



Budget support in development cooperation

An effective aid instrument?

The Commission attaches high hopes to budget support as an aid instrument and aims to raise its share in EU development cooperation to 50%. The Commission's Green Paper on budget support to third countries has been put to stakeholders and is currently being debated in the European Parliament.

Project aid can be very effective towards a limited number of beneficiaries, provided that project partners are competent. Budget support, on the other hand, normally targets the whole of society in the partner country by helping to improve national public systems.

Popular recipients of sector budget support are the sectors which contribute to the Millennium Development Goals (MDGs), such as health and education.

Evaluation of budget support is highly complex, as results cannot be easily attributed to inputs. This aid modality has been evaluated against achievement of the MDGs and its general effectiveness. The role of national control mechanisms, including parliaments, audit institutions, and civil society, is of primary importance to ensure democratic oversight and accountability.

In this briefing:

- Green Paper on budget support
- Budget support or project approach?
- Sector budget support
- Evaluation, conditionality, and policy dialogue
- Parliamentary activities
- Main references

Glossary

Budget support: Funds that a donor (normally a national government, the EU or an international organisation) channels directly into the treasury of the recipient country, in order to achieve mutually agreed goals. It is usually conditional on the inclusion of capacity-building measures, dialogue with the partner country and the establishment of conditions for disbursement.

General budget support (GBS): Supporting a country's national development strategy

Sector budget support (SBS): Funds used to support a particular sectoral strategy

Green Paper on budget support

State of play

Currently, budget support accounts for about 25% of all EU aid (see figure 1). The Commission aims to raise this figure to 50%.¹ In October 2010, the Commission published its Green Paper ([COM\(2010\) 568](#)), setting out its approach towards the future of budget support to third countries. Besides the main recipients, developing countries, this also concerns accession and neighbouring countries. The Green Paper initiated a public consultation, which the Commission intends to use for input into a White Paper. The Parliament is in the process of commenting on these policy proposals with a [report on Future of EU budget support to developing countries](#)



Image Copyright Joachim Wendler, 2011.
Used under licence from Shutterstock.com

drafted by Charles Goerens (ALDE, LU). The DEVE committee will vote on this on 25 May 2011.

Features of EU budget support

Recipient countries must fulfil the following eligibility criteria:

- a well-defined national (or sectoral in the case of SBS) policy and strategy,
- a stability-oriented macroeconomic framework, and
- a credible and relevant programme to improve public financial management.

The Commission stresses that countries must continue to observe these principles for funds to be disbursed. Funds are used in the public interest, such as for health-care, education, and democratic institutions.

Policy proposals/suggestions

The Commission considers that budget support must be

coordinated among donors² (within and beyond the EU) and with other instruments, such as policy dialogue, performance assessment and capacity-building (for example, technical assistance for core government services).

It takes up some of the principles enshrined in the [Paris Declaration on Aid Effectiveness](#), 2005 and the [Accra Agenda for Action](#), 2008, and applies them to EU aid:

Ownership calls for donor countries to respect partner country leadership in achieving their own development strategies. Partner (recipient) countries are asked to involve civil society and the private sector in the coordination of aid.

Managing for **Results**: budget support should focus on outcomes that can be measured quantitatively and qualitatively. The Accra Agenda stresses **parliamentary oversight** to monitor results, and transparency in the use of funds, both on behalf of donor as well as partner countries.

This goes hand in hand with the Commission's proposal to strive for **public support** from stakeholders within the EU and citizens in partner countries.

Similarly, budget support should be used in a way that improves **accountability** of governments to their citizens, parliaments and supreme audit institutions (domestic accountability) as to the use of funds, and donor and partner countries to each other

(mutual accountability).

Finally, budget support should be **predictable**. The Accra Agenda commits partner countries to strengthening budget planning processes and to linking expenditure to results over the medium term.

Donors should inform partner countries regularly what funds they should expect each year and in a three-to-five-year horizon.

The Commission consulted stakeholders on their opinions on the following **open issues**:

- Political governance and the role of political dialogue;
- Role of **policy dialogue**, role of conditionality, links to performance and results;
- Domestic and mutual accountability;
- Programming of budget support and its coherence with other instruments;

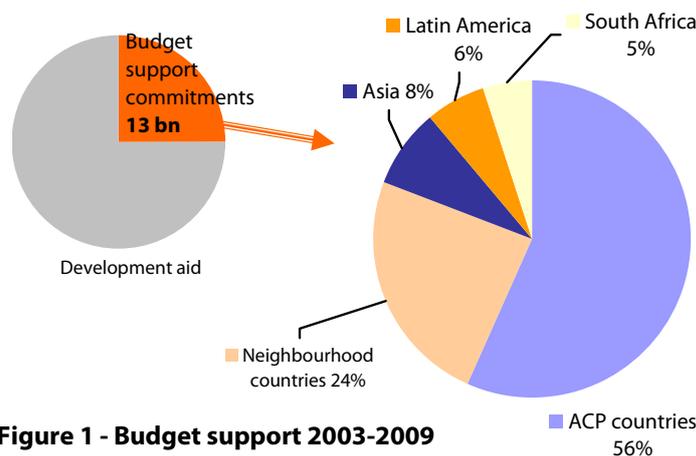


Figure 1 - Budget support 2003-2009
Data source: Commission Green Paper, 2010.

- Strengthening risk assessment and dealing with fraud and corruption;
- Budget support in situations of fragility; and
- Growth, fiscal policy and mobilisation of domestic revenues.

Budget support or project approach?

Project approach

Project support bypasses national systems and is thus more direct. This can mean less danger of losing funds to corruption, and it means a certain independence from governments. But it also means that project donors miss an opportunity to help improve a country's systems. Project donors can work directly with the people, and thus, projects can also fulfil certain principles in aid effectiveness agreements, such as **ownership**:

A successful example is an EU-funded [project](#) in one of the largest slums in Nairobi, Kenya. The local water company provided access to clean water and sewers and built small, robust toilet blocks. Ownership of the project was encouraged by involving slum dwellers in the sale of water and management of the sanitary installations. The EU funded 75% of the €740 000 used, and project officers in the [EU Delegation to Kenya](#) stated that it works very well because the project partner is competent.

Advantages of budget support

The most often quoted advantage of budget support is that, instead of only project beneficiaries, it addresses the **whole society** of a country, by helping to improve systems, including cross-cutting issues. Budget support is also more predictable and sustainable than project funding, if a sound institutional and policy framework is in place.

The most recent extensive study, by the International Development Department (IDD) at Birmingham University, for the OECD, concludes that budget support has had many positive effects, including

expanded basic services (especially health and education, but sometimes access for more people meant a reduction in quality per client). The budget process and the transparency of **public finance management** has been strengthened in most countries. The study did not find budget support to be more vulnerable to corruption than other forms of aid. Not least because anti-corruption measures are often included in donors' collaboration with partner countries.

Budget support gives donors better access to **dialogue** with the government. This can be used to argue against other policies (e.g. generalised tax subsidies for fuel) that might offset the savings a country makes by receiving budget support.³

It can also be argued that budget support is a more democratic aid modality than the project approach, as parliaments and audit institutions **scrutinise** the budget and therefore also foreign aid disbursements.⁴ It should therefore, in theory, improve accountability to partner countries' citizens, given that elections are free and governments share their power.

Disadvantages and risks of budget support

The February 2011 [European Court of Auditors report on the Commission's management of GBS](#) considers that the Commission does not tailor its programmes sufficiently to the **specific circumstances** and changing priorities in the partner countries. Objectives and conditions are often too general.

Raquel C. Alvarez, an adviser to the Spanish Prime Minister, argues that many donors employ budget support not for developing countries' benefits but to **increase aid delivery** while cutting administrative costs.

Furthermore, supplying governments with a large part of their budget does not give them incentives to generate their own income, perpetuating **dependence**. This was, however, not confirmed by the IDD

study, which also found no evidence that budget support crowded out private investment.

Mentioned above as an advantage for donors, their influence can also be a threat, keeping partner countries dependent: through **their influence on national budgets**, donors often fail to encourage countries to pursue their own policies. Moreover, **domestic accountability** can be damaged in countries that are heavily dependent on aid: governments are liable to pay more attention to donors than to their own people. This can also encourage corruption.

The academic Nicholas Eubank puts forward the example of **Somaliland**: having seceded from Somalia in 1991, it is not internationally recognised and has received less budget support than other countries. Consequently, its government has had to work hard for the continued support of its people precisely because it could not revert to alternative sources of income.⁵ Although Somaliland's democracy showed some flaws recently, the country works much better than Somalia.⁶ Alvarez concurs that budget support is sometimes (ab)used to make up for tax revenues foregone.

Sector budget support (SBS)

The Commission consulted stakeholders on the best way to blend the two instruments of GBS and SBS. It sees SBS as **less** vulnerable to **political risk**, as it is related to specific sectors, not the overall development agenda of a country. Therefore, it is easier to justify to taxpayers and parliaments at home, even if political difficulties or corruption increase in the partner country.

[ODI, the Overseas Development Institute](#), considers that SBS has improved access to basic public services (such as education and healthcare) as well as the efficiency of public expenditure. It adds that the EU should pay greater attention to service delivery,

concretely improving capacities and systems needed for managing, supporting and supervising frontline service-providers. For this, more sector-specific expertise is needed.⁷

The [German government](#), one of the most critical respondents to the public consultation when it comes to GBS, advocates using SBS more. It considers that this instrument can be applied more safely when a country's governance system is not considered fit for dealing with GBS, because SBS allows the policy dialogue to be targeted better. SBS should then be directed towards sectors that contribute to achieving the **Millennium Development Goals** (MDGs).

Evaluation, conditionality, and policy dialogue

Means of evaluating budget support

The **European Court of Auditors** considers that the Commission needs a more effective evaluation method for budget support, which assesses the actual impact of this aid modality. Currently, it focuses too much on its potential to improve aid delivery.

One way is to measure the impact budget support has on partner countries' **MDG performance**. Commission DG DEV staff analysed the performance of high GBS recipients against four MDGs: enrolment in primary education, gender parity in education, child mortality, and access to water. GBS figures were taken from the [OECD DAC database](#), and [MDG indicators, from the UN](#). The study concluded that high GBS recipients have performed better in these MDGs than countries that received little or no GBS.⁸

IDD evaluated Partnership GBS (meaning GBS which supports the poverty reduction strategies of partner countries) in seven countries, using an "**Enhanced Evaluation Framework**" (EEF) and a "Causality Map".⁹ GBS is difficult to evaluate for the following reasons: **Counterfactuals** (how it would

have been without GBS) exist only hypothetically, as not only the funds have to be taken out of the equation, but also dialogue, agreed strategies, mutual learning, technical assistance, and other accompanying measures. **Causality** is one of the most difficult elements to evaluate, as similar effects could have been achieved independently within the country or through other projects.

The EEF analyses the interdependence of different causal and temporal levels, with each other and with the adjustment of budget support policies.

A [DG EXPO Policy Department study](#) analysed national control mechanisms in Ghana, Burkina Faso and the Dominican Republic. Parliamentary budgetary oversight was found to be weak, although supreme audit institutions have improved, partly due to higher donor attention.

Policy dialogue, political dialogue, and conditionality

The Commission proposes the following distinction: **Political dialogue** should focus on the "underlying principles" that govern EU external action: democracy, the rule of law, human rights, equality and solidarity, respect for the UN charter and international law. It puts the question to stakeholders whether budget support should be suspended if adherence to these principles deteriorates.

Policy dialogue, on the other hand, should continue in almost all circumstances, since it concerns agreed development objectives, particularly public financial management, growth strategy, macroeconomic stability, fiscal policy (taxes and budget), sectoral policies (especially in the social sector), and the fight against corruption. National parliaments, audit institutions, and both private and non-profit sectors should be included in policy dialogue.

The [ACP-EU Joint Parliamentary Assembly](#) supports this distinction, saying that budget support should not be linked to political

conditionality. Political dialogue should be integrated into overall cooperation. A high-level policy dialogue should instead contribute to improving the efficiency of budget support.

The German government, on the other hand, considers this distinction to be too **artificial**. It says that staff in donor and partner countries have to be adequately trained in order to debate progress in both areas, according to quantitative and qualitative criteria agreed beforehand. A more comprehensive dialogue is also supported by IDD, finding that technical solutions need political commitment to be effective and to endure.

The Court of Auditors states that the Commission has to develop a framework for **managing risks**, such as bad financial management and corruption.

The German government considers that **conditionality** has to be **predictable**. Donors should detail their conditions clearly in advance, from a unified stance. Thus, second or third instalments (tranches) can be based on evaluation showing a successful outcome.

A **suspension** of budget support can have harmful effects, such as macroeconomic destabilisation and the interruption of essential services (e.g. health and education).

Parliamentary activities

The [study for DG EXPO](#) recommends that, in general, the EU should pay greater attention to parliaments in development work. The **European Parliament** should use its influence in the ACP-EU Joint Parliamentary Assembly and its [Office for the Promotion of Parliamentary Democracy](#) to strengthen parliaments in their oversight function and to evaluate their success regularly. Civil society organisations (CSOs) can assist with evaluation. The Court of Auditors also stresses this important role of parliaments, CSOs and audit institutions.

The EP insisted in its 2006 [resolution on aid effectiveness and corruption in developing countries](#) on the importance of supporting national parliaments in their role of budget authorities, using dialogue, information-sharing and capacity-building. It added that a proportion of budget aid should be reserved for civil society watchdogs. It called for the earmarking of budget aid to specific sectors.

In its [legislative resolution on a financing instrument for development cooperation](#), of February 2011, the EP calls for the introduction of sector-specific budget support or project aid to alleviate difficulties that small-scale banana farmers will face owing to the planned liberalisation of the banana trade.

Main references

[Evaluation of General Budget Support: Synthesis Report](#) / IDD and Associates, May 2006, commissioned by OECD.

[The future of EU budget support to third countries](#), COM(2010) 568 final, 19.10.2010.

[The Rise of Budget Support in European Development Cooperation: A False Panacea](#) / Raquel C. Alvarez, FRIDE, January 2010.

Disclaimer and Copyright

This briefing is a summary of published information and does not necessarily represent the views of the author or the European Parliament. The document is exclusively addressed to the Members and staff of the European Parliament for their parliamentary work. Links to information sources within this document may be inaccessible from locations outside the European Parliament network. Copyright © European Parliament, 2011. All rights reserved.



<http://www.library.ep.ec>

Endnotes

- ¹ [Report on Budgetary support as a means of delivering Official development assistance \(ODA\) in ACP countries](#) / ACP-EU Joint Parliamentary Assembly, session document, 14.05.2011.
- ² See Library Briefing [Vers la complémentarité des politiques européennes du développement](#) / Marta Latek, 2010.
- ³ [Ghana: Budgethilfe zwischen Dialog und Powerplay](#) / Richard Gerster, 2009.
- ⁴ Commission Green Paper, p. 11.
- ⁵ [Peace-building without external assistance: Lessons from Somaliland](#) / Nicholas Eubank, Center for Global Development, January 2010, 37 p.
- ⁶ [EU Somalia country report](#), May 2011.
- ⁷ [ODI's Response to the EC Green Paper on the Future of EU Budget Support to Third Countries](#), January 2011.
- ⁸ [Budget support and MDG performance](#) / Jonathan Beynon, Andra Dusu, Commission DG DEV, 30.03.2010.
- ⁹ [Evaluation of General Budget Support: Note on Approach and Methods](#) / IDD and Associates, March 2007, see p. 19 for Enhanced Evaluation Framework and p. 22 for Causality Map.