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**BUDGET SUPPORT, POVERTY AND CORRUPTION: A REVIEW OF THE EVIDENCE**

Geske Dijkstra



# Budget Support, Poverty and Corruption: A Review of the Evidence

*Geske Dijkstra*

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*till*

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# Foreword by the EBA

Around the year 2000, budget support was considered to be the effective and often preferred aid modality. Used at the discretion of recipient governments, normally accompanied with policy dialogue, budget support is arguably the aid instrument that best complies with the principles of aid effectiveness. Following Swedish government priorities, it increased up to 2008. However, after that it decreased dramatically and by 2016, no general budget support was provided by Sweden. A similar change is apparent in the aid portfolio of other donor countries.

Budget support has an important role to play in the debate on effectiveness and harmonization of development aid, not least at the European level. In many cases, budget support is the preferred modality by partner country governments (see, for example, EBA 2016:09). It is based on trust and ownership and avoids parallel structures and processes by using recipient countries' systems. It has been considered to have low transaction costs, coordination gains and a potential to strengthen dialogue with poor countries' governments. However, while having strong supporters and backing in international agreements, it has also been depicted as risky and fostering corruption. Thus, budget support is controversial among Swedish policy makers as well as in the public debate.

In this review of evidence, Professor Geske Dijkstra shows that the decline in budget support to a large extent is explained by factors in donor countries rather than by lack of evidence on effectiveness or limitations in its possibilities to reduce poverty. The author concludes that budget support has contributed to non-income poverty reduction and that its resources, and sometimes the dialogue as well, have facilitated more expenditure for the priority sectors. "This has led to more class rooms, more drug availability, and more staff for education and health. In turn, this has contributed to higher school enrolment rates, to more gender equality in access to primary education, to more access to health services, and more access to water and sanitation. In some countries, access to secondary education significantly improved as well. In many countries there were also improvements in outcomes such as

primary school completion rates, immunization rates, infant and child mortality rates, and maternal mortality rates”. In addition, “contrary to the many expectations on the high fiduciary risks of budget support, there is no evidence that it increased corruption”.

The review demonstrates how challenging it has been for the donor community to uphold the aid effectiveness principles in the light of political opinions and considerations in donor countries. Often withdrawal of budget support has been used as an, ineffective, punishment of recipient countries’ non-compliance with donor priorities.

The study raises pertinent questions about learning and the use of evidence in the design of aid. As such, it contributes to the discussion about why donors and/or recipients prefer certain forms of support. Another question coming out of the study is how donors should work to strengthen the legitimacy of effective aid modalities that for some reason is difficult to communicate or explain for people outside the aid “industry”.

It is my hope that this report will find its intended audience among a broad public interested in aid effectiveness, learning and evidence in development cooperation.

The author’s work has been conducted in dialogue with a reference group chaired by Torgny Holmgren, member of the EBA. However, the author is solely responsible for the content of the report.

Gothenburg, August 2018



Helena Lindholm

# Sammanfattning

Budgetstöd är bistånd som inte är kopplat till projekt och som mottagarlandets regering kan använda fritt. Biståndet åtföljs oftast av en policydialog. Under de senaste åren har budgetstödens volymer minskat. I den här rapporten undersöks i vilken utsträckning det minskade intresset beror på bristande effektivitet. Rapporten innehåller en sammanfattning av tillgänglig kunskap om instrumentets effektivitet.

Rapporten utgår från en policyteori om förväntade effekter utifrån budgetstödens insatta resurser: finansiering samt policydialog eller försök att utöva inflytande. Detta är en ”anpassad” policyteori. I rapporten hävdas att den ursprungliga policyteorin som betonade mottagarlandets ägarskap och fokuserade på ett mål, fattigdomsminskning, efterhand har ersatts av en ny policyteori där bidragsgivarna har återinfört olika policyvillkor och där dessa villkor alltmer är inriktade på politisk styrning. Att förbättra den politiska styrningen har blivit ett andra mål för budgetstödet. I rapporten följs resultaten av resurser och policydialog i en orsakskedja från harmonisering, anpassning och förutsägbarhet via kortsiktiga prestationer som stärkta lokala system, lägre transaktionskostnader, ökad makroekonomisk stabilitet samt ökade resurser till prioriterade sektorer, till effekter som förbättrad policy, styrning och fattigdomsminskning.

De delfrågor som tas upp är:

1. Hur ser de mellanliggande resultaten ut för det generella budgetstödet (aktiviteter och prestationer)? Uppnåddes förväntade prestationer? Varför eller varför inte?
2. Ger policydialogen givarna inflytande över politik och styrning? Varför eller varför inte?
3. På vilket sätt bidrar resurserna för budgetstöd – policydialog och finansiering – till förbättringar i fråga om sociala indikatorer och fattigdomsminskning utifrån möjligheterna till inflytande på regeringspolitik och via statens utgifter?

Metodmässigt utgår rapporten från IOB:s tidigare syntesstudie av budgetstöd (Dijkstra, De Kemp och Bergkamp, 2012). I den ingår en omfattande litteraturgenomgång, en systematisk jämförelse av sex nyligen utvärderade fall samt ekonometrisk forskning från flera länder om budgetstödet effekter. I den här rapporten presenteras också resultat från senare akademiska studier och utvärderingar av budgetstöd. I alla nyligen genomförda landutvärderingar ingår kvantitativa analyser av hur det slutliga utfallet har påverkats av budgetstödet, i synnerhet för utvalda sociala indikatorer. Detta bidrar till mer robusta svar på delfråga 3.

## Mellanliggande resultat

I genomsnitt utgjorde budgetstöd mellan 14 och 28 procent av det totala offentliga utvecklingsbiståndet i de nyligen utvärderade länderna. Detta ledde till en betydande anpassning av biståndet till lokala system. Även om vissa givare fortsatte med separata variabla utbetalningar, harmoniserades utbetalningsvillkoren i de flesta länder. Förutsägbarheten från år till år för budgetstödet var bra, och bättre än för projektstöd. Förutsägbarheten inom ett enskilt år förblev till viss del problematisk. Utbetalningarna genomfördes senare än utlovat och den största delen av flödet inträffade mot slutet av året. Budgetstödet har inneburit minskade transaktionskostnader. Dessa positiva resultat gällde dock främst för utvärderingsperiodernas tidigare delar.<sup>1</sup> Fördelarna gick mångt och mycket förlorade som en följd av mer intensivt fokus på samhällsstyrning, reaktioner på upplevda överträdelser av underliggande principer i budgetstödsprocessen och generellt lägre budgetstödvolymer.

Bidragsgivarna tillämpade inledningsvis viss selektivitet i budgetstödet, i synnerhet avseende styrning. Bidragsgivarna hade dock ofta svårt att respektera ägarskapet. När budgetstödet hade inletts använde de policydialogen för att påverka policyer och, i allt högre grad, styrningen. Denna brist på respekt för ägarskapet tycks

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<sup>1</sup> Brytpunkten varierar mellan olika länder men ligger någonstans mellan 2005 (Uganda och Etiopien) och 2011 (Burkina Faso).

ha ökat över tiden. I många länder försämrades policydialogen till följd av en ond cirkel; ett ökande missnöje bland givarna med landets utvecklingsresultat, ofta rörande styrning, vilket ledde till ännu högre ambitioner i policydialogen, vilket i sin tur orsakade ett ännu större missnöje. Det ledde slutligen till tillbakadraget stöd. Detta minskade harmoniseringen då respektive givarland tog egna beslut i dessa frågor. Styrningsfrågans dominans har inte bara gjort frågan om ägarskap svår, den påverkar även andra fördelar med budgetstöd, såsom harmonisering, anpassning till lokala system och förutsägbarhet.

## Effekter på policy och styrning

När givarna lyckades samordna sina preferenser för policydialogen och gemensamt enades om ett litet antal indikatorer, möjliggjorde det positiva övergripande effekter i dialogen utifrån bättre samordning och mer resultatriktade nationella policyer. Kombinationen av nationella system, en omsorgsfull policydialog och teknisk assistans ledde till förbättringar i den offentliga finansiella styrningen i samarbetsländerna. Budgetstödet *övergripande* effekter vad gäller ett förbättrat nationellt ansvarsutkrävande tycks dock vara begränsade. Policydialogen sker mellan givare och mottagarlandets regering, och att lokala system och budgetar används medför inte automatiskt intresse i parlament eller bland civilsamhällesaktörer. Policydialogen och de åtföljande aktiviteterna för kapacitetsuppbyggnad ledde dock till institutionella förbättringar för ett horisontellt ansvarsutkrävande (på utbudssidan). De bidrog till ökad insyn i budgetar och i budgetgenomförandet, i synnerhet genom att stärka parlamentsutskott för offentliga räkenskaper, revisionsmyndigheter och nationell revisionsrätt. Det direkta stödet från givarna till institutioner på efterfrågesidan av ansvarsutkrävandet var mer begränsat. I flera länders har dock parlament, media och civilsamhället tagit tillvara de ökade möjligheterna att ställa regeringar till svars, vilket tyder på att budgetstöd till viss del även har bidragit till ett förbättrat vertikalt ansvarsutkrävande. Budgetstödet bidrog inte endast till att stärka institutionerna för tillsyn av budgetgenomförandet, utan även institutioner med uppgift att övervaka korruption. Detta bidrog till att fler fall av korruption

upptäcktes. I de flesta länderna finns dock fortfarande en oro för i vilken omfattning gärningsmännen lagförs och bestraffas. Tvärtemot mångas farhågor, saknas belägg för att budgetstöd har bidragit till en ökad korruption.

Givarnas försök att påverka policy, styrning och mänskliga rättigheter har endast varit begränsat effektiva, något som ligger i linje med litteraturen om de tidigare så kallade strukturanpassningsprogrammen. Utvärderingarna pekar också på vissa förlorade möjligheter vad gäller policy. Givarna fokuserade ofta på för många enskilda resultatindikatorer. Detta skedde på bekostnad av en mer strategisk diskussion om att undanröja hinder i befintlig samhällsservice eller främja ekonomisk tillväxt. Givarna begränsades även av bristande kunskaper om hur budgetstöd eller regeringspolicyer skulle kunnat minska inkomstfattigdomen. Givarna var inte heller framgångsrika när de försökte skapa mer fattigdomsfokuserade policyer i områden där detta stred mot mottagarlandets regerings (upplevda) strategiska eller politiska intresse (Moçambique, Zambia). I fråga om samhällsstyrning och mänskliga rättigheter är det tydligt att hårda incitament, som hot om budgetstödsindragningar, i bästa fall lett till kosmetisk förändring. Mjuka incitament förefaller ha fungerat bättre. Vissa författare hävdar att givare skulle kunnat åstadkomma mer inom samhällsstyrningen om de agerade gemensamt, men det saknas tydliga belägg för denna tes.

Budgetstöd har bidragit till att uppnå eller, beroende på situationen i mottagarlandet, upprätthålla den makroekonomiska stabiliteten. Budgetstöd har gett länder en möjlighet att öka de offentliga utgifterna utan att det påverkar den makroekonomiska stabiliteten och därmed har stöden bidragit till ekonomisk tillväxt. I de flesta länderna ökade utgifterna för prioriterade sektorer. Överlag saknas också belägg för att budgetstöd minskar de nationella skatteintäkterna. Det förekommer dock stora skillnader mellan länder, och oroande tendenser i detta avseende förekommer i vissa nyligen utvärderade länder (Burundi, Sierra Leone och Uganda).

## Effekter på fattigdomsminskning

Länder med budgetstöd har minskat inkomstfattigdomen mer än andra utvecklingsländer, men det är samtidigt inget bevis för en kausal relation. Från landutvärderingar kan man dock dra slutsatsen att *om* budgetstödet har bidragit till att minska inkomstfattigdomen skedde det med största sannolikt genom dess effekt på den ekonomiska tillväxten. Tillväxt har samtidigt inte varit en tillräcklig faktor för att minska inkomstfattigdomen. Det framgår av erfarenheten från Burkina Faso, Moçambique, Tanzania och Zambia där inkomstfattigdomen knappast minskat.

Budgetstödet bidrog dock till att minska den icke inkomstbaserade fattigdomen. Budgetstödersurser, och ibland även dialog, har möjliggjort ökade utgifter i prioriterade sektorer. Detta har lett till fler klassrum, bättre läkemedelstillgänglighet och mer personal inom utbildning och hälsa. Det har i sin tur bidragit till att fler går i skolan, ökad jämlikhet vad gäller tillgång till grundskoleutbildning, bättre tillgång till hälsovård och bättre tillgång till vatten och sanitet. I vissa länder förbättrades tillgången till gymnasial utbildning avsevärt. I många länder såg man även resultatförbättringar vad gäller andelen elever som slutförde grundskolan, immuniseringsnivåer och nivåer för spädbarnsdödlighet och mödradödlighet. Att budgetstödet har bidragit till detta har visat sig både i kvantitativa landövergripande analyser och i fallstudier. I senare landsutvärderingar har man tillämpat mycket rigorösa metoder för att fastställa orsakssamband mellan de ökade investeringar som möjliggjorts genom budgetstödet och de slutliga sociala effekterna.

## Diskussion

Sammantaget är det tydligt att de minskade volymerna av budgetstöd inte kan motiveras utifrån att instrumentet inte är effektivt eller utifrån att farhågor om korrupktion har besannats. Budgetstöd har tvärtom varit ett mycket effektivt sätt att minska, särskilt den icke inkomstbaserade fattigdomen, och det har även bidragit till förbättringar inom offentlig finansiell styrning och tillsyn av samhällsinstitutioner.

Samtidigt har budgetstöd inte varit en framgångsrik metod för att uppnå det andra, och senare tillagda, målet om att förändra mottagarländernas politiska styrning. Det finns istället belegg för en trade-off mellan målen. En prioritering av det andra policy-målet i kombination med nedslående resultat (inom det tillagda målet) ledde till att många biståndsgivare, särskilt bilaterala givare, tillfälligt upphävde och återkallade budgetstöd. Det, i sin tur, ledde till en mindre förutsägbar finansiering och lägre budgetstödsvolym, vilket minskade budgetstödetts effekt på fattigdomsminskningen. Detta bekräftar regeln att ett instrument endast kan och bör ha ett mål (den så kallade Tinbergenregeln). Och för budgetstöd bör detta enda mål vara det ursprungliga målet om fattigdomsminskning.

Framväxten av ett mål om att främja den politiska styrningen berodde på flera faktorer. För det första fanns det i början av 2000-talet underliggande tvivel inom givarsamfundet om biståndseffektivitetsagendan. Trots den officiella betoningen på mottagarländernas ägarskap ansåg många givare att det krävdes fler villkor inom policy och styrning för att förbättra biståndets effektivitet. Budgetstöd tillsammans med åtföljande policydialog blev det ideala forumet för att genomföra dessa villkor. För det andra, och i motsats till den ursprungliga policyteorin, tillämpade givarna endast begränsad selektivitet i beslut om budgetstöd. För det tredje spelade utvecklingen inom givarländerna en roll i utvecklingen mot att ge den *politiska* styrningen en ökad uppmärksamhet, dvs. fokus på demokrati och mänskliga rättigheter, och även i den resulterande nedgången för instrumentet. En sådan faktor är 2008 års ekonomiska kris som medförde att medborgarna i allmänhet blev mer kritiska till utvecklingssamarbete. Detta förstärkte de upplevda riskerna med budgetstöd. Det ledde även till att regeringar kände sig tvungna att visa på mer konkreta resultat av biståndet. Detta är problematiskt när det gäller budgetstöd eftersom resultat är svåra att hänföra till enskilda givares insatser. En annan faktor är att konservativa regeringar fick en mer framträdande roll i många givarländer. Dessa regeringar är i allmänhet något mindre dedikerade till biståndseffektivitetsagendan.

## Policyrekommendationer

Med tanke på beläggen för att budgetstöd är effektivt i fråga om fattigdomsminskning så är frågan hur givare kan bygga vidare på de positiva resultaten och samtidigt beakta det politiska bakslaget för budgetstöd i de egna länderna. Givarna bör i grunden följa den ursprungliga policyteorin, vilket innebär en selektivitet i fördelningsbeslut för budgetstöd, en policydialog inriktad på fattigdomsminskning eller andra mål för hållbar utveckling, respekt för ägarskapet och en förutsägbar finansiering.

Innan bistånd, inte bara budgetstöd, fördelas till en regering i ett mottagarland bör givaren ha visst förtroende för landets respekt för demokratiska värderingar och mänskliga rättigheter.<sup>2</sup> I synnerhet vad gäller budgetstöd är det viktigt med en viss tillit till system för budgetering och ansvarsutkrävande i förhållande till de offentliga finanserna, men en vilja till förbättring är viktigare än den faktiska nivån. Ett viktigt villkor för budgetstöd är också ett mått av förtroende för mottagarlandets socio-ekonomiska policy.

Mot bakgrund av dessa kvalificerande villkor kan givare överväga en portfölj av olika biståndsformer. Om givarna saknar förtroende för den mottagande regeringens respekt för demokratiska värden och mänskliga rättigheter kan de överväga att ge bistånd till icke-statliga organisationer eller att inte ge landet bistånd alls. Vid ett beslut att ge bistånd till en regering är ett generellt budgetstöd eller ett sektorbudgetstöd i princip mer effektivt än projektstöd för de flesta målsättningar i biståndet. I båda fallen kan medlen användas fritt, men innehållet i policydialogen ser olika ut. Ett generellt budgetstöd är mer lämpligt för att hantera strategiska och övergripande frågor som är relaterade till fattigdomsminskning, eller för att uppnå de hållbara utvecklingsmålen. Ett sektorbudgetstöd kan inriktas mer i detalj på policy för en viss sektor, ett visst, eller en uppsättning, mål för hållbar utveckling.

Även på mottagarsidan kan man använda sig av en portfölj. Det är inte nödvändigt att ”alla” givare ingår i ett generellt budgetstöd.

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<sup>2</sup> Detta behöver inte gälla i så kallade fragila stater, men de ingår inte i denna rapport.

Mindre givargrupper har visat sig ge färre indragningar och en policydialog av högre kvalitet. Med tanke på att multilaterala givare i mindre grad påverkas av politik än bilaterala givare kan det vara klokt att ta emot generellt budgetstöd från (primärt) multilaterala givare, och samtidigt ta emot sektorbudgetstöd från olika mindre grupper bestående av (främst) bilaterala givare. Det skulle innebära att båda policydialogerna kan fokusera på utvecklingspolicy i stället för politik. Om det generella budgetstödet i delar ersattes med ett sektorbudgetstöd skulle det visserligen innebära en lägre harmonisering bland givare på central styrningsnivå, men medlen skulle fortfarande gå genom de inhemska systemen och förutsägbarheten för biståndet skulle sannolikt öka.

Givare bör undvika att använda budgetstöd som en hävstång för att förbättra det politiska styret eller minska korruptionen. Det finns belegg för att sådana försök, t.ex. genom mål i så kallade Performance Assessment matriser, endast får formell eller symbolisk effekt. Frekventa (hot om) indragningar baserade på styrningen begränsar också de positiva effekterna av budgetstöd. Rekommendationen att inte använda budgetstöd för att påverka politisk styrning innebär inte att givarna inte bör ta upp styrningsfrågor med mottagande regeringar. Men en sådan dialog om demokrati och mänskliga rättigheter bör föras separat från dialogen om budgetstöd.

Både det generella budgetstödet och sektorbudgetstödet sker inom de statliga budgeterings- och rapporteringssystemen så dessa instrument kan användas för att förbättra den offentliga finansiella styrningen och ansvarsutkrävandet vid nationella institutioner. Kombinationen av en policydialog och kompletterande tekniskt bistånd har visat sig vara effektivt, i synnerhet vad gäller den offentliga finansiella styrningen och institutioner inom horisontellt ansvarsutkrävande, t.ex. revisionsmyndigheten. Som ett komplement till budgetstödet bör givarna överväga att stödja institutioner för ansvarsutkrävande på efterfrågesidan, t.ex. genom parlament och civilsamhälle. Givare rekommenderas också att använda andra mjuka incitament som att främja deltagande i internationella nätverk.

Budgetstöddialogen kan även vara inriktad på policyer för minskning av (inkomst)fattigdomen eller för att främja genomförandet av agenda 2030. Men förväntningarna bör inte vara för höga vad gäller hur mycket budgetstöd kan bidra till att minska *inkomstfattigdomen*. Budgetstöddressurser kan möjligen indirekt bidra till att minska inkomstfattigdomen genom en växande fysisk eller social infrastruktur för de fattiga. Ett direkt bidrag är endast möjligt om resurserna bidrar till att finansiera kontantstödprogram. Utöver detta beror minskad inkomstfattigdom och ojämlikhet mer på regeringspolitik och inte på resurser. Biståndsgivarna kan bidra till att uppmärksamma en minskning av inkomstfattigdomen och ojämlikheten i policydialogen och även rekommendera och finansiera landspecifika studier om hur den offentliga politiken kan göra mer för de fattiga.

Policydialogen vid generellt budgetstöd eller sektorbudgetstöd bör vara baserad på mottagarlandets ägarskap, vilket underförstått innebär ett begränsat antal PAF-indikatorer. Ju mer de deltagande givarna lyckas harmonisera utbetalningskriterierna, säkerställa en förutsägbar finansiering och respektera ägarskapet, desto effektivare kommer det generella budgetstödet och sektorbudgetstödet att vara. Behovet av att säkerställa en förutsägbar finansiering innebär att utbetalningarna inte bör ske genom så kallade ”variable tranches”. Det finns inga forskningsbelägg för en bättre överensstämmelse med indikatorerna vid dessa variabla villkorade utbetalningar än för indikatorer relaterade till mer fasta utbetalningar, och kvaliteten på policydialogen höjs om man undviker dessa.



# Summary

Budget support is an aid instrument that is not linked to projects and that is freely spendable by recipient governments. It is usually accompanied by a policy dialogue. Budget support volumes have declined in recent years. This report examines the extent to which this reduced interest is due to a lack of budget support effectiveness. It summarises the evidence available on the effectiveness of this aid instrument.

The report starts from a policy theory on the expected effects of the two inputs of budget support, resources and policy dialogue or attempt to influence. This is an ‘adjusted’ policy theory. It is argued that the original policy theory, which stressed recipient country ownership and focused on one objective, namely poverty reduction, has been substituted by a new policy theory in which donors have reintroduced policy conditionality and in which this conditionality is increasingly focused on political governance. Improving governance has thus become a second objective of budget support. The report traces the effects of the two inputs of budget support along the causal chain – from throughputs such as harmonisation, alignment and predictability via outputs such as strengthened local systems, reduced transaction costs, improved macroeconomic stabilisation and more resources to priority sectors – to outcomes and impact such as improved policies and governance, and greater poverty reduction.

The sub-questions the report addresses are:

1. What are the intermediate effects (throughput and outputs) of general budget support? Did the expected outputs come about? Why or why not?
2. Do donors have any influence on policies and governance through the policy dialogue? Why or why not?
3. What is the contribution of the two budget support inputs, policy dialogue and resources, through their influence on government policies and spending, to improvements in social indicators and to poverty reduction?

Methodologically, the report takes the results of the IOB policy review of budget support (Dijkstra, De Kemp and Bergkamp, 2012) as starting point. This policy review includes an extensive literature review, a systematic comparison of six recently evaluated cases and cross-country econometric research on the effects of budget support. The current report additionally analyses the results presented in more recent academic studies and evaluations of budget support. All recent country evaluations include quantitative analyses of the effects of budget support-induced government policies on ultimate outcomes, and on selected social indicators in particular. This helps to provide a more robust answer to sub-question 3.

## **Intermediate effects**

On average, budget support constituted between 14 and 28 per cent of total ODA in the recently evaluated countries. This led to substantial alignment of aid to local systems. Although some donors maintained separate variable tranches, in most countries disbursement conditions were harmonised to a great extent. The between-year predictability of budget support was good, and better than for project aid. Within-year predictability remained somewhat problematic, with donors disbursing later than promised and most flows coming at the end of the year. Budget support decreased transaction costs. However, each of these positive findings held true mostly for the earlier parts of the evaluation periods.<sup>3</sup> These benefits largely evaporated by the end of the period as a result of more intensive governance discussions, varying donor responses to perceived breaks with the underlying principles, and lower budget support volumes.

Donors applied limited selectivity when starting budget support, in particular with respect to governance. And donors had difficulties in respecting ownership. Once budget support started, they began to use the policy dialogue to influence policies and, increasingly, governance. This lack of respect for ownership seemed to increase over time. In many countries, the policy dialogue deteriorated as a

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<sup>3</sup> The turning point varies between the countries but lies somewhere between 2005 (Uganda and Ethiopia) and 2011 (Burkina Faso).

result of a vicious circle: increasing donor dissatisfaction with country performance, often on governance issues, led to ever higher policy dialogue ambitions, in turn causing more dissatisfaction. In the end, this led to budget support suspensions and withdrawals, with each donor country making its own decisions on these matters, thus reducing harmonisation. The dominance of the governance objective was detrimental to ownership, and it also affected the other benefits of budget support, namely harmonisation, alignment and predictability.

## **Effects on policy and governance**

If donors succeeded in coordinating their policy dialogue preferences and jointly agreed on a small number of Performance Assessment Framework (PAF) indicators, positive systemic effects of the dialogue were possible for better coordination and higher results-orientation of national policies. The combination of the use of domestic systems, attention in the policy dialogue and technical assistance led to improvements in Public Financial Management. The *systemic* effects of budget support on increasing domestic accountability seemed to be limited. The policy dialogue is between donors and recipient government, and the use of local systems and budgets did not automatically generate interest in parliament or among civil society actors. Yet, the policy dialogue and accompanying capacity-building activities did lead to improvements in the institutions for horizontal accountability (the supply side). It contributed to increasing budget transparency and budget execution, particularly through strengthening Public Accounts Committees of Parliaments, Supreme Audit Institutions or Courts of Audit. Direct donor support to institutions on the demand side of accountability was more limited. Yet in several countries, parliaments, media and/or civil society had seized the increased opportunities to hold governments to account, implying that budget support also contributed somewhat to improvements in vertical accountability. Budget support strengthened not only institutions for the oversight of budget execution, but also other institutions aiming to monitor corruption. This helped detect more corruption cases. However, in most countries concerns remain about the extent

of prosecution and punishment of the culprits. Contrary to the many expectations on the high fiduciary risks of budget support, there is no evidence that it increased corruption.

In line with earlier literature on structural adjustment, the effectiveness of donor attempts to influence policies, governance and human rights was limited. With respect to policies, the evaluations point to some missed opportunities. Donors often focused too much on too many individual performance indicators at the expense of a more strategic discussion on how to remove obstacles to public service provision or foster economic growth. Donors were also hindered by a lack of knowledge about how budget support or government policies could reduce income poverty. However, when donors tried to make policies more pro-poor in situations where this conflicted with (perceived) strategic or political interest of the recipient government (Mozambique, Zambia), they were not successful. Regarding governance and human rights, it was clear that hard incentives, such as indicators in the PAF or (threats of) suspensions, led at most to cosmetic changes. Soft incentives appeared to be more effective. Although some authors argue that donors would achieve more in the governance area if they could speak with one voice, the evidence for this is not strong.

Budget support has contributed to achieving or, depending on the situation in the recipient country, maintaining macroeconomic stability. Budget support allowed countries to increase government expenditure without affecting macroeconomic stability, thus contributing to economic growth. In most countries, spending for the priority sectors, as defined in the Poverty Reduction Strategies, increased. On average, there is no evidence that budget support reduced domestic tax revenues. However, there are large differences between countries, with worrying trends in some recently evaluated countries (Burundi, Sierra Leone and Uganda).

## **Effects on poverty reduction**

Countries receiving budget support have experienced more reduction in income poverty than other developing countries, but this does not prove a causal relationship. From the country

evaluations, it can be concluded that *if* budget support contributed to a reduction of income poverty, it was most likely through its effect on economic growth. However, growth by no means proved a sufficient condition for reducing income poverty, as shown by the experiences of Burkina Faso, Mozambique, Tanzania and Zambia, where income poverty hardly decreased.

Budget support did contribute to the reduction of non-income poverty. Budget support resources, and sometimes the dialogue as well, have facilitated increased expenditure for priority sectors. This has led to more classrooms, more drug availability, and more staff in education and health care. This in turn has contributed to higher school enrolment rates, more gender equality in access to primary education, greater access to health services and greater access to water and sanitation. In some countries, access to secondary education significantly improved as well. Many countries also experienced improvements in outcomes such as primary school completion rates, immunisation rates, infant and child mortality rates, and maternal mortality rates. The contribution of budget support to these achievements has been shown in both quantitative cross-country analyses and case studies, with the more recent country evaluations applying rigorous methods for establishing the causal relationship between increased investment facilitated by budget support and ultimate social outcomes.

## **Discussion**

All in all, it is clear that the decrease in budget support volumes cannot be justified by a lack of effectiveness of the instrument, or by materialisation of the – assumed – fiduciary risks. On the contrary, budget support has been very effective at reducing poverty, particularly non-income poverty, and has also contributed to improvements in public financial management and in oversight institutions.

At the same time, budget support has not been able to achieve the second objective (added later) of improving political governance in recipient countries. Evidence points to a trade-off between the two objectives. The prioritisation of the second objective and the

disappointing results in this area have led many donors, especially bilateral donors, to suspend or withdraw their budget support. This in turn has led to less predictable funding and lower budget support volumes, thus reducing the effectiveness of budget support in poverty reduction. This confirms that each policy instrument should have only one objective (the Tinbergen rule). For budget support, this single objective should clearly be the original one of poverty reduction.

The coming to the fore of the objective of promoting political governance was the result of several factors. Firstly, there were latent doubts in the donor community on the aid effectiveness agenda of the early 2000s. Despite the official emphasis on ownership by recipient countries, many donors were (also) of the view that additional policy and governance conditions were required to improve aid effectiveness. Budget support, with its accompanying policy dialogue, became the ideal forum for implementing this conditionality. Secondly, and contrary to the original policy theory, donors applied limited selectivity in the allocation decision for budget support. Thirdly, several factors within donor countries played a role in the increasing attention paid to *political* governance, i.e. democracy and human rights concerns, and in the resulting demise of the instrument. One such factor was the economic crisis of 2008 that caused citizens to be more critical of development cooperation in general. This reinforced the perceived fiduciary and other risks of budget support. It also resulted in the need for governments to be able to show visible results of aid. This is more difficult with budget support, as the results cannot easily be attributed to the efforts of individual donors. Another factor was the rise of more conservative governments in many donor countries. Such governments are generally less committed to the aid effectiveness agenda.

## **Policy recommendations**

Given the evidence of the effectiveness of budget support for poverty reduction, the question is how donors can build on the positive outcomes of budget support, while taking account of the political backlash of budget support within their own countries.

Basically, donors should adhere to the original policy theory, meaning that they should apply some selectivity in their budget support allocation decision, focus the policy dialogue on poverty reduction or other Sustainable Development Goals (SDGs), respect ownership and secure predictable funding.

Before providing aid – not just budget support – to the government of a recipient country, donors should have some confidence in that government’s respect for democratic values and human rights.<sup>4</sup> For budget support, in particular, some confidence in budgeting and public financial accountability systems is important, although a willingness to improve is more important than the actual level. Finally, an important condition for budget support is a certain level of confidence in the recipient country’s socio-economic policies.

In view of these eligibility conditions, donors may consider a portfolio approach of different aid modalities. If donors do not have trust in the recipient government’s respect for democratic values and human rights, they may consider providing aid to non-governmental organisations or not providing aid to the country at all. In case donors decide to allocate aid to governments, general or sector budget support is in principle more effective than project aid for most aid objectives. In both aid instruments the resources are freely spendable but the content of the policy dialogue is different. General budget support is more suitable for dealing with strategic and cross-cutting issues related to poverty reduction or for achieving other SDGs. Sector budget support focuses more specifically on policies for a particular sector or on a particular (set of) SDG(s).

In a way, recipient countries can also apply a portfolio approach. It is not necessary that “all” donors participate in general budget support. Having smaller donor groups has proven to be associated with fewer suspensions and with a better-quality policy dialogue. Given that multilateral donors are less influenced by political concerns than bilateral donors, it may be sensible to receive general

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<sup>4</sup> This does not need to apply in fragile states, but fragile states are not included in this report.

budget support from (mainly) multilateral donors, while receiving sector budget support from different groups of (mainly) bilateral donors. This would mean that the policy dialogues can focus on policies instead of on politics and governance. And although the partial substitution of general budget support with sector budget support would imply less donor harmonisation at the *central* government level, resources would still be aligned to government systems and aid predictability would probably increase.

Donors should refrain from using budget support as leverage for improving political governance or reducing corruption. Evidence shows that these attempts, for example through the use of targets in the Performance Assessment Matrix, have at most had formal or symbolic effects. On the other hand, frequent (threats of) suspensions for governance reasons hamper the advantages of budget support. The recommendation not to use budget support as leverage for influencing governance does not mean that donors should not raise their governance concerns with a recipient government. But such a dialogue on democracy and human rights issues should be held separately from the dialogue on budget support.

Both general and sector budget support use government budgeting and reporting systems, so these instruments can be used for improving Public Financial Management (PFM) and domestic accountability institutions. The combination of policy dialogue and accompanying technical assistance has proven to be effective, particularly for PFM and horizontal accountability institutions such as Supreme Audit Institutions. As complementary measures to budget support, donors should also consider supporting institutions for vertical accountability (the demand side), such as parliament and civil society. Donors are recommended to use other soft incentives as well, such as promoting participation in international networks.

The budget support dialogue can also focus on (income) poverty reduction policies or on policies to foster achievement of the SDGs. But expectations of budget support contributing to the reduction of *income* poverty should be tempered. Budget support resources can indirectly contribute to income poverty reduction through expanding physical or social infrastructure for the poor. A direct

contribution is only possible if resources help finance social safety net programmes. Beyond this, the reduction of income poverty and inequality depends more on government policies than, on resources. Donors can call attention to the reduction of income poverty and inequality in the policy dialogue, and may recommend and finance country-specific studies on how public policies can be made more pro-poor.

The policy dialogue around general or sector budget support should be based on ownership by the recipient country, implying that the number of indicators in the PAF should be limited. The more participating donors succeed in harmonising disbursement criteria, securing predictable funding, and respecting ownership, the more effective general and sector budget support will be. The need to secure predictable funding also means that the use of variable disbursement tranches should be avoided. There is no evidence of better compliance with indicators for variable tranches than for fixed tranches, and avoiding variable tranches will improve the quality of the policy dialogue.



# Chapter 1. Introduction

## 1.1 Background

This report aims to review the effectiveness of budget support. General Budget support or, for short, budget support is a form of programme aid, and is thus aid that is not linked to projects. The resources flow directly to the Ministry of Finance, but this aid instrument is usually accompanied by a policy dialogue in which donors discuss their preferred policies with the governments of recipient countries. Around the year 2000, budget support came to be seen as the more effective aid modality. On the one hand, this instrument was considered better than the earlier balance of payments support. The policy conditionality that had accompanied balance of payments support, for example on trade liberalisation and on privatisation of state-owned enterprises, had not been effective (World Bank, 1998). The provision of budget support would be based on Poverty Reduction Strategy papers developed by recipient countries themselves, so would be based on ownership. On the other hand, budget support was considered the best approach to meet the aid effectiveness objectives as defined in several High Level meetings of donors and recipient countries. It was expected to further ownership, alignment (with recipient governments' strategies institutions and procedures), harmonisation and a results orientation - all considered important in the new aid approach. The Paris Declaration on Aid Effectiveness (High Level Forum, 2005), for example, stipulated that by 2010, 66 percent of all aid had to be given in "programme-based approaches". This includes General Budget Support (GBS), Sector Budget Support (SBS) and aid provided in Sector-Wide Approaches. This report focuses on GBS and SBS as both involve a non-earmarked flow of resources to the government.<sup>5</sup>

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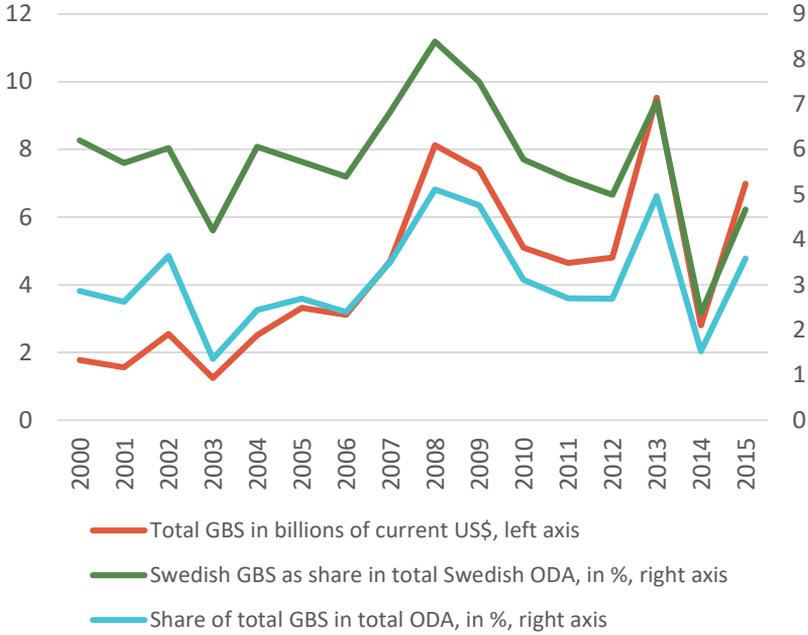
<sup>5</sup> In Sector Budget Support the policy dialogue is focused on a particular sector. Aid in Sector-Wide Approaches (SWAPs) is earmarked to projects but given to support sector wide government plans. OECD aid statistics do not provide information on the amount of aid provided in SWAPs and only since 2009 on SBS flows.

Yet, the evaluation of the Paris Declaration (Wood et al., 2011) shows that although programme-based approaches increased, project aid remained dominant. According to OECD/DAC figures, the amount of GBS rose between 2003 and 2008, but decreased after that. In 2013 there was another temporary increase (the blue line in Figure 1). However, the total GBS flows have never become very large. The share of GBS in total Official Development Assistance (ODA) was again largest in 2008 and 2013 but it was only 5 percent in those years (orange line in Figure 1). Yet, for particular recipient countries, the share of budget support in total aid was substantially higher. For example, between around 2005 and 2010, GBS amounted to 29 percent of total aid in Ghana, 30 percent in Zambia and 42 percent in Tanzania (Dijkstra, De Kemp and Bergkamp, 2012: 103).

However, in recent years the volume of budget support provided by all donors has decreased (Figure 1). This has to some extent been compensated by an increase in sector budget support, but by no means fully. The trend in SBS cannot be shown as this modality has only been registered since 2009. Sweden has allocated a larger share of its aid to GBS than the average DAC donor (green line in Figure 1). However, the share in total aid decreased sharply between 2008 and 2014. In 2015, there was a slight recovery.

This raises the question whether this decline in global GBS, and in Swedish GBS in particular, is related to the evidence on budget support's effectiveness. This effectiveness has been highly contested from the start. Budget support is perceived as a "risky" instrument, because the resources can easily disappear in the pockets of corrupt officials. For this reason, many evaluations have been carried out, and the topic also received attention in the academic literature. This report aims to review the evidence from donor-commissioned country evaluations, from existing comparative (synthesis) studies of those country evaluations and from cross-country quantitative studies.

**Figure 1. Trends in General Budget Support 2000-2015, in current US\$ billions and in %**



Sources: OECD/DAC, CRS for total ODA and total GBS (commitments), and [www.openaid.se](http://www.openaid.se) for Swedish data (disbursements)

It is, however, not the first review of the budget support evidence. Tavakoli & Smith (2013) have summarised the evidence from all the country evaluations carried out until 2011. A 2012 report of the Dutch Policy and Operations Evaluation Department (IOB) includes a comprehensive literature review of existing evidence, a comparative analysis of six country case studies, and econometric research to assess the impact of budget support (Dijkstra et al., 2012). Ronsholt (2014) carried out a slightly more recent review of the evidence on budget support for the Danish International Development Cooperation (DANIDA). Finally, the German Institute for Development Evaluation (DEval) recently carried out a systematic review of the evidence on budget support, applying rigorous criteria for assessing the evidence (Orth et al., 2017).

This report uses all sources including previous reviews. In formulating the research questions and in answering them, it follows the intervention logic of budget support as outlined below and based on Dijkstra et al. (2012). Most recent evaluations of budget support as well as the Orth et al. (2017) review use a slightly different policy theory. Later in this chapter I discuss the similarities and differences with these other approaches, and justify the choices made in this report.

## **1.2 The policy theory of budget support**

The benefits of the instrument are based on two properties that are the two inputs of this modality (Table 1). First, there is respect for ownership in the policy dialogue. This feature is supposed to distinguish budget support from the earlier balance of payments support that was accompanied by heavy conditionality, which often did not work (Collier et al., 1997; Dijkstra, 2002; Killick et al., 1998). Respect for ownership will bring better policy implementation than was the case with balance of payments support (output, middle column).

However, this respect for ownership presupposes some selectivity in the budget support allocation decision. Donors can have respect for ownership only if they have a basic level of trust in recipient country's policies (commitment to macro-economic stability and to poverty reduction), and perhaps also governance. The latter may include both the more technocratic aspects of governance, such as efficient, transparent and accountable public service delivery and absence of fiduciary risks, and the more political aspects, such as an elected legislative power, regular elections and respect for human rights (Leftwich, 1993). Different donors may have different views on the necessary governance conditions. In order to have this trust as the basis for ownership, donors must be selective in the choice of countries to which they provide budget support.

**Table 1. Original policy theory for budget support**

Inputs	Selectivity	Resources
Through-put	Respect for ownership in the policy dialogue	Alignment Harmonisation Predictability
Outputs	Improved policy implementation	Strengthening local systems as a result of use Lower transaction costs More macro-economic stability More resources for poverty reducing sectors More democratic accountability
Outcomes	Enhanced government effectiveness	
Impact	Greater poverty reduction	

Source: Dijkstra et al. (2012)

The second input is that the resources can be freely spent by the recipient government. This would make budget support more effective than project aid.<sup>6</sup> The fact that resources can be freely spent would lead to more alignment with government systems and to greater donor harmonisation – as compared to project aid. It was also expected that budget support would be more predictable than and less volatile than project aid.

The use of local systems can be expected to lead to positive “systemic effects” (Nilsson, 2004; Schmitt, 2017; White & Dijkstra, 2003) on local systems for planning, budgeting, implementation and monitoring (first output in the “resources” column). These systemic effects could well be reinforced by the policy dialogue, as it makes sense for budget support donors to focus the policy dialogue on an improvement of public financial management (PFM), in particular

<sup>6</sup> An additional reason for preferring budget support above project aid is that project money may be fungible: if the government would implement the project anyway, it can spend the resources at will.

of transparency and accountability of budgeting and reporting systems (White and Dijkstra, 2003: 550). The alignment to national systems and the donor harmonisation would reduce transaction costs for both recipients and donors. Budget support resources would also increase macro-economic stability and/or lead to additional resources for the social sectors. Furthermore, the fact that resources enter national budgets would imply that their use can be discussed in parliament and this would foster national democratic accountability, the last line under “outputs” in the “resources” column in Table 1.

The improved policy implementation and the additional resources that are now better spent would lead to enhanced government effectiveness in poverty reduction policies (outcome). In turn, this would lead to greater poverty reduction, both in terms of improved social indicators and in terms of reduced income poverty (impact).

In practice, this original policy theory was hardly applied. Although all donors had agreed to the Paris Declaration on Aid Effectiveness and thus had underlined the importance of “ownership” and the failures of conditionality, there was a certain amount of “schizophrenia” among the donor community. Many donor representatives were (also) of the opinion that conditionality in the earlier balance of payments support had not been enough and had to be strengthened (Renard, 2007; Rogerson, 2005). They saw budget support as an opportunity to continue to interfere with recipient countries’ policies. At the same time, and as discussed more extensively in chapter 2, donors applied only limited selectivity in the budget support allocation decisions. This limited selectivity implied that donors did not fully trust recipient countries’ policies and/or governance and it led to the return of conditionality in budget support (Knoll, 2008; Nilsson, 2004; Whitfield, 2009).

In several respects, conditionality changed and expanded as compared with the earlier structural adjustment programmes linked to balance of payments support. First, while under structural adjustment the IMF and the World Bank were the main actors on the donor side, now all multilateral and bilateral donors obtained a seat on the policy dialogue table (Swedlund, 2013; Whitfield, 2009).

And second, the focus of conditionality expanded; it did not only include policies but increasingly also governance aspects. And this governance not only included technocratic elements, for example quality and transparency of budgets and budget implementation, but also political elements such as respect for democracy and human rights (Dijkstra, 2013; Hayman, 2011; Molenaers, Cepinskas, & Jacobs, 2010; Swedlund, 2013).

All this leads to a slightly different intervention theory. Selectivity and respect for ownership in the policy dialogue cannot be taken for granted but must be investigated in evaluations. If both are limited, the policy dialogue accompanying budget support resembles the earlier conditionality and is more likely to be an “attempt to influence”. The donor input for this policy dialogue can then be called “preferences for the policy dialogue” (Table 2). As these preferences will not be the same for all donors, “donor harmonisation” becomes an issue for the policy dialogue as well. The reintroduction of donor attempts to influence also means that there may be an effect of the policy dialogue on most of the outputs listed in the “resources” column – in fact on all except the lower transaction costs.

Another change is that budget support now has two objectives: not only poverty reduction, but also improved policies and governance. The policy dialogue became crucial in achieving these improved policies and governance. And while in the original policy theory improving governance was limited to the more technocratic aspects and in particular PFM, governance now also included the more political aspects. Most donors see improved governance, both technocratic and political governance, as a means towards achieving more economic growth and greater poverty reduction. For this reason, improved governance appears as both outcome and impact variable in Table 2.

**Table 2. Actual policy theory on budget support**

Inputs	Selectivity and/or preferences for the policy dialogue		Resources		
Throughput	Harmonisation	Respect for ownership or attempt to influence in policy dialogue	Alignment	Harmonisation	Predictability
Outputs	Improved implementation of government policies, or of donor-desired changes in policy and governance, both technocratic and political governance		Strengthening local systems as a result of use Lower transaction costs More macro-economic stability More resources for poverty reducing sectors More democratic accountability		
Outcomes	Enhanced government effectiveness; Improved policy and governance				
Impact	Greater poverty reduction; Improved technocratic and political governance				

Source: Dijkstra et al. (2012).

### 1.3 Main questions

This leads to the following overall question and sub-questions for this report. The main research question is: What do we know about the effectiveness of budget support? The sub-questions are:

1. What are the intermediate effects (throughput and outputs) of GBS? Did the expected outputs come about and why or why not?

2. Do donors have influence on policies and governance through the policy dialogue? Why or why not?
3. What is the contribution of the two budget support inputs, policy dialogue and resources, through their influence on government policies and spending, to improvements in social indicators and to poverty reduction?

Starting from the policy theory as depicted in Table 2, the study examines the existing evidence along all steps of the framework. This means that the two inputs of budget support are considered, resources and respect for ownership or attempt to influence, and that two ultimate objectives of GBS are taken into account: both the original objective of poverty reduction, and the added objective of improving policies and governance. By following the intervention theory and to the extent that existing sources allow, explanations are also provided in order to answer the questions when and how GBS is effective.

Throughout this report, budget support will mainly be compared with project aid. Although the original policy theory had two counterfactuals, balance of payments support (for the policy dialogue) and project aid (for the resources channel), balance of payments support is hardly provided anymore. Yet it is important to investigate the degree of ownership and/or the extent of influence in the policy dialogue, because they also determine the degree of effectiveness of budget support as compared to project aid.

## **1.4 Previous studies**

The approach taken here is very similar to that used in most other evaluations and studies of budget support. This is not surprising, since all are based on the original “Evaluability study” (Lawson, Booth, Harding, Hoole, & Naschold, 2002), which in turn is based on the framework developed by Howard White for programme aid (White, 1996). The earlier evaluations of budget support have all used variants of the evaluability framework (IDD and associates, 2006; Lawson et al., 2005; Lawson et al., 2007).

More recent evaluations of budget support follow the Comprehensive Evaluation Framework (CEF) developed by the Budget Support Evaluation Steering Group of OECD DAC. A first version of this framework was piloted in budget support evaluations in Mali, Zambia, and Tunisia. After that, a final version was established (Van der Linde & Valmarana, 2012). Although it is a good evaluation framework, in my view the approach taken in this report is at least as valuable and in some respects possibly better. In what follows, I discuss the main differences.

First, the CEF includes capacity building or technical assistance as a third input of budget support. Although budget support is “sometimes accompanied by capacity development”, as Van der Linde and Valmarana (2012: 6) formulate it themselves when they define budget support, it is clearly not a necessary element of budget support. In my view it should therefore not be part of the intervention logic. Nevertheless, where relevant, I discuss the effects of technical assistance or capacity building in this report. Second, the CEF includes improvements in governance as a possible result at impact level that *may or may not* be analysed, depending on the specific partnership frameworks. In my opinion improving governance, including the more political aspects of it, has become a too important objective of budget support and cannot be omitted from the analysis. Third, the result chain of the CEF is rather complex while in general I think it is good to pursue parsimony in sketching the basic relationships. Another advantage of the simple structure of Table 2 is that the two inputs for budget support have separate results chains.

A fourth difference is that the CEF framework not only distinguishes between *levels* in the causality chain, but also between different *steps* in the analysis. While step 1 traces direct and induced effects of budget support, step 2 analyses the effects of government policies on expected outcomes and impact of budget support. The CEF framework recommends to apply quantitative analysis of specific government interventions to which budget support has contributed, by exploiting sectoral or geographical heterogeneity of government investments and using fixed effect regressions or difference-in-difference estimations. Step 3 then combines the results of steps 1 and 2 in order to identify the contribution of

budget support to development outcomes. This three-step approach rightly acknowledges that the results at, in particular, outcome and impact levels, may be influenced by many other factors, most notably by government policies. Step 2 allows for a separate analysis of these policies. Although my approach does not include this separate step 2, the intentions are the same. The effects of government (spending) policies are taken into account, and reported on, when answering subquestion 3.

With respect to the levels in the causality chain of the CEF, the two approaches are similar. The “direct outputs” level in the CEF is equal to the “throughput” level of Table 2, while the “induced outputs”, the next level in the CEF, are similar to the “outputs” in Table 2. All in all, I think my approach is broadly similar to that of the OECD and where it is different, it is simpler, more explicit about counterfactual(s) and more explicit about political governance as objective.

The earlier reviews also have somewhat different approaches. Ronsholt (2014) only covers donor-commissioned evaluations and does not systematically follow a policy theory on budget support. Furthermore, his study does not include the most recent evaluations, for example those of Uganda, Burundi, Burkina Faso, Ghana and Sierra Leone. Orth et al. (2017) is very comprehensive, covering 95 sources. It is a systematic review with explicit criteria for assessing the quality of the evidence, differentiating between “best” and “second-best” evidence. However, it uses somewhat arbitrary criteria for drawing conclusions, such as that a finding is only considered reliable if supported by at least ten sources – no matter whether these are original evaluations, or academic literature/reviews using these sources. It is based on a policy theory, broadly following the CEF. It traces the effects of all budget support inputs. In so doing, it considers budget support to have four inputs. Like Van der Linde and Valdarama (2012), it includes capacity building as a third input next to “resources” and “policy dialogue”, but then adds “conditionality” as a fourth. However, it is not so clear how “policy dialogue” and “conditionality” are defined and why these are considered separate concepts.

## 1.5 Methodology and sources used

This report is a literature review of the evidence of the effects of budget support. It examines the effects on the two ultimate objectives of general budget support, poverty reduction and governance. For both objectives, it traces the intermediate effects along the causal chain, following the intervention logic as sketched in Table 2. The review does not include separate studies of sector budget support, but most of the more recent evaluations of budget support include the effects of sector budget support. Given that in both cases the resources are transferred to the government, the effects, in particular of the resources, cannot be disentangled and will be taken on board in this report.

Given that the author was involved in an extensive literature review on the evidence of budget support in 2011 and 2012 (Dijkstra et al., 2012), and in order to keep the length of this report manageable, this report gives most attention to evaluations and studies that appeared after 2012, so between 2012 and 2017. The more recent literature includes evaluations, reviews and academic studies. The newer evaluations could be found on the website of the OECD/DAC. In order to find the academic literature, I searched the library of Erasmus University Rotterdam (connected with all academic libraries in the Netherlands) with “budget support” in keywords or title, and performed an additional search in the “Web of Science” database, again looking for “budget support” in the title. In addition, some additional academic sources were found by checking the references in the collected studies.

The different sections in this report start by briefly summarizing the evidence presented in Dijkstra et al. (2012). This includes highlights from its literature review, from the qualitative evidence based on comparing six country evaluations (Ghana, Mali, Tanzania, Zambia, Nicaragua and Vietnam) and from the results from the econometric analyses included in that study. The conclusions of this earlier study are considered to be of high validity, precisely because of the combination of literature review, quantitative and qualitative evidence (Dijkstra and De Kemp, 2013).

The sections then discuss the evidence from the more recent evaluations and academic literature. These recent evaluations have all been commissioned by the European Commission (sometimes together with the Independent Evaluation Group (IEG) of the World Bank). They use the CEF and have been subjected to extensive quality control through the presence of management teams in which many donor evaluation offices are represented, and reference groups. In general, I consider them to be of high and of roughly equal quality. All academic studies used have appeared in peer reviewed journals which guarantees their quality.

In order to draw conclusions, I compare the evidence from Dijkstra et al. (2012) with that from the more recent country evaluations, also taking into account the conclusions from the more recent synthesis studies and reviews. For some topics, academic studies can add evidence and/or help explaining certain findings and developments. Before presenting something as a finding from a study, I double checked whether the authors present evidence for a link between budget support inputs and a certain result. The evaluations carried out since 2012 have all used econometric analysis for drawing conclusions on the effect of budget support on, in particular, poverty indicators.

The focus in this report is on the effectiveness of budget support in low and lower middle income countries, thus excluding the evaluations of budget support in Morocco, Tunisia and South Africa.<sup>7</sup> As Lawson et al. (2014) shows, budget support has very different effects in these countries with much lower aid dependence and much higher institutional capacities. And Lawson et al. (2014) provide a very good summary of the budget support evaluations in these three countries.

The structure of this report is as follows. The sub-questions 1, 2 and 3 are answered in chapters 2, 3 and 4, respectively. Chapter 5 presents and discusses the main findings, and chapter 6 provides some policy recommendations.

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<sup>7</sup> In Morocco and South Africa, there was only sector budget support so these evaluations were already excluded for that reason.

## Chapter 2. Intermediate effects of GBS

This chapter assesses the intermediate effects of the two inputs of budget support, on the one hand the resources, and on the other hand the selectivity, or the preferences for the policy dialogue. It first looks at the throughput (Table 2), or the “direct outputs” (CEF) of budget support. For the resources these are alignment, harmonisation and predictability, and for the policy dialogue respect for ownership or attempt to influence, and also degree of harmonisation. Then the outputs (“induced outputs” in the CEF) are assessed, in particular for the resources channel (Table 2): lower transaction costs, macro-economic stability, and more resources for social sectors.

As depicted in Table 2, the alignment to recipient government systems for planning, budgeting, implementation, monitoring and evaluation would strengthen these systems. In addition, an increase in on-budget aid improves transparency of development efforts and may improve government accountability towards parliament and civil society. Yet, next to these systemic effects there may be effects from the policy dialogue on these outputs. Hence, these topics are left for the next chapter.

### **2.1 Throughput (1): Harmonisation, alignment, predictability**

The first question is whether and to what extent the throughputs harmonisation and alignment of budget support disbursements are achieved. Alignment is to a large extent determined by the volume of budget support relative to total aid, as budget support resources are channelled through national systems by definition. The extent of harmonisation depends on whether and to what extent donors use a joint assessment framework and harmonise their disbursement procedures. Dijkstra et al. (2012) concluded that only 31 countries (with more than 500,000 inhabitants) received a substantial amount of budget support, defined as at least 2.5 percent of total aid in the period 2002-2010. However, in the six selected case studies (Ghana, Mali, Tanzania, Zambia, Nicaragua and Vietnam, general budget

support constituted between 10 (Vietnam) and 42 percent (Tanzania) of total aid.

Table 3 adds data for the countries that have been evaluated more recently (again), starting with the four countries covered in Lawson's synthesis (Lawson et al., 2014), and ending with the recent evaluations of budget support in post-conflict states Burundi and Sierra Leone, where the situation is a bit different.

All in all, the extent of budget support and thus of alignment has been substantial in these countries. However, in almost all countries volumes of budget support have declined in recent years due to withdrawal of donors and lower amounts from those donors that continued. This has affected the annual averages negatively, particularly in Ghana where budget support dropped sharply after 2011. The exception is Sierra Leone where budget support increased in the final year, mainly due to the Ebola crisis. But in this country budget support has been very volatile during the full evaluation period (Lawson et al., 2016).

Most countries have a joint Performance Assessment Framework. However, harmonisation of assessment and of disbursement procedures is not complete, as many donors have variable tranches<sup>8</sup> with their own disbursement criteria. Yet, in most countries variable tranches do not constitute more than 20 percent of total volumes (Lawson et al., 2014: 31). This also holds for Ghana (Particip GmbH, 2017: 27). In Burundi and Sierra Leone, donors have maintained their own assessment and disbursement criteria. With these two exceptions the degree of harmonisation of assessment and disbursement criteria appears to be high, but this mainly holds for the earlier years. As shown below, with the increasing importance of governance criteria, the degree of harmonisation decreased.

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<sup>8</sup> A variable tranche is a portion (tranche) of budget support for which disbursement is dependent on meeting a certain condition (a policy or an outcome). This is opposed to the fixed tranche which will be disbursed anyway.

**Table 3. Budget support disbursements (inputs) in recent evaluation countries, annual averages**

	Mali (2003- 09)	Mozambique (2005-12)	Tanzania (2004-11)	Zambia (2005- 10)	Burkina Faso (2009- 14)	Uganda (2004- 13)	Ghana (2005- 15)***	Sierra Leone (2002-13)	Burundi**** (2005-13)
BS volume (US\$ million)	182	414	660	186	312	253	309	68	81
As % of ODA**	23	20	28	16	27	17	22	14	18
As % of total expenditure**	12	15	15	7	12	15	6	15	23
Number of BS providers	10	19	14	9	9	12	11	4	7

Source: Lawson et al 2014, and country evaluations of Burkina Faso, Burundi, Ghana, Sierra Leone and Uganda.

\*For Burkina Faso, Burundi, and Uganda percentages have been computed on the basis of estimated numbers from graphs. \*\*Amount was in EUR, converted against US\$ by using annual average inter-bank rate from OANDA website, accessed 21 August 2017.

\*\*\*As % of ODA holds for 2006-15 and is computed from OECD, CRS data on gross disbursements

\*\*\*\*Number for percentage of government expenditure excludes capital expenditure.

Earlier studies have shown that predictability of budget support was sometimes lower at the start of budget support but has improved in all cases (Dijkstra et al., 2012; IDD and Associates, 2006). According to a British study, the relation between commitments and disbursements was 96 percent on average for the period 2000-01 till 2007-08 (National Audit Office, 2008). Similarly, high levels of predictability of disbursements (of between 80 and 100 percent of commitments) hold for countries that have been evaluated more recently, Burkina Faso, Ghana, Mozambique, Tanzania, and Uganda. Budget support in the two post-conflict countries was much more volatile and less predictable. In Sierra Leone, for example, disbursements fluctuated between 60 and 170 percent of commitments. Yet, budget support was still more predictable than project aid (Lawson et al., 2016). In other countries volatility of budget support was limited, apart from a gradual decline visible from around 2010 onward.

In all countries, however, the within-year predictability has been much more problematic. Ghana, Tanzania and Mozambique are exceptions (Lawson et al., 2014: 31; Particip GmbH, 2017: 38). Most disbursements came at the end of the year and often later than planned, compromising budget management and sometimes leading to higher domestic debts, as in Mali (Lawson et al., 2011), or earlier in Rwanda and Mozambique (IDD and Associates, 2006), or to lack of productive use of budget support, as in Nicaragua (Dijkstra & Grigsby, 2010).

In recent years, predictability has decreased in most countries due to suspensions of budget support, often for reasons related to political issues, corruption or human rights violations. This is also concluded by Orth et al. (2017).

In summary, budget support resources are aligned to government systems by definition, and the volumes of budget support in the evaluation countries have been high. In recent years, however, volumes have declined thus decreasing the degree of alignment. In most countries, donors have achieved a high degree of harmonisation in assessment and disbursement criteria, at least in “normal” periods, in which governance issues did not dominate the policy dialogue yet. Within-year predictability remained a cause for

concern in many countries, with donors disbursing later than promised and most flows coming at the end of the year. Budget support volatility was not an issue in most countries. The between-year predictability of budget support disbursements was quite good, but it decreased in recent years due to governance-related suspensions.

## **2.2 Throughputs (2): Selectivity, ownership and harmonisation**

As already pointed out in chapter 1, many advantages of budget support are based on respect for ownership. This presupposes some selectivity in choosing the countries for providing budget support. Given the changes in the application of budget support, both selectivity and respect for ownership cannot be taken for granted it must be investigated to what extent donors have complied with this input and throughput.

For most donors, entry criteria include(d) a commitment to poverty reduction policies, a stable macro-economic environment, a minimum level of budget transparency and quality of public financial management (PFM), and good governance, including low corruption, respect for human rights and the rule of law, and some degree of democratic accountability. However, in practice countries began to receive budget support without meeting one or more of these criteria. While the macro-economic situation was usually good and countries had Poverty Reduction Strategies (although there were sometimes doubts on commitment to them), the quality of PFM was often weak and the governance situation was far from ideal (Dijkstra et al., 2012).

In a quantitative analysis, there proved to be little relation between governance scores in 2000 and received budget support during 2002-2010. On the other hand, there was a high correlation between qualifying for the HIPC initiative in the early 2000s and the receipt of budget support during that decade (Dijkstra et al., 2012). This points to path dependency being more important than selectivity in budget support allocation.

In all countries for which evaluations are available, the institutional mechanism for conducting the policy dialogue around budget support is defined in a Memorandum of Understanding (MoU) between the recipient government and the donors. These MoUs usually contain Underlying Principles (UP), to which countries must adhere for the long-term continuation of budget support, and Performance Assessment Frameworks (PAF) containing performance indicators that are monitored and adjusted annually.

Lawson et al. (2014) lists the UP for Tanzania as a representative example for most countries. Next to sound macro-economic management, commitment to poverty reduction, sound budgeting and PFM systems, the UP also include respect for human rights, rule of law, democratic principles, independence of the judiciary, accountability of government to its citizens, and active fight against corruption. It is clear that this list is very similar to the eligibility criteria listed above, implying that most recipient countries did not comply with these criteria at the start of budget support. This confirms the limited selectivity.

Most earlier evaluations and studies of budget support conclude that the attempt to influence policies and governance has come to dominate the respect for ownership.<sup>9</sup> In addition, the policy dialogue is not just about policies or technocratic aspects of governance such as PFM, but increasingly also about more political aspects of governance, including the extent of democracy, independence of the judiciary, respect for the rule of law and for human rights (Dijkstra et al., 2012; Hayman, 2011; Swedlund, 2013).

With respect to the Performance Assessment Framework (PAF), it generally contains indicators for macro-economic stabilisation, improvement of PFM, and for poverty budgets and policies. The extent of country ownership of the indicators varies between countries and also over time, but usually it is not very high (Dijkstra

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<sup>9</sup> This holds, at least, for low or lower middle-income countries. Ronsholt (2014) concludes that respect for ownership is higher in countries with lower aid dependence and fewer donors, thus in higher middle-income countries.

et al., 2012). Among the countries more recently evaluated, there was very little ownership in Burundi, Burkina Faso, Mali, and Sierra Leone.<sup>10</sup> In Mozambique, Tanzania and Uganda, the number of indicators and their level of ambition increased over time on the instigation of the donors (Lawson et al 2014), often towards “unrealistically high” levels (IEG and Particip GmbH, 2016: 15). This also points to decreasing ownership. In Ghana, the leading role of the government has also decreased over time, despite a decrease in the number of performance targets (Particip GmbH, 2017: 55). In Sierra Leone, the PAF itself was small but all involved donors had separate, additional disbursement indicators (Lawson et al., 2016). The recent reviews of budget support also conclude that ownership is limited, and that conditionality dominates the policy dialogue (Orth et al., 2017; Ronsholt, 2014).

In general, and although PAF indicators are considered disbursement triggers, it is usually not defined which percentage of the indicators must be met, and different donors have different ideas on the relative importance of different indicators. In sum, although in general there is a large degree of harmonisation in the PAFs, it is not complete. The extent of harmonisation, especially in the assessment, has further decreased in recent years because PAFs have come to include indicators related to political governance.

Molenaers (2012) studied five budget support donors and found that three of them were of the view that political governance should be part of the regular policy dialogue around budget support. She shows that three donors assess the eligibility criteria (so the UPs, as these are similar) annually, and that in all five countries headquarters play an important role in the decisions on eligibility and on suspensions. Given that officers in headquarters are closer to their political superiors and also to the media, these decisions are likely to be heavily influenced by domestic political factors in the donor country.

Studies and evaluations coincide that the UPs are formulated in vague terms, that it is not specified what is considered as a breach, and that clear procedures for assessing the principles or for defining

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<sup>10</sup> This evaluation specifically notes lack of ownership of the sectoral ministries, health and education (Lawson et al., 2016).

corrective actions are lacking. This leaves a lot of discretion with individual donors. When asked what they consider a breach of the UPs (Molenaers 2012), one donor said that a fundamental break with the UPs would be a reason for suspending budget support, while another argued that lack of progress with the UPs would already be sufficient. Three had an intermediate position, arguing that a deterioration in the UPs would be a reason for withdrawing budget support. In conclusion, harmonisation of the UPs is limited to their formulation and does not cover concrete assessment criteria or procedures for how to handle perceived breaches.

Overall, it can be concluded that selectivity at entry was limited and that donors had difficulties in respecting ownership of the recipient government. This lack of respect for ownership seems to have increased over time. There proves to be a vicious circle, increasing donor dissatisfaction with country performance, often on governance issues, leading to ever higher ambitions for the policy dialogue, in turn causing more dissatisfaction. This has negatively affected the quality of the policy dialogue but has also led to budget support suspensions and withdrawals. All this compromises the original technocratic idea of budget support providing long-term predictable financing for poverty reduction. It also reduces donor harmonisation. Although there are joint structures for the policy dialogue in the form of UPs and PAFs, there is very little harmonisation of actual assessments of these principles and of performance.

## **2.3 Outputs (1): Transaction costs**

Harmonisation and alignment should lead to lower transaction costs as compared to project aid. Evaluations generally conclude that transaction costs of budget support are still somewhat high, for example, due to (too) many negotiations on – often too large – joint assessment frameworks. In addition, they observe that there is still a lot of project aid. However, Bigsten and Tengstam (2015: 79) estimate, based on data from Sida on the different administrative costs on the side of the donor, that transaction costs of budget support are only one-third of those of project aid. To this we can

add reduced transaction costs for the recipient government given that existing local systems for planning, budgeting, implementation and reporting are used instead of separate systems for each project. Overall budget support has been accompanied by much lower transaction costs per aid dollar spent than project aid, for both donor and recipient (Dijkstra et al., 2012).

The evaluations of Mali and Burkina Faso conclude that transaction costs have decreased over the evaluation period. In Ghana they remained low. However, some other recent evaluations, in particular those on Mozambique, Tanzania, Uganda and Zambia, conclude that transactions costs have recently increased due to the increasing focus on political topics in the policy dialogue and the diverging views among donors on dealing with these topics. In most countries, the share of budget support in total aid has declined in recent years, which has increased transaction costs per dollar spent in this modality (see also Orth et al. 2017). In the countries where harmonisation among donors is still limited, Burundi and Sierra Leone, transaction costs have not decreased much at all (ADE, 2015; Lawson et al., 2016).

In conclusion, budget support has decreased transaction costs but these benefits have decreased over time due to more intensive governance discussions and lower volumes of budget support.

## **2.4 Outputs (2): Macro-economic stability, public spending and revenues**

Programme aid, including budget support, has been important in several countries for achieving macro-economic stability in the sense of reducing budget deficits and inflation. This was especially the case in countries like Nicaragua, Mozambique and Uganda in the early 1990s – countries that then had just emerged from civil wars. The same positive effect on macro-economic stability was found in the recent budget support evaluations in Burkina Faso, Burundi and Sierra Leone (ADE, 2015; Lawson et al., 2016; Particip GmbH, 2016).

The evaluation of budget support in Burkina Faso observes that next to resources, the policy dialogue, technical assistance, and external actors like IMF and the West African Economic and Monetary Union played a role in reducing the budget deficit (Particip GmbH, 2016: 20). In Burundi, budget support was initially used to pay external arrears on debt in order for the country to qualify for the HIPC initiative, thus also contributing to macro-economic stability. In Sierra Leone, budget support helped to reduce the deficit during the global financial crisis in 2009 and during the Ebola crisis in 2014. In the other countries, macro-economic stability was usually achieved before budget support started and was then maintained. In some other countries part of budget support resources has been used to pay-off domestic debts, thus fostering macro-economic stability in the future. This was found for Mali, Nicaragua and more recently for Burkina Faso.

In some cases, budget support endangered this stability temporarily, for example when governments had to borrow on the domestic market in order to compensate for late or failing budget support disbursements. In earlier years this happened in Malawi, Nicaragua, Mozambique and Rwanda (IDD and associates, 2006). Late or suspended disbursements, often as a result of variable tranches, led in some years to increased domestic borrowing more recently in Mali, Sierra Leone, Uganda and Zambia (IEG and Particip, 2015; Lawson et al., 2014; Lawson et al., 2016).

In Ghana, budget support resources helped to cushion the effects of external shocks and temporary falls in government income, for example after the 2008 crisis. Macro-economic stability was also an issue in the policy dialogue. Budget deficits and public debts began to increase from 2006 onwards, despite the received budget support and despite higher tax and non-tax (oil) income. This was due to large increases in public wages and high public spending in pre-election periods (Particip GmbH, 2017: 39-40). Budget support could not prevent these irresponsible macro-economic policies. However, the collective suspension of budget support at the end of 2013 contributed to a new agreement of the government with IMF in 2015, after which budget support was resumed.

In general, the most important financial effect of budget support has been to increase government expenditure. Dijkstra et al. (2012) show econometrically that an increase in budget support of 1 percent of GDP is accompanied by an increase in government expenditure of around 0.6 percent of GDP.<sup>11</sup> This would suggest that on average, 60 percent of budget support resources is used for additional spending. Almost all country evaluations of budget support confirm that there is a link between budget support and additional spending. Nicaragua proved to be an exception. In this country, uncertain and late disbursements prevented the government from spending these resources. Instead, they were all used for reducing domestic debts.

Of the four evaluations synthesised in Lawson et al. (2014), Mali, Mozambique and Tanzania also saw increased government expenditure as a result of budget support. Although in Zambia total government expenditure as percent of GDP did not increase, spending for priority sectors proved to exceed budget support resources. The evaluators conclude that this increase was the result of budget support resources, policy dialogues for general and sector budget support, and ownership (De Kemp, Faust, & Leiderer, 2011).

An important assumption in achieving increased government spending with budget support is that there are no negative incentive effects on government revenues. In their econometric analysis, Dijkstra et al. (2012) show that there is no effect of budget support on tax revenues. This effect is confirmed by the six cases examined in their study, as well as by Orth et al. (2017). At the same time, Orth et al. (2017) report that revenues did not substantially increase, thus possibly endangering the sustainability of the achievements of budget support. The more recent country evaluations have mixed conclusions on the behaviour of tax revenues. While concern about limited progress in increasing tax revenues is expressed for

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<sup>11</sup> For the period 2002-2010. Instrumenting for budget support leads to a slightly lower coefficient (around 0.5), pointing to some endogeneity and showing that part of budget support may be a response to expected government deficits.

Burundi,<sup>12</sup> Sierra Leone and Uganda, government revenues substantially increased in Burkina Faso, Ghana, Mozambique and Tanzania.

Spending on priority sectors as defined in the Poverty Reduction Strategies increased in virtually all countries as a result of budget support (Dijkstra et al. 2012, Ronsholt 2014, Orth et al. 2017). There were large increases in spending for priority sectors in most recently evaluated countries: Burundi, Burkina Faso, Mali, Mozambique, Sierra Leone Tanzania and Zambia. Uganda and Ghana are exceptions. In Uganda, spending for the priority sectors health, education and water increased until 2004, but stagnated later due to changed government priorities and reduced budget support (IEG and Particip, 2015). In Ghana, pro-poor spending as share of total spending and as share of GDP decreased between 2006 and 2015. Yet, budget support was able to ringfence some of this spending, in particular until 2012 (Particip, 2017: 39, xiii).

What the priority sectors are varies from country to country, but education and health have been important (almost) everywhere. Some studies have tried to establish effects on spending for these sectors econometrically. Dijkstra et al (2012) found that an increase in budget support by one percent of GDP led to an increase in health expenditure of between 0.14 and 0.37 percent of GDP. When instrumenting for budget support the coefficient was highly significant. They found a larger average effect on education expenditure, but this coefficient was not significant due to an insufficient number of countries for which data on education spending is available. Fernandes Antunes et al. (2013) examined the effect of budget support on health expenditure, in particular, and conclude that there was no effect. They used lags for all variables in order to control for endogeneity, applying a system GMM model. However, total government expenditure was one of the independent variables in their model and it may well be that budget support influenced health spending through its effect on total spending. Another limitation of this study is that the authors did

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<sup>12</sup> Tax revenues first increased substantially to 15.2% of GDP in 2011, but then decreased again to 12.8% in 2013 (p. 58).

not include the budget support from the World Bank (Poverty Reduction Support Credits, PRSCs) in their data.

Table 4 lists the conclusions of the country evaluations on budget-support-induced spending increases for selected (as per these evaluations) priority sectors. These conclusions are usually based on a combination of quantitative and qualitative sources, such as interviews.

A recent evaluation of the effects of the withdrawal of the Netherlands from 18 priority countries around 2012 provides further evidence. It includes case studies of six countries, four of which had received Dutch budget support (Burkina Faso, Nicaragua, Tanzania and Zambia). For these four countries, the evaluation concludes that expenditure for the priority sectors would have been higher if Dutch budget support had continued (de Kemp & Lobbrecht, 2016).

The overall conclusion can be that budget support has contributed to achieving or, depending on the situation in the recipient country, maintaining macro-economic stability. In most countries, it has also led to increased spending for priority sectors as defined in the Poverty Reduction Strategies. On average, budget support does not seem to have induced a decrease in domestic tax revenues but there are large differences between countries.

**Table 4. Sectors benefiting from expenditure increases due to Budget Support**

	Education	Health	Roads	Water	Agriculture	Social	Good governance
Burkina Faso 09-14	Yes	Yes		Yes			
Burundi 05-13	Yes	Yes					
Ghana 04-10	Yes	Yes					
Ghana 05-15		Yes, until 2012			Yes	Yes	
Mali 03-09	Yes	Yes				Yes	
Mozambique 05-12	Yes				Yes		Yes
Nicaragua 05-08				No increase over this period			
Sierra Leone 02-13	Yes	Yes	Yes				
Tanzania 04-11	Yes		Yes				
Uganda 04-13*	Yes	Yes		Yes			
Vietnam 01-06**	Yes	Yes		Yes			
Zambia 05-10	Yes				Yes		

Note \*. Government priorities changed and budget support was reduced, so hardly increases after around 2007.

Note \*\*. Interpretations vary on whether increases were due to budget support.

Sources: Dijkstra et al (2012) for Ghana 04-10, Nicaragua, Vietnam, Lawson et al (2014) for Mali, Mozambique, Tanzania and Zambia, and more recent evaluations for Burundi, Burkina Faso, Ghana 05-15, Sierra Leone and Uganda.

# Chapter 3. Effects of the policy dialogue

The main focus in this chapter is on effects of the donor attempts to influence, often called “policy and institutional effects” of budget support (Van der Linde & Valmarana, 2012). But there is also attention for the systemic effects. Systemic effects are usually defined as “flow-of funds” effects: the effect of the use of government systems for planning, budgeting, implementation and monitoring on the quality of these systems and on domestic democratic accountability. But as several evaluations note, there may also be systemic effects of the policy dialogue, in particular on policy planning, coordination and implementation and also on democratic accountability, to the extent that civil society actors participate in the dialogue. On the other hand, there can be negative systemic effects of the policy dialogue on domestic accountability if it leads to more outward accountability, to the donors, instead of inward accountability, to citizens and parliament.

After discussing the systemic effects of the policy dialogue on policy making, this chapter continues by analysing the systemic plus policy dialogue effects of budget support on PFM and domestic accountability, and the influence of donors on poverty reduction policies and good governance. The effect of dialogue and resources on poverty *expenditure* has already been dealt in Chapter 2. In all these areas, it is often difficult to disentangle the influence of the policy dialogue from that of other factors, in particular the technical assistance or capacity development programmes that have been set up and financed by donors.

## **3.1 Systemic effects of the policy dialogue on policy making**

Earlier evaluations and studies concluded that the dialogue around budget support has increased the coordinating role of the Ministry of Finance and on the coordination between ministries (De Renzio, 2006). Some more recent evaluations confirm this. Budget support

has increased the focus on indicators and on results in the policy process in Mali. In Tanzania, Mozambique and Zambia the number of indicators in the PAF was too high and they were often donor-driven. This led to lower participation of high level civil servants (Lawson et al., 2014). This hampered positive systemic effects on national policy making. In Sierra Leone, the policy dialogue helped to set up a framework for establishing and monitoring national policy targets that had not existed before (Lawson et al., 2016). In Burundi and Burkina Faso such positive effects could not be observed. In Burundi the policy dialogue was fragmented by donor and by sector. In Burkina, there were initially separate dialogue frameworks for budget support and for poverty reduction. In 2008 the two frameworks were merged, which led to some increase in ownership and also to participation of civil society. But the quality of sectoral dialogues varied.

In Ghana, budget support contributed to modest improvements in policy formulation and intra-sector policy coordination. Over time, the interest of both the government and the donors in the policy dialogue diminished. On the donor side, Ghana's achievement of middle income status in 2010 was perceived to lead to lower leverage for budget support. The government increasingly lost interest due to improved access to other financing sources, such as oil income, Eurobonds and aid from new donors like China. All this reduced the systemic and other possible effects of the policy dialogue.

All in all, the results are mixed. An important condition for seeing positive systemic effects on domestic policy making seems to be that donors succeed in coordinating their preferences for the PAF focusing on a limited number of indicators. In addition, volumes of budget support need to be sufficiently large (relative to other sources) in order to keep the attention of high-level public officers and the trust of donors that the policy dialogue has some leverage.

## **3.2 Public Financial Management**

PFM indicators constitute an important part of the PAFs and of the dialogue. Furthermore, the perceived fiduciary risks involved in

budget support have induced donors to provide high levels of technical assistance in this area. While improvements in PFM can be registered, it is difficult to conclude on whether and to what extent they are due to systemic effects, donor influence through the policy dialogue, or technical assistance.

Many evaluations and also synthesis studies conclude that the use of government systems for planning and budgeting has improved budget transparency (Dijkstra & Grigsby, 2010; Lawson et al., 2014; Ronsholt, 2014; Schmitt, 2017). They also report, however, that the share of budget support and on-budget aid<sup>13</sup> in total aid is low. For example in Mozambique, 46% of aid was off-budget (Schmitt, 2017). In Uganda, the share of off-budget aid from all sources<sup>14</sup> increased over the evaluation period to 84 percent (IEG and Particip, 2015: 13).

Most earlier evaluations conclude that budget support has led to some improvements in PFM and that indeed part of these improvements are due to the technical assistance that has accompanied budget support (Dijkstra et al., 2012; IDD and Associates, 2006). This is also reported by the more recent syntheses of evaluation results (Ronsholt 2014, Orth et al. 2017). Orth et al. (2017: 50) conclude that the inputs “policy dialogue” and “capacity development/technical assistance” have a positive effect on PFM systems while there is not sufficient evidence for a separate positive effect of the resources (the systemic effect). The combination of financial and non-financial inputs is definitely effective. They also observe that improvements in PFM, in particular, depend on the political will of the recipient government to carry out PFM reforms. In a regression analysis carried out across 100 countries, De Renzio, Andrews and Mills (2010) find that budget support is associated with higher quality of PFM systems.

Lawson et al. (2014) report improvements in budget transparency in Mozambique and Tanzania, but not in Mali and Zambia. They also note that despite the improvements, there are still substantial PFM problems in all countries, for example in

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<sup>13</sup> On-budget aid is all aid that is a) transferred to the government and b) included in the national budget.

<sup>14</sup> So including from NGOs.

budget credibility and in expenditure control, in particular with regard to local governments or other autonomous agencies. The Uganda evaluation comes to similar conclusions. Budget support, through the policy dialogue and accompanying technical assistance, has contributed to substantial improvements in the quality of budgeting and planning and in the efficiency of public spending, especially in the earlier period. But budget credibility is still weak<sup>15</sup> and there is limited transparency in inter-governmental fiscal flows. In addition, from 2009 onward the indicators for PFM are deteriorating. In Ghana, there have been some improvements in PFM, such as harmonisation of the budget classification structure, improved budget transparency and improved legislative environment for, in particular, auditing. The evaluators conclude that budget support has contributed to this progress. Burundi has also witnessed some progress in PFM but continues to face problems of budget credibility, budget execution, and expenditure control. In Sierra Leone, budget support and the accompanying technical assistance had a modest contribution to increased budget transparency and improved PFM systems. Despite having indicators in the PAF for reforms to payroll and procurement systems, political resistance prevented these indicators from being met. From 2010 onwards, the quality of PFM systems has deteriorated somewhat (Lawson et al., 2016).

All in all, most of the more recent evaluations confirm the earlier conclusions that the combination of the use of domestic systems, attention in the policy dialogue, and technical assistance has led to improvements in PFM. However, in Uganda and Sierra Leone, the PFM indicators are deteriorating in recent years. In Uganda this coincides with, and may be due to, much lower budget support volumes, but this is not the case in Sierra Leone.

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<sup>15</sup> The evaluators note that budget support is in part responsible for the lack of budget credibility, as the first “supplementary budget” in the year is a result of the late confirmation by donors of their contributions (IEG and Particip 2015:37).

### 3.3 Domestic accountability

There are many definitions of accountability. In general, accountability involves three stages (Bovens, 2010; Lindberg, 2013): first the agent (A), held to account in a certain domain, must provide information on that domain to the accountee or principal (P), second P may ask questions and A is obliged to answer, explain or justify its behaviour, and third, P assesses A's performance and may apply sanctions. When speaking of democratic accountability, the agent A is the government and the principal P is the population at large, or their representatives or spokespersons like parliament, civil society and media. This can also be called vertical accountability, as it involves the relations between state and citizens. Horizontal accountability is about the relation between different organs of the state. It involves the relation between the executive and formal oversight institutions such as Supreme Audit Institutions, ombudspersons, or parliaments.<sup>16</sup> Both types of accountability will be fostered with increased transparency of public budgeting and reporting systems, so there is a clear relationship with improved PFM. In analysing the effects of budget support on democratic accountability, many studies make a distinction between the supply and the demand side. The supply side of democratic accountability focuses on public sector institutions and the demand side on citizens, civil society or media.<sup>17</sup>

This section starts with briefly analysing the possible systemic effects of the policy dialogue on democratic accountability, then continues with possible effects on, first, horizontal and then vertical accountability.

In several countries, civil society representatives were allowed to participate in sectoral dialogues but hardly ever in the national dialogue on general budget support. Ghana is an exception. In this country, donors made efforts to have civil society participate in the policy dialogue and in the review of the PAF. But overall, the

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<sup>16</sup> Parliaments can be seen as involved in both horizontal (as they are public sector institutions) and vertical (as they represent citizens) accountability.

<sup>17</sup> Again, parliaments can be on both sides.

systemic contribution of budget support in this area has been limited.

Orth et al. (2017: xvii) conclude that budget processes as well as Supreme Audit Institutions improved as a result of budget support, but that it is not clear whether that is due to systemic effects of the resources or to policy influence. Lawson et al. (2014) report improvements in Supreme Audit Institutions (SAI) in Zambia, Mozambique and Tanzania. They observe that SAIs also benefitted from increased budgets, facilitated by GBS resources. The same combination of GBS-induced attention and resources has benefitted the SAI in Uganda (IEG and Particip, 2015: 38). In Sierra Leone budget support contributed to the setting up of institutions like a SAI and parliamentary accounts committees. This led to more transparency of budgets and accounts. In Mali, however, the donors had pressured the government to include indicators on decentralisation, public sector reform and for the establishment of an independent Court of Audit but they were not met. In Ghana, the policy dialogue and accompanying capacity development strengthened some accountability institutions such as Ghana Audit Service, the Commission on Human Rights and Administrative Justice, and the Public Accounts Committee of the Parliament. However, these institutions are still too weak to carry out their oversight role well (Particip, 2017: 55, 59, 60).

Orth et al. (2017) conclude that there are no consistent positive effects of budget support on the demand side of accountability, which they define as consisting of parliament and civil society. This is confirmed in the more recent evaluations, showing mixed results. On the positive side, in Sierra Leone the budget support-induced increased transparency of budgets and accounts led to more awareness in the media and civil society of governance and corruption issues. In Burkina Faso, budget support contributed to improving the oversight of PFM and of corruption issues by civil society (Particip, 2016). In Ghana, budget support donors have helped further strengthening civil society organisations and their role in, in particular, sector policies, has increased (Particip, 2017). On the other hand, in Uganda the parliamentary Public Accounts Committee publicly debates SAI reports but is overburdened and

has been unable to consider all. For Burundi, evaluators conclude that the main effect of budget support is an increased accountability to donors, away from parliament and civil society (ADE, 2015).

Schmitt digs deeper into the effects of budget support on domestic accountability in Mozambique (Schmitt, 2017). He confirms the evaluation result (ITAD, 2014) that budget support strengthened the institutions at the supply side of accountability, including the SAI. But there has been less support for institutions at the demand side. Yet, he observes that the number of civil society organisations active in accountability issues has increased. Representatives of these institutions confirm that budget support has led the government to improve PFM and transparency, but that this transparency is still limited, especially with respect to budget execution, revenues and at local level. Overall, democratic accountability in the country is still weak.

In sum, the systemic effects of budget support on increasing domestic democratic accountability seem to be limited. The policy dialogue is between donors and executive, and the use of local systems and budgets did not automatically generate interest among parliament or civil society actors. However, budget support and accompanying capacity building activities did lead to improvements in the supply side of domestic accountability, increasing transparency of budgets and of budget execution – through strengthening the SAIs and related oversight institutions. Direct donor support to institutions on the demand side was usually more limited. Yet in some countries (Burkina Faso, Sierra Leone) parliaments, media and/or civil society have grasped the increased opportunities to hold governments to account.

### **3.4 Corruption**

Budget support is often said to entail fiduciary risks and thus to fuel corruption. It is always difficult to measure corruption itself. Most existing measures are based on perceptions and suffer from severe weaknesses (Arndt & Oman, 2006; Kenny, 2017). When looking at the relation between the amount of budget support received (as percent of GDP) between 2002 and 2010, and the change in the

World Governance Indicator for Control of Corruption between 2000 and 2010, there proves to be a weakly significant positive correlation (Dijkstra et al., 2012). This positive association between budget support and the reduction of corruption is the more surprising, as there was no relation between budget support and the level of the corruption indicator in 2000. However, the qualitative evidence from the six cases in that same study shows that there are only limited effects of budget support on controlling corruption. But there is certainly no proof for budget support increasing corruption in the recipient countries. Ronsholt (2014) states that no conclusion is possible on the effect of budget support on corruption.

Budget support contributed to improvements in the legislative and institutional framework for combating corruption in Mozambique, Sierra Leone, Tanzania, Uganda and to some extent also in Ghana (Lawson et al., 2014, IEG and Particip, 2015, Lawson et al., 2016, Particip, 2017). Of course, these are first steps and they are in itself not sufficient for eliminating corruption. To the contrary, when there is more oversight and more awareness, it is likely that more corruption scandals appear. A common conclusion of these evaluations is that although more corruption is detected, government could do much more in prosecuting the culprits. But there are also cases with more limited success. In Burundi, the lack of coordination of donors in the policy dialogue and in the provision of technical assistance led to disappointing results in the building up of institutions. If anything, corruption increased in the evaluation period (ADE, 2015). In Burkina Faso, budget transparency increased, the Court of Audit was strengthened and an anti-corruption law was adopted and this helped civil society in its fight against corruption. But the lack of government commitment in this area hampered success (Particip GmbH, 2016: 23,26). Budget support did not manage to adequately deal with endemic corruption among the highest government levels.

Orth et al. (2017) conclude that budget support has a positive effect on the efforts in monitoring corruption, but that prosecution and punishment is still limited. These authors also state that contrary to some expectations, there is no evidence of budget support having

increased corruption. This seems to be an adequate summary of the existing evidence.

### **3.5 Poverty reduction policies**

The experience with structural adjustment policies was that donor attempts to “buy” policy reforms with conditionality did not work. Political factors within recipient countries determine whether policy reforms are carried out (Collier et al. 1997; Dijkstra, 2002; Killick, Gunatilaka, & Marr, 1998). However, the case of the policy dialogue around budget support could be slightly different, in particular with regard to poverty reduction policies. Around 2000 all countries, both donors and recipients, have agreed to achieving the Millennium Development Goals by 2015. Although there may be more or less agreement on, and government commitment with, the countries’ Poverty Reduction Strategies, these strategies are usually focused on achieving the MDGs. This may facilitate a dialogue focusing more on the “how” of achieving these goals than on the “what”. This does not exclude of course that actual choices may bring fundamental disagreements to the fore.

However, and in line with the centrality of the MDGs, most Poverty Reduction Strategies targeted mainly the social sectors and sometimes some other priority sectors like water and roads. They seldom included strategic analysis of how government policies would reduce *income* poverty (see also Lawson et al., 2014). This lack of insight also held for donors participating in the policy dialogue. The policy theory of budget support is relatively silent on how budget support is supposed to lead to income poverty reduction. On the one hand, donors expected economic growth to trickle down to the poor, and on the other, they expected that improvements in social and physical infrastructure for the poor (health, education, roads) help to increase their incomes.

In practice donors seem to have had limited influence on poverty reduction policies. In Vietnam and to some extent in Nicaragua (after 2007) governments themselves carried out policies that targeted the poor and there was no donor influence on these policies (Dijkstra et al., 2012). On the other hand, donors did not manage to

change the maize subsidies in Zambia that mainly benefited the rich farmers and not the poor (De Kemp et al., 2011). In Mozambique, donors were not able to change ineffective agricultural policies either (ITAD, 2014).

In Uganda, the donors have not been able to prevent the change in priorities by the Ugandan government to productive infrastructure and military expenditure. From 2008 onward, the policy dialogue was held with the Office of the Prime Minister as central actor instead of with the Ministry of Finance and Economic Development. This implied that donors had even less influence on sector policies. In Burkina Faso, the donors did not give much attention to sectors that were important for income poverty reduction, such as agriculture or small and medium enterprises (IEG and Particip, 2015: x). And they hardly discussed the high population growth, another important factor influencing poverty reduction. In Ghana, the policy dialogue contributed to strengthening targeted social interventions, which, however, are reported to have “modest results” (Particip, 2017: 79). In Sierra Leone the effect of the policy dialogue on health and education sector policies was limited. In health, the policy dialogue in Sector Budget Support was more effective in supporting reforms, notably in payroll policies.

A common observation in many evaluations is that the policy dialogue focused too much on setting and monitoring performance levels on a large number of individual indicators, while neglecting strategic discussions on solving bottlenecks for public service provision or economic growth (IEG, 2010; Particip GmbH, 2016; Lawson et al., 2014, Ronsholt 2014; Particip, 2017). In the more recent years,<sup>18</sup> policy dialogues have focused increasingly on governance issues, again reducing the attention for poverty policies.

Holvoet and Ingberg (2015) examine the effect of two policy dialogue-related instruments on the increase in female primary enrolment rates, using Qualitative Comparative Analysis (QCA) for 14 African countries. The two instruments are, on the one hand, the use of sex-disaggregated indicators for primary enrolment in the

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<sup>18</sup> This varies by country, in Nicaragua it started already in 2007 (Dijkstra, 2013).

PAF, and on the other, the establishment of gender working groups. They include several over variables that may explain increased girls' enrolment, namely aid, aid to education, income level, the existence of free primary education and the extent of institutional gender discrimination in the country. They find that both sex-disaggregated indicators and gender working groups have a high correlation with positive outcomes. In highly aid dependent countries with low gender discrimination, gender working groups, which they call "soft incentives", are sufficient for increasing female primary enrolment. In countries with more gender discrimination, both gender working groups and sex-disaggregated indicators ("hard incentives") are necessary for a positive outcome, but they are not sufficient.

In conclusion, the example of the donor influence on improving female enrolment shows that donors have some possibilities for influence. But the evidence of donors using these opportunities for influencing poverty reduction policies is scarce. Donors were often focused too much on too many individual performance indicators, at the cost of a more strategic discussion on how obstacles in public service provision could be removed or economic growth could be fostered. Donors were also often hindered by a lack of knowledge on how budget support or government policies would be able to reduce income poverty. However, and in line with the previous experience under structural adjustment, where donors tried to make policies more pro-poor in areas where this conflicted with (perceived) strategic or political interest of the government, they have not been successful.

### **3.6 Political governance and human rights**

As discussed above, issues like free and fair elections, protection of rule of law and of civil and human rights were usually included in the Underlying Principles but increasingly also formed part of the policy dialogue and of the PAF.

The IOB evaluation finds that there is a slight positive correlation between the amount of budget support received between 2002-2010, and improvements in some of the World Governance Indicators between 2000 and 2010. Apart from control of

corruption (discussed above), this also holds for “voice and accountability” and “rule of law” and for an overall governance score based on factor analysis (Dijkstra et al., 2012). However, the coefficients are small, and these correlations do not necessarily mean causal relations: other factors may be of influence and the causality may be the other way around.

As also mentioned above, a common conclusion of the earlier structural adjustment literature is that governments will only implement policies (and other reforms) with which they agree, and that they will meet other conditions only partly, cosmetically, with severe delays, or not at all. The six countries analysed in the IOB study confirm that donors have very limited influence on political governance issues and human rights. In Nicaragua and under huge pressure of donors, the government adopted a law on merit-based appointments of judges, but this was only cosmetically implemented and did not change the political influence on the judiciary.

In Mali and Ghana, the donors focused more on elements of technocratic governance than on political governance. In Mali, the non-compliance with these governance indicators in the PAF did not lead to suspensions or threats of suspensions and a positive environment for the policy dialogue in other areas was maintained. In the other countries reviewed by Lawson et al. (2014), Mozambique, Tanzania and Zambia, suspensions did occur, leading to a deterioration in the donor-government relationships. However, these suspensions were not effective in changing governance. Lawson et al. (2014) conclude that when government commitment to the Underlying Principles is lacking, threats of suspension of budget support are not effective.

ITAD (2014) reports one positive effect of the policy dialogue on governance, namely the decision of the Mozambican government to adhere to the Extractive Industries Transparency Initiative (EITI). This was accomplished by a combination of hard and soft incentives. There was an indicator in the PAF, but donors also engaged in many other efforts to influence policy makers, such as invitations for study tours, a conference in which high-level policy makers participated, and technical assistance.

Ronsholt (2014) concludes that donor attempts to change governance are seldom effective. He adds that donors often have different ideas on the promotion of human rights, rule of law and democratic accountability, and that this reduces the effectiveness of attempts to influence these issues. This is certainly also the conclusion of Faust et al. (2012) on the basis of what happened in Zambia. They report that when all donors suspended budget support after a severe corruption case in 2009, the government implemented three reforms demanded by the donors.<sup>19</sup> After that, donor views began to diverge again and no results were achieved. They conclude that if donors agree on the governance goal and harmonise their sanctions, they will be successful. However, the authors also state that the three reforms adopted did not lead to improvements in participation and democratic accountability. The – temporary – donor harmonisation may just have led to cosmetic or formal reforms, and not to substantial changes.

After the corruption discovered within the Office of the Prime Minister in Uganda in 2012, all donors temporarily suspended budget support. The government then took some important measures for improving financial management and combating corruption. Although some concerns remained, this restored the policy dialogue and some donors resumed budget support, although in smaller volumes than before (IEG and Particip 2015: 11, 73). In Burkina Faso, Sierra Leone and Burundi, donors had very limited influence on governance. Corruption indicators deteriorated in the evaluation period in Burkina Faso and Burundi. In Sierra Leone, the UK's Directorate for International Development (DfID) maintained a variable performance tranche for governance and accountability. Rather than stimulating performance, it led to frequent delays of part of the disbursements, and in 2007 even to a delay in disbursing the fixed tranche (Lawson et al., 2016: 22-23).

Overall, and in line with earlier literature, the effectiveness of donor attempts to influence political governance and human rights was limited. This holds in particular for the use of hard incentives, such as indicators in PAF, and (threats of) suspension. Soft

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<sup>19</sup> A salary reform, reform of the budget cycle leading to earlier parliamentary approval of the budget and a decentralisation implementation plan.

incentives appear to work better. Some authors argue that donors would achieve more with more harmonisation, but the evidence for this is not very strong.

### **3.7 Suspensions and withdrawals**

The increasing attention for governance has led to many suspensions and increasingly also to withdrawals of budget support. Molenaers et al. (2015) registered 131 cases of budget support suspensions by bilateral donors between 2000 and 2011, and most of these were for governance reasons. Thirty-one percent of the suspensions had to do with corruption, and 41 percent with political issues such as electoral fraud, human rights violations or repression of the opposition.

In Ethiopia, problems around the election and oppression of the opposition induced a suspension of budget support in 2005. This did not lead to an improvement of political governance, and the trend was more in the opposite direction. While the World Bank continued budget support to the country, most bilateral donors ended budget support. The EU took an intermediate position, continuing sector budget support and similar modalities (Del Biondo & Orbie, 2014). Of the seven countries more recently evaluated (Burundi, Burkina Faso, Ghana, Mozambique, Sierra Leone, Tanzania and Uganda), six have experienced one or more suspensions from around 2008 onward. As discussed below, most of these suspensions were for governance reasons. Ghana is the exception. In this country, donors suspended budget support collectively in late 2013 due to concerns on the macro-economic situation and on PFM weaknesses. In February 2015, and after the government had agreed on a new stabilisation programme with the IMF, budget support was resumed. It can be said that the suspensions had some influence on the government's return to the IMF and on more responsible macro-economic policies (Particip, 2017: xiv, 30).

In Uganda the relation between government and donors already deteriorated from around 2004 onward. The donors had difficulties in accepting the shifting priorities of the government, away from

social spending towards productive infrastructure and growth, and the decision to end the additionality of budget support. Furthermore, they were unhappy with high-level interference in policies, for example the abolishment of the graduated tax (a local tax) and the introduction of universal secondary education, and they had increasing concerns about governance issues, in particular corruption and human rights. After the corruption discovered within the Office of the Prime Minister (OPM) in 2012, which was the principal interlocutor for the budget support donors, many donors withdrew their budget support. Six out of twelve donors resumed it after the government had established a High-Level Action Matrix that focused on specific financial management reforms and some other actions. This led indeed to improvements in PFM but it did not help to improve prosecution and punishment of corruption cases (IEG and Particip, 2015: 39).

In Tanzania, some donors briefly suspended disbursements in 2008 after the discovery of two big corruption cases. They wanted to pressure the government to take actions in line with the UP to “actively fight corruption”. The government took actions but several donors felt that more could have been done in prosecuting the culprits. Although all donors later agreed that there had not been a breach with the UP, trust in the government had decreased and this affected the quality of the policy dialogue (ITAD, 2013). In Mozambique some donors suspended budget support after criticisms of the election process in 2009, and this happened again after irregularities found in health procurement in 2011 and in the education payroll in 2012. In this country, the latter two suspensions were not considered legitimate by the evaluators (ITAD, 2014). In both Tanzania and Mozambique, the suspensions had limited effect on the government’s resources and hardly brought about changes. The main effect of frequent (threats of) suspensions was a lower quality of the policy dialogue (Lawson et al. 2014).

In Burkina Faso donor trust in the government began to decrease in 2011, after perceived increases in corruption and increased political interference in the management of public expenditure. Several donors ended budget support programmes and others reduced disbursements. The policy dialogue also changed, focusing more on governance issues. However, the donors did not achieve

any substantive reforms (Particip GmbH, 2016). In Burundi, and after 2010, three donors (Belgium, Norway and The Netherlands) lost confidence in the government due to continuing high fiduciary risks and political tensions, and a failure to carry out structural reforms. They switched from budget support to (sector) common funds (ADE, 2015). In Sierra Leone the situation is a bit different: there were many delays in disbursements for various reasons. Most delays in DfID disbursements in the period 2006-2008 were related to governance reasons. As mentioned above, these temporary suspensions did not bring about substantial changes, although, by way of exception, in 2007 they contributed to the public release of a SAI report and to the granting of independent prosecutorial powers to the Anti-Corruption Commission. The other three (multilateral) donors in this country delayed disbursements for incompliance with other variable tranches, for example related to performance in PFM or service delivery in health and education. There is no evidence of better compliance with PAF indicators relevant for disbursement of variable tranches, than for other PAF indicators (Lawson et al., 2016).

In their econometric analysis Molenaers et al. (2015) found that suspensions responded to a decrease in an indicator for democracy (voice and accountability), and also became more likely with multilateral suspensions, higher economic growth of the donor, and a larger donor group in the country. On the other hand, higher aid dependence and ideological similarity between donor and recipient government were associated with lower suspensions.

All in all, it can be concluded that the stated reasons for most suspensions and withdrawals of budget support were related to governance concerns in the recipient countries. In most cases however, suspensions were not successful in bringing about the desired improvements in governance. As revealed by the analysis by Molenaers et al. (2015), factors on the donor side also play a role in these suspensions. This will be further elaborated upon in chapter 5. It means that effectiveness of suspensions and withdrawals must also be assessed in that perspective.

## Chapter 4. Poverty reduction

This chapter examines the contribution of budget support to poverty reduction, taking into account the two inputs of budget support, resources and policy dialogue. Budget support may have contributed to poverty reduction through its impact on expanding government spending and through its influence on poverty reduction policies. Poverty reduction is here meant to include both income poverty reduction, and improvements in social indicators (non-income poverty).

As discussed above, the policy theory on how budget support should reduce income poverty is not very well developed. Many evaluations observe that countries seldom have well-developed pro-poor strategies (IEG, 2010; Ronsholt, 2014). Usually, donors and countries expect poverty reduction to come about through trickle down effects from economic growth, and by investing in social and physical assets of the poor. However, this trickle-down effect is by no means guaranteed and will be limited in countries with high income inequality to begin with. The investment in social and physical assets of the poor is expected to bring about improvements in social indicators, which in turn probably will lead to higher economic growth and to income poverty reduction in the medium to long term. Within social indicators, we can make a distinction between access indicators, for example, enrolment rates, and access to health, water and sanitation, roads, and electricity, and final outcome indicators, such as increased literacy rates and reduced child and maternal mortality rates.

Given that economic growth is a necessary – though not sufficient – condition for income poverty reduction but also for sustained improvement in social indicators, the chapter begins with a section on the relation between budget support and economic growth. After that, sections on income poverty and non-income poverty follow. Analytically, this chapter includes quantitative cross-section studies that examine the direct effect of budget support on the impact variables growth, income poverty and social indicators, but also case studies that examine the contribution of budget support by tracing its influence through government policies. Most

recent case studies include quantitative analysis of the effect of government policies on relevant social indicators.

## **4.1 Budget support and economic growth**

It is difficult to assess the contribution of budget support to growth, as growth usually depends on many factors. Foreign aid in general, and budget support in particular, can at most have a small contribution. In addition, the analysis needs to take into account that countries may receive aid because they have difficulties in achieving growth. The more sophisticated and robust econometric studies on the effect of aid on growth show that aid has a small positive effect on growth, especially in the longer term (Arndt, Jones, & Tarp, 2010). The same authors also find a positive long-run effect of aid on structural transformation and on social indicators (Arndt, Jones, & Tarp, 2015).

Earlier econometric analysis of relative benefits of budget support or program aid versus project aid give contradicting results, with Cordella and Dell’Aricia (2003) finding that programme aid has a more positive effect than project aid, and Ouattara and Strobl (2008) concluding the opposite. Bigsten, Platteau and Tengstam (2011) find a positive effect of budget support on growth, especially after two or three years, but they carried out a simple Ordinary Least Squares (OLS) regression and this may suffer from endogeneity bias. IEG (2010) found more growth in 22 countries with a Poverty Reduction Support Credit (PRSC, the budget support instrument of the World Bank) than in 52 non-PRSC countries between 2000 and 2007, 4.2 percent versus 3.0 percent per year.

With respect to the case studies, many earlier evaluations conclude that budget support has some effect on economic growth by achieving macro-economic stability or by allowing increased government expenditure without increasing the fiscal deficit (Dijkstra et al., 2012). This held, for example, in Ghana, Tanzania, Mali, and Zambia. According to the IEG evaluation of the PRSC in Ghana, the policy dialogue helped to improve the investment climate and to abolish energy subsidies, both of which contributed to growth (as cited in Dijkstra et al., 2012: 165). In Vietnam and

Nicaragua budget support resources were relatively limited and could not impact growth. In Vietnam growth was very high due to the government successfully carrying out reforms, but these reforms would have been carried out anyway, also without the policy dialogue around budget support (Grawe, 2010).

Writing on Mali, Mozambique, Tanzania and Zambia, Lawson et al. (2014) conclude that budget support contributed to growth by allowing for increased government expenditure without a need for raising taxes or increasing domestic borrowing, so that aggregate demand could rise. They add that budget support helped to overcome infrastructure bottlenecks by financing investment, and that the support to macroeconomic stability helped to improve external confidence in the economy. However, they also state that budget support's contribution to growth could have been higher if governments had used resources more effectively to address these infrastructure constraints, for example in energy supply.

The Uganda evaluation reports that growth has been high but it does not assess the contribution of budget support. In Burkina Faso, budget support resources have contributed to the high growth rate through enabling macro-economic stability, but the policy dialogue has not added much to this financial effect. Donors have hardly addressed the lack of effectiveness of public spending in general and the inappropriate priorities for public investment, in particular. They did give attention to governance issues and corruption, perceived as other bottlenecks to growth, but with limited success.

The recent Ghana evaluation concludes that most growth was due to other factors such as increased oil income, but it reports some modest contributions of budget support, in particular through effects on macro-economic stabilisation: cushioning the effects of sudden declines in revenues, inducing a new IMF agreement through the 2013-2014 suspension, and helping Ghana in setting up institutions for responsible oil revenue management. On the other hand, the policy dialogue could not maintain government commitment to growth-enhancing policies in agriculture, the business environment or regarding diversification (Particip, 2017).

In Burundi, budget support resources may have contributed to growth until 2010 by fostering macro-economic stability. After 2010, disbursements decreased and the government had to take austerity measures, which probably did not help growth. Second, budget support's policy dialogue and the accompanying technical assistance have led to some reforms in the investment climate and in the coffee sector, but these reforms were insufficient to bring about more investment<sup>20</sup> and higher coffee production. So the contribution of the policy dialogue to growth was limited.

Lawson et al. (2016), relying on three studies carried out around 2008, conclude that budget support made an important contribution to the high growth rate in Sierra Leone in the post-war period. It did so through increasing aggregate demand, raising confidence among domestic and foreign investors, and financing salaries of public service providers. In the more recent period, budget support most likely helped growth by maintaining macro-economic stability in the crisis years 2009 and 2014, and by financing an expansion of the road network.

Orth et al. (2017) conclude that there is a positive effect of budget support resources on reinforcing macroeconomic stability, and through this, on economic growth. This is certainly also the common finding in the more recent country evaluations discussed above. It can be added that in the two post-conflict countries Burundi and Sierra Leone budget support helped *to achieve* (and not reinforce) macro-economic stability. Orth et al. (2017) do not find sufficient evidence for an effect of the policy dialogue on macro-economic stabilisation or growth. The very diverse experiences discussed above confirm this. While in some countries (Ghana in the earlier years, to some extent Burkina Faso) the policy dialogue helped to improve the investment climate, in other countries opportunities were missed or the dialogue was not effective.

All in all, budget support contributes to growth but mainly through its resources and mainly through its effect on macro-economic stabilisation. This can also partly be explained by the fact that the Poverty Reduction Strategies on which budget support was

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<sup>20</sup> Lack of respect for rule of law and high taxes were main investment barriers.

based, hardly paid attention to growth (IEO, 2004; OED, 2004). In so far as they addressed growth, they mentioned macro-economic stabilisation and market liberalisation. The strategies, often elaborated in order to access debt relief and with little ownership, reflected the continued dominance of the Washington Consensus (Craig & Porter, 2003; Stewart & Wang, 2003). Later strategies gave some more attention to economic growth, but this usually meant a somewhat higher priority for physical infrastructure. Other than this, growth policies did not become very concrete (Canagarajah & Diesen, 2006; Woll, 2008). According to some more critical voices, budget support has maintained the conditionality in favour of market liberalisation and in particular, trade liberalisation. As a result, the likely effect of budget support is more negative than positive for economic growth (Langan, 2015) Knoll, 2008.

## 4.2 Income poverty

IEG (2010) compares countries with a PRSC with countries without this aid modality. In PRSC countries the poverty headcount (percentage of population living in poverty) proved to have reduced by 8 percentage points between 1999 and 2005, while in non-PRSC countries this was 5 percentage points. Dijkstra et al. (2012: 173) carried out the same analysis for countries with and without budget support, and show that countries with budget support have a significantly larger reduction in the poverty headcount between 2000 and 2007: 11 percentage points versus 6 percentage points (with poverty measured as living on less than \$1.25 per day). However, the value of these simple with-without comparisons is limited as they do not control for other factors influencing poverty reduction, or for possible endogeneity: countries may receive a PRSC or budget support *because* they carry out good and/or successful poverty reduction policies.<sup>21</sup>

The first joint evaluation of budget support could not conclude on the effect of budget support on the reduction of income poverty due to lack of sufficient data, the short time period of budget

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<sup>21</sup> The reverse is also possible: Countries receive budget support because they have more difficulties with reducing poverty.

support provision, and methodological problems (IDD and Associates, 2006). In the six case studies presented in the IOB study, the contribution of budget support was assessed but the results varied. In Vietnam and Mali income poverty decreased most, but there was little relationship with budget support. High growth rates were important, but also the fact growth happened to be in the cotton sector leading to rural income increases (Mali) and that the government carried out pro-poor and pro-rural policies, providing the rural population access to education and infrastructure (Vietnam). High economic growth in Zambia and Tanzania hardly led to reductions in poverty, mainly due to the fact that the rural poor did not benefit from this growth. In Zambia, donors had tried in vain to make agricultural policies more pro-poor, as also discussed above. In Nicaragua rural poverty decreased in the period of budget support as a result of high coffee prices and probably also of social protection programmes set up by the Ortega government – in the latter, there may be an effect of budget support resources but not of the policy dialogue.

As to the more recent evaluations, the evaluation on Mozambique reports no change in the percentage of the population living below the poverty line between 2003 and 2009, despite high average annual growth rates of 7 percent. This is the more striking given that agricultural growth was high as well. The evaluators explain this discrepancy by pointing to data problems, in particular regarding the poverty surveys. In addition, high growth, also in agriculture, may have been driven by some large investment projects that do not benefit the poor (ITAD 2014: 150). For Burundi poverty data is only available for one year so no conclusions can be drawn.

In Uganda income poverty levels have fallen, but the evaluation does not assess the contribution of budget support. For Uganda this is a bit disappointing as the government began to prioritise growth and the productive sector since the early and mid-2000s, and most likely budget support resources have facilitated these investments. In Ghana, budget support contributed to a further reduction in income poverty, in particular during the first part of the evaluation period. This was accomplished through improving access to basic services and through the attention in the policy dialogue for

maintaining pro-poor interventions. The evaluation of Burkina Faso notes that although budget support contributed to growth, there was a limited impact on poverty reduction as there was not much attention for sectors that could have led to pro-poor growth (Particip, 2016: x, see also above). Orth et al. (2017) conclude that the effects of budget support on income poverty reduction are not consistent, which is in line with the huge variation reported in the evaluations discussed above.

All in all, the studies show that if budget support contributed to the reduction of income poverty, it was most likely through its effect on economic growth. However, growth proved by no means sufficient for reducing income poverty, as testified by the experiences of Burkina Faso, Mozambique, Tanzania, and Zambia. The limited results of budget support for income poverty reduction can also be explained by the fact that budget support has supported the countries' Poverty Reduction Strategies. These strategies not only paid limited attention to growth, but were very much targeted to achieving the Millennium Development Goals (MDGs). Although the first MDG contains a target on income poverty reduction, the attention in the Poverty Reduction Strategies has been on the MDGs related to non-income poverty, in particular in the areas of (gendered) education, (gendered) health, and water and sanitation. As a result, the budget support policy dialogue also focused on achieving targets related to non-income poverty.

### **4.3 Non-income poverty**

Chapter 2 of this report already concluded that expenditure for priority sectors as defined in the Poverty Reduction Strategies increased in almost all countries. This section examines what this has meant for the access to social services and for final outcomes with respect to social services. I begin by presenting the results of some quantitative cross-country studies.

Several studies have examined differences between countries receiving budget support and countries not receiving that support, in the achievement of the MDGs. Beynon & Dusu (2010) found that access to primary education and to water and sanitation

improved more in countries with budget support. In addition, the gender equality in access to primary education improved more and infant and child mortality rates decreased more. IEG (2010) found the same for countries with and without a PRSC. However, in countries without a PRSC the increase in access to secondary education was higher than in PRSC countries. This could be explained by the higher priority budget support donors usually gave to primary education rather than secondary education.

Dijkstra et al. (2012) show that countries with budget support have a slightly higher improvement in the Human Development Index (HDI) between 2000 and 2011. A regression analysis that controls for other factors such as economic growth, improvements in governance, other aid and whether the country benefited from the Heavily Indebted Poor Country initiative, confirms a significant effect of budget support on an improvement in the HDI.<sup>22</sup>

Dijkstra et al. (2012: 193) carried out a similar multivariate regression analysis in order to assess the effect of budget support on several social indicators. They present separate results for including and excluding other aid as regressor; probably the actual effect is underestimated if other aid is included, and vice versa. They also present results when budget support is instrumented for. There prove to be robust positive effects on access to primary education, number of teachers in both primary and secondary education, and share of well-educated teachers in primary education. In health, the only robust outcome is an increase in the share of deliveries attended by skilled staff, and in immunisation rates – but the latter only if other aid is excluded.

The earlier case study evaluations conclude that budget support allowed an expansion of services in, for example, health and education, but that the contribution of budget support to improved social indicators was difficult to assess due to lack of data and attribution problems (IDD and associates, 2006). They also conclude that the expansion was often accompanied by a deterioration in the quality, for example in education.

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<sup>22</sup> Growth was the only other significant factor.

Orth et al. (2017) also conclude that budget support has not been effective in improving the quality of service delivery or the administration of the services. However, although quality is indeed low, there is not much proof that quality decreased. In primary education, for example, student-teacher ratios and student-classroom ratios have often improved. This was the case, for example, in Uganda and Zambia (Dijkstra et al., 2012). Student-teacher ratios also improved in Tanzania, at least in the latter years of the evaluation period (Itad, 2013: 98). In Mozambique, student-teacher ratios improved while student-textbook ratios decreased (Itad, 2014: 169, 171). In Mali, student-teacher ratios and textbook-student ratios both improved (ECO consult, 2011). Furthermore, lower exam pass rates or completion rates may be the result of the fact that children from poorer families, of whom the parents never had access to education, now attend primary school (Dijkstra et al., 2012, Lawson et al., 2014). In Mozambique, poverty proved to be an important hindrance for completing primary school (Itad, 2014). All in all, this means that budget support resources have often helped to lower student-teacher ratios, student-class room ratios or student- text book ratios, thus contributing to the quality.

The case studies included in Dijkstra et al (2012) vary in their conclusions on the contribution of budget support to higher access to services and to improved social indicators. Most of the (huge) improvements in social indicators in Vietnam, for example, are due to government policies and not to budget support. The newer evaluations are, in general, more positive. And all of them use econometric analysis in order to establish causal relations between specific government investments, facilitated by budget support resources, and i) improved access and ii) improved final outcomes. The results for education and health are presented in Table 5.

**Table 5. Contribution of budget support to access and final outcomes in education and health in recently evaluated countries**

	Education access		Health access		Education outcomes		Health outcomes	
	trend	BS	trend	BS	trend	BS	trend	BS
Mali 03-09	+	Yes	+	Yes	+	Yes	+	Yes
Zambia 05-10	+	Yes	+	Yes	+	Yes	+	Yes
Tanzania 04-11	+	Yes	NA	NA	+	Yes	NA	NA
Mozambique 05-12	+	Yes	NA	NA	+	Yes	NA	NA
Uganda 04-13	+	Yes*	+	Yes*	0	0	0	0
Sierra Leone 02-13	+	Yes	+	Yes	+	Yes	+	Yes
Burundi 05-13	+***	Yes***	+***	Yes***	-	Yes***	NA	NA
Burkina Faso 09-14	NA	NA	+	Yes	NA	NA	+	Yes
Ghana 05-15	NA	NA	+	Yes**	NA	NA	+	Yes**

Legend:

BS: Lists whether there was a positive contribution of budget support to the indicator(s), “yes”, “0”= neutral, or “No”

Trend: + (or -): Positive (negative) trend for at least one indicator and no information on other indicators, or positive (negative) result for majority of indicators;  
0: neutral result, or positive result for one indicator and negative result for another

NA: No information in report

\*Mainly in first half of evaluation period.

\*\*Until 2012.

\*\*\*Until around 2010.

Sources: country evaluations.

In Mali, the higher budgets for health and education facilitated by (general and sector) budget support led to large improvements in education and health outcomes between 2002 and 2009. The primary enrolment rate, for example, increased from 64 to 81 percent and the primary completion rate increased from 40 to 56 percent (Eco consult, 2011). Similarly, in Zambia, the higher budgets for the social sectors led to increases in staff for health and education, to more classrooms and more availability of essential drugs. Statistical analyses show that these investments were effective in improving immunisation rates, child and maternal mortality rates, reducing the prevalence of illnesses such as malaria, tuberculosis and diarrhoea, and increasing enrolment and completion rates (De Kemp et al., 2011).

The evaluation in Tanzania focuses on education and agriculture, but in the latter no econometric analysis was possible due to data constraints. Budget support resources facilitated higher expenditure for the priority sectors and most of this went to education. This led to huge increases in access to primary and secondary education. In recent years, exam pass ratios in primary education have also increased, and the lower pupil-teacher ratio to which budget support contributed is a main factor behind this result. Yet, this result is considered fragile and more investment in quality is necessary (Itad, 2013). In Mozambique, budget support resources contributed to large increases in primary enrolment (by 40 percent) and in secondary enrolment (by 65 percent, although starting from a very low base).<sup>23</sup> Children from poorer households, in particular, could benefit from increased access, and the gap between boys' and girls' enrolment decreased to 4 percentage point (Itad, 2014). In addition, gross completion rates in primary education increased dramatically. Budget support contributed to this result, for example through lowering the student-teacher ratio.

The Uganda evaluation focuses on results in education, health and in water and sanitation. In education, budget support resources facilitated large increases in both primary and secondary enrolment, in particular in the first half of the evaluation period. The budget

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<sup>23</sup> In 2008, secondary enrolment was still at only 17.3 percent.

support dialogue helped to achieve gender parity in gross primary enrolment, but did little to prevent relatively high female dropouts or to improve the quality of education. Access to health services increased as a result of public investment in the sector, partly financed by budget support, but inequality between urban and rural areas remained. The policy dialogue had some effect on health policies, and budget support resources facilitated some government initiatives, such as the abolishment of user fees. However, maternal mortality rates declined only slowly and recent trends in some indicators, for example in female HIV infection rates, are a reason for concern. The water and sanitation sector had a successful Sector-wide approach financed by sector budget support and other aid. It led to increased access to water in rural areas and in small towns. Budget support facilitated these outcomes by resources and policy dialogue (IEG and Particip, 2015). All in all, results are better in water and sanitation than in health and education. The latter sectors undoubtedly suffered from the changed priorities of the Uganda government. As shown in chapter 2, budget support could not prevent that spending for the priority sectors stagnated.

In Sierra Leone, budget support helped to increase primary and secondary enrolment rates, while also contributing to increases in exam pass rates at all levels. In 2014, female and male primary enrolment rates had become equal. Budget support also contributed to improvements in access to health services, in nutrition and in maternal mortality rates (Lawson et al., 2016).

In Burundi, budget support contributed to an expansion of services in health and education, at least until around 2010. For health, this conclusion is just based on qualitative analysis. In education, a common donor fund to support this sector also played a role. The enrolment rates in primary and secondary education increased dramatically, at least until 2009-10. Econometric analysis shows that there was a contribution from budget support through more infrastructure, more staff and by offering school meals. Repetition and drop-out rates in education are still high, however, and pass rates have declined. The number of teachers proved to be the most important factor on the supply side, and budget support

contributed to its increase – although it was not sufficient yet (ADE, 2015).

In Burkina Faso, budget support contributed to improved access to health services, leading to improvements in some outcome indicators such as the maternal mortality rate and the prevalence of underweight among children. There was more access to water in urban areas and more attention for sanitation, but access to water in rural areas lagged behind. A big problem in this country is the lack of effectiveness of public spending, for example reflected in under-execution of investment budgets. The budget support dialogue was not effective in addressing these problems (Particip GmbH, 2016: 24-27).

The Ghana evaluation focuses on three sectors: health, energy and natural resources, and agriculture, and these sectors received substantial sector budget support as well. In health budget support contributed to better policy-making and monitoring and evaluation, and also to improved health coverage and outcomes, in particular through financing more health staff. But these positive results were only visible until around 2012. In the energy and natural resources sector budget support facilitated an improved legal framework and helped strengthening relevant agencies. However, this did not improve actual policy implementation and there is evidence of a further deterioration of the environment: pollution, in particular of water, increases, and the resource base decreases. Budget support facilitated the setting up of relevant programmes with the Ministry of Agriculture in order to stimulate non-cocoa agricultural production, but these suffered from implementation problems (Particip GmbH, 2017).

The ending of Dutch budget support in Burkina Faso, Nicaragua, Tanzania and Zambia is estimated to have had negative effects on service delivery and outcomes in health and education (De Kemp and Lobbrecht, 2016). The people living in more deprived regions often suffered most from the lower investments in the sectors.

Overviewing the evidence from the recent evaluations, we can conclude that budget support contributed in all countries where this was examined to increased access in health and education (Table 5 above). The evidence for a contribution of budget support to final

outcomes in education and health is also quite strong. Some of these positive conclusions are only valid for a certain period, which is related to the declining volumes of budget support in recent years. Almost all of these conclusions from evaluations are based on econometric analysis within the respective sectors. Combined with the cross-country quantitative evidence showing positive contributions of budget support on improvements in the HDI and in some important social indicators the overall conclusion is that budget support indeed contributed to the reduction in non-income poverty. The main channel for this positive outcome has been the increase in resources, and in several of the reviewed studies this increase comes from both general and sector budget support. On the other hand, many studies conclude that the policy dialogue around budget support has done little to improve the efficiency or quality of service delivery (IEG, 2010; Dijkstra et al. 2012; Lawson et al., 2014; ADE, 2015).

# Chapter 5. Conclusions

Budget support is considered the preferred instrument for increasing aid effectiveness. Based on the expected advantages of respect for ownership, harmonisation, alignment, and predictability, budget support was considered to be the most effective aid modality for achieving poverty reduction. In practice however, donors began to use this instrument for improving governance, and in particular political governance. This report has reviewed the evidence on the effectiveness of budget support, taking into account these two goals. It has followed the policy theory of budget support, tracing the effects of the two inputs, resources and donor preferences for the policy dialogue, via the throughputs respect for ownership, harmonisation, alignment and predictability, and the outputs lower transaction costs, enhanced macro-economic stability, increased government spending for priority sectors, systemic effects on PFM and domestic accountability, and improved policies and governance, to the ultimate outcomes economic growth, income and non-income poverty reduction, and, again, improved governance in all its aspects.

The review builds on the earlier comprehensive IOB evaluation of budget support and adds more recent sources including country evaluations, syntheses of those evaluations, reviews and academic literature. The conclusions prove to be more or less in line with the earlier study, yet the negative consequences of donors giving ever more priority to the added objective of improving governance have become more evident. This chapter first summarises the findings. This is followed by a discussion and finally by some policy implications.

## 5.1 Summary of findings

On average, budget support constituted between 14 and 28 percent of total ODA in the recently evaluated countries. This led to substantial alignment of aid to local systems. Although some donors maintained separate variable tranches, in most countries disbursement conditions were to a very large extent harmonised.

The between-year predictability of budget support was good, and better than for project aid. Within-year predictability remained somewhat problematic, with donors disbursing later than promised and most flows coming at the end of the year. Budget support has decreased transaction costs. However, all these positive findings held mostly for the earlier parts of the evaluation periods.<sup>24</sup> The benefits largely evaporated as a result of more intensive governance discussions, varying responses of donors to perceived breaks with Underlying Principles, and lower volumes of budget support.

Donors applied limited selectivity when starting budget support, in particular with respect to governance. And donors had difficulties in respecting ownership. Once budget support started, they began to use the policy dialogue to influence policies and, increasingly, governance. This lack of respect for ownership seems to have increased over time. In many countries the policy dialogue deteriorated as a result of a vicious circle: increasing donor dissatisfaction with country performance, often on governance issues, led to ever higher ambitions for the policy dialogue, in turn causing more dissatisfaction. In the end, it led to suspensions and withdrawals, with each donor country making its own decisions on these matters, thus reducing harmonisation. The dominance of the governance objective not only made ownership a foul, but also affected the other benefits of budget support, namely harmonisation, alignment and predictability.

If donors succeeded in coordinating their preferences for the policy dialogue and jointly agreed on a small number of indicators for the PAF, positive systemic effects of the dialogue were possible on better coordination and higher results-orientation of national policies. The combination of the use of domestic systems, attention in the policy dialogue, and technical assistance led to improvements in Public Financial Management. The *systemic* effects of budget support on increasing domestic accountability seem to be limited. The policy dialogue is between donors and executive, and the use of local systems and budgets did not automatically generate interest among parliament or civil society actors. Yet, the policy dialogue

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<sup>24</sup> Turning point varies between countries but lies somewhere between 2005 (Uganda and Ethiopia) and 2011 (Burkina Faso).

and accompanying capacity building activities did lead to improvements in the institutions for horizontal accountability (the supply side). It contributed to increasing transparency of budgets and of budget execution, in particular through strengthening Public Accounts Committees of Parliaments, Supreme Audit Institutions or Courts of Audit. Direct donor support to institutions on the demand side of accountability was more limited. Yet in several countries parliaments, media and/or civil society have grasped the increased opportunities to hold governments to account, implying that budget support also contributed somewhat to improvements in vertical accountability. Budget support not only strengthened institutions for the oversight of budget execution but also other institutions meant to monitor corruption. This contributed to more detection of corruption. However, in most countries concerns remain on the extent of prosecution and punishment of the culprits. Contrary to the many expectations on the high fiduciary risks of budget support, there is no evidence that it increased corruption.

In line with earlier literature on structural adjustment, the effectiveness of donor attempts to influence policies, governance and human rights was limited. With respect to policies, the evaluations point to some missed opportunities. Donors were often focused too much on too many individual performance indicators, at the cost of a more strategic discussion on how obstacles in public service provision could be removed or economic growth could be fostered. Donors were also hindered by a lack of knowledge on how budget support or government policies would be able to reduce income poverty. However, where donors tried to make policies more pro-poor in areas where this conflicted with (perceived) strategic or political interest of the recipient government (Mozambique, Zambia), they were not successful. In the area of governance and human rights, it is clear that hard incentives, such as indicators in the PAF or (threats of) suspensions were at most able to lead to cosmetic changes. Soft incentives appear to have worked better. Some authors argue that donors would achieve more in the governance area if they manage to speak with one voice, but the evidence for this is not strong.

Budget support has contributed to achieving, or, depending on the situation in the recipient country, maintaining macro-economic

stability. Budget support allowed countries to increase government expenditure without affecting macro-economic stability, and thus contributed to economic growth. In most countries, spending for the priority sectors as defined in the Poverty Reduction Strategies increased. On average, there is no evidence of budget support decreasing domestic tax revenues. However, there are large differences between countries, with worrying trends in some recently evaluated countries (Burundi, Sierra Leone and Uganda).

Countries with budget support have experienced more reduction in income poverty than other developing countries, but this does not prove a causal relationship yet. From the country evaluations, it can be concluded that *if* budget support contributed to a reduction in income poverty, it was most likely through its effect on economic growth. However, growth proved by no means a sufficient condition for reducing income poverty, as testified by the experiences of Burkina Faso, Mozambique, Tanzania, and Zambia where income poverty hardly decreased.

Budget support did contribute to the reduction in non-income poverty. Budget support resources, and sometimes the dialogue as well, have facilitated more expenditure for the priority sectors. This has led to more class rooms, more drug availability, and more staff for education and health. In turn, this has contributed to higher school enrolment rates, to more gender equality in access to primary education, to more access to health services, and more access to water and sanitation. In some countries, access to secondary education significantly improved as well. In many countries there were also improvements in outcomes such as primary school completion rates, immunisation rates, infant and child mortality rates, and maternal mortality rates. The contribution of budget support to these achievements has been shown both in quantitative cross-country analysis and in case studies, with the more recent country evaluations applying rigorous methods for establishing the causal relation between increased investment facilitated by budget support, and ultimate social outcomes.

## **5.2 Discussion**

Two clear findings stand out. One is that budget support, and particularly its resources, have contributed to economic growth and to the reduction of non-income poverty, while having much less effect and at most an indirect one (through economic growth) on income poverty reduction. The other is that donors have increasingly attempted to use budget support as instrument for improving governance, in particular for fostering democracy, human rights, and anti-corruption actions. However, these efforts have not been very effective, and there appears to be a trade-off between the two objectives. In the following, I first explain the two main findings and then discuss the trade-off. In the part of this section, I discuss the fall in budget support volumes in recent years.

### **5.2.1 Poverty reduction**

The achievement of substantial improvements in social indicators means that budget support has been quite effective in meeting its original objective, at least the non-income part of poverty reduction. This is a huge accomplishment. To a large extent, it can be attributed to the high degree of alignment of policy priorities between donors and recipient countries in the years 2000s and beyond. The universal agreement on the Millennium Development Goals (MDGs) played an important role. Budget support resources helped to carry out the recipient countries' Poverty Reduction Strategies, which were often targeted to these MDGs. This favoured policies and spending decisions targeted to increased access to social services, and hence enabled these positive outcomes.

The limited (direct) results of budget support for income poverty reduction can be attributed to two factors. First, although the first MDG contains a target on income poverty reduction, the emphasis in the Poverty Reduction Strategies that were supported by budget support was on the MDGs related to non-income poverty, in particular in the areas of (gendered) education, (gendered) health, and water and sanitation. Resources were therefore mainly invested in sectors like health, education and water. These investments

potentially have medium or long term effects on income poverty but as yet, these effects can hardly be visible.

Second, neither the policy theory of budget support nor the Poverty Reduction Strategies were explicit on how government policies or resources would reduce income poverty. In this light, the expectations on budget support's contribution to reducing income poverty were far too high. To the extent that resources can play a direct role in reducing income poverty, this is through social safety net or cash transfer programmes. However, in the early 2000s, knowledge of and experience with these type of programmes was still limited and they were seldom included in Poverty Reduction Strategies. In order to reduce income poverty in a more structural way, government policies such as tax and subsidy policies but also policies that affect the distribution of assets (land) in a country and that intervene in the production structure, are probably more important than government resources.

Similar explanations hold for the fact that the main contribution of budget support to growth was through its effect on macro-economic stabilisation. The Poverty Reduction Strategies hardly paid attention to growth. In so far as they did, they stressed macro-economic stabilisation and market liberalisation, and in later years some also mentioned the importance of physical infrastructure. Some country evaluations report a contribution of budget support to growth through helping to finance infrastructure. But to the extent that the policy dialogue around budget support pushed for market liberalisation, and to the extent it was successful, it may have negatively influenced growth.

## **5.2.2 Governance**

Regarding the second important finding, the question is why the objective of improving political governance got so much prominence, despite already existing evidence of limited effectiveness of conditionality. In fact, two issues require an explanation. First, the fact that policy conditionality entered the policy dialogue almost from the start, and second the fact that governance, and in particular corruption issues and issues related to

free and fair elections and human rights took centre stage, and ultimately led to suspensions and withdrawals of budget support by many donors, and in particular bilateral donors.

With respect to the first, and as already discussed in Chapter 1, many authors have already pointed to the “schizophrenia” in the aid industry at the time when all donors and recipient embraced the Paris Declaration. While the official discourse was that aid was ineffective due to conditionality and lack of ownership, many actors in the aid community were of the view that the real reason for aid’s ineffectiveness were inadequate policies and governance in recipient countries (Renard, 2007; Rogerson, 2005). Secondly, chapter 2 shows that donors applied very little selectivity in the budget support allocation. They defined eligibility criteria and/or underlying principles, but in an opaque way and many of these criteria and principles were not met at the start. This situation reinforced the latent doubts on, and lack of trust in, governance of recipient governments. This also induced the reintroduction of conditionality. A third explanation is more theoretical and in that sense complementary to the other two. Wolff (2015) argues that technocratic, New-Public-Management-like instruments are often selected before there is normative consensus about objectives. Budget support can be seen as such as technocratic, de-politicised instrument. This would explain that once in place, the other – hidden – objective, that of influencing policies and governance, quickly came to the surface.

The increasing importance of, and lack of tolerance for, issues like corruption, infringements of democratic practices and human rights violations has to do, on the one hand, with developments in the recipient countries, and on the other, with changes in the donor countries. There were problems with the elections and treatment of the opposition in Ethiopia (2005), Uganda and Nicaragua (2008) and Mozambique (2009); in many other countries corruption scandals appeared (again) around 2007 or in the years after that. But concerns on electoral processes were not new or unexpected, and most likely, budget support has contributed to corruption coming into the open, through its support to improved budget systems and domestic accountability institutions.

Probably the developments within the donor countries were more important for the critical responses to these issues. The circumstances were slightly different in different countries, but the global economic crisis in 2008 made all donor governments more critical of development cooperation in general. This implied that donors came to see budget support as a more political instrument (than other aid modalities) for which the eligibility criteria really had to be met. In addition, in many European countries more conservative governments were elected, also contributing to a more critical stance toward budget support. In Sweden, for example, the liberal/conservative government that took office after the elections in 2006 sharpened the eligibility criteria for budget support in 2008, putting a much greater emphasis on human rights and democracy (Larsson, 2018). The conservative government that took power in the UK in 2010 also began to apply much stricter conditionality on governance, in particular accountability systems (Koch & Molenaers, 2016). Germany temporarily suspended budget support globally in 2008 in order to investigate the fiduciary risks of the instrument. In the Netherlands, political governance was at the heart of the critical debates in parliament on budget support in around the same year (Dijkstra et al., 2012). Wolff (2015) sees the European Commission as champion of the technocratic instrument of budget support, and argues that this induced an ever more critical and politicised stance in the member states. Ultimately, this also influenced the budget support policy of the EU itself. In 2011, and after strong pressures from several member states (the UK, Germany, the Netherlands, and Nordic countries) the EU began to apply much stricter criteria with respect to democracy and human rights issues (Koch and Molenaers, 2016).

### **5.2.3 The trade-off**

Given the results obtained in the reduction of (non-income) poverty, there is a clear trade-off between the two objectives of budget support. If donors gave priority to fostering political governance and this led to reducing or ending budget support, the poverty reduction objective could no longer be achieved. In turn, prioritizing poverty reduction required donors to not use budget

support for promoting governance. This shows that the “Tinbergen rule” holds (Tinbergen, 1952): the number of instruments should be equal to the number of objectives. In this case it implies that one instrument (budget support) can only have one objective.

This trade-off has already been highlighted in previous studies. Some authors analyse the trade-off in a neutral way, analysing which stand the EU takes, for example (Del Biondo & Orbie, 2014). Others are more outspoken. The addition of the objective of improving governance not only reduced ownership, but also led to uncoordinated actions of donors to delay or suspend disbursements. It severely reduced alignment, harmonisation, and predictability and thus reduced the resources available for poverty reduction (Dijkstra et al., 2012; Dijkstra, 2013; Molenaers, 2012; Molenaers et al., 2015). Furthermore, the use of the policy dialogue for governance issues and not for policies, limited donor influence on poverty policies (Dijkstra, 2013; Lawson et al., 2014).

Faust et al. (2012) draw another conclusion from the observation that there is a trade-off between the two objectives. They argue that donors in Zambia gave different priorities to the objective of improving democratic accountability, and that this led to incoherent signals to the government. They conclude that if donors would all have the same goal hierarchy, i.e. give preference to improving democratic governance over poverty reduction, progress in democratisation would be possible. However, given the limited results in the promotion of political good governance in general, this can be questioned.

#### **5.2.4 The decline of budget support**

In recent years, several donors have stopped providing budget support altogether, and others, like the European Commission and the UK, maintain much stricter governance criteria. Donors continuing budget support as before included the World Bank and other multilateral development banks. Yet, overall volumes have declined substantially (Figure 1). It is clear that the declining interest for budget support among, in particular, bilateral donors does not have any relationship with the evidence. Budget support has

contributed greatly to the advancement of the Millennium Development Goals, while the (assumed) fiduciary risks proved to be limited. To the contrary, budget support helped to improve public financial management systems and domestic accountability institutions.

One of the reasons for the declining volumes of budget support was the fact that political governance had become a second objective for budget support and the resulting disenchantment when this objective was not achieved. But there are other factors as well, like the earlier mentioned economic crisis of 2008 and the fact that in many donor countries more conservative governments were elected. These governments are in general less committed to the aid effectiveness agenda and more to an agenda that promotes domestic strategic or commercial interests. Faust and Koch (2014) show econometrically for 15 European donors that lower growth rates and more conservative governments have a more negative effect on budget support volumes than on aid volumes in general (Faust & Koch, 2014).

Furthermore, it seems that citizens in donor countries have become more critical toward development cooperation in general. According to surveys, more than half of the people in France, the UK, and the US think that most aid is wasted and ends up in the hands of corrupt officials.<sup>25</sup> Against this background, providing budget support is harder to justify than project aid, and brings political risks for governments in donor countries. The more critical stance toward development cooperation in general also brings about a need for donor governments to show visible results of aid. This is perceived to be more difficult with budget support: while positive effects of budget support can be shown, it is not easy to attribute them to an individual donor. The effects always are the joined results of the collective of donors and of the actions of recipient governments.

In line with this, Koch et al. (2017) argue that collective action problems of donors are the main factor behind the reduced interest in budget support. The joint nature of programme-based

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<sup>25</sup> As reported in Kenny (2017).

approaches (general and sector budget support, sector-wide approaches) gives donors an incentive to free-ride on the financial and technical contributions of other donors. Whilst there are certainly benefits for individual donors – by having a seat on the table they can push for their own political or sector agendas, - the main benefits and also the potential political costs (fiduciary and other risks) will accrue to all participating donors (Koch, Leiderer, Faust, & Molenaers, 2017). However, according to this reasoning, rational donors would maintain some budget support or sector budget support in all countries in which they are active, in order to reap the individual benefits without incurring high costs. This is not what we see in practice. Nevertheless, the lack of visibility of individual donor efforts can provide part of the explanation for the decrease in budget support.

All in all, the most important explanations include the more critical stance of citizens toward development cooperation that reinforced the perceived risks of budget support and increased the need for visibility of results, the rise of conservative governments, and the disenchantment with the results on the second objective of budget support, namely that of improving democracy and human rights.

# Chapter 6. Policy recommendations

Budget support continues to be the most effective instrument for fostering growth and poverty reduction. The advantages of budget support as compared to project aid still hold. And in the current context of declining growth rates and government revenues in Africa, budget support can be particularly helpful to sustain government expenditure, in particular for the social sectors, without endangering macro-economic stability.

The question is how donors can build on the positive outcomes of budget support, while also taking into account the political backlash of budget support within their own countries. The latter holds, in particular, for bilateral donors. In the following, I first sketch the conditions for choosing this modality, also in comparison with other aid modalities, and then I give some recommendations on the use and the design of the instrument.

## 6.1 Conditions

A first condition is that there must be a minimum degree of consensus between donor and recipient on socio-economic policies in the recipient country. In the years 2000s, this agreement was guaranteed by the joint focus on the MDGs. These goals have now been followed up by the Sustainable Development Goals (SDGs) that are also universally agreed upon. There is no a priori reason why there cannot be a broad consensus again on a recipient country's development goals.

Second, budget support requires some level of trust in the governance of the recipient. It makes sense for donors to assess the governance situation in a country before providing aid.<sup>26</sup> Some trust in political governance, so the extent of democracy and respect for human rights, is important for all aid channelled to governments, not just for budget support. For budget support in particular, a basic

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<sup>26</sup> This does not need to apply in fragile states but fragile states are not included in this report.

confidence in budgeting and public financial accountability systems (the more technocratic aspects of governance) is also important. But given the opportunities to improve these systems *through* budget support, this can be a dynamic assessment: a willingness to improve, or evidence of actual improvements in the recent past, are more important than the level of these systems.<sup>27</sup>

In practice, donors may consider a portfolio approach with regard to aid modalities to a particular recipient. If donors do not have trust in the recipient government's respect for democratic values and human rights, they may consider providing aid to non-governmental organisations or not providing aid to the country at all. In case they decide to allocate aid to governments, general or sector budget support is in principle more effective than project aid for most aid objectives. In both cases, resources flow to the accounts of the Ministry of Finance, so the policy dialogue and (eventual) accompanying capacity building activities can focus on improving budgeting, reporting and auditing systems. General budget support is more suitable for dealing with strategic and cross-cutting issues related to poverty reduction. Sector budget support can focus in more detail on policies for a particular sector.<sup>28</sup>

In a way, recipient countries can also apply a portfolio approach. Although it is in the interest of the recipient government to have a substantial flow of resources through budget support, it is not necessary that "all" donors participate in general budget support. To the contrary, when donor groups are smaller budget support proves to be more predictable as there are fewer suspensions (Molenaers et al., 2015). In addition, the quality of the policy dialogue proves to be better (Lawson et al., 2014). It may be sensible for a recipient country to prefer receiving general budget support from multilateral donors, and sector budget support from different groups of bilateral donors. Multilateral donors are less influenced by political concerns and are better able to secure predictable funding. It would mean that both policy dialogues can focus on policies instead of on politics and governance. And although the partial substitution of general

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<sup>27</sup> When budget support to Vietnam started, the public budget comprised just one page.

<sup>28</sup> See also Lawson et al. (2014: 82).

budget support by sector budget support would imply less donor harmonization at the *central* government level, resources would still be aligned to government systems and aid predictability would probably increase.

## **6.2 The use and design of budget support**

When donors have a basic trust in a country's governance and begin to provide budget support, they should refrain from using budget support as leverage for improving political governance. The performance assessment matrix (PAF) should not include targets on political governance issues. The evidence shows that attempts to influence democracy and human rights can at most have formal or symbolic effects and do not bring about substantive changes. On the other hand, frequent (threats of) suspensions for governance reasons hamper the advantages of budget support, in particular the predictability of funding, but also the possibility of having a fruitful policy dialogue on issues more directly related to the objective of this aid modality.

The recommendation to not use budget support as leverage for influencing governance does not mean that donors should not raise their governance concerns with a recipient government. But such a dialogue on democracy and human rights issues should be held separately from the dialogue on budget support.

In view of the fact that both general and sector budget support use government budgeting and reporting systems, these instruments can be used for improving Public Financial Management (PFM) and domestic accountability institutions. The combination of policy dialogue and accompanying technical assistance has proven to be effective, in particular for PFM and horizontal accountability institutions such as Supreme Audit Institutions. As complementary measures to budget support, donors should also consider supporting institutions for vertical accountability (the demand side), like parliament and civil society. Donors are recommended to also use other soft incentives like promoting participation in international networks.

The evidence shows that strengthening PFM systems and domestic accountability institutions brings more corruption cases into the open and sometimes also leads to more attention for corruption in parliament, in the media and among civil society. Donors should be satisfied with these positive effects. Similarly, to the case of promoting democracy and human rights, the policy dialogue should not be used as leverage for combating corruption. This means that donors should not punish revealed corruption by suspensions and withdrawals of budget support. The costs of these (threats of) suspensions in terms of reduced effectiveness of budget support are much larger than the very uncertain possible benefits.

The budget support dialogue can also focus on poverty reduction policies or on policies to foster achievement of the SDGs. As mentioned above, general budget support can focus on strategic, macro and cross-cutting issues related to these objectives, while sector budget support can deal with more detailed sector policies. In their synthesis of EC-commissioned budget support evaluations, Lawson et al. (2014: 85) recommend to focus budget support on the reduction of *income* poverty and inequality. This is based on the observation that public policies in recipient countries did not pay sufficient attention to these goals, and that the policy dialogue on budget support did not prioritise them either. They recommend “increased attention for agriculture and the productive sectors, as well as to infrastructure and employment creation” in budget support. However, no matter how important these topics are, it is not so clear that budget support resources or the policy dialogue are able to contribute to them. First, providing budget support implies funding the public sector. Whilst public resources can build infrastructure, there is no obvious link between these resources and strengthening productive sectors or increasing employment. Second, it is doubtful whether (most) donors<sup>29</sup> have sufficient analytical capacity for a meaningful participation in a policy dialogue on these topics. Donors can raise attention for the reduction of income poverty and inequality in the policy dialogue, and they can offer to finance studies on how public policies can become more

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<sup>29</sup> The World Bank is an exception, but the Bank tends to dominate the dialogue with a particular view on these issues. Other donors may foster pluralism by, for example, commissioning studies by academics from other institutions.

pro-poor. The results of these studies can then provide inputs to the policy dialogue on pro-poor public policies. The budget support resources may help financing critical infrastructure for the poor, for example electricity, water, and roads, and they may contribute to social safety net programmes in recipient countries. All in all, it seems important that the expectations with regard to the contribution of budget support resources to income poverty reduction are tempered.

The policy dialogue around general or sector budget support should be based on ownership of the recipient country, implying that the number of indicators on the PAF should be limited. The more the participating donors succeed in harmonizing disbursement criteria, secure predictable funding, and respect ownership, the more effective general and sector budget support will be.

This also means that the use of variable tranches should be avoided. Evidence from several studies shows that compliance with indicators for variable tranches is not better than for those related to fixed tranche (TTAD, 2014; Lawson et al., 2016; Ronsholt, 2014). On the negative side, variable tranches tend to lead to delays in disbursements, sometimes requiring governments to engage in additional borrowing as shown in chapter 2. The use of variable tranches also tends to focus the policy dialogue on compliance with these particular indicators, while there is often no reason to prioritise some indicators above others. In addition, these discussions on formal compliance with specific indicators may distract the attention from more strategic issues.

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## List of abbreviations

CEF	Comprehensive Evaluation Framework
CRS	Creditor Reporting System
DAC	Development Assistance Committee
DANIDA	Danish International Development Agency
Deval	German Institute for Development Evaluation
DfID	Directorate for International Development
GBS	General Budget Support
GDP	Gross Domestic Product
HDI	Human Development Index
IOB	Policy and Operations Evaluation Department
MDGs	Millennium Development Goals
ODA	Official Development Assistance
OECD	Organisation for Economic Cooperation and Development
PAF	Performance Assessment Framework
PFM	Public Financial Management
PRS	Poverty Reduction Strategy
PRSC	Poverty Reduction Support Credit
QCA	Qualitative Comparative Analysis
SAI	Supreme Audit Institution
SBS	Sector Budget Support
SDGs	Sustainable Development Goals
Sida	Swedish International Development Agency
UP	Underlying Principles

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