motivated by the deteriorating fiscal situation of the Korean government. After the Asian financial crisis in the late 1990s, public debt increased dramatically. The growing debt was driven partly by rapid rises in public expenditures to strengthen the social safety net and thereby assuage widening income disparities resulting from the economy-wide restructuring. Looking ahead, population ageing in Korea is progressing at an unprecedented pace, generating additional pressure on public finances.

The medium-term fiscal plan puts government spending decisions in a five-year framework. Based on prudent economic growth projections, the plan determines the annual overall expenditure levels over the medium term of the 14 major sectors of government spending. Consistency between such medium-term resource allocation decisions and annual budget appropriations is enforced through the top-down system. This system assigns firm spending ceilings to line ministries according to the medium-term fiscal plan, but delegates lower-level budgeting decisions to ministries, provided that the latter's aggregate expenditures remain within their assigned ceilings. The greater autonomy given to line ministries requires, in turn, greater accountability on their part. This is ensured through the performance management system, which was introduced to examine the performance of spending programmes and, thus, strengthen the link between budgeting and performance. The digital budget information system will allow the budget office to monitor ministries' spending in real time. The task force charged with developing this information system was also tasked with overhauling the budget classification structure. Accordingly, a new programme budget and cost accounting system was developed in 2005, for full implementation by 2007.

The performance system in Korea

Performance-based budgeting was introduced in Korea in three phases. The first was an experimental pilot project carried out between 2000 and 2002. Entitled 'Performance Budgeting', the performance-based system was modelled on the USA's Government Performance and Results Act (GPRA), with some modifications. Divisions in the 22 ministries and agencies that participated in this project were asked to develop annual performance plans. This first initiative ended with the change of the incumbent administration.

Building on that experience, the second initiative began as one component of the Four Major Fiscal Reforms of 2003. Twenty-two ministries and agencies were selected and asked to submit their annual performance plans to the Ministry of Planning and Budget (MPB) along with their annual budget requests. This second initiative was also inspired by the GPRA, but implemented only a limited subset of GPRA features. While the GPRA requires each agency to submit strategic plans, annual performance plans and annual performance reports for every single programme, the Korean version requires performance plans and reports only for major budgetary programmes with a value above US$1 million. This second initiative, entitled 'Performance Management System of the Budgetary Programme', was expanded to cover 26 ministries/agencies in 2005.

A third initiative, the 'Self-Assessment of the Budgetary Programme' (SABP), was introduced in 2005. This system was based on the USA's 'Program Assessment Rating Tool' (PART), with some modifications. Under the SABP, 555 programmes (about a third of all government programmes) were reviewed in 2005, at a pace that would allow the MBP to review every major budgetary programme over a three-year cycle. Similar to PART, the self-assessments were made according to a checklist developed by the MPB that lists questions on planning, management and results.

Legal and institutional framework

The Korean performance system was implemented as an initiative of the MPB, and is not as yet defined in any law. The ministry's role has been to design performance programmes and implement them by giving directives and guidelines to line ministries/agencies on how they should adopt and operate a performance management system. However, an umbrella bill, intended to supersede the outdated Budget and Accounts Act, has been submitted to the National Assembly (the legislature). This bill includes a comprehensive, updated definition of the budget system, including performance management. Meanwhile, a new law was enacted in 2005 that gives the Office for Government Policy Co-ordination the authority

to supervise and co-ordinate the various existing performance evaluation systems within the government.

There is no legal requirement yet to present performance information in the annual budget proposal or supporting documents. Nevertheless, the MPB has provided the National Assembly with the SABP evaluation results. There are legal requirements (stipulated in the 2005 law) for line ministries/agencies to submit strategic plans, annual performance plans and performance reports to the Office for Government Policy Co-ordination. There is no legal requirement regarding programme evaluation, but a question in the SABP asks whether a particular programme is evaluated by an independent organisation, which encourages line ministries to conduct evaluation.

The MPB has been the key actor in developing and implementing performance-based budgeting in Korea. Its roles include oversight of performance budgeting programmes, issuing guidelines to line ministries/agencies, and evaluating the latter's performance information. The ministry has relied heavily on advice and assistance from the Korea Institute of Public Finance, a public think tank, which has been instrumental in developing manuals and running training programmes on performance budgeting for line ministry/agency staff. In order to get the attention of line ministries/agencies, the MPB encourages them to use performance evaluation results in preparing their budget requests. Upon receiving the budget requests, the ministry incorporates the performance information into its decisions during budget formulation.

In 2005, the MPB signalled its intention to strengthen performance budgeting further by creating a bureau that specialises in performance issues. This newly created bureau is fully in charge of both policy decisions and programme implementation in performance budgeting.

Scope and coverage

To date, performance budgeting in Korea has adopted a partial approach: it mainly covers major budgetary programmes, defined as those either with budgets over US$1 million or whose nature merits special attention (e.g. programmes over which the legislature or the National Audit Office has taken issue). More specifically, 22 out of 39 ministries/agencies have developed performance measures for 100% of their major budgetary programmes.

Performance measures have been developed for some of the other smaller programmes as well. Starting in 2006, the performance system is being expanded comprehensively, requiring performance information to be developed for every programme.

Regarding efforts by ministries/agencies to implement performance management, none has yet set up special units solely or mainly for conducting evaluations. That task usually falls to budget departments within most ministries/agencies. Overall, ministries/agencies do not have much experience with evaluations at this point. The situation is expected to improve rapidly, as the SABP encourages evaluations on a regular basis.

Measurement and assessment of results

Setting goals

Decision-makers in ministries/agencies have not been involved actively in developing strategic goals/objectives. The usual practice is for the budget department to develop them with the help of outside professionals. Nor have politicians been involved actively in setting goals, which is done on an organisational basis. Strategic plans were developed in 2006 and will be updated every three years.

Performance measures: outputs, outcomes and measurement issues

Korea's performance system is oriented toward outcomes, but outputs are used when it is difficult to define or develop appropriate outcome measures. The system started with outcome-oriented performance information, taking the USA system as the benchmark model.

Developing outcome measures is a difficult task for ministries/agencies. Since these measures are often too broad, there has been some resistance from ministries/agencies. In particular, policy-oriented ministries, whose outcomes are affected heavily by external factors, have found it very difficult to develop meaningful outcome measures. Allowances are made for such external factors in assessing performance information, but there is as yet no systematic approach to incorporating them into the evaluations.

Setting targets

Performance targets, which are included in performance plans, are set by ministries/agencies. The plans and targets, however, reflect significant input from the MPB as to whether they are appropriate. In making such judgments, the ministry uses time-series data and benchmarking against similar cases.

Following an initial self-assessment by ministries/agencies, the MPB makes the final assessment of performance. Throughout the entire process, assessments rely entirely on performance information produced by the ministries/agencies themselves.

Lacking a formal process for independent verification, the MPB tries to ensure the reliability of performance data by penalising wrong or misleading information.

Integrating performance information in the budget process

The MPB uses annual performance reports and the SABP in its negotiations with line ministries during the annual budget process. This practice has encouraged ministries/agencies to use performance information in formulating their budget requests.

The results from the 2005 SABP show a strong correlation with budget requests from ministries/agencies. This means that final budget allocation decisions by the MPB tend to favour programmes with strong performance results. Thus, it appears that the ministry's emphasis on performance assessments has resulted in a positive relationship between performance information and budget allocation.

In the Korean case, the use of performance information in budget decisions has focused on identifying possible savings in order to finance higher priority spending. Specifically, increasing expenditures for welfare programmes has required savings/freezes in other sectors, and the MPB has asked ministries/agencies to find room for new or higher priority programmes through savings and reallocations totalling up to 10% of their budgets. Ministries/agencies used performance information heavily in their budget restructuring efforts.

Budget negotiations: linkage of performance information to budgeting decisions

Performance information is discussed as part of the budget negotiations between the MPB and the spending ministries. These negotiations include discussions on a spending ministry's performance over the previous year; however, targets for the next year are not discussed. The MPB also encourages ministries to use performance information in the formulation of their budget requests, and in restructuring their budget allocations.

As a mechanism for linking performance information to resource allocation, the programme ratings produced by the SABP are used by the MPB to reduce the budgets of ineffective programmes. The budget cut announced by the MPB was 10%.

On the part of spending ministries, performance information is used to reshuffle budget allocations within ministries/agencies and to justify existing appropriations. Ministries often use performance information to obtain more money, and they find it to be an effective tool for preventing cuts by the MPB.

Disagreement between the MPB and ministries/agencies frequently occurs, and the MPB has the final authority in settling differences. In this process, past

performance information is the most frequently used rationale for performance targets. Sometimes, the performance of another comparable organisation is cited as a benchmark reference.

The budget departments of ministries/agencies use performance information in preparing their budget requests, but it is too early to tell whether the use of the information has had any significant impact on their management system.

In order to help line ministries/agencies to develop effective performance information systems and to monitor performance, the MPB offers training courses and provides manuals, with the help of its research affiliate, the Korea Institute of Public Finance. Korea's performance system has not developed to the stage where recommendations from evaluations go beyond budget allocation to programme management. The MPB plans to expand the scope of its evaluations to include such recommendations.

Incentives

The primary mechanism at the disposal of the MPB to encourage ministries/agencies to improve performance is to cut the budgets of ineffective programmes. There are also incentives targeted at individuals, such as staff performance evaluations; promotions are often affected by such evaluations.

While spending ministries often attempt to use performance results to justify the resource level of existing programmes, the MPB mainly considers these results before determining the resource level for a programme. In 2005, for example, the MPB made significant use of the SABP in resource allocation decisions.

If an agency/ministry does not meet its performance target or receives a poor evaluation, it may be penalised with a budget cut. Apart from budget cuts, there is no penalty on an organisational level; nor are there explicit penalties or incentives affecting senior civil servants directly, despite the fact that they are required to sign performance agreements. However, senior civil servants are quite aware of the likelihood that organisational performance will have an impact on their own career prospects.

Not much change has taken place regarding a reduction of input control, following the introduction of performance-based budgeting. Because top-down budgeting and performance management were introduced at the same time, in theory this should have reduced input control significantly and delegated more authority to line ministries. However, with top-down and performance budgeting barely out of the inceptive stages, the MPB still closely supervises budgeting decisions by line ministries. Overall, it is still too early to judge the pros and cons of the relaxed input

control that is being implemented as a feature of top-down budgeting, introduced only in 2005.

Thus far, there is no clear evidence of distorted behaviour resulting from perverse incentives that may arise inadvertently from the new performance system. However, it has been noted that ministries/agencies behave strategically to protect important programmes. For example, they tend to give lower ratings to less important programmes and better ratings to those that they consider important within their programme portfolio.

There is some gaming, goal distortion and presentation of misleading information. For example, ministries/agencies have been known to select performance indicators not because they are good indicators but because they improve the odds of earning a good rating. In an attempt to prevent such behaviour, the MPB issued a warning that, in the 2006 SABP, misleading information may result in a major budgetary penalty for the offending ministry. To check the accuracy of performance information, the MPB will use information from the National Audit Office and the National Assembly.

Reporting of performance information

The availability of information about performance is still somewhat limited. For example, the results of the 2005 SABP were provided to the National Assembly as separate supplementary material to the budget documents. Thus, the MPB, the ministries/agencies and the legislature do use performance information during budget formulation and deliberation.

However, such performance information is not yet available to the public. Nor are ministries' performance plans and reports made public. It is too early to tell how politicians are using performance information, because systematic information was first provided only in 2005. Although the National Audit Office produces information that, in theory, may be used to cross-check the information generated by spending ministries, there is no formal process yet for auditing performance information.

Key challenges

The problems encountered to date are predominantly of a technical nature, because Korea is still in the early stages of building a performance system. Political and cultural problems are also observed, especially when it comes to using performance information and improving the system. The limited technical capacity of ministries/agencies impedes efforts to develop useful performance information. Progress is being made through training programmes to augment technical capacity, but deficiencies in

data availability also hinder agencies from producing useful information. It appears that considerable time and effort will be needed to develop good performance measures and data. For example, the Ministry of Construction and Transportation has found it very difficult to come up with reasonable outcome measures, and, as a result, uses mostly output measures. Likewise, policy-oriented ministries are struggling to identify concrete measures/indices that can link their efforts to outcomes.

Incentives for civil servants to improve the performance management system pose another problem. While the motivation for introducing a performance system is often strong, incentives for improving an existing system may be inadequate, because the results may not be readily apparent to the public and politicians. In contrast, introducing a new performance system is usually counted as a major achievement.

Cultural challenges are also present. Early on, there was significant resistance/inertia in the civil service, which was not accustomed to being evaluated. However, recently it appears that Korean civil servants are coming to accept result-oriented performance management as a normal part of bureaucratic culture.

In addition, Korea's civil service faces institutional challenges. Civil servants rotate through different assignments on a regular basis. This practice allows them to accumulate general knowledge and skills, and also helps to circumvent opportunities for corruption. However, a clearly negative consequence is that the practice tends to work against civil servants' gaining expertise in any specialty, including performance management. Another problem is the existence of too many fragmented evaluation systems. Not counting a myriad of small systems, there are four major evaluation systems, each operated by a different ministry/agency. As a result, line ministries are voicing complaints about the redundant administrative burden these impose.

Solutions

The MPB, with the Korea Institute of Public Finance, recently set up a task force and established training programmes to address the problems mentioned above. Currently, a manual is being compiled on how to develop performance information, which should help to disseminate a standardised framework for performance evaluations.

In overcoming the initial bureaucratic resistance, the President's leadership has helped greatly in giving the necessary impetus to the introduction of the performance management system. The strong link enforced by the MPB between performance information and budget allocations has acted as an additional motivation for ministries/agencies to invest in improving the quality of their performance information. The concurrent effort by the MPB to provide workshops and training

courses for ministries/agencies has helped them to build their capacity for defining and producing meaningful performance information.

On the issue of gaming, there is no explicit mechanism for dealing with the problem. How specific instances of gaming are resolved is entirely up to the MPB and the agency budget departments.

Lessons learned and impact

At present, Korea is in the initial stages of implementing performance-based budgeting; it is, therefore, too early to form an assessment. However, it should be noted that the introduction of performance-based budgeting as one component within a broader range of comprehensive reforms has helped to lower resistance and to resolve institutional problems. At the same time, concerns have been raised that the concurrent implementation of multiple major reforms, in itself, imposes an inappropriately heavy burden on the government.

Overall, performance information has had a positive impact on the budgeting process. It is too early to determine the impact of performance information on ministry/agency performance.

Despite Korea's meagre experience time-wise in introducing performance budgeting, some general lessons can be drawn. Reorganisation of ministries/agencies and the budget structure needs to be done before introducing the performance system. In Korea, performance information is focused on individual programmes/projects, but cost information is not readily available, because organisational units, programmes and the budget structure need to be realigned so that they are consistent with each other. As a result, it has been extremely difficult to develop meaningful outcome measures and efficiency/effectiveness measures.

Korea's short experience has shown also that, in introducing the performance system, decision-makers should be patient about reaping any benefits. There is a concern that decision-makers in Korea may be more interested in introducing the performance system than in monitoring or improving it. If a particular country is accustomed to getting quick returns from the reforms, it will not be easy to develop and improve the system.

The political and administrative culture of Korea poses some idiosyncratic challenges that other countries hopefully need not consider. Regular rotation of assignments in the civil service may work against the capacity development of ministries/agencies. Lack of patience on the part of decision-makers may force the MPB to take ill-advised or excessive measures in order to show quick results. It was

partly because of this kind of pressure that the MPB felt forced to quickly implement a 10% budget cut for ineffective programmes.

Korea's experience confirms that a performance system evolves over time and raises different challenges at each stage. At the initial stage, merely developing relevant information is the main challenge. As the performance system evolves, other changes become more important, namely behavioural change, such as how to get various actors to use performance information in the decision-making process, and how to monitor the performance of the performance system itself.

The lessons from the Korean experience can be summed up as follows: make sure the infrastructure is ready for the reforms. Proper cost accounting and a solid programme budget structure will help greatly to maximise the benefits of the performance system. There should be proper understanding of performance-based budgeting among civil servants; otherwise, wasteful and distorting behaviour may proliferate.

Looking forward, the major ongoing problem for Korea is the quality of performance information. More training and research is needed, along with a greater commitment to invest in collecting and organising the information. Specifically, the analytical and administrative capacities of the MPB and ministries/agencies need to improve. This may require reinforcement of units specialising in evaluation in both the MPB and ministries/agencies.

6.3 Structured approach to performance management

Youngsun Koh
Note by Alta Fölscher

The Korean government has introduced a highly structured system to systematically and consistently compare programmes across government for budgeting purposes. The detail of this system was shared with conference participants by Youngsun Koh from the Korea Development Institute. This note provides highlights from his presentation, which supplement the main paper in this chapter.

The reform context

A medium-term expenditure framework (MTEF) was introduced in Korea in 2004, with the publication of the National Fiscal Management Plan (NFMP). The rolling plan covers five years: the current year, the budget year and an additional three outer years. It comprises two parts, a section on macro fiscal policy and a section on sectoral fiscal policy, which covers the major policy directions and spending allocations for each sector. Every year, the plan is prepared by the Ministry of Strategy and Finance

(MoSF), supported by (amongst others) the Korea Development Institute (KDI, see main paper), which organises sector workshops to discuss the major policy issues. Although the plan is submitted to the National Assembly together with the draft budget, it is not a legal instrument and is used only for information purposes.

The introduction of the NFMP is underpinned by a modernised budget process, which allows for line-ministry inputs prior to formal budget preparation and the setting of spending ceilings for the purposes of the process. Figure 6.3.1 sets out the main features of the modernised budget process: whereas previously the MoSF issued the budget circular directly after undertaking macroeconomic forecasting, the ministry now sets out its main macro fiscal and sector policy directions in the NFMP, and establishes a firm ceiling for spending based on the NFMP through a Cabinet decision, before sending out the circular. There is also a prior process at line-ministry level whereby line ministries update their cost estimates as an input into drafting the NFMP.

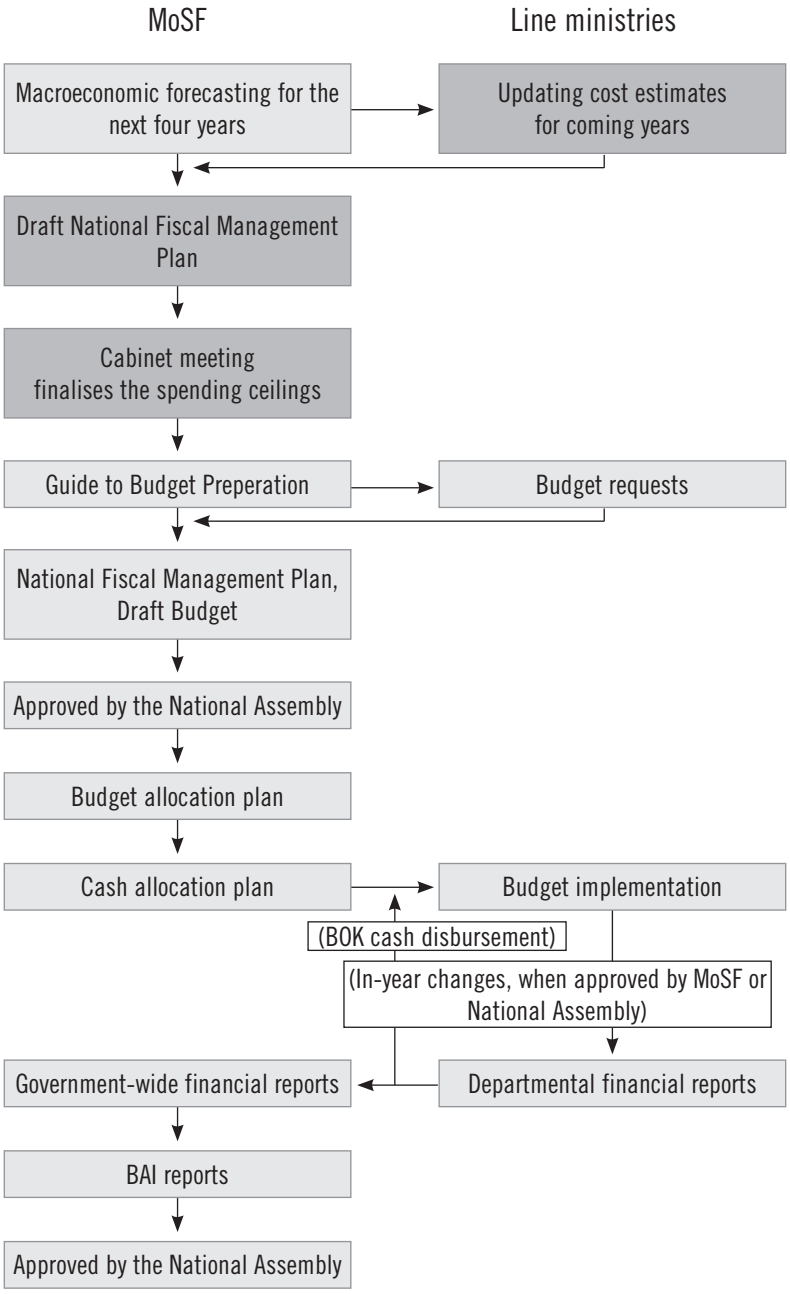
While the NFMP has played an important role as a medium for dialogue between the government and the public on medium- to long-term fiscal policy issues, it has been plagued by lack of consistency across successive NFMPs, by unclear specification of fiscal targets (it is unclear exactly how firm the spending ceiling and debt and fiscal targets are that are posed in the document) and by too optimistic macroeconomic forecasts. The latter has discredited the NFMP as an instrument somewhat, as actual economic growth is often slower than expected.

However, it has had a real impact on the quality of budgeting. The setting of spending ceilings prior to the budget process has succeeded in passing on a willingness to make trade-offs to line ministries. Whereas ministries used to request almost 40% more than the previous year's final budget, requests now are limited to an additional 15%. At the same time, there is evidence that ministries now enjoy greater autonomy in setting their spending priorities.

Performance management in Korea

The introduction of a medium-term expenditure approach to budgeting has gone hand in hand with the introduction of tools for improving expenditure performance. Korea conceptualises its approach to performance management in terms of three activities: performance monitoring, programme evaluation and programme review. Together these three activities comprise the system of performance management.

Figure 6.3.1: The modern budget process in Korea



The Performance Goal Management System

Performance monitoring measures programme performance on a continuous basis with a predetermined set of indicators. Through this system – driven by the Performance Goal Management System introduced in 2003 – spending ministries can produce information on their inputs, outputs and outcomes in a timely, routine and cost-effective way.

The Performance Goal Management System is led by the MoSF. It is based roughly on the system put in place by the Government Performance and Results Act (1993) of the federal government in the USA, but does not require strategic plans. Instead, it requires ministries to set up performance goals and indicators for all their programmes and to prepare annual performance plans and reports. These are submitted to the MoSF at the start of the annual budget cycle.

Self-assessment of budgetary programmes

However, the government has recognised that this system, by itself, rarely explains in a satisfactory manner the causal relationships between input, outputs and outcomes. To supplement performance monitoring, Korea has an established system of programme review, introduced in 2003. These reviews, which are self-assessments of programmes undertaken by ministries, use both programme performance information and outcomes of evaluations (where available, see below) in a structured way to better assess the value for money of spending programmes and to improve budget allocations.

The self-assessment process occurs at line-ministry level, but within a framework developed by the MoSF. Again, the system is modelled on USA processes, particularly the Programme Assessment Rating Tool, which is used at federal level. It requires ministries to assess their own programmes with spending levels above a certain threshold in a three-year cycle.

The assessment is based on 11 questions common to all types of programme, plus a few additional questions specific to particular types of programme. These are infrastructure investment, procurement of facilities and equipment, capital injections, subsidies to private entities, grants to local government, and research and development. The common question assessment overall is scored at 100 and uses the weighted sum of the individual question answers. If an agency scores more than 90, its performance rates as 'very good'. If it scores between 80 and 89, it is 'good', between 60 and 79 'adequate', 50 to 59 'poor' and lower than 50 'very poor'. Scores are calculated using the weighted sum of the questions. Table 6.3.1 provides the weighted score per question in brackets. For the question on the achievement of

programme objectives a four-scale option is provided, with 100%, 67%, 33% and 0% being the options. Table 6.3.1 sets out the common questions asked.

Table 6.3.1: Common questions

Design (30)	Programme design (15)	Is the programme duplicative of other programmes? (7.5)
		Is the programme design cost-effective and appropriate? (7.5)
	Performance plan (15)	Do performance indicators have a clear relationship with programme objectives? (7.5)
		Are the performance targets set at reasonable levels? (7.5)
Programme management (20)		Is the implementation being monitored regularly (5.0)
		Have the problems encountered during the implementation been solved? (5.0)
		Is the programme being implemented as planned? (5.0)
		Are efforts being made to reduce costs or increase efficiency? (5.0)
Performance assessment and feedback (50)		Has an objective and comprehensive programme evaluation been carried out? (5.0)
		Did the programme achieve the intended objectives? (40.0)
		Is the agency in charge of the programme utilising the assessment results for programme improvement and modification? (5.0)

The MoSF reviews the self-assessment results annually, and takes them into account when preparing the annual draft budgets and the NFMP. Those with poor and very poor performance will have their budget cut by at least 10% or terminated for the subsequent year. In 2007, 384 programmes were reviewed, of which 104 were classified as poor or very poor.

In-depth evaluations of budget programmes

In addition to performance monitoring and structured self-assessment of budget programmes, the government has undertaken in-depth evaluations of government programmes since 2006. These evaluations address the question of why and how the programme produced certain outputs and outcomes. It is undertaken by professionals and uses relatively sophisticated tools of data collection, investigation and analysis. Therefore, it is costly and cannot be undertaken for all government programmes. Instead, the MoSF commissions evaluation studies on programmes that it considers to be in need of critical assessment. It draws on the assistance of the KDI to undertake the studies: the KDI organises evaluation teams and oversees the processes. Since the introduction of the system in 2006, the government has evaluated about ten programmes a year.

The programme evaluations are focused on three points:

- *Programme relevance*: What are the objectives of the programme? What justifies the government intervention? Is the programme properly targeted?
- *Programme effectiveness*: Did the programme produce its intended results? Are there any side-effects – positive or negative?
- *Programme efficiency*: Is the programme implemented in an efficient way? Are there alternatives with lower costs or higher performance for the same cost?

Korea's experience

The introduction of performance tools, together with a medium-term budgeting approach, in Korea has achieved the institutionalisation of a performance-orientation in the government. Already, there is a greater interest in outputs and outcomes rather than inputs and processes, and the importance of performance management is generally accepted. However, Korea is encountering many problems common to the introduction of performance management systems, namely:

- many of the programmes have multiple objectives that are not prioritised properly;
- many programmes still lack performance indicators;
- performance information is not yet collected consistently and compiled systematically;
- many line ministries are not yet fully supportive of the efforts of the MoSF to manage the budget for performance; and
- the new system requires significant capacity of a new kind, and neither the line ministries nor the MoSF have sufficient human resources to handle performance management optimally.