

# Chapter 2

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## Evaluation Essentials

- The Bank's engagement with PSR has gone through four phases.
- PSR was initially neglected, except in building institutions to carry out public investment projects that the Bank was financing.
- In the 1980s, institutional development gained recognition as a key component for carrying out policy reforms supported by development policy lending.
- In the 1990s, many became convinced that institutional development needed to be central in most CASs.
- Since 1997, the public sector and governance agenda has been formalized, and anticorruption has been added explicitly.



The north block of the Secretariat building in Delhi, India, is the administrative heart of the government.

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# Historical Overview of Public Sector Reform at the World Bank

The current prominence of public sector governance in the World Bank is a relatively recent feature of its agenda. Issues related to public sector capability have been present in Bank operations from its earliest days, above all when it came to evaluating creditworthiness and making decisions to lend and when ad hoc institutions were designed to ensure the success of specific projects.

Only recently, however, has the Bank identified governmental capability as a central obstacle to successful development and allocated an important share of its funding operations and analytical work to improving the institutional capability of borrowers, not only in the specific projects or sectors financed by the Bank, but in the overall conduct of government functions.

The Bank's engagement with PSR has gone through four main phases. The discussion of them is based on interviews with more than 45 current and former Bank staff and on review of more than 75 documents and publications (see Bibliography and appendix E [see <http://www.worldbank.org/ieg/psr/appendix.html> for appendix E]).

**1946–82**—PSR was neglected except in the building of institutions to carry out public investment projects that the Bank was financing.

**1983–89**—Institutional development gained recognition as a key component for carrying out policy reforms supported by adjustment lending.

**1990–96**—The collapse of communist states, frequent failures of macroeconomic adjustment

programs, and persistence of project loan failures in Africa convinced many people that institutional development needed to be central in most CASs.

**1997–2007**—The public sector and governance agenda was formalized, and anticorruption was added explicitly to the agenda.

## 1946 to 1982: PSR at the Margins

During the Bank's first 36 years of operation, public sector management (PSM) capacity was almost entirely absent in Bank statements, as a major determinant either of the success of Bank projects or of overall economic development in borrower countries. Only a small number of loans and technical assistance projects concerned themselves with broad institutional development in member countries, beyond the design of specific project implementation units.

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The vigorous institutional development and PSM effort by other donors suggests that the 36-year-long, almost complete absence of that work in the Bank's agenda had more to do with particular

features of the institution than with predominant development thinking. The most evident distinctive feature separating the Bank from other donors during the first two to three decades of its existence was its dependency on market financing. To raise funds in the market, the Bank cultivated a lending culture that stressed visibly and measurably productive loans, stressed the energy and transport infrastructure sectors, and downplayed social and institutional objectives. The creation of IDA in 1960 introduced a quasi-grant element into Bank lending, but Bank lending strategy remained constrained by the primacy of market funding well into the 1970s.

Among the earliest sources of contact with public administration issues were country surveys prepared by Bank missions between 1950 and 1966. In all, 25 surveys were carried out—the first in Colombia and the last in Morocco. Many touched on basic issues of administrative capabilities and political economy. Some of the reports, such as the one on Colombia, resulted in the creation of new national bodies for programming and planning or in strengthening machinery already in existence.

The Bank's initial involvement with PSM took the form of an insistence on national planning mechanisms in borrower countries (Mason and Asher 1973). The second area of institutional development in which the Bank was operationally involved was the creation of development finance institutions. Between 1950 and 1971, the Bank helped design and fund 39 such operations, mostly during the 1960s.

More broadly, the Bank was drawn increasingly into the creation, support, and guidance of project implementation units (PIUs) and sector institutions as instruments to ensure efficient management and coordination of energy, transport, and agricultural investments. The development of sector lending in particular enabled the Bank to contribute to the strengthening of government in specific areas, such as railways and communications

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in India, power in Mexico and Colombia, and ports in other countries.

Another encounter with public administration took the form of a growing volume of training and advisory work, including technical assistance missions and the creation of the Economic Development Institute in 1956—an implicit recognition of deficiencies in government capacity. By the early 1950s, there was a “growing belief at the Bank that the relatively low level of economic management in the countries which it dealt with constituted a major impediment to development” (Mason and Asher 1973, p. 324), and in 1952, the Board approved the exploration of a training initiative. Nonetheless, government managerial capacity was not a significant feature in the Bank's strategy in these years.

An exception to the prevailing neglect of government capacity during these years was a study on rural development in Africa (Lele 1975). The study contains a rich discussion of cultural factors affecting rural development and of the need “to build human and institutional development capacities.” The subsequent increase in concern for good government, in both analysis and operations, came to be closely associated with the Sub-Saharan Africa Region, where extreme governmental deficiencies became the seeds for a strategic reappraisal. A subsequent study reinforced the call for attention to government capacity (World Bank 1981).

### **1983 to 1989: Focus on Quality of Government**

Quality of government first appeared as a central developmental issue for the Bank in the 1983 World Development Report (World Bank 1983). The principal section in the report, “Management in Development,” discussed the appropriate size, role, and managerial efficiency of the state:

*Policy and institutional reform are complementary. Policies are relevant only if there is the institutional capacity to carry them out, while strong institutions are ineffective—even counterproductive—if the*

*policy framework discourages efficiency*  
(World Bank 1983).

One precipitating factor for this conceptual “bend in the road” was the strong evidence that government weakness and corruption was key to explaining the project failures and disappointing development record of the 1970s, especially in Africa. In both rich and poor countries, the previous development model had placed a great deal of faith in government, but financial crisis and economic failure naturally led to a reappraisal of government’s role and capabilities.

A new consensus developed in favor of smaller and better government. In response to the Legal Department’s objections against any political intervention by the Bank, the concern for governmental quality was cast in the politically neutral terms of managerial capacities.

The changing composition of Bank operations also contributed to the rethinking of government. During the 1970s the Bank expanded its work related to basic needs policies and its lending for education, health, and urban social infrastructure—sectors that demanded more of the general administrative capacities of governments than infrastructure lending. Furthermore, the rise in adjustment lending drew the attention of the Bank and policy makers to the institutional constraints on successful adjustment; policy reforms needed institutions that could implement them.

In 1983, the Bank created its first organizational unit dedicated to research and operational support related to administrative efficiency in government, the Public Sector Management Unit. During the 1980s, the unit devoted much of its time to the restructuring of public enterprises. Another line of PSM work was civil service reform, focusing especially on downsizing.

By 1986, in addition to the central PSM unit, specialized PSM units had been created in three Regional departments and in the Industrial Restructuring Division. A 1986 internal review of institutional development lending found that most

Bank managers were not convinced of the worth of institutional development work and that the Bank lacked intellectual and conceptual leadership in the institutional development field.

The growth of structural adjustment and sector adjustment lending throughout this period became a vehicle for an expansion and broadening of the scope of institutional development operations. Adjustment lending could accommodate a variety of concerns and targets, creating space for reform in core administration, especially in civil service and financial management, and for across-the-board reform in the management of state-owned enterprises.

A review of institutional development work carried out through sector adjustment loans between 1983 and 1987 found that 55 of 65 sector adjustment loans approved by the Bank included institutional development components and that results were mixed, with good implementation of simpler reforms but poor results with more complex and politically sensitive reforms (Paul 1990). Though much institutional development work was packaged in adjustment loans, the principal instrument for achieving institutional development was project-related and freestanding technical assistance, which accounted for 95 percent of total Bank technical assistance resources during the 1980s.

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A more complete study of PSM operations during the 1980s mirrored previous conclusions; the record was mixed. PSM successes had been limited, and roughly half the PSM effort had gone into Africa, where dramatic breakthroughs were lacking. The key problems were the political costs of bureaucratic reform and the long maturation periods required for PSM success. The relatively unsatisfactory record of institutional development efforts during these years was confirmed by a 1988 IEG review of performance evaluation, which noted that in a large number of operations the principal determinants of underperformance were institutional. A special report on Africa concluded,

“The root cause of weak performance has been the failure of public institutions” (World Bank 1989).

### 1990 to 1996: Increasing Awareness of Governance Agenda

Between 1990 and 1996, four factors increased the Bank’s awareness of the governance agenda and induced a more active response: (i) the collapse of communism, which created an unprecedented need for reconstructing the public sector; (ii) recognition of the need for “second-generation” reforms of the institutions; (iii) donors’ increasing demands and expectations for IDA as conditions for the replenishment of IDA funding; and (iv) the unacceptable failure rate of investment lending, especially in Africa. Intellectual currents also came to bear, as institutional economics helped to legitimize the governance-related concerns voiced by noneconomists.

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The operational response toward the former communist states transitioning to democracy and a market economy went through a learning process, moving from privatization and social safety support to a growing recognition of the need for core institutional and public administration development:

*At the beginning of the transition, the Bank understood the need to reorient and strengthen public sector institutions, but it greatly underestimated the consequences of still-weak core institutions and public administrations managing the transition process . . . . PSM reform has often been approached in an ad hoc manner, without a comprehensive long-term institutional development and reform strategy (IEG 2004a, p. viii).*

The Bank’s report on adjustment lending (World Bank 1990) recognized that early adjustment loans were often too optimistic about governments’ implementation capacity and reform commitment. This directed attention both to measures that enhance government implementation capabilities and to what the

*A 1992 task force justified Bank involvement in governance, particularly in political aspects that had previously been proscribed.*

report called “the political economy of reform.” In the pursuit of growth, conditionality had thus evolved to include administrative reforms as well as macroeconomic measures. Although it stated that the Bank must avoid interfering in politics, the report considered that “the cost of failure was too great for the borrowing countries and the Bank to ignore the potential contribution of a better understanding of the reality of the political economy of adjustment.”

A task force report titled *Governance and Development* (World Bank 1992a) spelled out a justification for Bank involvement in matters of governance, particularly in its more sensitive, political aspects such as the rule of law, transparency, corruption, and military expenditures. It said little about the traditional “technocratic” aspects of public sector financial and human resource management; these already had a long record in the Bank’s agenda, and the issues had more to do with efficacy than legal and political propriety.

The heart of the report was an elucidation of the relationship between economic growth and governance. The report ended by sanctioning particular governance considerations that had previously been excluded.

In October 1996, World Bank President James Wolfensohn set new precedents by speaking out against “the cancer of corruption” at that year’s Annual Meeting (Wolfensohn 1996). This speech opened the way to a more explicit discussion of the subject within the Bank. This was made acceptable under the Bank’s bylaws by redefining “the ‘C’ word not as a political issue but as something social and economic” (Mallaby 2004, p. 176).

There was a cost to this tactic in that the Bank would engage on the corruption issue while still, in practice, adhering to a prohibition against looking seriously at the political system, which is often the root cause of corruption (Thomas 2007, p. 742). Perhaps the biggest boost to the growing anticorruption movement came about because of the East Asian crisis of 1997–98, in which public opinion identified market failures with corruption, most notoriously in Indonesia.

### 1997 to 2007: PSR Efforts Become Central, Include Anticorruption

The Bank's work on broad institutional development and governance increased substantially between 1997 and 2000. This work moved to the center of CASs, as will be elaborated in the next chapter.

The 1997 World Development Report, *The State in a Changing World* (World Bank 1997b), laid out the rationale and created an official commitment for that enhanced role. In the same year, the Bank issued a report titled *Helping Countries Combat Corruption: The Role of the World Bank* (World Bank 1997a). This report stated the developmental and legal rationale for including anticorruption in the Bank's agenda; admitted that "the Bank has some catching up to do," including with its internal controls; and laid out a comprehensive operational proposal that placed anticorruption efforts within the Bank's framework for improving PSM and governance. It also highlighted cooperation with civil society and other donors.

The greater prominence of the governance theme after 1997 was more of a tipping point than a major change in the underlying forces. For a decade or more, the most powerful factor driving governance was the rising tide of democracy. This factor was most dramatic in the transition countries, but also in Latin America and, more spottily, even in some African and Middle Eastern countries. Democracy brought the rhetoric of accountability, decentralization, transparency, and rule of law, all of which relaxed the inhibitions that had previously prevented the Bank from including such topics in country dialogues with a large number of borrowers—much less incorporating them as loan conditions. A related factor was the end of the Cold War, which relaxed the pressure to support authoritarian and corrupt governments for political reasons. The Bank now had a freer hand to engage governments on governance issues.

This trend was closely related to the vigorous growth of civil society organizations and the Bank's relations with them. Nongovernmental organizations (NGOs) emerged as active devel-

opment partners of governments in social and environmental work and also as watchdogs of governments. In both roles, stronger civil society was itself a major form of institutional growth and acted as advance troops for the direction in which the Bank was going.

Non-Bank donors were moving in the same direction, placing greater priority on governance and civil society in their aid programs. They not only set an example and created expertise but also influenced the Bank from within, through financial leverage of the substantial donor trust funds managed by the Bank.

Rising concerns with corruption contributed to the strategic reformulation during this period. One cause was the publication of comparative measurements of governance, including corruption, by several sources, including Transparency International. The message of these ratings was reinforced by emerging revelations of large-scale corruption in several borrower countries. The argument that corruption was only part of a larger problem changed from a reason for inaction on corruption into a reason for action across the whole governance front.

Following the publication of the 1997 World Development Report, other circumstances came into play to reinforce a governance agenda. One was a new strategic proposal, the Comprehensive Development Framework. This framework gained important momentum in 1999 when the G-7 agreed to support an enhanced Heavily Indebted Poor Countries (HIPC) Initiative. The new initiative was tightly monitored to ensure that debt relief funds would be spent honestly and applied toward poverty reduction. The Comprehensive Development Framework was aptly suited for the across-the-board surveillance and control of governance implied by the enhanced initiative.

The step from soft IDA credits to open HIPC debt-forgiveness grants also brought into the open the issue of the fungibility of the money the Bank loaned. The rationale for financial transfers continued to be growth and poverty reduction,

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*When the fungibility of money lent by the Bank emerged as an issue, pressure increased to ensure that recipient governments were efficiently using their entire budgets.*

but, if funds were fungible, the loans could no longer be justified solely in terms of the cost benefit of specific investments or of promised policy changes.

To justify continued support, it would be necessary to assure taxpayers in donor countries that recipient governments were making honest and efficient use not only of the support received but of their entire budgets. The governance agenda, especially accountability and transparency, became both a way to improve development performance and a necessary condition for the continuation of IDA replenishments and of aid in general.

A 1997 reorganization of the Bank had a substantial effect on the Bank's capacity to expand PSR operations. One new thematic area, poverty reduction and economic management (PREM), was to carry forward the PSR agenda. Previously, PSM had been the responsibility of a small, specialized unit; after 1997 the field gained prominence and resources that allowed it to manage specialized PSM projects and influence a variety of operations in all regions. A coordinating mechanism was created around the same time—the Public Sector Board.<sup>1</sup> PREM quickly expanded its capacity for PSM, growing from about two dozen specialists in 1997 to around 200 by 2000, mostly in Regional units.

A strategy paper, *Reforming Public Institutions and Strengthening Governance: A World Bank Strategy* (World Bank 2000) set out the operational agenda for this new effort. It provided a road map for implementing an agenda of PSR for “core public institutions.” These included the civil service as a whole, public financial management, legal and judicial reform, regulation of the private sector, and decentralization. This expanded coverage highlighted the shift from past operations, which had focused on the institutional

*The 2000 strategy set out for the first time the Bank-wide agenda for PSR.*

capacity for specific projects. Corruption was to be “explicitly taken into account,” and new, programmatic lending instruments, better suited to the com-

plexities and longer time requirements of institutional change, would be developed.

The fungibility problem was acknowledged and became an argument for heightened fiduciary safeguards.<sup>2</sup> Analytic work would be increased and moved upstream and would be more participatory to enhance local ownership and align with the cultural and historical specificity of institutional reform paths and political economy.

In 1998, the Bank increased the detail and importance of the governance part of the Country Performance and Institutional Assessment (CPIA). For allocations of IDA funding, the revised CPIA placed heavier weight on the quality of government management, including transparency and corruption, as well as the technical aspects of civil service and financial management, which had been in the CPIA before. This increased the leverage for the governance agenda.

The need for fiduciary control was more directly addressed in 2004 by a multiagency partnership—including the Bank, the IMF, and several bilaterals, with a secretariat housed in the Bank—that developed a performance measurement framework for Public Expenditure and Financial Accountability (PEFA). It focused mainly on financial management, with increased weight given to transparency and accountability and the downstream phases of the budget cycle. It also considered at the margin some aspects of civil service and tax administration.

Again in 1998, another opportunity for donor coordination arose, in this case between the World Bank and the European Bank for Reconstruction and Development. This coordination led to the creation of the Business Environment and Enterprise Performance Survey (BEEPS), which measures aspects of the business environment in 22 transition countries. Other new diagnostic instruments—the IGR, the Public Expenditure Tracking Survey (PETS), and the Quantitative Service Delivery Survey—evolved at the Bank in the late 1990s to complement the PER.

The governance agenda designed between 1997 and 2000 has mostly remained in place, with two additions. The first addition was upgrading the importance of “the demand side,” meaning citizen participation, voice, and effective power in the conduct of government (see World Bank 2004b). Second, in 2006, the Bank prepared a reinforced governance and anticorruption strategy, “Strengthening World Bank Group Engagement on Governance and Anticorruption” (World Bank 2007c), which the Board approved in 2007. The strategy laid out seven principles:

- The Bank’s work on GAC is part of the mandate to address poverty reduction, not an end in itself.
- Strategy must be country driven.
- Strategy must be adapted to country circumstances, not “one size fits all.”
- Strategy requires the Bank to remain engaged even in countries with weak governance, so the poor do not “pay twice.”
- The Bank will work with many stakeholders.
- The Bank will not act in isolation, but with partners.
- The Bank will work to strengthen, not bypass, country systems through stronger institutions.

The staff, Board, and governments recognized that the effect of this strategy would depend less on the broad principals than on the specifics of implementation, with emphasis on learning by doing. The Board approved a GAC implementation plan in October 2007 with the understanding that it would be a living document, evolving to reflect the lessons of experience.

*Since 2000 the importance of citizen participation has been recognized and anticorruption has become a central concern for the Bank.*