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The Role of Budget Support in British Development Policy

By Matthew Sudders, Head of Bilateral Relations, Department for International Development (DFID)

The moderator, Mr. van de Sand, reminded the audience that this event belongs to a series of presentations on Budget Support (BS), organised by SID Chapter Bonn,

He pointed out the high degree of scepticism within the German development community towards this aid concept, also with regard to the current financial crisis which would lead to a need for tougher arguments concerning the financing of development policies. Furthermore, previous events on BS had shown a strong concern about its inherent risks when provided to potentially corrupt and oppressive governments in Developing Countries.

He referred to DFID as one of the most outspoken defenders of BS amongst the bilateral donors with plenty of experience in this field and admitted the floor to Mr. Sudders.

Mr Sudders started his presentation by giving an **overview of the British development cooperation system.**

DFID had been set up as a separate government department after the 1997 election of the current Labour Government. Among the structural changes which took place as a consequence of this, Mr. Sudders mentioned the fact that the former DFID Secretary of State had become a cabinet minister of equal rank as the Foreign Secretary and the Finance Minister. Furthermore, instead of just being the implementation body of development cooperation, DFID had developed to cover almost all development cooperation, insofar as the funds for multilateral institutions and the bilateral cooperation had become concentrated within DFID, which currently was managing 90% of the UK ODA.

DFID had been evolving from being an organisation which exclusively ran projects to one engaged in the provision of Budget Support. The speaker explained that as a government ministry, DFID obtained his funding from the national treasury for a period of three years. In order to monitor the allocation of these funds, the British Government had put in place the so called **Public Service Agreement (PSA)** which set out the key aims and objectives of every government department. The DFID - PSA was based on the Millennium Development Goals (MDGs) as long-term targets, and also set out another series of objectives to be reached within a period of three years in order to track progress along the way towards the MDGs. In the latest version of PSA the government had chosen to establish one single integral PSA for the whole of government instead of having different agreements per department.

Mr. Sudders pointed out that the British Government had successfully managed to reach a wide consensus across all parties on development policy including the aim to reach an 0,7 ODA/GNI ratio by no later than 2013. He also made clear that this cross party consensus not always covered the exact allocation of aid funds, but rather the

level of efforts being made on development assistance and the commitment to the achievement of the MDGs.

He also noted the particular challenge DFID was facing due to the fact that the DFID budget had been increasing significantly (more than doubled in the past three years), government had imposed a reduction of staff by 10 percent over the same period in order to reduce the costs of administration and bureaucracy.

Mr Sudders stated that in recognition of the continuing increase in budget, DFID was now being represented in Cabinet by the Secretary of State for International Development (Douglas Alexander), in the House of Commons by Minister of State (Gareth Thomas) and also by two Parliamentary Under-Secretaries of State.

As the **core priorities for DFID** the Secretary of State had defined the following four **focal areas**:

- growth (considered as the exit strategy for aid),
- climate change,
- fragile states and conflicts as well as
- international institutional reforms.

According to Mr. Sudders, one third of the total DFID staff (2600) was Staff Appointed in Country (locally engaged staff from the Developing Countries), and 50 percent was based in the London and East Kilbride headquarters.

The speaker described the **organisational structure of DFID** as extremely decentralised, given that its policy function was based in London, while the country programmes were run under the responsibility of the respective country office, which had the authority to commit DFID to spending up to £20 Million a year, without the involvement of the minister. This was believed to enable the office to better react to the local situation.

The role of ODA in the UK development system was set out in the **International Development Act**, which established that all ODA had to be used for poverty reduction. The compliance with this requirement was assessed by the Secretary of State.

Subsequent to this first part of the presentation, Mr van de Sand encouraged the audience to pose their comments..

One question referred to the **relation between the DFID field offices and the British embassies** in developing countries. Mr Sudders explained that compared to the period immediately after the creation of DFID in 1997 when the newly created institution still had very much underlined their independence from the Foreign Ministry, the recent trend was to work together more closely, which was also promoted by the common PSA; in some cases the DFID office and the embassy were even located in the same building, a trend that was to be carried forward in the future.

The question aroused what would happen if DFID failed to meet the **targets set out in the PSA**. Mr. Sudders stated that DFID had to report on its progress against the PSA every three month. This report was rather to be seen as an option to assess the causes in cases where targets had not been achieved and to justify the measures taken, rather than about drawing consequences in terms of punishment mechanisms.

According to Mr. Sudders, the main use of the PSA in DFID was to give everybody clarity about the overall objectives and enable a clearer understanding within the public how taxpayer's money was spent. These reports were passed to the treasury which might also publish them to Parliament.

When asked about the **DFID cooperation with NGOs on the country level**, Mr. Sudders replied that there were three ways for NGOs to receive funding from DFID: one was the so-called **Partnership Agreement**, through which a sort of "Budget Support" was provided – almost unconditional – over a period of three years for mainly big civil society organisations (like Oxfam or Save the Children). Secondly, NGOs could apply for DFID funding for particular projects or programmes. In addition, also the DFID country offices due to their devolved authority were able to provide financing even to local Civil Society Organisations.

Mr. Sudders proceeded with the second part of his presentation in which he addressed the issue of **Budget Support in the British development cooperation system**, particularly with regard to impacts and challenges.

Concerning **DFID's rationale for delivering Budget Support**, he specified the following aspects:

- **Effective Governments** are seen as the **key players** in an effective state and as the precondition for sustainable development, since they were the only actors to deliver nationwide services, implement sound economic management systems and ensure peace and security. Development agencies must enable governments to manage their finances, provide essential services and raise money locally.
- BS is believed to **strengthen government systems** and help governments to deliver core functions. Independent evaluations had shown that in **Rwanda** BS had helped the government to build financial and political stability, whereas in **Ghana** and **Tanzania** it had contributed to a more stable macro economy. In **Mozambique**, there was a noticeable increase in public spending on the poor population: 3,300 new classrooms a year had been built, and there had been a 50% increase in the number of children in school from 2.3 million in 2000 to 3.7 million in 2004.
- BS is also considered as to have the potential to **enable governments to be accountable** for their actions and **responsive to their citizens**. More money routed through the government's budget meant that the government could be held to account about its decisions to spend money and the achieved results: donors could not longer be used as an excuse for poor service delivery.
- By using **government systems**, BS as part of a long-term policy is believed to help **strengthen** them. This improvement in systems is attributed to two aspects: firstly, using the planning and budgeting system would make them more central to the government and the country. Secondly, donors and governments would put their time and money into improving government systems rather than into parallel project systems. Technical Assistance (TA) and Capacity Building programmes would support government-led PFM reforms in all Budget Support countries.

Subsequently, Mr. Sudders commented on **DFID's approach to risk management** in relation to the delivering of BS.

He stated that there were only **three conditions** to be met by recipient governments:

- a clear commitment to poverty reduction,

- the strengthening of Human Rights, and
- the continuous improvement of Public Financial Management (PFM) and Governance.

Mr. Sudders pointed out that on the part of DFID there was no absolute standard for PFM below which BS would not be conceded. In contrast, more importance was attached to a credible reform programme addressing PFM, instead of the fulfilment of specific indicators. This assessment was therefore of a rather relative kind, always based on the local context and knowledge. DFID's bottom line in the decision on BS was therefore to look whether the expected benefits outweighed the potential risks.

According to Mr Sudders, there are three ways of **protecting the delivered BS funds**:

DFID's risk assessment based on the PEFA-process (Public Expenditure and Financial Accountability), controlled by international experts and approved by the British National Audit Office. Furthermore, DFID'S country offices had to ensure that governments had credible reform programmes to improve their systems and to provide TA in order to support them. Different kinds of safeguards were used to prevent misuse of funds (e.g. procurement approval by experts outside the national system or an additional audit of a particular sector). As an evidence of DFID's careful handling of BS Mr. Sudders cited the fact that out of the 31 countries where DFID was spending over £10 Million, only 15 countries currently received Budget Support, which represented only 18% of DFID's total bilateral programme.

According to the speaker, DFID manages the **fiduciary risks of Budget Support** together with country office staff, government and economist advisers, by:

- Assessing the strength of government systems and the risk of using them
- Assessing the corruption risk as part of this
- Analysing the credibility of government's reform programme
- Analysing the implications for aid instrument choices and making sure that there is a range of instruments suitable to the specific country context.

In relation to **corruption risks**, Mr. Sudders gave the example of DFID's experience in **Bangladesh**, where the local country office was considering the option to provide BS in a specific sector where government was meeting the relevant criteria in terms of reform programmes and commitment to poverty reduction. But since Bangladesh every year ranked at the top end of the worlds most corrupt countries according to the Transparency International Corruption Perception Index, it was politically unacceptable to be giving Budget Support to the country.

The speaker corrected the not uncommon perception of DFID being almost exclusively giving Budget Support by providing some data on the **allocation of development aid**:

- DFID gives aid to over 100 countries
- DFID conducts full scale programmes in around 60 countries and runs offices in 45 countries
- 31 countries receive more than £10 Million per year
- There are 25 Focus countries – monitored by central government as part of the PSA
- **15 countries receive Budget Support**: the total amount of BS represents around **18% of DFID's bilateral programme**

Mr. Sudders indicated that BS had probably been the most evaluated aid type in the past few years. The following **achievements of BS** were based on the results of these external independent and multi-donor evaluations:

According to these, BS had **reinforced and built effective states** by strengthening budget and planning processes as well as PFM systems and increasing the accountability both within government and between government and citizens. It provided a more effective and efficient way of delivering aid, in terms of lower additional costs for government, since aid money was spent through national rather than parallel systems, and a more efficient allocation of all government spending. Due to the collaboration on GBS, donor harmonisation improved across all sectors. Examples for delivering results were the case of **Malawi**, where health spending increased from \$15m in 2000 to \$46m in 2005 and u-5 mortality rate had fallen 30% since 2000, and **Rwanda**, where Budget Support had enabled free primary education in 2004 and the building of 900 new primary school classrooms, putting 500,000 more children into school. Primary net enrolment in the latter country had increased from 91% in 2003 to 95% in 2006.

In this context, Mr Sudders quoted the **National Audit Office (NAO) Report**, published on 8 February 2008: *“Budget support has allowed developing country governments to increase expenditure in priority sectors, and helped to expand access to essential public services and improve public financial management in partner countries.”*

The guest speaker explained that the DFID policy had been updated recently, considering the lessons learnt and recommendations from recent evaluations. Among the main **policy changes** was the clear notion that BS had the best impact when combined with other aid interventions, which meant that BS had to be accompanied by some form of TA around PFM or other kinds of aid, and a stronger focus on political governance.

Other changes were the Country Level Fiduciary Risk Assessment as well as a more streamlined and detailed guidance provided by DFID on how to assess and monitor corruption risks, external scrutiny of all BS programmes and a clear relationship with the PEFA-framework.

Subsequently, Mr Sudders elaborated on the **impacts of BS** set out in the evaluations:

According to that, BS has led to increased expenditures on pro-poor areas and increased services delivered. There was strong evidence from all evaluations that this had always occurred where BS had been delivered for a few years in succession. In some countries the proportion of overall spending on health and education as well as the absolute amounts had also increased. Furthermore, BS had contributed to a greater efficiency of overall spending due to government being able to control overall expenditure on capital and recurrent spending. Transaction costs of implementation had decreased, since governments were able to use their own systems instead of parallel processes. Due to more aid money using the systems and to more technical assistance and capacity building focused on them, financial management systems had been strengthened. BS had also reinforced existing macro-economic stability and good economic management, since BS could be used to stabilise domestic debt levels and increase expenditures. BS becoming a more important tool for allocating resources had contributed to increased accountability within the government – instead of towards the donors – which also set the basis for

more accountability between government and citizens due to an increased transparency about how all government revenue (including aid) was being spent.

Mr Sudders acknowledged that there was a **weaker evidence of impacts of budget support on poverty and growth rates**, since these were affected by many different issues which made it difficult to attribute any improvements to any particular aid type.

In order to **maximize the impacts of BS**, DFID would concentrate on the following aspects:

Firstly, BS had to be combined with other aid interventions, in order to strengthen accountability between state and citizens, build capacities to formulate, implement monitor and evaluate policy, and to strengthen analysis of use and impact of government expenditures.

Secondly, BS had to be designed and delivered in an effective way, in order to increase predictability and align monitoring and review processes with government systems.

Thirdly, there was a need to strengthen the way other aid was delivered, to make sure that DFID's overall aid was on the government's budget and accompanied by coordinated TA, since aid flows delivered outside government systems and plans undermine possible impact of budget support.

There were also some **challenges for DFID** identified by parliamentary inquiries, experts and national reports. Among these was the need to keep a strong focus on the objectives of development policy (in terms of increasing the speed of achievement of the MDGs and even closing down programmes not needed any more). Furthermore, there had to be a continuous improvement of government assessments and the aim to refute the reservations of the public towards BS due to corruption risks and other concerns by "telling the story better."

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