



# IOB Evaluation Newsletter

## # 1207

## Budget support: Conditional Results *Review of an instrument (2000-2011)*

7 | Budget Support: Conditional Results | Evaluation Newsletter # 12 07 | Budget Support: Conditional Results | Evaluation Newsletter # 12 07 | Budget Support: Conditional Results | Evaluation Newsletter # 12 07

From the late 1990s onwards, various donors provided development assistance in the form of direct support to recipient countries' budgets. The idea was that this would contribute to more harmonisation of aid and to more alignment with partner countries' priorities and thus promote ownership as well. It would lead to more efficient and more effective aid with more sustainable results.

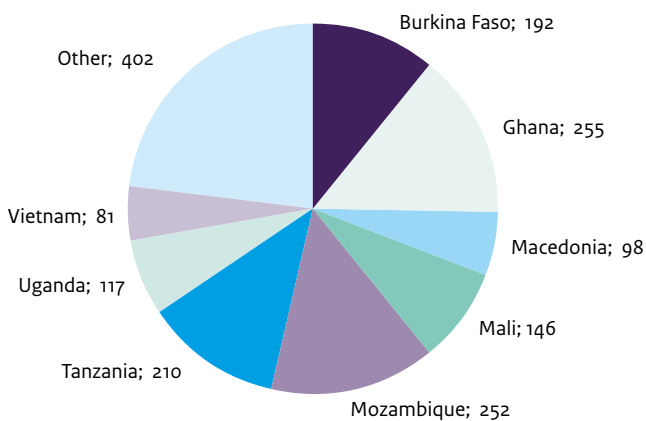
But there was criticism as well. It was feared that budget support could vanish into the pockets of officials in corrupt regimes and undermine, rather than reinforce, the desired socio-economic and political development.

The Policy and Operations Evaluation Department (IOB) of the Netherlands Ministry of Foreign Affairs has examined Dutch policy on budget support and its impact. IOB's conclusion is that the modality can be a good instrument for supporting policy in recipient countries. Budget support has contributed to economic growth and helped to extend social services, especially in education and health. Financial management and democratic control also improved. But the instrument is not suitable for pursuing major reform if it is not backed by the recipient government.

## Dutch budget support

Between 2000 and 2011, 23 countries received a total of €1.75 billion in budget support from the Netherlands. This constitutes approximately 3.4% of the Netherlands' overall assistance in this period. Most support went to Burkina Faso, Ghana, Mali, Mozambique, Tanzania and Uganda.

Figure 1: Distribution of Dutch budget support\*



\* Total expenditures in EUR million (2001-2011)

The Netherlands was a frontrunner when it comes to budget support, but initially the ministry did not have a well-developed strategy. Policy and implementation took shape gradually, and decision making was often dominated by political considerations. The objective of poverty reduction was increasingly pushed into the background, however, while promoting good governance and political dialogue moved increasingly into the foreground.

Sometime around 2008 there was a shift in thinking about the instrument. A number of serious irregularities came to light in some countries, one shortly after the other, involving human rights violations, election fraud and restrictions of political freedom. The Netherlands consequently suspended budget support to these countries. The 2010 coalition agreement attached stricter conditions to this aid modality, and shortly thereafter, the Dutch Minister for Development Cooperation ended support to most countries.

## Budget support at the international level

Global expenditure on budget support increased from US\$1.9 billion in 2002 to US\$5.3 billion in 2009. Expenditures were lower in 2010 (US\$4.7 billion), but the decrease at the international level was not nearly as steep as in the Netherlands. The most important providers were the United Kingdom, the European Union and the World Bank. Norway and Sweden also provided a relatively large amount through this modality.

Despite international agreements, budget support continued to constitute only a limited part of overall development assistance. Countries such as Tanzania (42%), Ghana (29%) and Mali (25%) received a large part of their (bilateral) aid in this form, but this was not the case for other countries, such as Nicaragua (13%) and Vietnam (10%). Budget support constituted less than 3% of almost all countries' GDP (with the exception of Burundi, Rwanda, Mozambique, Sierra Leone and Tanzania).

## Increased aid predictability

In the early years, many countries only received the support towards the end of the year, which forced them to take out expensive loans or to delay investments. Predictability improved later, though it varied significantly between countries. Delays were also caused, however, by recipient countries not always honouring their agreements on time.

## Influence on policy

On average, recipient countries used 60% of the support to increase expenditures in that same year. The rest went to reserves or served to pay off current (domestic) debts. There is no evidence that tax revenues decreased as a result of budget support. In fact, they increased in several countries.

Donors were not able to use the policy dialogue to significantly influence economic policy. Usually this was not necessary. The resources did help to improve macro-economic stability or increase expenditures on poverty reduction (especially on social services). The instrument also helped to improve governments' financial management and financial transparency. The direct contribution to general resources gave donors an argument for putting improvements in these areas on the agenda.

## Economic growth

Critics claim that budget support has a negative impact on economic growth. There is no evidence for this, however. In the past ten years, average growth figures in recipient countries were higher than in countries that received little or none of this form of assistance. International comparative research shows mixed results, but in recent years there is growing evidence that aid in general has a positive impact. The latter is also true of general budget support, though the impact is, almost by definition, modest.

## Poverty

Despite economic growth, poverty is only gradually decreasing in many countries. Poverty reduction is also a long-term effort. A few years of economic growth is not sufficient to dramatically increase

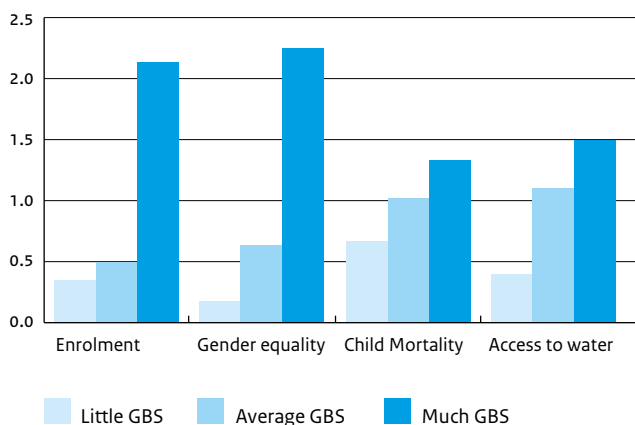
incomes in rural areas. Whether economic growth leads to poverty reduction depends mainly on the policy implemented in these countries. Donors only have limited influence.

On average, countries that received budget support achieved slightly better results, but there are large differences between countries. The direct contribution of budget support is necessarily limited: it comes down to less than six euros per inhabitant per year in the most important recipient countries, while at least half of the population in these countries lives below the poverty line.

## Access to services

Countries used the largest part of their budget support to improve social services and other activities that will impact income levels only in the long term. The poorest groups in particular have benefited from this. Although they still lag seriously behind, the gap is closing.

**Figure 2:** Impact of budget support on social indicators



School enrolment improved in Zambia from 51% to 73% in the poorest groups (between 2000 and 2007). In Tanzania it increased from 58% to 68% (2005-2010), and in Ghana from 43% to 59% (2004-2010). Lower secondary enrolment rose from 72% to 90% in Vietnam (2002-2005). Financial impediments for access to health decreased in Tanzania for the poorest 20% of the population from 52% to 42% and in Ghana from 74% to 60%. In Zambia, the government abolished user fees in health, which vastly improved access. In Mali, the number of local health care centres doubled. It was only in Nicaragua that social indicators barely improved during the period that the country received budget support, because the government did not implement a targeted poverty reduction policy (at least not until 2007).

Budget support helped to generate improvements on the UN human development index, which is based on income, education and health indicators.

## Impact on reform

Notwithstanding these results, donors did not succeed in producing more fundamental reform, such as an independent judiciary, greater involvement of civil society or ending clientelism in the public sector. Threatening to suspend or actually suspending budget support rarely generated the desired change. The fact that donors did not always act in harmony played a role in this. On the other hand, there is no shred of evidence that budget support caused governance to deteriorate. Many developing countries have achieved slightly better scores on good governance indicators in recent years, especially countries that received budget support.

## Why haven't donors achieved more?

Basically from the start, donors have not met the conditions for budget support: good socio-economic policy in recipient countries and the capacity to spend the resources effectively. As a result, there was no guarantee that ownership would be respected. Whereas the original policy theory mainly emphasised budget support as a financing instrument, the emphasis increasingly shifted onto policy dialogue. The resources not only functioned as a financial incentive but also as a means of 'buying your way in'. In addition to good (socio-economic) policy and effective governance, countries also had to improve the quality of (political) governance. In practice, donors created an extensive list of conditions in areas such as better democratic control, an independent judiciary, more citizen participation, the fight against corruption and other governance-related reforms. This was somewhat at odds with the original policy theory objectives and created potential conflicts between the original and new objectives: what should donors do if a country has a good policy for reducing poverty but has a more casual attitude towards democratic freedoms (such as Vietnam or Rwanda)?

The shifts were also clearly visible in Dutch policy making and implementation. The Netherlands increasingly put its money on objectives upon which budget support had little impact, with disregard for results in social areas. The minister emphasised on several occasions that budget support could not buy reforms, and yet that is clearly what Dutch policy aimed to do. It is telling that budget support was never terminated because the minister had doubts about recipient governments' commitment to their poverty reduction policies, but because these countries achieved poor results in the area of good governance.

The policy review shows that budget support can be an effective instrument if the donor and recipient agree on the main policy and expenditure priorities. This is highlighted by the results in education and health. But it is not possible to use budget support to enforce reforms. Financial incentives do not work for reforms that are not backed by the political elite. Threatening to suspend aid is equally ineffective. Internal political interests are often much more important.

The Policy and Operations Evaluation Department (IOB) of the Ministry of Foreign Affairs carries out independent assessments of the efficiency, effectiveness, relevance and consistency of Dutch foreign policy. It thus provides accountability concerning the results of policy, as well as information to enhance policy. The quality of the IOB's assessments is guaranteed by means of systematic and transparent procedures.

All IOB evaluations are in the public domain and are brought to the notice of parliament. The IOB also seeks to make evaluations accessible to the Dutch public and to partners in the countries concerned. Reports can be freely obtained and a summary of the most important findings is published in the form of the IOB Evaluation Newsletter.

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