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Article

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Aussenwirtschaft

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Suggested Citation: Gerster, Richard (2007) : Aid Effectiveness: The Case of General Budget Support, Aussenwirtschaft, ISSN 0004-8216, Universität St.Gallen, Schweizerisches Institut für Aussenwirtschaft und Angewandte Wirtschaftsforschung (SIAW-HSG), St.Gallen, Vol. 62, Iss. 3, pp. 343-370

This Version is available at:

<https://hdl.handle.net/10419/231133>

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Aid Effectiveness: The Case of General Budget Support

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This article describes general budget support as an instrument of development cooperation. Based on poverty reduction strategies, poorer developing countries are increasingly receiving general budget support which enables their governments to carry out their core responsibilities more effectively. Strengths, weaknesses, opportunities and risks are discussed in a holistic approach. In view of aid effectiveness and efficiency the author draws on an evaluation which was carried out in the context of the DAC/OECD in 2006, as well as on experience made in Switzerland's budget support engagement. He argues that the budget support methodology could also inspire the cooperation with non-governmental organisations.

Keywords: Economic Development Cooperation, Budget Support, Aid Effectiveness, Transaction Costs, Paris Declaration.

JEL Codes: F35, E6, F5, O19, O2.

1 Introduction

1.1 What is General Budget Support?

The characteristics of general budget support (GBS) are that it is directly channelled through the partner government's systems and that it is not earmarked for specific projects or expenditure items.¹ By making direct contributions to the state budgets of partner countries who give proof of their engagement for poverty reduction, general budget support enables these countries to carry out their core responsibilities efficiently and cost effectively – for example in the area of health or justice. The decisive elements are the government's budgetary priorities, its human resource management, its procurement rules and its accounting systems.

Disbursements are made to the ministry of finance through the central bank and depend on the fulfilment of any reform objectives that have been agreed upon in the dialogue with the government. Budget support creates leverage

* The author would like to thank SONJA BEELI for her assistance in preparing this article. He is also grateful to IVO GERMANN who commented on an early draft. The responsibility for any errors rests with the author.

1 For a discussion of the GBS definition see IDD 2006, p. 6; SPA 2007 Vol. II, p. 27.

beyond its volume because increased effectiveness and efficiency in the use of resources extends to the partner country's finances. Contrary to general budget support, sectoral budget support is earmarked for a selected area of the state's operations and therefore limited in its availability.

General budget support is no blank cheque; indeed it comprises a package of measures based on the partner government's poverty reduction strategy. The package includes: (1) the financial contribution, (2) the accompanying performance agreement which lays down the prerequisites and conditions of the cooperation, (3) a continuous dialogue on the progress of reforms, (4) technical cooperation which, for example, strengthens the government's capacities through further education and training, and (5) the harmonisation of aid procedures among the donors with a simultaneous adjustment to the processes used in the partner country. This set of instruments allows for an adaptation to the specific circumstances in a partner country.

1.2 Facts and Figures

Budget support is coordinated in groups of up to 19 donors. The members of the largest group in Mozambique are: Austria, Belgium, Canada, Denmark, Germany, the European Commission (EC), Finland, France, Great Britain, Ireland, Italy, the Netherlands, Norway, Portugal, Spain, Sweden, Switzerland, the African Development Bank and the World Bank. The „elephants“ among the donors of budget support are: the World Bank, partially the African Development Bank, the United Kingdom, the EC, Norway and Sweden. The United States are consistently absent, Japan is participating in exceptional cases.

A survey done by the Strategic Partnership with Africa (SPA) for 2005 found that the volume of budget support committed to 15 countries was 2.9 billion US\$ out of which 2.4 billion US\$ were disbursed during 2005. 43% of the disbursed amount is from the international financial institutions, 37% from bilateral donors and 20% from the EC. (SPA 2007) The following countries have the highest percentage of budget support in relation to their national income (GDP): Rwanda (8.4%), Sierra Leone (7.9%), Malawi (6.3%) and Mozambique (5.3%). The average of all 15 countries lies at 3.6%. On average, general budget support constituted 19% of the participating donors' portfolio.

GBS is part of and has become a vehicle for the wider harmonisation and alignment agenda in development cooperation. Broad cooperation and coordination among donors is a pre-condition for effective GBS provision. The Paris Declaration on Aid Effectiveness, signed in 2005 by virtually all donors, projects an increase of programme support to 66% of total public assistance by 2010. GBS and sector budget support (e.g. for health or education) are key elements of programme aid. It is therefore no surprise that a number of countries that receive GBS are equally at the forefront of the implementation of the Paris Declaration agenda. As an advanced example, the Government of Zambia has laid down its vision of development cooperation in the form of the "Zambia Aid Policy and Strategy", and the donor community has subscribed to a "Joint Assistance Strategy for Zambia" which includes a partition of labour among donors in order to change the situation in which sectors such as health and education are over-supported while justice remains an orphan. In GBS, this choice of sectors becomes obsolete anyway.

Budget support intends to support a partner country in setting up basic government framework conditions and services for the entire population. Building capacities and institutional change does not take place overnight which is why budget support needs a long breath. At the same time, in the interests of real sustainability, early exit strategies are important. In reality this aspect is often neglected. Many donors prefer dealing with the expense side of budgeting. Only a few donors, among them Switzerland, assign top priority to the mobilisation of tax revenue in the partner countries. The tax base needs to be broadened. In Mozambique, the share of foreign aid in public spending has already been reduced from 70% (1995/96) to 48% (2004). After 2010 it should amount to a mere 25%. PEDRO COUTO, Vice Minister of Finance has said:

„We do not like to beg permanently. That is why generating our own revenue is so important. We have a long way to go and depend on support until we reach our goal.” (GERSTER 2005, p. 79)

1.3 The Example of Ghana – A Success Story?

Since 2002 the government of Ghana has increased the current and investment expenses in poverty reduction from 4.8% to 8.3%.² This makes it pos-

² Numbers from the UK Department for International Development DfID, Ghana.

sible, for example, to hire 10,000 teachers. Primary education is now free of charge. In 2005, some 650,000 students were newly enrolled to school. 440 class rooms have been constructed. School enrolment has increased from 81% to 87%. Similar progress is reported from the health sector. Thanks to cautious macroeconomic management, key indicators such as inflation and interest have developed positively. This macroeconomic stability is a precondition for sustainable development. The successes are due to the government's engagement, but budget support from abroad has facilitated the changes.³ As EBENEZER MIREKU, private entrepreneur from Ghana says:

"For the business sector, doing business in Ghana today is far better than before. The striking difference between now and then is that planning is now possible, because the political and economic environment is relatively predictable." (MIREKU 2006, p. 3)

In spite of such progress, voices from the grassroots show that well-educated teachers, school books and affordable medication are still scarce goods in villages (CONWAY 2006). Participation of the population at the community level is equally marked by many weaknesses. Is Ghana a success story? Compared to the 1990s, yes – compared to the vision of the Millennium Development Goals not (yet).

1.4 Switzerland's Engagement

Towards the end of the 1980s, SECO (State Secretariat for Economic Affairs) started with balance of payments assistance in various countries. Blacklists of goods such as arms, whose import could not be financed with it, in conjunction with good governance, aimed at ensuring the development relevance of balance of payments assistance. This early form of programme aid was later converted into general budget support. Today SECO is administering budget support in Burkina Faso, Ghana, Mozambique, Nicaragua and Tanzania.⁴ The Swiss Agency for Development and Cooperation (SDC) is engaged in sectoral budget support in various countries. Switzerland's sometimes proactive and often early engagement is appreciated by its partners. Mozambique's Prime Minister LUISA DIOGO said: "Switzerland makes a difference." (GERSTER 2005, p. 78) This statement also addresses the quality of the dialogue: knowledgeable of the local context, informed by exper-

3 See ODI/CDD 2007.

4 See SECO 2005.

ience from other programmes, respectful and competent. Namely in the field of finance and tax, Switzerland complements budget support with technical assistance. In Burkina Faso, Mozambique and Nicaragua, local economists head the area department of macroeconomy in the Swiss coordination offices. SECO is successfully building and exchanging its know-how in budget support in the context of the SPA, DAC/OECD and through strategic partnerships with consultants. Yet budget support still constitutes only a few percent of Switzerland's total development cooperation.

2 Milestone DAC Evaluation

2.1 The DAC Guiding Principles on GBS⁵

In its broad based activities on aid effectiveness, the Development Assistance Committee (DAC) of the OECD identified four guiding principles for the provision of GBS:

- Budget support should reinforce partner countries' ownership;
- Budget support should help to enhance the performance and accountability of partner countries' systems of Public Financial Management (PFM);
- Transaction costs incurred by budget support should be minimised;
- Budget support should be delivered in a way that enhances the predictability of resources and reduces their volatility.

2.2 Background of the GBS Evaluation

In the context of the Development Assistance Committee (DAC) of the OECD, a broad-based evaluation of general budget support was concluded in 2006. It is said to be one of the most complex evaluations of all time. As is the case for budget support itself, cooperation was also integral to the evaluation: Great Britain, the Netherlands, Germany and even sceptics such as Japan and the USA – 14 donors in all – contributed to it. The bases for the evaluation were case studies in seven countries (Burkina Faso, Malawi, Mozambique, Nicaragua, Rwanda, Uganda, Vietnam) over the period of 1994-2004. Tanzania was evaluated separately – but in a way that was comparable to the methodologies used in the other seven countries – in 2004. Ghana followed, again separately, in 2006/07. The total costs amounted to

5 DAC 2005, p. 12-13.

more than two million Euro, which is less than one tenth of a percent of the roughly four billion dollars used for budget support during the evaluation period. Implementation, under the lead of the University of Birmingham took more than two years. (IDD and ASSOCIATES 2006, BERNASCONI 2006)

The DAC Evaluation provided elements for a critical assessment. The report of the evaluation is likely to be used as a self-service shop for selective evidence to confirm preconceived opinions about budget support. The report is differentiated due to its scientific approach. Strengths and weaknesses are reported in detail. Furthermore, as experiences with partnership-based budget support date back only a few years, instances for which it is not possible to draw well-founded conclusions are indicated. The report notes that "in all but two cases, the overall assessments by the country studies were clearly positive." (IDD and ASSOCIATES 2006, p. 3) One exception was Malawi, where a first effort got off to a false start due to over-optimistic expectations. In the second case, Nicaragua, budget support started flowing too late for the DAC Evaluation to draw conclusions. In all cases budget support was rated to provide an adequate response to the local context.

2.3 Selected Results

- Budget support contributed to the partner countries' overall economic stability and strengthened the capacities of public authorities'.
- Public expenditure focused increasingly on poverty reduction. However, the description of expenditures relevant to poverty reduction is still too vague and superficial.
- Social services, especially in the areas of education and health, expanded – yet their quality could not keep up with the increase.
- The donors' understanding of the political context in the partner countries often left much to be desired.
- The framework conditions needed for a prosperous private sector were often neglected.
- While countries such as Mozambique reported impressive rates of poverty reduction in recent years, the DAC Evaluation could not create a direct, causal link between them and budget support.
- On one hand, budget support fortifies the partners' ownership of their chosen path of development; on the other hand conditions for cooperation and policy dialogue make the line between acceptance and interference a fine one.

Based on this profile of strengths and weaknesses, the DAC Evaluation classifies budget support as an effective instrument in development cooperation, but no *panacea*. In doing so, the DAC Evaluation also clearly illustrates the limits of evaluations. Examining programme aid is far more complex than traditional project evaluations. As mentioned before, the external interventions consist of a number of diverse measures. The chain between input and impact in the sense of poverty reduction consists of many links and is exposed to numerous external forces, which make a direct attribution of success and failure to the external interventions difficult. Not only are the inputs made up of a diverse package but the envisaged reduction in poverty is equally multidimensional (income, empowerment, security).

3 Budget Support and Development Cooperation Portfolios

Currently, budget support only amounts to a few percent of total bilateral official development assistance. Numerous partner countries are pushing for an increase in budget support. Both increased room to manoeuvre and low transaction costs also point in this direction. Specifications made by partner countries are an integral part of their development cooperation strategies, which are worked out jointly with other donors (Joint Assistance Strategies). As mentioned above, the Paris Declaration on Aid Effectiveness⁶ foresees an increase in programme aid to 66% by 2010. General and sectoral budget support are important parts of programme aid. However it can be assumed that the imprecise definition of programme aid is a motivation for the adoption of statistical tricks in order not to have an obvious failure in meeting the ambitious goals. A high level review of the Paris Declaration is scheduled to take place in Ghana, in 2008.

The future development cooperation portfolio will be comprised differently, yet nobody doubts that both project and budget support will have their role to play. This is for several reasons: Not all partner countries meet the core preconditions for budget support. Being on the path towards democracy, human rights and a constitutional state is implicitly or explicitly a precondition for budget support. Neither macroeconomic stability nor a credible poverty reduction strategy are a given everywhere. General budget support would be a hazard in the case of fragile states such as Somalia or Haiti.

6 See http://www.oecd.org/document/18/0,2340,en_2649_3236398_35401554_1_1_1_1,00.html.

General budget support aims at strengthening the state in its core functions and therefore usually works with the central government as partner. Other stakeholders beyond the ministry of finance – line ministries such as agriculture or education – are equally decisive for reaching the Millennium Development Goals. Government entities in provinces or at the local level, as well as the private sector and civil society, hold a prominent place in any vision of a functioning society. Decentralised state actors can also be reached by budget support but the private sector and civil society especially are still potential partners for projects.

It should not be forgotten that donors also aim to minimise their risks. In this context it is a basic principle not to put all eggs in one basket. Furthermore, the communication of successes and failures of budget support and, through that, its understanding by the public are still in their infancy. That is why in addition to general or sectoral budget support other programmes and projects with public and private partners will remain in development cooperation portfolios.

Between general budget support and isolated project aid lie many forms of cooperation. Support for an entire sector such as health or education is closest to general budget support. Projects with government partners are often implemented through parallel structures. Instead of making use of the state channels for planning, budgeting, implementation and accounting, separate project implementation units are created, through which the state structures are increasingly weakened.⁷ Even acknowledging that official channels often are not performing satisfactorily, such parallel structures, in any case, are no sustainable solution.

Programme aid is therefore a constructive complement and challenge to the traditional forms of international cooperation: Budget support demands cooperation with other donors and in doing so is a motor for the harmonisation of the different forms of cooperation. Very practical questions such as the design of progress reports, the coordination of programme visits or the synchronisation of dates of disbursement take centre stage. Prior achievements have a positive effect on the donors' entire cooperation portfolio. When identifying performance indicators for the government, specific objectives directly strengthening project work can be incorporated from the sectors. For example, allocating sufficient funds for the water sector can be

7 Most donors maintain incoherent portfolios: On the one hand they provide budget support in order to strengthen partner government institutions; on the other hand donors undermine these budget support objectives through off-budget payments for projects. See DE RENZIO 2006, p. 631.

a precondition for the capacity building of water authorities to be fully effective. Budget support requires a holistic approach beyond sectors and stands in stark contrast to the extensive fragmentation characteristic of many cooperation portfolios, a fragmentation that goes far beyond the necessary diversification of risks. In an international analysis of 21 countries, which compares the fragmentation of development cooperation, measured by the average volume of projects, Switzerland occupies the poor rank of 19 (CENTER FOR GLOBAL DEVELOPMENT 2006).

The DAC Evaluation explicitly states that large transaction cost savings were found in the partner countries (IDD and ASSOCIATES 2006). The limits of these improvements are mainly due to the other instruments in the portfolio which are continued in parallel. The high transaction costs of project aid, particularly the smallest projects, which are generally incurred for both sides, should not be overlooked.

NGOs, among others, rightly point to the donors' power of definition, which is still strong in budget support. An area of conflict between the donors' own understanding and that of the partner government when it comes to the definition of policies cannot be negated. The fight against poverty, for example, often enjoys higher priority for the donors than for the partners, even if there is agreement on paper. In the context of project-oriented cooperation, the power to define is generally even stronger. The opportunities for interference this creates are often the reason for working in the project mode instead of budget support.

4 Selected Issues

4.1 Measuring the Progress of Reforms

Budget support is based on performance. The disbursement of payments only takes place if the government is implementing its strategy for poverty reduction successfully. That is why, in the context of budget support, the entire breadth of a government's activities is examined. A number of criteria, the so-called performance assessment framework (PAF) is negotiated in order to measure the progress of reform. The diverse set of progress indicators ranges from the percentage of girls enrolled in school to the containment of HIV/Aids; it may include the number of kilometres of improved roads, access to micro credits, the number of detainees awaiting trial, re-

structuring of various ministries, the administration's decentralisation, or the improvement of bank supervision and tax reforms.

The PAF represents a change in paradigm from the imposed conditionality of the 1980s to an approach based on partnership. The government makes a proposal, which serves as the basis for negotiation with the donor community. The level and nature of inclusion of other stakeholders, such as decentralised units of the administration, parliament and civil society, leaves much to be desired in many countries. The PAF comprises between ten and fifty indicators with a two- to five-year horizon. Its functionality depends not only on how appropriate the indicators are but also on the availability of meaningful data at the right time. The PAF aims at focussing the reform process on some key elements and at making the conditions for the disbursement of payment tranches transparent. However, the donors' influence is still strong. It is therefore not surprising to see that this change in paradigm is more often pointed out by the donor side than it is felt by the partner governments in their daily work.

When it comes to the predictability of budget support, the donors must not use any criteria that lie outside of the agreed PAF. Improved predictability is a key concern for the partner countries. Aid is predictable when the partners can depend on the volume and timing of the agreed payments (DAC 2005). Surveys conducted by the IMF have shown a dramatic lack of predictability, not only for budget support, but for aid in general. It fluctuates six to forty times more than fiscal revenue (BULIR and HAMANN 2005). Short-term predictability of budget support has improved – not least of all because progress with reforms over the past year serves as the basis for the donors' commitments for the following year. The commitments for the current year are considered to be irrevocable if basic conditions such as the protection of human rights, respect for democratic principles or keeping macroeconomic stability are adhered to. Mid-term predictability, however, is reflected as an unsolved problem by the DAC Evaluation – both for budget support and project aid.⁸ In the model country Tanzania this uncertainty amounts to five percent of national income over the next two years. “No developed countries have to take such uncertainties into account”, says ALLISTER MOON, World Bank economist in Tanzania. Predictability should increase as donors increasingly operate in a multi-year framework for budget support. Bilateral donors generally tie the continuation of their cooper-

8 IDD AND ASSOCIATES 2006, p. 53; see also SPA 2005, for reasons given by donors and partner governments for the delay of disbursements.

ation to a satisfactory judgement of the overall progress of reforms. The World Bank chooses a small number of specific indicators relating to economic policy measures from the PAF basket and makes its disbursement dependent on their performance.

Some donors, namely the European Commission and Switzerland, with Sweden, Norway and the United Kingdom occasionally joining, differentiate between fixed and variable tranches. As with all other bilateral donors, the fixed proportion of a contribution is dependent on the overall assessment of the progress of reforms, which is undertaken jointly with the government. The variable tranche, however, is tied to very specific reforms and indicators. The EC generally works with result-oriented indicators (outcome /impact) drawn from the areas of education and health. Switzerland picks indicators from selected areas, for example, the mobilisation of the state's own resources, the management of public finances or the improvement of the framework conditions for the private sector. Variable tranches allow for a more flexible reaction to insufficient progress by avoiding an "all-or-nothing" situation. This approach possibly also stimulates a result-oriented way of thinking in the administration of the partner country. Variable tranches with specific indicators are doubtless popular with donors at home. Parliament and the public like to hear that payments are tied to, for example, progress in the education sector. However, that the idea that selected reforms can be strengthened in a targeted manner by performance-related payments is bound to be an illusion. Variable tranches are too small in order to really make a difference compared to the overall volume. In specific cases, it has been found that persons from the government who were in charge of a specific sector were not even aware of these variable payments.

Identifying relevant indicators to measure the success of certain reforms is anything but simple. While, for example, everyone agrees that education, especially for girls, is an excellent investment for the future, there are different options for measuring the implementation of this investment. Should it be done based on the number of newly built school houses? If so, what about the available furniture and teaching material? It is also possible that no teachers are available because not enough young people finish secondary school and teacher training. Girls might enrol in school at the beginning of the school year but leave during the course of it because they are needed at home, or parents have decided that investing in their daughter's education is not worthwhile. Judging the progress of reform also requires the government to be able to control the chosen indicators. While the proportion of money spent on education is within its competence, it cannot

really control whether parents send their girls to school. Culture and context are equally relevant. Reality and reforms are more than just a bundle of indicators. That is why in the end an overall assessment and a strategic dialogue are more important for the continuation of the cooperation than making payments contingent upon specific indicators.

Performance-based budget support is confronted with further pitfalls and problems: The large number of participating donors makes a clear alignment towards key reforms difficult as competing priorities exist. The broad-based negotiation process provides an open door for an enlarged catalogue of measures and indicators. Clear directions given by the partner government are most effective in order to reduce the PAF's size. The trend towards outcome/impact indicators within PAFs is strongly dictated by the donors' agenda. Taxpayers in donor countries have to be presented with tangible results. Possibly the partners' impact perspective is also strengthened. A political culture that chooses approaches and sets priorities based on results achieved in the past is a precondition for such a perspective – and this is anything but a given, be it in Switzerland or the South/East.

Indicators should merely function as a measuring instrument for a broader set goal *pars pro toto*. There is, however, a certain danger that they can take on a life of their own if they serve as disbursement triggers. Measuring primary school enrolment should not detract attention from investing in and monitoring finishers or secondary school leavers. The required data may be lacking. In Zambia, the water sector remained out of the PAF despite its poverty relevance because there were no reliable statistics available. In Tanzania's PAF, progress in reforming the judicial system is measured by the number of cases that have been pending in court for more than two years. The government and donors agree that it is very difficult to collect meaningful data.

4.2 The Role of the IMF

Partner countries have to be on the way towards macroeconomic stability, in terms of low inflation, sustainable balance in foreign trade and payments, and balanced public accounts, in order to qualify for budget support. In most cases, macroeconomic stability is among the underlying principles for GBS. This may not be identical to a formal on-track status of the partner country's arrangement with the IMF. Without questioning the IMF's macroeconomic expertise, the DAC Evaluation cautions against formally tying gen-

eral budget support to a positive assessment by the IMF. This could create an accumulated risk and increase the payments' volatility.

Unlike the World Bank, the International Monetary Fund (IMF) is never a member of donors groups but has observer status. However, its Poverty Reduction and Growth Facility (PRGF) is also budget support, as the PRGF-loans are aligned to the partner government's poverty reduction strategy. But the harmonisation of the IMF's set of macroeconomic conditions with those of the other donors remains limited. In the context of increased aid, a discussion has arisen as to whether the IMF indirectly imposes an upper limit, for example, for health expenses, even if more external resources are available. In order to gain clarity about this issue, the Center for Global Development appointed a high-ranking working group.⁹ Close cooperation, though not free of tensions, between the IMF and the donor groups is the rule. In countries such as Tanzania – since January 2007 without PRGF-loans – the IMF is using a new tool, the Policy Support Instrument, in order to signal good macroeconomic conduct.¹⁰

It has happened that bilateral donors have lobbied in a coordinated manner via their capitals, in favour of changes in the decisions of the IMF Executive Board, in support of the partner country. It is well known that in the past 20 years the IMF's conditionality has constantly been criticised as being ineffective and unsocial. In spite of the substantiated nature of these criticisms, the view has become accepted that macroeconomic stability is a precondition for effective poverty reduction and therefore for budget support. This is no plea for standardised procedures. Varying contexts demand varying procedures and solutions. Pluralism with respect to economic policies is desirable, if alternative approaches are thriving on local ground.¹¹

4.3 Policy Dialogue

There is continuous dialogue between the donors and the government about the alignment of economic and social policies. The specific process of the dialogue varies from country to country. Thematic groups that are open to expertise from other institutions (university, NGO, private sector)

9 The working group is chaired by DAVID GOLDSBROUGH, see: <http://www.cgdev.org/content/article/detail/10683>.

10 There is a risk of reduced flexibility compared to the PRGF, see e.g. ODI/CDD 2007 for Ghana or GERSTER and MUTAKYAHWA 2006 for Tanzania.

11 See the paragraphs „Risks“ and „Political dimension“ further down.

meet at irregular intervals. Large rounds of discussions, so-called annual reviews, are held every year. They are based on the progress reports on the implementation of the national poverty reduction strategy. Once all parties agree on both the assessment of what has been achieved in the past year and the outlook for the coming year, which is organised by thematic groups, a short text is prepared for the final declaration "Aide Mémoire". This final declaration is agreed upon by both sides and seen to be binding. The joint text not only records successes but also identifies weaknesses.

In October 2006, the government of Tanzania and the donors discussed successes and failures of the past year as well as measures for the future. Six thematic groups prepared the dialogue: economic growth and reduction of income poverty, improved quality of life and social welfare; governance and accountability; allocation of resources and coherence of the state budget; management of public finances; and macroeconomic achievements. It was the first time that the thematic groups were also open to external circles (NGOs etc.). The dialogue in the thematic groups was followed by rounds of discussion focussing on five cross-cutting themes. Lead staff of both the responsible ministries and the donors' side participated. Thanks to this concentrated manner, the entire range of state activities and problems was displayed. It is challenging for both the government and the donors to have competent representations in these working groups and to develop a shared perspective.

In 2004, Mozambique for the first time mandated external experts with a "learning assessment" (HARDING and GERSTER 2004). Together with another independent consultant, the author has been asked by the government and all GBS donors to observe the dialogue process, the performance assessment and the accountability frame to report about its strengths, weaknesses and potential areas for improvement. Restructuring the process for the dialogue and the creation of a PAF to monitor donor performance were among the most important proposals. Conducive conditions for a learning assessment are (1) full access to all documents and discussions, (2) the independence of the team, and (3) that the final report should be in the public domain. Tanzania followed suit in 2006 (GERSTER and MUTAKYAHWA 2006) and Zambia in 2007 (GERSTER and CHIKWEKWE 2007). SPA took up the innovative instrument of the learning assessment and advocates its use. Against this background, SECO as an early mover since 2004 and now together with SPA, decided to promote its use in other countries.

4.4 Risks

Even those states that are known as ‘model pupils’ and therefore preferred by donors for administering budget support are anything but *eldorados* for development cooperation. The states are weak. Corruption is part of the daily business. The governments not only represent reformers but equally profiteers. “In the past five years, Mozambique has changed from an extreme venture to a high-risk country”, says a Swedish expert of the situation. The donors expect the partner countries to invest the money in their taxpayers’ sense (fiduciary risk), which means for poverty reduction. The banking crisis in Mozambique sharply illustrated the potential danger. Two large commercial banks in Mozambique became insolvent. The government decided to save them by injecting financial resources of more than 100 million Swiss francs. The donors only agreed to this rescue mission after hard negotiations. In return, Mozambique promised to shape the supervision of banking according to international standards and to undertake further reforms in the financial sector. The issue at stake is not only to prevent the misuse of aid money. The opportunity created by budget support lies much more in ensuring that the public finances are managed carefully overall.

Beyond the fiduciary risk of the simple misuse of money, there are also the risks of bureaucracy in the sense that money just dries up between the central ministries and the citizens at the grassroots. Poverty reduction through budget implementation is finally happening in the provinces, in the districts, at the village level and not just in the capital. Experience shows that mere trust in trickle-down would be naive. The decentralisation of government structures to facilitate services at the grassroots and the strengthening of local governments are key. The capacity of the people to insist on their rights to services and a responsive attitude by the local authorities are two sides of accountability that mitigate the risk of (non-)implementation. If parents know how much money is allocated for their school, they can make an effort to track the funding. Good practice to counterbalance the implementation risks is to (1) include indicators on decentralisation in the PAF, (2) ensure access to information and transparency about allocations, (3) enhance the empowerment of the people, e.g. through support to NGOs, (4) include decentralised tiers of administration in the budget support review process.

There is global consensus about the Millennium Development Goals. The ways to reach the goals, however, are manifold. It is a fact that – depending on the historic and political context in a country – priorities are set differently. In politics, pluralism rules, not universal recipes. Pluralism is a demo-

cratic right but it carries a risk – economic policies can be misleading, have unintended side effects or may even lead nowhere. Memories of the debate on structural adjustment programmes in the 1980s and 1990s, and their social damage, surface in this context. Besides the corruption debate, policy risks narrow the benefit of reforms for the poor (value for money).¹² The lights went out repeatedly during the annual review in Dar Es Salaam's conference centre. The energy crisis was tangible. But proposals for its solution differ, including among donors. Should the national energy company TANESCO be privatised and tariffs for energy be shaped in a cost-covering manner? The first generation of poverty reduction strategies neglected the productive private sector and prioritised – under international pressure – public services in education and health. Was this best for poverty reduction? How is equity balanced against economic growth?¹³ In any scenario, the consequences are mainly borne by the partner countries' governments and population – not by the IMF/World Bank or bilateral donors. Policy space is needed to mitigate the partners' policy risks.

Among the seven partner countries that were examined in the DAC Evaluation, Vietnam stands out.¹⁴ The donors support the government's policy and reform programmes, which deviate in relevant aspects from economic orthodoxy, for example regarding privatisation. Furthermore, political measures are non-negotiable – contrary to other countries. This is possible because the government can show impressive results in poverty reduction¹⁵, because Vietnam is an interesting market and because its dependency on external aid is limited.¹⁶ In the "diffuse" context of many African countries, the aim is to find a precarious balance between influence and understanding through dialogue. The partner government needs to be responsible for the chosen policy not only formally but also in reality, as the risks of success and failure lie in the partner country anyway.

The donor side usually has relatively large human resources at its disposal in order to analyse factual issues, develop proposals and carry on negotiations. As legitimate as this is, it can become dangerous if external interventions start competing with local capacities. This risk of crowding out exists for example vis-à-vis the administration. In 2004, in Burkina Faso the donors made a proposal for a new memorandum of understanding, which the gov-

12 As an example, see the Zambia case study AFRODAD 2007.

13 UNWIN 2004 takes a critical stand towards budget support and fears more damages than benefits for the poor if growth rather than equity stands in the foreground of economic policies.

14 Refer to BARTHOLOMEW, LEURS and McCARTY 2006 for the following specifications.

15 Between 1993 and 2002 the percentage of people living below the poverty line fell from 53% to 29%.

16 Public aid amounts to around 5% of the gross national income.

ernment declined, because it saw taking the lead in the cooperation to be their own task. A risk of displacement also exists vis-à-vis civil society. The donors find themselves in a privileged situation in the budget support dialogue with the government. It is important to take precautions in order for parliament and civil society not to be left out. Conversely, budget support can be used to increase their influence on political decisions. An important possibility is, for example, the promotion of local think tanks in order to propose alternatives in economic policy.

Foreign aid always includes the risk of displacing local sources of financing. That can be disastrous, because taxes are more than a fiscal issue. Taxpayers are demanding returns in the form of services from the state and accountability with respect to its activities. At the same time, revenue is a precondition for sustainable public finances. The DAC Evaluation that has just been concluded has found no indication that budget support has crowded out tax income in partner countries. However, the claims of budget support should go further: In view of a long-term exit strategy, the mobilisation of local state revenue needs to be promoted actively. That is why in some countries an increase in tax revenue is part of the agreement between the government and the donors.

Risks are perceived differently, depending upon one's perspective. As a result of budget support, the partner government often fears being confronted with a group of donors acting in phalanx instead of being able to negotiate individually with the respective countries and institutions. A 'united front' of donors increases the risk of a country being left with a fatal gap in the financing of its state budget in the case of disagreements or should donors cease their payments in a coordinated manner. Furthermore, instrumentalising budget support in favour of donors' interests is not something that can be ruled out completely. Unlike the government, the donors usually judge this to be a minor risk and stress instead the increased security for the government when planning its finances.

4.5 Political Dimensions

The effectiveness of budget support depends to a large extent on the domestic drive for reforms. The clientelistic nature of political systems may be in contrast to that requirement and some observers argue that donor interventions "reinforce these negative characteristics rather than contributing to the creation of more developmentally oriented states" (DE RENZIO 2006,

p. 634). The DAC Evaluation judges the political influence on partner countries to be low. Considering the long-lived efforts to embed certain political approaches in partner countries this finding is rather disillusioning. Wanting to turn over a political landscape in a partner country with external support is an unrealistic expectation. It is about democracy and adherence to human rights, which are an explicit element of budget support in all countries – with the exception of Vietnam, where the government refuses external interference. In Zambia, the government keeps budget support at arms' length from the political level and tries to have the dialogue at the level of civil servants. If partners are not convinced of innovations, influence also remains limited when it comes to macro economic issues.

A much more promising approach is the support of "think tank capacities" in the partner countries, where local scientists and politicians can develop their own schemes. In 1996, in a situation of conflict, the government of Mozambique asked for a strategic cooperation with Harvard University and with JEFFREY SACHS, for which they sought support from certain donors. With financial contributions from Switzerland, Norway and Sweden, and with the technical know how of Harvard University, it was possible to establish a research department in the Ministry of Finance, the so-called *Cabinete de Estudos*. Its primary outputs are independent analyses and proposals for the administration, which do not have to permanently seek ownership because they originate from within. Switzerland and Sweden continue to provide support for this institution at a lower level. At the same time opportunities are being examined to establish an independent think tank in order to broaden the personal and institutional basis for significant economic analyses and policies.

The issue of limited political influence relates to the fact that general budget support is particularly exposed to unpleasant political changes. The DAC guidelines on poverty reduction state that political conditionality should not be used in relation to a specific instrument of cooperation but should be part of policy dialogue. All too often, this is mere theory. If relationships deteriorate, general budget support is the first to go.¹⁷ In Uganda, as conflict with the brutal rebel movement, the Lord's Resistance Army, in the north, lead to 1,4 million people being internally displaced, and increased corruption as well as criticism of governance emerged, some donors turned towards cutting general budget support. Similarly, Ethiopia, for a long time known as the donor darling, faced a tighter state budget due to cuts in gen-

17 For the following examples Uganda and Ethiopia see SPA 2007, Vol. II, p. 39–43.

eral budget support in response to its suppression of the opposition and violation of human rights.

The donors' political situation is more important for general budget support than for other instruments of cooperation. After a shift to the right in Denmark and Canada, for example, general budget support was suspended for a longer period of time. Generally a renewed move towards conditionality in the classical sense occurs, not because partner governments would not perform when it comes to reform processes, but as a consequence of conservative movements in the donor countries' public. Or as a senior official in Tanzania says: "In order to increase the predictability of budget support we have to analyse the donors' political context in the future."

A growing percentage of budget support equals a country's increased dependency on this financial input. In four of the countries examined in the DAC Evaluation, the contributions of budget support rose above 10%: in Uganda 22.6%, Mozambique 16.3%, Burkina Faso 14.7% and Vietnam 13.9% (IDD and ASSOCIATES 2006). Generally, however, the overall dependency on all forms of development cooperation ought to be more important than merely the dependency on budget support. Taking a somewhat provocative stand, one can also ask whether it is not the donors who are increasingly dependent on the partner governments. If a state budget is co-financed to a large extent, a coordinated withdrawal by the donors also means a destabilisation of the country. Assuming normal circumstances, however, this is what is furthest from the donors' mind. Therefore it is more difficult for donors to exit from budget support than from fragmented project support. Furthermore, especially large donors such as Great Britain depend on development success in order to justify their expenses to the public. This situation impairs their capacities for criticism and action.

4.6 Accountability

When it comes to accountability, the rules and practices of partner governments at home are crucial.¹⁸ Parliament, civil society organisations, the public at large and the media are at the centre. Or as the DAC Evaluation says:

"PGBS (Partnership General Budget Support) donors (indeed all donors) need to be careful that their accountability demands do not overshadow those of national institutions. However, it is possible for

18 For an overview see DE RENZIO 2006, p. 636–641.

national accountability and accountability to donors to be mutually reinforcing." (IDD and ASSOCIATES 2006, p. 5)

This potential is not yet fully exploited, because on the donors' side, seeing their contributions used enjoys higher priority than taking an overall view of the budget. Switzerland is the only donor that disburses budget support only after parliament has approved the budget, in order to strengthen its role. A constructive process of accountability also includes possibilities for the participation of administrative units at the sub-national level. This is also true in terms of the processes that are valid for the PAF. The donors' leverage on a country's economic policies remains substantial even within the context of budget support based on partnership without conditionalities. There are critical voices that see the donors to be too closely involved in core policy processes, so that "strengthening of domestic accountability remains an elusive objective" (DE RENZIO 2006, p. 627).

Increased domestic revenues are a precondition for reducing dependency on external aid. In Zambia, for example, revenue mobilisation has a high profile. However, paying taxes is more than just a fiscal issue. Contributing to the government's revenue influences governance relations. Taxpayers become different citizens who demand effective and efficient services from the public sector. Policy makers should not only be concerned with how much taxes are raised but also whether ways and means of consensual tax relationships can be found (IDS 2007).

The fact that donor governments are accountable at home for the use of tax money influences the design of budget support. Parliament, the population, media and NGOs want to know whether the use of public funds is in line with legislation and budgetary allowances. Domestic accountability of donors has three notable implications for the partnership: (1) The set of criteria against which the reform progress of the partner government is measured includes measures and indicators of particular interest to the donors' home constituencies, which, for example, relate to corruption. (2) When granting subsidies, governments often make use of the right to administer an independent inspection with respect to the use of the money at any time. How can this be done meaningfully while respecting the partner country's sovereignty? (3) Accountability demands visible results. However, with budget support, specific progress such as an increase in school enrolment or more companies established cannot be (directly) attributed to the external contributions. Successes are less tangible and adequate reporting becomes more complex and demanding.

In addition to governmental accountability at home, a development partnership also implies a shared responsibility between donors and partners to account for achieved successes as well as failures. Donor and partner governments are accountable to each other especially when it comes to the implementation of agreed objectives: The performance agreement between the partner government and the donors has already been mentioned. Together with the dialogue, the PAF forms the core of the partner government's accountability towards the donors. The practice of each donor demanding a progress report meeting its specific formal requirements at different points in time have given way to a trend of harmonisation in which shared reports are accepted. Ideally – as is already the case in Mozambique – these are the same reports used by the government to render account towards its own parliament. Strengthening the level of information and the role of parliament in this process is more than a side effect.

Further steps towards increasing the balance in the partnership are underway. Again in Mozambique a framework, the so-called Donor PAF, has been created to require and record the donors' progress in the implementation of their obligations.¹⁹ The donors are, for example, liable for the observation of an agreed timetable of disbursements, for the coordination of missions, or for the contributions to building adequate capacities in the government. Generally these measures constitute the implementation of the Paris Declaration on Aid Effectiveness. Predictability should replace the donors' arbitrariness. However, the basic imbalance of power between donor and recipient cannot be suspended. Tanzania has for years had an "Independent Monitoring Group (IMG)" in place that regularly and independently observes government – donor relations. The 2007 Joint Assistance Strategy of Zambia equally provides for an IMG to monitor donor performance.

5 Challenges for NGOs

Today, many NGOs adopt a sceptical stand towards budget support.²⁰ Swiss NGOs have been predominantly positive for several years, first towards balance of payments assistance and later towards budget support, because it compares favourably with other instruments of economic cooperation, for example because of its focus on poorer countries. While they have demanded policy dialogue and an alignment with those sectors that have high

19 Various reports about this instrument under: http://www.gersterconsulting.ch/fs/fs_main.asp?kt=2

20 See for example Action Aid and Care 2006; AGEZ, KOO and EU 2005.

priority in terms of poverty reduction, they have also supported the general orientation. "In our opinion balance of payments assistance deserves to be increased as various reform programmes suffer from chronic underfunding", they write in a submission of 1995.²¹ More sceptical tones were heard a decade later, in the context of the international discussion of the opportunities and limitations of budget support (LAUBSCHER and NIGGLI 2006, NIGGLI 2006). In 2005 and 2006, SDC organised dialogues with the Swiss NGOs about the issue of harmonisation, during which budget support was also on the agenda. A general rejection of GBS would be difficult to justify in view of the DAC Evaluation. Nonetheless, a constructively critical stand, as it is for example taken by Eurodad, points to important weaknesses (EURODAD 2006).

A number of NGOs are afraid that expanding budget support will crowd out the resources that so far have gone to the NGOs. As there is hardly anyone who sees budget support as a *panacea*, this competition for financial resources is unlikely. The Paris Declaration with its specification of 66% of programme aid by 2010 exerts a certain pressure. The current low share can be seen as a backlog. The increase of budget support will be mainly at the expense of other bilateral instruments and will not reduce the contributions for NGOs. This is even more so as the accountability of the government towards civil society increases in importance. Competition for scarce resources could break out within the NGO community itself, because it remains to be seen whether financial contributions for the support of civil society need to be channelled through international, Northern NGOs or whether they can be allocated directly to the South. This question will be raised independently of budget support and it can only be answered based on the implications for effectiveness, efficiency and the public.

As mentioned before, the government's accountability towards parliament, NGOs and the public gains in importance through budget support. Multi-polar power and countervailing power are both a precondition and consequence of democracy and the constitutional state. If donors look at the entire society in a partner country, they strengthen not only the state, but also parliament, the private sector and civil society. This perspective becomes an opportunity and a challenge for NGOs both on the operational level as well as in the context of their lobbying efforts. Smaller donors without a political agenda, such as Switzerland, are especially well positioned to address

21 Statement by the Arbeitsgemeinschaft: Swissaid/Fastenopfer/Brot für Alle/Helvetas/Caritas, December 18, 1995.

internal accountability in the policy dialogue. In donor groups, Switzerland remarkably often held the rotating chair (2004–2007 in Mozambique, Tanzania, Burkina Faso und Nicaragua). This illustrates that large sums are not the only contributions that count, but that willingness and capacity to actively address issues such as (mutual) accountability are equally relevant. For NGO lobbying, this means that building up an adequate mix of instruments (project and programme aid, support for government and civil society) with both individual donors and donor groups should be the main concern.

The formation of strong donor groups is also relevant for NGO lobbying. The cooperation among donors also raises the question of the division of labour among donors. It is increasingly addressed by formulating Joint Assistance Strategies (JAS) of all donors in a country, as for instance in Zambia and Tanzania. It does not make sense for all donors to be engaged in education and health, and leave aside the judiciary. Equally, not every donor needs to support parliament and civil society in addition to budget support. But the group as a whole should have a holistic view of society. The already mentioned high level of fragmentation of Swiss development cooperation could also be an issue for NGOs to address.

Last but not least it is also the Southern NGOs that are challenged in the context of budget support. In Burkina Faso, SDC promotes dialogue between NGOs and the government, based on criteria that have been established by the NGOs themselves and which are used to measure the government's and administration's performance and progress (THIÉBA 2006). As a first step, information is gathered that serves to identify the most urgent problems – in the rural areas of Burkina Faso, for example – malfunctioning infrastructure, lack of access to credit or dumping competition through foreign agricultural products. On this basis the farmers involved will decide themselves what they consider high priority goals and indicators. That is how NGOs coming from the grassroots can make alternative proposals for the PAF, feeding them through the finance commission of parliament. A pilot phase has started showing both opportunities and challenges, such as insufficient access to information. This ambitious undertaking assumes sufficient capacities on the side of the NGOs as well as leeway on the political level.

Budget support is equally a cause for a methodological query regarding cooperation between NGOs and their partners in the South. Budget support as an instrument cannot only be used in cooperation with the state. The

same package of measures – financial contribution, performance agreement, dialogue, capacity building, harmonisation – also makes sense for civil society partners that fulfil basic requirements. Instead of struggling with the partners' accounting, the strategic alignment of the cooperation would take centre stage in the dialogue. Generally, NGOs have been the pioneers before innovations have been established as standards for countries. The question is, will budget support become the methodological lesson for NGOs?

6 Conclusions

The experience to date with GBS can be summarised in five key conclusions:

- (1) In order to reach the Millennium Development Goals, government performance in fulfilling its core tasks towards its citizens is crucial. GBS is an instrument to strengthen government policy and implementation capacities effectively.
- (2) The local context of the partner country in terms of governance, macroeconomic stability and poverty reduction strategies needs careful analysis to determine whether GBS is an appropriate instrument and how exactly to shape it.
- (3) GBS requires a holistic approach beyond the Ministry of Finance. Effective checks and balances in society, including parliament, civil society, and the private sector are required and may need strengthening as well.
- (4) Even if the volume of GBS continues to rise, other aid modalities with public and private partners will play important roles within the donors' cooperation portfolios of the future.
- (5) GBS is an excellent vehicle to enhance donor harmonisation and alignment to partner country systems as well as mutual accountability. The influence of the donors' domestic accountability on the cooperation modalities needs attention.

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einführen, von den bisher hochgehaltenen Prinzipien Meistbegünstigung und Inlandgleichbehandlung abrücken und zusätzliche Grenzformalitäten (Ursprungszeugnisse) aufbauen. Nach einer begrifflichen Abgrenzung der regionalen Freihandelsräume im ersten Teil geht der zweite Teil des vorliegenden Beitrags der Frage nach, warum es in der GATT- und WTO-Geschichte zu einer derartigen Ausuferung der regionalen Vereinbarungen kommen konnte. Der dritte Teil handelt von den Korrekturen, die im Rahmen der WTO notwendig wären, um die heutige Welthandelsordnung vor einer erneuten Zersplitterung zu bewahren. Ohne Gegensteuer wird die im GATT und in der WTO entstandene Welthandelsordnung zweifelsohne in ihrer Existenz gefährdet werden und an Attraktivität verlieren.

When the General Tariff and Trade Agreement was initiated in 1947, the goal of this system was the mutual opening of national markets. In the meantime, the created world trading order is in danger to split apart into regional markets. The World Trade Organization (WTO) currently counts 200 trade unions, free trade areas, preferential agreements and economic partnerships that went back to introducing their own tariffs, distanced themselves from the most favoured nation and national treatment clauses and created additional trade barriers such as certificates of origin. The first part of the paper contains a conceptional differentiation of regional free trade areas; the second part discusses the proliferation of regional agreements despite GATT and WTO. The necessary corrections are debated in the third part of the article. Without any countermeasures, the world order created by GATT and the WTO will continue to lose appeal and even be threatened in its existence.

Aid Effectiveness: The Case of General Budget Support *Richard Gerster*

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Dieser Artikel beschreibt die allgemeine Budgethilfe als Instrument der Entwicklungszusammenarbeit. Basierend auf Strategien zur Armutsbekämpfung fließt ärmeren Entwicklungsländern in zunehmendem Umfang Budgethilfe zu. Diese soll dazu beitragen, dass die Regierungen ihren Kernverpflichtungen gegenüber der Bevölkerung wirksam nachkommen können. Der vorliegende Beitrag diskutiert die Stärken, Schwächen, Möglichkeiten und Risiken von Budgethilfe im Rahmen eines ganzheitlichen Ansatzes. Im Hinblick auf die Wirksamkeit und Effizienz der Hilfe stützt sich der Autor namentlich auf eine im Rahmen der OECD durchgeführte Evaluation sowie auf Erfahrungen, welche die Schweiz im Rahmen ihrer Budgethilfe-Engagements gemacht hat. Er argumentiert, dass die Methodik der Budgethilfe auch die Zusammenarbeit mit Nicht-Regierungsorganisationen inspirieren könnte.

This article describes general budget support as an instrument of development cooperation. Based on poverty reduction strategies, poorer developing

countries are increasingly receiving general budget support which enables their governments to carry out their core responsibilities more effectively. Strengths, weaknesses, opportunities and risks are discussed in a holistic approach. In view of aid effectiveness and efficiency, the author draws on an evaluation which was carried out in the context of the DAC/OECD in 2006, as well as on experience made in Switzerland's budget support engagement. He argues that the budget support methodology could also inspire the co-operation with non-governmental organisations.

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