

Good Practice Guidance Note

Implementing a Medium-Term Perspective to Budgeting in the Context of National Poverty Reduction Strategies

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1. Introduction

This Guidance Note is based on a *Synthesis Report* reviewing country experience with the implementation of Medium Term Expenditure Frameworks (MTEFs) and the links being made to national poverty reduction strategies (PRSPs).¹ The Synthesis is based on nine country case studies: Albania, Benin, Burkina Faso, Cameroon, Ghana, Rwanda, South Africa, Tanzania, and Uganda. Except for the Albania case, which was prepared separately and is included with the kind permission of the World Bank author, all the cases were undertaken between June and October 2002 with the financial assistance of DFID and the EC. Consultants carrying out the case studies followed a common checklist of questions covering the main features of MTEF functioning, organisational and institutional integration and links with the national Poverty Reduction Strategy (PRSP) and other strategic planning processes.

This Guidance Note is an attempt to translate some of the main findings and messages from the *Synthesis Report* and the *Case Studies* into a set of principles and practices for those working in the field of public expenditure reform and poverty reduction.

2. Objectives

1. To identify good and improving practices that will be of use to practitioners and donors in developing a medium term perspective to budgeting and building more effective linkages with national priorities for poverty reduction.
2. To provide guidance on how to manage the relationships between donor-supported processes and the capacity of national and local authorities to allocate and use resources efficiently and effectively in line with national priorities.
3. As part of the above, to illustrate ways of improving the linkages between budgetary processes and the preparation and implementation of national Poverty Reduction Strategies.

¹ This Guidance Note was prepared by Alison Evans and Malcolm Holmes with assistance from Tim Williamson and Karin Christiansen (both ODI/CAPE). The Synthesis Report prepared by Malcolm Holmes and Alison Evans plus the individual country case studies by various authors are available at www.odi.org.uk/pppg

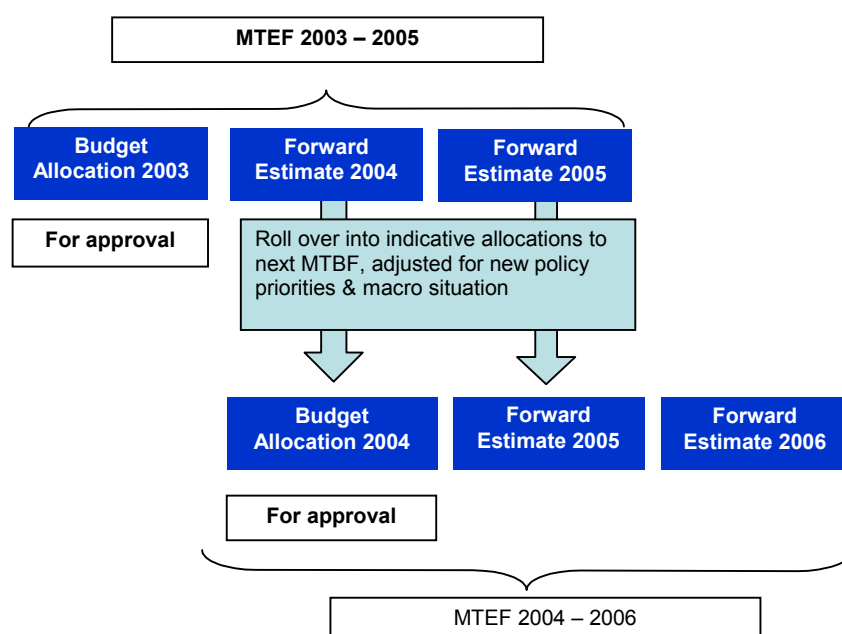
3. What is a medium term perspective to budgeting?

A medium term perspective to budgeting is increasingly recognised as crucial to the effective linking of policy, planning and resources. The specific instruments, **generically referred to as Medium Term Expenditure Frameworks or MTEFs**², are becoming important elements of the latest approaches to budget management and, increasingly, of the new ‘comprehensive’ approach to international development.

The appeal of MTEFs lies in their potential to link the often competing short term imperatives of macroeconomic stabilisation with the medium and longer term demands on the budget to contribute to improved policy making and planning, and to the efficiency and effectiveness of service delivery. Effective MTEFs discipline decision-making and enforcement in support of all three of these objectives. MTEFs are usually a whole of government framework for supporting a strategic and policy based approach to budget preparation. An MTEF is an integral part of the annual budget cycle and typically consists of:

- i. a top-down resource envelope consistent with macroeconomic stability and broad policy priorities
- ii. a bottom-up estimate of the current and medium term cost of existing national programmes and activities; and
- iii. an iterative process of decision-making, using rolling baselines (Figure 1) that reconciles these costs and new policy ideas with available resources.

Figure 1: Rolling baselines and the MTEF



² The term MTEF is used throughout this Guidance Note as shorthand for a range of medium term approaches to budgeting.

Central to the MTEF concept is the acknowledgement that the budget preparation phase is (and should be) fundamentally **political**, because it is about making real policy choices based on societal preferences and linking them to practical plans and resources (Box 1). To make real policy choices the political process must be supported by certain **technical** elements, that include:

- a medium term fiscal framework setting out the aggregates;
- estimates of the future costs of existing policy, and
- sector strategies setting out sector and sub-sector priorities for future spending.

Not all of these technical elements are going to be in place at the start of an MTEF process, but making progress towards them is a critical part of early MTEF development.

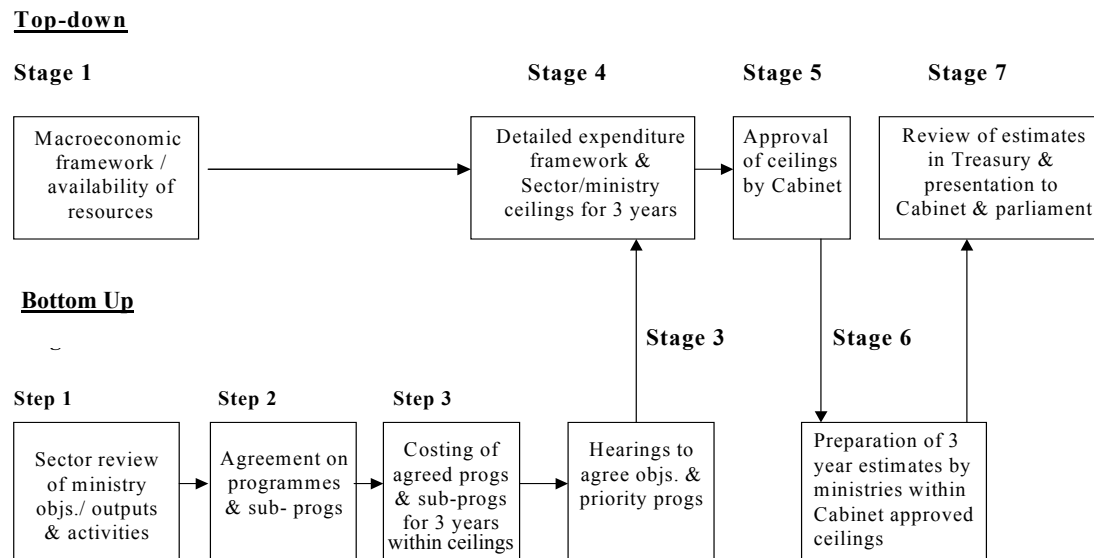
Box 1: Budgeting and Political Realities

The MTEF concept is underpinned by certain values, such as the values of *fiscal discipline* and *improving budgetary outcomes*. It is acknowledged that politicians rarely discipline themselves and are often driven by concerns, including re-election, that are not necessarily in line with better budgetary outcomes. It is quite possible that the rational, rule-based approach of the MTEF is quite antithetical to the way in which politics operates in a country; and without political backing, technocratic efforts to construct an MTEF can be left high and dry.

But there are also many instances where it is evident to the political elite, as well as to key technocrats, that if they want to deliver effectively on their 'political choices' and build the confidence of their citizens, they need a better budget process to do it. Viewed from this angle, the MTEF (and budget process more generally) becomes not merely a technical instrument for consolidating and optimising the use of resources but a potentially crucial instrument for building and reinforcing political legitimacy and hence domestic accountability.

While there is a particular logic to an MTEF process (Figure 2), it should not be treated as a blueprint nor as an end in itself. Implementing a medium term perspective is one part of a wider reform agenda for improving public sector resource management, service delivery and final outcomes. That the process of designing and implementing an MTEF can, in certain cases, also be a driver of wider reforms (as well as a driver of better budgetary outcomes) is an added reason to pursue it.

Figure 2: Possible stages of a medium term approach to budgeting



4. Good Practices in Implementing Medium Term Approaches

I. Getting Started

❖ Budget basics

- Budget basics – such as improved macroeconomic and fiscal management capacities and budget preparation procedures - help in moving budget systems towards a medium term perspective as well as increasing the pace of implementation.
 - The case studies suggest that above all else a commitment to fiscal discipline is crucial for a successful shift towards an MTEF (South Africa, Uganda, Albania, Tanzania).
 - Timely and accurate financial information, such as information on budget outturns on a regular basis, is also critical.

❖ But don't wait

- The absence of most of the budget basics does not necessarily prevent moving to a medium term perspective, however. Country experience shows that making the shift to a medium term perspective early on can provide a crucial incentive to build up the basics; although leaving it too long can also be problematic.
 - In Tanzania, the introduction of a medium term perspective resulted in greater attention to the integrated financial management system (IFMIS) and improvements in budget planning.

- In Tanzania, Uganda and South Africa, MTEF introduction increased internal demands for greater budget comprehensiveness.
- Uganda, with its ordered approach to sequencing (from fiscal discipline to resource allocation to resource use) left addressing a number of budget basics until late in the implementation process. Evidence suggests that earlier attention, especially to performance monitoring, would have been appropriate

❖ **Keep it simple**

- If the existing budget process is weak then it is important ensure that the initial MTEF design is kept simple.
- The main focus early on should be ***changing the processes and rules*** – such as the processes surrounding budget drafting and negotiation - rather than focusing on producing highly detailed budget estimates and costings.
 - In South Africa a simplified approach was initially taken to the preparation of budget estimates
 - Burdening the process early on with detailed estimates or costing information can be counterproductive, as witnessed in Ghana and Burkina Faso
- Where the initial conditions are weak it is still better to start out with an ***MTEF as a whole of government commitment rather than as a pilot in one or two sectors.***
 - Piloting can lead to an imbalance between sectors in terms of progress with public expenditure management reforms and in expectations about future resource availability, as recently shown in Benin.
 - The need to move quickly to an aggregate resource constraint and a set of overall budget priorities does not preclude developing a more medium term focus to linking priorities and resources at sector level (as in Cameroon) or to linking resources to performance indicators (as in some sector strategies linked to a PRSP as in Uganda). In the event that some piloting is absolutely necessary (for capacity or other reasons) then it is critical that the medium term fiscal framework – setting out the aggregate resource envelope - covers the whole of government.

❖ **Involve the political level early**

- Engaging the political level at key decision points in the budget cycle - Ministers/Cabinet and later on Parliament – in making strategic choices about where and how resources should be prioritised is an important part of developing an effective MTEF process.
 - Albania, South Africa and Uganda all provide good examples of a process that has moved in this direction. Diagrams showing political engagement in the MTEF process in Albania and Uganda are presented in Annex 1.
- Political engagement not only gives substance to the MTEF process it is also vital for ensuring the credibility of expenditure ceilings. If politicians are unwilling to be constrained either by a hard budget constraint or by agreed priorities then the process can easily be undermined (Box 1).
 - Lack of clear political engagement at the outset of the process in Tanzania, and the heavy ‘bottom-up’ emphasis in Rwanda’s MTEF may

be reasons why there it has been harder for the Ministry of Finance to maintain a hard budget constraint.

- Political engagement early on does not mean that ceilings should be binding at the outset, on the contrary, a central purpose of the budget preparation process is to ensure that resources are going to priorities and reflect what is working and what is not. However there should be two clear phases in the budget process - first deciding and fixing aggregate sector ceilings, and then secondly deciding the allocations to institutions/programmes within sectors and detailed allocations. Once decisions are made at each stage they should be binding.
- This also applies to the **PRSP** also. Getting the PRSP embedded within a political decision making process is highly beneficial, and the mutual effects on the budget process can be significant.
 - In Albania, the close involvement of the Prime Minister in both the PRSP and MTEF meant that each built on the other, reinforcing the credibility of both and ultimately the annual budget.
 - In Uganda, political backing from the President and an empowered Ministry of Finance have been critical in taking both the MTEF and the national Poverty Eradication Action Plan forward.

❖ **Fiscal stability, honesty and realism in projecting the aggregates**

- Establishing fiscal stability improves funding predictability, and enhances the credibility of the ceilings and hence decisions made during the MTEF and budget process. Early attention to fiscal stability is therefore crucial to the implementation of an MTEF; this is the case even if the initial focus is in developing a medium term perspective at sector level.
 - Experience from OECD and developing countries suggests that achieving this is as much to do with honesty and realism in setting the aggregate resource constraint as anything else (Box 2).
- The negative effects of unrealistic aggregate estimates - such as over-optimistic GDP growth, revenue and the size of the resource envelope – include funding unpredictability and (usually) critical shortfalls in actual expenditure. This can be very demoralising for the MTEF process.
 - In Burkina Faso revenue overestimations are a persistent problem. Recently this has been compounded by exaggerated growth estimates in the country's PRSP. The country study notes that “there is a political incentive to overestimate revenue and the size of envelopes for line ministries. It seems as if the MoF does not wish to face line ministries with realistic revenue figures.”
- Lack of realism in the aggregate estimates in developing countries is also a function of the volatility of aid flows. In fact, in many countries it is the unpredictability of donor funding that is the major problem.
- A critical response tried by a few countries is to adopt a more conservative approach to estimating economic growth, revenue and the resource envelope.
 - In Uganda, the government adopts more conservative forecasts than the IMF for the **purposes of its budget making**. While the growth assumptions are not changed a more conservative forecast is employed

allowing government to pursue short term fiscal stability and greater predictability at the same time.

- Countries are also adopting more conservative approaches to estimating external financing. Again in Uganda, where donors have tended to overestimate the level of disbursements, especially for budget support, forecasts for the 2002/3 budget were adjusted down by 10% from the figures derived from the donors.

Box 2: Key lessons from the OECD

Experience of implementing medium term approaches to budgeting in OECD countries has thrown up a number of important lessons, including:

- The potentially damaging effects of over-optimistic assumptions about future economic growth. OECD experiences point to the importance of conservative estimates for economic growth, revenue and the resource envelope.
- A tendency for line agencies to view the out-year estimates as entitlements. A crucial lesson here is to be clear about the status of out-year estimates and their binding nature (subject only to future policy change).
- Bottom-up budgeting does not fit well with a medium term approach. OECD countries have gradually moved to a more top-down approach to budget formulation, while agencies continue to prepare estimates within this framework 'bottom-up'.
- Political engagement is key with individual ministers engaging in decisions about allocating the top-down ceiling for their expenditure area, and much greater discipline in the parliamentary approval process.

II. Issues Requiring Early Attention

❖ Getting the institutional arrangements right

- Separate budget and planning agencies can undermine the comprehensive approach to budget making. Things are a lot easier when there is a single budget agency (within Finance) which is also reflected at line ministry level.
 - Even when Finance and Planning Ministries are subsumed, it is often the case that separate budgeting and policy/planning units persist at line ministry level. Quickly moving to integration of policy/planning and budgeting functions at sector level is a crucial basis for sound sector expenditure frameworks.
- Linkages to the national PRSP are also aided by ensuring that the PRSP process is coordinated by the same budget agency.
 - In Ghana, the fact that initially the PRSP were headed by the relatively weak planning agency helped to weaken the strategic focus of the MTEF and also the integration of the PRSP and MTEF.
 - In Albania, although separate planning and finance offices exist, the Prime Minister chaired the steering committees for both the MTEF and PRSP and responsibility for overseeing PRSP implementation now resides within the budget department of the Ministry of Finance.
- Where there is no immediate prospect of creating a single budget agency clear institutional arrangements are necessary for ensuring a 'joined-up' planning and budgeting process.

- Benin has made the Development Ministry responsible for the PRSP and MTEF while Albania has a cross-government working group that includes Deputy Ministers from 10 ministries and sector technical working groups in the same 10 ministries responsible for elaborating sector issues as they relate to both poverty reduction and budget strategy.

❖ **Getting the Process Right**

- Country experience confirms the importance of creating space at the outset of budget preparation to focus on the medium term strategy, while ensuring tight links between this phase and the preparation detailed estimates. Preparation of detailed estimates too soon can distract from this more strategic focus and render the MTEF virtually useless.
 - In Uganda, Albania and.. there are two distinct phases to the budget process – the first focuses on strategy and culminates in the decisions on inter-sector budget ceilings, and the second involves the preparation of detailed estimates within the agreed ceilings, and culminates in the reading of the budget.

❖ **Putting policy objectives and performance information in the budget debate**

- In the political and technical debates surrounding the MTEF process it is important that policy objectives and past performance are discussed and presented alongside proposed resource allocations.
 - This relates both to aggregate fiscal, and sector/ministry spending objectives and performance
 - At the outset this need not require comprehensive performance information, but the intention should be that allocation decisions are made on the basis of the achievement of policy objectives.

❖ **Devolving budgetary decisions to appropriate levels**

- Budget agencies should be prepared to move away from trying to control the minutiae of allocation decisions, and allow line ministries to make strategic budgetary decisions within their top-down ceilings.
 - Line agencies and managers are better able to make decisions over allocations.
 - Budget agencies should challenge the validity of chosen allocations in light of the policy objectives set out

❖ **Comprehensiveness**

- The comprehensiveness of the budget framework is critical – from including all funding in the budget as a minimum to subjecting all policies and projects to the budget discipline (see below on implementation).

❖ **Linking recurrent and capital expenditures**

- Under dual budgeting systems recurrent budgets are often evolve into entitlements (e.g. salaries), whilst development budgets become increasingly fragmented, made up of multiple inefficient projects. MTEFs provide an opportunity for linking allocation decisions on the recurrent and development budget, and enable both sequencing the implementation of development projects, and ensuring the.

- Initially, presenting recurrent allocations alongside development and increasing the time horizon to the medium term, as in Uganda, this can change the perspective of allocation decisions
- As the strategic part of the budget cycle evolves, so can the decision making over allocating resources to recurrent and development activities be integrated.

III. Moving Ahead with Implementation

❖ Sequencing

- Making the transition from the annual budget to an MTEF based process involves a sequence of stages from macro to resource allocation and to resource use (and performance monitoring). The process should of implementation should be mapped out
 - Uganda started in the early 1990's with delivering fiscal predictability through a three-year macroeconomic framework, before introducing strategic approaches to resource allocation to spending ministries, and then a results orientation.
 - The South African and Ugandan cases also highlight the importance of the centre (MoF) delivering predictability of policy and funding if it is going to demand improvements in performance from sector and local government ministries and departments.

❖ Integration

- Key characteristics of a maturing MTEF are:
 - the integration of the MTEF into the budget cycle;
 - the integration of the various phases of the budget cycle; and
 - the integration of this cycle with other systems and processes of government, such as the national PRSP and planning systems.
- From a practical point of view, what is required is identifiable links from one phase of the budget process to the next, and within each phase. For example:
 - Clear links from the forward estimates of the cost of existing policy for the first year beyond the budget to the starting point for the next MTEF and annual budget round.
 - Initial ceilings that reflect *reality* i.e. the current macroeconomic outlook; the cost of existing policy; any large policy priority shifts reflecting, for example, PRSP consultations; obvious expenditure pressures and cross-cutting issues.

❖ Reinforcing the strategic phase to budgeting

- The effectiveness the strategic phase is greatly aided by the preparation of some form of **strategic document** to help focus the discussion, and justifying allocations in terms of policy objectives (both fiscal and service). The value lies in creating a common framework for stakeholders to present cases and engage in debates about priorities, options and choices.
 - In South Africa, such a document is called the Budget Policy document; in Uganda the Budget Framework Paper. In Burkina Faso, the Circulaire

Budgetaire seems to serve a similar function. As already mentioned, such documents have the potential to become a key mechanism for integrating the MTEF and PRSP.

- Lengthening the budget formulation phase to include this strategic discussion highlights the importance of incorporating updated macro-estimates into the budget timetable and reflecting these in allocations.
 - The *strategic document* often sets out the justification for any proposed alterations from previous MTEFs in aggregates, to sector budget ceilings, and or strategy objectives.

Box 2: Top-down budgeting – what it does and what it doesn't mean

A top down approach to budgeting is a characteristic of most mature budgeting systems in both the OECD and the developing world. Central is the notion that policy and planning are more likely to be implementable and sustainable where they are informed and disciplined from the outset by the likely available resources. A top-down approach is not about cutting the budget off from information that demands a reallocation of resources or additional funding. It does not preclude participation in the budget process. Rather it is a way of gathering all the information that already exists about the aggregate resource constraint and existing policies, and provides a sequenced framework to the process of debating and making decisions on the appropriateness of existing and future allocations, on the basis of new information of what works and what doesn't, and changing priorities.

❖ **Adopting a strategic approach at sector level**

- Strengthening strategic management capacity at the sector level is crucial to overall budget credibility and improved budget execution. Doing so helps to identify exactly what decisions should be being made where (between the centre and individual ministries for example) and translate priorities into realistic sector expenditure frameworks.
 - This is being done in some countries through annual PER processes (Tanzania, South Africa, Rwanda). Elsewhere it is happening through sector working groups (SWGs) (Albania and Uganda).
 - In Albania, SWGs include representatives of other ministries and agencies involved in the sector; in Uganda they include representatives of all stakeholders including civil society and donors.
- SWGs are making real progress in a number of countries, but close attention also needs to be given to ensuring the SWGs do not replace but rather complement, support and feed into strategic management at ministry and agency level.
 - In Uganda, it has been mentioned that SWGs have become very powerful in certain sectors, becoming the 'effective opposition' on some issues of strategy and priority.
- Formal sector strategic planning, often under SWAP type arrangements, provide an important basis for strategic budget proposals in the MTEF. Also sector review process under SWAPs can be used as entry points for discussing sector budget strategies.
 - In Uganda there is a strong link between Sector Strategic plans, and MTEF allocations. However sector strategies are often unaffordable, and strategic planning processes can lead to unrealistic expectations. The MTEF can be used as a basis for increased realism in strategic planning.

❖ MTEF-PRSP Linkages

- An MTEF has the potential to provide a bridge between the PRSP and the Budget: principally as a tool for allocating budget resources more strategically towards PRSP implementation.
 - To make this happen it is vital that the PRSP and MTEF are confronting the same macro framework and preferably the same medium term fiscal targets
 - Relevant PRSP issues need to be incorporated at the starting point for MTEF/Budget preparation
 - Using the Budget Framework Paper or Budget Guidelines (Uganda, Tanzania) to report to Parliament on how PRSP priorities are to be incorporated into the next budget, and synchronising the Annual Progress Report³ to fit with this budget cycle, is another key way to build better MTEF-PRSP links.
 - The systems for monitoring and reporting of outputs and outcomes should be developed in such a way that they cover the needs with respect to tracking both Budget and PRSP performance.

❖ Using results in the Budget process

- Both the MTEF and strategic sector processes can provide platforms for the introduction and use of performance measures to justify expenditure allocations.⁴
 - Tanzania and Uganda require sectors, as part of the budget process, to describe past performance and (re)state on a rolling basis the strategies, objectives and targets they intend achieve.
 - In Cameroon, where there is no over-arching MTEF, performance information is being used in the development of medium term sector strategies in education and health.
- Performance information is, nevertheless, only valuable when used to inform the political decision-making and accountability process.
 - In Ghana the 1997 MTEF used performance information, however the MTEF bore little relation to the budget because it was not used to inform political decisions.
- Countries tend to be better at setting performance targets in their budget strategies than establishing systems for monitoring and measuring performance, which in turn undermines the accountability for results and the drive to improve performance.

³ The Annual PRSP Progress Report is currently produced by PRSP-adopting governments and submitted to the IFI Boards for 'approval'. Donors are being encouraged to base their own performance assessments of PRSP implementation on the APR in order to reduce the potential number of reporting and monitoring systems around the PRSP. Overtime it is envisaged that the APR will become a more significant tool for internal accountability relating to the achievement of PRSP outcomes, but for it to do so, it must be synchronised with the national budget cycle

⁴ See recent ODI/CAPE Research on Results Oriented Public Expenditure Management 2002 www.odi.org.uk/

- The introduction of performance indicators into the allocation system should be accompanied by the establishment of systems for measuring, monitoring and evaluating performance.
- In Uganda monitoring and evaluation has remained weak and fragmented which undermines the legitimacy of performance reviews in the **Budget Strategy** documentation, and therefore the legitimacy of decisions made to improve future budget allocations.

5. The Government Perspective

Initiating, and sustaining an MTEF process and increasing its effectiveness over time requires not only a series of political and technical decisions but **also needs changes in behaviour** in both the budget agency and line agencies, and between different levels of government. Behavioural change is best driven from within government, and it requires strong leadership and commitment from the budget agency and the Minister of Finance to push through the changes and ensure a credible MTEF process. Change also requires patience, as it takes years to build a successful MTEF process, and for institutions to change their behaviour to fit the new incentives of an MTEF.

❖ Getting behavioural change (Table 1)

- Budget agency behaviour – minister of finance ‘protecting’ technical staff, especially the budget director from political interference
- Cabinet – ensuring the rules of the game are clearly specified, and that Cabinet are aware of those rules.
- Line Ministries – linking their planning and budgeting processes, making the same officers responsible for both.
- Parliament and citizens – regular reporting and access to information. Involving parliament in the approval of MT ceilings before the budget is read.

Table 1: Changing Roles of Line and Budget Agencies

Cabinet	Budget Agency	Line Agency
<ul style="list-style-type: none"> - Prepared to use the budget to discipline policy decisions - Discusses budgetary decisions in the context of policy objectives - Able to stick to decisions on budget ceilings - Hold ministers to account for performance 	<ul style="list-style-type: none"> - Predictable budget policy and process - Deliver realistic, conservative fiscal projections - Deliver predictable ceilings and funding - Transparent process for reallocating funds between sectors - Be prepared to leave budget decisions to line agencies 	<ul style="list-style-type: none"> - Be prepared to set out clearly policy objectives in the budget process - develop sector strategies and plans - Must be prepared to live within budget ceilings one approved - Examine ways to improve efficiency and effectiveness of spending - Report on resource use and performance

❖ Managing aid flows and the hard budget constraint

- MTEFs are essentially about consolidating and using existing resources better. However the context for MTEF implementation is invariably one in which additional resources are on offer (and sometimes conditional on an MTEF), primarily from donor agencies. Given the volatility of most aid flows, this presents a challenge for governments planning on or implementing an MTEF.
 - Tanzania bringing off-budget resources on budget
 - Scenarios (check David Bevan's work)
- A strategic focus in budgeting assists in the rationalising projects, and alongside sector strategic plans, can be an entry point for harmonising donor support.

❖ **Citizen participation in government decision making**

- Bottom-up budgeting is not compatible with an MTEF approach, unless budgeting ceilings are cascaded down to the levels at which participation takes place. In seeking increased citizen participation, particularly in strategic planning processes, it is important to watch for any possible inflation of expectations about the size of the resource envelope. Citizen participation in government decision-making is usually most effective where there is a strong central process for identifying national priorities and ensuring fiscal stability, essentially a strong Ministry of Finance – this is the same for the MTEF.
- Nevertheless, participation in the budget process is a potentially important anchor for institutionalising participation in both PRSP and MTEF processes.
 - In Uganda, civil society provides a strong and direct input into the PEAP (PRSP). The PEAP and planning process are closely integrated and provide the overall framework within which policies are developed. The MTEF and the Budget process provide medium-term macro-fiscal framework and resource constraints for the PEAP. Resource allocations under MTEF/Budget strongly influenced PEAP.
 - In Tanzania the Public Expenditure Review process is a broad-based stakeholder process linked to the preparation of the Budget Guidelines and assessments of the effectiveness of public spending. Assessments of progress towards PRSP targets and goals, particularly as they affect expenditure allocations in priority sectors, are increasingly integrated into the PER process.

❖ **Decentralisation**

- Many countries are pursuing decentralisation at the same time as they are implementing MTEFs and PRSPs. The country cases highlight the challenges decentralisation pose for countries, including managing some complex power shifts.
- The principles and benefits of MTEF implementation are equally relevant for local government, and in the context of service delivery. However the benefits of moving towards and MTEF need to be examined in the context of the capacity of local governments and the way they are financed.
 - In Uganda the national MTEF process has been reproduced in Local Governments, and local governments produce strategy documents called "Local Government Budget Framework Papers".

- There are different ways in which local government budgets can be presented in the national MTEF and this largely depends on the budget classification system, and the way local governments are funded.
 - Again in Uganda local government service delivery is funded by earmarked conditional grants, and these appear in the national MTEF as aggregated national totals.
 - South Africa is unique in that its MTEF encompasses both national and provincial government and involves a set of interlocking institutional arrangements to support decision-making across the two levels of government. The South African approach needs to be understood in its specific institutional and political context.
- Countries undertaking decentralisation need to pay close attention to how an MTEF and PRSP can support decentralisation while also delivering improved fiscal outcomes, a more strategically based resource allocation (particularly to poverty reducing ends) and better results on the ground. Country experience shows that the interaction between these processes needs to be explicitly managed.

6. Donor Support to MTEF Implementation

Donors are often be keen to support the implementation of MTEFs in low-income countries, however it is important for donors to acknowledge that a successful MTEF is a political tool just as much as a technical tool, and without political support to the process ex-ante, an MTEF is unlikely to be successful. Experience shows that successful MTEFs are driven by budget agencies, and Ministers of Finance and not by donors. There are two ways donors can support MTEF implementation – by directly providing technical support to a Government which wants to implement an MTEF, and by aligning donor behaviour towards government MTEF, PRSP and sector processes.

❖ Donor support for MTEF implementation

- Before any donor considers supporting an MTEF process long term, the core technical and political leaders in Budget agencies must be convinced of the merits of the MTEF approach. All too often donors either present MTEFs as a technical tool to governments, which is implementable as a project, with clearly defined outputs and practices.
 - In Ghana, despite the many commendable aspects of MTEF implementation, the **projectisation** of the process has created major problems for integration: whether of the MTEF/budget and policy/planning; of politicians and resource allocation decisions; or of the MTEF and the day to day work of Finance and Planning officials.
 - Evidence from some countries suggests that implementing MTEFs as a result of donor conditionality leads to less than optimal processes.
- Leaders in the finance ministries need to be convinced of the benefits of an MTEF, but also what an MTEF involves in terms of behavioural change, before any offer of long term technical support can be made credible.

- Technical assistance is likely to be required, however this should be at the request of the Budget Agency first and foremost.
 - When the MTEF concept is being introduced to line agencies, it should be done by the Budget agency, rather than by donor-funded consultants.
 - Once a budget wide MTEF process is underway, donors can offer to provide technical assistance to line agencies, to assist them develop strategic perspectives within the new Budget agency perspective.

❖ **Aligning Donor Aid modalities and behaviour towards the MTEF**

- Donors need to be aware of the incentive (and disincentive) effects created by donor financing and improve the predictability of resource flows
 - Providing indications of funding over the medium term
 - Rules for disbursement/harmonisation
- Often donor behaviour undermines the credibility of the budget processes. Extra-budgetary projects break down the discipline of top down-budget ceilings, and the incentives for strategic thinking within sectors. Donors need to reinforce rather than undermine the credibility of top down ceilings by aligning themselves towards sector, budgetary and PRSP processes.
 - Demands for additionality of donor support should be substituted for demands to be involved in the debate on the allocation of resources between sectors in the MTEF. As greater budget predictability is realised, donors could move towards direct budgetary support.
 - In Uganda and Tanzania donors are involved in sector working groups and review processes. The national PER process is the entry point for discussions between government and donors on overall MTEF allocations.

Box 4: Predictability and Aid Modalities

Donors are increasingly concerned with the effectiveness of aid and are looking to new aid modalities to deliver assistance in ways that reduces such costs and enhances predictability. Programme support, increasingly in the form of direct budget support, is one such modality. In many ways, programme support appears more compatible with the philosophy behind medium term budgeting, not least because it is transparently on-budget with a more predictable disbursement schedule. However, there is recent evidence to suggest that in fact the volatility and predictability of programme aid is higher than that of project aid. A recent IMF working paper finds the following:

- Aid is more volatile than domestic revenues and tends to be pro-cyclical
- Fiscal planners at country level are highly uncertain of aid receipts and the information content of commitments made by donors is either very small or statistically insignificant
- There are much larger prediction errors in programme aid than with project assistance and a stronger tendency to over-estimation.

Addressing the unpredictability of aid flows is vital to improving the chances of an effective domestically owned MTEF/budget process.

Source: IMF Working Paper WP/01/167