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On the
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**COUNTRY-BASED SCALING UP:
ASSESSMENT OF PROGRESS AND AGENDA FOR ACTION**

Attached for the October 21, 2007, Development Committee Meeting is a background report entitled "Country-Based Scaling Up: Assessment of Progress and Agenda for Action," prepared by the staff of the World Bank.

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September 26, 2007

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ABBREVIATIONS AND ACRONYMS

AAA	Analytical and Advisory Services
AAP	Africa Action Plan
ACP	African, Caribbean, and Pacific countries
AFD	Agence Française de Développement
AIDS	Acquired Immune Deficiency Syndrome
AMC	Advance Market Commitments
APRM	Africa Peer Review Mechanism
BSG	Budget Support Group
CAS	Country Assistance Strategy
CDF	Comprehensive Development Framework
CDMAP	Capacity Development Management Action Plan
CEM	Country Economic Memorandum
CFAA	Country Financial Accountability Assessment
CG	Consultative Group
COMPAS	Common Performance Assessment System
CPAR	Country Procurement Assessment Report
CPI	Consumer Price Index
CPIA	Country Policy and Institutional Assessments
CSLP	Cadre Stratégique de Lutte contre la Pauvreté
DAC	Development Assistance Committee
DEC	Development Economics Vice Presidency
DfID	Department for International Development – U.K.
DRC	Democratic Republic of Congo
DSA	Debt Sustainability Analysis
EC	European Commission
EDPRS	Economic Development and Poverty Reduction Strategy
EFA-FTI	Education for All-Fast Track Initiative
EU	European Union
FDI	Foreign Direct Investment
GAC	Governance and Anti-Corruption
GAVI	Global Alliance for Vaccines and Immunization
GBS	General Budget Support
GDP	Gross Domestic Product
GEF	Global Environmental Facility
GFATM	Global Fund to Fight AIDS, Tuberculosis, and Malaria
GNI	Gross National Income
GPG	Global Public Goods
GPRS	Growth and Poverty Reduction Strategy
GTZ	German Technical Co-operation
HIPC	Heavily Indebted Poor Countries
HIV	Human Immunodeficiency Virus
IBRD	International Bank for Reconstruction and Development
IDA	International Development Association
IEO	Independent Evaluation Office – IMF
IFFm	International Finance Facility for Immunization
IFIs	International Financing Institutions
IMF	International Monetary Fund

IPRS	Interim Poverty Reduction Strategy
JSAN	Joint Staff Advisory Note
LICs	Low-Income Countries
MAMS	Maquette for MDG Simulations
MAP	Madagascar Action Plan
MCA	Millennium Challenge Account
MCC	Millennium Challenge Corporation
MDA	Ministries, Departments and Agencies
MDBs	Multilateral Development Banks
MDG	Millennium Development Goals
MDRI	Multilateral Debt Relief Initiative
MKUKUTA	National Strategy for Growth and Poverty Reduction–Tanzania
MoFEP	Ministry of Finance and Economic Planning
MOPAN	Multilateral Organizations Performance Assessment Network
MTEF	Medium Term Expenditure Framework
NGOs	Non-Governmental Organizations
NPV	Net Present Value
ODA	Official Development Assistance
OECD	Organisation for Economic Co-operation and Development
PARPA	Action Plan for Reducing Absolute Poverty–Mozambique
PASDEP	Plan for Accelerated and Sustained Development to End Poverty
PEFA	Public Expenditure & Financial Accountability
PER	Public Expenditure Review
PFM	Public Financial Management
PIUs	Project Implementation Units
PPP	Purchasing Power Parity
PRGF	Poverty Reduction and Growth Facility
PRS	Poverty Reduction Strategy
PRSC	Poverty Reduction Support Credit
PRSP	Poverty Reduction Strategy Paper
RER	Real Exchange Rate
RMS	Results Measurement System
RPG	Regional Public Good
RRP	Results, Resources, and Partnership
SARS	Severe Acute Respiratory Syndrome
SBAS	Strategic Budget Allocation System
SIDA	Swedish International Development Cooperation Agency
SPA	Strategic Partnership with Africa
SSA	Sub-Saharan Africa
SWAp	Sector-Wide Approaches
UJAS	Uganda Joint Assistance Strategy
UK	United Kingdom
UN	United Nations
UNAIDS	Joint United Nations Programme on HIV/AIDS
UNDESA	UN Department of Economic and Social Affairs
UNDP	United Nations Development Programme
UNICEF	United Nations Children's Fund
USAID	U.S. Agency for International Development
WBG	World Bank Group
WHO	World Health Organization

Executive Summary

1. Five years after Monterrey, and two years after Gleneagles, the international community needs to pick up the pace in delivering on its commitments to scale up assistance to developing countries to support their efforts to accelerate growth and progress toward the Millennium Development goals (MDGs). In the context of an increasingly complex aid architecture—marked by a proliferation of aid channels, fragmentation of aid flows, and increased earmarking of aid—it also needs to renew its commitment to the country-based development model. Centered on country-led development strategies, the country-based model constitutes an essential platform for aligning aid from multiple sources with national priorities and systems.

2. Developing countries' policies and institutional capabilities have improved in recent years, contributing to stronger growth and important gains in reducing poverty. Improved policies and institutions have attracted larger private capital inflows, which have become the dominant source of external financing for the more prosperous developing countries. For most low-income countries, however, official development assistance (ODA) remains the major source. To achieve the MDGs, these countries must build on their recent gains in economic performance. They must accelerate growth and boost investment in MDG-related services. This will require stronger domestic resource mobilization (public and private) and stronger efforts to attract foreign private investment. For many low-income countries, sustained and predictable increases in ODA also will be necessary.

3. **Strengthening the Country-Based Development Model.** Three key dimensions of the country-based model define the strength of a country's strategic and implementation framework for scaling up development results and its effectiveness as a vehicle for alignment and harmonization of partner support: a country-led and results-oriented development strategy that sets out clear priorities and programs; a sound macroeconomic framework; and a capable institutional framework for implementation of the country strategy. There is progress on all of these dimensions in a broad range of low-income countries. Anchored in Poverty Reduction Strategies (PRSs, or equivalent national development strategies), a stronger strategic and implementation framework is emerging at the country level to support scaling up. However, progress varies considerably across countries, with some countries more ready than others to effectively utilize an increase in resources.

4. While specific needs and priorities vary across countries, there are three key areas that require action by countries, and support from their development partners, to further strengthen national strategies and institutions for scaling up development results:

- Sharpening the focus of PRSs on stronger, shared, private sector-led growth with better diagnostics for growth and sector strategies.
- Costing PRSs, strengthening PRS-budget links, and assessing scaling-up scenarios in terms of their implications for macroeconomic and fiscal frameworks.
- Strengthening public sector capacity, especially improving public financial management and accountability and strengthening the results assessment framework, including monitoring, evaluation, and statistical systems.

5. **Scale-Up Opportunities.** The report calls for a differentiated, performance-based approach to scaling up aid, linked to countries' needs *and* readiness to make effective use of increased resources. Thanks to the progress countries are making in strengthening their development strategies and institutional frameworks for implementation, there is a broad range of countries that can productively absorb increased aid, with amounts and modalities tailored to their circumstances. In addition, the growing attention to global and regional public goods creates opportunities for scaled-up support.

- There are several strong performers, typically second-generation PRS countries, where the strengthening of the strategic and institutional framework is sufficiently advanced to merit early delivery on the Gleneagles commitments. Also, a larger proportion of aid can be provided to these countries in the form of budget support. Some examples include Burkina Faso, Ghana, Madagascar, Mozambique, Rwanda, Tanzania, and Vietnam.¹
- There is scope for scaling up of aid in many first-generation PRS countries, starting with moderate increases but building to larger amounts as absorptive capacities expand. In these countries aid programs could comprise a mix of modalities such as budget support, investment projects, including sector-wide approaches, and technical assistance, depending on specific country circumstances. Examples include Armenia, Bangladesh, Honduras, Kyrgyz Republic, and Mali.
- Fragile states, particularly post-conflict and re-engagement countries, also present opportunities for selective, focused, and carefully sequenced increases in aid for projects and programs tailored to their weaker governance contexts. Examples of fragile states presenting opportunities for increased support include Central African Republic, Haiti, and Liberia.
- Investments in global and regional public goods will be an increasingly important vehicle for scaled-up aid to developing countries. Promising areas for scaling up include clean energy, climate adaptation, regional infrastructure initiatives, and aid for trade. Stronger development strategies and implementation frameworks position countries better to integrate these increased investments into national programs.

6. **Improving the Delivery of Aid.** On the supply side of aid, there is progress in raising its quantity and quality, but overall the progress is slow and uneven. Both total aid and aid to Sub-Saharan Africa have risen, but at rates well short of those needed to achieve the Gleneagles commitments. Moreover, the upward trend in ODA stalled in 2006. Much of the recent rise in aid has been for debt relief. Aid for core development programs—program and project aid—has seen relatively little increase. Better performing countries, with demonstrated capacity to make effective use of increased resources, are on average seeing larger increases in aid. This is the case with some strong performers in the PRS-II group, such as Ghana, Madagascar, and Rwanda in Africa and Vietnam in East Asia. However, the increases in aid so far even to such countries that present strong scale-up opportunities are typically far short of what they need and can effectively use. There is some improvement in aid predictability, but the average level of predictability remains low.

¹ Individual countries identified for scaling up of aid in this report are intended as examples rather than an exclusive list, as there are other countries that are also making progress in enhancing their capacities for effective use of increased resources.

7. Overall, there is some encouraging progress in the implementation of the Paris Declaration. However, even as gains are made on the aid alignment and harmonization agenda, the changing aid architecture is posing new challenges for aid effectiveness. Global/vertical funds bring much needed attention and resources to their focus areas, and are increasingly important as sources of funding for GPGs, but their development impact will depend on how effectively they are aligned and integrated with country programs. This is a particularly important issue in health. Similarly, the valuable additional resources provided by the emerging new bilateral donors will be the more effective the more they accord with the alignment and harmonization principles of the Paris Declaration.

8. These trends in the quantity and quality of aid suggest the following priorities for aid delivery going forward:

- Delivering on commitments to increase aid through a stronger donor response to the scale-up opportunities that exist in a number of countries—better performing countries with a sustained record of reform and improving economic performance and some fragile states, in particular post-conflict and re-engagement countries—and for key global and regional public goods.
- Improving aid predictability through mechanisms that lengthen the time horizon of aid commitments and set clear rules for qualification and disbursement: the recent European Commission proposal on MDG Contracts points in the right direction.
- Ensuring coherence in aid delivery in the context of the changing aid architecture, using country PRSs as the core instrument to secure strategic alignment of funding from different sources—including vertical funds, new bilateral donors, and private foundations—with country development priorities and the principles of the Paris Declaration to harmonize aid delivery.

9. **Role of the World Bank.** With its global development mandate, its services spanning financing, knowledge, and coordination, and its close engagement with both aid-recipients and donors, the Bank has a key role in supporting the scaling-up effort, based on a strong country development model. Looking ahead, there are three strategic priorities:

- Strengthening country strategies and systems to help countries absorb and effectively use scaled-up aid flows. Priority areas for action include: strengthening analytic support to PRSs, notably in growth diagnostics, analysis underpinning strategies in key sectors, and assessment of scaling-up scenarios; and stepping up technical and financial assistance to countries for institutional strengthening, especially for public financial management and results assessment.
- Promoting coherence in aid delivery, using the Bank's coordinating and convening role to provide a platform for improved aid alignment and harmonization. Priority areas for action include: forging ahead with the Results, Resources, and Partnership (RRP) process, aimed at strengthening aid coordination through more upstream engagement between countries and donors and a sharper focus on results and mutual accountability; engaging more systematically with vertical funds, new bilateral donors, and private foundations to support the integration of their programs into country strategies and donor coordination mechanisms

as well as ensure that financing from all sources is consistent with the country's debt sustainability (the joint Bank-Fund Debt Sustainability Framework is a key tool for that purpose); and promoting consensus on approaches for tackling global and regional issues and helping countries and donors to integrate agreed actions into national development strategies.

- Reinforcing partnerships for stronger engagement at the country and global levels: with the IMF, on the macroeconomic dimensions of scaling up and in improving collaboration more broadly in the work in low-income countries in follow-up to the Malan Report; with OECD-DAC, EC, and bilateral donors in the implementation of the Paris Declaration and the RRP process; with the regional development banks, especially the AfDB in the implementation of the Africa Action Plan; and with the UN system, especially in engaging with fragile states.

10. The Bank's ability to play its key role in strengthening the country-based development model and providing a platform that promotes aid effectiveness and integration of global and regional development programs depends on a strong IDA. Ensuring that IDA15 replenishment is commensurately strong is therefore a crucial element of the broader effort to scale up development results and supporting resources in low-income countries.

11. **Issues for Discussion.** The following issues are proposed for discussion by the Development Committee:

- What do Ministers consider as the key areas that require action by countries to strengthen country strategies and capacities for scaling up development results?
- Do Ministers agree with the report's assessment that there is a broad range of countries that can productively absorb increased aid, with amounts and modalities tailored to their circumstances? What are the constraints to scaling up on the donor side and how can they be addressed?
- What key challenges do Ministers see in improving the delivery of aid? How can aid predictability be improved? How can coherence in aid delivery be ensured in the increasingly complex aid architecture?
- Do Ministers agree with the proposed agenda for the Bank to support the scaling-up effort? What actions do they consider as particularly high priorities? Do they agree that a strong IDA15 replenishment is a critically important step in ensuring the effectiveness and coherence of the overall aid effort?

I. Introduction

1. At the Gleneagles and UN Millennium+5 summits two years ago, the international community, building on the Monterrey Consensus, committed to substantially increase support to countries that were putting in place policies and capacities to scale up development results. The commitments included a special focus on Africa, with the objective of doubling aid by 2010. The country-based development model, centered on country-owned and results-oriented growth and poverty reduction strategies, was envisaged as the main vehicle for scaling up to accelerate progress toward the Millennium Development Goals (MDGs) and related outcomes. Donors committed to aligning and harmonizing their support around the country-driven strategies in a way that reinforced, rather than weakened, domestic systems. The country-based approach to scaling up development assistance to poor countries has been supported in successive Development Committee communiqués.² More recently, the Gleneagles commitments were reaffirmed at the 2007 G8 summit in Heiligendamm.

2. Five years since Monterrey, developing countries have made important progress in strengthening the strategies, policies, and institutions that underpin their development, although progress has been uneven and significant challenges remain in effectively linking the strategies to operational frameworks. Donors have also taken some important steps toward improving the quality of aid, but aid predictability remains an important issue. Moreover, the rise in the quantity of aid since 2003, which was largely fuelled by debt relief, stalled in the past year.

3. While progress in scaling up has been slow, the demands for aid remain large. Broad-based global economic growth since 2000 has propelled impressive reductions in poverty while the MDG targets have helped stimulate more rapid expansion of basic health and education services. However, despite these gains, nearly one billion people remain in extreme poverty. Most developing regions are off track on the health-related MDGs—reducing child and maternal mortality—while Sub-Saharan African is off track on all MDGs.³

4. The context for scaling up has evolved in important ways in the post-Monterrey period as a result of changes in the global aid architecture. Special-purpose global funds utilizing vertical approaches to aid delivery—directly funding specialized activities in countries, e.g., combating a major disease such as HIV/AIDS—are of increasing importance in total aid flows. There has also been a trend toward increased tying of aid from bilateral sources to specific purposes. Additionally, the sources of aid have increased in number, with several middle-income countries emerging as important donors, but often operating outside the aid coordination mechanisms used by traditional donors. Flows from private foundations also have increased in significance. These developments have made the aid architecture markedly more complex, characterized by a proliferation of aid channels, fragmentation of aid flows, and increased earmarking of aid. While the new sources of aid bring with them the prospect of much needed increases in aid flows to help countries step up their efforts to achieve the MDGs, they also pose new challenges to aid

² See, for example, World Bank and IMF. 2007a.

³ For more information on progress in achieving the MDGs, see World Bank. 2007e.

effectiveness and to ensuring that the scaling up of aid achieves the desired development objectives at the country level.⁴

5. Effective scaling up also faces the challenge of reconciling the multiple objectives inherent in the delivery of aid. Given the political economy of aid in donor countries, donors feel the need to demonstrate that aid delivers quick and visible results while the country-based development approach calls for medium- to long-term commitments for building capacity and institutions. Similarly, absorptive capacity concerns point to scaling up first in better performing countries, yet there is a strong interest in increasing support to fragile states, which present high risks but also the promise of high rewards.

6. Against this background, the report assesses progress in the scaling-up agenda and highlights the main challenges and priorities going forward. The analysis concentrates on low-income countries, with a particular focus on those in Sub-Saharan Africa. Despite the sharp rise in private capital flows to developing countries, official development assistance (ODA) remains the chief source of external financing for most low-income countries. In Sub-Saharan Africa, home to a majority of these countries, official flows on average account for about two-thirds of all capital inflows. ODA also has a role, but a smaller role, in middle-income countries—to catalyze reforms, support efforts to tackle concentrations of poverty, help counter negative shocks, and support global public goods. Issues relating to middle-income countries are addressed in a separate paper.⁵

7. The main report presents a concise synthesis of the analysis and the main messages; details of the supporting analysis are presented in annexes.⁶ Section II reviews progress being made at the country level in strengthening the country-based development model. Section III assesses how donors are responding, in terms of providing more and better aid, to the progress countries are making in developing their potential to scale up. Section IV draws implications for the role of the World Bank, working with partners, in supporting the scaling-up effort.

II. Strengthening the Country-Based Development Model

8. The changing aid architecture has made the country-based development model even more important for aid effectiveness, as it provides an essential platform for aligning aid from multiple sources, including vertical funds and private foundations, with national priorities and systems. A strong country-led strategic framework is vital for ensuring complementarity among the different aid modalities in supporting the country development objectives. By embedding shorter-term interventions within medium- to long-term strategies, the country-based development model can help to reconcile the tension between achieving immediate results and supporting longer-term development goals. Even in fragile states at an early stage of strategic and institutional development, some integrating framework at the country level is necessary to ensure coherence in donor support. Much of the growing agenda relating to global and regional public goods, such

⁴ For a fuller discussion of the changing aid architecture and its implications, see IDA. 2007b.

⁵ See World Bank. 2007k.

⁶ The analysis also draws on several recent reports prepared for IDA15 and the Development Committee on the international aid architecture, the country-based model, aid alignment and harmonization, global public goods, and fragile states: see IDA 2007a, 2007b, 2007c; and World Bank 2007c.

as environmental preservation, also involves embedding interventions and related support in national strategies and systems.⁷

9. Strengthening the country-based development model thus lies at the core of the scaling-up agenda. This report reviews progress on three key dimensions of the country-based model that define the strength of a country's strategic and implementation framework for scaling up development results and its effectiveness as a vehicle for alignment and harmonization of partner support:

- a country-led and results-oriented development strategy that sets out clear goals and priorities and policies and programs to achieve them;
- a sound macroeconomic framework; and
- a capable institutional framework to support the implementation of the country strategy.

10. The analysis finds progress on all of these dimensions in a broad range of low-income countries. A stronger strategic and implementation framework is emerging at the country level to support scaling up, though progress of course varies across countries, with some countries more ready than others to utilize an increase in resources effectively to scale up development results.

Poverty Reduction Strategies

11. The strategic framework for development has strengthened with progress on Poverty Reduction Strategies (PRSs). As of July 2007, 62 countries were implementing PRSs or interim PRSs, 22 of which were implementing their second PRSs. Of the 21 fragile states that have instituted PRS mechanisms, four have a PRS-II, ten have a PRS-I, and seven have either an Interim PRS or a Transitional Results Matrix. The quality and operational effectiveness of the PRSs have improved, especially in the second-generation PRS (PRS-II) countries.

12. In the last five years, countries have made significant gains in strengthening their poverty reduction strategies (or equivalent national development strategies). The Paris Declaration monitoring process, launched in 2005, assesses progress toward building evidence-based strategic frameworks—the basis of the PRS initiative—according to two broad measures: Indicator 1 – the extent to which countries have operational development strategies; and Indicator 11 – the strength of results-oriented frameworks.⁸ World Bank assessments indicate that the proportion of PRS countries that have a largely developed operational development strategy or have made significant progress toward establishing one has increased from less than half in 2001 to four-fifths in 2006. The proportion of countries that have made similar progress toward developing a results-oriented framework has increased from one-fifth to almost two-thirds over the same timeframe. Progress has been strongest among PRS-II countries.⁹

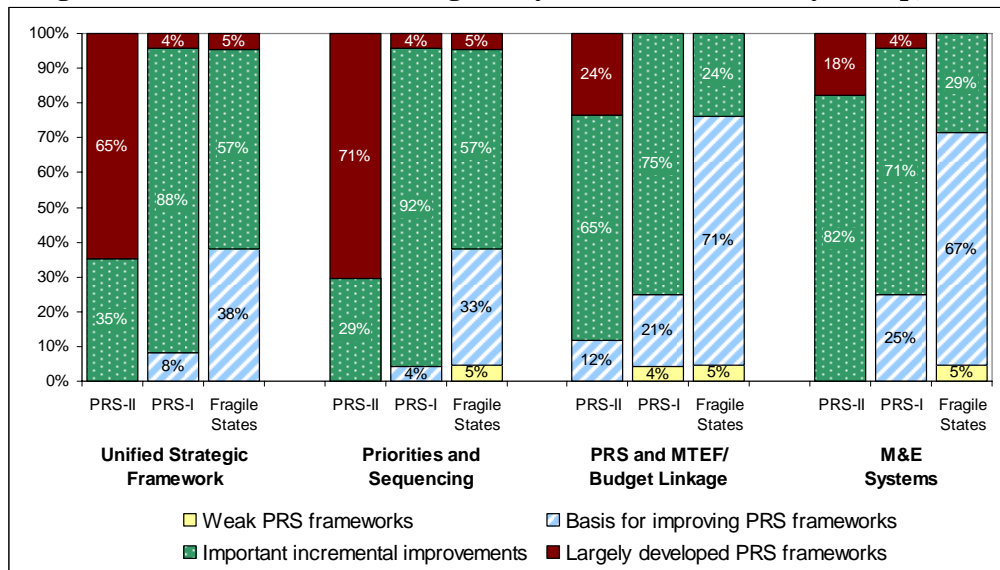
⁷ See World Bank. 2007c.

⁸ See Annex 1 for a fuller discussion of country-level progress in preparing and implementing PRSs.

⁹ For further details, see World Bank. 2007h.

13. Indicators 1 and 11 of the Paris Declaration monitoring process are based on several sub-indicators, four of which are featured in Figure 1 below.¹⁰ Progress is especially strong on building unified strategic frameworks with clear priorities and sequencing. Most PRS-II countries have reached good standards in terms of forging unified and well-prioritized strategies, while the vast majority of PRS-I countries have also demonstrated important incremental progress. Improvements have also been made in a number of PRS-II countries in linking the PRS to the budget and the medium-term expenditure framework and in bolstering monitoring and evaluation (M&E) systems. However, on average, progress on these institutional dimensions has been more limited. Only about a quarter of PRS-II countries (including Rwanda, Tanzania, Uganda, and Zambia) have largely developed links between their PRS and the budgetary framework. Mozambique, Tanzania, and Uganda are among the fewer than one-fifth of PRS-II countries whose country-level M&E systems can be considered largely developed.

Figure 1. PRSs: Indicators of Progress by Criteria and Country Group, 2006



Source: World Bank. 2007h.

14. The formation of strong links between the PRS and the budget represents an institutionally demanding objective. The shortcomings captured in Figure 1 are in part due to weaknesses in the budget itself, particularly in the areas of execution and reporting.¹¹ The poor predictability of aid and off-budget financing mechanisms often add to the challenge of forging reliable budgets and medium-term expenditure frameworks linked to the PRS. Successful experiences in developing stronger links between the PRS and key domestic systems

¹⁰ In the charts presented in this report, the PRS-II group includes 18 countries (Benin, Bolivia, Bosnia and Herzegovina, Burkina Faso, Ethiopia, Ghana, Madagascar, Malawi, Mauritania, Mozambique, Nicaragua, Rwanda, Senegal, Tanzania, Uganda, Vietnam, Yemen, and Zambia); the PRS-I group includes 22 countries (Albania, Armenia, Azerbaijan, Bangladesh, Bhutan, Cameroon, Cape Verde, Dominica, Georgia, Guyana, Honduras, Kenya, Kyrgyz Rep., Lesotho, Mali, Moldova, Mongolia, Nepal, Niger, Pakistan, Serbia, and Sri Lanka); and the fragile states group includes 21 countries (Afghanistan, Burundi, Cambodia, Central African Republic, Chad, Congo DR, Congo, Republic of, Cote d'Ivoire, Djibouti, The Gambia, Guinea, Guinea-Bissau, Haiti, Lao PDR, Liberia, Nigeria, Sao Tome and Principe, Sierra Leone, Sudan, Tajikistan, and Timor-Leste) that have instituted some PRS mechanism—either a PRS, an interim PRS, or a Transitional Results Matrix.

¹¹ IMF. 2007b.

demonstrate the importance of building on existing processes and domestic ownership of the reform agenda.¹²

15. Well-defined results assessment frameworks, linked to national monitoring, evaluation, and statistical systems, are crucial for effective resource use. With an enhanced focus on managing for results, countries have in recent years been making progress in establishing results-oriented reporting and assessment frameworks that monitor progress against key dimensions of the national and sector development strategies.¹³ In Uganda for example, the establishment of the national monitoring system was catalyzed by domestic pressure for evidence-based decision-making. The national system integrates several agency systems to track progress on the PRS. In Burkina Faso, the Ministry of Finance regularly consolidates results from the regions and sectors for dissemination to parliament and other government and non-government groups. Nonetheless, broad-based progress in building national monitoring and evaluation frameworks remains constrained by institutional fragmentation and weak capacity, especially in statistical systems, as well as by a lack of operational detail in many PRSs.

16. While the first-generation PRSs tended to have a strong focus on social sectors, the second-generation PRSs have broader treatment of economic growth and private sector development. For example, enhancing private sector competitiveness and boosting growth are central pillars of the second-generation PRSs in Bosnia and Herzegovina, Ghana, Mozambique, Nicaragua, Tanzania, and Vietnam. Improving the private investment climate is increasingly a core area of emphasis in country reform programs, and progress is reflected in improving indicators of private sector policy and institutional framework for a broad range of low-income countries.¹⁴ As second-generation PRSs become more mainstreamed into national planning processes, they have started also to set out longer-term visions of development, linking medium-term PRS targets to longer-term objectives of sustained growth and MDG achievement. The articulation of a clear and prioritized agenda for stronger, shared growth is, however, hampered in many cases by insufficient growth diagnostics and sector analysis. Lack of supporting analysis also constrains the costing of the development strategy and the assessment of the resource and macroeconomic implications of scaling-up options to achieve longer-term goals such as the MDGs.

Macroeconomic Framework

17. Developing countries' macroeconomic performance has improved considerably in recent years. Growth has picked up pace, inflation has moderated, and fiscal deficits have declined (Figure 2 presents key indicators for low-income countries). While variable across countries, the improvement in macroeconomic performance has increasingly become more broadly based. Sub-Saharan Africa, long trapped in anemic growth, has shared in the acceleration of growth. There are 20 countries in the region that have achieved average GDP growth of more than 5 percent in the past five years. Better performing low-income countries have also seen their debt burdens reduced significantly, first through the HIPC Initiative and more recently through the Multilateral Debt Relief Initiative (MDRI).

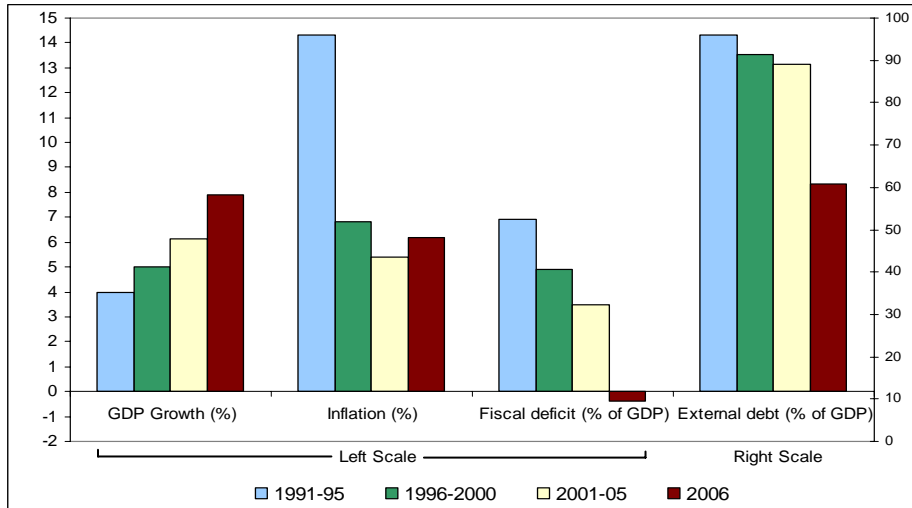
¹² See Wilhelm and Krause. 2007; and Bedi et al. 2006.

¹³ For more details, see World Bank. 2006a.

¹⁴ See World Bank 2006d and 2007e.

18. The acceleration of growth and gains in financial stability are underpinned by improved management of macroeconomic policies. Within the low-income group, countries that have prepared and are implementing PRSs on average achieve a higher CPIA score for macroeconomic management (Figure 3).¹⁵ There is a trend toward improved macroeconomic management also in most fragile states. Continued implementation of sound macroeconomic policies will be important to build on these gains.

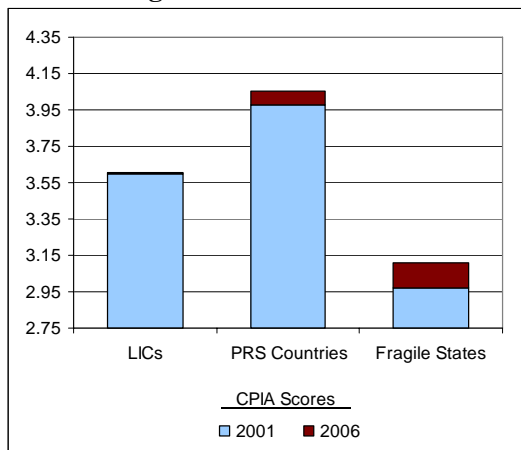
Figure 2. Low-Income Countries: Growth and Macroeconomic Performance



Note: Numbers for 2006 are staff estimates.

Source: IMF and World Bank database.

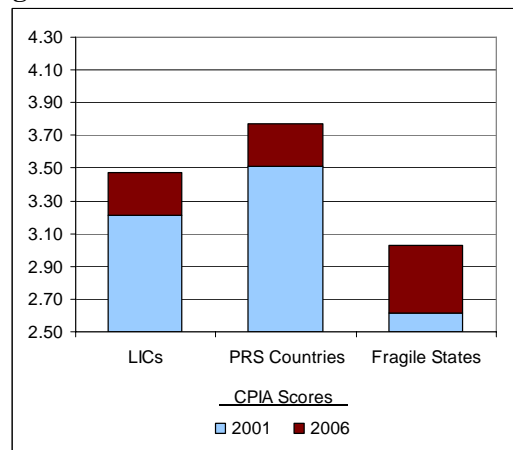
Figure 3. Management of Macroeconomic Policies



Note: Reported scores are averages of three CPIA criteria: macroeconomic management; fiscal policy; and debt policy.

Source: World Bank CPIA database.

Figure 4. Indicators of Revenue Mobilization



Source: World Bank CPIA database.

19. Countries are also making efforts to strengthen domestic revenue mobilization. Average CPIA scores for revenue mobilization for low-income countries have improved, a trend which is strongest among PRS countries (Figure 4). Stronger domestic revenue mobilization is important

¹⁵ Country Policy and Institutional Assessment (CPIA) scores are prepared by Bank staff and range from a low of 1 to a high of 6.

both to raise more resources to support development today and to underpin longer-term fiscal and debt sustainability. Even for countries with substantial access to grant financing, efforts must be made to tap the potential for increasing domestic revenues, and to utilize those resources efficiently, in order to avoid developing continued heavy dependence on aid.

20. Stronger macroeconomic fundamentals provide countries with a more stable and secure financial environment in which to pursue the goals of accelerated growth and poverty reduction. The more favorable macroeconomic context of recent years has allowed aid recipients to more fully spend and absorb increases in aid, in contrast to earlier years when more uncertain macroeconomic conditions prompted them to save part of the aid increments. Motivations for initially limiting the spending and absorption of aid included building reserves to strengthen macroeconomic stability, hedging against aid volatility and possible future reductions in aid, and concerns about exchange rate appreciation. As countries' macroeconomic positions strengthened, they opted for fuller spending and absorption of aid. This has been the case with countries such as Ethiopia, Ghana, Madagascar, Nicaragua, Rwanda, and Tanzania, which experienced surges in aid during 1999-2005. The experience of these countries provides little evidence of significant real exchange rate appreciation accompanying a rise in aid inflows. Analysis of the recent surges in aid shows that, with careful macroeconomic management and effective use of the incremental resources in productivity enhancing investments, sizable increases in aid can be absorbed without a significant appreciation of the real exchange rate and loss of external competitiveness.¹⁶

21. Improvements in developing countries' macroeconomic management have been accompanied by a strengthening of the supporting analytical framework. Initiated in the wake of the debt relief operations, joint Bank-Fund debt sustainability assessments (DSAs) now systematically and regularly analyze a country's debt outlook.¹⁷ Fiscal policy for growth studies provide a stronger, medium-term analytic framework for assessing fiscal space and implications for policy in terms of the level and composition of spending and options for resource mobilization.¹⁸ Alternative strategies to scale up development results are being analyzed—including their costing, macroeconomic implications, and policy trade-offs over time and across sectors—using models, notably the Bank's Maquette for MDG Simulations (MAMS).¹⁹ Fiscal space and MAMS analyses allow an examination of the potential of efficiency gains and increased domestic (public and private) resource mobilization, as well as increased external resources, to fund scaled-up development strategies, consistent with maintenance of longer-term fiscal and debt sustainability. Detailed analysis using these instruments, however, has so far been limited to a few countries. Going forward, countries' macroeconomic management of aid inflows will be facilitated by the stronger analytic framework that has emerged.

Institutional Framework

22. Sound public institutions and capacity are critical for development effectiveness. Effective public resource management requires strong systems for public expenditure

¹⁶ See Annex II for an analysis of macroeconomic management of aid inflows in a sample of countries. See also IMF. 2007a.

¹⁷ See IDA and IMF. 2005; and IDA and IMF. 2006.

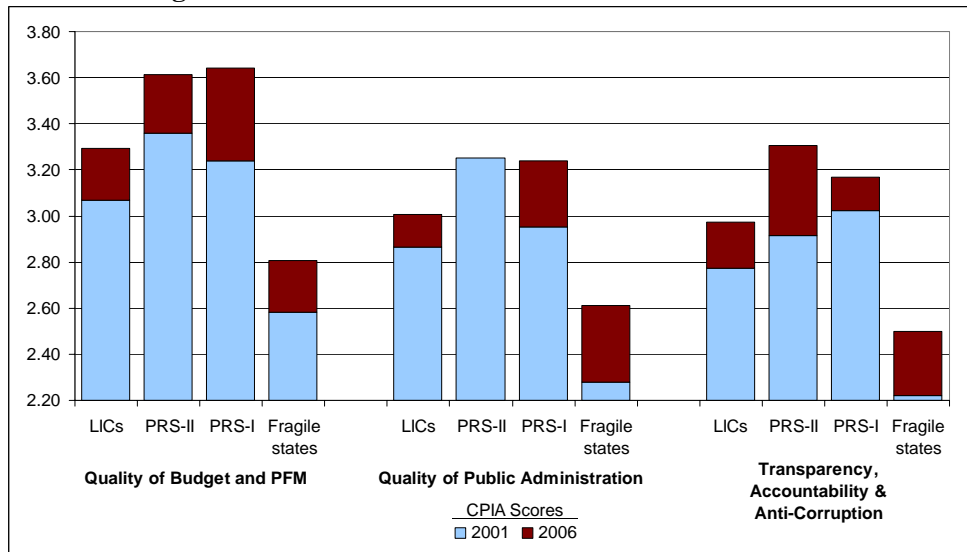
¹⁸ See World Bank. 2007b.

¹⁹ See Bourguignon et al. 2007.

management and financial accountability. Effective planning and implementation of projects requires adequate capacity in sector ministries and implementing agencies, including at the subnational level. In decentralized administrative structures, sound systems for intergovernmental fiscal relations are an important aspect of the overall public resource management framework.

23. Improving the quality of governance and strengthening key systems such as the public financial management (PFM) framework have been an increasingly important focus of reform in developing countries. The reform efforts are reflected in improving indicators for the quality of public institutions and management in most low-income countries.²⁰ From the standpoint of aid effectiveness, a strong PFM system (budget and expenditure management, procurement, accountability mechanisms) is an especially important element of the governance agenda. The Bank's CPIA indicators show improvement in PFM across the three categories of countries analyzed: PRS-II, PRS-I, and fragile states (Figure 5). They also indicate improvement in the quality of public administration, and in transparency, accountability, and control of corruption in the public sector. In general, performance has been strongest in PRS-II countries, but recent years have seen a more broad-based improvement in the PRS group as a whole. There is an encouraging improvement in the indicators for fragile states but from a much lower base, reflecting their weaker governance contexts.

Figure 5. Governance Trends in Low-Income Countries



Source: World Bank CPIA database.

24. Strong efforts are needed to ensure continued progress in upgrading public sector governance, especially in the fragile states but also in many PRS countries where, despite recent improvements, the process of institutional strengthening is still at a relatively early stage. Improvement of PFM is a core area of World Bank support to countries for governance reform and capacity building and it receives strong emphasis in the Bank's new Governance and Anticorruption Strategy.²¹ Diagnostics and the design and monitoring of reform in the PFM area

²⁰ See Annex III for a more detailed assessment.

²¹ World Bank. 2007d.

have been strengthened by the development of a comprehensive set of public expenditure and financial accountability (PEFA) indicators.²² As of July, 2007, PEFA assessments had been completed, substantially completed, or commenced in 68 countries. Initial results from the PEFA assessments, when compared with results of earlier public expenditure management assessments for HIPC countries, confirm the finding of a gradual improvement in PFM obtained from the CPIA indicators.

25. While strengthening PFM and related systems is a major focus of governance reform in the low-income countries, their reform efforts also span other important dimensions of institutional strengthening, including building the administrative capacity of key public agencies, reforming the civil service, building local government capacities, and strengthening government transparency and accountability mechanisms more generally. This is a broad, challenging, and long-term agenda, requiring a sustained reform effort. But progress is being made in many countries, as reflected in the improving indicators for the quality of public administration and transparency, accountability, and control of corruption noted above. In Africa, Burkina Faso, Mozambique, Rwanda, and Tanzania, among others, are engaged in public sector capacity building and civil service reform. The Africa Peer Review Mechanism (APRM) has become an important means to spur broad-based governance reform. APRM reviews have been completed, for example, in Ghana and Rwanda, and the recommendations are being implemented by both governments. There are similar examples of broad-based public sector reform and capacity building in other regions: for example, in the Western Balkans and several countries in Central Asia.

Priorities in Strengthening Country Strategy and Institutional Framework

26. How to build on the progress summarized above? While specific needs and priorities vary across countries, the assessment reveals three key areas for action by countries, and support from their development partners, in further strengthening country strategies and capacities for scaling up development results:

- Underpinning PRSs with stronger growth diagnostics and sector analysis to sharpen their focus on the agenda for stronger, shared, private sector-led growth, supported by well-developed strategies and implementation plans for key sectors.
- Costing PRSs, strengthening PRS-budget links, and assessing scaling-up scenarios in terms of their implications for macroeconomic and fiscal frameworks.
- Strengthening public resource management and institutional capacities, especially the systems and capacities relating to PFM and results reporting and assessment, including statistical systems.

Scale-Up Opportunities

27. Efforts to accelerate progress toward the MDGs and related development outcomes will rely primarily on resources generated by the countries themselves. Developing countries must

²² The PEFA framework is a product of partnership between the World Bank, the IMF, the European Commission, France, Norway, Switzerland, UK, and the Strategic Partnership with Africa. See <http://www.pefa.org>.

build on recent progress to mobilize more domestic resources—moving more vigorously to spur private investment and economic growth, strengthening revenue administration, and improving the efficiency of spending. They must also build on reforms to improve their investment climate to attract more private non-debt capital inflows, especially foreign direct investment (FDI). Infrastructure scaling up, where the financing requirements are especially large, offers opportunities for leveraging more private investment, including through public-private partnerships.

28. Still, for many low-income countries significant increases in official development assistance (ODA) also will be needed. For most low-income countries, ODA remains the major source of external financing. Total net private capital flows to developing countries reached a record \$647 billion in 2006, composed of \$325 billion in FDI, \$94 billion in portfolio equity, and \$228 billion in debt flows. Recorded private remittances also continued their upward trend, reaching almost \$200 billion in 2006. The lion's share of the private capital flows is directed to middle-income and "blend" countries (countries with low per capita incomes but stronger capital market access). Low-income countries excluding the "blends" receive less than 2 percent of private debt and portfolio equity inflows and only about 5 percent of FDI. Remittances are more important, with low-income countries receiving nearly 15 percent of total estimated inflows. The bulk of these inflows, however, is concentrated in a few countries.²³

29. One of the dilemmas donors face as they scale up ODA is how to allocate it. Fundamental to aid effectiveness is the principle of performance-based aid allocation. While countries that are strong performers are clear candidates for scaled-up assistance, the improving performance of fragile states, as shown above, would suggest that there is scope for selectively increased assistance also to this group of countries. Moreover, recent concern with "aid orphans" suggests that greater attention should be given to countries that typically receive far less aid than would seem warranted by their needs and absorptive capacity. In fact, thanks to the progress countries are making in strengthening their development strategies and institutional frameworks for implementation, there is a broad range of countries that can productively absorb increased aid to accelerate progress toward their development goals—with amounts and modalities tailored to their circumstances. Another issue of growing importance is how to scale up support for global and regional issues that require global or regional collective action, but country-level implementation.

30. ***PRS-II Countries.*** There are a number of strong performers in the PRS-II group of countries where the strengthening of the strategic and institutional framework for scaling up development results is sufficiently advanced to merit an early delivery on the Gleneagles commitment to provide significant increases in aid, including a doubling of aid to Africa. Some examples in Africa include Burkina Faso, Ghana, Madagascar, Mozambique, Rwanda, and Tanzania. Box 1 presents a scaling-up scenario for Ghana. Similar scenarios for Madagascar, Rwanda, Tanzania, and Uganda are presented in Annex II and summarized in Box 2. Some of these countries have already seen increases in their aid inflows, but this category of countries needs and can absorb substantially more to accelerate growth and progress toward the MDGs. A larger proportion of aid can be provided to these countries in the form of budget support, where circumstances are appropriate, although more investment finance is also needed to meet their

²³ World Bank. 2007e and 2007f.

considerable needs, especially in infrastructure. In East Asia, Vietnam is a strong performer with sizable needs and demonstrated capacity to utilize scaled-up support. The aforementioned countries are not the only ones that demonstrate a significantly enhanced absorptive capacity. Most other countries in the PRS-II group also are in a position to absorb substantial increases in aid, although not immediately on the same scale as the strongest performers in the group.

Box 1. Ghana: A Strong Case for Scaling Up

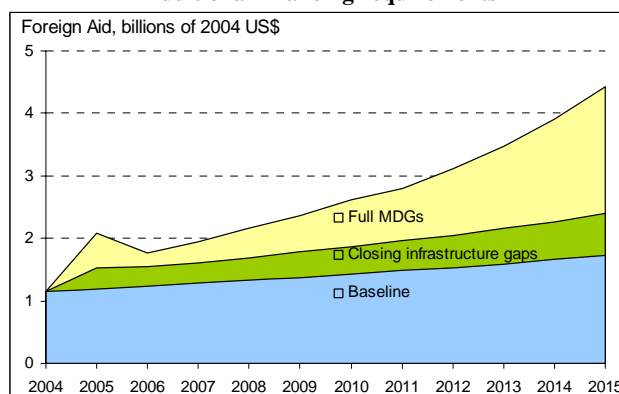
Ghana has emerged as one of the best performing African economies, with growth consistently surpassing 5 percent since 2001 and rising to above 6 percent in 2006. Improved macroeconomic management and significant and ongoing progress on structural and institutional reforms present a real opportunity to accelerate growth and progress toward the MDGs. A forthcoming CEM simulates three growth scenarios to 2015 using the MAMS model, including a baseline scenario with annual growth at 6.9 percent, an accelerated growth with closing of infrastructure gaps scenario yielding growth at 7.4 percent, and a full MDG achievement scenario with growth rising to 7.8 percent. The simulations show that Ghana can take on additional resources without suffering from Dutch disease. Thanks to continuing progress, PFM capacity is not considered a binding constraint, but stronger efforts will be needed to build sectoral capacity, especially in health, to realize the full MDG achievement scenario. Ensuring “value for money” is a strong, overarching emphasis in the Government’s public resource management strategy.

MDG scenarios, 2015

	Baseline growth (6.9%)	Accelerated growth (7.4%) with closing of infrastructure gaps	Accelerated growth (7.8%) with full MDG achievement
Poverty headcount ratio (%)	12	10.2	9.8
Primary completion rate (%)	89	94	100
Under-5 mortality (per 1,000 live births)	97	95	40
Maternal mortality (per 100,000 births)	440	428	185
Access to safe water (%)	62	75	85
Access to sanitation (%)	47	70	85

Note: All values in the last column are MDG targets except the poverty rate where the MDG target of 26 percent is exceeded.

Additional financing requirements



Baseline growth puts Ghana in a position to achieve the poverty reduction MDG well ahead of 2015. However, Ghana will not achieve many other key MDGs, including primary completion, child and maternal mortality, and access to safe water and sanitation. In the accelerated growth with the closing of infrastructure gaps scenario, primary completion and access to safe water and sanitation approach MDG targets, but the health MDGs remain elusive (see table). The full MDG scenario achieves the health MDGs but at the cost of a substantial additional commitment of resources. In the baseline scenario, ODA requirements are estimated at about \$1.5 billion annually (about 10 percent of current GDP), only modestly higher than present levels. In the closing of infrastructure gaps scenario, additional ODA of \$350-430 million p.a. (2.5-3 percent of GDP) is needed, which should be feasible. In the full MDG achievement scenario, however, further large increases in financing are needed, averaging \$750 million annually between 2007 and 2011 (5-6 percent of GDP) and rising to \$1.7 billion annually between 2012 to 2015 (8-9 percent of GDP; see chart). Given the magnitude of the additional financing requirement, it is unlikely that all of it can be met from ODA, which underscores the need for even stronger efforts by Ghana to mobilize domestic resources, improve efficiency, and catalyze private participation.

Source: World Bank. 2007i (forthcoming); Ghana MAMS simulations.

31. **PRS-I Countries.** There is scope for scaling up of aid also in many countries in the PRS-I group, starting with moderate increases but building to larger amounts as absorptive capacities expand, with aid programs comprising a mix of modalities including budget support, investment projects, including sector-wide approaches, and technical assistance, depending on specific country circumstances. There is a two-way relationship between aid and institutions: aid is more effective when institutions are strong, but properly directed aid can also be instrumental in building stronger institutions. Even where current systems and capacities fall short, aid may be

scaled up based on a clearly improving trend in institutional capabilities and national commitment to a program of continued institutional strengthening that aid helps support. The building of country capacity and the scaling up of aid can thus proceed in parallel, rather than sequentially. Examples of PRS-I countries with scope for scaling up aid include, but are not limited to, Armenia, Bangladesh, Honduras, Kyrgyz Republic, and Mali.

Box 2. Scaling-up Possibilities: More Country Examples

The country cases summarized below draw on MAMS applications, fiscal space studies, and DSA reports. These PRS-II countries are all strong African performers, with potential to scale up development results that merits support from donors. Although these countries have recently benefited from MDRI debt relief, which significantly improved their external debt situation, they need to limit recourse to non-concessional sources for meeting official external financing requirements in order to preserve debt sustainability.

Madagascar. Improved policies in the past five years have boosted growth, with growth of 6 percent likely over the medium term. A recent application of MAMS analyzes two scenarios. A baseline scenario, based on current trends, achieves moderate progress toward the MDGs. A more ambitious scenario achieves the health and water and sanitation MDGs, almost achieves the primary completion MDG, and makes significant progress toward the poverty MDG (at about 70 percent, the poverty rate is well above African average). The financing requirements of this scenario are double those of the baseline scenario (aid recently has averaged about 8 percent of GDP). If all of the large additional financing is met from foreign aid, the real exchange rate appreciates by more than 20 percent. Meeting part of the additional financing from increased domestic resource mobilization alleviates the pressure on the exchange rate. A recent fiscal space study assessed tax revenue to be below its potential by at least 3 percent of GDP. As part of the latest PRS, the Government plans to undertake a major tax reform. Another implication of the scaled-up scenario is the need for stepped-up efforts to strengthen institutional capacities.

Rwanda. Rwanda has achieved an impressive recovery from conflict. Growth has averaged 5.3 percent since 2000. Alongside macroeconomic progress, service delivery has improved. These achievements have been supported by sizable aid inflows. Rwanda's Vision 2020 aims to raise per capita income growth to 6-7 percent. This will require substantial increases in investment to address poor infrastructure that acts as a major constraint to private investment and growth. Rwanda also faces large commitments in education and health. A recent fiscal space study assessed options to finance the needed increases in development spending. Rwanda has raised revenue collection substantially but, given the narrow tax base, there are limits to further revenue enhancements. There is scope for improving the efficiency of spending. The Government has started several initiatives to strengthen budgeting and expenditure management. Even with improved domestic resource management, accelerating progress toward the MDGs will require a significant increase in aid—an estimated 15-20 percent increase per year over the current aid level of nearly \$500 million. Better alignment with government programs will enhance aid effectiveness.

Tanzania. The macroeconomic framework underpinning growth has improved. Public financial management has been strengthened. Aid coordination has improved with the preparation of a Joint Assistance Strategy. MAMS simulations show that the poverty reduction MDG is almost achievable with continuation of the higher average growth of recent years—about 5.5 percent. But an acceleration of growth to the 6-7 percent range, quite feasible if Tanzania's reform momentum to improve the climate for private investment is sustained and adequately supported by partners, would achieve the target well ahead of schedule. However, achievement of most other MDGs will require substantial further increases in aid, over and above the baseline scenario that assumes about the same level of aid relative to GDP as at present—about 10 percent. Stronger domestic resource mobilization (expanding the revenue base, strengthening tax administration, improving expenditure efficiency) also will be needed. The appreciation of the real exchange rate from scaled-up aid is estimated to be moderate, but the results reinforce the importance of a continued policy focus on improving Tanzania's competitiveness.

Uganda. Uganda needs to reinvigorate growth (growth averaged more than 5 percent in 2000-06, but still well below the 6.9 percent rate achieved in the 1990s). A recent fiscal space study and MAMS application assess alternative financing options for boosting growth and investment in MDG-related services. A particularly high priority is strengthening infrastructure. There is scope for mobilizing resources through better expenditure management. Cutting unproductive spending and allocating savings to higher priority programs can boost growth by 0.4-0.5 percent p.a. and improve a range of MDG indicators. Similar gains are observed if aid is scaled up and allocated to growth and MDG-oriented functions. Raising taxes, however, results in a decline of private investment growth. The analysis points to a financing strategy that employs a mix of improved expenditure efficiency, domestic revenue mobilization that emphasizes improved collection and broadening of the tax base, increased public-private partnerships, and higher aid (aid has averaged about 10 percent of GDP over the past decade). Longer term, the Government aims to reduce reliance on aid, an effort that will require careful design and sequencing.

Source: See sources cited in Annex II. Some of the analysis presented is based on work in progress.

32. ***Fragile States.*** Fragile states, particularly post-conflict and re-engagement countries, present opportunities for selective, focused, and carefully sequenced increases in aid. Development assistance is inherently risky in these environments, but rewards to successful interventions also can be high. Helping to rebuild public institutions and systems is an overarching longer-term priority for aid programs, while immediate responses can focus on urgent needs in the areas of infrastructure and social services, through projects tailored to a weaker governance context. SWAps can also be effective investment lending instruments for particular sectors with well-defined policy frameworks. Budget support, while not appropriate in the most risky situations, can be used effectively in fragile states under certain circumstances. They are most appropriate when the focus is on critical “zero-generation” policy reforms that have national ownership and are supported by robust and transparent monitoring systems. Aid programs to fragile states would benefit from greater stability in aid flows, avoiding the tendency for an abrupt and premature decline following the immediate post-stress period. Despite recent increases, overall aid to fragile states remains low in relation to their level of policy performance and poverty. While fragile states present special needs and challenges, the principle of performance-based allocation remains a fundamental basis for scaling up of assistance. Examples of fragile states presenting opportunities for increased support include Central African Republic, Haiti, and Liberia.

33. ***Global and Regional Public Goods.*** Stronger development strategies and implementation frameworks also position countries better to manage increased investments, and related donor support, that will be needed to address key global and regional challenges, such as climate change, communicable diseases, and global and regional trade integration. Ultimately, global and regional challenges need to be addressed through actions at the country level, such as investments in clean energy, disease control, and transport links connecting to regional networks. Investments in such global and regional public goods (G/RPGs) will be an increasingly important vehicle for scaled-up aid to developing countries. Promising areas for scaling up include improvement of access to clean energy, climate change adaptation, regional infrastructure initiatives, and aid for trade. Control of communicable diseases, already the major focus of GPG funding, will remain an important area of support. Regional investments are especially important for small economies by allowing them to reap economies of scale and other efficiencies by acting collectively. Some good examples of regional investment opportunities are: regionally coordinated transport development in Sub-Saharan Africa to better connect the region’s landlocked countries to markets in neighboring countries and to maritime trade; regionally integrated power supply and distribution to help Africa’s small economies expand their access to reliable and cheaper energy; and transport and energy integration in the Western Balkans, in the South Caucasus, and in Central Asia.

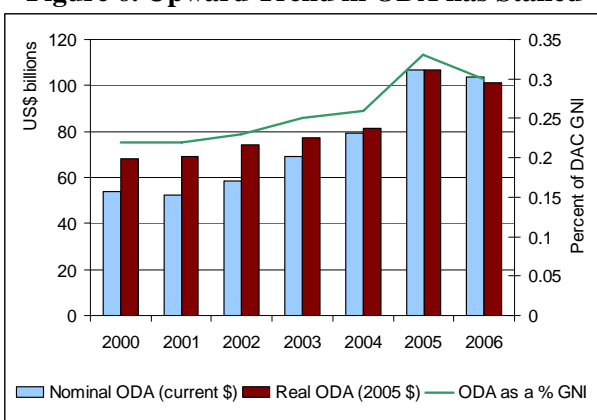
III. Improving the Delivery of Aid

34. How are the donors responding, in terms of providing more and better quality aid, to the progress countries are making in developing their potential to scale up effectively? The assessment in the paper reveals a mixed picture: there is progress in scaling up and improving aid, but overall it is slow and uneven, with new challenges arising from the changing aid architecture.

Increasing Aid to Exploit Scale-Up Opportunities

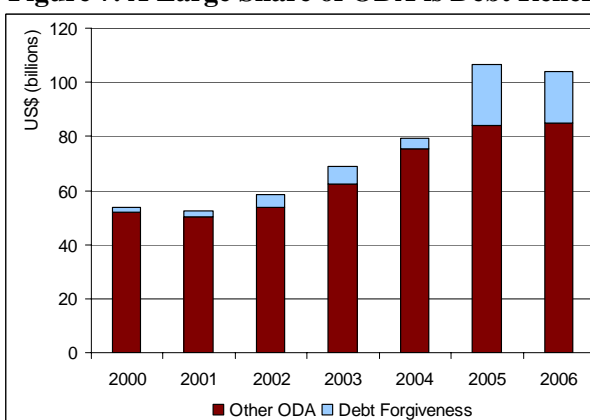
35. After rising in recent years, total net official development assistance (ODA) from DAC countries declined by 5 percent in real terms in 2006 (Figure 6). At \$103.9 billion in 2006, total net ODA was still \$24 billion higher than its pre-Gleneagles level. But much larger, and sustained, increases in aid will be needed to reach the Gleneagles target of a \$50 billion increase in real terms by 2010 (raising total net ODA to \$130 billion in constant 2004 dollars). Aid to Sub-Saharan Africa shows broadly the same pattern: it has risen but at well short of a rate that would achieve the targeted doubling of aid by 2010. Moreover, the bulk (about 70 percent) of the increase in aid post-Gleneagles is accounted for by debt relief—the Multilateral Debt Relief Initiative (MDRI) and exceptional debt relief to Iraq and Nigeria (Figure 7). Aid for core development programs—program and project aid—has shown relatively little increase. Debt relief has significantly reduced the debt burden of the beneficiary countries and contributed to an expansion of the fiscal space for development spending. However, as debt relief operations wind down, other categories of aid will need to increase quite sharply to reach the Gleneagles targets for total ODA.²⁴

Figure 6. Upward Trend in ODA has Stalled



Source: OECD/DAC database.

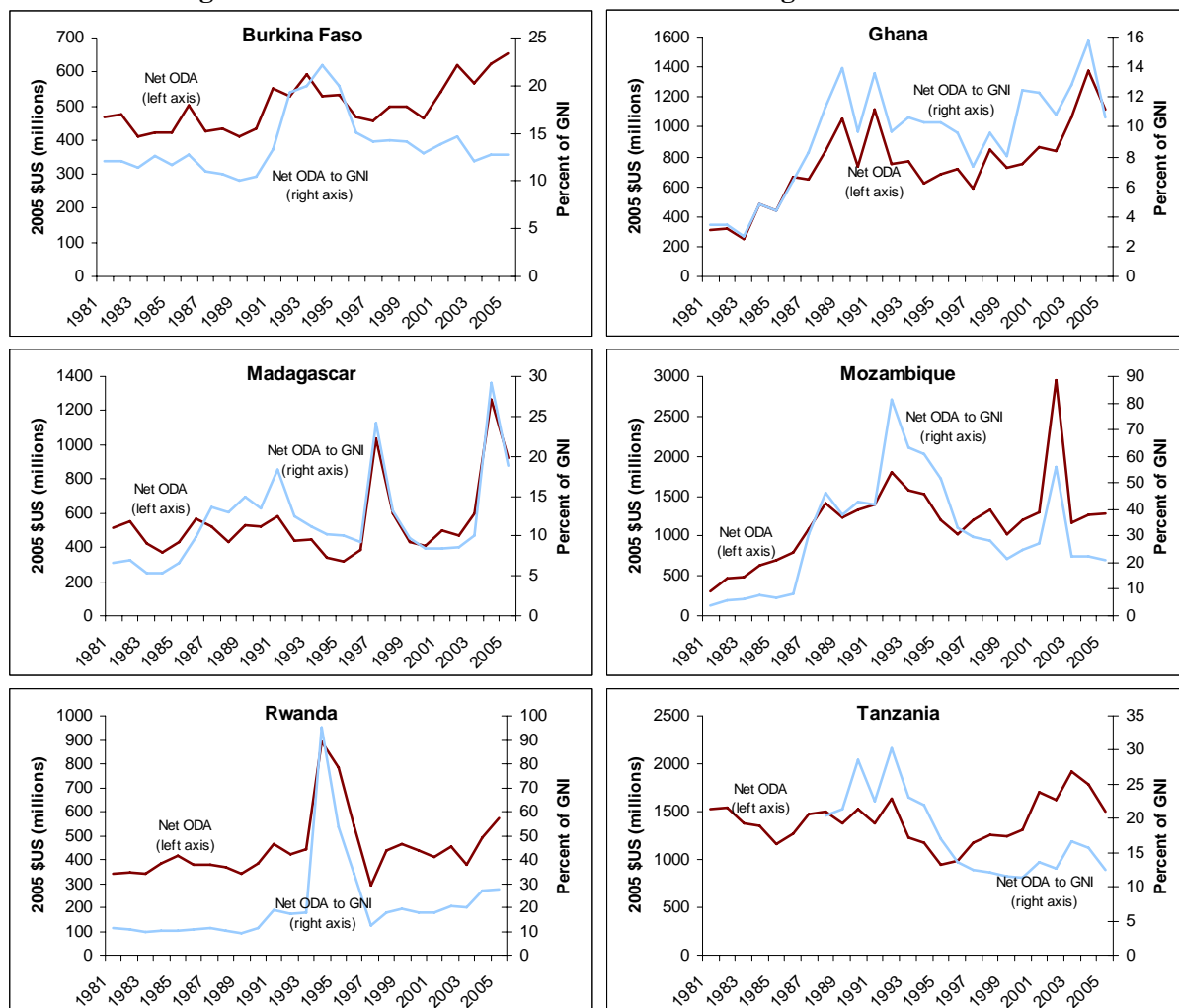
Figure 7. A Large Share of ODA is Debt Relief



36. Within these aggregate trends, there are some positive developments in terms of the distribution of aid. Better performing countries, with demonstrated capacity to make effective use of increased resources, are on average seeing larger increases in aid. This is the case with some strong performers in the PRS-II group: examples include Burkina Faso, Ghana, Madagascar, and Rwanda in Africa (Figure 8) and Vietnam in East Asia. However, increases in aid even to such countries that present strong scale-up opportunities typically fall well short of what they need and can effectively use. Strong performers on average are also seeing a larger proportion of aid being provided in flexible forms. Another group of countries that is seeing proportionally larger increases in aid are the fragile states. Much of the increase in aid to this group, however, is concentrated in a few major post-conflict situations.

²⁴ See Annex IV for a more detailed analysis of trends in ODA.

Figure 8. ODA Trends in Some Better-Performing African Countries



Source: OECD/DAC database.

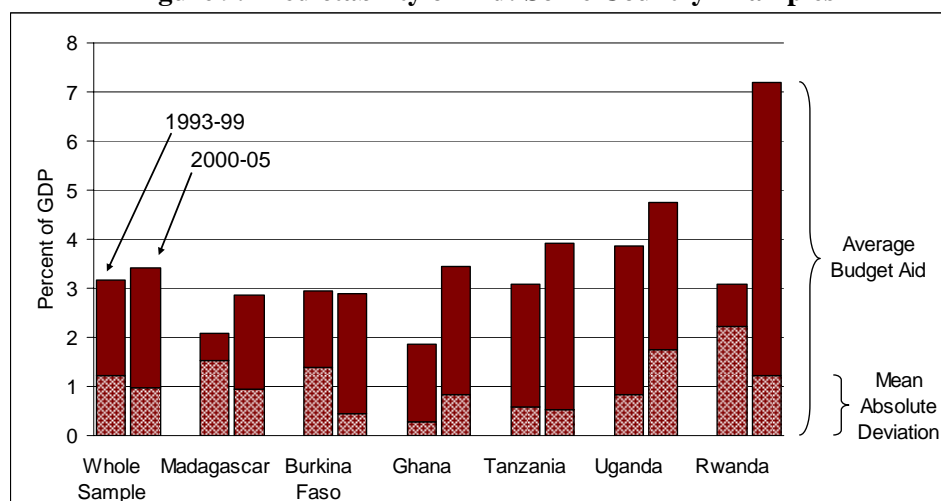
Improving Aid Predictability

37. Analysis shows an improving trend in aid predictability, but the average level of predictability remains low. Much of the improvement relates to the predictability of aid in the near term; medium-term predictability, important for countries' planning and implementation of PRSs and programs for achievement of MDGs, remains much more problematic.²⁵ Low-income countries in Sub-Saharan Africa experience the highest level of unpredictability. Predictability is especially important for budget support, yet this component of aid is typically vulnerable to greater fluctuation.

²⁵ Recent analysis shows that predictability is not only important for the development effectiveness of aid but can also help alleviate potential Dutch disease effects of aid by allowing better inter-temporal smoothing of consumption and investment decisions. See Devarajan et al. 2007.

38. Since deviations in actual aid flows from expected levels can arise in part due to factors on the recipient side, such as failure to meet conditions attached to disbursements or more generally a lack of capacity in managing aid-funded programs, one would expect aid predictability to improve as recipients' performance and capacities improve. There is some evidence that predictability is indeed improving in the better performing countries, but the pattern is uneven. In a sample of thirteen countries with relatively large aid inflows, the mean absolute deviation in budget aid receipts from expected levels declined between 1993-99 and 2000-05, but was still almost one-third of the expected levels in the latter period (Figure 9). Within the sample, among the better performing countries, the predictability of budget aid improved for some (e.g., Burkina Faso and Madagascar), stagnated for others (e.g., Tanzania), and even regressed for some (e.g., Ghana²⁶ and Uganda). The persistence of relatively low predictability of aid even in some better performing countries is a phenomenon that warrants further investigation.²⁷

Figure 9. Predictability of Aid: Some Country Examples



Note: Deviation is measured as the absolute difference between the budget aid projected in the government's program with the IMF and actual disbursement. The periods compared are 1993-99 and 2000-05; however, for Ghana, Madagascar, and Rwanda, the calculations for the first period cover only a subset of that period for lack of data.

Source: Celasun and Walliser. 2007.

39. More tangible improvements in predictability will require greater transparency in aid allocations, longer-time horizons for aid commitments aligned as much as possible with the recipient's medium- to long-term development strategy, and clearer and simpler rules for disbursements linked to performance. In this regard, some recent initiatives show more promise. The European Commission has launched a proposal for six-year aid contracts with the African, Caribbean, and Pacific (ACP) countries. Called the MDG Contract, the arrangement aims to make EC's budget support longer-term and more predictable to countries with a strong performance track record and a multiyear monitoring framework.²⁸ The U.S.'s Millennium Challenge Account employs 4-5 year aid contracts with pre-agreed disbursement schedules with

²⁶ Data for more recent years show an improvement in aid predictability in Ghana.

²⁷ The Bank is in the process of developing more detailed analysis of aid predictability at the country level, and plans to organize a workshop on the subject during FY08.

²⁸ European Commission. 2007.

qualifying countries.²⁹ Several European bilateral donors are adopting multiyear planning frameworks for aid budgets. The recent DAC initiative to ask donors to provide medium-term projections on aid at the country level is also a useful step.³⁰ Donors are increasingly providing medium-term aid projections at aid coordination meetings, though the practice is uneven and the coverage of projections in most cases is partial. On the recipient side, strengthening in-country capacity for management of aid resources would enhance the scope for greater predictability in aid flows.

Accelerating Progress on Alignment and Harmonization

40. The Paris Declaration commits the international community to improve aid effectiveness through better alignment and harmonization. DAC's 2006 survey of the implementation of the Paris Declaration shows notable, though uneven, progress on these dimensions.³¹ Indicators such as the use of program-based approaches (43 percent of total aid) and country PFM systems (40 percent) show both progress and the scope of the unfinished agenda. The Paris Declaration sets out the principle that implementation should take place at the country level. However, fewer than one-third of donors report progress on decentralization. At the country level, progress is generally greater among the strong performers in the PRS-II group. Joint assistance strategies have been prepared, for example, in Ghana, Tanzania, and Uganda. These countries have also prepared aid harmonization action plans, as have Burkina Faso, Mauritania, Nicaragua, Senegal, and Vietnam. Burkina Faso, Mozambique, and Tanzania have instituted mutual accountability reviews.

41. Aid coordination mechanisms are being revamped in a number of countries to focus more consistently on results, the link to overall development finance, and mutual accountability. In Ghana, for example, the Consultative Group process has been restructured to achieve a stronger focus on results, resources, and partnership, as exemplified by the Results, Resources, and Partnership (RRP) meetings organized by the Government of Ghana in 2006 and 2007, co-chaired with the World Bank. A group of several donors including the Netherlands, Sweden, UK, EU, UNDP, OECD/DAC, and the World Bank will be working with the Governments of Ghana, Madagascar, and Tanzania to help strengthen their results and resources partnerships during the coming year.

42. Such successes need to be replicated in a larger number of countries. Factors contributing to success include strong government leadership anchored in a clear national development strategy and strong commitment by donors to the actual implementation of the Paris principles. The increased focus on division of labor and complementarity among donors, as reflected in the recent adoption by the European Union of a voluntary Code of Conduct on complementarity and division of labor in development policy, should help with more effective collaboration on the ground.³²

²⁹ <http://www.mcc.gov/programs/compacts.php>

³⁰ OECD/DAC. 2007b.

³¹ OECD/DAC. 2007a.

³² Council of the European Union. 2007.

43. Fragile states present their own specific challenges for effective coordination of donor support and interventions. Progress has been made in defining a framework for engagement in these countries, as set out in the recent OECD/DAC principles for good international engagement in fragile states, which commit DAC members to prioritize state-building and peace-building in their assistance programs in fragile states.³³ More integrated approaches are being elaborated in the areas of state-building, peace-building, and relief-to-recovery transitions. For example, in 2003, the World Bank joined the UN and bilateral donors to carry out a Joint Needs Assessment for Liberia. Its findings were set out in a Results-Focused Transitional Framework reflecting a highly coordinated agreement between Liberia's development partners and the country's transitional government to focus reconstruction on a set of priority results. Similar efforts have been undertaken in Central African Republic, Haiti, Somalia, and Sudan, aimed at increasing the coherence between peace-building efforts and support for the country's economic, social, and institutional recovery.

Better Aligning Global Funds with Country Programs

44. Even as gains are made on the alignment and harmonization agenda, the changing aid architecture is posing new challenges for aid effectiveness. Global/vertical funds have grown rapidly in significance. Although the share of these funds in total ODA is still about 3 percent, they have become sufficiently large to dominate financing in their focus areas in many low-income countries. Most of the largest funds are engaged in health sector financing, with a narrow focus on combating specific communicable diseases, e.g., the Global Fund to Fight AIDS, Tuberculosis, and Malaria (GFATM) and the Global Alliance for Vaccines and Immunization (GAVI). In seven African countries, support from vertical funds earmarked for fighting HIV/AIDS ranges from about one-third to one-half of total spending on health.³⁴ Support to specific activities in the health sector is also the focus of the recently launched innovative financing mechanisms including the International Finance Facility for Immunization (IFFm), Advance Market Commitments for development of vaccines (AMC), and the air ticket levies.

45. While vertical funds bring much-needed attention and financing to their focus areas, and are increasingly important as sources of funding for GPGs, they can also have unintended effects that can undermine development effectiveness at the country level. Where these funds are narrowly targeted to a sector or sub-sector, and are large and scale up quickly, problems can occur, particularly in the short-run, such as misalignment with recipients' inter- and intra-sectoral priorities, mismatch between the size of funding and domestic absorptive capacity, and budgetary fragmentation when separate financing mechanisms are used (roughly one-half of health aid is off-budget). An example of the potential for mismatch between the allocation of resources and country priorities is the case of Rwanda: in 2005, spending on HIV/AIDS was 22 times the amount spent on maternal and child health.³⁵ Even though malaria is the leading cause of morbidity and mortality in the country, it receives only about a third of the donor funding allocated to HIV/AIDS (Figure 10). Reflecting the dominance of earmarked funding for specific diseases, on average only about 20 percent of all health aid to poor countries goes to support the government's overall program for the sector.

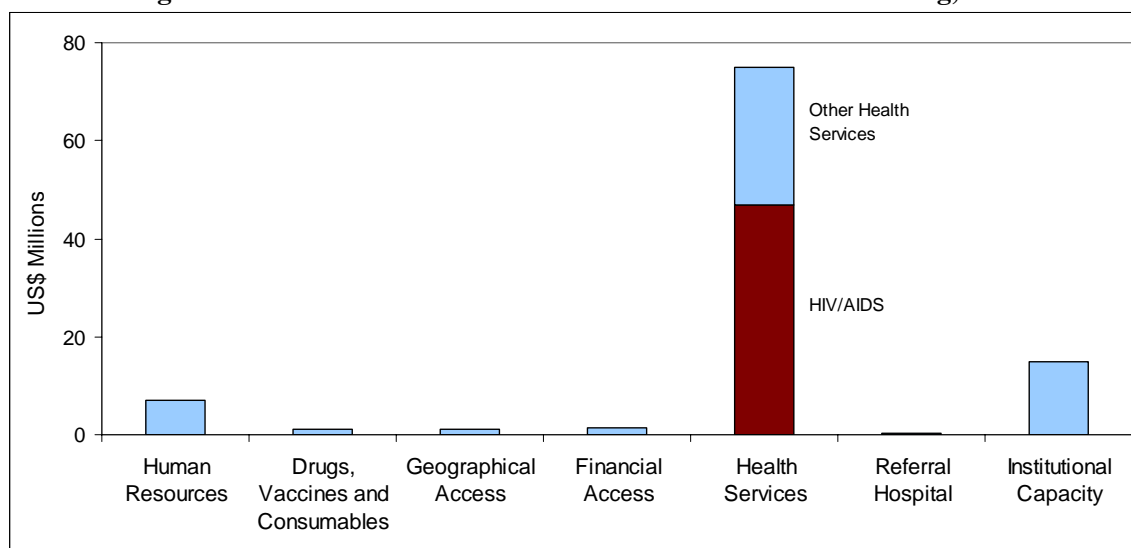
³³ OECD-DAC. 2007c.

³⁴ World Bank. 2007c.

³⁵ Republic of Rwanda. 2006.

46. Such consequences, however, are not inevitable. The key is to better align and integrate vertical and earmarked funds with country development strategies. This is important to achieve better complementarity between vertical funds and other sources of financing in supporting country strategy and priorities. It also ensures the longer-term effectiveness and sustainability of the programs supported by the vertical funds, as their success ultimately depends critically on related country policies and investments. Strong country strategies (PRSs) with sectoral depth are essential for this purpose. Vertical programs should be integrated with the national budget and use national systems as much as feasible. The issues concerning strategic coherence and harmonization are the most serious in the health sector. They also arise in other sectors that are the focus of global programs, namely, education and environment, but are less pronounced because the approaches followed by the major programs in those sectors (Education for All-Fast Track Initiative and Global Environment Facility) put more emphasis on harmonization and alignment.³⁶ The EFA-FTI, for example, uses a country-based approach to the education sector involving the local donor group, which jointly endorses the government's education sector strategy and then coordinates the scaling up of donor funding to support it.

Figure 10. Rwanda: Distribution of Donor Health Sector Funding, 2005



Source: Republic of Rwanda. 2006.

47. Given the increased and rising importance of vertical funds, it would be desirable to develop and agree upon good practice principles relating to these funds as an extension of the Paris Declaration. Joint efforts initiated by the OECD/DAC and the World Bank to that end in the lead-up to the High Level Forum on Aid Effectiveness in Accra in 2008 are very timely.³⁷ In the health sector, a promising recent initiative is the International Health Partnership launched jointly in September 2007 by several donor governments, international organizations (including

³⁶ World Bank. 2006c.

³⁷ The OECD and the World Bank have recently co-organized two policy workshops on the question of enhancing linkages between global programs and country strategies (Paris, December 4-5, 2006; and Mauritius, June 20-21, 2007).

the World Bank), and global health funds with the aim of working better together to improve the effectiveness of health aid.³⁸

48. There is also the need to strengthen harmonization with the emerging new bilateral donors. The valuable additional resources provided by the new donors will be the more effective the more they adhere to the alignment and harmonization principles of the Paris Declaration. To the extent flows from these donors take the form of loans, careful attention needs to be paid to debt sustainability. The Bank-Fund Debt Sustainability Framework is a tool that can be used by creditors and borrowers alike to assess and manage risks. The increasing participation of the new donors and major private philanthropic foundations in country aid coordination meetings is a trend that should be encouraged.

Priorities in Improving Aid Delivery

49. The foregoing review of scaling up aid and improving its quality suggests the following three priorities for aid delivery going forward:

- Delivering on commitments to increase aid through a stronger donor response to the scale-up opportunities that exist in a number of developing countries—better performing countries with a sustained record of reform and improving economic performance and fragile states with opportunities for selective and carefully sequenced increases in aid—and for key G/RPGs.
- Improving aid predictability through mechanisms that lengthen the time horizon of aid commitments and set clear rules for qualification and disbursement: the EC proposal on MDG Contracts points in the right direction.
- Ensuring coherence in aid delivery in the context of the changing aid architecture, using country PRSs as the core instrument to secure strategic alignment of funding from different sources—including vertical funds, new bilateral donors, and private foundations—with country development priorities and the principles of the Paris Declaration to harmonize aid delivery.

IV. Role of the World Bank

50. With its global development mandate, its services spanning financing, knowledge, and coordination, and its close engagement with both aid-recipients and donors, the Bank has a key role in supporting the scaling-up effort, based on a strong country development model. Its role encompasses three strategic priorities:

- helping countries build outcome-driven national development strategies and institutional capabilities to effectively absorb scaled-up aid;
- supporting a platform for improved aid coherence, predictability, and scaling up; and
- reinforcing strategic partnerships to address key capacity and financing issues.

³⁸ <http://www.dfid.gov.uk/news/files/pressreleases/ihp.asp>

Supporting Outcome-Driven National Development Strategies and Systems

51. Through its analytical, technical and financial contributions, the World Bank assists governments in examining country-specific issues to arrive at sequenced and prioritized national development strategies. The Bank supports governments in identifying macroeconomic and sectoral constraints to stronger, shared, private sector-led growth; assessing the macroeconomic and fiscal implications of development strategies and scaling-up scenarios; strengthening institutional capacity; and building systems for evidence-based decision making.

52. A clearly defined and prioritized strategy for stronger and shared growth forms the cornerstone of a country's scaling-up efforts. The Bank carries out significant analytical work to help countries strengthen their growth strategy and its impact on poverty reduction. Complementing its regular Country Economic Memoranda and Poverty Assessments, the Bank is implementing several initiatives to strengthen growth diagnostics. It has launched a Growth Commission to take stock of current knowledge on growth and draw out implications for policy makers.³⁹ Together with DFID, SIDA, SwissAid, GTZ, and AFD, it has established a Diagnostic Facility on Shared Growth that is supporting country-based analytical work and identifying good practice analytical tools and policy approaches. Pilot growth diagnostics have also been conducted for several countries.⁴⁰ Efforts are now being undertaken to mainstream innovative approaches for shared growth diagnostics into the Bank's regular analytical services. Through its Doing Business reports and Investment Climate Assessments/Enterprise Surveys, the Bank has also substantially strengthened its country diagnostic work on improving the private investment climate, a key driver of economic growth.⁴¹

53. The Bank, together with the Fund, assists countries in assessing the macroeconomic and fiscal implications of different scaling-up scenarios. In addition to examining such issues in public expenditure reviews and growth analytics, fiscal space studies apply a medium-term analytic framework to help countries assess the macroeconomic and fiscal implications of a growth-oriented fiscal policy in support of a bold national development strategy.⁴² As noted earlier, application of models, notably the Maquette for MDG Simulations (MAMS) developed at the Bank, also help countries to analyze alternative financing strategies and assess policy trade-offs. Since the first application of MAMS in 2005, the model has been used increasingly to develop and analyze scaling-up scenarios for stronger growth and MDG achievement (Table 1). While a stronger analytic framework has emerged to examine the macroeconomic and fiscal implications of scaling up, the challenge lies in extending these analytic tools to as many countries as possible.

54. Well-costed sector strategies linked to the PRS provide an important input for assessing the macroeconomic and fiscal implications of scaling up and for linking the PRS to the budget. The Bank is collaborating with partners, such as the UNDP, in helping countries to cost priority interventions. In Rwanda, for example, the use of both "high" and "low" costing scenarios has helped to illustrate the resources required to meet the MDGs and prioritize expenditures to achieve the best-possible outcomes with limited resources. The Bank is collecting and

³⁹ See <http://www.growthcommission.org>.

⁴⁰ See <http://www.worldbank.org/prem> for completed country growth diagnostic studies.

⁴¹ See World Bank.2006d; and <http://www.worldbank.org/privatesector/ic>.

⁴² See World Bank. 2007b.

disseminating good practice approaches for costing. Going forward, it must enhance incentives and resources available to staff to work with governments to prepare operationally focused sector diagnostics to strengthen costing, budget planning, and PRS implementation.

Table 1. MAMS Applications in Country Work

Country	Year	Issues Addressed	Product/Context
DRC	2007	Fiscal space and debt sustainability	Public Expenditure Review
Ethiopia	2005	MDG strategy	Government MDG Needs Assessment
	2005	Poverty reduction strategy	Input to/ review of PRS
	2006	Fiscal space, aid, trade-offs	Report: Review of Public Finance
	2007	Labor market, migration	Report on Urban Labor Markets
Ghana	2007	MDG strategy	Country Economic Memorandum
Honduras	2007	MDG strategy	Public Expenditure Review
Kenya	2007	Long-run growth; policy trade-offs	Country Economic Memorandum
Madagascar	2007	MDG strategy	Not yet determined
Malawi	2007	Government spending composition and trade-offs	Public Expenditure Review
Tanzania	2007	Government spending composition and trade-offs	Country Economic Memorandum
Uganda	2006	Growth	Country Economic Memorandum
	2007	Growth, alternative financing strategies, trade-offs	Public Expenditure Review
Venezuela	2007	Sustainable poverty reduction strategies	Poverty Assessment

Source: DEC Program on MAMS, The World Bank. This table does not cover MAMS applications in some Latin America countries under the joint World Bank-UNDP-UNDESA project “Assessing Development Strategies to Achieve the MDGs in Latin America.”

55. Recent Bank initiatives demonstrate a strong commitment to strengthening governance and institutional capacity across different country contexts, while working with a variety of development partners. Under its new Governance and Anti-Corruption (GAC) strategy, the Bank aims to work with governments to support the development of capable and accountable institutions, which will be better placed to effectively absorb increased aid.⁴³ The strengthened GAC strategy aims to integrate governance analysis into country assistance strategies (CASs), sector work, and lending operations. It also involves a significant training component on governance managed by the World Bank Institute. The Africa Region’s Capacity Development Action Plan, covering 43 Sub-Saharan countries including both good performers and fragile states, is supporting institutional capacity building for effective delivery of public services, as well as strengthened PFM.⁴⁴ Broad-based public sector reform and capacity building is an important focus of support also in other Bank Regions. For example, in the Western Balkan countries, Armenia, Georgia, Azerbaijan, and Moldova, the Bank is supporting the EU pre-accession process and the European Neighborhood Policy by providing support to strengthening state institutions, financial management, and economic standardization. The Bank is also increasingly supporting public sector capacity at local and regional levels, for example, through bottom-up participatory reforms such as community-driven development and assistance for decentralized service delivery.

56. Working closely with the Fund, the Bank is a global leader in assisting governments to strengthen public financial management systems, a key element in building capacity to effectively absorb scaled-up resources. Support for PFM spans diagnostic tools as well as technical and financial assistance for country-led PFM reform strategies.⁴⁵ The focus of the

⁴³ See World Bank. 2007d.

⁴⁴ See World Bank. 2006b.

⁴⁵ World Bank and IMF. 2003; and IMF. 2007b.

Bank's analytical support has broadened from public expenditure assessments to institutional reviews that analyze the quality of the PFM systems and processes. PFM lending represents the dominant part of the Bank's public sector management portfolio (which itself comprised 15.5 percent of the total Bank lending in FY2007). Together with the IMF and other donors, through the PEFA program, the Bank has supported the development and implementation of a comprehensive assessment framework to evaluate and monitor progress in PFM reforms.

57. Donor support to assist governments improve results assessment frameworks is increasing, but remains less coordinated than in the case of PFM. Priorities in this area include building capacity for monitoring and evaluation as well as statistical systems at the national, sub-national and sectoral levels. The Bank collaborates with governments to reinforce existing national monitoring institutions rather than develop parallel systems.⁴⁶ It has also introduced an innovative results tracking system under IDA14 (Box 3). Through the Africa Action Plan, the Bank and other donors are providing financial and technical assistance to PRS countries to develop and implement Monitoring and Evaluation Plans linked to national and sector strategies.⁴⁷ Support for building country statistical capacity is also growing, although important financing and capacity constraints remain, especially in the Africa region. Under the 2004 Marrakech Action Plan for Statistics, countries are receiving medium-term support for implementing national statistical strategies as well as short-term support to address critical data gaps.⁴⁸ Going forward, it will be important for the Bank and other donors to work closely with governments to ramp up support for these systems and to encourage better dissemination of results to expand domestic demand for evidence-based decision making and to support more effective public policy.

Box 3. Promoting a Results-Based Culture: IDA14 Results Measurement System

The Bank, through IDA 14, has introduced a Results Measurement System (RMS) to provide an overall assessment framework for IDA and its borrowers. The RMS has a two-tiered approach, with the first tier tracking trends in big picture outcomes relevant to IDA's overall development strategy and the second tier tracking IDA's contribution to development outcomes. To avoid attribution concerns, the second tier includes indicators of the quality of IDA programs as well as selected outputs of IDA projects in four key sectors. Early experience with implementation of the RMS is encouraging.⁴⁹ A more explicit results measurement system for Bank products has stimulated the use of baselines for investment lending, reinforced the institution's results culture, and strengthened support of and demand for statistics and monitoring indicators in borrowing countries.

58. The Bank's strengths in country diagnostics and development of PFM and other country systems are crucial in supporting development strategies, capacity, and accountability in fragile states. The Bank approaches peace-building and state-building as common goals across fragile states, but adopts differentiated assistance strategies, consistent with the Bank's mandate, that reflect the pace and direction of governance change. The Bank has fulfilled a critical role in several fragile recovery situations, such as Afghanistan, Democratic Republic of Congo, and Timor-Leste: leading analytical work on economic and governance issues; supporting government processes to develop budget priorities and build PFM systems; financing policy

⁴⁶ For good practice lessons on building national monitoring systems see: Bedi et al., 2006.

⁴⁷ World Bank. 2007a.

⁴⁸ For more information on the Bank's program to build capacity in countries, see: <http://www.mfdr.org/documents/MarrakechActionPlanforStatistics.pdf>

⁴⁹ See <http://www.mfdr.org/rt3/>

reform, infrastructure and basic service delivery; and supporting transparent public-private sector relationships.⁵⁰ The Bank is distilling best practice through staff guidance notes and a *Good Practice Note on Country Assistance Strategies in Fragile States*.

Improving the Quantity and Quality of Aid to Achieve Results

59. The World Bank is supporting the international community in meeting its commitments to provide more and more effective aid through two channels. First, the Bank is increasing the quantity and quality of its own development assistance. Second, through its coordinating and convening role, the Bank is actively supporting increased donor alignment and harmonization, with contributions ranging from co-chairing country aid coordination meetings and participating in collaborative assistance strategies to promoting sector-wide approaches and performing joint diagnostic work. This dual role is reflected both in the Bank's engagement at the country level and its support for global and regional public goods.

60. World Bank lending to IDA countries has increased significantly since 2000, especially to Africa where the Bank is the largest provider of development assistance. Total IDA commitments have increased from around \$4.4 billion in FY00 to almost \$12 billion in FY07, reaching their highest level ever. IDA commitments were particularly robust in the Africa Region in FY07, totaling a record \$5.8 billion, a full \$1 billion more than the previous year and more than three times the level of FY00. Revised in April 2007, the Bank's Africa Action Plan outlines the Bank's strategy in the region and provides an important means of mobilizing financing from other development partners.⁵¹ A large part of countries' financing requirements pertains to infrastructure development. Under its Infrastructure Action Plan, the Bank is increasing its support to countries and also helping them leverage more private investment.⁵² IDA is the largest multilateral source of aid financing for physical infrastructure. It is also a major source of external financing for low-income countries for social sectors, and is the largest source of financing for education. A full commitment from donors in the current IDA15 replenishment will be crucial to ensure the Bank's continued ability to scale up its support to the world's poorest countries.

61. Complementing scaled-up support from IDA, IFC and MIGA have stepped up their operations in low-income countries. IFC support for private sector development projects in Sub-Saharan Africa doubled in FY07 to \$1.4 billion. MIGA guarantees for projects in the region rose to \$311 million in FY07, up from \$131 million in the previous year.

62. The predictability of Bank support has continued to improve. Within-year predictability has improved, facilitated by a shift toward front-loaded budget disbursements and SWAs, which encourage the Bank and other donors to commit funds in advance of budget preparation. Short-term predictability has also improved since Bank conditionality has become more aligned with government policy frameworks. Moreover, increased use of programmatic approaches, both in lending (e.g., programmatic PRSCs) and in non-lending activities, is contributing to more

⁵⁰ IDA. 2007c. World Bank support for *common donor frameworks in fragile states*—such as the Governance and Economic Management Assistance Program in Liberia and the Afghanistan Reconstruction Trust Fund—has helped to harmonize donor approaches to PFM and public sector reforms and state capacity building.

⁵¹ See World Bank. 2007a.

⁵² See World Bank. 2005b.

predictable support to countries in the short to medium term. Under the IDA15 replenishment, the exceptional IDA allocation period for post-conflict countries will be extended from seven to ten years and for re-engagement countries from three to five years. While the Bank has traditionally been a leader with respect to multi-year projections, with three-year IDA tranches for most borrowers (longer term for post-conflict and re-engagement countries) and five-year CASs, several donors have recently moved to longer-term funding mechanisms, allowing them to offer increasingly predictable financing.

63. The Bank also plays a key role in efforts to improve aid alignment and harmonization. It aligns its CASs with partner countries' own development strategies. It prepares its CASs in consultation with partner governments and other stakeholders, and tailors its programs to country needs as defined in the national strategy. The Bank is fully committed to strengthening the country model and its indicators for the Paris targets are moving in the right direction. According to the 2006 OECD Survey on Monitoring the Paris Declaration, 42 percent of Bank development assistance was channeled through country financial management systems, while 57 percent of all Bank disbursements were for program-based approaches. Donor coordination in analytic work is also increasing: almost one-half of Bank's analytic work was prepared jointly with others, with joint fiduciary and PFM assessments among the most frequent.^{53 54} The Bank regularly monitors its performance on aid alignment and harmonization based on the Paris indicators and provides periodic reports to its Board. More broadly, the annual Global Monitoring Report assesses the Bank's (and other IFIs') contribution to the overall scaling-up effort and the MDG agenda.

64. In addition to aligning its own aid and thereby setting an example for other donors, the Bank performs a more direct role in coordinating donor activities and aligning them with the country model. The Bank's contributions vary by country and depend, among others, on the level of partner government engagement, the role that other donors are willing and able to play, and the level of coordination and alignment that already exists. Areas of Bank involvement include donor meetings, collaborative assistance strategies, coordinated budget support, and sector-wide approaches (Box 4).

65. The Bank's strengths at the country level allow it also to play a key role in addressing global and regional issues, such as climate change, communicable diseases, and global and regional trade integration. By leveraging its country-focused assistance and policy dialogue, the Bank helps to integrate global and regional priorities into country strategies. At the same time, through its involvement in global policy making, it helps promote consensus on approaches for tackling such global and regional issues. The Bank has had a long and major involvement in supporting global programs, playing multiple roles spanning convening, financing, implementation, acting as a catalyst, and serving as a trustee (e.g., for the Global Environment Facility, Global Fund to Fight AIDS, Tuberculosis, and Malaria, and EFA-FTI). Going forward, a particularly important challenge will be tackling climate change, which will require sizable and well-coordinated development assistance to countries. As part of its response, the Bank has developed a Clean Energy for Development Investment Framework.⁵⁵ The Bank has also stepped up its support to regional programs, which, for example, are an important area of emphasis in the

⁵³ OECD/DAC. 2007a. and IDA. 2007a.

⁵⁴ Nicaragua, Bolivia, and Haiti provide good examples of joint PFM/fiduciary diagnostic work, which was carried out with the Inter-American Development Bank and bilateral donors. See also: IDA. 2007a.

⁵⁵ See World Bank. 2007j.

Bank's Africa Action Plan. The Bank has developed four Regional Integration Assistance Strategies (RIASs)—for Central Africa, East Africa, Southern Africa, and West Africa—to set the strategic framework for Bank support for regional integration aligned with regional priorities. To underpin its increasing engagement in global and regional public goods, the Bank is developing a framework for its role in providing G/RPGs, including criteria for its involvement and financing modalities.⁵⁶

Box 4. Country Examples of Joint World Bank-Donor Coordination

Donor meetings. In *Bosnia-Herzegovina*, the World Bank co-chaired, with EC, five international donor meetings. The \$5.1 billion worth of funds that were mobilized through these meetings have been instrumental in the quick and successful reconstruction of the country's basic infrastructure and services.

Collaborative assistance strategies. In *Uganda*, the Bank initiated the development of the Uganda Joint Assistance Strategy 2005-09 (UJAS). Originally subscribed to by a group of seven development partners, UJAS currently guides the activities of 10 members including AfDB, Germany, Netherlands, Norway, Sweden, UK, Austria, EU, Ireland, and World Bank. The UJAS partners have increasingly aligned their support to the government development program, and reduced transaction costs for the Government by eliminating the need for discussing and reviewing separate donor strategies. Going forward, this expanding group of donors will rely on the Government's annual assessment of the results of the PRS to judge its own development effectiveness, rather than having each development partner undertake separate monitoring exercises.

Coordinated budget support and common performance assessment frameworks. In *Nicaragua*, since the initiation of the Budget Support Group (BSG) in 2004, the Bank has been working with the donor community to better coordinate and harmonize budget support instruments. With support from the Bank, the BSG developed a comprehensive performance assessment matrix in 2005, which for the first time put performance expectations from various donors into a common format. The BSG meets regularly to review progress.

Sector-wide approaches. *Ghana's* health SWAp, which evolved since the mid-1990s, is considered to be one of the most advanced arrangements of aligned delivery of external partners' assistance at the sectoral level. It led to a much more coordinated approach by (a) moving from a large number of individual, typically external partner-initiated and extra-budgetary projects toward a single sector strategy and expenditure program; and (b) strengthening and using domestic systems and procedures for planning, budgeting, procurement, auditing, and evaluation. The development of the SWAp was country driven, with the essential support of a core group of donors, including the World Bank.

Strengthening Collaboration with Partner Agencies

66. **IMF.** A strong partnership between the Bank and the Fund is an essential component of a successful scaling-up framework and will be further strengthened in the follow-up to the "Malan Report". Joint Bank-Fund analyses of public financial management and debt sustainability issues have been among the most successful areas of collaboration.⁵⁷ Moving forward, more collaboration will be required in examining the macroeconomic and fiscal implications of scaled-up aid flows. The IMF's medium-term strategy calls for a deeper involvement of the Fund in assessing the relationship between aid inflows, MDG-related resource needs, and macroeconomic stability.⁵⁸ To complement this, the Bank will need to step up collaboration with partner countries to cost PRSs and to develop sector strategies with clear expenditure and outcome priorities. The Fund will need to work closely with the Bank and partner countries in assessing the impact of alternative resource flows on macroeconomic stability and targeted

⁵⁶ See World Bank. 2007c.

⁵⁷ World Bank and IMF. 2007b and 2007c.

⁵⁸ IMF. 2007a.

expenditure outcomes. Both institutions will need to work together to help countries develop an appropriate longer-term fiscal policy and expenditure frameworks to anchor a stable and increased spending path. Finally, Bank-Fund reviews of annual reports on PRS implementation will be streamlined to strengthen country ownership, donor coherence (joint donor feedback on the PRS will be facilitated), and operational linkages between the PRS and the budget process.

67. **OECD/DAC.** The Bank and OECD/DAC's complementary roles in the scaling-up agenda build on their respective institutional strengths. DAC hosts four joint-ventures—Managing for Development Results, Monitoring the Paris Declaration, Public Financial Management, and Procurement—which have been instrumental in building a repertoire of good practice in these areas and reinforcing donors' commitment to country-based development and aid effectiveness.⁵⁹ The DAC Network on Governance and the Fragile States Group and its recent *Principles for Good International Engagement in Fragile States and Situations*⁶⁰ have strengthened the principles underpinning the Bank's work in fragile states. In addition, DAC is working with countries and donors to track current and projected aid and to better assess progress in delivering on international commitments. Together with other donors, the Bank contributes to the analytical foundations of this work and is also a key partner in coordinating its implementation at the country level. Future priorities for Bank-OECD/DAC collaboration include efforts to promote short- and long-term predictability of aid flows and to build a body of good practice in national monitoring and evaluation systems. The OECD/DAC and the Bank will also explore options to collaborate with vertical funds, emerging donors, and private foundations to help better integrate these aid flows into the country-based model.

68. **UN.** The World Bank has been collaborating with the UN on the scaling-up agenda and in developing a coordinated approach to support in fragile states. A joint World Bank-UNDP paper on scaling up and the country-based development model presented before an OECD/DAC-World Bank meeting in June 2006 highlighted the urgency of scaling up in good performing African countries.⁶¹ The Bank is a member of the high-level MDG Africa Steering Group recently established by the UN Secretary General with the aim to support the implementation of commitments toward achieving the MDGs. The Bank's differentiated approach to fragile states recognizes the importance of partnership with the UN: the Bank tends to play a larger role in situations where states are transitioning or gradually reforming; while in prolonged crises or deteriorating situations the UN system often makes critical contributions on political and security issues. A forthcoming World Bank-UN partnership note to support joint work in crises and emergencies will provide a common platform for needs assessments and recovery planning, and outline common principles for collaboration in multi-donor trust funds. In consultation with other partners, the Bank and the UN are also updating their results-based planning framework to clarify linkages with other actors and strengthen the focus on peace-building and state-building in fragile states.⁶²

⁵⁹ The Bank chairs the joint ventures on financial management and procurement, has chaired the results group, and is vice-chair of the overall Working Party on Aid-Effectiveness, which is the parent body of the various joint ventures and is the body charged by the Paris Declaration to promote aid effectiveness.

⁶⁰ OECD/DAC. 2007c.

⁶¹ World Bank and UNDP. 2006.

⁶² IDA. 2007c.

69. **EU.** The Bank-EU partnership focuses on “business unusual” and “value added,” with particular attention to division of labor, coordination of program aid, aid predictability, and issues related to vertical funds, emerging donors, and new trust funds.⁶³ There has been significant progress in harmonizing and aligning support around PRSs since the Limelette Process was introduced in 2003.⁶⁴ The process seeks complementarity between the Africa Action Plan and EU’s Strategy for Africa. The two institutions are seeking to develop a framework for aid effectiveness as an input to the Accra High-Level Forum on Aid Effectiveness in 2008. The EU has recently developed a “Code of Conduct” on division of labor in development policy and the Bank is exploring collaborative efforts to pilot this code in several African countries.⁶⁵

70. **MDBs.** Collaboration between the regional multilateral development banks (MDBs) and the World Bank has grown in recent years. This partnership was a driving force behind the Paris High-Level Forum on Aid Effectiveness. The MDBs have developed a common performance assessment system (COMPAS) to monitor their results orientation in terms of improvement of internal processes, support to in-country capacity building for managing for results, and inter-agency cooperation for results. In March 2007, the MDB heads set up a working group, with IMF participation, with the mandate to identify opportunities for increased collaboration and improved effectiveness in fragile states and situations. Initial efforts of the working group have focused on harmonization of implementation arrangements, results monitoring, and issues around the definition of fragility. The Bank is also collaborating closely with the AfDB in the implementation of the Africa Action Plan.

71. **Bilateral Donors.** Partnerships with bilateral donors—both within countries around joint assistance initiatives and coordination mechanisms and at an agency level on cross-cutting thematic issues—are providing important impetus to the scaling-up agenda. Most recently, the Bank has been collaborating with the Swedish and Dutch Ministries for Foreign Affairs and DfID, along with the EU, UNDP and OECD/DAC, to promote the Results, Resources, and Partnership (RRP) process in countries for scaling up and aid effectiveness.⁶⁶ The RRP process has gained attention as a means of encouraging countries to articulate more results-oriented development strategies underpinned by accurate cost and resource estimates, around which donors can align and increase development finance. The RRP process will also support country-to-country learning through dissemination of good practice approaches for country-based scaling up. Together with the other RRP partners, the Bank is initially planning to provide country-specific support to Ghana, Madagascar, and Tanzania to strengthen core systems and results and resources frameworks. The Bank’s Africa Action Plan aims to support the RRP process in ten countries in the region.

72. **Vertical Funds, New Bilateral Donors, and Private Foundations.** The Bank is strengthening partnerships with vertical funds, newly emerging non-DAC donors, and private foundations at the agency and country level to encourage the integration of these assistance programs with country priorities and systems. The Bank’s new Strategy for Health, Nutrition, and Population Results recognizes the growing importance of vertical funds in the health sector

⁶³ World Bank-EC Consultation Meeting on Limelette – Details of Discussions, April 27, 2007.

⁶⁴ The annual topics of Limelette have included PRSPs (2003), budget support and public finance management (2004), and infrastructure, public finance management, and trade and regional integration (2005).

⁶⁵ See World Bank. 2007a.

⁶⁶ See, for example, OECD/DAC. 2006.

and calls for complementary approaches to ensure sector-wide benefits.⁶⁷ Over the past year, the Bank has established a working partnership with the Export-Import Bank of China. This has included a series of workshops, seminars, and training events on fiduciary and financial management, procurement, environmental safeguard analysis, and social impact analysis. In May 2007, the two organizations signed a Memorandum of Understanding aimed at building collaboration for development, with a particular focus on Africa. In cooperation with partner countries, the Bank is working to broaden participation in aid coordination meetings to include new donors. These initiatives represent an important starting point in a process to strengthen relations between DAC and non-DAC donors, based on mutual priorities and potential complementarities. The Bank is also disseminating the joint Bank-Fund Debt Sustainability Framework as a tool to ensure that financing from all sources is consistent with the recipient's debt sustainability.

World Bank Priorities to Support Scaling Up

73. The country-based development model provides the overarching framework for supporting and implementing scaled-up strategies to meet the MDGs. To strengthen the country model, countries and donors need to stay committed to a long-haul process, addressing the gaps that remain at the right pace. For countries, this means strengthening their PRSs, their results and resources frameworks, and the domestic systems that underpin them. For donors, this means a coordinated and harmonized approach to using and supporting the elements of the model that are already in place, and assisting countries to fill the technical and financing gaps that exist. Both countries and donors need to invest in mutual accountability mechanisms to monitor aid flows and utilization as well as to assess country and donor performance against prior commitments.

74. For its part, the Bank can contribute by supporting the strengthening of country strategies and systems; promoting alignment, harmonization, and coherence in aid, using its coordinating, convening, and catalytic role; and increasing the quantity and quality of its own development assistance. This requires alignment of the Bank's internal resources and incentives with the priorities in the scaling-up agenda, as outlined below; deepening of partnerships with other donors; and an IDA funded with a critical mass of resources to play its key role in the effective scaling up of aid.

75. The Bank has a major role to play in assisting countries by providing diagnostics to underpin country strategies and technical and financial support for institutional strengthening, especially bolstering key country systems. Priorities include:

- Enhancing capacity for macroeconomic and fiscal analysis of alternative scaling-up scenarios, in collaboration with the Fund.
- Strengthening diagnostics for stronger, shared growth and sector strategies; and expanding the capacity of Bank staff to assess sectoral policy frameworks, including expenditure and institutional issues, to better support sector-wide lending as well as the integration of vertical funds into these arrangements.

⁶⁷ See World Bank. 2007g.

- Scaling up work on governance and anti-corruption at the project, country, and global levels—by providing diagnostic, technical, and financial support to build transparent and effective institutions.
- Pursuing improvements in public financial management through continued support to PEFA and expanded efforts to provide multi-year assistance to country-led reforms.
- Strengthening capacity for managing for results in partner countries by improving national results frameworks, in particular ramping up support for monitoring and evaluation institutions and enhancing statistical capacity.

76. The Bank's global reach, strong cross-sectoral presence in most developing countries, and substantial convening power vest it with a key role in promoting donors' commitment to scaling up around the country-based model. The Bank's role in this agenda incorporates both "traditional" bilateral and multilateral donors as well as non-DAC donors, vertical funds, and private foundations. Priorities include:

- Forging ahead with the RRP process to support countries in developing stronger results, resources, and mutual accountability frameworks for implementing ambitious national development strategies and demonstrating successful examples of scaled-up aid. The ability of the RRP process to contribute to progress in scaling up will depend on countries' ownership of and donors' commitment to this process for stronger, more upstream engagement.
- Supporting a global partnership for improved country-level monitoring and evaluation systems to enable evidence-based decision making in an environment of scaled-up aid.
- Building relations with donors, including vertical funds, non-DAC donors, and private foundations, to help ensure that efforts to address global and regional issues are fully integrated into the country-based development model; and promoting consensus on approaches for tackling global and regional issues.
- Promoting cooperative approaches, using the joint Bank-Fund Debt Sustainability Framework as a key tool, to ensure that financing from all sources is consistent with the country's debt sustainability.

77. IDA provides a crucial vehicle for delivering aid and promoting aid effectiveness. It is vital that IDA continues to play its key role in supporting country-based development. With this goal in mind, it will be important to ensure a strong IDA15 replenishment, one that fulfills donors' pledges, and meets countries' expectations, for scaled-up assistance.

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**COUNTRY-BASED SCALING UP:
ASSESSMENT OF PROGRESS AND AGENDA FOR ACTION**

ANNEXES

ANNEX I

STRENGTHENING THE PRS FRAMEWORK

1. Country based development rests on the effective implementation of domestically-driven, comprehensive and results-oriented development strategies. Domestic ownership of a unified strategy, the prioritization and sequencing of interventions, close links between planning and budgeting institutions, and effective monitoring and evaluation (M&E) mechanisms represent mutually reinforcing elements of the country based development model. This annex assesses low income countries' progress and the World Bank's supportive role in each of these areas.

2. Country based development is particularly important in the light of changes to the international aid architecture and prospective scaling up. A strong country based development model can provide a platform upon which an increasingly complex set of aid modalities (as described in Annex IV) can be integrated to the benefit of recipient countries. Domestic ownership of development priorities will ensure that scaled up aid reinforces, rather than weakens, the pursuit of countries' development goals. Strong links between national development strategies and the budget can promote a virtuous cycle as increasing levels of aid are channeled through domestic systems. And good monitoring and evaluation systems will enable evidence-based decision-making and effective implementation of scaled up programs.

PRSs: Overview of Progress

3. Since their inception in 1999, Poverty Reduction Strategies have become increasingly important for country based development. As of July 2007, 62 countries were implementing PRSs or interim PRSs: 32 countries had a first PRS,⁶⁸ 22 were implementing their second PRSs⁶⁹ and 8 countries had either an interim PRS or a transitional results matrix. The quality and operational effectiveness of the PRSs have improved, especially in the second-generation PRS (PRS-II) countries. Of the 21 fragile states that have instituted PRS mechanisms, four have a PRS II, ten have PRS I, and seven have either an Interim PRS or a Transitional Results Matrix.⁷⁰

4. The quality of poverty reduction strategies and their implementation frameworks has improved over the last few years, with the second generation PRS countries making the most progress. The Paris Declaration assesses the quality of PRSs according to two broad measures: Indicator 1 measures the extent to which countries have operational development strategies; and Indicator 11 gauges the strength of results-oriented frameworks.⁷¹ As demonstrated in Figure 1,

⁶⁸ PRS I countries include: Albania, Armenia, Azerbaijan, Bangladesh, Bhutan, Cameroon, Cape Verde, Dominica, Georgia, Guyana, Honduras, Kenya, Kyrgyz Rep., Lesotho, Mali, Moldova, Mongolia, Nepal, Niger, Pakistan, Serbia, Sri Lanka plus 10 fragile states. Grenada, a non-fragile state which has an interim PRS, is not included in the ensuing analysis.

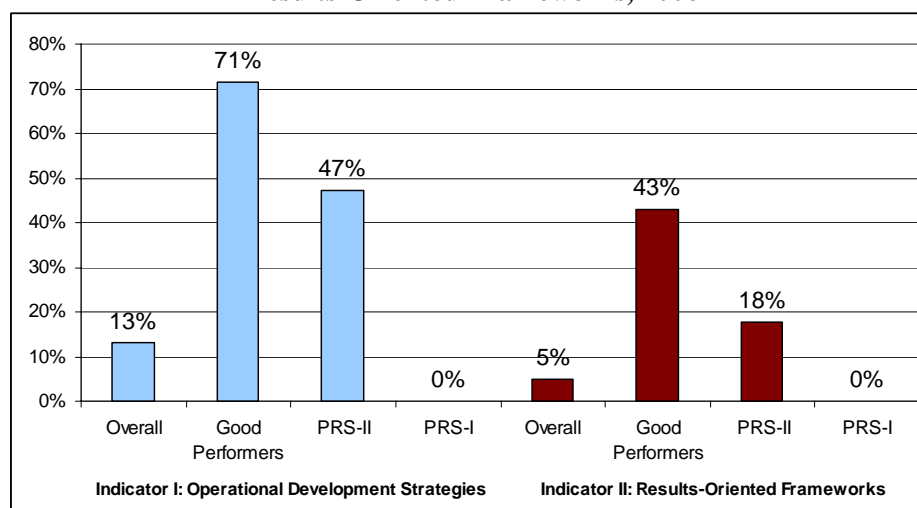
⁶⁹ PRS II countries include: Benin, Bolivia, Bosnia and Herzegovina, Burkina Faso, Ethiopia, Ghana, Madagascar, Malawi, Mauritania, Mozambique, Nicaragua, Rwanda, Senegal, Tanzania, Uganda, Vietnam, Yemen and Zambia plus 4 fragile states.

⁷⁰ Among the group of fragile states, 4 (Cambodia, Lao PDR, Tajikistan, The Gambia) have a PRS II, 10 (Burundi, Chad, Congo DR, Djibouti, Guinea, Guinea-Bissau, Nigeria, Sao Tome and Principe, Sierra Leone, Timor-Leste) have a PRS I, 5 (Afghanistan, Congo, Republic of, Cote d'Ivoire, Haiti, Liberia) have an interim PRS, and 2 (Central African Republic and Sudan) have Transitional Results Matrices.

⁷¹ Indicator 1, "operational development strategies" tracks the number of countries with national development strategies (including PRSs) that have clear strategic priorities linked to a medium-term expenditure framework and

almost half the PRS II countries have largely developed operational development strategies and almost one-fifth have met the more challenging goal of having a largely developed, results-oriented framework. Among a subset of 7 African “good performing” countries⁷², the picture is even rosier: Burkina Faso, Ghana, Tanzania, Rwanda and Uganda have largely developed operational development strategies; Mozambique, Tanzania and Uganda have met these standards for results-orientation.

Figure 1. Percentage of Countries with Largely Developed Operational Development Strategies and Results-Oriented Frameworks, 2006



Source: World Bank. 2007. *Results-Based National Development Strategies: Assessment and Challenges Ahead*. Draft, September 7.

Note: PRS II countries do not include fragile states with a second PRS. See Table 1 and footnote 72 for a list of the good performers.

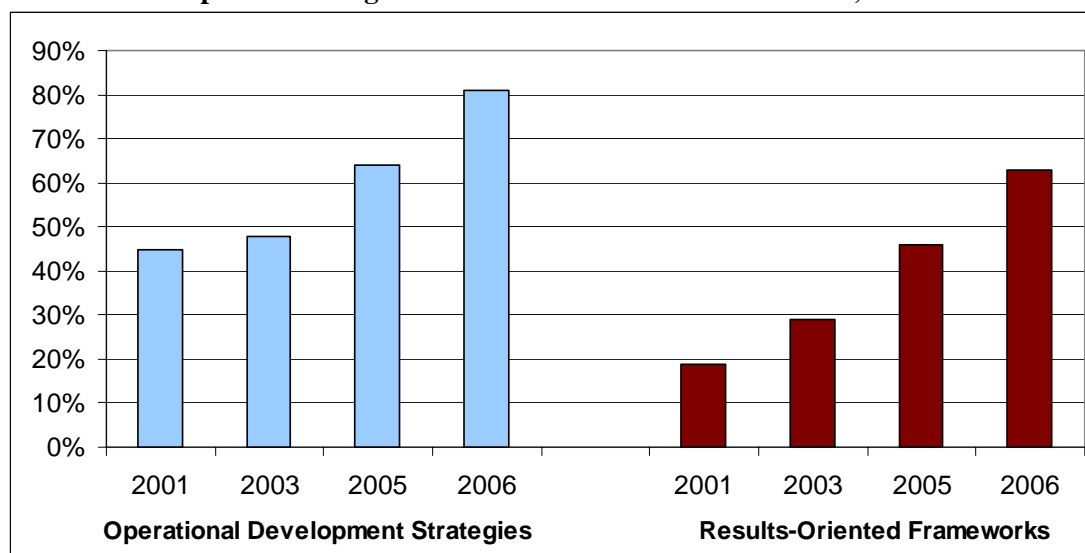
5. Although many of the PRS II countries and all PRS I countries still fall short of the Paris targets, a growing number of countries have implemented improvements in the quality of their PRSs. As indicated by Figure 2, the percentage of countries which either have largely developed operational development strategies and results-oriented frameworks or made progress toward realizing these goals has increased steadily since 2001. Moreover, as noted in a forthcoming

reflected in annual budgets. While indicator 11, “Results-oriented frameworks,” measures the number of countries with transparent and monitorable performance assessment frameworks to assess progress against (a) the national development strategies and (b) sector programs. See World Bank. 2007. *Results-Based National Development Strategies: Assessment and Challenges Ahead*. Draft, September 7.

⁷² A joint World Bank-UNDP 2006 paper (*Using the Country-Based Development Model to Scale Up for Results: An Agenda for Action*, Contribution to the OECD/DAC-World Bank Third Meeting on Scaling Up for Results (DCD/RD(2006)2/RD2, June 27) proposed that scaling up should initially focus on “a few good performers... where country demand is likely, performance is solid, poverty reduction strategies and implementation modalities are relatively strong, and donor alignment and harmonization is better developed.” It identified Burkina Faso, Ghana, Mozambique, Rwanda and Tanzania according to these criteria. To this group of five we have added Madagascar and Uganda. These countries emerge as good practice PRS countries in a number of reviews: World Bank and IMF. 2005. *2005 PRS Review – Balancing Accountabilities and Scaling Up Results*; Wilhelm, Vera and Phillip Krause. 2007. *Minding the Gaps – Integrating Poverty Reduction Strategies and Budgets for Domestic Accountability*. Conference Version, Washington DC: The World Bank; and Bedi, Tara, Aline Coudouel, Marcus Cox, Markus Goldstein, and Nigel Thornton. 2006. *Beyond the Numbers: Understanding the Institutions for Monitoring Poverty Reduction Strategies*. Washington DC: The World Bank. Uganda meets the Paris targets across all criteria employed in this paper (see Table 1).

World Bank review, the 21 countries classified as fragile states have made almost as much progress as other countries toward forging operational development strategies and results-oriented frameworks, albeit starting from a much lower base.⁷³ For example, Cambodia has integrated long- and medium-term goals and targets into its national development strategy and assessed the challenges ahead for meeting the MDGs. And Guinea has begun to integrate sector and local government strategies into a unified strategic framework.

Figure 2. Countries that have made Substantial Progress toward Building Operational Development Strategies and Results-Oriented Frameworks, 2001-2006



Sources: World Bank. 2001. *Comprehensive Development Framework – Meeting the Promise? Early Experiences and Emerging Issues*; World Bank. 2003. *Getting Serious About Meeting the Millennium Development Goals: A CDF Progress Report*; World Bank. 2005. *Enabling Country Capacity To Achieve Results: CDF Progress Report 2005, Vol. I*; and World Bank. 2007. *Results-Based National Development Strategies: Assessment and Challenges Ahead*. Draft, September 7.

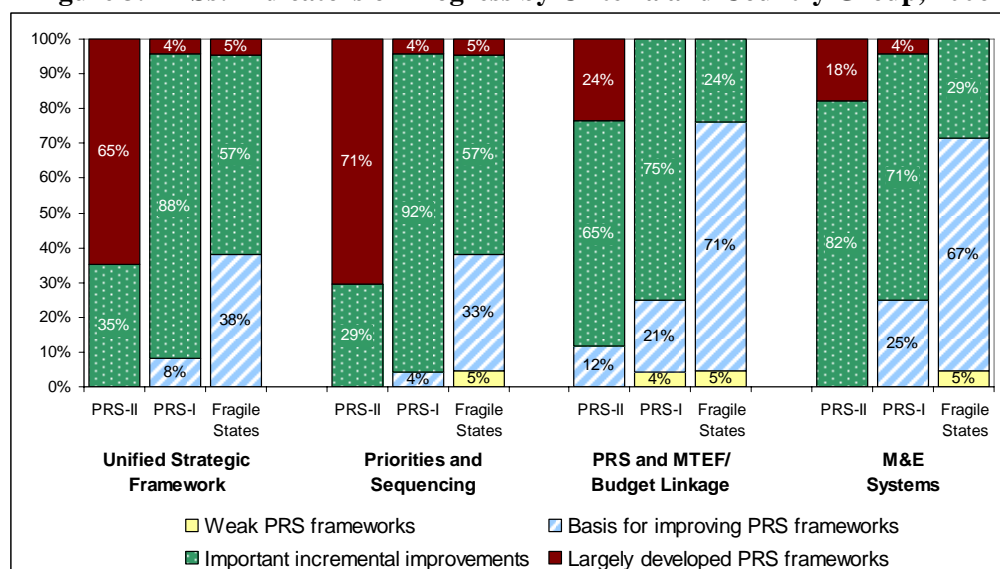
Note: Figure depicts percentage of countries that scored an A “action taken” or D “largely developed” for these indicators in any given year.

6. Country performance across four specific measures of PRS quality – unified strategic framework, prioritization and sequencing, PRS-budget links, and monitoring and evaluation – reveals both important progress and serious challenges. Within indicators 1 and 11, the forthcoming World Bank review assesses countries according to a number of sub-indicators, including: the extent to which countries have unified development strategies tying together a long-term vision, medium-term strategy, sector programs and local plans; the level of prioritization within these strategies; the strength of links between the PRS and the budget and MTEF; and the existence of country-level monitoring and evaluation systems. Consistent with the broad indicators on PRS performance, PRS II countries have made more progress in these four areas than PRS I countries. Figure 3 demonstrates that PRS II countries have reached good standards in terms of forging unified and well-prioritized strategies, while the vast majority of PRS I countries have also demonstrated incremental improvements. The strengthening of key domestic institutions – whether public financial management or monitoring and evaluation

⁷³ World Bank. 2007. *Results-Based National Development Strategies: Assessment and Challenges Ahead*. Draft, September 7.

systems – remains a deeper challenge.⁷⁴ Among the seven good performers, almost all have a prioritized and united strategic framework, but only Tanzania and Uganda are considered to have systems substantially in place to strengthen the link between their PRS and the budget and enable effective monitoring and evaluation (Table 1).

Figure 3. PRSs: Indicators of Progress by Criteria and Country Group, 2006



Source: World Bank. 2007. *Results-Based National Development Strategies: Assessment and Challenges Ahead*. Draft, September 7.

Table 1. Indicators of Progress in Seven Countries, 2006

	Unified strategic framework	Prioritization	Strategic link to the budget	M&E systems
Burkina Faso				
Ghana				
Madagascar				
Mozambique				
Rwanda				
Tanzania				
Uganda				

 Largely developed

 Action taken

Source: World Bank. 2007. *Results-Based National Development Strategies: Assessment and Challenges Ahead*. Draft, September 7.

⁷⁴ World Bank. 2007. *Idem*.

Domestic Ownership of the PRS

7. Country ownership of national development strategies has increased significantly. Ownership – a broad and complex notion – can be characterized as the extent to which the PRS builds on the needs and priorities of an individual country and the degree to which these priorities receive buy-in from the various levels of government and civil society. Although ownership is difficult to measure, the extent to which the PRS represents a unified development strategy can be an important indicator: if the PRS is just one of many medium-term development strategies, ownership tends to be low; conversely, where the PRS represents *the* medium-term development strategy for policy makers and other key stakeholders, ownership tends to be high. Using the extent to which countries have a unified development strategy as an indicator, Figure 3 points to a high level of ownership, especially among PRS II countries.

8. The majority of PRS II countries have managed the difficult task of fully integrating the medium-term strategy, sector strategies and the long-term vision and have made headway in aligning local planning with national strategic planning. As countries have transitioned from first to second PRSs, they have typically paid more attention to the integration of sector strategies into the PRS, thereby creating a more comprehensive and operational framework. Some have also broadened the sectoral composition to encompass growth-generating sectors – such as infrastructure and private sector development – in addition to the social sectors, which were the primary focus of most first generation PRSs. For instance, sector strategies in transport and rural development fed into Madagascar’s MAP. Ghana’s GPRS II was based on sector strategies for private sector development, finance, power, food and agriculture, and trade, among others. Experience in the better performing PRS II countries shows that linking the long-term vision with a medium-term strategy can be facilitated by strong leadership from the President’s office or institutional changes, such as a merging the Ministry of Finance with the ministry responsible for planning.

Prioritization and Sequencing

9. PRS II countries have also demonstrated the most progress in setting clear, sequenced and balanced priorities. While the vast majority (92 percent) of PRS I countries have established a basis for prioritization and sequencing, more than two-thirds (71 percent) of the PRS II countries now have a well-sequenced and prioritized strategy largely in place (Figure 3). MKUKUTA in Tanzania adopts an outcome-based approach to help implementing agents (whether the government, private sector, or regional authorities) to further prioritize and sequence the allocated resources within each sector. The outcome-based approach has also enabled a mainstreaming of cross-cutting priorities such as disability, employment and the environment. Burkina Faso’s CSLP II was also fine-tuned to place greater emphasis on cross-cutting issues like gender, regional integration, and small business development. Transitioning from a first to a second generation PRSP, Madagascar reduced the number of major programs in its MAP from 15 to 8 and introduced 13 major goals to be reached by 2012. Annual performance

agreements with precise targets were presented in 2005 and 2006, and each of the 23 sector ministries was attributed to the strategic axis of the PRSP.⁷⁵

10. The domestic political economy can present obstacles to prioritization and sequencing. The domestic political economy impacts prioritization since countries face internal tensions between a desire to reach ambitious objectives and mobilize additional resources, on one hand, and the need to demonstrate results and work within prevailing fiscal constraints, on the other. While some second generations PRSs have prompted a more targeted results focus, in other cases the PRS framework remains very broad in scope. In Ethiopia, for example, the recently completed PASDEP (PRS II) is built around eight pillars, but contains about 500 indicators. Donor feedback suggests that the matrix be streamlined to a reduced and manageable set of indicators – 5 to 10 indicators per pillar – with further details provided by sectoral M&E systems.⁷⁶

11. Prioritization also remains hampered by inadequate analytical work: many PRSs are based on predominantly qualitative analysis, rather than strong empirical methods. Some of the most pertinent elements of growth diagnostics – such as identification of the binding constraints to growth, analysis of the distributional impact of growth, or discussion of the macroeconomic implications of increased aid – were often found to be weak in a recent review of PRSs.⁷⁷ Accurate costing estimates are likewise hindered by country-level technical and capacity constraints.

Strengthening PRS-Budget Links

12. Some countries have made impressive progress in improving public financial management and strengthening the links between the PRS and budget. As demonstrated in Figure 3, less than a quarter of PRS II countries – specifically, Rwanda, Tanzania, Uganda and Zambia – have largely developed linkages between the PRS and key domestic systems including the budget and MTEF. Achievements in these countries reinforce the findings of recent research⁷⁸: namely, that the most successful reforms build on existing domestic processes and are driven by a high level of government ownership (see Box 1). As indicated in Annex III, the process of linking PRSs with budgets begins with getting the basics of public financial management right.

13. The formation of strong links between the budget and PRS represents an institutionally demanding objective. The shortcomings captured in Figure 3 are in part due to weaknesses in the budget itself, particularly in the areas of execution and reporting⁷⁹. Systems for tracking poverty reducing expenditures and assessing the potential leakage of funds are likewise weak in many countries. While MTEFs are indeed important instruments for linking the budget and PRS, their

⁷⁵ Complexity remains high at the budget level where 146 programs are linked to more than 4500 indicators. See Wilhelm, Vera and Phillip Krause. 2007. *Idem*. Madagascar study background paper.

⁷⁶ World Bank and IMF. 2007. *Ethiopia Joint Staff Advisory Note*.

⁷⁷ These findings emerged from a review of seven recent PRSPs (Benin, Burkina Faso, Ghana, Madagascar, Mozambique, Tanzania and Uganda) conducted in PRMPR to research the quality of growth analytics in PRSPs.

⁷⁸ Wilhelm, Vera and Phillip Krause. 2007. *Idem*.

⁷⁹ IMF. 2007. *Fiscal Policy Responses to Scaled-Up Aid—Strengthening Public Financial Management* (SM/07/199 Supplement 2, June 7).

effective implementation rests on high domestic ownership and strong institutional links between ministries of finance and planning – conditions which are rarely entirely fulfilled in PRS countries.⁸⁰ And, as indicated in Annex IV, the poor predictability of aid often adds to the challenge of forging reliable budgets and MTEFs.

Box 1. Linking PRS to the MTEF and Budget

In *Uganda*, the PRS now guides the development of sector strategies and strategic resource allocation in the MTEF and budget, while sector strategies direct the more detailed sector level MTEF and budget allocations. Compatibility between the PRS and the budget is further facilitated by the improved results-orientation of the latter. The inclusion of input, output, outcome, and impact indicators in the PRS and, more generally, the effort to track the entire results chain are important elements that help strengthen the link between the budget and outcomes.

In *Tanzania*, MKUKUTA has increasingly focused on the national budget process as the primary means of reaching PRS objectives. The medium-term expenditure framework and public expenditure reviews are key instruments ensuring consistency of MKUKUTA priorities and budget allocations. A strategic budget allocation system (SBAS) is used to create an instrumental link between MTEF allocations and the development strategy. The MTEF seeks full integration of external resources into the government budget and exchequer system. The execution of the budget in line with expenditure plans is reported by Government and reviewed by development partners and domestic stakeholders in the annual PER process.

In *Rwanda*, the MTEF for 2005-2007, which is also submitted to parliament, is considered a key instrument for translating EDPRS priorities into annual budget allocations to achieve required outputs. EDPRS priorities inform line agency strategies and sector strategic plans (consisting of strategic issues papers and sector MTEFs) as well as district development plans. Sectoral MTEFs are supposed to serve as the basis for ministerial and unit level work plans, which are implemented and monitored as part of Annual Action Plans that individual ministers sign and are held accountable for by the President. These reports in turn feed into budget execution reports, joint sector review, PERs and, ultimately, the EDPRS progress report.

Sources: Wilhelm, Vera and Phillip Krause. 2007. *Idem*; Interviews with country staff; Republic of Rwanda. 2007. *Economic Development and Poverty Reduction Strategy*. Draft.

Improving Monitoring and Evaluation for Better Results

14. Strong institutions for monitoring and tracking results as well as measures for impact evaluation are essential for efficient public spending and generating additional aid flows. While most country-based monitoring and evaluation systems are in their infancy, a foundation for tracking PRS implementation and its impact on poverty is being built in some countries. Among the “good performing” African countries, Mozambique, Tanzania and Uganda have taken actions to put in place sound M&E systems. These countries demonstrate that demand for evidence-based decision-making and strong political leadership are crucial for making progress. Uganda’s PRS monitoring system is a product of domestic pressure for evidence-based policy making and incorporates a number of monitoring agencies and procedures which were in existence prior to the PRS. In Mozambique, an annual *Balanço do Plano Económico e Social* tracks PARPA II implementation and progress toward meeting the MDGs, while sectoral indicators have been integrated through the PARPA II Strategic Matrix.

15. The dissemination of information among key stakeholders can feed into development planning and generate demand for better M&E systems. Dissemination of M&E relies in part on

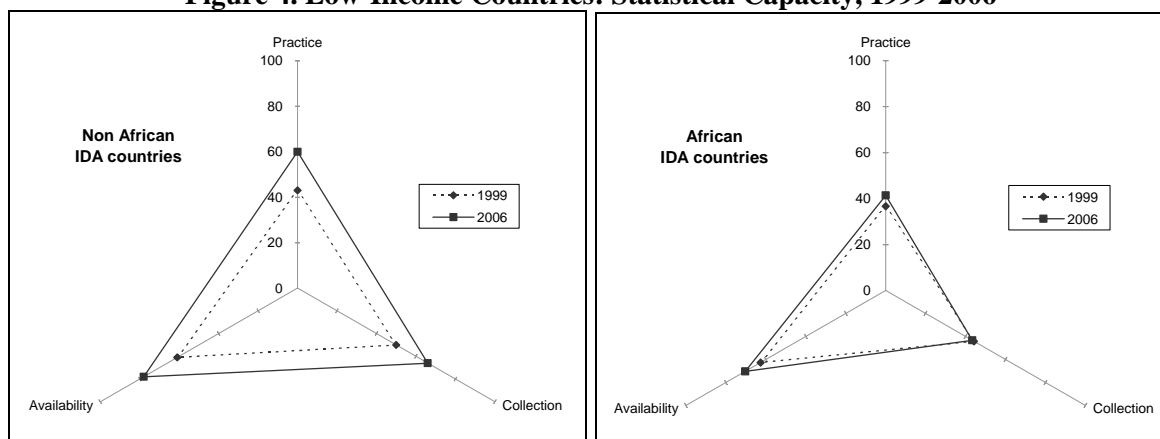
⁸⁰ Wilhelm, Vera and Phillip Krause. 2007. *Idem*.

the interest and will of the political leadership. In Burkina Faso, the *Secrétariat Technique pour la Coordination des Programmes de Développement Economique et Social*, housed within the Ministry of Finance, consolidates the results from regional and sectoral M&E in annual reports which are then transmitted to inter-ministerial committees and parliament. Dissemination among policymakers can create a virtuous cycle, whereby development information feeds into policymaking and generates further demands for data and analysis, creating incentives for improved monitoring and evaluation.

16. Deep challenges to developing adequate country-level monitoring and evaluation systems remain. As demonstrated in Figure 3, very few PRS I countries are approaching the Paris targets for M&E systems and even among PRS II countries the vast majority lack largely developed systems. Measuring statistical capacity according to three key aspects – statistical practice, data collection, and indicator availability – Figure 4 indicates that African IDA countries continue to lag behind non-African IDA countries. While the virtuous cycle described above is possible, the all too common counterpoint is a vicious cycle: bad quality data and/or analysis fail to generate demand for information, while a lack of demand weakens incentives to improve the quality of data and analysis. A number of problems contribute to this vicious cycle, including:

- A lack of operational detail, costing, and prioritization in many PRSs, making it difficult to select meaningful indicators for monitoring PRS implementation.
- Inadequate statistical capacity and weaknesses in routine administrative data and public expenditure management systems, making it difficult to track PRS expenditures.
- Difficulties in the coordination of activities; territoriality among public sector agencies, combined with a lack of incentives to participate, leading to resistance to rationalization and coordination and hampering the translation of formal plans into practice.

Figure 4. Low-Income Countries: Statistical Capacity, 1999-2006



Source: World Bank, Development Data Group (<http://www.worldbank.org/data/countrydata/csid.html>)

The World Bank's Contribution to Strengthening the PRS Framework

17. The World Bank is committed to strengthening country based development through the PRS. The Bank has engaged in two major reviews of the PRS process (2002 and 2005) since it was introduced in the late 1990s. These reviews have noted that the PRS approach is a major challenge for low-income countries, whose governments must manage a complex policy

dialogue with a wide range of stakeholders so as to develop a medium-term development and poverty reduction strategy, complete with short- and long-term goals and monitoring systems.⁸¹

18. Clients' perceptions of World Bank effectiveness in fostering country ownership have improved in recent years. About 70 percent of MOPAN⁸² respondents see the Bank as actively supporting national and local participatory approaches. Almost two-thirds of respondents consider Bank conditionality to be reasonable, up from half of respondents in 2004. These improved perceptions are likely to be the result of efforts within the Bank to align development policy lending with governments' priorities as expressed in their PRSs.⁸³

19. Recent initiatives have drawn attention to the importance of unified strategies in fragile states. The OECD/DAC has drawn up *Principles for Good International Engagement in Fragile States and Situations*⁸⁴ in April 2007, encouraging a coherent approach between donors and alignment with local policies and systems. Also in 2007, the heads of the Multilateral Development Banks set up a working group to establish areas for common approaches in fragile states. These principles can be expected to reinforce PRS mechanisms and strengthen country ownership in states which are typically characterized by nascent policies and institutions.

20. World Bank analytical contributions have helped to develop better prioritized and sequenced development strategies. A recent review of World Bank Economic and Sector Work notes that "analytic work is increasingly building on issues identified in CASs or PRSPs and that it is feeding into the design of programs, policy actions, and operations".⁸⁵ For example, in Mozambique, Bank analytical products prepared with the Government helped define the policy priorities and institutional systems that underpin PARPA. The Poverty Assessment provided the analytical basis for the overall identification of PARPA's priorities and endorsement of its strategy to date. The Country Economic Memoranda helped to focus PARPA on the links between key sectors and the overall growth strategy, analyzing how Mozambique's natural resources – land, forestry, fisheries, mining and water – could be better managed to contribute more to overall growth. Similarly, the financial sector, investment climate, and legal and judicial sector reviews have contributed to improving the country's institutional foundations for shared growth and helped to form the basis for PARPA's structural reforms. Finally, reviews and assessments of public expenditures, financial accountability, and procurement helped form the basis for improving public financial management and the links between the strategy and national systems.

21. Looking ahead, the Bank is planning a number of activities to improve diagnostics on the binding constraints to shared growth and poverty alleviation through toolkits and the development of modeling techniques. Studies looking at specific country issues and policy questions are supported by a multi-donor trust fund on shared growth.

⁸¹ World Bank and IMF. 2005. *Idem*.

⁸² Multilateral Organizations Performance Assessment Network is a group of like-minded donors which began in 2003 to jointly survey the partnership behavior of multilateral organizations at the country level.

⁸³ IDA. 2007. *IDA's Role in Enhancing Aid Effectiveness through Strengthened Alignment and Harmonization* (Draft).

⁸⁴ OECD/DAC. 2007. *Principles for Good International Engagement in Fragile States and Situations*. Paper submitted to the DAC high level meeting (DCD/DAC(2007)29, April 3-4).

⁸⁵ IDA. 2006. *Economic and Sector Work Progress Report* (IDA/SecM2006-0542, October, 31).

22. Alongside the UNDP, the Bank has contributed to the costing of priority interventions. In Rwanda, a permanent team of four costing experts assist and train sector costing representatives in developing models and methods, tailor-made to Rwanda circumstances; the use of both “high” and “low” costing scenarios has helped to illustrate the resources required to meet the MDGs and enable the prioritization of expenditures to achieve best possible outcomes with more limited resources. In Tanzania, the United Nations has provided support for the costing of MKUKUTA in priority sectors including agriculture, water, health and roads. Costing exercises have also identified the interactions, synergies and complementarities between sectors. In Rwanda, sector working groups for the EDPRS undertook a sector mapping exercise to identify inter-linkages between the various sectors which have fed into the development of log frames. When costing the road sub-sector for MKUKUTA in Tanzania, stakeholders from all sectors were invited for a two-day consultative workshop in order to identify inter-sectoral linkages and crosscutting issues.

23. The Bank’s Maquette for MDG Simulations (MAMS) has informed the implementation of PRSs in eight African countries since its inception in 2005. As a dynamic general equilibrium model, MAMS has helped to inform strategic priorities by demonstrating the economy-wide impact of interventions and indicating the most effective use of funds within a given resource constraint. Annex II contains a fuller discussion of MAMS.

24. The Bank has strengthened PRS-budget links by providing multi-year support to country-led public financial management reform programs. As discussed in greater detail in Annex III, the Bank has helped PRS countries to strengthen the basics of public financial management in order to foster stronger links between planning and budgeting.

25. Through the Africa Action Plan, the World Bank and other donors are providing assistance to PRS countries to develop and implement Monitoring and Evaluation Plans linked to their national strategies by the end of FY08.⁸⁶ The 2005 PRS review noted that “while there does seem to be increased donor support for monitoring, it tends to continue to focus on each donor’s own reporting requirements and priorities, thus impeding the development of national ones.” The Bank has attempted to reinforce existing national monitoring institutions rather than develop parallel systems. In Madagascar it has supported the government in the development of a *Stratégie Nationale de Développement de la Statistique* to improve statistical capacity. In Uganda it has supported a National Integrated Monitoring and Evaluation Strategy to incorporate various relevant agencies and ex-ante systems under one institutional roof. The Bank has also been at the forefront of efforts to disseminate best practice, most notably through the recent publication of a study of 12 first generation PRS monitoring systems.⁸⁷ The Trust Fund for Statistical Capacity Building provides grants of up to \$400,000 for improving statistical capacity.

⁸⁶ World Bank. 2005. *Meeting the Challenge of Africa’s Development: A World Bank Group Action Plan*. (Report Number 33949, September 26).

⁸⁷ Bedi, Tara, Aline Coudouel, Marcus Cox, Markus Goldstein, and Nigel Thornton. 2006. *Idem*.

ANNEX II

ASSESSING THE MACROECONOMIC FRAMEWORK FOR SCALING UP

1. A stable, sound macroeconomic framework is an essential foundation for efforts to scale up development results. An environment of financial stability and sustainability is a necessary condition for achievement of strong and sustained economic growth and durable progress toward the MDGs. Macroeconomic management has improved in most developing countries in recent years. Stronger macroeconomic fundamentals have been an important factor contributing to the recent broad-based improvement in developing countries' growth performance. Better-performing poor countries have also seen their debt burdens reduced significantly, first through the HIPC Initiative and more recently through the MDRI. For a number of developing countries, these developments have created a more stable and secure financial environment in which to pursue the goals of accelerated growth and achievement of the MDGs. They have enhanced the countries' macroeconomic absorptive capacity to take advantage of increases in foreign aid in support of their development goals. Continued implementation of sound macroeconomic policies will be important to maintain this more favorable macroeconomic context.

2. Improvements in macroeconomic management have been accompanied by advances in the supporting analytical framework. These include:

- A framework developed by the IMF that distinguishes between various combinations of spending and absorption of aid to analyze the macroeconomic implications of the different policy options for managing increases in aid inflows.
- A framework for Debt Sustainability Analysis (DSA), developed jointly by the Bank and the Fund, for systematic assessment of a country's external debt strategy and outlook, including application of stress tests—an important follow-up to the debt relief operations to help guide policy to avoid a rapid re-accumulation of debt and preserve debt sustainability.
- Work on fiscal policy for growth at the Bank that has produced a stronger, medium-term analytic framework for assessing fiscal space and implications for policy both in terms of the overall fiscal stance and expenditure path and the composition and efficiency of spending.
- Work on growth diagnostics at the Bank to ground policy in a sharper analysis of key constraints to stronger growth.
- Models, notably the Maquette for MDG Simulations (MAMS) developed at the Bank, to analyze alternative strategies to scale up development results to achieve the MDGs and related outcomes, including their costing, macroeconomic implications, and policy trade-offs over time and across sectors.

3. Macroeconomic management of aid flows will be facilitated by the stronger analytic framework that has emerged, both for providing inputs to countries in the formulation of macroeconomic policies as part of scaled-up poverty reduction and MDG strategies and for informing policy dialogue among development partners. The challenge will be its systematic application, extending the use of the analytic tools to as many countries as possible. As an example, detailed analysis of alternative scale-up strategies using MAMS has so far been limited to a relatively small number of countries.

4. This annex reviews findings from recent analytic work on the macroeconomic framework for scaling up in a sample of countries. The sample includes six strong performing countries in Africa that have experienced increases in aid in recent years and are good prospects for a further scaling up of aid in the period ahead: Ghana, Madagascar, Mozambique, Rwanda, Tanzania, and Uganda. It also includes Nicaragua. The next section reviews these countries' macroeconomic management of the recent increases in aid inflows, based on the analytic framework that distinguishes between the spending and absorption of aid. The following, forward-looking section presents findings from some scaled-up aid and MDG scenarios based on the MAMS framework and fiscal space and debt sustainability analyses.

Macroeconomic Management of Aid Inflows

5. The basic purpose of aid is to allow recipient countries to increase their consumption and investment (i.e., *spend* the aid) using the transfer of external resources from the donor (i.e., *absorb* the aid). A spend and absorb strategy is instrumental in ensuring that aid helps raise the rate of economic growth and reduce poverty by financing new investments and social spending. Box 1 summarizes the basic policy options available to an aid recipient in terms of the spending and absorption of aid and their likely macroeconomic implications.

Box 1. Spending and Absorption of Aid		
<p>The macroeconomic policy response to aid is characterized by the recipient government's decisions on <i>spending</i> and <i>absorbing</i> the aid. Aid is spent if leads to a widening of the fiscal deficit (net of aid). Aid is <i>absorbed</i> if leads to a widening of the current account deficit (net of aid). Absorption measures the extent to which aid produces a real transfer of resources through higher imports (or a reduction in domestic resources used in producing exports). The central bank determines absorption through sales of foreign exchange, and through monetary policy that influences aggregate demand, and hence the demand for imports.</p> <p>The table below summarizes the basic short-run policy combinations available to a recipient of increased aid. Cases 1 (<i>spend and absorb</i>) and 2 (<i>not spend but absorb</i>) or a combination thereof are the more desirable outcomes—with spending done by the public sector in the first and the private sector in the second. The risk of Dutch disease depends very much on the composition and productivity of the spending that aid helps finance. Case 3 (<i>spend but not absorb</i>) is a problematic response. It is similar to a fiscal stimulus in the absence of aid (aid stays in reserves). The result is either an increase in money supply and a rise in inflation or a rise in interest rates and possible crowding out of the private sector, depending on whether the government spending is sterilized or not. Case 4 (<i>neither spend nor absorb</i>) may help build reserves and smooth volatile aid flows but in the long run is equivalent to forgoing aid altogether.</p>		
	<i>Absorbed</i>	<i>Not Absorbed</i>
<i>Spent</i>	<p>Case 1. Central bank sells aid dollars. Current account deficit (net of aid) widens to allow real transfer of resources through higher imports.</p> <p>Aid is used for public investment and consumption. Fiscal deficit (net of aid) rises.</p> <p>Money supply unchanged. Risks Dutch disease.</p>	<p>Case 3. Central bank uses aid to accumulate foreign exchange reserves. There is no real resource transfer and no effect on the current account balance.</p> <p>Fiscal deficit rises as aid is spent.</p> <p>If unsterilized: money supply rises. Risks inflation.</p> <p>If sterilized: domestic public debt rises. Risks higher interest rates and crowding out of private sector.</p>
<i>Not Spent</i>	<p>Case 2. Central bank sells foreign exchange but fiscal deficit remains unchanged.</p> <p>Helps achieve stabilization; provides resources for private investment.</p>	<p>Case 4. Central bank accumulates foreign exchange as reserves; fiscal deficit net of aid unchanged.</p> <p>No real transfer and no Dutch disease.</p> <p>Equivalent to rejection of aid (in the long run).</p>

Source: IMF, 2007. Aid Inflows: The Role of the Fund and Operational Issues for Program Design.

6. In a recent IMF paper, this methodology is used to analyze macroeconomic management of aid in several countries that received significant increases in aid during 1999-2005.⁸⁸ The findings are summarized in Table 1. While individual country experiences vary appreciably in their specifics, they reveal a broad pattern. In the early phase of the aid surges, countries tended to adopt a cautious approach that limited the spending and absorption of aid, relaxing the policy stance in later years toward fuller aid spending and absorption. Also, the country cases provide little evidence of significant real exchange rate appreciation accompanying the surge in aid.

Table 1. Macroeconomic Management of Aid: Country Experiences, 1999-2005

Country	Summary
Ghana	Cautious approach limited aid spending and absorption because of the need to stabilize the economy and reduce the fiscal deficit. Aid was used largely to replace domestic financing and to build international reserves. Another reason for caution was aid volatility: the average swing in fiscal aid inflows during 1999-2005 was more than 5 percent of GDP. Following a sizable depreciation in 2000, the real exchange rate was relatively stable despite higher inflation versus trading partners. The 2006 PRGF-supported program was the first to encourage a spend and absorb approach.
Madagascar	Initial Fund program in 1999 emphasized lowering debt and restraining borrowing following debt relief. After 2002, fiscal and current account developments largely tracked foreign aid, with aid spending exceeding absorption. Aid forecasts tended to be optimistic. CPI-based real exchange rate showed appreciation during 2002-03 but unit labor cost-based RER did not and export growth remained healthy.
Mozambique	Mozambique's Fund-supported program has had three distinct phases since 1999. Initially, the policy was to spend and absorb an expected surge in aid. The program starting in 2004 targeted fiscal consolidation in the face of a projected decline in aid. More recently, the program has shifted back to a spend and absorb strategy, anticipating a rise in aid. In general, aid inflows were quite volatile and unpredictable during 2000-05. The real exchange rate depreciated during 2000-03. Partial aid absorption associated with accumulation of reserves partly reflected a fear of Dutch disease. A real appreciation took place in 2004 but was corrected in 2005.
Nicaragua	Increases in aid during 2001-03 resulted in little additional spending and only partial absorption as Nicaragua's Fund-supported program focused on improving fiscal sustainability and international reserve cover. Aid was used mainly to substitute for domestic financing, expanding room to crowd in the private sector. More recently, the policy stance has shifted gradually toward a spend and absorb approach.
Rwanda	Until the attainment of the HIPC completion point in 2005, the emphasis in the Fund-supported program was on debt sustainability, with stringent limits on external borrowing and efforts to reduce domestic debt. Aid-based fiscal spending was initially limited. A shift to a spend and absorb approach started in 2004. Since 2004, aid has increased rapidly, making coordination of fiscal and monetary policies a challenge. Aid absorption increased, but still was constrained by authorities' concern about real exchange rate appreciation, resulting in higher-than-programmed reserve accumulation.
Tanzania	Aid generally was fully spent but absorption initially lagged as the Government was concerned about exchange rate appreciation and reluctant to use foreign exchange resources to sterilize the impact of increased capital inflows. This resulted in larger-than-programmed reserve accumulation. In later years (2003-05), both programmed and actual aid absorption rose as foreign exchange sales were increased. The Dutch disease effect was deemed small considering the cumulative 40 percent real depreciation during 2001-04.
Uganda	The surge in aid from about 8 percent of GDP in 1997/98 to a peak of 12 percent in 2003/04 was largely spent, reflected in a rise in the fiscal deficit (excluding grants) from about 6.5 percent of GDP to 10 percent. Aid absorption, however, lagged, with the central bank accumulating reserves. Episodes of sales of treasury bills took turns with episodes of foreign exchange sales to keep money supply and inflation under control. Program design shifted later to allow larger foreign exchange sales and greater absorption.

Source: IMF, 2007. *Idem*.

⁸⁸ IMF, 2007. *Idem*. See also IMF, 2005. *The Macroeconomics of Managing Increased Aid Inflows: Experiences of Low-Income Countries and Policy Implications*; and Berg, Andrew, Shekhar Aiyar, Mumtaz Hussain, Shaun Roache, Tokhir Mirzoev, and Amber Mahone. 2007. "The Macroeconomics of Scaling up Aid – Lessons from Recent Experience." Occasional Paper 253, International Monetary Fund, Washington, DC.

7. There are several factors that explain the countries' initial reluctance to fully spend and absorb the incremental aid: desire to secure macroeconomic stability by strengthening previously weak reserve positions and/or reducing domestic public debt; perceived need to hedge against aid volatility and possible future reductions in aid; and concerns about exchange rate appreciation and loss of competitiveness. As countries' macroeconomic positions strengthened, they opted for fuller spending and absorption of aid.

8. Looking ahead to the prospect of a further scaling up of aid in the period ahead, these findings suggest that, thanks to the progress countries have made in recent years in strengthening their macroeconomic positions, they are better placed today to spend and absorb future increments in aid. Analysis of the recent surges in aid also shows that, with careful macroeconomic management and effective use of the incremental resources in productivity-enhancing investments, sizable increases in aid can be absorbed without a significant appreciation of the real exchange rate and loss of external competitiveness. In addition to the spend and absorb decisions presented in Box 1, the impact of aid inflows on the real exchange rate depends on the *composition* of spending supported by the incremental resources. Directing aid to strengthening of basic infrastructure enhances the productivity of private activity and bolsters growth, dampening the impact on domestic prices and the real exchange rate. Infrastructure investment also eases the impact of the spending of aid on domestic demand through its relatively high import intensity. These findings are corroborated by the analysis of model-based scaling-up scenarios in the next section.

Scaling-up Scenarios: Macroeconomic Framework, Fiscal Space, and Resource Needs

9. In support of countries' efforts to develop scaled-up poverty reduction and MDG strategies, the Bank has stepped up its work to provide needed analytic inputs. A key instrument developed for this purpose is MAMS, a dynamic general equilibrium model that allows an integrated analysis of alternative scaling-up strategies in terms of their costing, macroeconomic implications, and the distribution and sequencing of investment taking into account intersectoral linkages and absorptive capacity constraints.⁸⁹ Its scope encompasses not only growth and poverty reduction but also key human development outcomes. As such, since the model's first country application in 2005, it has been used increasingly to develop and analyze scenarios for the achievement of the MDGs and related development outcomes. Cost estimates for the scaling-up scenarios generated by the model, and analysis of the implications of alternative means of financing, have been quite useful in assessing options for raising the needed additional resources, including through scaled-up aid. Table 2 summarizes completed and ongoing applications of the MAMS in several countries.

10. Another important source of input to the development and analysis of scaling-up scenarios, especially the analysis of the path of public expenditure and its composition and efficiency and of the options for mobilizing needed additional financing, is the recent work at the

⁸⁹ See Bourguignon, François, Carolina Diaz-Bonilla, and Hans Lofgren. 2007. "Aid, Service Delivery, and the MDGs in an Economy-wide Framework." Draft, April 16. Forthcoming in Bourguignon, François, Luiz Pereira da Silva, and Maurizio Bussolo (eds.). *The Impact of Economic Policies on Poverty and Income Distribution: Macro-Micro Evaluation Techniques and Tool*. New York NY: Palgrave.

Bank on fiscal space issues. Initially piloted through twelve country studies, the fiscal space work is now being mainstreamed into the Bank’s regular economic and sector work.⁹⁰

Table 2. MAMS Applications in Country Work

Country	Year	Issues Addressed	Product/Context
DRC	2007	Fiscal space and debt sustainability	Public Expenditure Review
Ethiopia	2005	MDG strategy	Government MDG Needs Assessment
	2005	Poverty reduction strategy	Input to/ review of PRS
	2006	Fiscal space, aid, trade-offs	Report: Review of Public Finance
	2007	Labor market, migration	Report on Urban Labor Markets
Ghana	2007	MDG strategy	Country Economic Memorandum
Honduras	2007	MDG strategy	Public Expenditure Review
Kenya	2007	Long-run growth; policy trade-offs	Country Economic Memorandum
Madagascar	2007	MDG strategy	Not yet determined
Malawi	2007	Government spending composition and trade-offs	Public Expenditure Review
Tanzania	2007	Government spending composition and trade-offs	Country Economic Memorandum
Uganda	2006	Growth	Country Economic Memorandum
	2007	Growth, alternative financing strategies, trade-offs	Public Expenditure Review
Venezuela	2007	Sustainable poverty reduction strategies	Poverty Assessment

Source: DEC Program on MAMS, The World Bank. This table does not cover MAMS applications in some Latin America countries under the joint World Bank-UNDP-UNDESA project “Assessing Development Strategies to Achieve the MDGs in Latin America.”

11. The analysis of the scaling-up options is also informed by the joint Bank-Fund Debt Sustainability Analysis (DSA), which assesses a country’s debt sustainability under a variety of assumptions, providing guidance on the financing strategy that is consistent with the country’s prospective ability to service debt.⁹¹ Preparation of a DSA is now required for all IDA-only countries.

12. The country cases presented below illustrate how these analytic instruments are being used at the country level to analyze possibilities for scaling up progress on poverty reduction and other MDGs and related financing needs. The analysis presented draws on MAMS applications, fiscal space studies, and DSA reports (some of the analysis presented is preliminary, as it represents work in progress). It is intended to provide inputs to the country’s poverty reduction and MDG strategies and to inform dialogue with development partners on the case for scaled-up support for those strategies. The subject countries are all strong African performers, with potential to scale up development results that merits serious consideration from donors for scaled-up support.

Ghana

13. Ghana has emerged as one of the best performing African economies, with growth consistently surpassing 5 percent since 2001 and rising to above 6 percent in 2006. Improved macroeconomic management and significant and ongoing progress on structural and institutional reforms present a real opportunity to accelerate growth and progress toward the MDGs.

⁹⁰ See World Bank. 2007. *Fiscal Policy for Growth and Development: Further Analysis and Lessons from Country Studies*. (SecM2007-0086, February 23) for a summary of the country studies and the overall analytic framework.

⁹¹ See IDA and IMF. 2005. *Operational Framework for Debt Sustainability Assessments in Low-Income Countries—Further Considerations* (IDA/R2005-0056 and SM/05/109, March 29); and IDA and IMF. 2006. *Review of Low-Income Country Debt Sustainability Framework and Implications of the MDRI* (IDA/R2006-0046 and SM06/123, March 27).

14. **Scaling up and MDG Scenarios.** A forthcoming CEM simulates three growth scenarios to 2015 using the MAMS model, including a baseline scenario with annual growth at 6.9 percent, an accelerated growth with closing of infrastructure gaps scenario yielding growth at 7.4 percent, and a full MDG achievement scenario with growth rising to 7.8 percent.⁹² Both the MAMS and an independent simulation analysis⁹³ show that Ghana can take on additional resources without suffering from Dutch disease. Thanks to continuing progress, PFM capacity is not considered a binding constraint, but stronger efforts will be needed to build sectoral capacity, especially in health, to realize the full MDG achievement scenario. Ensuring “value for money” is a strong, overarching emphasis in the Government’s public resource management strategy.

15. The baseline growth puts Ghana in a position to achieve the poverty reduction MDG well ahead of 2015 (Table 3). However, Ghana will not achieve many other key MDGs, including primary completion, child and maternal mortality, and access to safe water and sanitation. In the accelerated growth with the closing of infrastructure gaps scenario, primary completion and access to safe water and sanitation approach MDG targets, but the health MDGs remain elusive. The full MDG scenario achieves the health MDGs but at the cost of a substantial additional commitment of resources. In the baseline scenario, ODA requirements are estimated at about \$1.5 billion annually (about 10 percent of current GDP), only modestly higher than present levels. In the closing of infrastructure gaps scenario, additional ODA of \$350-430 million p.a. (2.5-3 percent of GDP) is needed, which should be feasible. In the full MDG achievement scenario, however, further large increases in financing are needed, averaging \$750 million annually between 2007 and 2011 (5-6 percent of GDP) and rising to \$1.7 billion annually between 2012 to 2015 (8-9 percent of GDP; Figure 1). Given the magnitude of the additional financing requirement, it seems unlikely that all of it can be met from ODA, which underscores the need for even stronger efforts by Ghana to mobilize domestic resources, improve efficiency, and catalyze private participation.

Table 3. Ghana: MDG Scenarios, 2015

	Baseline growth (6.9%)	Accelerated growth (7.4%) with closing of infrastructure gaps	Accelerated growth (7.8%) with full MDG achievement
Poverty headcount ratio (%)	12	10.2	9.8
Primary completion rate (%)	89	94	100
Under-5 mortality (per 1,000 live births)	97	95	40
Maternal mortality (per 100,000 births)	440	428	185
Access to safe water (%)	62	75	85
Access to sanitation (%)	47	70	85

Note: All values in the last column are MDG targets except the poverty rate where the MDG target of 26% is exceeded.

Source: World Bank. (Forthcoming). *Ghana: Country Economic Memorandum*; and Ghana MAMS simulations.

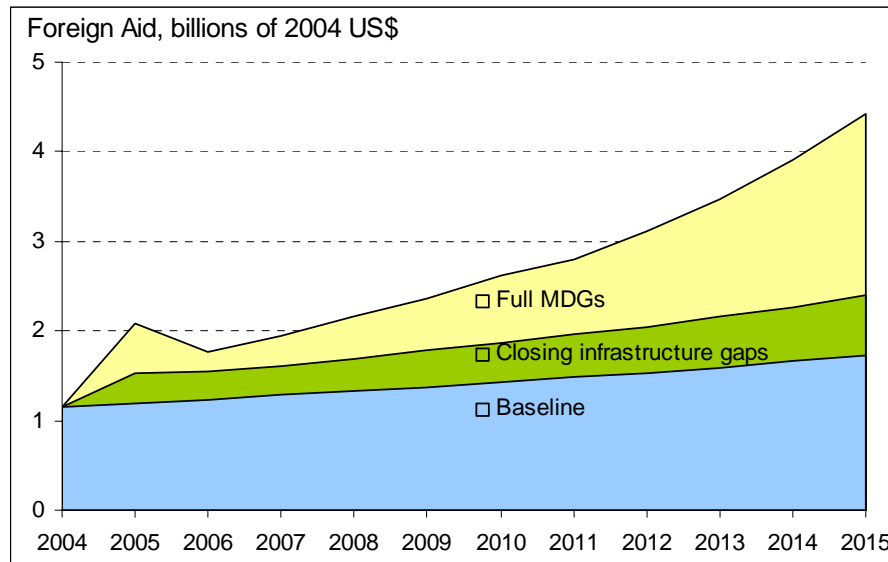
16. **Debt Sustainability Analysis.** The joint Bank-Fund DSA for Ghana prepared in 2007 concludes that Ghana’s risk of external debt distress is moderate, albeit close to the low risk category. Risks to total public debt are also moderate. This assessment is contingent upon Ghana maintaining its improved growth performance and meeting its external financing requirements

⁹² World Bank. (Forthcoming). *Ghana: Country Economic Memorandum*.

⁹³ Elbadawi, Ibrahim and Linda Kaltani. 2007. “Scaling up Aid for Ghana: Maintaining Competitiveness, Avoiding Dutch Disease, and Accelerating Growth.” Background Paper for the Ghana CEM.

mainly from concessional sources, keeping recourse to nonconcessional borrowing within prudent limits.

Figure 1. Ghana: Scaling-up Scenarios – Additional Financing Requirements



Source: World Bank, 2007 (Forthcoming). *Ghana: Country Economic Memorandum*; Ghana MAMS simulations.

Madagascar

17. Madagascar is a good example of how rapidly the right policies can propel a previously lagging country. While most MDGs for Madagascar are far from being achieved, the path endorsed by the new Government since 2002 has provided more and much needed financing to education, health, and infrastructure. Growth prospects have recently improved, with annual growth of 6 percent likely over the medium term. Although Madagascar lags behind many African countries in education, it is superior on some other MDGs, such as health. Most distressing is the poverty rate, which at over 70 percent is well above the African average.

18. **Scaling up and MDG Scenarios.** A recent application of the MAMS model analyzes two scenarios.⁹⁴ A baseline scenario, based on current improved trends, achieves moderate progress toward the MDGs. A more ambitious scenario achieves the health and water and sanitation MDGs, almost achieves the primary completion MDG, and makes significant progress toward the poverty MDG (Table 4). The financing requirements of this scenario are double those of the baseline scenario (aid recently has averaged about 8 percent of GDP). Despite the relatively better initial health indicators, the additional financing requirement is largest for achieving the health MDGs. If all of the large additional financing is met from foreign aid, the real exchange rate undergoes a sizable appreciation (more than 20 percent), risking competitiveness and growth

⁹⁴ Mensbrugge, Dominique van der and Shou Tan. 2006. "A MAMS Approach to Analyzing the Millennium Development Goals in Madagascar." Draft. The paper is being updated to take into account the significant change to the macroeconomic framework as a result of the recently confirmed nickel mining investment of more than \$2.5 billion. The MAMS model will also be used for simulating options for managing the impacts of the sizable foreign investment inflows.

unless productivity gains are enhanced. Meeting part of the additional financing from increased domestic resource mobilization alleviates the pressure on the exchange rate. Another implication of the scaled-up scenario is the need for stepped-up efforts to strengthen institutional capacities.

Table 4. Madagascar: MDG Achievement Scenario

	1990	2004	2010	2015	2015
	<u>Actual</u>	<u>Actual</u>	<u>Proj.</u>	<u>Proj.</u>	<u>Target</u>
Poverty headcount ratio (%)	68	74	54.8	47.3	34
Primary completion rate (%)	35	45	84.4	97	100
Under-five mortality rate (per 1,000 live births)	168	123	62	56	56
Maternal mortality ratio (per 100,000 births)	550	550	164	137	138
Access to improved water source (%)	40	46	66.7	77.8	70
Access to improved sanitation facilities (%)	14	32	44.8	57	57

Source: Mensbrughe and Tan. 2006. Idem.

19. **Fiscal Space Assessment.** There is scope for raising part of the required additional financing from domestic revenue mobilization as well as for improving efficiency of public spending. At 10 percent of GDP, tax revenue generation in Madagascar is low. A recent fiscal space study assessed tax revenue to be below its potential by at least 3 percent of GDP.⁹⁵ As part of the latest PRS, the Government plans to undertake a major tax reform. The composition of the budget is generally well aligned with development priorities. Still, there is potential for improvement, e.g., in the balance between new investment and operations and maintenance spending.

20. **Debt Sustainability Analysis.** Debt relief under both the HIPC Initiative and MDRI has reduced Madagascar's previously high debt burden to a sustainable level. Madagascar's debt indicators are now below the debt burden thresholds in the baseline scenario. With the improved growth and exports prospects as a result of the new mining investments, the 2007 DSA shows that the debt situation is not significantly vulnerable to shocks. Debt sustainability appears somewhat vulnerable, though, if large export shocks materialize. Overall, Madagascar's risk of debt distress is low. Maintenance of debt sustainability will depend on successful promotion of growth and exports and careful management of external borrowing, with maximum reliance on grants and highly concessional loans.

Rwanda

21. In the past decade, Rwanda has achieved an impressive recovery from conflict. Within the framework of Poverty Reduction Strategies (Rwanda has progressed to its second PRS), it has been implementing wide-ranging reforms. Following average annual growth of 15 percent during 1995-99, the immediate post-conflict reconstruction phase, growth has averaged 5.3 percent since 2000, while inflation declined to a moderate 6 percent. Alongside macroeconomic progress, service delivery has improved, especially in the area of human development. These achievements have been supported by sizable aid inflows, which increased from about 11 percent of GDP in 2000 to 16.5 percent in 2006.

⁹⁵ World Bank. 2007. *Fiscal Policy for Growth and Development: Further Analysis and Lessons from Country Studies*. Idem.

22. ***Fiscal Space and Scaling up.*** Rwanda's Vision 2020 aims to raise per capita income growth to 6-7 percent in the medium- to long term. Poor infrastructure, especially transport and energy, is a major constraint to stronger growth. Substantial increases in infrastructure spending are needed to spur private investment. Rwanda also faces large commitments in education and health. A recent fiscal space study assessed options to finance the needed increase in development spending.⁹⁶ Rwanda has raised revenue collection substantially but, given the narrow tax base, there are limits to further revenue enhancements. There is some scope for improving the composition and efficiency of spending to enhance its growth and MDG impact. Currently, spending on infrastructure and agriculture is low. Education receives the largest share of the budget, but nearly a third of the recurrent budget goes to higher education. While malaria is the biggest cause for mortality and morbidity, it receives only a fraction in aid of what is allocated to HIV/AIDS. In health, only a small proportion of aid enters the government budget; the rest is managed directly by donors and channeled to NGOs through single-issue vertical programs, leaving government-run health programs, such as those for maternal and child health, badly under-funded. To improve public resource management, the Government has started several initiatives to strengthen budgeting and expenditure management and monitoring.

23. Even with improved domestic resource management, achieving Rwanda's development goals will require a significant scaling up of aid. Better alignment with government programs that support Rwanda's needs will enhance aid effectiveness. The financing requirements to achieve the MDGs are estimated at an incremental 15-20 percent per year over the current aid level of nearly \$500 million.

24. ***Debt Sustainability Analysis.*** Although debt levels have been reduced by the HIPC Initiative and MDRI, new borrowing must be limited and undertaken only on highly concessional terms. The 2007 DSA concludes that while the immediate risk of debt distress has been reduced, Rwanda's debt situation could quickly become unsustainable without a high and sustained level of grant financing and strong export growth.

Tanzania

25. Tanzania has experienced a notable increase in aid since 2000, but substantial further scaling up of aid will be needed to support strong growth and accelerate progress toward the MDGs. The Government has been hard at work, with support from donors, to address both micro and macro absorptive capacity constraints. The macro framework underlying the growth and poverty reduction strategy has improved significantly.⁹⁷ Public financial management has been strengthened, including improvement of the medium-term budget framework.⁹⁸ The mechanisms for aid coordination have improved, including preparation of a Joint Assistance Strategy.

26. ***Scaling up and MDG Scenarios.*** The MAMS simulations for Tanzania are preliminary but early results show that the poverty reduction MDG is almost achievable with continuation of

⁹⁶ World Bank. 2007. *Fiscal Policy for Growth and Development: Further Analysis and Lessons from Country Studies*. Idem.; and World Bank. 2007. *Rwanda: Toward Sustained Growth and Competitiveness Country Economic Memorandum* (Report No. 36860-RW).

⁹⁷ IDA and IMF. 2006. *Tanzania: Poverty Reduction Strategy Paper-Joint Staff Advisory Note*.

⁹⁸ World Bank. 2006. *Tanzania - Public Expenditure and Financial Accountability Review: FY05*.

the higher average growth of recent years—about 5.5 percent p.a. (Table 5).⁹⁹ But an acceleration of growth to the 6-7 percent range, quite feasible if Tanzania’s reform momentum is sustained and adequately supported by partners, would achieve the target well ahead of schedule. However, achievement of most other MDGs will require substantial further increases in aid, over and above the baseline scenario that assumes about the same level of aid relative to GDP as at present—about 10 percent. The simulations underscore the need for the additional financing to be raised on concessional terms for continued debt sustainability. They also point to the need for stronger domestic resource mobilization through higher revenues (more from expanding the revenue base and improving tax administration than raising taxes) and improvements in expenditure efficiency. The appreciation of the real exchange rate from the scaled-up aid inflows is estimated to be moderate, but the results reinforce the importance of a continued policy focus on improving Tanzania’s competitiveness.

Table 5. Tanzania – Baseline Scenario of Key MDG Results

	2005	2010	2015	Target
National poverty headcount ratio (%)	34.4	29.5	20.1	19.3
Primary completion rate (%)	54.2	62.8	71.0	100
Under-five mortality (per 1000 live births)	83.2	75.7	66.5	48.0
Maternal mortality (per 100,000 births)	578	460	325	133
Access to water (%)	57.0	57.6	59.6	70.9
Access to sanitation (%)	91.0	91.0	91.2	92.0

Note: The poverty headcount is based on the national poverty line, set at per capita PPP \$0.79/day (2000 prices).

Source: Tanzania MAMS simulations (preliminary).

27. **Debt Sustainability Analysis.** Tanzania received substantial debt relief in 2006 under the MDRI, amounting to about 60 percent of the country’s total external debt stock at the end of 2005. As a result of the debt relief, all external debt indicators are now significantly below the debt thresholds. The NPV of external debt declined to 15 percent of GDP and 60 percent of exports, and debt service payments fell to 5 percent of exports. This puts Tanzania at a low risk of debt stress, given prudent macroeconomic and debt management. Stress test analysis confirms this assessment.

Uganda

28. Uganda achieved one of the highest growth rates in Africa in the 1990s, with growth averaging 6.9 percent. This performance was supported by improved macroeconomic management and a range of structural reforms. Foreign aid over the past decade has averaged 10 percent of GDP. During 2000-06, growth slowed, partly because of lower coffee prices hurting the country’s major export, but still averaged over 5 percent. Uganda needs to reinvigorate efforts to achieve stronger and sustained growth and accelerate progress toward the MDGs.

29. **Fiscal Space and MDG Scenarios.** A recent fiscal space study and MAMS application examine alternative financing strategies for achieving higher growth and increasing investment in MDG-related services.¹⁰⁰ A particularly high priority is strengthening infrastructure, where

⁹⁹ World Bank Tanzania Country Team. 2007. *MAMS for Tanzania: Data Sources, Assumptions, and Preliminary Results* (March).

¹⁰⁰ World Bank. 2007. . *Fiscal Policy for Growth and Development: Further Analysis and Lessons from Country Studies*. Idem.; World Bank. 2007. *Uganda: Fiscal Policy for Growth, Public Expenditure Review*, (Report No.

high costs and poor quality of transport and energy services act as a severe constraint to growth. There is significant scope for mobilizing more resources for infrastructure and other priorities through improvement of government expenditure composition and efficiency. Administration expenses and defense consume 48 percent of the budget. There are also inefficiencies in expenditure within the priority sectors—inadequate road maintenance, teacher absenteeism and other waste in education. Simulations show that cutting unproductive expenditure and reallocating savings to sound programs in higher priority areas such as infrastructure, education, and health can boost growth by 0.4-0.5 percent p.a. and improve a broad range of MDG indicators. Similar gains are observed if aid is scaled up and allocated to growth and MDG-oriented functions. Increasing expenditure by raising taxes, however, results in a decline of private investment growth.

30. The analysis points to a financing strategy that employs a mix of: improved expenditure efficiency; higher aid; and domestic revenue mobilization that emphasizes improved collection and broadening of the tax base rather than higher tax rates. Longer-term, the Government aims to reduce reliance on foreign aid, an effort that will need careful design and phasing.

31. *Debt Sustainability Analysis.* Additional debt relief under the MDRI would reduce the external debt-to-GDP (exports) ratio to about 10 percent (50 percent) in 2007, putting Uganda at a low risk of debt distress. Prudent debt management and efficient use of new external resources will be needed to ensure that the debt burden remain lows in the long-term.

ANNEX III

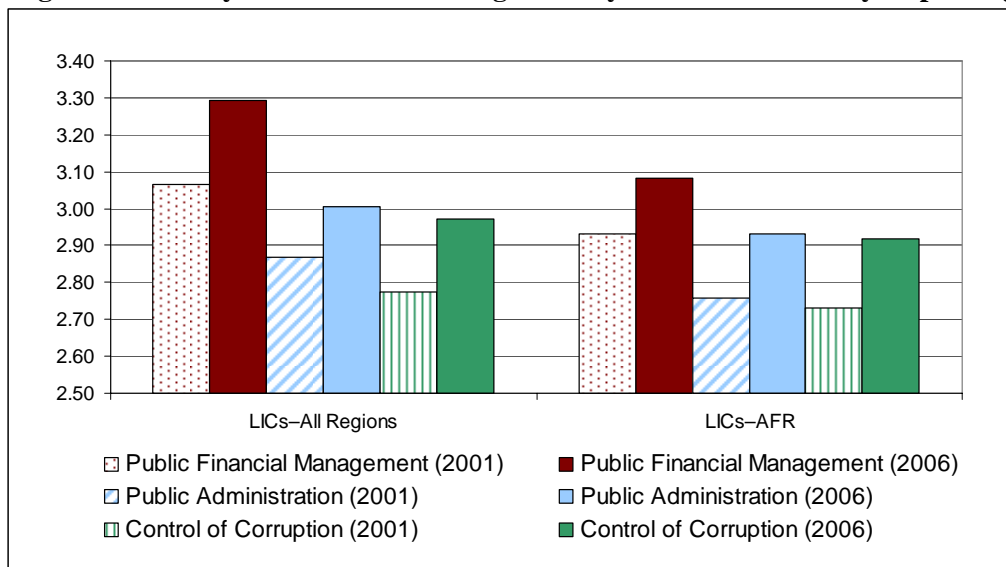
STRENGTHENING INSTITUTIONAL CAPACITY AND SYSTEMS

1. There is a broad consensus that sound public institutions are critical for economic development and aid effectiveness. Strong institutions promote growth and human development by encouraging both higher investment and improved efficiency in public spending. Sound institutions are also crucial for strengthening country ownership of the development agenda by promoting priority-setting, budgeting, implementation and oversight, among other public actions. The importance of institutions is only heightened by the prospect of scaled-up aid: adequate administrative capacity and public financial management are particularly important for ensuring that scaled-up assistance is delivered and managed effectively.

Progress in Developing Countries

2. Across the globe, countries with committed governments have made progress in improving governance and reducing corruption. As measured by the Bank's Country Policy and Institutional Assessment (CPIA) scores for 2001-2006, the quality of budget and financial management and of public administration systems is gradually improving in low-income countries and in the Africa region, a key region of focus for scaling up aid (Figure 1). This includes improvement in the links between budgets and policy priorities such as poverty reduction as well as the quality of financial management and fiscal reporting. There is also improvement in transparency, accountability, and control of corruption in the public sector.

Figure 1. Country Public Sector Management Systems are Gradually Improving

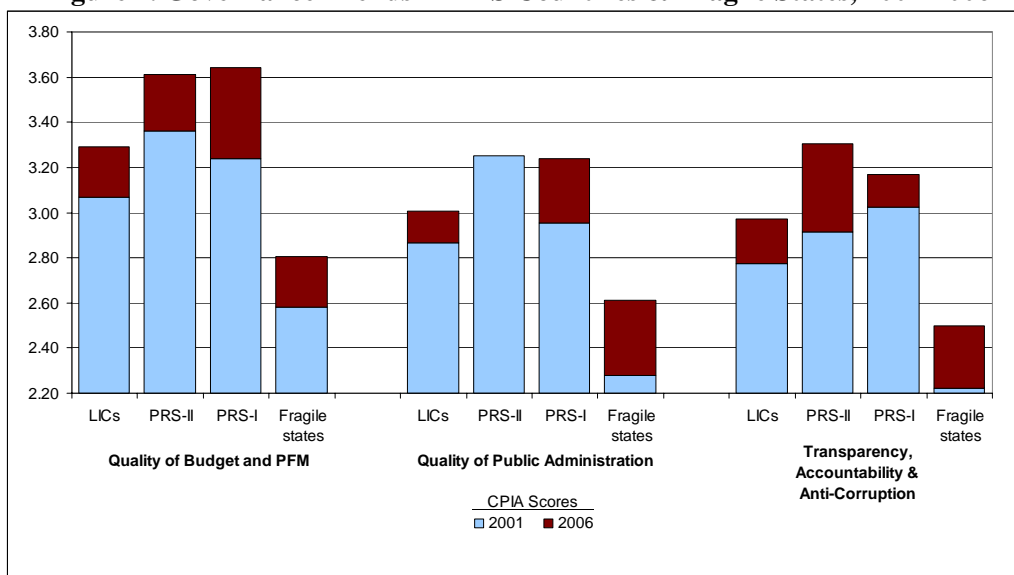


Source: Governance CPIA Data, 2001 and 2006. CPIA scales are from 1 to 6.

3. Figure 2 presents the same governance CPIA indicators for countries that have prepared PRSs and for fragile states that have prepared some instrument setting out the national development strategy (PRS, Interim PRS, or a Transitional Results Matrix). The indicators show improvement for both groups of countries. The average score for the PRS countries exceeds that

for all low-income countries for all three dimensions of public sector governance presented: public financial management; public administration; and transparency, accountability, and control of corruption. Fragile states start from a lower level, given their weaker governance contexts, but the improvement in their indicators is encouraging. The seven “good performing” African countries that have been the initial focus of scaling-up discussions have achieved the highest average governance scores when compared to the averages for PRS-I and PRS-II countries.¹⁰¹ For example, the Government of Madagascar has completed a governance and anti-corruption report focusing on how to improve service delivery to households. Tanzania has improved accountability, transparency and resource management for service delivery, building on administrative reforms of the 1990s. Regionally, the African Peer Review Mechanism (APRM) has become an important means to empower reformers, and APRM reviews have been completed in Ghana and Rwanda, with both governments implementing the recommendations.

Figure 2. Governance Trends in PRS Countries & Fragile States, 2001-2006



Source: Governance CPIA Data, 2001 and 2006. CPIA scales are from 1 to 6.

4. Data for 23 Heavily Indebted Poor Countries (HIPC) along three dimensions (budget formulation, execution, and reporting) reveal a 10 percent improvement in the 15 HIPC indicators corresponding to these dimensions between 2002 and 2004. Five of these 23 HIPC countries assessed in 2004 improved their PFM system performance by 20 percent or more. As a successor to the HIPC public expenditure management indicators, the World Bank, IMF, and other donors have developed a more comprehensive set of public expenditure and financial accountability (PEFA) indicators to support diagnostics and monitoring of progress of reforms in the PFM area. The PEFA Public Financial Management Performance Measure Framework has been implemented in 68 countries, with plans for use in another 18 countries (see Box 1). Initial analysis of PEFA assessments completed to date reveal that lower-income country PFM systems tend to score as well as higher-income groups on budget credibility, comprehensiveness and transparency, policy-based budgets, accounting and reporting, and external scrutiny. However,

¹⁰¹ The seven ‘good performers’ are Burkina Faso, Ghana, Madagascar, Mozambique, Rwanda, Tanzania, and Uganda. See Annex I footnote 5 for a detailed discussion of the selection criteria. All seven countries are PRS II countries.

lower-income countries tend to score much lower on predictability and control in budget execution. Overall, all groups score relatively low on more downstream PFM system operations (predictability and control, accounting and reporting, and external scrutiny) than in the upstream areas (budget credibility, comprehensiveness and transparency, and policy-based budgets).¹⁰²

**Box 1. Public Expenditure and Financial Accountability (PEFA):
The PFM Performance Measurement Framework**

Started in 2001, PEFA is a partnership between the World Bank, the European Commission, the UK's Department for International Development, the Swiss State Secretariat for Economic Affairs, the French Ministry of Foreign Affairs, the Royal Norwegian Ministry of Foreign Affairs, the International Monetary Fund and the Strategic Partnership with Africa. PEFA aims to support integrated and harmonized approaches to assessment and reform in the field of public expenditure, procurement, and financial accountability.

The *PEFA PFM Performance Measurement Framework* provides 28 indicators covering the entire PFM cycle and is linked to six objectives—policy-based budgeting, predictability and control in budget execution, accounting, recording and reporting expenditure, external scrutiny and audit, comprehensiveness and transparency, and budget credibility. The assessment has been implemented in 68 countries and is planned for use in a further 18 countries. Repeat assessments using this tool will gradually allow tracking of PFM performance over time and have been completed or substantially completed in 4 countries, commenced in 2 countries, and planned in 10 countries.

Status of PEFA Assessments (as of July 26, 2007)

Assessments	Completed	Substantially completed	Commenced	Planned	Total assessments
Total number of assessments ¹⁰³	37	21	23	29	110
First Generation PRS (22 countries)	5	7	3	5	20 out of 22 countries
2 nd Generation PRS (18 countries)	7	4	4	1	16 out of 18 countries
Fragile States (21 countries)	2	5	2	4	13 out of 21 countries

Source: PEFA Secretariat

5. Increasingly, countries are completing PFM analysis and assessments on an annual basis. In Tanzania, Uganda, Ethiopia, Ghana, and Vietnam, analytic work is carried out annually and the content determined jointly with country officials and donors, widening the scope for leadership and improved results. For example, Ghana has improved its budget classification system and identification of pro-poor spending and introduced regular reconciliation of

¹⁰² Dorotinsky, Bill. 2007. *PFM System Performance: Early Patterns from PEFA Assessments*. Unpublished draft analysis, IMF. Analysis is based on 31 complete or near-complete country PEFA performance assessments as of November 2006 covering all regions, grouped by GDP per capita into three groups (greater than US\$2,000 per capita, between US\$2,000 and US\$1,000 per capita, and less than US\$1,000 per capita).

¹⁰³ 1st Generation PRS (22): *Albania, Armenia, Azerbaijan, Bangladesh, Bhutan, Cameroon, Cape Verde, Dominica, Georgia, Guyana, Honduras, Kenya, Kyrgyz Rep., Lesotho, Mali, Moldova, Mongolia, Nepal, Niger, Pakistan, Serbia, Sri Lanka*. 2nd Generation PRS (18): *Benin, Bolivia, Bosnia and Herzegovina, Burkina Faso, Ethiopia, Ghana, Madagascar, Malawi, Mauritania, Mozambique, Nicaragua, Rwanda, Senegal, Tanzania, Uganda, Vietnam, Yemen, and Zambia*. Fragile States (21): (PRS I): *Burundi, Chad, Congo DR, Djibouti, Guinea, Guinea-Bissau, Nigeria, Sao Tome and Principe, Sierra Leone, Timor-Leste*; (PRS II): *Cambodia, Lao PDR, Tajikistan, The Gambia*; (IPRS): *Afghanistan, Republic of Congo, Cote d'Ivoire, Haiti, Liberia*; (TRM): *Central African Republic and Sudan*. (*Italics*=completed, substantially completed, commenced, or planned). NB: Grenada, a non-fragile state with an IPRS, also has a completed PEFA assessment.

accounting and banking data (Box 2 provides a brief summary of the findings from a recent PEFA review of public financial management in Ghana.)

Box 2. Ghana's PFM System

In 2006, the annual external review of public financial management conducted in the context of the Multi-Donor Budget Support framework mainly focused on establishing a baseline to enable evidence-based monitoring of developments over time. To this effect, Ghana's PFM system was assessed against the set of indicators of the PEFA PFM Performance Measurement Framework. The key findings of the June 2006 PEFA assessment against six core PFM objectives are as follows:

- *Credibility of the Budget:* Aggregate expenditure and revenue outturns broadly match the budget plans, but credibility is diminished by variance across budget heads, reflecting weaknesses in budget formulation and the treatment of contingencies.
- *Comprehensiveness and Transparency of the Budget:* This improved considerably over the period 2004-2005, through the incorporation in the Budget Statement of information on internally generated revenues, direct donor disbursements, HIPC and statutory funds. However, in-year reporting is less comprehensive, hampering overall budget scrutiny and management.
- *Policy-based Budget:* While budgets have become more policy-based in recent years, performance is held back by limited ability to cost strategies, the lack of effective wage bill planning, and the absence of a transparent link between planned and executed budget activities.
- *Predictability and Control in Budget Execution:* Government has improved commitment and other internal controls, but recognizes weaknesses in management and oversight of control systems.
- *Accounting, Recording, and Reporting:* Predominantly a paper-based system, resulting in delays and data errors. Analytical and technical capacity constraints hamper MoFEP and MDA efforts to monitor and analyze budget performance.
- *External Scrutiny and Audit:* There is now more timely completion of accounts and financial statements and submission of audit reports to the legislature, which in turn is more actively scrutinizing both budget and accounts. However, effective follow-up on audit findings remains a question, and excessive detail of budget documents undermines effective Parliamentary scrutiny.

The 2007 external review, using the OECD/DAC methodology, confirmed that the legislative framework is the stronger pillar of Ghana's public procurement system, with implementation being the main challenge.

6. Bank research demonstrates that operations aimed at public financial management reform tend to perform well, regardless of country context. While the success of operations which focus on administrative and civil service reform and decentralization is more sensitive to governance conditions,¹⁰⁴ operations which focus on PFM reforms have a success rate of 82 percent, including 78 percent in weak governance settings. A review of PFM reforms in post-conflict countries stresses the importance of first strengthening basic central budgetary institutions (IMF 2007). For example, with World Bank support, Haiti has implemented reforms in the area of budget formulation, execution, and reporting: budgets for FY2005 onwards have been presented before the start of each fiscal year and in accordance with a new Organic Budget Law; information on key allocations and execution has been published regularly; a computerized budget management system has been expanded; and the difference between budgeted and actual expenditures has been reduced.

¹⁰⁴ Only 12 of 25 operations aimed at administrative and civil service reform and decentralization completed in the FY03-FY06 period were rated successful, with the failures concentrated in very weak governance settings.

Bank Support to Strengthening Country Institutional Capacity and Systems

7. The World Bank's Governance and Anti-Corruption (GAC) strategy aims to support the development of capable and accountable states and institutions that can devise and implement sound policies, provide public services, set the rules governing markets, and combat corruption.¹⁰⁵ Unanimously endorsed by the Board in March 2007, the strategy underscores that good governance is integral to the Bank's mandate to fight poverty. The strategy takes a comprehensive approach that involves working at the country, operational, and global levels to enhance and integrate governance and anticorruption measures. While the Bank is committed to staying engaged even in the most poorly governed settings, the GAC strategy calls for calibration of country level assistance to country realities, with the WBG adopting a consistent approach toward operational decisions across countries, systematically anchored in national strategies.

8. The strengthened GAC will help to support an agenda for scaled-up assistance. The Bank is already scaling up good governance practices and systematically integrating governance analysis into sector work. Within its mandate and with government in the lead, the Bank is also scaling up engagement with civil society, media, parliaments, and local communities in project design and supervision. It is working with the private sector and industrialized countries to tackle the supply-side of corruption, through international conventions such as the United Nations Convention Against Corruption and the Stolen Asset Recovery (StAR) initiative. The Bank is working with donors and other international partners to ensure a harmonized approach and collective action, based on respective mandates and comparative advantages.

9. Recent Bank initiatives demonstrate a strong commitment to strengthening governance across institutional contexts, while working with a variety of development partners. The Africa Action Plan (AAP) establishes "building capable states" as one of four strategic pillars guiding the Bank's work in Africa, while the recent Capacity Development Action Plan highlights the Bank's core competencies in both good performers and fragile states (Box 3). In the Africa region alone, the Bank is working with the AfDB, DFID, the EU, AFD, Germany's GTZ, the IMF, Norway, and USAID on capacity building. Bank-Fund collaboration in public financial management is anchored in the principles of: (a) government articulation of a public expenditure reform strategy in the Poverty Reduction Strategy Process or other country-owned work; (b) an integrated and well-sequenced program of diagnostic work by development partners; (c) well-coordinated technical and financial support from development partners for implementation of the country's public expenditure reform strategy; and (d) periodic reporting by countries of performance in public expenditure policy, financial management and procurement.¹⁰⁶

10. The World Bank is the leading donor globally in providing support for strengthening public sector management. In FY07, WBG support to governance was \$3.8 billion – \$3.4 billion for public sector governance, and \$424 million to support improvements in the rule of law. This comprised 15.5 percent of total Bank lending. The principal areas of support included public financial management, public finance policy, public administration, decentralization, legal and judicial reform, and anticorruption strategies. Public Financial Management reforms represent

¹⁰⁵ World Bank. 2007. *Strengthening World Bank Group Engagement on Governance and Anticorruption*, (R2007-0036/2, March 21).

¹⁰⁶ World Bank and IMF. 2003. *Bank/Fund Collaboration on Public Expenditure Issues*, (SecM2003-0077, February 14).

the dominant part of the Bank's public management portfolio and PFM conditions account for more than half of the public sector governance conditions and benchmarks in development policy lending to IDA countries. Among the numerous lending activities in the area of governance, the Bank has supported Rwanda's Public Sector Capacity Building project, which targets public expenditure management and procurement, public sector reform, and national M&E systems, and Tanzania and Mozambique's Public Service Reform projects, which aim to improve capacity for service delivery.

Box 3. Africa Region's Capacity Development Management Action Plan

The Africa Region's action plan to support capacity development—the CDMAP—was launched in July 2006. It was based on extensive consultations with African governments, civil society, and the private sector. CDMAP emphasizes delivering results by creating space for learning by doing, supporting domestic accountability mechanisms, and avoiding supply-driven initiatives. It embodies 20 actions focused on five goals and outcomes: (i) more reliable and accountable public financial management systems, (ii) improved capacity for effective delivery of public services, (iii) better and more appropriate skills to support growth and competitiveness, (iv) capacity to deliver essential services in post-conflict countries, and (v) improved capacity for country leadership through more effective management and monitoring for results.

CDMAP covers 43 countries and a wide range of sectors. The Bank will scale up its support for capacity development from 22 percent of its portfolio at the end of FY05 to 38 percent by the end of FY08. IDA expects to allocate \$3.2 billion to capacity development over FY06 to FY08. Actions will be undertaken selectively where they can get the best results. There are a handful of countries (for example, Burkina Faso and Tanzania) where strong government ownership and good donor coordination support significant broad-based progress in capacity development. In some areas, such as public financial management, mutual accountability between governments and their development partners is beginning to result in more effective (sequenced, coordinated, country-specific) capacity development plans. CDMAP seeks to replicate these examples more broadly.

Source: World Bank. 2007. *Accelerating Development Outcomes in Africa: Progress and Change in the Africa Action Plan*. Development Committee paper (DC2007-0008, March 29).

11. World Bank support is associated with country PFM improvement. Countries with improved PFM performance between 2002 and 2004 according to HIPC expenditure tracking assessments received about one and a half times more IDA lending on average than those with declining PFM performance. More striking, comparing HIPC countries that improved by two or more benchmarks with those that declined by two or more shows improving countries received nearly twice as much lending and one-fifth more AAA.

12. There is an increasingly broad array of diagnostic and analytic work in public sector governance that helps build capacity and increase ownership of the reform agenda.¹⁰⁷ To

¹⁰⁷ At the country level, *Development Policy Reviews* and *Investment Climate Assessments* help identify some of the more binding constraints to development. *Institutional and Governance Reviews* help uncover some of the political and institutional drivers of these obstacles, while *Governance and Anticorruption Diagnostic Surveys*, *Doing Business*, *Anticorruption in Transition*, and WBI's *Worldwide Governance Indicators (WGI)* document and benchmark specific forms of weak governance and corruption and serve as an input to action plans. Public financial management (PFM) analytic work such as a *PFM Performance Report* using the Public Expenditure Financial Accountability (PEFA) program framework—and where appropriate, the institutional aspects of *Public Expenditure Reviews (PERs)*, *Country Financial Accountability Assessments (CFAAs)*, *Country Procurement Assessment Reports (CPARs)*, and the IMF's fiscal modules of the *Reports on Observance of Standards and Codes (ROSCs)*—can help assess and identify strengths and weaknesses of the country's public financial management system. The Department of Institutional Integrity's (INT) investigative findings and Detailed Implementation Reviews can help identify specific country or sectoral fiduciary risks. Sector-specific diagnostics are currently under development.

streamline diagnostic work, the Bank is increasingly focusing on integrated assessments that assess public expenditure, financial accountability, and procurement systems (Table 1).

Table 1. PERs and Integrated Assessments Delivered in FY 2001-2006

Assessments	2001	2002	2003	2004	2005	2006	Total
PER	11	25	20	29	21	34	140
Integrated Assessments	1	7	2	3	7	18	38
of which:							
PER-CFAA-CPAR		1	1	1	1	11	
PER-CFAA	1	5	1	2	3		
PER-CPAR						1	
CFAA-CPAR		1			3	6	
Total	12	32	22	32	28	52	178

Source: World Bank

ANNEX IV IMPROVING THE DELIVERY OF AID

A. Introduction

1. Donors have committed to more and better aid in a number of international fora. At Gleneagles (2005), the Group of Eight pledged to increase aid to Sub-Saharan Africa by \$25 billion a year by 2010—a doubling of aid to the region—and donors also agreed to increase aid by another \$25 billion elsewhere. This builds on the earlier commitment by the international community in the 2002 Monterrey Consensus to scale up aid resources to developing countries. Along with pledges of higher aid volumes, donors and partner countries alike are focused on improving the effectiveness of aid through better alignment, harmonization, and coordination. This commitment to enhance the quality of aid is embodied in the 2005 Paris Declaration, which builds on the Rome Meeting of 2003.

2. This annex assesses the recent progress on scaling up the quantity and quality of aid. It reviews whether donors are providing more aid, especially to countries with demonstrated potential to use increased resources effectively, and whether aid is becoming more predictable and long term. It also presents progress on the harmonization and alignment agenda, and addresses the special challenge presented by a changing aid architecture—proliferation of aid channels, substantial degree of earmarking, and fragmentation—to donors and partner countries.

B. Progress on Scaling Up Aid Volumes is Mixed

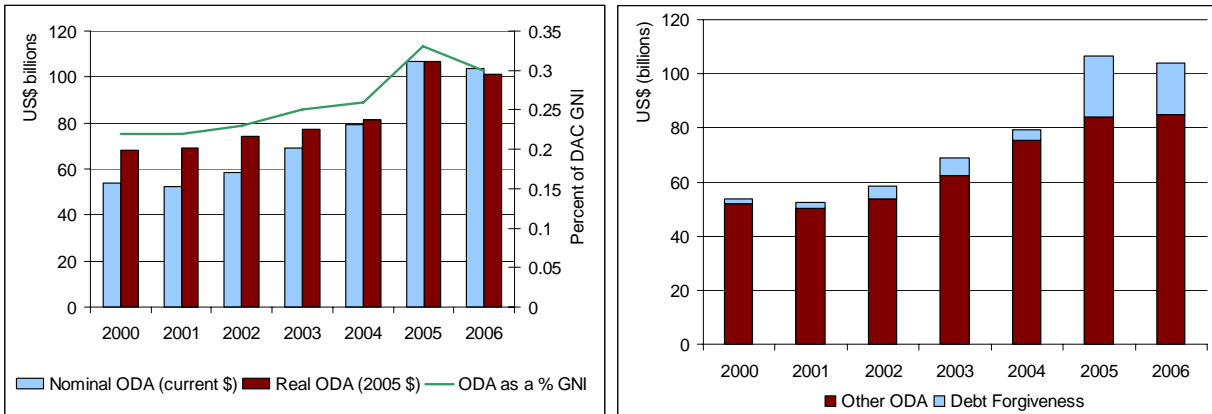
Recent Trends in ODA

3. Nearly two years after Gleneagles, there is little evidence that donor promises are translating into actual increases in aid. Aid from Development Assistance Committee members edged lower in 2006 to \$103.9 billion, falling 5.1 percent in real terms, and is projected to decline slightly in 2007. This recent pull back has halted the expansion in DAC members' ODA, which has grown by 30 percent (in nominal terms) in 2004-06 and has nearly doubled since 2001 (Figure 1). The expansion in real terms has been more moderate at 46 percent in 2001-06, representing an average annual increase of 7.7 percent. The change in ODA varies considerably by donor (Table 1). Over this same period, the share of ODA in donors' combined gross national income (GNI) climbed from 0.22 percent to 0.33 percent before falling to 0.3 percent, but remained below the level of the early 1990s.

4. Although a stepped up focus on aid post-Monterrey has boosted aggregate aid levels since 2001, a substantial amount of the expansion in ODA is due to higher amounts of debt relief. For example, the jump in ODA in 2005 of \$27.3 billion and the subsequent pull back were driven by debt relief operations. Exceptional debt relief to Iraq and to Nigeria boosted net debt relief grants to \$22.7 billion in 2005, an increase of \$18 billion over 2004 levels. These grants fell off in 2006 to \$19.2 billion, but still represented a substantial share (nearly a fifth) of ODA; by contrast, net debt relief grants comprised less than 5 percent of ODA in 2000-01. ODA for core development programs—that is, ODA excluding debt relief, humanitarian aid, and administrative costs—

accounted for about 70 percent of net ODA in 2006.¹⁰⁸ A winding down of debt relief operations in the near term will impact ODA flows, including in 2007. Other categories of net ODA will have to expand very rapidly in 2008-10 if donor promises of an additional \$50 billion in annual aid (over 2004 levels) are to be met. This is prompting concern that donors may fail to deliver on their aid promises.

Figure 1. Trends in Nominal and Real ODA



Source: OECD-DAC database.

5. Although aid by DAC donors has stalled, a wide range of other donors—official and private—are stepping up their assistance to developing countries. ODA from non-DAC reporters (non-DAC countries that report aid flows to the DAC) has more than doubled in real terms during 2001-05, and is set to rise further: Saudi Arabia and other Arab countries provided \$1.4 billion in assistance in 2005 and the Republic of Korea and Turkey \$750 million and \$600 million, respectively. And emerging market donors, particularly China, are becoming more important providers of official support to poor countries. The Chinese government has provided an estimated \$5.7 billion in aid to Africa through May 2006.¹⁰⁹ The country has also pledged to double its assistance to Africa by 2009 (that is, over 3 years).¹¹⁰ Private giving through foundations, charities, and other nongovernmental organizations has grown briskly, more than doubling over 2001-05 and reaching \$14.7 billion in 2005.

¹⁰⁸ Debt relief from the donors' perspective—budget effort—can be quite different from that of the recipients' perspective—availability of resources (debt relief represents additional financial resources for recipients if debt is being serviced, but amounts to an accounting exercise if it is not). Hence, one important question that arises is whether ODA debt forgiveness grants represent additional flows (cross-border flows) to recipients. At Monterrey, donors pledged that debt relief would not displace other components of ODA.

¹⁰⁹ This does not include debt relief estimated at \$1.5 billion that the country has also provided to the region. See Wang, Jian-Ye. 2007. "What Drives China's Growing Role in Africa?" IMF Working Paper WP/07/211.

¹¹⁰ This includes setting up a \$5 billion China-Africa development fund to promote investment by Chinese companies in Africa and \$5 billion in loans and credits to the region. China has also pledged to cancel large amounts of debt that are owed to it by the poorest African countries. Taylor, Darren. 2007. "Chinese Aid Flows into Africa" Voice of America 08 May 2007 available at www.voanews.com/english/archive/2007-05/Chinese-Aid-Flows-into-Africa.cfm?CFID=172438641&CFTOKEN=30119561.

Table 1: ODA by Donor, 2001-06

	Net ODA (Constant 2005 US\$ millions)			Net ODA as percent of GNI
	<u>2001</u>	<u>2005</u>	<u>2006</u>	<u>2006</u>
DAC Donors				
Australia	1,477	1,680	2,062	0.30
Austria	937	1,573	1,479	0.48
Belgium	1,302	1,963	1,911	0.50
Canada	2,175	3,756	3,411	0.30
Denmark	2,487	2,109	2,171	0.80
Finland	552	902	812	0.39
France	6,290	10,026	10,164	0.47
Germany	7,201	10,082	10,175	0.36
Greece	322	384	369	0.16
Ireland	451	719	961	0.53
Italy	2,527	5,091	3,563	0.20
Japan	10,262	13,147	11,884	0.25
Luxembourg	221	256	269	0.89
Netherlands	4,784	5,115	5,329	0.81
New Zealand	204	274	274	0.27
Norway	2,175	2,786	2,725	0.89
Portugal	420	377	379	0.21
Spain	2,835	3,018	3,631	0.32
Sweden	2,445	3,362	3,866	1.03
Switzerland	1,270	1,767	1,642	0.39
United Kingdom	6,441	10,767	12,177	0.52
United States	12,583	27,622	22,092	0.17
Total DAC	69,360	106,777	101,347	0.30
Non-DAC Donors*	1,646	3,905	n.a.	n.a.

* Non-DAC donors that report to the DAC. These include Czech Republic, Hungary, Iceland, Korea, Republic of, Kuwait, Poland, Saudi Arabia, Slovak Republic, Turkey, United Arab Emirates, and a few other donors.

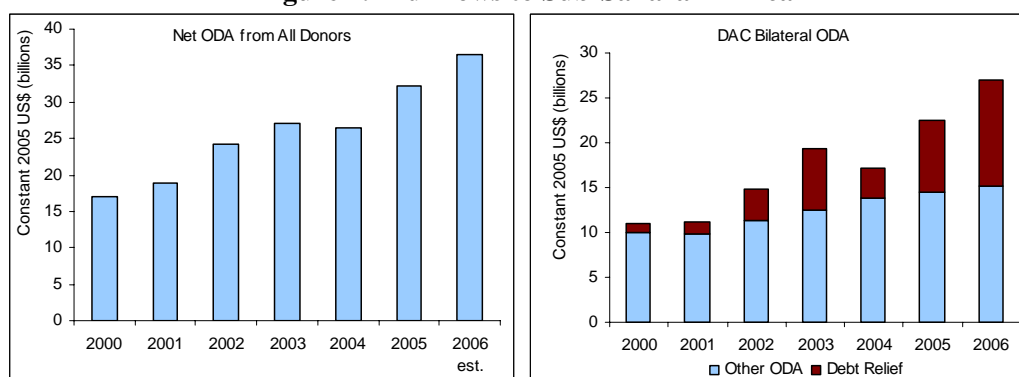
n.a. is not available.

Source: OECD-DAC database.

Aid to Sub-Saharan Africa: Actions Lag Promises

6. The G-8 promises at Gleneagles of a scale up of aid to Africa have yet to translate into additional resources for the region. Although bilateral donors are providing larger amounts of aid to the region and are allocating a larger share of ODA to Sub-Saharan Africa—a third in 2004-05 compared to about a quarter in 1999-2000—much of the increase represents debt relief grants. For example, bilateral net ODA from DAC members rose by 23 percent to \$28 billion (preliminary) in 2006; debt relief grants accounted for over three-quarters of this increase. The increase in ODA excluding these grants was about 5 percent. During 2005-06, debt relief grants averaged about 40 percent of bilateral aid. These grants also helped boost overall aid flows to the region to an estimated \$37 billion in 2006, from \$32 billion in 2005. The prominence of debt relief in aid flows is evident since 2001: net ODA in real terms (2005 dollars) more than doubled to the region over 2001-06, but close to 70 percent of the expansion represented debt relief (Figure 2).

Figure 2. Aid Flows to Sub-Saharan Africa



Source: OECD-DAC database and authors' estimates.

Aid to Strong Performers: Is There Evidence of a Scale Up?

7. Although a range of reforming countries is well positioned to absorb more aid, the scaling up of support from development partners to these countries has been limited. Several country groups are identified. One group is comprised of the second generation poverty reduction strategy countries or PRS-II countries—countries where the strengthening of the strategic and institutional framework for scaling up development results is adequately advanced to merit an early delivery on donor commitments to double aid. Among the PRS II countries, Burkina Faso, Ghana, Madagascar, Mozambique, Rwanda, and Tanzania were initially singled out for scale-up efforts by the OECD-DAC and the Bank. These countries are referred to as the group of 6 strong performers. Another group is comprised of 22 first generation poverty reduction strategy countries—PRS-I. For these countries, performance on country ownership, prioritization and sequencing, PRS-budget links, and monitoring and evaluation typically lags that of the PRS-II group.¹¹¹ The fragile state group consists of 21 countries that are classified as fragile based on their CPIA ratings.¹¹² The extent of scaling up of aid in these groups is measured in terms of ODA volumes, size of aid relative to GDP, and per capita aid levels. All measures yield similar results.

8. Despite a doubling of overall nominal net ODA during 2001-05, the increase in ODA varies widely across the country groups (Table 2). The fragile states group saw the largest increase as their ODA volumes rose by over 400 percent. By contrast, the expansion of aid in strong performers was more muted with the 6 strong performers seeing an increase of 56 percent and other PRS-II countries recording only a 28 percent increase. The expansion in real ODA was likewise largely concentrated in fragile states. At 14 percent, the 6 strong performers again saw larger increases than the other non-fragile state groups, some of which actually saw a decline. The 6 strong performers also saw a larger expansion in ODA for core development programs than other groups.

¹¹¹ See annexes 1 and 3 for the performance of these groups across various measures of PRS quality and governance.

¹¹² This group is a sub-set of countries classified as fragile based on CPIA scores.

Table 2. Where Did Aid Flows Go?

	Nominal net ODA by recipient (current US\$ millions)			Change 2001-05 (in %)	Real ODA by recipient (constant 2005 US\$, millions)			Change 2001-05 (in %)
	2001	2004	2005		2001	2004	2005	
All IDA/Blend	28,470	39,907	50,746	78	38,053	40,817	50,746	33
PRS-I	8,787	9,942	10,592	21	11,546	10,141	10,592	-8
PRS-II (excl. 6 Strong Performers)	7,809	11,045	9,994	28	10,607	11,268	9,994	-6
6 Strong Performers	3,903	6,720	6,076	56	5,348	6,867	6,076	14
Fragile States	3,405	8,904	17,766	422	4,686	9,115	17,766	279
Other countries	4,567	3,297	6,319	38	5,865	3,427	6,319	8
Memo: 6 Strong Performers								
Burkina Faso	390	614	660	69	544	627	660	21
Ghana	641	1,362	1,120	75	873	1,387	1,120	28
Madagascar	374	1,248	929	149	504	1,274	929	85
Mozambique	931	1,246	1,286	38	1,308	1,279	1,286	-2
Rwanda	299	488	576	93	412	499	576	40
Tanzania	1,269	1,761	1,505	19	1,707	1,801	1,505	-12

Note: Excludes countries with populations under 1 million.

Source: OECD-DAC database.

9. Evidence of scaling up of aid is even less widespread when measured in terms of ODA to GDP and aid per capita. The only country group to show any appreciable increase in these two indicators is fragile states. For this group, the aid to GDP ratio rose by 5 percentage points. Fragile states' aid per capita figures also saw a strong increase.

10. While the data suggest that the development community's focus on fragile states is beginning to translate into increased assistance, these results have to be interpreted cautiously. For one thing, debt relief and humanitarian relief account for a substantial amount of this increase. For another, these aggregate trends mask the wide variation across different groups—aid “darlings” and aid “orphans.” Large increases in aid have been concentrated in Afghanistan, Democratic Republic of Congo, Nigeria, and Sudan, while some other fragile states have seen modest changes or even a decline in aid volumes.

11. Although recent trends point to a somewhat positive picture regarding the increase in aid to the 6 strong performers, there is substantial variation across these countries. Within this group, Madagascar and Rwanda have seen a substantial scale-up of aid: in Madagascar, aid rose by 85 percent in real terms and ODA relative to GDP increased by 10 percentage points; Rwanda saw a similar increase in its ODA to GDP ratio, as aid flows grew by 40 percent in real terms. Ghana and Burkina Faso also received more aid, but ODA relative to GDP was practically unchanged. By contrast, Tanzania and Mozambique actually saw a decline in real ODA.

12. The trend in the composition of aid to the 6 strong performers is favorable. The share of flexible ODA (ODA less humanitarian relief, debt relief, and technical cooperation) is rising in these countries. These countries are also seeing larger amounts of budget support—15 percent of aid—as compared to 4 percent in other Sub-Saharan African countries.

13. Looking ahead, what are the prospects of a scaling up aid to these 6 strong performers? Many of these countries have adopted ambitious growth-oriented development strategies that are receiving support from donors. Ghana is a promising example of where development partners are

responding positively to the country's program for accelerating growth. There is a strong likelihood that ODA will expand from an estimated \$1.4 billion in 2006 to about \$2 billion a year over 2007-09 (including debt relief). Tanzania could also see a scale-up of resources in the context of the country's joint assistance strategy.

C. The Reliability of Aid Resources Remains Problematic

14. Evidence from recent studies indicates that both volatility and predictability of aid remain problematic, although welcome signs of change are appearing. For example, the March 2005 Paris Declaration, which was signed by over 100 recipient countries and donors, emphasizes that aid predictability is a key dimension of improving the effectiveness of aid, and the declaration includes an indicator for measuring progress in this area. A few donors have moved to greater transparency in aid allocations and to providing forward commitments in multi-year frameworks. Donors have also asked the DAC to undertake monitoring surveys to collect 3-year forward projections on aid at the country level. Despite the international community's recognition of the need for more stable and reliable flows, donor progress in implementing practices aimed at improving aid predictability is slow.

Trends in Aid Volatility and Predictability

Aid Volatility

15. Donor reported data show substantial annual fluctuations in ODA disbursements.¹¹³ The average annual absolute change in real ODA (gross disbursements less debt relief, emergency aid, and food aid) in 2000-05 is under 20 percent for all low-income countries (Table 3).^{114, 115} Low-income countries in Sub-Saharan Africa have experienced the highest yearly change in aid at 21.2 percent. There is wide variation across African countries, however. Top performers (as measured by the CPIA) experience uncertainty in aid receipts, but to a lesser degree than other countries. For example, the average annual absolute change in ODA is 15.1 percent for the 6 strong performers and 11.3 percent for other top African performers.

16. ODA relative to GDP also shows large variation. During 2001-05, the annual change in ODA to GDP was within ± 10 percent of the previous year's level for about 28 percent of cases. That is, in just over a fourth of cases this indicator was within 90 percent to 110 percent of the previous year's level. But nearly three-quarters of the time the variation in ODA to GDP was outside of this range, indicating a low level of certainty of aid from one year to the next.

¹¹³ The variability of aid is measured by comparing the absolute values of percentage changes in annual disbursements of real gross ODA. Because some types of aid are expected to be more uncertain as they are a response to natural disasters or economic and social crises, these are excluded from the analysis. Thus, the focus here is on gross ODA disbursements less emergency and food aid and debt relief.

¹¹⁴ Results are for low-income countries with aid/GDP of 5 percent or more.

¹¹⁵ Using the Hodrick-Prescott filter technique to smooth the time series lowers the volatility of aid, but does not affect the conclusion that aid is uncertain. The H-P filter pays more attention to long-run fluctuations and is less sensitive to short-term fluctuations. Bulir and Hamann use this technique to smooth the time series for both aid and government revenues. Bulir, A. & A. J. Hamann. 2006. "Volatility of Development Aid: From the Frying Pan into the Fire?" IMF Working Paper No 06/65.

Moreover, the number of cases where countries experienced a decline in ODA to GDP from the previous year exceeded the number of cases where it rose.

Table 3. Aid Volatility in Low-Income Countries, 1980-2005

Average year-to-year percentage absolute change in real ODA (gross disbursements less debt relief, emergency aid, and food aid); data are for LICs where ODA/GDP is 5 percent or more.

	1980s	1990s	2000-05
Sub-Saharan Africa	19.7	22.3	21.2
6 Strong Performers	15.3	19.4	15.1
Other top African performers	18.8	12.3	11.3
Other African LICs	21.4	25.6	25.6
All other regions	22.8	46.4	17.5

Note: Top performers are countries in the top tercile of the overall CPIA score within the group of African LICs.

Source: OECD-DAC database and authors' estimates.

Aid Predictability

17. The predictability of aid is the gap between expected and realized amounts of aid, where expected amounts could be announced commitments or projections based on best information on donor intentions.¹¹⁶ Empirical findings based on donor reported data, recipient information from IMF staff reports, and surveys (Strategic Partnership with Africa and the Paris Declaration) suggest that aid predictability is low.¹¹⁷ However, there is also evidence that aid predictability is improving. This improvement is confined to aid in the near term, and medium-term aid resources remain unpredictable.

18. Donor reported data indicate that the absolute deviation of aid commitments from disbursements is substantial, but that the size of deviations has declined in recent periods.¹¹⁸ There is considerable country-level variation in aid predictability. In Sub-Saharan Africa annual aid disbursements deviated from commitments by an average of 2.2 percent of GNI in 1991-2000 and by 0.9 percent in 2001-05 (Table 4).¹¹⁹ Several factors could explain the lack of predictability—both aid shortfalls and excesses of commitments over disbursements. The contributing factors on the donor side include administrative delays, revisions of aid allocation, and political considerations. The way donor budgets are approved and administered also contributes to the unpredictability of aid. The donor agencies that make commitments are different from the institutions that make funding decisions (parliaments) and those that disburse (ministries of finance). This disconnect is widespread, although there is country variation. On the

¹¹⁶ The recent literature measures predictability in two ways: (i) do donors deliver on their own aid promises as measured by the deviation between donors' reported commitments and disbursements; and (ii) the forecasting error of budget aid disbursements based on aid projections and outruns from IMF programs or government PRSPs.

¹¹⁷ Strategic Partnership with Africa. 2006. *Joint Evaluation of General Budget Support 1994-2004*, developed under the auspices of the DAC Network on Development Evaluation. OECD/DAC. 2007. *2006 Survey on Monitoring the Paris Declaration*. Paris, France: OECD.

¹¹⁸ Commitments in the OECD-DAC database are new resources available for disbursements. Since some commitments are associated with multi-year disbursements, commitment data should be viewed as only being indicative of likely disbursements during a period

¹¹⁹ See Celasun, Oya and Jan Walliser. 2007. *Predictability and Procyclicality of Aid: Do Fickle Donors Undermine Economic Development*. Paper presented at the 46th Panel Meeting of Economic Policy in Lisbon, (June 1). They find that commitments are good at predicting disbursements, but the coefficient is not equal to 1. Some countries report disbursements as commitments which could affect this result.

recipient side failure to meet conditions attached to disbursements or slippage on project implementation can impact predictability.¹²⁰

19. Recipient side data are needed to assess the gap between aid projections and disbursements. Drawing on data from IMF staff reports for 1992-07 for 13 countries, Cellasun and Walliser estimate the average mean absolute forecasting error of budget aid disbursements to be over 1 percent of GDP during 1993-2005.¹²¹ This figure is high because budget aid is 3 percent of GDP on average: thus, one third of budget aid is unpredictable. However, excess aid and shortfalls almost even out over time, so that disbursed aid on average differs from projected aid by 0.2 percent of GDP. Predictability has improved in recent years: a recent IMF report (2007) finds that projections of next-year aid inflows have become more accurate.¹²² While earlier Fund-supported programs tended to underestimate aid due to overly cautious aid projections, recent programs carry more accurate forecasts and lower projection errors.¹²³

Table 4. Trends in Aid Predictability, Bilateral Gross ODA

	1991-2000			2001-2005		
	Gross disbursements/ GNI	Commitments minus disbursements to GNI	Absolute value of commitments minus disbursements to GNI	Gross disbursements/ GNI	Commitments minus disbursements to GNI	Absolute value of commitments minus disbursements to GNI
Sub-Saharan Africa	10.4	-1.2	2.2	8.9	0.0	0.9
SSA LICs	12.3	-1.3	2.4	11.2	0.0	1.1
6 Strong Performers	15.0	-1.2	2.0	11.6	0.2	1.0
Burkina Faso	10.4	-0.8	1.4	7.3	0.4	0.9
Ghana	6.3	0.1	0.6	10.4	0.0	0.6
Madagascar	9.2	-1.6	1.8	8.8	0.5	0.9
Mozambique	32.9	-4.0	4.7	21.6	-0.4	1.9
Rwanda	18.5	-0.6	2.4	12.2	0.3	0.9
Tanzania	12.8	0.0	1.2	9.4	0.4	0.6
Other IDA Countries	7.7	0.3	2.1	7.3	0.6	1.9

Note: Data are for IDA eligible countries. Commitments are new resources available for disbursements. Since some commitments are associated with multi-year disbursements, commitment data should be viewed as only being indicative of likely disbursements during a period.

Source: OECD-DAC database and authors' estimates.

20. The 2006 baseline survey on monitoring the Paris Declaration spotlights the state of play regarding aid predictability: the percent of donors' aid disbursements released according to agreed schedules in annual or multi-year frameworks and the accurate recording by partners of donors' aid disbursements to the government sector. The survey finds that \$19.9 billion of the \$21.1 billion that donors scheduled for disbursement was actually disbursed in 2005. Yet, the amount recorded by partners was only \$14.8 billion—that is, 70 percent of scheduled disbursements (a 30% gap) and 75 percent of actual disbursements. Under-recording is

¹²⁰ Cellasun and Walliser (*Idem*) find that predictability increases with the number of years a country has implemented an IMF program (or successive IMF programs). The result suggests that sustained implementation of IMF programs signal a country's commitment to stable macroeconomic management, and donors respond by providing more predictable aid.

¹²¹ Cellasun and Walliser. *Idem*.

¹²² IMF (2007). *Aid Inflows—the Role of the Fund and Operational Issues for Program Design*.

¹²³ Despite evidence of substantial unpredictability of aid, Strategic Partnership with Africa. 2006. *Idem* – a survey of budget support by 20 donors in 15 African countries – finds that in recent years donors are disbursing more of their general budget support commitments in-year, although there has been some slippage in 2005/06 with in-year disbursements falling to 82.8 percent of commitments from 87.1 percent in 2004/05.

commonly observed in almost all countries; in 8 of the 34 countries, the gap in recording was more than 50 percent. This pattern of under-recording could be due to the inability of government systems to capture and process this information, due to inappropriate notification processes on the part of donors, or because projects may not be included in the budget.

21. To facilitate the process of scaling up, donors agreed in 2005 that the DAC undertake an effort to collect information on three-year forward projections of aid at the country level. By providing information on resource availability at the country level over the next few years, donors would improve transparency in aid allocations, better coordinate aid, and enhance predictability of resource flows. The first such monitoring exercise took place in 2006. The results were weak—coverage was only 27 percent of aid flows—reflecting the challenge donors face in providing 3-year forward projections at the country level.

22. The 2006 SPA survey results also point to the limited availability of donors' forward commitments of budget support. Although recipient governments place a high priority on multi-year commitments, both SPA general budget support and SPA sector support surveys suggest that medium-term commitments and programs by donors decline in outer years. Donor commitments in signed formal agreements or in announced agreements for 2006-08 are lower by 40 percent in value and by more than half in terms of the number of programs. Ninety percent of donors that had committed general budget support in 2005 made a firm commitment for 2006, but this proportion dropped off to 67 percent for 2007. The pattern of medium-term commitments is similar for sector budget support. Given the incompleteness and uncertainty of donors' forward commitments, it is not surprising that an IMF IEO report (2007) concluded that projections of medium-term aid underestimated aid flows.

Improving the Predictability of Aid

23. The recognition that 'business as usual' will not work and that newer mechanisms are needed to ensure predictable and stable flows that are aligned as much as possible to a country's long-term development strategy, is prompting change.

24. For example, the DAC is following up its 2006 exercise on future aid allocations with a more focused monitoring effort. This year's aid allocation work attempts to address some of the constraints to donor predictability. A key constraint is that although donors are increasingly discussing 3-4 year forward spending plans with partners, the reality of budget mechanisms poses a challenge—aid budgets have an annual cycle and are subject to parliamentary approval, which can lead to adjustments in planned spending.¹²⁴ Another factor that has a bearing on predictability is that multi-year programming may not cover all components of ODA or all partners. Given the reality of donors' budget processes, the DAC's approach to collecting indicative spending plans is focused on collecting information on future flows of programmable aid only (as opposed to all aid) at the country level. The approach also focuses on estimating a range of possible financing paths for each recipient country based on a wide range of future aid scenarios. The idea is for donors to use these scenarios to inform their aid allocations.

¹²⁴ OECD-DAC. 2007. *Scenarios of Future Aid Flows: DAC Technical Meeting on Aid Allocations and Scaling Up for Results* (DCD/RD(2007)5/RD2, June 15); and OECD/DAC. 2007. *Methodology for the DAC 2007 Survey of Aid Allocation Policies and Indicative Spending Plans* (DCD/RD(2007)5/RDI, June 11).

25. The EC has adopted mechanisms to make aid more predictable. One of these is the graduated response to aid delivery. Within the framework of the PRS, the EC's general budget support (GBS) provides fixed and variable tranche disbursements. While the fixed tranche component is a traditional aid modality linked to conditionality, the variable tranche provides resources in a graduated form dependent upon the achievement of agreed targets and indicators. The variable tranche usually has two sub-tranches: one is linked to satisfactory management of public finances and the other to a set of agreed poverty reduction indicators. Several donors, including the Netherlands, Sweden, and the United Kingdom, are showing interest in the EC's graduated response approach.¹²⁵

26. The EC has also launched a proposal—the *MDG Contract*—to make its GBS more long term and predictable.¹²⁶ It is not a new EC financial mechanism, but rather an enhanced form of GBS for implementation under the 10th European Development Fund, which will provide €22,682 million over the period 2008–13. The proposed features of the MDG contract include a six year time horizon, a virtually guaranteed minimum level of support, annual monitoring with a focus on results, and a performance assessment in a multi-annual framework that takes into account previous performance and future prospects. The MDG contract will be targeted at countries with a strong track-record of implementing GBS, a medium-term framework for assessing performance, and substantive PFM reforms.

27. Consultative Group and Roundtable meetings and formal mutual accountability reviews of progress are important mechanisms for promoting more predictable and long-term financing from donors. Ghana is using a revamped CG process—Results, Resources, and Partnership (RRP) process—built on the aid effectiveness principles of the Paris Declaration to link funds to ambitious country-owned strategies and development results. The June 2007 Ghana Consultative Group Annual Partnership meeting drew strong donor support for the country's development strategy. In Tanzania, a similar process emerged from the merging of the CG Meetings, the Annual Public Expenditure Review Consultative meeting, and the PRSP Annual Review meeting.

28. The United States' Millennium Challenge Account (MCA) is designed to provide larger, more predictable, and longer term commitments to countries which qualify for its funding. Countries are eligible for MCA funding based on their demonstrated commitment to sound policies and good governance. MCA selects recipients based on policy and institutional changes that have already been implemented. Funding tranches are linked to specified results and not future policy changes. Each recipient government works with the Millennium Challenge

¹²⁵ A recent study (Gelb, A and B Eifert. 2005. "Improving the Dynamics of Aid: Towards more Predictable Budget Support" World Bank Policy Research Working Paper No 3732) suggests a practical way of addressing the issue of budget aid predictability. It recommends applying performance-based allocation rules with a flexible pre-commitment rule, such that aid levels adjust sharply only in response to major performance changes. This mechanism would allow for pre-commitment of aid in a multi-year framework while avoiding drawn-out periods of misallocation. In addition, donors could fund a country's reserve holdings—that is a buffer reserve fund of 2-4 months of imports—so that the reserves could cushion a shortfall in disbursements arising from exogenous factors unrelated country performance.

¹²⁶ European Commission. 2007. *Technical Discussion Paper on a "MDG Contract" – A Proposal for Longer-Term and More Predictable General Budget Support* (June 19).

Corporation (MCC), which administers the MCA, to plan and negotiate a multi-year agreement (compact) of about 4-5 years on how to use a specified amount of money. Each agreement includes a disbursement schedule for the entire time span of the agreement. Disbursement is not subject to the U.S. Congressional appropriations process because compacts are signed only after enough money is appropriated to the MCC to cover the cost for all years of the compact. Disbursements are also not conditional on implementing future reforms, but are subject to the recipient's compliance with specific procurement policies or mutually agreed conditions, including maintenance of good governance. These aspects of the MCA are designed in part to increase the predictability of aid.

29. Innovative financing initiatives can also foster greater aid predictability. The pilot International Finance Facility for Immunization, which issued its first \$1 billion bond last November, will provide up to \$4 billion in funds to support immunization over its 20-year life. The air ticket levy will generate continuing aid flows. The pilot Advance Market Commitment for vaccines against pneumococcal diseases offers assured financing to subsidize the price of target vaccines, coupled with undertakings from participating manufacturers to provide sustainably priced vaccines over the long term.¹²⁷ Various private entities have also proposed a wide range of innovative financing mechanisms. Innovation should be encouraged not for its own sake, but to solve specific problems, and with an awareness of the risks and costs of aid fragmentation. In particular, further exploration is needed of initiatives designed to spur more predictable and effective aid flows, that address market gaps or failures, that provide new financing for global and regional public goods, and that mobilize funds through public-private partnerships.

D. Accelerating Progress on Alignment and Harmonization

30. Improving aid delivery is central to scaling up development results. The 2005 Paris Declaration, which builds on the Rome Meeting of 2003, embodies the international community's commitment to increasing the effectiveness of aid. Partner countries, donors, and the IFIs are taking substantial actions toward meeting the Paris commitments. Much has been achieved in implementing this agenda at the international level, within donor institutions, and most importantly at the country level, where harmonization and alignment activities have engaged all development partners. But the breadth and depth of actions is varied among countries. It is clear that development partners and donors will need to continue focusing on this agenda and make appropriate changes in practices, processes and procedures to achieve the intended development impact.

Progress on Alignment and Harmonization: Building on the Momentum for Change

Donor and Developing Country-Level Actions

31. Following the adoption of the Paris framework in 2005, donors have taken a broad range of actions to disseminate the agreed commitments. Two-thirds of DAC donors have included the

¹²⁷ Six donors—Italy, the United Kingdom, Canada, Russia, Norway, and the Bill and Melinda Gates Foundation—have pledged \$1.5 billion in commitments to the first pilot Advance Market Commitment.

Paris Declaration as a strategic priority in official statements, indicating political ownership.¹²⁸ Many donors have also developed action plans for implementing the Paris framework.¹²⁹ But implementing the Declaration involves a broad and complex process of change. Donor agencies are organizing to strengthen internal processes. They are also making some progress on improving internal incentive systems—both at the institution and individual level—so as to make them more compatible with a sharpened focus on harmonization, alignment, and results.¹³⁰ The Paris Declaration sets out the principle that implementation should take place at country level. However, fewer than one-third of donors report progress on decentralization.

32. The Bank and other multilateral development banks are reflecting their commitment to the Paris Declaration by improving the effectiveness of their own programs, as well as pushing for greater collective implementation of the Paris principles throughout the donor community. In a number of areas substantial actions are being taken. The MDBs have undertaken efforts to harmonize their procedures, strengthen country systems where necessary, and align with these systems where possible. Also, there is an increasing use of joint or collaborative country assistance strategies to harmonize country diagnostics, align with country priorities, and prepare a coordinated portfolio of activities. In implementing the Paris Declaration further, MDBs face a number of additional common challenges, including addressing incentive issues as a key means of promoting further progress on aid effectiveness. Continued attention by all levels of management and evolution of internal processes where needed will be required to provide staff with an environment more conducive to harmonization and alignment.

33. Donor coordination is also being strengthened through the Bank's Africa Action Plan and partnerships such as the Limelette Process. The Africa Action Plan provides an outcome-oriented framework of partnership between the Bank and other development actors to help every African country achieve the MDGs.¹³¹ The Limelette Process is a partnership between the Bank's Africa Region and the EC.¹³² There is consensus that Limelette IV—the upcoming Bank-EC partnership meeting—should focus on strategic, high-level partnership issues with a particular attention to division of labor, coordination of program aid, aid predictability and issues related to scaling up, including vertical funds, emerging donors, and new trust funds.¹³³

34. The EU has recently adopted a voluntary Code of Conduct on Complementarity and Division of Labor in Development Policy to facilitate division of labor as a way to improve aid effectiveness. Among the 10 operational principles of the code of conduct for donors' actions are: concentration in a limited number (three) of sectors in a country based on a donor's comparative

¹²⁸ OECD/DAC. 2006. *Donor Reporting on Dissemination of the Paris Declaration* (DCD/DAC(2006)60).

¹²⁹ As of November 2006, 16 DAC members had adopted an action plan on implementing the Paris Declaration. An additional three members have adopted the principles of harmonization, alignment and results in their aid strategies and policies, and four others have intentions of having an action plan.

¹³⁰ Also see ODI. 2004. *Incentives for Harmonization in Aid Agencies*. Study prepared by ODI for the DAC Working Party on Aid Effectiveness.

¹³¹ See the World Bank. 2007. *Accelerating Development Outcomes in Africa: Progress and Change in the Africa Action Plan*. Development Committee paper (DC2007-0008, March 29).

¹³² The "Limelette Process" was launched in April 2003, as an annual meeting between the Bank's Africa Region and European Commission's DG DEV. It aims to exchange views on practices and improve mutual coordination on the ground. The annual topic changes: PRSPs (2003), budget support and public finance management (2004), and infrastructure, public finance management and trade and regional integration (2005).

¹³³ World Bank-EC Consultation Meeting on Limelette – Details of Discussions, April 27, 2007.

advantage; enhancement of donor coordination by supporting a lead donor arrangement in each priority sector; ensuring adequate donor support in sectors that are relevant for poverty reduction; and establishing priority countries for EU donor engagement.¹³⁴

35. A review of country-level harmonization and alignment actions/activities suggests a broad and growing attention to these issues. At least 60 countries around the world are collaborating with their development partners on country-level harmonization and alignment actions. Of course, the breadth and depth of actions differ among countries reflecting the adaptation of the elements of the Paris Declaration to the country context and circumstances. The evidence suggests that substantial implementation of the harmonization and alignment agenda is taking place in 5-8 countries, and good, but less extensive implementation, in 10-15 others. Many of these countries are preparing or implementing harmonization road maps or action plans articulating the aid relationship with donors—that is, the shared agenda between the government and donors to make progress toward localized Paris indicators and targets, establish mutual accountability, and facilitate managing for results. These countries are seeing a range of mechanisms and processes to improve the alignment and harmonization of aid, including joint assistance strategies (collaborative country assistance strategies), division of labor, and revamped Consultative Group processes.

Results of the 2006 Baseline Monitoring Survey

36. A 2006 baseline survey covering 34 countries and 37 percent of total donor assistance provides comprehensive data for assessing where development partners and recipient countries stand with respect to the Paris Agenda. The results of the survey spotlight a number of challenges that need to be addressed if the targets of the Paris Declaration are to be met. Past experience suggests that many of the targets are attainable if partner countries and donors build on the momentum fostered by the Paris Declaration.

37. Results for indicators pertaining to donors' implementation of the Paris Indicators are presented here. The survey shows that 40 percent of donors' disbursements use the partner country's PFM system and an almost equal percent of disbursements use the country's procurement system. Better quality of PFM systems (as measured by the CPIA) do tend to be associated with a higher use of these systems for aid that is provided to the public sector. Nevertheless, there is wide variation among bilateral donors (DAC members) on the use of PFM systems for delivering aid to government sectors—from a low of 10 percent to a high of 90 percent. The survey results show that greater attention is needed with respect to PIUs. In the 34 countries surveyed 1832 parallel PIUs are relied upon to implement projects, with the Paris target to reduce this number by two-third to 611 by 2010. Although a number of agencies, including the Bank and the EC, are looking to merge existing PIUs into the structures of ministries or agencies, substantial effort will be required to overcome hurdles to achieving this.

38. The baseline survey gathered information on two dimensions of harmonization: the use of common arrangements within program-based approaches; and the conduct of joint missions and

¹³⁴ The Bank and the EC are in discussions to see how the two institutions can cooperate in the implementation of the code of conduct in a few pilot countries.

sharing analysis. The survey finds that the donors provide 43 percent of their aid through program-based approaches such as budget support and sectorwide approaches, relative to the Paris target of 66 percent.¹³⁵ In addition, the extent to which donors conduct joint missions is very low—the survey found that 18 percent of missions were undertaken jointly, while 42 percent of country analytic work was prepared jointly with another donor, relative to the 2010 Paris targets of 40 percent joint missions and 66 percent of joint analytical work. Greater donor efforts are going to be needed if the 2010 targets are to be met.

39. Among the better performers, the 6 strong performers boast a relatively robust performance on a wide range of indicators. Many of these countries have undertaken substantial implementation of the harmonization and alignment agenda. Several of them share common factors such as strong government leadership in setting out priorities in development assistance, an effective implementation process for poverty reduction strategy, a mature government-donor aid relationship, and a well functioning aid coordination mechanism. Consequently, these countries are often in the top tercile in the indicators that underpin the Paris Declaration. Other PRS-II countries show considerable variation in harmonization and alignment actions (Table 5).

Table 5. Country-Level Progress on Harmonization and Alignment Actions and Selected Indicators of Aid Effectiveness: 6 Strong Performers and other PRS-II Countries

	6 Strong Performers					Other PRS-II countries								
	Burkina Faso	Ghana	Mozambique	Rwanda	Tanzania	Benin	Bolivia	Ethiopia	Malawi	Mauritania	Nicaragua	Senegal	Uganda	Vietnam
Harmonization action plan														
Collaborative CAS														
Quality of dev. Strategy														
Quality of financial management														
Aid on budget														
Coordinated TA														
Use of country FM systems														
Use of country proc. systems														
Parallel PIUs														
Predictability														
Program based														
Coordinated missions														
Joint analysis														
Results framework														
Mutual accountability														

Note: 6 Strong Performers excludes Madagascar. Colors/patterns denote the position of the country relative to other countries (in the survey) with respect to the indicator that is being measured: gray - top tercile, lines – middle tercile, and dots – bottom tercile. For the first two and last indicators, gray denotes yes, lines denote some progress, and dots denote no.

Source: Adapted from IDA 2007. *IDA's Role in Enhancing Aid Effectiveness through Strengthened Alignment and Harmonization* (Draft).

Challenges Moving Forward

40. The Paris Framework has generated a momentum for change in aid delivery practices. The survey points to the progress that has been made and the areas that need attention. Moving

¹³⁵ The results need to be interpreted carefully because some donors' definitions of PBAs may not represent the use of common procedures with other donors.

forward, donor efforts to scale up harmonization and alignment will increasingly need to focus on division of labor processes, expanded use of delegated cooperation, greater use of country harmonization and alignment action plans, and improving incentives within agencies.

41. Even as important gains are being made at both the donor and country level on improving the way aid is delivered, a changing aid environment calls for the need to address a number of remaining challenges. Notable amongst these are the trend towards greater use of global funds/vertical funds or earmarking and the increasing importance of emerging market donors. The challenge for the donor community and recipients is how to better align and integrate vertical and earmarked funds in country strategies and how to strengthen the complementarities between these funds and traditional aid. [A detailed discussion of the challenges in integrating global/vertical funds with country programs is presented in the next sub-section.]

42. The growing importance of newer donors is adding to the complexity of the aid architecture. Not much is known about the size and composition of flows from emerging donors, and better information is needed to facilitate monitoring and donor coordination. Although several emerging market donors have signed the Paris Declaration, the extent to which they are formulating and implementing Paris Declaration actions plans is not available. The recent (May 2007) memorandum of understanding between the Bank and the Export-Import Bank of China (China's state policy bank for international economic development and cooperation) is a welcome move to build collaboration on development, with a particular focus on Africa.

43. Addressing the above challenges is central to enhancing the effectiveness of aid. Donors and partners will need to pay attention to these issues in formulating and implementing their "second generation" Paris Frameworks.

E. Delivering Global Program Aid More Effectively

44. Global programs are issue-based aid vehicles that are a response of the donor community to a special challenge or problem. Recent years have seen a sharp rise in number and size of global programs. Contributions have risen from around \$1 billion in the 1990s to \$3 billion in more recent years. A few large programs account for 95 percent of the contributions of global programs, however. For example, three programs—GFATM, GEF, and UNAIDS—received nearly 90 percent of donor contributions in 2006, and 14 of the programs that are included in the major 20 in 2006 were established after 1994. The biggest increase in size and concentration of funds has been in the area of health.

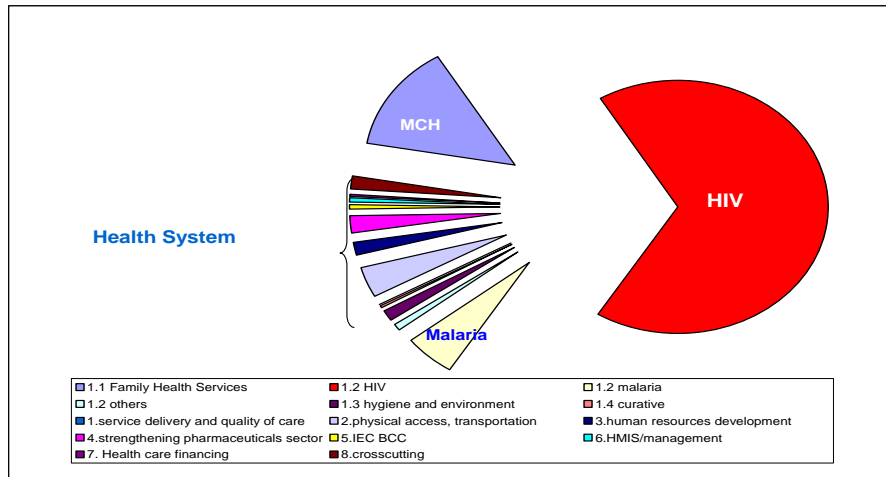
45. The growing prominence of global programs reflects a number of advantages of vertical approaches. These aid vehicles allow donors to rapidly mobilize and channel resources, while providing scope for economies of scale through specialization and enabling relatively rapid monitoring of impact on the ground. In addition, they can draw much needed political attention to pressing issues

46. While vertical funds bring much-needed attention and financing to their focus areas, and are increasingly important as sources of funding they can also have unintended effects. Where these funds are narrowly targeted to a sector or sub-sector, and are large and scale up quickly,

problems can occur, particularly in the short-run. The challenges posed by vertical approaches to aid delivery are most evident in the health sector. A recent study shows that 7 African countries receive HIV/AIDS funding that is larger than 30 percent of their total public health budget; in some countries this funding exceeds public sector health spending.¹³⁶ Such single-issue funding can lessen attention on other health priorities. For example, in Ghana malaria is the main cause of sickness and mortality, but donor funding to fight malaria is 60 percent of the amount allocated for HIV/AIDS. In Rwanda, donor funding in health is unevenly distributed: \$47 million is directed towards HIV/AIDS; a much lower amount (\$18 million) is earmarked for malaria, which is the leading cause of morbidity and mortality; and only \$1 million is allocated for the management of childhood diseases.¹³⁷

47. Verticalization can also pose obstacles for sustainability and absorption. For example, in Ethiopia and Rwanda 55 percent of foreign financed projects are negotiated on an annual basis. This short-term pattern of financing introduces uncertainty in aid amounts. Large year-to-year variations in aid levels constrain long-term plans of building capacity in the health sector—that is, hiring nurses and doctors and scaling up health services. An indication of problems of absorptive capacity (at the sector level) in Ethiopia is evident from the capital budget execution rate for external assistance, which are exceptionally low at between 15-20 percent, compared with 80 percent for domestic resources. But strengthening the absorptive capacity of the health systems usually receives less attention than HIV in donor pledges (Figure 3).

Figure 3. Ethiopia: Health System Receives Less Attention than HIV in Donors' Pledges



Source: Government of Ethiopia-Irish Aid-UNICEF-World Bank. 2007. *Reaching the Health MDGs in Ethiopia: Facing or Escaping the Scaling Up Challenge*.

Policies and Actions

48. Such consequences, however, are not inevitable. Countries and donors must work together to minimize these potential challenges and maximize the contribution of global funds to country based development. The Paris Declaration goes some way to address these issues: it

¹³⁶ Lewis, Maureen. 2005. "Addressing the Challenge of HIV/AIDS: Macroeconomic, Fiscal and Institutional Issues," CDG Working Paper 58, Washington: Center for Global Development.

¹³⁷ Republic of Rwanda. 2006. *Scaling Up to Achieve the Health MDGs in Rwanda*. A Background Study for the OECD-DAC High-Level Forum Meeting in Tunis (June 12-13).

recognizes the need to better integrate global programs and horizontal aid in recipient countries' broader development agendas; and it reinforces the centrality of the country-based approach to development aid—the need for strong national development strategies, such as PRSs, so that aid can be aligned with country priorities and country systems. A range of complementary actions and policies are essential of realizing the rewards of vertical approaches, including country-owned development strategies, complementary investments, fiscal sustainability, and favorable investment climates conducive to growth and private sector development.

49. A recent study by the World Bank finds that the ability to align with country-led strategies also depends up on the characteristics of global programs.¹³⁸ Vertical programs should be integrated with the national budget and use national systems as much as feasible. The issues concerning strategic coherence and harmonization are the most serious in the health sector. They also arise in other sectors that are the focus of global programs, namely, education and environment, but are less pronounced because the approaches followed by the major programs in those sectors (Education for All-Fast Track Initiative and Global Environment Facility) put more emphasis on harmonization and alignment.¹³⁹ The Fast Track Initiative, for example, uses a country-based approach to the education sector involving the local donor group, which jointly endorses the government's education sector strategy and then coordinates the scaling up of donor funding to support it.

50. The Bank's strong support of the country-based model of development heightens the institution's role in addressing the challenges of integrating global programs and country programs with national priorities. In addition, the Bank plays a platform or "glue" role to provide strategic coherence to other forms of aid. This "glue" role derives from the institution's multi-sector perspective, its convening power, and its global reach combined with local presence. These dimensions allow the Bank to adapt to country situations, to act as a first mover when appropriate, and to leverage other funding to scale-up poverty reduction interventions.¹⁴⁰ Thus, the Bank can bring greater coherence in development assistance at the macro and intra-sectoral level. It can also play a central role in enhancing harmonization and coordination among donors. Moving forward, the Bank can play a critical role in helping to raise the effectiveness of aid in a changing and complex aid environment, if appropriate financing is available for IDA.

51. Work on aid effectiveness and health has yielded a substantial body of evidence and a number of important streams of work have been started or are ongoing. In 2004-05, a High Level Forum on the Health MDGs assessed aid effectiveness issues in health. A set of Best Practices Principles for Engagement of Global Health Partnerships at the Country Level was proposed in 2005. These principles for improving the delivery of health aid are based on the Paris Declaration, but also include a few best practice principles on governance of global health programs—namely: provide clarity and transparency to decision-making roles, objectives and

¹³⁸ World Bank. 2006. *Integrating Global Partnership Programs with Country-Led National Programs: Synthesis of Findings and Recommendations*. Contribution to OECD Policy Workshop on Global Programmes and the Paris Agenda (COM/DCD/DEV(2006)7, December 5).

¹³⁹ World Bank. 2006. *Idem*.

¹⁴⁰ IDA. 2007. *The Role of IDA in the Global Aid Architecture: Supporting the Country-Based Development Model*. (IDA/SecM2007-0450, June 1).

procedures; have a strong commitment to minimizing overhead costs; and be subject to regular external audits.¹⁴¹

52. In 2006 the Bank and the OECD-DAC co-sponsored a policy workshop to focus attention on improving the alignment of global programs at the country level. The Bank proposed good practice guidance for integrating global programs—all global programs, not just health—at the country level. The good practices are anchored in the Paris Declaration and also draw on the best practices for global health partnerships (see above).¹⁴² This was followed by a workshop in Mauritius (June 2007) on how to enhance the linkages between global programs and country strategies to achieve development results. In preparation for the Ghana HL Meeting, the OECD-DAC organized a meeting in May 2007 to propose areas of aid effectiveness in health that could be taken forward by the WHO and the Bank. One area of interest that has been identified is support of health systems.

¹⁴¹ Report of the Working Group on Global Health Partnerships. 2005. *Best Practice Principles for Global Health Partnerships Activities at Country Level*. High Level Forum on the Health MDGs (November 14-15).

¹⁴² OECD/DAC. 2006. *Draft Good Practice Guidance for Integration and Effectiveness of Global Programs at the Country Level* (COM/DCD/DEV(2006)9, November, 24).