



National Audit Office

DEPARTMENT FOR INTERNATIONAL DEVELOPMENT

Providing budget support to developing countries



SUMMARY

1 Budget support is the Department for International Development's (DFID's) preferred method of delivering financial aid where country circumstances are suitable. It is aid provided directly to a partner government's central exchequer in support of that government's programmes. It is accompanied by other inputs, in particular support to strengthen government systems and discussion over policies. Budget support is spent using the partner government's financial management systems. It aims to reduce poverty through helping to fund the poverty reduction strategy of the beneficiary country. DFID and many other donors and aid experts consider that budget support can help to strengthen developing country government capacity, increase donor harmonisation, expand service delivery and ultimately

assist in poverty reduction. DFID's use of budget support has increased from £268 million to £461 million over the past five years. It now represents nearly twenty per cent of DFID's bilateral expenditure and is likely to increase further in future years provided circumstances in the recipient countries permit.

2 This study examines the aims of budget support, what it is achieving, how DFID manages the risks of using it and how DFID takes individual funding decisions. Our methods included four country case studies and a detailed documentation review for ten countries where DFID provides budget support, as well as literature review, data analysis and surveys. Our methods are at Appendix 1.

Our findings:

On results of budget support (Parts 2 and 3)

3 Budget support has:

- often enabled partner governments to increase expenditure on priority areas;
- resulted in partner governments providing more services, particularly in health and education;
- helped increase the capacity of partner governments to plan and deliver services effectively and to develop better poverty-focused policies;
- helped partner governments to strengthen their financial management systems and encouraged other donors to support such reforms;
- facilitated donor alignment to, and support for, the developing nation's own strategies; and
- reinforced existing economic stability and good economic management.

Developing country officials we spoke to during our country visits expressed a preference for budget support over other forms of aid. They also welcomed DFID's efforts to promote its use with other donors and to support technical and sector working groups.

4 But challenges remain:

- service expansion has often been at the expense of service quality;
- progress in strengthening financial management systems has been slower than expected; and
- DFID and other donors expect budget support to reduce the transaction costs of administering aid, but have found it difficult to quantify these costs.

5 Budget support can also improve domestic accountability by increasing the proportion of development expenditure reflected in government accounts and therefore increasing the potential for scrutiny by domestic stakeholders. In complementary projects to budget support, DFID also assists parliaments, civil society organisations and State Audit Institutions to improve domestic accountability. In many countries, however, these institutions are not yet fully effective.

On monitoring and evaluating budget support (Part 4)

6 Monitoring the impact of aid, and particularly budget support, is challenging given the weaknesses in developing country data and difficulties in attributing changes to a particular type of aid such as budget support. DFID has encouraged joint arrangements between donors to reduce monitoring burdens. But there is still scope to tighten DFID's specification of poverty reduction objectives in some budget support programmes and to improve performance assessment frameworks further. DFID and other donors use data generated by partner government systems to monitor progress. But some gaps in baselines and weaknesses in partner government statistical systems sometimes constrain effective monitoring. DFID provides more support to statistics than other bilateral donors but overall donors have not always done enough to help partner governments strengthen these systems.

On assessing the risks of budget support (Part 5)

7 DFID has done a good job of moving public financial management up the development agenda. It has taken a lead role in developing and using tools to assess the quality of developing country systems and to assess the level of fiduciary risk. But there is scope for DFID to sharpen its estimates of the significance of weaknesses for potential inefficiencies or leakage, and to set out more clearly the extent to which UK and other funds are at risk.

8 DFID requires a shared commitment to three objectives as a basis for providing aid through developing country governments: reducing poverty and achieving the Millennium Development Goals; strengthening financial management and accountability; and respecting human rights and other international obligations. DFID's monitoring of the first two commitments is well established but monitoring of commitment to human rights has been less systematic.

On taking funding decisions (Part 6)

9 DFID analyses country circumstances and systems well when framing its assistance programmes and considers the prospects for budget support widely both internally and with its partners. But it is weaker at documenting evidence of its overall assessment of the risks of budget support against the benefits or comparing the costs and benefits of budget support with other types of aid. DFID's country teams expect to increase budget support in the future and to use it in more countries if circumstances permit. To manage this projected expansion well it will need to link more clearly its assessment of risks and benefits to the design of budget support programmes and the amount committed.

Our conclusions and recommendations

10 As part of a broader move by donors away from traditional project-based aid, DFID has increased its use of general support for the budgets of beneficiary countries, which are then responsible for managing these funds. DFID has been one of the leading bodies promoting budget support and improving best practice in its management. Budget support has allowed developing country governments to increase expenditure in priority sectors, and helped to expand access to essential public services and improve public financial management in partner countries. Evidence on the extent to which budget support has yielded better value for money than other ways of delivering aid, or has had an impact on income poverty, is not conclusive. Nevertheless the evidence to date supports the argument that budget support has some comparative advantages in helping to build capacity in government systems while supporting increased service delivery, and can be an effective component of many assistance programmes. Budget support also carries significant risks that the national administration may not be capable of using the funds efficiently and effectively or funds may be misapplied for political reasons or through corruption – and that aid will consequently not contribute fully to reducing poverty. We set out below recommendations to help DFID improve its appraisal and management of budget support, and to judge better the value for money provided. More detailed recommendations are at Appendix 2.

- a** **DFID should always set out clearly its precise objectives for budget support programmes, specifying exactly what it expects to achieve and by when.**
- b** **DFID should build on its current monitoring arrangements to make sure that for each budget support programme it can systematically assess progress against its objectives.** Such monitoring should reflect a balance of process, output and outcome indicators and be coordinated with development partners.

- c** DFID has done more than most donors to strengthen statistical systems for monitoring progress. But the available information is often still not sufficient for donors to monitor all key aspects of poverty reduction on a timely basis. In countries where it uses budget support, **DFID should identify any key weaknesses in the national monitoring systems and give increased priority to mitigating them, seeking support from other donors in doing so.**
- d** **DFID should, together with its partners, further strengthen its risk assessments and analysis of developing country government systems.** Specifically, it should make more explicit its judgement of the significance of system weaknesses for potential inefficiencies or leakage of aid in the recipient country. It should use more quantified estimates of these factors where possible. It should use this information to tailor appropriate safeguards to mitigate risks.
- e** **DFID needs to set up systematic in-country monitoring along the dimensions of human rights in its guidance.** Before using budget support, DFID should establish transparent procedures to respond quickly, firmly and proportionately if concerns arise and make sure contingency plans for other ways of delivering aid cover the most significant risks.
- f** **DFID should improve its analysis of the prospects for using budget support by:**
 - formalising appraisal of options which vary the proportion of budget support in a country programme;
 - formalising appraisal of options for using alternative forms of aid; and
 - bringing together the risks and benefits of each option to facilitate comparison.¹
- g** In support of the above, **DFID needs to rationalise and strengthen the guidance and support available to country teams and keep it up to date.**

¹ Figure 26 sets out key considerations for budget support appraisal.