

Public Expenditure Analysis and Management in the Republic of Kariba: A Case Study

*Developing More Effective Ways
to Control and Manage
Government Resources*

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with Rick Stapenhurst



The Economic Development Institute
of the World Bank

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Foreword

One of the principal objectives of EDI's Governance program is to help expand a government's capacity to improve service delivery to the public. It does this by adding an emphasis on changing mindsets and developing leadership to the more traditional approaches of public sector capacity building of promoting conventional technical tools and skills-building at the central government level.

The Regulatory Reform and Private Enterprise division of the Economic Development Institute of the World Bank (EDIRP) adapts its approach to the promotion of good governance to client country circumstance. Thus, for example, it has facilitated public awareness raising workshops at both a regional and national level in Sub-Saharan Africa (Uganda, Tanzania, Malawi, and Mauritius), Eastern and Central Europe (Ukraine and Georgia), Latin America (Bolivia and Nicaragua), and South Asia. Elsewhere, it has developed and implemented workshops to strengthen those institutions that play a role in curbing corruption: parliaments (in Ghana, Ethiopia, and Uganda), the media (in Francophone Africa, Indian Ocean countries, Uganda, and Tanzania), and supreme audit institutions (in Ghana and Zambia).

Sound financial management systems are powerful instruments for preventing, discovering, or facilitating the punishment of fraud and corruption. Budget reform is an important element of public sector reform, which in turn incorporates elements of skills-building and institutional strengthening.

Governments should match policy, affordability, structures with functions, but they should undertake only what they can do well, given their own resource constraints. Empirical studies suggest that corruption afflicts the allocation of budget resources, especially

those devoted to education. A well-functioning budget system can help ensure the matching of government policy with affordability and, in so doing, minimize the possibilities of “financial leakage” and at the same time greatly assist the work of those “oversight” institutions, such as the auditor general, the Public Accounts Committee, and Parliament.

EDI, in collaboration with World Bank Operations and Ministries of Finance in client countries has facilitated workshops in reforming budget processes. This case study is an outgrowth of such workshops. Set in the fictitious country of Kariba, it concentrates on how senior officials can develop more effective ways to control and manage government resources. It highlights the principal elements of a well-functioning system of expenditure management, including strategic focus, transparency, predictability, accountability, affordability, accuracy, timeliness, flexibility, and efficiency in the use of resources.

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Teaching notes for this case study are also available.

Introduction[†]

Edward Phillips barely had time to prepare for the task force meeting. As the new director of the Budget Office in the Republic of Kariba, he had just assumed his formal duties last week—leaving a promising career as professor of public finance at the national university for what he hoped would be a relatively brief stint in public service. His predecessor had been summarily dismissed on the grounds that he was neither able to bring any discipline to the resource allocation process nor to provide any useful advice on effectively managing the machinery of government.

When the Permanent Secretary of Finance urged Phillips to accept the position, he had argued forcefully that Phillips' knowledge and expertise could help reform a situation that was far from optimal. The allocation of resources over the recent past did not reflect the government's priorities, and individual ministers and their ministries were, for the most part, pursuing their own agendas.

In an attempt to begin the process of reform, the permanent secretary had recently appointed a task force to advise the government on upgrading Kariba's current system of expenditure management. Its membership included Mia Petrovic, deputy governor of the Bank of Kariba; Louis Gerrard, auditor general; Patricia Barre, permanent secretary of the Ministry of Health; Colin McNamara, permanent secretary of the Ministry of Education; Peter Hurst, permanent secretary from the Cabinet Office responsible for policy; as well as José Eduardo, permanent secretary from the Cabinet Office responsible for the management of the public service. Phillips himself, as director of the Budget Office, would act as chair.

As he prepared for the first meeting of the task force, Phillips reflected upon the serious problems that were

[†] The circumstances presented within this case have been drawn from a composite of actual country experiences. The characters are fictional.

confronting his country and the critical role of the Budget Office in addressing them.

Background Notes

Kariba, a former British colony, became independent in the early 1960s. Before independence, Kariba had a small but fairly professional public service, adequate infrastructure, a well-developed system of education, and a decent health care system. It was considered a middle-income country with abundant mineral resources. Fertile land and a benign climate enabled production of a great variety of agricultural products for its own use as well as for export. Hydropower both was and is its primary energy source, with some surplus available for export. All petroleum and natural gas are imported.

For more than 30 years after independence, Kariba was governed by a single party and president, whose attitude toward the private sector ranged from indifference to outright hostility. At various periods, Kariba has been confronted with guerrilla conflicts in several bordering states, which necessitated spending significant sums on national defense and foreign representation. The public sector grew rapidly during the 1960s and 1970s and was viewed as the engine for national development. Prior to the 1980s, Kariba prospered, in large measure because of world demand for its non-renewable resources—in particular, its large copper deposits.

Copper prices declined precipitously in the early 1980s, leading to a rapid drop in government revenues. Assuming, incorrectly as it turned out, that this decline resulted from short-term market fluctuations and not long-term reduction in demand due to the growing use of fiber optic cable, the government borrowed heavily abroad and continued to pursue an expansionary fiscal and monetary policy at home. Predictably, the country's international indebtedness grew to alarming proportions. Consequently, several bouts of hyperinflation resulted in a series of devaluations for the local currency, the ngo.

Against a backdrop of increasing macroeconomic instability, a new government was elected in 1992. It sought to reverse many of the policies of its predecessor, including adopting a tight fiscal and monetary policy to reduce inflation and stabilize the currency, and privatizing a number of loss-making state enterprises. This approach lowered the inflation rate and reduced several of the more prominent drains upon the state treasury.

Kariba currently has a population of roughly 10 million, twice what it was at independence. Although its population density is relatively low by international standards, at well over 3 percent its rate of growth is one of the highest in the world. Most inhabitants live in the urban areas. Many have a low level of education, live in shantytowns, and support themselves with intermittent low-skilled work.

Kariba has seen its position drop from middle-income status to one of the poorest countries in the world. At independence, it had over US\$1 billion in the treasury, but the country's current debt now stands at almost US\$5 billion. Its per capita income has declined steadily over the last three decades to the current level of roughly US\$550. Real growth has been either declining or holding at the same level for most of the last 20 years, and real income is now roughly half what it was in the 1960s. In spite of its fertile land and climate, the country is often a net importer of basic food stuffs.

After more than 30 years of one-party rule, the new government has inherited a public service that is overstaffed, underpaid, demoralized, and unproductive. Chronic under-investment in public infrastructure has resulted in poor quality roads, hospitals, schools, etc. The percentage of students enrolled in primary education is declining, and infant mortality is increasing. The crime rate is growing, and the ability of the police to maintain law and order is being severely tested.

The mandate of the government expires later this year, and an election will be held in the fall. The

ruling party is expected to form the next government, as the other parties are fragmented, poorly financed, and not well organized. Nevertheless, support for the ruling party has been waning, and senior government officials are reluctant to jeopardize their standing among the Civil Service by engaging in any major downsizing at this time. The international situation has improved, and there are currently no significant internal or external threats. However, the army remains powerful and, if provoked, could be a threat to the government.

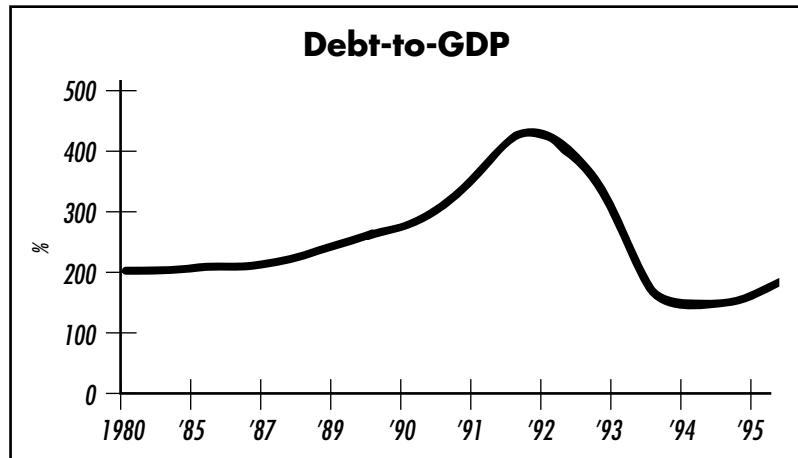
The Initial Meeting of the Task Force

Against this sobering background, Edward Phillips convened the first meeting of the Task Force on Expenditure Management. All of the task force members were dedicated professionals and the meeting began promptly at the appointed hour. After a brief round of introductions, Phillips outlined the nature of the task force's mission: to restructure Kariba's current budget process to enhance fiscal discipline and to ensure that resources be allocated to high-priority government programs.

He then asked Mia Petrovic, deputy governor of the Bank of Kariba, to offer some brief remarks regarding the macroeconomic framework under which government fiscal policy and expenditure reform would have to take place.

Macroeconomic Framework

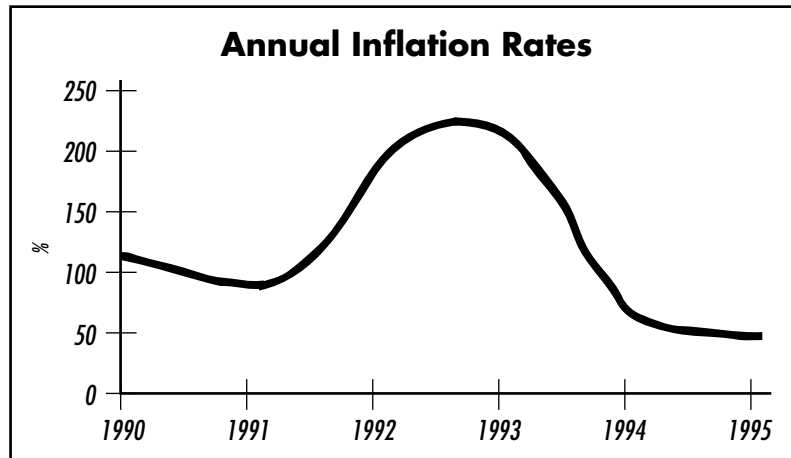
Petrovic, a dynamic woman in her mid-40s, made a number of points related to the consequences of the fiscal and monetary policies that had been pursued over the last two decades. She noted that, as a consequence of the government's having relied on borrowed capital to bridge the gap between revenues and outlays, a growing share of revenue was now required simply to service the debt. The debt-to-GDP ratio had increased steadily over time, and by 1980 it amounted to 200 percent. It peaked at over 400 percent in the early 1990s and currently hovers



around 185 percent. This, in her view, was high by any international standard.

Petrovic noted that high annual deficits generally create two related sets of problems: an increase in the size of the national debt, and inflation. She reminded her audience that the annual deficits from the previous regime's expansionary fiscal policy had resulted in an ever-increasing stock of government obligations that had to be serviced. These servicing costs represented a non-discretionary demand on government resources. If the debt was not repaid at maturity, it must be "rolled over" at the prevailing rates, and Kariba would be left hostage to exogenous shocks rather than being able to fully control her own agenda. Excessive government borrowing in the domestic market effectively "crowded out" other potential borrowers, thereby stifling capital investment by the business sector. This, she opined, had profoundly damaged Kariba's economic capacity and ability to compete internationally.

Since a significant portion of Kariba's debt had been financed through the creation of money, Petrovic reminded her listeners of the inflationary consequences of "monetizing" the debt. She noted that Kariba had recently experienced several peri-



ods of high inflation, which in turn resulted in several currency devaluations. Annual inflation rates exceeded 50 percent for the first half of the 1990s, and they peaked at nearly 200 percent in 1992 before abating. Inflation rates are currently in the 30 percent range.

Petrovic noted that the initial effect of devaluation had been to make exports more competitive. However, given that Kariba's exporting businesses relied, in large measure, upon importing equipment, the initial competitive advantages of devaluation quickly evaporated. Inflation had a devastating effect on individuals whose income was fixed. It tended to favor business and individual investors in capital assets, while putting those who had invested in domestic financial assets at a disadvantage. It also favored domestic debtors at the expense of domestic financial investors. In a brief aside, Petrovic voiced her opinion that inflation also had an implicit redistributive effect on various expenditures. It tended to favor more politically sensitive programs—such as wages and defense expenditures—at the expense of less politically sensitive programs.

Petrovic concluded by underscoring the need for strict fiscal and monetary discipline. She noted that the nation's economic difficulties had resulted in a

pronounced decline in the resources available to the public sector. The ratio of public expenditures to GDP dropped from about 40 percent in the 1980s to less than 20 percent today—a real decline of about 50 percent. In addition, a greater share of total expenditures was required simply to service the debt. Although some recent developments on the revenue side held promise, it was unlikely that there would be any real increase in the level of aggregate government expenditures over the next two years. Ministries and agencies would have to toe the line, improve their productivity, and learn to get more from less.

Priorities and Expenditure Patterns

After Petrovic finished, Peter Hurst, Permanent Secretary from the Cabinet Office responsible for policy, noted that evidently in the current circumstances the government can no longer continue to fully fund all of its obligations. Priorities would have to be set. The Cabinet agreed, in principle, that scarce government resources would, after interest payments, be directed to the social, economic, and law and order sectors. Expenditures on programs that did not contribute directly to either the economic or the social benefit of the country would be given a lower priority.

Patricia Barre—the tough and outspoken Permanent Secretary for Health—interrupted Hurst. She told him that the government had been espousing this policy for the last three years, yet results had unfolded quite differently. During this period, the share of expenditures devoted to the high priority sectors declined rather than increased. Expenditures devoted to the social sector declined from 34 percent in 1988 to only 19 percent by 1995. Similarly, the share of expenditures going to the economic sector declined from 19 percent in 1986 to only 10 percent in 1995. Expenditures in the law and order sector declined from 6 percent in 1983 to only 3 percent by 1995. Conversely, the share of expenditures devoted to defense and foreign affairs re-

mained virtually unchanged over the 10-year period ending in 1995, while the cost of running the government had more than doubled.

Although initially caught off guard by the permanent secretary's intervention, Hurst quickly recovered. He acknowledged that there had occasionally been some deviation between Cabinet policy and the actual distribution of expenditures. However, he argued, the ministries and operating departments themselves bore considerable responsibility for these deviations. The distribution of resources within sectors, for example, was often inconsistent with the government's stated priorities.

Turning directly toward Barre, he noted that—in the case of expenditures on health—the government's stated objective was for universal access to affordable health care of good quality, close to the family. How-

Program Expenditures by Sector

(percentage of total)

	<i>Debt service</i>	<i>Economic</i>	<i>Social</i>	<i>Law and order</i>	<i>Foreign affairs</i>	<i>Defense</i>	<i>Machinery of gov't.</i>	<i>Total</i>
1983	17	16	33	6	2	11	15	100
1984	14	16	34	6	2	14	14	100
1985	18	15	33	5	1	15	13	100
1986	24	19	24	3	2	12	16	100
1987	18	11	29	4	4	16	18	100
1988	14	18	32	4	3	17	12	100
1989	7	18	23	3	2	16	31	100
1990	7	17	29	4	3	15	25	100
1991	13	12	22	3	2	14	34	100
1992	12	12	23	3	2	14	34	100
1993	14	12	23	3	3	14	31	100
1994	11	10	17	3	2	12	45	100
1995	15	10	19	3	3	11	39	100

Health Expenditures by Percentage of Distribution—A

	<i>1980–90 average</i>	<i>1991</i>	<i>1992</i>	<i>1993</i>	<i>1994</i>	<i>1995</i>
Administration	8	10	11	14	17	21
Supplies	10	14	17	16	14	9
Local institutions	13	18	16	12	9	5
Major hospitals	29	25	24	25	28	29
Other health services	40	33	32	33	32	36
Total	100	100	100	100	100	100

ever, over the past decade, spending on primary health care had declined by almost a third. Moreover, an ever-increasing share of the health care budget had been devoted to administration—mainly in the form of wages—with the ratio of funds going to the larger hospitals remaining fairly constant. By comparison, the share of the budget directed to local institutions had declined from 18 percent to only 5 percent.

Thus, while the demand for health care had been rising—due to such factors as the rapid population growth and increased public awareness—the quality of health care had been declining, especially in local institutions and at the primary level.

Hurst maintained that health was not unique in this regard. Glancing at the Permanent Secretary for education, he noted that the government's stated objective was to improve both access to education as well as the quality of primary education. Yet, in spite of the government's stated objective, the portion of the education budget devoted to primary education continued to decline from 52 percent to only 40 percent over a five-year period. By comparison, the portion of the budget devoted to secondary education increased from 26 percent to 34 percent. Similarly, the budget for university education increased from 22 percent to 25 percent of the education budget. Hurst also noted

Health Expenditures by Percentage of Distribution—B

	<i>1980–90 average</i>	<i>1991</i>	<i>1992</i>	<i>1993</i>	<i>1994</i>	<i>1995</i>
Primary preventive	37	34	30	35	24	24
Tertiary	36	40	34	35	36	38
Administration	27	26	36	30	40	38
Total	100	100	100	100	100	100

that the cost per secondary school student was eight times higher than spending at the primary level and the cost per university student was 254 times greater.

Finally, Hurst observed that, within the education budget, a growing share was required simply to cover the cost of salaries and boarding, and a declining share was going to learning material. All of this underscored his original point that government had to set priorities. Should Kariba opt for CAT scans in the university hospital, or malaria treatment in the countryside? University education for the elite, or primary education for all? These decisions had been made at the center, yet the ministries repeatedly failed to allocate their resources according to government priorities. In his view, this situation had to change and it had to change quickly.

Education Expenditures by Percentage of Distribution—A

	<i>1990</i>	<i>1991</i>	<i>1992</i>	<i>1993</i>	<i>1994</i>	<i>1995</i>
Primary	52	50	53	41	41	40
Secondary	26	25	31	34	34	34
University	22	25	16	25	25	25
Total	100	100	100	100	100	100

Education Expenditures by Percentage Distribution—B

	1990	1995
Salaries	40	56
Boarding costs	30	36
Learning materials	20	9
General administration	10	5
Total	100	100

The Cash Budget

The Permanent Secretary for Education, Colin McNamara, could not let criticism of his ministry pass without a response. Strongly supported by the Permanent Secretary for Health, he argued that all of the ministries agree that any blame for the failure to allocate resources in line with Cabinet priorities rested squarely with the government's decision two years ago to move to a cash budget. This approach, in which the government spent only the monies that it had on hand or could borrow at prevailing market rates, had created tremendous disruptions in the ability of operating agencies to plan strategically and to implement government policy effectively.

McNamara and Barre reminded their colleagues that, to be assured that there was sufficient cash in the bank to meet outstanding obligations, the Ministry of Finance only disbursed funds on what was essentially a day-to-day basis. Thus, while Cabinet may have allocated resources and Parliament subsequently appropriated them, ministries were unsure of the actual amount of money they would actually receive. In practice, disbursements varied considerably from the figures listed in the formal budget, and some ministries received as little as 40 percent of what they sought. Furthermore, even the sums the Ministry of Finance eventually disbursed were released at inconvenient times in an apparently arbitrary and non-transparent fashion.

Confronted with this uncertainty, ministries could not plan from one week to the next—and strategic multiyear planning is a waste of time. Any funds the Ministry of Finance released were first used to take care of the backlog of accumulated bills. Remaining funds were quickly claimed by other commitments, regardless of actual operational requirements. All of the ministries knew, McNamara stated, that their unused funds may be scooped up by the Ministry of Finance at any moment.

Finally, McNamara revealed that, to maximize potential allocations from the Ministry of Finance, ministries tended to submit overstated cost estimates. Any rational official would do the same, he contended, when confronted with the dysfunctional incentive system maintained by the central agencies.

This notwithstanding, Auditor General Louis Gerrard reminded his colleagues of the rationale for moving to a cash budget: In the early 1990s, the International Monetary Fund had become increasingly concerned about the government's fiscal and monetary policies and insisted that this move be a precondition for further aid from the international community. The cash budget was intended to pressure the government into hold expenditures within the limits of current revenue. And it had largely been successful. Inflation is down and the currency stabilized. The government—by setting priorities and making hard choices among competing programs—was meeting its deficit reduction targets.

Gerrard admitted, however, that the move to a cash budget had resulted in a number of unintended negative effects. In the first instance, funds had tended to gravitate away from less politically sensitive sectors, such as the social and economic sectors, in favor of defense and foreign affairs. The cash budget had also resulted in a number of hidden “outstanding liabilities,” as ministries waited to pay creditors for goods and services received until the Ministry of Finance actually released the funds. Both expenditures and the annual deficit tended to be understated.

The auditor general noted that, from the perspective of both his office and the Ministry of Finance, the type of actions Permanent Secretaries McNamara and Barre described provided the rationale for closely monitoring and controlling the ministries. Staff in the central agencies were convinced that, if left on their own, the ministries would spend the funds allocated to them without due regard for good cash management. Ministries frequently incurred commitments up to their authorized limit (and occasionally beyond), even though they knew that actual disbursements tended to be significantly lower. The Ministry of Finance was invariably left picking up the tab.

At this point Permanent Secretary McNamara noted that it was difficult for authorizing officers to monitor spending effectively given the poor status of Kariba's accounting and budget controls. Financial information on expenditures was typically several months late, seldom comprehensive, and often inaccurate.

Gerrard conceded that the government's accounting systems needed to be improved. However, in his view, the problem was not just one of receiving accurate and timely information. Ministries, agencies, and departments occasionally spent funds on initiatives sanctioned neither by Cabinet nor Parliament. Gerrard noted that funding for general administrative expenses, which included numerous trips abroad for permanent secretaries and deputy permanent secretaries, was invariably well over budget in many of the ministries. However, ministries often spent only a small fraction of their allotted budget on recurrent departmental charges, such as supplies. As a result, government employees often lacked stationery and equipment, infirmaries were frequently without medications, and children had to share or do without textbooks.

Gerrard concluded that, in his view, the fundamental problem was that most ministries viewed themselves as spending agencies and had not accepted responsibility for managing their budget. Expenditure

controls were not practiced rigorously. Commitments were not well documented, nor were they closely related to the budget. Accounting control was viewed as the exclusive responsibility of his office, and many in the Civil Service did not consider budget management to be a part of their work program.

Why should they, Barre shot back, when all of their accounting personnel were seconded from the Auditor's Office? These were the officers who controlled the checkbook.

At this point, Edward Phillips summarized their conversation so far, taking care to emphasize the points of commonality. He noted that there appeared to be consensus among the members of the task force that, as a result of a move to a cash budget, a wide gap had developed between the Ministry of Finance and other central agencies and the operating ministries. The Ministry of Finance was inclined to pursue a control-and-manage approach toward ministries. For their part, ministries tended to supply the Ministry of Finance with information that would ensure that they got as much of the available resources as possible regardless of actual costs or needs. This situation did not augur well for any sort of corporate approach to management, strategic planning, or good cost estimation.

The O'Toole- Michaels Report

Just before assuming the post of budget director, Phillips received a detailed report on Kariba's current system of expenditure management, drafted by Malcolm "Chips" O'Toole and Steve Michaels, two notable international consultants who played a major role in implementing innovative budget reforms in an obscure British dependency in the South Pacific. The report was highly critical of a number of aspects of Kariba's current system of expenditure management. Phillips took this opportunity to share its contents with member of the task force.

The report contended that expenditure planning involves several interconnected components. These

components included the players—policymakers, planners, and operators—and the programs required to deliver the government’s agenda, the proper costing of these programs, and even decisions about the most appropriate planning period. Each component played an integral role in the delivery of the government’s agenda. Moreover, the expenditure plan was only as good as its weakest link. O’Toole and Michaels examined each element of Kariba’s current system and benchmarked it against best practice.

The Policymakers

As the government’s key policymakers, Cabinet ministers play a pivotal role in the expenditure process. One of the most important functions of the Cabinet is to establish priorities for the government. This occurs first at the macro level, in the form of overall fiscal targets, and second at the micro level, in the allocation of government resources among individual sectors. These priorities form a blueprint for the other players to follow. Therefore, the priorities must be clearly established, be transparent, and have the commitment of the whole Cabinet. It is critical that, to the greatest extent possible, policymakers avoid giving mixed signals or frequently amending priorities.

In the case of Kariba, O’Toole and Michaels observed that the current situation was far from ideal. While the Cabinet set out its priorities, those priorities were often poorly recorded and disseminated, so that even permanent secretaries were frequently unaware of them. New developments often forced repeated adjustments. The forecast of revenues had been, on balance, overly optimistic, and expenditure forecasts had been routinely understated. The resulting fiscal forecasts lacked credibility and required continuous amendments in the expenditure framework.

Furthermore, individual Cabinet ministers tended to pursue their own agenda once they left the Cabinet room. In one celebrated incident, the Minister of Defense—one of the most powerful and

ruthless men in the country—called the previous director of budget three months into the fiscal year and demanded that his entire annual budget be released immediately. The director complied. This resulted in a severe reduction in the funds available for other ministries and precipitated a minor crisis in the Cabinet that eventually contributed to the budget director's abrupt departure.

The Planners

O'Toole and Michaels went on to note that, once the government's priorities had been established, the next step was to develop an action plan to ensure that the government's objectives could be realized. Normally, the role of planning was delegated to the central agencies—usually the Cabinet Office and Ministry of Finance. Line ministries could also play an important role in the planning process. Their involvement at this stage helped to foster corporate vision, which reduced the risk of the plan being side-tracked by other agendas. Line ministries were also often best placed to recommend the most efficient and effective programs for delivering the government's agenda.

Here again, the situation in Kariba was far from ideal. While the central agencies had made some attempts to develop an action plan, the exercise had been found lacking on a number of fronts. As previously noted, the government's agenda was predicated on a set of economic and fiscal assumptions that were frequently suspect, which made it difficult for the central agencies to have faith in any plans based on them.

The involvement of operating ministries in the planning process to date has been virtually nonexistent. In instances where operating ministries provided cost estimates, the central agencies either heavily discounted or ignored the estimates. Thus, the ministries have few incentives to produce good cost estimates or to suggest cost-containing alternatives to deliver the government's agenda.

The Operators

The permanent secretaries of the various ministries should play a pivotal role in implementing the government's agenda. Their role is to translate into the actual programs the priorities established by the Cabinet and laid out in the action plan developed by the Cabinet Office and the Ministry of Finance. However, in Kariba, ministries tend to follow their own agenda. Since permanent secretaries report to individual ministers, their first allegiance is to their immediate superior, and the corporate priorities of the Cabinet are relegated to lower status. The Cabinet Office neither reviews the permanent secretaries nor sanctions failure to pursue the government's agenda.

Within the ministries, few permanent secretaries spent much time addressing budgetary issues. They perceived this task to be tedious and somewhat artificial and delegated it to junior clerks within their budget offices.

Permanent secretaries were also fairly disengaged from the whole process of program monitoring and evaluation. O'Toole and Michaels noted that the normal review of programs by operating ministries had been the exception rather than the rule, and programs were typically reviewed only by the central agencies. Any change to existing programs was almost always driven by the central agencies, which—in light of their general unfamiliarity with the issues at stake—occasionally made costly mistakes. This approach also made it difficult to identify the responsibility center for a program that was not generating the intended results. The central agencies alleged that operating ministries would ascribe any shortcomings to problems in the design of the program by central agencies.

Budget Systems and Time Lines

O'Toole and Michaels noted that Kariba had experienced a long and painful series of unsuccessful efforts at budgetary reform. On the recommendation of several donor agencies in the late 1960s, the Ministry of Finance attempted to implement a program planning

and budgeting system. The objective of this effort was to move away from the incrementalism and heavy bias toward historic expenditure patterns implicit within a traditional line-item budget and to use techniques such as cost-benefit analysis and cost effectiveness to put Kariba's expenditures on a more rational and objective basis. This attempt failed for a number of reasons, including the difficulty in defining and accurately costing government programs, the rigidities involved in changing or adjusting programs once established, and weak analytic capacity in the line ministries and provinces. In the 1970s, the country briefly flirted with a zero-based budgeting system, but it proved too cumbersome to implement and failed to correct the strong bias toward historical expenditure norms.

Kariba currently uses a traditional, incremental line-item budgeting system for recurrent expenditures and a development budget and public investment program for capital expenditures. The former is managed by the Budget Office in the Ministry of Finance, and the latter by the Ministry for National Economic Recovery and Development. Under the current budget process, the Ministry of Finance receives macroeconomic forecasts for the next fiscal year (which is identical to the calendar year) from the National Economic Planning Board in March. It then issues a call circular to the ministries outlining the general revenue and expenditure parameters under which they are to prepare their budgets in April. Ministries prepare their budgets during July and August, typically by multiplying their historic expenditure levels by the figures they receive in the call circular. They meet with the Ministry of Finance in September and October to discuss and negotiate these sums. The budget is finalized in November and debated in Cabinet in December. The president then presents it to Parliament for approval in mid-January, which typically takes from four to six weeks. Often the budget for the existing fiscal year is not often approved until late February or early March.

In theory, the capital budget is derived from the first year of the public investment program, which is

rolled over annually. However, O’Toole and Michaels noted that the links between the public investment program and the annual recurrent budget were poorly developed. It was not uncommon for projects to be approved with significant downstream expenditure implications without the knowledge or approval of the Budget Office. The public investment program currently contains more than 150 projects, several of which have been on the list for over a decade. The total cost of these projects amounts to 8 percent of Kariba’s current gross domestic product (GDP), whereas annual funding for capital expenditures has been running at around 2 percent of GDP. In light of the large gap between the demand for capital investment and the actual funds available for it, the government has been forced to spread its limited resources thinly over a large number of projects, delaying the estimated completion dates for many of them but avoiding the political difficulties involved in canceling sensitive projects.

The government has marketed the public investment program aggressively to bilateral and multilateral donors. It has achieved considerable success in gaining funds for historic preservation, cultural enrichment, and the environment, with the promise that it will put up significant matching funds in return.

The report went on to note that choosing the appropriate period for setting the expenditure framework is very important. On the one hand, too short a planning time may not allow delivery on the government’s agenda. On the other hand, too long a time may prove unrealistic given the number of factors that could give rise to the need for change. The challenge, O’Toole and Michaels argued, is to choose the time horizon that avoids the pitfalls of either extreme.

In the case of Kariba the government has tended to concentrate on a very short period—usually the current fiscal year. One can appreciate the motivation for choosing such a period in light of the government’s precarious fiscal position and its need to carefully

monitor the cash budget. However, concentration on the short term has effectively precluded any strategic medium-term approach to planning. To adopt a more strategic approach to investment programming and to ensure that the downstream implications for current spending decisions are fully captured in the recurrent budget, O'Toole and Michaels strongly recommended that Kariba adopt a medium-term expenditure framework.

The Costing of Programs

Finally, O'Toole and Michaels observed that Kariba's current budget does not accurately reflect the cost of providing public goods and services. They recommended that the government give due consideration to both input factors—wages, supplies, capital, etc.—and output factors—the quality and quantity of the goods or services to be delivered. On the input side, the costing should be driven by current costs as opposed to historical costs and it should be based on true costing and not simply “incrementalism.” The input factors should be determined not on the basis of the status quo but on the most efficient way of delivering the programs in the future.

Coping with the Wage Bill

Phillips concluded his summary of the O'Toole–Michaels report. From the comments around the table, he noted that the participants generally agree with its diagnosis, but less so with its prescriptions.

Patricia Barre and Colin McNamara, the permanent secretaries for health and education, again took the lead. They argued that they in fact have much less control over their budgets than the report implies. This is particularly true in the area of personnel emoluments, where the central agencies exercise great influence over the bulk of the line ministries' recurrent budget. They also contended that the general hiring freeze imposed by the center is making it very difficult for ministries to deliver on their mandate.

Estimated Employment in Local and Central Government

Education	64,900
Health	18,800
Law and order	18,700
General	
Administrators	35,900
Technicians	9,000
Managers	2,100
Total	149,400

José Eduardo, the elderly but influential permanent secretary from the Cabinet Office responsible for public service management, intervened in the discussion. He noted that, in the case of Kariba, personnel emoluments were both the largest single component of recurrent expenditures and the fastest growing. Over the 15-year period from 1975 to 1990, public sector employment increased from 20 percent of total employment to over 40 percent. The public sector had now become the main employer in Kariba, and both the central and local government currently accounted for roughly 150,000 employees.

The wage bill accounted for about 4 percent of the GDP and consumed an ever-growing share of recurrent expenditures. Corrective action was, Eduardo contended, required to address the situation so as to free up the funds necessary to finance the supplies and capital expenditures required to properly deliver government programs. He observed that in 1990 the funds available for basic supplies were roughly equal to the wage bill; however, by 1995, this ratio had declined by roughly 50 percent.

Eduardo acknowledged that central agencies had exercised a relatively high level of control over wages and salaries, but he argued that this was true in many countries. In Kariba, the need for strict central con-

trol over both the size of the wage bill and the number of people permanently employed stemmed from a number of factors, including the past performance of the ministries, the tight fiscal position of the government, and the fact that the center would probably have to bear any additional costs in reducing excess labor.

Eduardo noted that wages were among the most rigid and inflexible public sector expenditures, since reducing the size or mix of permanent employees often gives rise to expensive incentive packages to induce them to leave. Kariba could achieve reductions in the size of the public sector labor in several ways. The most cost effective form of rationalization would be through normal attrition, often accompanied by a hiring freeze. (In some instances, there may not be a match between those who remain in the public service and the skills required to perform particular tasks, so some selective hiring may be in order.) This, he noted, is normally carried out on a case-by-case basis with the concurrence of a central agency.

To the extent that normal attrition is insufficient to accommodate the planned reduction in the labor force, other options were often required. One approach was to reduce the work week, with a corresponding reduction in the wages and salaries paid to each person. This approach would not increase the unemployment level—a major concern in the case of Kariba.

Other options tended to be more costly but are otherwise effective. Departure incentives could be offered to redundant employees, which could take the form of early retirement for employees with a relatively long record of employment in the public sector and who meet certain age criteria. For other employees, cash incentives may be necessary; these tended to be on the order of two weeks' pay per year of service. Another alternative would be to freeze the salary of surplus employees or alternatively to gradually reduce their current salary over a specified number of years. This tended to provide a strong incentive for affected employees to seek alternative employment; it was also preferable to freezing or awarding lower

increases to the whole of the public service, which could have an adverse effect on morale, result in an exodus of the brighter and more valuable employees, and make recruitment more difficult.

At this point, the auditor general observed that the promotion of employees through the ranks appeared to have been a function of the number of years a person had been in the public service, rather than on the need for the function or the person's performance. There was no evidence, to his knowledge, of any internal audit function on matters related to performance, classification, continuing need for a function, or the actual verification of a match between the individuals on the payroll and the individuals in the labor force. This lack of control, he suggested, result in persons being paid for jobs that they were not qualified to perform; persons being paid for jobs that are redundant; and incidences of bogus employees on the payroll.

Gerrard observed that, to help control the increase in the wage bill, the government had often granted across-the-board wage increases at a level below the level of inflation. This resulted in a decline in real wages per employee of some 50 percent over the past two decades. The end result was that the average wage of persons on the payroll was, for the most part, substantially below the poverty level, and many were engaged in part-time employment in the private sector to supplement their income. Levels of absenteeism were high, morale and productivity were low, and requests for "incentive payments" to speed up the delivery of government goods and services were common.

Many participants noted that attempts to undertake any meaningful downsizing have been, for the most part, unsuccessful. Under current contractual arrangements, redundancy measures are extremely costly and may total as much as four or five times an employee's annual salary. These incentives must be paid in cash, which is particularly problematic for a government operating on a cash budget regime.

The permanent secretaries from the operating ministries blamed the central agencies for the current situation, pointing to the control they command on staffing, wage settlements, and contract arrangements with employees' unions. The central agencies blamed the operating ministries and cited incidents such as the large number of redundant positions, improper or inflated position classifications, disregard for numerous staffing freezes, bogus employees on the payroll, and the high incidence of temporary employees on ministry staffs. The director of the Budget Office noted that the lack of clear delineation of the responsibilities related to the management of the public service is a matter of urgent concern.

Conclusion

Edward Phillips thanked the members of the task force for what had in his opinion been a lengthy but productive meeting. He observed that there was general consensus regarding the critical need for a well-articulated plan to effect changes in both the way in which the machinery of government was functioning and the manner in which scarce resources were being allocated. He asked the participants to consider before their next meeting what should be the fundamental elements of an action plan for rectifying the problems they identified.

As the task force members departed, Phillips pondered the appropriate course of action. Clearly, the current system lacked credibility and was not supporting the efficient and effective allocation of resources in accordance with government priorities. Equally clearly, fundamental reform was necessary. But beyond these basic points, opinions differed widely and sharply. What were the most pressing issues to be addressed? How could the task force develop a viable action plan for implementing them? How could they convince the participants in the budget process to go along with their recommendations?

Questions

1. How credible is the current budget system? What are its principal weaknesses?
2. What are the principal issues that should guide any reform of Kariba's budget system?
3. Which Ministries will support efforts to move to a more transparent and predictable budget system? Which Ministries will oppose such efforts? Why?
4. What should Phillips do? What should his next steps be?

