18 Key Principles of PFM Reform in MENA

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**Introduction:** While circumstances vary by country, there are some generic principles for PFM reform. For this Quick Note these principles were drawn from the personal experience (within and outside the World Bank) of the author as well as selected readings presented at the end of the note.

1- **First, Define the Problem.** The starting point for reform is asking what the problem is. Officials embrace change more readily when faced with specific problems that they must address. If the problems are not internally recognized, reform attempts, even if externally financed and supported, is more likely to fail.

2- **Develop a PFM Strategy, but Remain Flexible.** PFM reforms benefit from being implemented as part of a home-grown, country-led comprehensive PFM strategy. PFM reform strategies that assume that a developing country’s budgetary systems can be up-graded to OECD standards within the typical multi-year span of a donor funded project—and without an appropriate enabling institutional environment—are unrealistic.

3- **In Most Cases, Say No to the “Big Bang”** It is important to take a holistic approach to reform—but this does not mean launching simultaneous multiple large-scale projects. Such a “big bang” approach requires conditions rare in most developing countries: political opportunities, government stability, skills, information, and organization. It entails intensive coordination with multiple stakeholders, and does not allow for absorptive capacity to grow as the reform initiative expands.

4- **“Basics First”—But Agree on What Constitutes “Basics”** Countries with low capacity should focus first on the basics (the foundation) on which the reforms are to be built. The “basics” could include for example:

- a well-functioning budgeting input that generates a comprehensive and credible annual budget;
- budget execution controls and spending ceilings that are consistent with the country’s fiscal policy and targets;
- reliable accounting system that meet the IPSAS - cash reporting standards for central government operations;
- efficient cash management, including a single treasury account and sound internal controls that avoid arrears;
- complete, timely, regular, and transparent financial reporting; and

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5- Beyond the Basics: Approach with Care! The decision to move beyond the basics to more advanced functions should be determined by country and reform circumstances. This transition must be adequately sequenced as when governments tried to “leap-frog” to more sophisticated reforms—such as performance budgets, and accrual accounts—most failed because of premature implementation and limited ownership.

6- Beware of the Allure of “Best Practices” Benchmarking a country’s status to peer comparator countries with relatively similar contexts, and identifying the “good practices” that can be adapted to the local context, is a better approach.

7- Deal with Ongoing PFM Reforms: It’s Complicated! Successful ongoing reforms could be incorporated in the new reform. Nonetheless, in some cases, tough choices will need to be made to terminate, delay, or modify ongoing reform elements if their costs outweigh their benefits.

8- Nontechnical Factors: Ignore Them and They May Sink Your Reform. Success of reforms depends to a large extent on the nontechnical context—that is, political, economic, institutional, and organizational factors. It is essential to analyze these factors and adjust the reform to mitigate risks. In some circumstances, an analysis of the nontechnical factors will lead to a conclusion that launching reform is not possible at a given time, or that certain implementation actions need to be delayed.

9- Recognize the Strengths and Limitations of the Ministry of Finance. Having a wide array of champions both inside and outside of the Ministry of Finance will help move PFM reform forward, especially in countries where ministers are replaced frequently. In most cases, however, securing the firm support and long-term commitment of the Minister of Finance is essential for the PFM reform to succeed.

10- Look Beyond the Ministry of Finance. It is crucial to understand and take into account the relationships among the different players and stakeholders in PFM reform. The allocation of roles and responsibilities among these players varies substantially from country to country (e.g., centralized versus decentralized structures). The wider political economy context is critically important, and is shaped by several institutional interfaces—formal political institutions, administrative institutions, civil society, and external actors—as well as by such structural constraints as the degree of ethnic fragmentation.

11- Ensure That Accountants and Economists Work Well Together. PFM experts may compete over the leadership of a PFM reform process. Accountants tend to focus on improved controls, accounting, reporting, and internal and external auditing systems, whereas economists concentrate on budgeting, fiscal discipline, and macroeconomic issues. Both sets of skills are vital for the success of PFM reforms.

12- Develop Feedback Loops. Having accurate, timely, and meaningful feed-back loops, from both state and non-state actors, is crucial to making PFM reforms more effective. Such feedback loops lead to smarter project design that reflects lessons of the past, midcourse corrections, and improvements, instead of relying on late evaluations. They also inform subsequent decision-making—for example, when considering whether to move beyond the basics to more advanced reforms.

13- Manage the Risk of Failure. In a note on “Sequencing PFM Reforms,” Jack Diamond summarizes the five correlated dimensions influencing the overall risk of failure in PFM reforms: “the scope, the degree of behavior change involved, the number of institutions covered, the time required for completion, and the reform action’s ‘visibility.’” He also proposes three guiding principles for sequencing: “First, whenever possible minimize reform risks while maximizing reform impact. Second, match the risk profile of reform actions to the risk environment. Third, allow flexibility in deciding between different sequencing strategies.”

14- Life Happens. Natural disasters happen, economic shocks occur, revolutions erupt, elections are lost, Ministers of Finance are replaced, government priorities change, and donors develop new strategies. To respond to these unforeseen events the PFM reform strategy must be designed
with flexibility and with the understanding that a well-thought-out change of course during implementation is not a sign of failure, but is the best way forward.

**15- Mind the Gap.** Analyzing PEFA scores, Matt Andrews has distinguished between PFM dimensions linked to legislation, processes, and procedures (that is, de jure reforms) from those linked to implementation (that is, de facto reforms). He finds that average scores for de jure dimensions are consistently higher than those of de facto ones. In many cases, instead of focusing on closing the gap between laws and practice and helping countries implement approved budgets (the challenging part of PFM reform), some PFM practitioners, donors and countries focus on introducing more laws and decrees (the easier part of PFM reform).

**16- Manage the Donors and their Consultants.** All donors and PFM experts agree that (i) PFM reforms need to be home-grown and country-led, and (ii) donor coordination is crucial. However, the exact opposite often happens: donors develop the reforms, and international consultants lead their implementation (often on the excuse of weak country capacity). There are excellent examples of donor coordination and country leadership that need to become more frequent.

**17- Remember: Communication Matters.** Strategic use of communication increases the chance of achieving successful PFM reforms and may help mitigate many of the risks related to their non-technical aspects, such as a lack of political will to instigate reform. Toward this end, key elements of a communications strategy will need to be developed, including: defining communication objectives; targeting key groups; utilization of media outlets; and delineation of messages.

**18- Fragile and Conflict-Affected States (FCS): Appreciate the Diversity.** Most of the principles discussed here apply to FCS but their interpretation may be different. For example, in some FCS, focusing reform efforts on budgetary execution could be a priority over budgetary preparation. Also, the number of donors tends to be much higher in FCS, posing a challenge for aid coordination and harmonization. It is important to recognize that FCS states are quite diverse and what works in Iraq may not be appropriate in Yemen.

Suggested references that inspired some of the ideas in this article:


- Diamond, Jack. 2013. “Good Practice Note on Sequencing PFM Reforms.” PEFA.


