

# Chapter 6

---



Parliament building in Cape Town, South Africa. Photo by Trevor Samson, courtesy of World Bank Photo Library.

# Strategic Summary, Ratings, and Recommendations

---

The motivation of countries for PSR has varied widely and mostly has involved factors beyond the control of the World Bank Group. Awareness of the motives is important for the Bank to choose the appropriate instruments.

## Reform Motivations, Expectations, and Success Factors

**Popular pressure** and the desire for faster economic growth and improved public services frequently motivate reform. In countries with well-established democratic processes and a free press, such as Mexico, Costa Rica, Chile, India, and the Czech Republic, the demand for PSR has been substantial.

The Bank has sometimes played an encouraging role by fueling the demand with information, working with local think tanks and academic institutions, and supporting special institutions, such as Mexico's Federal Institute for Access to Information. Participatory PERs in Tanzania, Uganda, and Vietnam that the World Bank supports have increased the popular interest in public expenditure and whetted the appetite for more information, especially in local think tanks and NGOs. But these types of PERs are still not common.

A **fiscal crisis** has frequently motivated countries to seek support from the Bank and other donors for PSR, especially if financial assistance is expected. Among the four areas of PSR discussed here, tax administration and basic financial management have been most frequently what the

government was eager to do as a remedy for fiscal crisis. Actual and potential taxpayers suffer in a fiscal crisis, so they are then more likely to support better revenue collection. South Korean businessmen were explicit about this in 1998, as they increased voluntary tax compliance to help the country during the financial crisis. The Ministry of Finance, the World Bank Group's typical counterpart, is motivated to see reforms in these areas and is the typical agent for accomplishing them.

So the fiscal crisis motivation most often leads to tax administration and PFM as entry points (Russia, Tanzania, Colombia, Indian states, and Argentina). In rare cases, the government has successfully used civil service retrenchment as a fiscal development policy measure (Tanzania and some Indian states), but more often this does not go beyond temporary freezes on salaries and hiring. Fiscal crises are almost always temporary, so except as memories they do not sustain the motivation that is needed for more complex reforms that take longer to implement.

**European Union accession** has also successfully motivated PSR, and the positive results are striking. Other factors may also have contributed

to these positive outcomes, such as completing the dual transitions to democracy and from state-planned to market economies. The governance CPIA ratings for the 10 accession countries have almost all improved since 1999.<sup>1</sup>

Although this specific model is not replicable in most other parts of the world, three features of the situation of the European Union accession countries have general lessons. First, the European Union's conditions for entry are comprehensive and standardized, with the pre-announced rewards (accession and major funding) dependent on the extent and pace with which the country meets the standards. Second, the promise of rewards and enforcement of standards are both highly credible and extend over a long period—forever on the issue of admission. Third, the European Union–accession scenario enhanced the World Bank's effectiveness by emphasizing its role as an advisor and facilitator, not an arm twister, and its relatively small financing for PSR had importance mainly through the earmark of money for technical assistance and the supervision process.

A fourth category of motivation, and one over which the Bank has considerable control, is **financial support**, which includes general budget support through loans, credits (IDA loans), grants, debt relief (HIPC), and investment loans for the costs of specific PSR activities. Budget support often carries high hopes as a motivator, but four realities have limited the effectiveness of financial support as motivation for reform:

- First, countries where the Bank has the most financial leverage have the furthest to go to improve institutions, but the weakest capacity to implement change. Countries with strong institutional capacity to implement change, in contrast, are also likely to have good access to financial markets and are thus less motivated by the attractiveness of Bank financing. Indeed, some see the acceptance of Bank financing as the price to pay for getting the expertise that comes with the money—a price these countries are still willing to pay.
- Second, the Bank is often the leader of a concert of donors, which adds to the financial leverage but also makes the demands more diverse and less focused, as each donor has its own set of priorities. The Bank has helped coordinate these demands—sometimes at a government's request—with varying degrees of success. In Tanzania and Guyana, this went relatively well, but in other cases—Bangladesh and Honduras—multiple agendas led to overly complex sets of conditions.
- Third, the Bank may find itself under pressure to lend for various reasons—international political strategy, defensive lending to avert default, or the momentum of delivering budget support on a predictable annual cycle. It has sometimes done this despite PSR conditions that are vague or not well enforced, as a way to justify the lending. This type of lending undermines the credibility the World Bank's seal of approval for PSR programs.
- Fourth, the Bank's tight schedules for commitment and disbursement of lending, especially for IDA, often conflict with the long period typically needed to implement PSR and the need to respect political cycles and build consensus and capacity. Investment projects did better in this regard, especially if they were adaptable program loans, like the public service reform loan in Tanzania. These relatively small investment projects were useful as a financial incentive to the implementing agency, but not for political ownership by the government as a whole. Consequently, the most effective PSR support from the Bank has often come in situations where the country does not urgently need lending.

**Expectations** for the progress and effects of PSR are the foundations for motivating the government to undertake them and the Bank and other donors to finance them. Thus, the ideal balance is for expectations to be high enough to motivate but not so high that they misguide efforts or that failures to meet them erode credibility and commitment. Expectations for PSR have often been unrealistic. Some of this is due to overstated goals and the mismatch of objectives with disbursement

timelines. The generic problem was recognized at least as early as the 1992 Wapenhans report (World Bank 1992a), and the programmatic development policy (now, development policy) loans and adaptable program loans were introduced as instruments to allow longer time horizons.<sup>2</sup>

Nonetheless, the momentum of high budget-support programs encouraged the search for success stories that were sometimes overhyped and led to overstated objectives, at least in the period under evaluation. Thus, compared to middle-income countries that pay essentially the full market rate for loans, the pressure to exaggerate was greater for the IDA countries, which faced if anything greater challenges to produce results in the short and medium term.

Expectations about reforming civil service and reducing corruption have been especially difficult to manage. Successful reforms in these areas have taken a long time in any country, with important historical antecedents. Although the Bank dutifully repeats the mantra of “no one size fits all,” it has not developed guidance on what pace of progress to expect, given the initial conditions in a country. Most developing countries today (such as Western Europe and the United States 150 years ago) have political systems that depend fundamentally on patronage. Some countries have progressed more quickly in recent years, but an open dialogue about the realistic expectations has been missing.

### Country PSR Strategy Entry Points

In concluding, there are two cross-cutting questions: First, what should be the scope of reforms? Second, what is the best mix of policy-based and investment lending?

There are continuing debates over whether reforms should be rapid and comprehensive in scope, taking a “big bang” approach, or incremental and opportunistic (Wescott 2006). Some stress the need for a “top-down,” politically driven, all-encompassing reform process to take advantage of narrow windows of opportunity. In contrast, North views piecemeal reforms as more

typical: “The single most important point about institutional change, which must be grasped if we are to begin to get a handle on the subject, is that institutional change is overwhelmingly incremental” (North 1990, p. 89). Although there would seem to be more evidence of success of incremental rather than strategy-driven reform, both types have worked at times, and both have sometimes failed.

One pattern we do see is that rapid reform only succeeds when there is strong support at the beginning—European Union accession countries are the best group of cases—whereas gradual reforms have sometimes succeeded when public support was initially weak (but did exist), because early successes of reform pilots builds support for more.

With either pattern of reforms, it has been useful for the Bank to get a comprehensive and politically savvy overview and strategy at the beginning, which then gets modified as events unfold. This need not be formal ESW, publicly disseminated. Sometimes a background paper on sensitive political issues can be presented as research in an academic setting, with a government representative as discussant; the Bank then need not take an official position. The case studies show that with governments unsure about doing PSR, focused and technocratic AAA (not necessarily formal ESW) has often opened the door for wider dialogue and eventually for lending support for PSR.

The Bank and its borrowing partners have tried a variety of combinations of investment lending and development policy lending, including for the support of PSR. Investment and technical assistance lending by itself can work well when the government has the appropriate policy and legal framework in place and the implementing agency has good motivation, institutional autonomy, and clear access to the funds. This is more likely to prevail in middle-income countries and more modern Indian states. Where the appropriate policy framework and incentives are not in place, an investment loan will not generate them, even with

a willing implementing agency, as in Venezuela and Argentina.

Where the country is getting substantial Provincial Reform Loan or PRSC funds, the Bank and other development partners often have assumed that governments will give adequate resources and attention to implementing institutional reforms, but this has not always happened, as seen in Uganda and Bangladesh (see IDD & Associates 2006). In such cases, the big but not always reliable inflows of budget support go to the large high-priority areas, such as education and health; this is appropriate, but the details of implementing new systems of financial management or personnel administration get bypassed.

However, in other cases, channeling aid through country systems has strengthened budget processes, including comprehensiveness and transparency. In cases where there is a multiyear investment technical assistance loan, especially an adaptable program loan, then the agency managing the project gets funds as needed for implementation but also gets the long-term and focused attention of the supervision team, which may help to improve fiduciary systems.

### Summary Evaluation Ratings

To arrive at summary ratings, the evaluation builds up from ratings in each of the four themes and differentiates AAA and funding operations. Because the borrower performance and outcome are so heterogeneous and largely beyond the Bank's control, the ratings here are for Bank performance

as a way to focus the learning process. Nonetheless, the country outcomes carry over somewhat to the ratings of Bank performance, as it contributes to outcomes.

For every cell of the resulting  $2 \times 5$  matrix, shown in table 6.1, there are examples of highly satisfactory work. So the results reflect the median, based mainly on the tasks that were done but also considering opportunities missed. Almost every borrower country needed some support in every cell of the matrix. Sometimes other development partners covered part of the program, so the Bank played a lesser role there and in some cases played none. In every case the Bank and country authorities (and often other development partners) share the credit or blame for the outcomes, with the Bank having more control and therefore more responsibility for the AAA and the countries having more control over the selection, design, and especially outcomes in the project areas.

The ratings here focus on Bank performance, particularly the more strategic aspects of setting agendas, fostering synergies within country portfolios, and allocating and organizing Bank resources. Thus, the ratings here differ from those for individual PSR projects, which are usually rated satisfactory for Bank performance.

In the PFM area, the diagnostics have developed strongly, especially since 2000, with PEFA and Public Expenditure and Institutional Reviews being highly satisfactory examples. In most cases, the Bank offered well-structured packages of lending

**Table 6.1: Overall Bank Performance Ratings, 1999–2006**

Reform area	AAA	Lending
Public expenditure and financial management	Highly satisfactory	Moderately satisfactory
Civil service and administration	Unsatisfactory	Moderately unsatisfactory
Tax administration	N.A. (IMF usually leads)	Satisfactory
Direct anticorruption and transparency	Moderately unsatisfactory	Moderately unsatisfactory
Integration and consistency across themes	Moderately unsatisfactory	Moderately unsatisfactory
Overall	Moderately satisfactory	

Source: IEG assessment.

Note: AAA = analytical and advisory activities; IMF = International Monetary Fund.

support, although sometimes the packages were overly complex or gave too little attention to behavioral aspects of institutional change. Government ownership for PFM investment projects was usually good, because the main counterparts—the ministries of finance—have a clear interest in such projects. Implementation of the budget—procurement and financial management—still has received too little attention, especially in policy reform lending projects. The set-up of Bank projects with PIUs and ring fencing has sometimes hindered improvement in financial management of the rest of the country’s resources.

For civil service, there has been some improvement in the decade since the previous IEG evaluation, but not enough. Although some projects have followed and had success with incremental approaches that emphasize improving personnel management, in other places the Bank (often with the IMF) continued to support simplistic retrenchment programs of the same sort that failed in the past. Too often CSA diagnostic AAA is simply not done before projects tackle reform, as in 8 of 18 case study countries. The absence of a good analytic and diagnostic framework hinders both AAA and projects for CSA reform. Promising pilots in a few countries have not been replicated widely or brought into a multiagency context to build international consensus for the equivalent of PEFA. Analysis and projects do not focus often enough on the features that would do the most to improve the quality and efficiency of service delivery, although there has been some movement in that direction.

Tax administration, the smallest area of Bank activity in the PSR field, illustrates the potential for reform when there is a good diagnostic and reform framework (typically led by the IMF) combined with typically enthusiastic government support and effective project management from the Bank.

Anticorruption and transparency is new as an area of its own. The Bank has done a lot of survey work that contributes to anticorruption diagnosis, especially to improve the environment for business (as with BEEPS), but there has been less diagnostic work at the country level about cor-

ruption in the core PSM areas that are the focus of this report. The CPAR and CFAA, for instance, have not usually given much attention to corruption issues pertaining to procurement and financial management. The requisite analysis of political factors in the specific country contexts was typically missing.

Even more than in other areas, top-level government ownership is essential for making progress against corruption, but the diagnostic work and program design rarely took this into account. Furthermore, adequate guidelines for how to do this did not exist, even in the 2007 GAC strategy. (The learning process under way for its implementation aims to address this, but it is beyond the scope of this evaluation.)

Because the main themes of PSR—PFM, civil service, and anticorruption—look at different sides of essentially the same phenomenon, the whole portfolio of Bank support for PSR should be greater than the sum of the parts. But it is less. Coordination and integration across the themes has often been inadequate or lacking, although this improved in some country programs during the evaluation period. The country GAC strategies, now being developed as pilots, offer an opportunity to address this shortcoming more systematically.

The overall rating for Bank performance is *moderately satisfactory*, although the picture is heterogeneous. PFM has been the largest area of Bank activity for PSR, and performance there has been moderately to highly satisfactory. This outweighs the shortcomings in other areas.

## Recommendations

There are many favorable trends in PSR that the Bank should continue to pursue and many areas where improvements are needed. This chapter highlights three recommendations.

### **Recognize the complexity and political nature of PSR**

First, the design of PSR projects and resource allocation to them needs to reflect the fact that they face more complex political and sequencing

issues than in most traditional areas of the Bank's activity. This implies, therefore, the need to (i) set project objectives with realistic recognition of the time it takes to get significant results, (ii) understand the political context, identifying prerequisites to achieve the objectives, and (iii) focus first on the basic reforms that a country needs in its initial situation and that generate political support for the process.

The PEFA indicators provide a good basis for this in the PFM area, because they will track incremental progress. As institutional change needs sustained support, that support usually needs to include investment projects; although development policy lending can help secure the enabling policy changes, it is not generally a substitute for investment loans.

The political complexity and typically longer duration of public sector reforms mean more analytical and preparatory work, including on political issues. They also mean that any one loan, especially fast disbursing, will promise more modest, incremental progress. For some countries, these changes may entail more loans per year. Investment loans will often need to have longer duration. This does not mean to stop encouraging a government to progress as fast as possible, but it does recognize the value in setting more realistic targets that, when accomplished, will enhance the credibility of public sector reform in that country and more generally.

These considerations are especially relevant for countries starting with weaker-than-average capacity, and the initial steps there may need to focus on capacity building and data collection. Countries with severe governance problems, where the "bottom billion" live, may need more AAA for PSR—nonlending technical assistance as well as formal ESW—prior to policy reform lending.

### **Prioritize PSR efforts**

Second, devote more effort at both country and thematic levels to identify in each country where PSR—including anticorruption efforts—will contribute most to poverty reduction and growth. This

would feed into the country GACs mandated by the 2007 GAC. Based on this, the country teams would clarify the sequencing and priorities with which they would be addressing the long-term agenda of reducing corruption and improving other aspects of governance.

Enabling such diagnosis at the country level may require a strategic framework from the center. The country team might meet as a group to compare and synthesize knowledge about areas where corruption is a problem. Comparing cost of corruption across all sectors may not be possible in the near term, but the country GACs could include AAA to assess the costs of corruption within specific areas that previous information (Worldwide Governance Indicators, CPIA, CPARS) identifies as problematic—such as business licensing, procurement, and tax administration.

For instance, researchers in Italy have developed a method to measure corruption by comparing the growth of infrastructure stock with amounts of spending, which in the context of Bank work would also identify the project areas where corruption is draining off the most public investment resources (Golden and Picci 2005). The Bank's diagnostic work looks comparatively at corruption costs to some extent already, as in *Doing Business* and *BEEPS*. The recommendation is to do this more systematically, aiming at comparability. An alternative approach could look comprehensively at all areas (procurement, human resources management, taxation, licensing and regulation, and so forth) of one or more sectors identified as pivotal for that country—such as natural resource management, health, or agriculture.

To complement estimates of the cost of corruption, institutional and political analysis (perhaps in the Institutional Governance Review format) would need to consider the cost and feasibility of the measures that aim to reduce the most costly types of corruption. Having zero tolerance for corruption in Bank-financed investment projects makes sense in light of their high value for development (that is why the Bank finances them) and the strong institutional mechanisms that are

available to fight corruption in these projects. These justifications from the country point of view are in addition to the rationale of protecting the anticorruption reputation of the Bank.

To reduce the negative effect of corruption on growth and poverty reduction, Bank support for PSR should emphasize (i) building systems (in areas such as PFM, procurement, tax administration, and human resources management and information systems, as well as in licensing and registration services, social services, and so on) that reduce the opportunities for corruption that is most costly to development (including any that might be in Bank-supported projects) and (ii) making better information public (as with PETS, EITI, publicly discussed PERs, citizen report cards, and so forth) in ways that stimulate public demand for more efficient and less corrupt service delivery.

Building the capacity of demand-side institutions, like the legislature and its audit office and the news media, is often needed to complement the measures to improve access to information. Only when the country has both strong political will and an adequate judiciary system should the Bank's support for anticorruption put primary emphasis on anticorruption laws and commissions.

### **Set a better framework for CSA**

Third, keep CSA reforms (including human resources management systems) as a major component of PSR, but design and implement them

with a better framework, and give more attention to the budget-execution phases of PFM. Despite the difficulties of improving CSA reform, it is not something that can be ignored. Improving PFM to the point where it gets beyond just processes and has real effects on public service performance and accountability has not happened without also improving the civil service.

A better framework for CSA reform will require things such as elaboration and implementation of a PEFA-like set of actionable indicators for CSA performance, which is foreseen in the 2007 GAC strategy. There may need to be variants corresponding to different types of public administrations—such as presidential, continental European, and Whitehall. These indicators would guide the analysis of CSA issues in CASs/Country Partnership Strategies, as would AAA and lending.

As the framework for CSA diagnosis and reform improves, the Bank's staffing for public management, including the civil service area, may need enhancement in line with its importance in the lending programs. Finding resources for this will face the usual budget constraints, and management may consider shifting some resources out of standard macroeconomic analysis, especially where the Bank's program is relatively small and the IMF already does a lot of analytic work. For instance, the Bank might consider having a political scientist or public management specialist with some macroeconomics background as the core of its team for some small countries.