TOWARD A MEDIUM-TERM EXPENDITURE FRAMEWORK (MTEF)

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A Medium-Term *Expenditure* Framework must flow from a Medium-Term *Fiscal* Framework, which rests on the Medium-Term Macroeconomic Framework.

The government expenditure pattern cannot be defined in isolation from the broader fiscal prospects, which must be in turn have been defined in the context of the overall macroeconomic prospects.
THE MTFF

- Includes both revenues and expenditure
- In principle, expenditure should be defined first—based on society’s preferences—and then revenue raised to finance those expenditures
- In practice, programming must iterate back and forth from forecast revenue to expenditure, to reach a package consistent with the overall policies and targets for the economy as a whole
- Analyze fiscal prospects as a whole—no item should be exempt from scrutiny or defined as a mere residual.
MTEF

- Why a medium-term perspective?
  - one year is too short to adjust priorities
  - in any given year, the discretionary margin is small—phasing out programs or introducing new ones takes time
  - realistic expenditure projections signal to the public the direction of change
  - the annual budget must reflect:
    - future funding of entitlements
    - future recurrent costs of investment
    - contingencies affecting fiscal risk.
  - An MTEF is not a multi-year budget
VARIANTS OF MEDIUM-TERM EXPENDITURE PLANNING

- **Traditional planning**: covers all major programs over fixed period. Provides vision, but is rigid and, because it is not revenue-constrained, can be unrealistic.

- **Forecasting MTEF**: medium-term top-down projections of an estimate of aggregate expenditure for each ministry and agency, reformulated each year.

- **Programming MTEF**: (see figure)
  - revenue constrained
  - built from the bottom up
  - entails clear distinction between ongoing and new programs; thus
  - defines fiscal space for new programs.
ILLUSTRATION OF A 4-YEAR MTEF

- Revenue = Expenditure
- Projected revenue
- Expenditure on existing programs
- Available resources for new programs
KEY ELEMENTS OF AN MTEF

- Sound revenue forecast comes first
- Estimate medium-term costs of *current* policies (*on-going programs*), taking into account growth, inflation, demographic and other factors built in the policies. (Because some ongoing programs/projects will be completed, the aggregate cost will decline.)
- Cost out proposed *new programs*, consistent with govt policy
- Adjust *aggregate* cost of new programs to the projected *net* revenue
- Do not allocate in advance projected net resources to each ministry (they will take it as an entitlement)
- ‘Roll’ the MTEF yearly & use as the framework for the annual budget.
It is critical to:

- Provide for sound preparation and appraisal of large projects
- Assure predictability of resources for project completion—with procedure for multi-year authorization
- Monitor closely both financial and physical implementation of projects, including through direct feedback
- Estimate recurrent cost of projects—critical for effectiveness of investment and the integrity of the MTEF
ESTIMATING RECURRENT COSTS

- **Objective:** quantify the impact on future current budgets, to underpin sustainability and prevent wasting assets. **Steps include:**
  - Limit detailed estimation to large projects (approximate calculation for small projects)
  - Collect standard cost norms from inter-national experience and technical manuals (structure for easy retrieval and updating)
  - Decide on time period over which to estimate recurrent costs (at least 5 years)
  - In TORs for feasibility studies require to estimate recurrent costs
Decide on major cost elements to be independently estimated

Formulate *simple*, *standard* format, suitable for aggregation

For large projects, examine alternative variants of project design that have different combinations of initial investment and future recurrent costs;

Because MTEF is updated annually, recurrent cost estimates must also be reviewed and updated annually as called for by changes in projected inflation, interest rates, import prices, etc.
WHAT SORT OF ANIMAL IS IT?

- **Encourage “black cows”** – sound, well-financed projects with demonstrated impact on productivity
- **Control “pink piglets”** – small projects, usually for patronage, systems maintenance or political/regional reasons. Don’t waste time on each, but limit *total* expenditure
- Watch out for **“white elephants”**
- very costly, ideological or “prestige” projects with large future expenditure requirements. Contraception is the only effective strategy against White Elephants – once they are conceived it’s usually too late to stop them.
- late to stop them.
Programmatic MTEF is complex, and requires substantial capacity and elements of program budgeting. Be prepared for a gradual and long effort, but plan for a few quick results:

- Start with a simple 3-year rolling forecast of aggregate expenditure, by sector, consistent with MTFF and MTMF.
- Introduce bottom-up programming for a few programs, based on in-depth analysis and allowing learning by doing.
- Gradually expand to other programs, and «fill in» MTEF from the bottom up.
SOME TECHNICAL ISSUES

- Cooperation vs coordination
- Contingency reserves?
- Fostering savings? «Efficiency dividends»
- Length? «Need versus capacity paradox»
- Current or constant prices?
- Relationship between policies, programs, and expected results
RELATIONSHIP BETWEEN POLICIES, PROGRAMS AND EXPECTED RESULTS

Policy goals

\[ \text{Program objectives} \]

\[ \text{Planned outcomes } \rightarrow \text{ process } \leftarrow \text{ Actual outcomes} \]

\[ \text{(effectiveness)} \]

\[ \text{Planned outputs } \rightarrow \text{ process } \leftarrow \text{ Actual outputs} \]

\[ \text{(efficiency)} \]

\[ \text{Planned inputs } \rightarrow \text{ process } \leftarrow \text{ Actual inputs} \]
SOME TECHNICAL AND INSTITUTIONAL REQUIREMENTS

- Adequate revenue forecasting procedures and systems in place
- Program appraisal and costing procedures gradually developed
- A modicum of fiscal discipline
- Reasonably good information
- Appropriate participation
- MTEF publicity and dissemination
SOME PRACTICAL LESSONS

- **Three do’s:**
  - Fullest feedback from frontline staff
  - Monitor developments closely
  - Expand gradually, and when reach the point of diminishing returns-- STOP

- **And three don’t’s:**
  - Don't develop MTEF only from the top down and only by prescription
  - Don't try for a “Big Bang”
  - Don't forget reality checks”
MAIN ADVANTAGES OF MTEF...

- The very attempt at introducing MTEF generates awareness of the need to look beyond the immediate urgencies.
- It can help improve the link to policy and budget transparency.
- With its implicit emphasis on results of expenditure, MTEF can spur greater attention to efficiency and effectiveness of public spending.
- It fosters an improvement in line ministries’ capacity, and their eventual empowerment and accountability.
...SOME PROBLEMS...

- Bureaucratic resistance
- Weak local ownership
- Large transaction costs place heavy strain on limited budgeting capacity
- Can be a distraction from urgent budget issues

...AND TWO GENERAL LESSONS

- When you hear ‘best practice’ call the cops
- Adapt, don’t adopt
A formal medium-term expenditure framework can cause substantial waste, frustration, and illusion—if it is premature or badly implemented.

If it is realistically constructed, an MTEF can strengthen the budget machinery, but cannot substitute for it.

However, a medium-term perspective for annual budgeting is essential in any case—in order to inject into the budgeting system an awareness of the future, and provide for a systematic and robust DIALOGUE on the results of public spending.