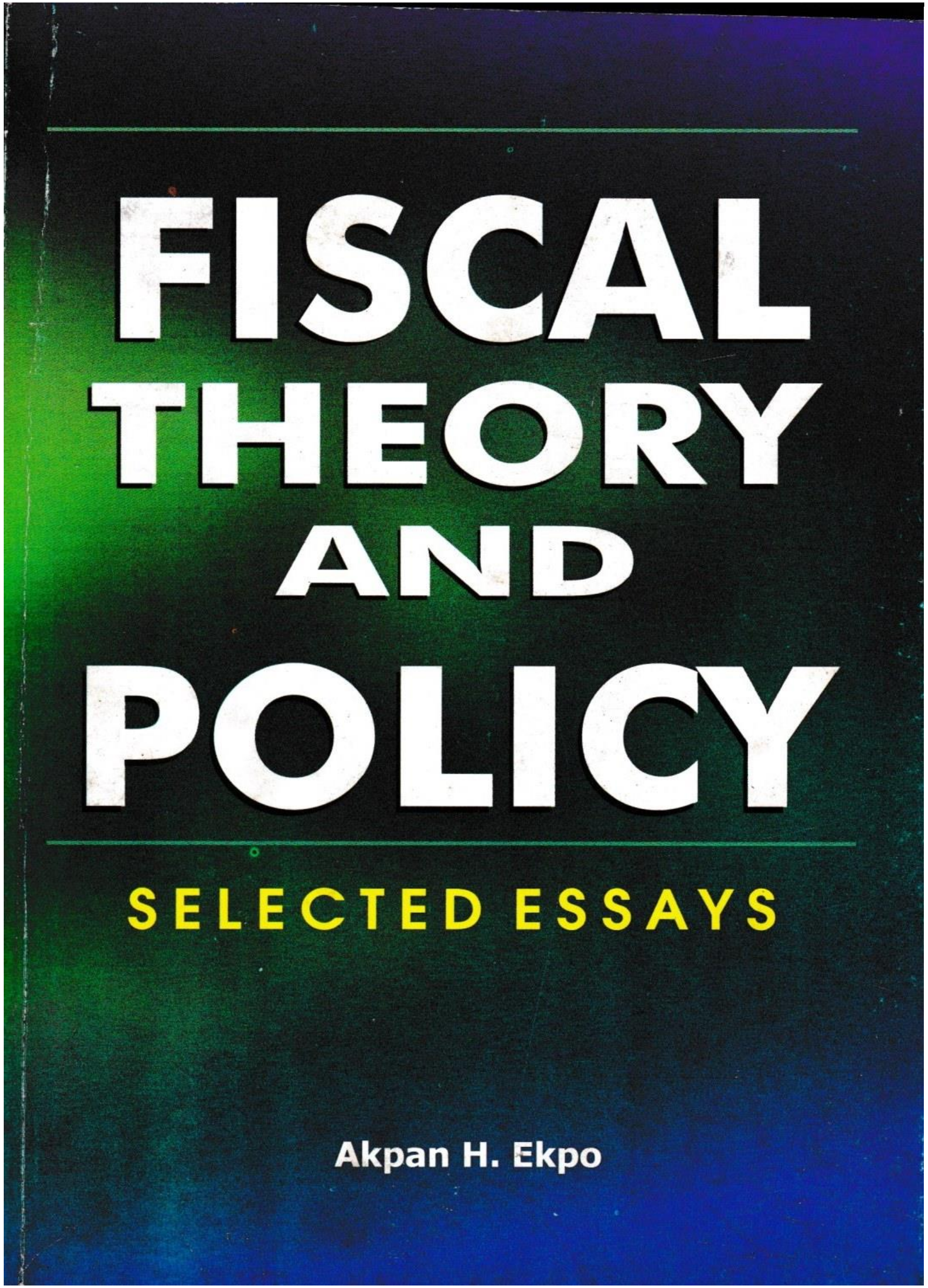

Chapter Six

POVERTY-ORIENTED BUDGET DESIGN AND IMPLEMENTATION*

I. Introduction

There is a tendency for economists of the previous centuries to regard the existence of market failure as the fundamental rationale for public expenditures. It is now accepted that the reduction of social inequalities and poverty is also a legitimate concern of government and goal of economic policy. Poverty is multi-dimensional, extending from low levels of poor health and lack of education, to other non-material dimensions of well being, including gender gap, insecurity, powerlessness and social exclusion (IMF/World Bank Development Committee, 1999 and Kankwenda et al, 2000).

Progress towards poverty reduction has been disappointing in the world level in general, and in African countries in particular during the preceding decades. The number of the poor has been rising in many parts of the world, especially in Sub-Saharan Africa (SSA), where the absolute number of the poor continue to rise and social indicators remain below those of other low-income countries (IMF/World Bank Development Committee, 1999). While the proportion of the population living with less than US$1 per day in SSA has remained in the neighbourhood of 46.5% since 1987, the number of people living with less than US$1 per day was increasing, going from 74 million in 1987 to 291 million in 1998 (Chen and Ravallion, 2000).

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Among other causes of this increased poverty, weak economic growth in most low-income countries remains the most important. However, in some countries where the rate of Gross Domestic Product (GDP) growth was higher than that of the population, no significant progress has been recorded in terms of poverty reduction, because of the unequal distribution of the economic growth fruits and/or the lessening of the potential impact of growth on the poverty level, as a result of poor governance. It is, therefore, imperative that resources must be made available if poverty reduction is to make sense. African governments must budget for poverty reduction. "Getting rid of poverty and other social inequalities and undoing the damage to the environment is, of course, a long-term undertaking. Nevertheless, it is possible to gauge the extent to which governments are moving in the direction of meeting their commitments to social and economic aims through a scrutiny of their budgetary activities" (Cagatay et al, 2000)".

Public budgeting is at its essence about the generation and use of public resources. Examination of public budgets tells us whether governments' allocation of public resources is in line witn the commitments they have made to the population. Budgets matter precisely because they are powerful policy tools with profound implications for social equity outcomes (Cagatay et al,, 2000). As a consequence, budget designing and implementation are decisive in the poverty reduction objective that have adopted the international community in general and the developing countries in particular. A government will be deemed serious in reducing poverty if its budget provides and shows commitment to funding poverty reduction programs. Poverty-oriented budgets have become fashionable in countries that are determined to reduce

poverty in SSA.

The purpose of this paper is to analyse poverty-oriented budget designing and implementation in Africa and other developing/transition economies. It examines the following sub-areas: (1) conceptual issues of budgeting and implementation of poverty-oriented budgets, (2) designing medium-term expenditure frameworks, (3) identifying and costing poverty-oriented expenditures, (4) tracking poverty-reducing expenditures, (5) financing poverty reduction strategies and, (6) participation in budget policy formulation and implementation. The final part concludes the paper and discusses its policy implications.

I. Conceptual issues in the designing and implementation of poverty-oriented Budgets

Budget involves a set of objectives, and the resources to achieve those objectives. The resources are allocated through a decision-making process involving various institutions holding and representing discrete interests. The interactions between these institutions are crucial in determining resource allocation outcomes. From the very start of modern budgeting, attempts were made to structure the institutional framework of the budget process so that the desired allocations would be achieved. Later on, attention was focused on the decision-making process based on analytical methods, which imposed rigorous techniques (Fozzard, 2001).

Modern budgeting systems were developed as a means of exerting legislative control over resource allocation decisions made by the executive. Dividing responsibility for and authority achieved this over the resource allocation process between institutions whose competence and relations were defined in law and supplemented by rules and procedures.

A clea r distinction was maintained between policy and administrative functions: the former was regarded as the exclusive preserve of politicians in Cabinet and the legislature, and the latter the responsibility of bureaucrats within the Ministry of Finance and spending agencies. Appropriate procedures between the different institutions can help achieve the expected budget outcomes (See box 1). This is the administrative budgeting approach.

As the State began to assume a more activist role in social and economic development, government programs proliferated and the level of expenditure expanded rapidly. For effective and efficient use of these resources, a technically rigorous approach to decision-making. This was found in the application of a rationalist approach, which entailed fundamental changes in budget structure and the policy formulation and resource allocation processes.

In contrast to the administrative approach, where policy is the exclusive realm of politicians, technicians are involved in the definition of policy goals through a process of problem analysis. Once the goals have been defined, technicians seek the appropriate means to achieve them by appraising alternative strategies. This entails an identification of preferred option using transparent, ideally quantitative, criteria. Implementation of the preferred option is monitored and evaluated with the results fed back to subsequent policy analysis and formulation.

The application of the rationalist approach of budgeting required an explicit link between the means and ends of public policy, between resource allocations and policy objectives. To clearly identity these links, many countries introduced budget classifications based on programs, comprising a set of activities intended to achieve a specific objective. The resources are allocated between programs on the basis of their contribution to stated policy

objectives. These allocations are projected over a multi-year period so as to reflect the financial implications of policy decisions. They are then revised annually to take into account the results of program monitoring and evaluation. In this way, decision-makers may appraise alternative applications of scare resources and ensure that resource allocations reflect policy priorities and the effectiveness of public programs.

In developing countries, the rationalist approach is associated with development planning and, by extension, public investment programming. These are usually aimed at promoting economic growth and the expansion of social services, and identifying a prioritised list of development projects for this purpose. In order to finance these projects, governments establish development budgets as distinct from the recurrent budget used to finance government's day-to-day operations. Planning and management of the development budget is usually the responsibility of specialist planning agency and departments in sectoral ministries. In most fully developed poverty-reduction oriented budgets these distinctions are eliminated and line ministers and finance and planning ministers think jointly about development and recurrent budgets. This is because large sections of investment budgets often turn out not to have much to do with investment (e.g. recurrent costs and counterpart funding in donor-funded projects, technical assistance and training costs) and major proportions of recurrent budgets are actually a major contribution to human capital investment and poverty reduction (e.g. teacher training and salary, road maintenance, etc.) One of the major advantages of programme budgeting is that it allows governments to eliminate the false distinction between investment and recurrent spending.

This budgeting system encounters numerous problems in both developed and developing countries. Programs are difficult to define, particularly where objectives crossed traditional administrative boundaries. So are appropriate objectives and indicators of performance. Since administrative structures continue to manage resources, there is a tendency for programs to be defined as to reflect what the institution is currently doing rather than with reference to policy goals. In addition, there is a problem of the vast amount of information required to assess the relative priority of programs and their performance. Often such information is not collected on a routine basis.

In mid-1990s it was fashionable to move away from planning of budgets by objective, to incremental budgeting through mechanisms such as Public Expenditure Reviews (PER) focussed on particular sectors or types of expenditure and suggested incremental reforms to them. However, the PRSP has changed all of this, putting programme and objective-based budgeting back at the core of budget objectives, especially due to its linkages to the Millennium Development Goals.

In the incremental approach, decision-making is subject to bounded rationality in which actors are satisfiers rather than optimizers. Within these constraints, decision-makers are expected to behave self-interestedly, or at best, take a partial view of the public interest in which self-interest will have a preponderant influence. This self-interest will reflect the institutional role of each of the actors in the policy-making process and interactions between these actors will respect both formal, procedural rules and informal, social norms. The final outcome of the decision-making process can, therefore, be seen as the product of a set of games involving strategy and skill, played by self-interested actors performing stylized roles and as a consequence of the rules of games.

To reduce uncertainties of budgeting, decision-makers will rely on their experience, take their cue from other participants, and seek to satisfy rather than optimize, and prefer cautious, incremental change to risky, radical shifts in policy or budget allocations. This lends certain predictability to the budget process, with stable roles leading to stabilized behaviour.

The nature of the budget process also promotes incremental decision-making. Allocation decisions tend to be made sequentially rather than by assessing trade-offs between alternative claimants. Furthermore, budgeting is repetitive, with the same allocation issues being addressed in successive budgeting exercises. In this way, participants arrive at a tacit agreement regarding each claimant's fair share, constituting a convergence of expectation on roughly how much an agency is to receive in comparison to others. Once the fair share is established, bargaining about allocation decisions is restricted to the distribution of additional resources rather than redistribution of the budget base. Allocation decisions are ultimately a product of political bargaining.

While the incremental approach may provide some insight by explaining a stable routine, that is fairly resistant to external shocks, and that adjusts itself only gradually to changes in environmental circumstances, it contributes little where these conditions do not hold. When circumstances are changing, as during the fiscal crises, and when government is no longer able to distribute increments and often had to cut back on base allocations, mechanistic incremental budgeting is invalid. It is clear that, by focusing narrowly on inter-sectoral allocations, incremental approach underestimate the complexity of budgetary decisions, in particular with the relation between micro and macro-budgeting focusing respectively on resource allocation and stabilisation.

Similarly, it failed to recognise the complexity of institutional interactions, notably evidence that institutions play a variety of roles with regard to different actors.
Poverty oriented budgets ought to follow a typical budget cycle (see figure 1). Some critical steps in the cycle are worth examining:

* ***Setting aggregate spending limits***: A feasible and credible budget can be prepared solely on the basis of accurate forecasts of economic growth and resource availability. For example, if revenue projections are too optimistic, then cutbacks will follow. If this becomes a regular feature the budget will lack credibility.

* ***Setting sector spending limits***: These limits ought to reflect judgements on the nature and appropriateness of existing budget commitments.

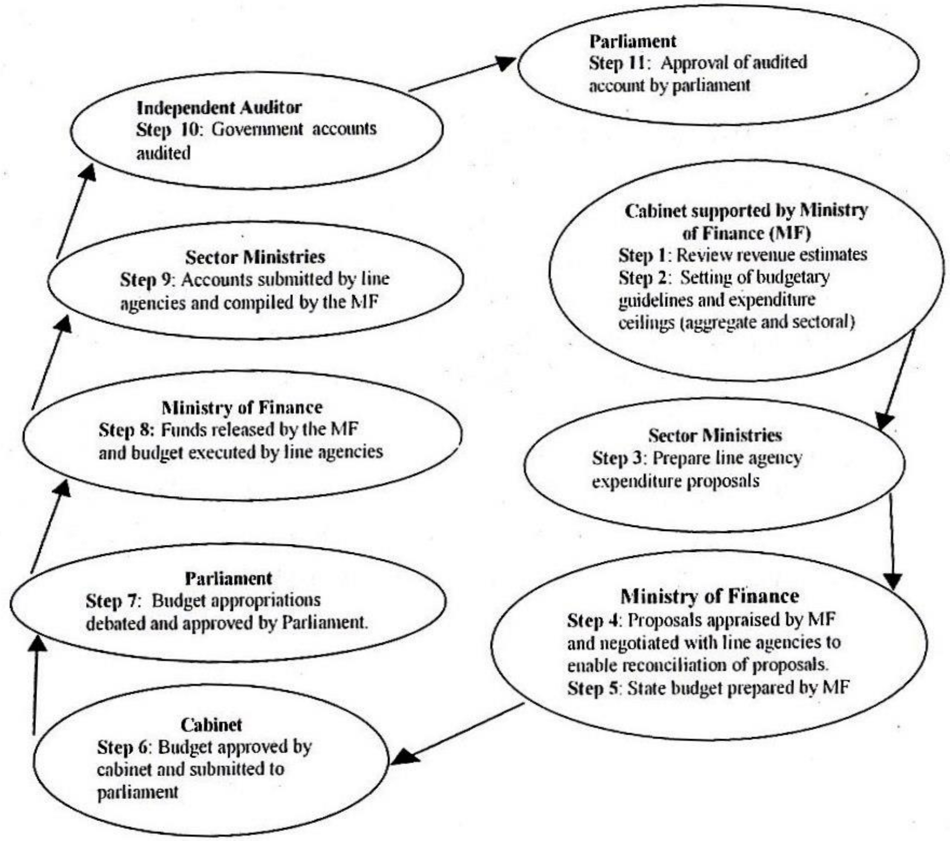
* ***Preparing and analysing line agency bids:*** This comes into place after line agency bids are prepared and examined (Step 3 and 4). "Typically, line agencies will have limited time after the distribution of the budget guidelines and limits to prepare their bids ... Hence, line agency budget departments will often take the previous year's budget as the base and request a percentage increase rather than budgeting on the basis of planned service levels and their cost estimates" (Fozzard, et al, 2001).

* ***Ensuring budget compliance***: It is important that budget discipline be adhered to – policy and programmes changes should take place during the budget formulation phase of the cycle. However, some

flexibility is allowed through contingency reserves and by permitting the movement of funds from one budget sub-head to another under certain conditions.

* ***Providing adequate feedback on budget implementation:*** The budget cycle includes a feedback loop in which ex-post monitoring and evaluation informs next year's budget development (linking steps 9 and 2). Decision-makers can also identify areas in which controls on spending are too tight (or loose) and make the adjustments needed to improve the poverty impact of public programmes. In the case of poverty reduction strategies, improving the quality of expenditure analysis is crucial. It is important that decision-makers at all levels adopt a critical and questioning attitude towards expenditure.

Figure 1. The Budget Cycle



Source: Authors' construction.

3. Designing medium-term expenditure frameworks (MTEF)

Many developing countries have merged the planning agencies with the ministries of Finance. Although the distinction between the development and recurrent budget is maintained, resources are programmed together through a MTEF, which intended to provide an ex-ante framework within which a realistic view of aggregate resources can be aligned with program priorities. Usually built for a multi-year period, the MTEF consists, in its essence, of:

* A 'top-down' resource envelope consistent with macro-economic stability and both internal and external resource availability, prepared by core financial management and planning agencies;
* A 'bottom-up' estimate of the current and medium term cost of existing national priorities prepared by line agencies; and
* A negotiation process, which matches the demand for resources with availability through iterative decision-making.

he first year of the MTEF establishes the budget limits for the coming year; the outer years are indicative, rolled forward by one year and revised during the next budget cycle. Ideally, MTEF expenditure projections are broken down to program level and link to output indicators.

The MTEF supports decisions regarding the level and allocation of resources, both government-wide and within spending agencies. It focuses on policy rather than the minute detail of budget submissions, by representing aggregate expenditure projections by sector and programs. Using alternative scenarios, decision makers can match aggregate expenditure with resource availability and assess the costs and benefits of policy options. The MTEF also helps to communicate policy, by setting out clear priorities, and provides a basis for negotiations with external financing partners. At a tactical level, forward projections of expenditure allocations help to guide and track the reallocation of resources in line with the government's development priorities. Forward projections also facilitate sector planning by indicating the likely flow of resources over the three to five years period, thereby allowing spending agencies to take into account the operations and maintenance requirement of investments and target levels of service delivery. Efficiency and effectiveness can be improved by requiring line agencies to define their mission, objectives and activities and linking expenditure to measures of performance in terms of output and outcomes (Fozzard and Foster, 2001).

Bevan and Polomba (2000) asserts that the MTEF offers a very appealing prospect that policy priorities can be agreed in transparent process, that budgetary finance can be aligned in the light of these priorities, and that expenditures take place as budgeted but also that they yield the intended outcomes. Since aid flows accounts for a significant part of total resources of developing countries' government in particular, they have implications for the budgeting process. The budget being the real focal point for deciding priorities and consequent spending allocations, it becomes all the more important that all aid flows can be considered during the budgeting process, even for the sort of project aid which has often been organized on an extra-budgeting basis. This implies that donors should make their intentions clear in advance, ideally on the MTEF period horizon.

It is then important that donors should accept the MTEF as the organising principle for their interactions with government. They will doubtless continue to have manifold direct dealings in respect of their aid programs, but they should see these as being framed by the MTEF. Ideally, increasing numbers of them should effectively sign up to the MTEF as the actual vehicle through which their aid is disbursed. If such a consensus is found, a system of regular meetings (macroeconomic working group) must be established to allow the donors to share 'ownership' of the budgeting process. These should be probably quarterly, and involve discussion of substantive, ongoing issues, rather than being limited to dissemination of what has already been decided elsewhere. For more credibility, these meetings should have a much wider function than simply bringing relevant donors 'on board' to the

ongoing MTEF process. This confers increased scope but also greater responsibility on government to examine the options and choose between them. In this view, the best financing donors can provide is the untied budget support. The second-best is sector programme support. The third best is projects, which are integrated into the budget, and the worst is projects funded outside the budget.

Given the presence of fungibility in government spending, the only real guarantee that the funds at government's disposal will be spent in ways that are comfortable to donors is for an over-arching device like MTEF to stipulate the composition overall. If the composition elaborated in the MTEF is acceptable, and if it is duly delivered, the problem is solved. The more general difficulty with the designing of consensus MTEF is the notion of priority areas. There could be three rather different types of rationale for delineating priority areas:

* A disagreement between donors and government on the desired composition of spending;
* The government itself could feel that the composition of spending is inappropriate, but that would take time to reshape it;
* The choice of the priority sector that should be protected against cuts.

In both first cases, a properly articulated MTEF seems to be the better device, whereby a compromise is reached, or a trajectory determined. As the third rationale is concerned, the protection could be required in two rather different circumstances:

* Where political powerful sectors seek to undo the previously agreed budget allocation, at the expense of the weaker;
* Where the need for cuts originates in revenue shortfalls.

In the first case, a clear commitment to protect the weaker sectors may be valuable as a supplement to the budget process, but it is a sign of weakness in that process all the same. In the second case, the argument would be to protect sectors where interruption would be particularly costly, rather than sectors that were in some abstract sense 'more deserving'. That is the case of social sectors in poverty-oriented budget.

In general, the MTEF has the advantage to deliver macroeconomic stability and overseeing a substantial shift in expenditure composition, most notably in favour of social sectors. It also has a good record of protecting priority sectors against damaging budgetary cuts. It however, involves some problems for macroeconomic management. The process of preparing MTEF needs to take more active view of the macroeconomic framework within which budgetary decisions are located. The links between the long-term goals and the associated cots of achieving these goals need to be more actively interacted with the MTEF and associated budget allocations, to ensure that budgets accurately reflect priorities. These always imply much activity on the monitoring/evaluation/output/outcome fronts. It also requires changes in donor behaviour, by imposing fuller integration of donor projects into the budgeting process, both ex ante and ex post in tracking outturns (Bevan and Palomba, 2000).

The biggest problem with MTEFs is actually the frequent shortage of donor resources and other revenues which make it impossible to obtain objectives which have been painstakingly negotiated with the line ministries, and therefore risk discrediting the MTEF process by making line ministries ask why they should bother to draw up and negotiate with ministry of finance such complex plans. The best way to make METFs succeed will be to find ways to

protect the budget from budget shortfalls of resources, through reliable donor aid flows and compensatory financing mechanisms.

MTEFs have been implemented with various degrees of success in South Africa, Ethiopia, Ghana, Malawi, Mozambique, Tanzania and Uganda. Hudu Siita (2001) shows that the Ghanaian MTEF started with the following primary objectives, namely:

* Preparing of strategic plans in which objectives, and identified outputs and activities in a manner in which poverty activities could be clearly identified;
* Improving macroeconomic balance by developing consistent and realistic estimates of available resources covering both government and external resources;
* Restructuring and rationalizing resource allocation so that priority areas such as the social sector receive adequate funding;
* Introducing a forward or medium term perspective in the planning of policies, expenditures and revenues (the 3-year framework).

The designing process of that MTEF involves a series of steps from the top down and bottom up:

Top Down:

- Defining total government and external resources available;
- Allocating these resources between sectors and ministries on the basis of policies and priorities to arrive at the budget ceilings.

Bottom Up:

- Sector ministries estimating their resource requirements on the basis of their policies and priorities;

- This bottom up information on requirements being provided to the Ministry of Finance and Cabinet to inform reallocation of resources between sectors and ministries.

In line with the Ghanaian government policy objectives of providing improved social services especially in education and health, the social services sector share of total resources increased from 28.1% between 1995-98 to 31.8% in 2001 (see table 1 in appendix).

MTEF needs to fit in with wider planning processes and gives way to a Long Term Expenditure Framework (LTEF), which assesses the budget more comprehensively and over a long period. In the case of Uganda, the MTEF derives its priorities from the Poverty Eradication Action Plan (PEAP) but the level of expenditure is based on a realistic assessment of resources rather than a needs based assessment derived from the PEAP.

As part of the LTEF of the country, the PEAP is the major vehicle for directing funds into the priority sectors. Its has four pillars of action to directly increase the ability of the poor to raise their incomes and to improve the quality of life, including investments in primary education, clean water, and improved basic health care. The public expenditure required to achieve the targets set out in the PEAP over the next ten years is estimated. That estimate is prioritised and phased and the MTEF is the mechanism by which the targets of the longer term PEAP are adjusted to match the resources available in the short to medium term. Mijumbi, P. (2001:16) summarizes the planning and budget process in Uganda in the following manner:

Vision 2025 An overview of long-term goals and aspirations by the year 2025.

The PEAP *The national planning framework on which to develop detailed sector strategies.*

MTEF *Annual, rolling 3 years expenditure planning, setting out the medium terms expenditure priorities and hard budget constraints against which sector plans can be developed and refined.*

Sector planning: Sector working groups involving donors as well as Government work on budget framework papers (sectoral MTEFs), disciplined by hard budget constraints set by the MTEF. Sector wide approaches with defined objectives, programmes, indicators, and monitoring, and review arrangements exist in education, health and are being introduced elsewhere.

District planning: Discretion is presently limited because most finance is in the form of conditional grants, specifying how funds are to be allocated and used, requiring detailed work plans, specifying reporting and monitoring arrangements. Districts are now included in the MTEF process, with district MTEFs setting out the medium expenditure priorities and hard budget constraints against which district plans can be developed and refined.

Participatory processes: Budget process is remarkably open, with donors directly involved in sector working roups and overall budget discussions, plus consultation with NGOs, private sector, other civil society organisations, and attempts to involve MPs informally as well as in the context of formal budget approval procedures. The Local Government Development Programme is developing more participatory approaches to local Government planning and monitoring process. Participatory poverty assessments ensure that policy is informed of the views and experiences of poor.

4. Identifying and Costing Poverty-Oriented Expenditure

Given the budget constraints that face any government, and particularly the limited revenue available in low-income countries, there is a need to prioritise among alternative interventions and choose those, which at the margin have the largest poverty impact. Understanding the causal mechanisms underlying poverty outcomes is vital in determining appropriate public action(s). Similarly, a good grasp of the type of poverty, which confronts the country, can help to better target government interventions (IMF/World Bank Development Committee, 1999).

Poverty embraces material aspects that can be captured in terms of monetary indicators such as income or expenditure levels. It also includes non-material aspects relating to the quality of life, such as nutritional and health status and education attainment. To generate a more complete picture of poverty in a country, it is usual to supplement income-based measures of poverty with non-income indicators such as child or infant mortality, life expectancy, or educational status, etc.. This may also have to be supported by sectoral (employment status) or regional (rural or urban) profiles of the poor.

Given a particular type of poverty, there exist numerous measures that can be taken by the government for better poverty reduction outcomes. These will have different costs, and are likely to have knock-on effects on other outcomes. Due to the existence of the multiple links between poverty outcomes on the one hand and levers for public actions on the other, we will only emphasize the global

view encompassing public actions and poverty reducing outcomes. Therefore, our discussions will focus on: (1) increasing market opportunities for the poor, (2) improving capability and delivery of essential services, (3) increasing empowerment and participation and, (4) increase security and reducing vulnerability.

4.1 Reducing Income Poverty and Increasing Market Opportunity for the poor

It is well known in the literature that aggregate economic growth in its essence is not enough for poverty reduction (Ravallion, 2001 and Sahn, 2001). 'Economic growth as measured in the national accounts, is not always reflected in average household living standards as measured in surveys, at least in the short run' (Ravallion, 2001:22).

The policies need to enable such growth to generally include measures to ensure macroeconomic stability, appropriate fiscal and exchange rate policy and financial sector development. For the economic growth to contribute to poverty reduction it should be driven by sectors where the poor work and at the same time, the barriers to access that restrict market opportunity of the poor have to be removed by the public action. This will require knowledge about the constraints that are most relevant to the poor, and about where the poor work (for example, which type of crops the poor grow). The latter is important to assess the effect of policy changes and economic developments.

For example, the increase in cocoa world price, while benefiting to all cocoa growing countries, its impact on poverty varied according to regions and to countries. Within the cocoa growing countries, the poor of the non-growing regions such as the Northern Cameroon will benefit little or not at all from the coca price increase, whereas the poor of the Centre, South and West regions will fully benefit from it. Similarly, the poor in Ivory Coast, whose main activity is growing cocoa, will gain from this price increase than those of Senegal and Chad who are not growing cocoa.

In addition to sustained growth, measures designed specifically to increase access to economic opportunities for poor groups will likely be needed in many low-income countries. This will be particularly important in countries with high levels of income inequality. Among the interventions for consideration are pricing and competition policies, lifting trade barriers against pro-poor sectors, labour market interventions, rural infrastructure, urban development, the distribution of land, the expansion of the quality of education and financial and micro-finance development.

4.2 Improving capacities and delivery of essential services

It is clear that the multi-sectoral approaches are the key to improve poverty outcomes. Child mortality is affected e.g. by the level of income (national and household), access to safe water and sanitation, education (specially women) and some categories of health interventions (immunization) The same is true for child malnutrition. Community services like health care services including immunization and AIDS programs particularly to the aged, pregnant women and infants, private toilets and village safe drinking water supply, extension services, public drainage systems, construction and maintenance of market facilities particularly in the rural areas as productive assets and opportunities to help the poor improve their livelihoods and job opportunities, energy provision to remote areas, are critical in this respect; not only the mere physical presence, but also the quality of these services, and therefore the institutional design of delivery mechanisms as well as funding.

4.3 Increasing empowerment and participation

Empowerment is a key outcome, as well as instrument for improving poverty outcomes more generally, through better diagnosis of priorities and causes, and monitoring. Levers for public action to empower the vulnerable or disadvantaged individuals such as people with disabilities, destitute, the aged and street children include social welfare services. To improve governance, these include strengthened governmental processes, like budgetary management backed by audits, as well as broader based accountability[2] , programs to promote police and armed forces, customs, judicial structures, anti-corruption institutions, parliamentary development, effective decentralization, girls' education and combat discrimination including gender discrimination.

The quality of governance and overall social functioning can influence both growth and poverty. Recent empirical evidence for a large sample of countries reveals a strong positive causal relationship from improved governance to better development outcomes – in particular, growth in per capita incomes, infant mortality and adult literacy. The dimensions of governance that matter include voice and accountability, political instability and violence, and perceptions of corruption. The levers for public action to improve governance include

4.4 Security and reducing vulnerability

The sources of insecurity range from the global and macro levels – including natural disasters and climate- to idiosyncratic risk – especially ill-health or death in the family. The poor respond to these risks with a series of ingenious market and non-market mechanisms, but these are not enough, and these risks lead to decisions and outcomes, which adversely affect their development. Public action can help reduce vulnerability to national, community and individual shocks – especially those with irreversible effects for the poor. Assets, such as land, livestock or savings, safety nets to ease the social distress of vulnerable groups, food buffer stocks, access to emergency care, etc. are a central part of the risk management strategy of the poor. Helping to build up these assets is a key policy in providing security to the poor. Country-based diagnosis is again needed to identify appropriate levels of public action.

Poverty-reduction target setting is intrinsically linked to the government's budgetary process and its fiscal constraints, which opens another avenue for gauging the viability of development targets. Attaining target must not only be technically feasible, it must also be fiscally sustainable. The fiscal sustainability of development targets can thus be gauged by the government's capacity for increasing public spending, which means assessing target's costs.

Assessing the cost of reaching poverty-reduction targets is even more difficult than setting targets. The cost of attaining output and outcome targets depends on the shape of sectoral and program production function, the level of technical efficiency in the various sectors and programs and the factor prices for various inputs. Part of the difficulty in estimating the costs of reaching a set of targets is due to the fact that all up cited parameters are likely to be changing simultaneously at least over the medium term, in deed, some determinants of costs, such as the level of technical efficiency, are themselves objectives of policy, so they should not be treated as fixed parameters over the whole planning horizon.

The process of administrative and political decentralization that is underway in the country may also affect estimating the cost of reaching a target. If e.g.

responsibility for public service delivery, and the hiring of teachers, medical staff and agricultural extension personnel passes from central to local government, it is likely that all determinants of a target's costs will be affected. Indeed, a major aim of decentralization is precisely to influence these factors, so as to improve efficiency.

In general the cost estimations should use the social or shadow prices of inputs when these diverge from observed market prices. From the viewpoint of fiscal sustainability, what matters in the end is what the government has to pay in order to attain a set of targets, not what it ought to pay. However, detailed sectoral cost analyses have to be done and information on the objective, outputs, activities and inputs have to be provide. See table 2 in appendix for an example of costing of poverty reduction activities.

5. Tracking poverty-reducing expenditures

This section, adapted from IMF/IDA (2001), revolves around: (1) the principles of expenditure tracking and (2) the recommended approaches of tracking poverty-reducing expenditures. For public spending to have significant impact on poverty, it must be budgeted and disbursed for activities that help the poor expand their access to resources and their income-earning potential. Tracking these expenditures can help to:

- Know how the government is focusing on allocation and implementation of public expenditures in the formulation of its poverty reduction strategy;
- Ensure citizens and governments in donors countries that the resources provided under poverty-reducing initiatives are devoted to poverty reduction strategies;
- Ensure the poor, citizens and parliaments that poverty-reducing resources are being used for the purpose intended;

- Find out if the ultimate aim of reducing poverty is tilting the composition of overall public spending toward poverty-reducing programs.

5.1 Principles of expenditure tracking

Countries with well-developed budget classifications can rely on existing systems to identify and track poverty-reducing expenditures. Where such systems are not yet comprehensive, setting up a virtual poverty fund offers a short-term approach. Budget line items that are considered to contribute to poverty reduction are tagged, and these together constitute the virtual fund. All tagged items are monitored by the Ministry of Finance as part of overall budget execution.

By using the existing budget processes, this approach avoids the pitfalls of a separate institutional mechanism while enabling tracking of all poverty-reducing programs. Virtual funds are taking several forms: (1) really accounting framework as Poverty Action Fund (PAF) in Uganda, (2) general government account in the central bank as the Multilateral Debt Fund (MDF) in Tanzania or the HIPC Fund in Cameroon or (3) tagging of certain budget line items as poverty-reducing.

Tracking of overall spending may be handicapped by weaknesses of public expenditures management system in the country, the use of separate institutional poverty funds has sometimes been advocated as a means to channel and monitor the use of the poverty-reducing resources. However, the use of separate institutional poverty funds is inadvisable for several reasons:

* Institutional poverty funds do not necessarily capture additional spending on poverty-reducing programs;
* Even in the absence of fungibility, a separate institutional fund would not provide assurance that sufficient resources were being committed to achieve targets for poverty reduction;
* In many cases, creating institutional poverty funds would undermine the significant progress already achieved in most countries in providing comprehensive budgets. Diverting limited technical skills to create and manage these funds could aggravate problems of transparency, duplication, and governance in the budget as a whole.

In general, tracking poverty-reducing expenditures requires an appropriate budget classification system and an effective government accounting and auditing systems. Note should also be taken that devolution of poverty-reducing programs to local governments can make tracking more complex. The needed information could be unavailable or could be available only with a long lag. Those available could be insufficiently detailed or accurate.

5.2 Recommended approches

If systems are not in place for a comprehensive and complete assessment of the changes in the overall composition of public spending, short-run approaches to tracking poverty-reducing expenditures could be adopted. Among them are:

* <u>Measuring resources released for poverty-reducing strategies.</u> The various modalities adopted by creditors for delivering the assistance and their impact on fiscal variables will need to be clearly shown in donors' documents. Government should also be encouraged to include data on poverty-reducing assistance in their budget documents. Some poverty-reducing assistance may not immediately show up in the fiscal accounts. A country may need to set up a special account in the central bank to identify such assistance, and as the

assistance is provided, transfers would be made to the budget as grants. Some other assistance may accrue to public enterprises (write-downs of public enterprise debt guaranteed by the government for example). For a better tracking of overall resources allocated to poverty-reducing strategy, arrangements should be put in place to ensure that such assistance is passed on to the budget.

Medium goal: A comprehensive approach to expenditure tracking. The Public Expenditure Management (PEM) system should be able to determine how the total amount and the detailed allocation of overall poverty-reducing spending change as a result. This requires a baseline against which to assess changes in overall spending. Ideally, a MTEF should provide such baseline. The tracking of the impact of the poverty-reducing strategy on the poverty-related spending would then involve comparing a baseline MTEF, prepared before the strategy, with the strategy. This approach needs a government timely, credible, and transparent accounting, reporting, and auditing system to monitor and report on the budget outturn. The tracking of spending should also assess whether the resources spent actually reach the poor and provide them meaningful benefits. Increased budget allocations to poverty-reducing programs may not have desired impact on poverty if the funds do not actually reach their intended targets or if the programs are poorly designed or implemented.

Short-term approach. In the absence of a baseline MTEF, multi-year fiscal scenarios can help in assessing likely patterns of spending. The simple before-after comparisons can point to planned changes in the spending patterns resulting from poverty-reducing strategy assistance.

6. Financing poverty reduction strategies

This section is adapted from Ames et al. (2001) which asserts that once a country has developed a comprehensive and fully assesses the cost draft of its poverty reduction strategy, it will need to ensure that the strategy can be pursued and financed in a manner that does not jeopardize its macroeconomic stability and growth objectives.

To do so, policy-makers need to clearly assess the domestic and external resources of budget finance. This assessment includes a review of: (1) the existing tax and non-tax revenue base, including the effect of any changes in the tax system envisaged under the poverty reduction strategy, (2) the scope for financing public spending through net domestic borrowing in light of the need to maintain macroeconomic stability and to ensure adequate availability of credit to the private sector in support of private sector development and economic growth, and (3) the scope for external financing that is realistic and sustainable under the present circumstances.

6.1 Poverty incidence of fiscal policy

Fiscal policy can have a direct impact on the poor, both through the government's overall fiscal stance and through the distributional implications of tax policy and public spending. A key aspect of any poverty strategy will be an assessment of the impact of the existing tax and non-tax system on the poor. On the other hand, an important medium-term objective for many developing countries will be to raise domestic revenue levels with a view to provides additional revenue support to their poverty reduction strategies. The major constraint in the poverty reduction context is that revenues should be raised in as economically neutral a manner as possible, while taking into consideration equity concerns and administrative capacities. The essential elements of the poverty-reducing context best tax system are given in Box 2.[3]

In developing countries, taking account of allocation effects means that the tax system in particular should not attempt to affect savings and investment. Experience indicates that these aggregates tend to be incentive to taxes. As regards equity, the tax system should be assessed with respect to its direct and indirect impact on the poor. It is, however, difficult to have a tax system that is both efficient and progressive, particularly in those countries without a well-developed tax administration. Therefore, government will seek to determine a distribution of tax burdens seen as broadly fair rather than use the tax system to achieve drastic income redistribution.

Tax policy should aim at moving toward a system of easily administered taxes with broad bases and moderate marginal rates. Where revenue systems are being administered by a civil service that is highly constrained in term of human resources, technical support, and funding, countries should rely on final withholding, and keep to the absolute minimum any exemptions, special provisions, or multiples rates.

6.2 Poverty incidence of other sources of budget financing

The scope of domestic budgetary financing will depend on a number of factors, including the sustainable rate of monetary growth, the credit requirements of the private sector, the relative productivity of public investment, and the

desired target for the net international reserves. Sacrificing low inflation, through faster monetary growth, to finance additional expenditure is generally not an effective means to reduce poverty because the poor are most vulnerable to price increases.

At the same time, since private sector development stands at the center of any poverty reduction strategy[4], governments need to take into account the extent to which public sector borrowing crowds-out the private sector's access to credit, thereby undermining the country's growth and inflation objectives. Given that at any point in time there is a finite amount of credit available in an economy, policy-makers must therefore assess the relative productivity of public investment versus private investment and determine the amount of domestic budgetary financing that would be consistent with the need to maintain low inflation and support sustainable economic growth.

The amount and type of available resources to finance the budget will vary depending on the particular circumstances facing the country. Countries that have access to external grants need to consider what amount is available and sustainable under the present circumstances. The same is true in case of external debt, but policy-makers also need to determine whether the terms on such borrowing are appropriate and whether the added debt burden is sustainable. To the extent that the country is benefiting from, or may benefit from, external debt relief under the enhanced Heavily Indebted Poor Countries (HIPC) initiative, net resource flows will be freed up to finance poverty-related budgetary expenditure. Domestic debt reduction could also represent a viable use of additional domestic assistance, since it would both free up government resources to be directed at priority expenditure, as well as free up additional domestic credit for use by private sector.

There may be a limit to the amount of additional financing that a country would deem appropriate. For example, there may be absorptive capacity constraints that could drive up domestic wages and prices, as well as appreciate the exchange rate and render the country's exports less competitive, thereby threatening both stability and growth [5]. There may also be uncertainty regarding aid flows, especially over the medium-term, as well as considerations regarding long-term dependency on the external official aid. In the absence of medium-term commitments of aid, policy-makers may therefore wish to be cautious in assuming what levels of assistance would be forthcoming in the future.

7. Participation in budget formulation and Implementation

There is a consensus in the literature analyzed that, although there are problems, constraints, tensions and unexpected results deriving from Participatory Budgeting (PB), is certainly an important step, with implications regarding the state's role in facilitating citizen participation in policy making. Certainly, the literature on participation has generally been pessimistic about the state's role in improving democracy and in building up democratic institutions. Abers (2000), points out three central problems of participation from that literature:

* Programs usually face the implementation problem which has to do with the fact that, even when governments genuinely seek to implement participatory decision-making mechanisms that would give greater decision-making control to the less powerful, the more powerful are often able to resist such changes successfully;

* The inequality problem that has to do with the fact that even if open forums are created in which all participants formally have an equal right to influence decision-making, socio-economic inequalities tend to inhibit the effective participation of certain groups of people;

* Programs usually face the cooptation problem in that, even if such open forums are genuinely representative, inequalities between governments and participants with respect to control over information and resources tend to lead to the manipulation of participatory venues by government officials.

Despite these views, the empirical literature on experience of budgetary participation evaluates these programs as having been quite successful (Souza, 2001). The reasons provide for such positive evaluation vary as much as the label given to PB. This is because participation implies different things to different people. To some, it is a means of improving efficiency, to others, it is limited to enhancements in social justice, meaning the improved access of people and social groups historically excluded from the decision-making process. To others, participation is nothing more than rhetoric.

The benefits from participation can be found in its capacity to improve policy effectiveness, promote consensus on state actions and gain access to detailed information about policy contexts and real needs of ordinary citizens. Then, the principal goal of participation is the empowerment of social groups that have typically been ignored by social and economic development policies (Souza, 2001).

With participation, multilateral organizations seek transparency, accountability and voice. The "Voice of local people, particularly the poor, can be increased by policy reforms at the national level that allow greater freedom to join non-governmental organizations, trade unions and other bodies to understand better and influence decisions that affect them" (World Bank, 1994 :42). It is then, a way of transforming unorganized people into members of a civil society that can influence (but not decide) issues that directly affect them. It is cautious in respecting the boundaries between the role of popular participation and that of elected officials in representative democracy.

It is shown in the literature that PB has been able to reflect priorities of the poor in budgets (Santos, 1998 and Abers, 1998). However, it less clear as to whether it has been able to reflect the need of non-participants. Desposato (2000), in analyzing the results of a 1991 survey in 150 municipalities across Brazil shows that the poorest and less-educated voters mentioned economic survival concerns (cost of living, low salaries and job opportunities) as their top priority and not infrastructure, which is PB's main focus on investment.

Figures, statements and analyzes also provide sufficient grounds for arguing that PB does increase the capacity of excluded groups to influence investment decisions and that it does increase their access to basic urban services, especially infrastructure (Abers, 2000).

The PB can then be viewed and interpreted differently according to the fields of management, education, politics and social change (Souza, 2001). In the management realm, there is the view that PB is an urban management mechanism with the poor and as a sustained mechanism of joint management of public resources through shared decisions on the allocation of budgetary funds. In the realm of education, PB is considered as an educative process that involves all the key local actors (mayor, bureaucracy, councilors, delegates, grass-root

movements, etc.) as well as the institutions in which they operate. In the political realm, it is viewed that PB increases transparency, accountability and credibility. It is also mentioned that it is a way of breaking down (or challenging) clientelism, authoritarianism and patrimonialism. In the sociological realm, PB allows a fair distribution of scarce resources in an extremely unequal society and is an innovative instrument for the reconstruction of the public life and is a new form of relationship between local public power, popular organizations and the rest of society to address the demands of the poorest segments of the population[6].

8. Conclusion and policy implications

The main conclusions and policy implications that can be drawn fro this discussion, whose purpose was to analyse poverty-oriented budget designing and implementation in Africa and other developing/transition economies through a review of the budgeting objectives, the designing of the medium-term expenditure frameworks, the identifying and costing poverty-oriented expenditures, the tracking of poverty-reducing expenditures, the financing of poverty reduction strategies and, the role of participation in budget policy formulation and implementation, can be briefly stated as follows:

* Budgeting, which is a means of exerting legislative control over resource allocation decisions made by the executive, enable guidance, through technical analysis, of public resource allocation decisions. These decisions are however, taken in a political process, where technical analysis is one of the factors taken into consideration, even though not the most important. A clear distinction was made between development and recurrent budgets in the earlier budget process, which went from planning of

budgets by objectives to program budgeting after incremental budgeting. PRSP is putting program budgeting at the core of budget objectives mainly because it allows governments to eliminate false distinction between investment and recurrent spending. The key factor influencing the durability of such programme budgeting will be whether resources are provided with sufficient stability and certainty to allow programme targets to be met. Significant divergences often noted between budget outcomes and the national ideal or public interests show that, the budgetary problem is obviously that of efficient resource allocation, as well as effective application of decisions;

* A proper tracking of the impact of poverty-reducing strategies requires Medium Term Expenditure Frameworks (MTEF). This has the advantage of providing an ex ante framework within which a realistic perspective of aggregate resources coincide with political policy designed in a transparent process and which ensure on the one hand, that budget financing complies with these priorities and on the other, that expenditures and their effects may be tracked. The fundamental problem of MTEFs is that they involve more tracking and evaluation activities. Insofar as MTEFs demand more tracking and evaluation, it is vital for countries to introduce systems which allow them to track poverty-related expenditure more precisely, which in many African countries do not exit-very few have poverty reduction-focussed MTEFs;

* The tracking of poverty-reducing budgets (programs) sheds light on how the government focuses on designing and implementing poverty-reducing strategies (programs), persuades donors that funds put at their disposal are effectively used to reduce poverty, assures the poor that their fate is effectively taken into account and, to see if the overall goal of poverty reduction is pursued through the ever increasing public expenditure allocation to poverty-reducing programs. There are different approaches of tracking budgetary expenditure which depend on the degree of elaboration of the country's budgetary account. The ultimate aim should be to track all aspects of budget expenditure for their direct and indirect impact on poverty reduction, and not to create separate accounting systems and funds for allocation of poverty-focussed expenditures;

* The increase of economic opportunities, improvement of capacities and delivery of essential services, increasing empowerment and participation, amelioration of security, including food security, and reduction of vulnerability are the major domains of government actions, whose impact on poverty-reduction are significant. Nevertheless, there is need to go beyond traditional 'social sector' expenditures. Government can also spend for poverty reduction in effective decentralization, improvement of budget management, fair judicial system actions to reduce violence measures to mitigate environment disaster risks, transparency and accountability. However, government priorities in each country will depend on national circumstances;

* The financing of poverty-reducing budget must be based on a special tax system that minimizes tax impact on the poor. This tax system must be put in place at the same time as the other internal financing sources (debt and money supply growth) take into account the macroeconomic stability and the degree of crowding-out the private sector of domestic credit (the sector being at

the centre of every genuine poverty-reducing strategy). Likewise, external sources must be envisaged at a level compatible with the need to maintain a sustained and durable macroeconomic stability and growth;

* Though the participatory budgeting poses a few problems, there is a general consensus on its capacity to better reflect the priorities of the poor in budgets. Participation may be viewed and interpreted from the perspective of management as a strong access mechanism to public resource management through participatory budgetary resource allocation decisions. In the social realm, participation contributes in a more equitable distribution of scarce resources. It is also considered as an innovatory instrument of public life and a new form of relation between local government authority, grass-root organizations and the rest of the society in response to the needs of the poor. The key aspects of participation which are vital are: (1) the best and most successful participation process, (2) the stage and the degree of detail the participation should occur, (3) how to balance the interest of different groups and make sure that the poor rather than interest groups are genuinely represented and, (4) how to balance domestic constituencies with the intervention of international and donor organizations to ensure that national priorities are the lead.

The results of the analysis suggest that the quality of political leadership and commitment to poverty reduction are vital factors in any poverty reduction strategy. Nevertheless, there are few aspects, which require more detailed research. They are:

* How African countries can switch to programme budgeting based on attaining the Millennium Development Goals (MDGs);
* Appraising the poverty impact of all budgetary expenditures;
* How to enhance participation to ensure that decentralized budget monitoring by the population becomes the norm in African countries;
* How to make sure that the voices of the poor rather than those of interest groups are heard;
* Appraising the impact of monitoring and evaluation on the African budgetary process;
* Analysing African country's circumstances to see whether the orthodox theories about inflationary effects and crowding out by government expenditure are really valid.

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