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Evaluation of Budget Support in Zambia

Implementation, direct effects and political economy

Stefan Leiderer
Jörg Faust

Evaluation of budget support in Zambia

German Development Institute (DIE)

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Abbreviations

ABB	Activity Based Budgeting
ACP	African, Caribbean and Pacific
AFD	Agence Française de Développement
AfDB	African Development Bank
AIID	Amsterdam Institute for International Development
APT	Annual Performance Tranche
BMZ	German Ministry for Economic Cooperation and Development
BMZ-E	Evaluation and Audit Department of the BMZ
BS	Budget Support
BoZ	Bank of Zambia
CCS	Commitment Control System
CIDA	Canadian International Development Agency
CO	Cabinet Office
COFOG	Classification of the Functions of Government
CP	Cooperating Partner
CPG	Cooperating Partners Group
CPG-HoC	Cooperating Partners Group Heads of Cooperation
CSO	Civil Society Organisation
CSPR	Civil Society for Poverty Reduction
DAC	Development Assistance Committee
DANIDA	Danish International Development Agency
DFID	Department for International Development
DIP	Decentralization Implementation Plan
DIE	German Development Institute

DPs	Development Partners
EAZ	Economic Association of Zambia
EC	European Commission
EU	European Union
EIU	Economist Intelligence Unit
EQ	Evaluation Question
ETC	Economic and Technical Cooperation Unit (of the MoFNP)
FMS	Financial Management System
FNDP	Fifth National Development Plan
GBS	General Budget Support
GDP	Gross Domestic Product
GNI	Gross National Income
GRZ	Government of the Republic of Zambia
HDI	Human Development Index
HIP	Harmonization in Practice
HIPC	Highly Indebted Poor Countries
HLPD	High Level Policy Dialogue
HoC	Heads of Cooperation
HoM	Heads of Mission
HQ	Head Quarter
IDA	International Development Association
IFMIS	Integrated Financial Management Information System
IFS	International Financial Statistics
IMF	International Monetary Fund
INTOSAI	International Organization of Supreme Audit Institutions
IOB	Policy and Operations Evaluation Department

JAR	Joint Annual Review
JASZ	Joint Assistance Strategy for Zambia
JEC	Joint Executive Committee
JSC	Joint Steering Committee
KfW	Kreditanstalt für Wiederaufbau
KPI	Key Performance Indicator
LCMS	Living Conditions Monitoring Survey
LCDs	Least Developed Countries
MACO	Ministry of Agriculture and Cooperatives
MDGs	Millennium Development Goals
MDGT	MDG-Tranche
MDRI	Multilateral Debt Relief Initiative
MMD	Movement for Multi-Party Democracy
MoFNP	Ministry of Finance and National Planning
MoH	Ministry of Health
MoU	Memorandum of Understanding
MPs	Members of Parliament
MPSAs	Ministries, Provinces, and Spending Agencies
MTEF	Medium Term Expenditure Framework
NGO	Non-Governmental Organisation
NOK	Norwegian krone
NORAD	Norwegian Agency for Development Cooperation
NRFA	National Road Fund Agency
OAG	Office of the Auditor General
ODA	Official Development Assistance
OECD	Organisation for Economic Co-Operation and Development

OPM	Oxford Policy Management
DAC	Development Assistance Committee
PAF	Performance Assessment Framework
PEFA	Public Expenditure and Financial Accountability
PEMFA	Public Expenditure Management and Financial Accountability
PFM	Public Finance Management
PRBS	Poverty Reduction Budget Support
PSM	Public Service Management
PRP	Poverty Reduction Programme
PRGF	Poverty Reduction and Growth Facility
PRSP	Poverty Reduction Strategy Paper
PSRP	Public Service Reform Programme
PRS	Poverty Reduction Strategy
RDA	Road Development Agency
ROADSIP	Road Sector Investment Programme
SAG	Sector Advisory Groups
SBS	Sector Budget Support
SDR	Special Drawing Rights
Sida	Swedish International Development Cooperation Agency
SWAp	Sector-Wide Approach
TA	Technical Assistance
TSA	Treasury Single Account
UNIP	United National Independence Party
UNDP	United Nations Development Programme
UK	United Kingdom
UPs	Underlying Principles

WB	World Bank
WDI	World Development Indicators
WHIP	Wider Harmonization in Practice
ZCCM	Zambia Consolidated Copper Limited
ZMK	Zambian kwacha
ZRA	Zambia Revenue Authority

Foreword

This evaluation of the inputs and the direct and induced outputs of budget support in Zambia was commissioned by the Evaluation Department of the German Ministry for International Cooperation and Development. It is part of a more encompassing evaluation which, led by Germany and the Netherlands in cooperation with Sweden, analyses the overall causal chain of budget support in Zambia, from inputs to impacts, in five different sectors. This study profited greatly from background papers of Oliver Saasa and research input by Johannes Schmitt and Maike Pasch as well as from research assistance by Sarah Nohr.

Disclaimer: Relative effectiveness of aid modalities

This report is part of an impact evaluation of budget support in Zambia. It is not an assessment of the relative effectiveness of different aid modalities.

In particular, this evaluation does not compare the effectiveness and/or efficiency of budget support as opposed to project aid as the counterfactual. Nonetheless, it is important to note that intervention logic contains to some extent an implicit counterfactual of traditional project-based aid. This has to do with the genesis of the aid instrument: budget support in its modern form emerged from the international aid effectiveness debate which took off in the 1990's and has so far culminated in the Paris Declaration on Aid Effectiveness and the Accra Agenda for Action.

The Paris/Accra agenda formulates a number of principles for making aid more effective; it has its roots in a widely shared frustration with the limited impact of decades of project-based aid (cf. Faust / Leiderer 2008; Leiderer 2010). It is commonly understood that programme-based approaches, including general and sector budget support, serve to implement these principles. Thus, to the extent that budget support provides inputs that traditional project-based aid does not – at least not in a similar way (e.g. high level policy dialogue, conditionality) - one may argue that there is an implicit counterfactual comparison here between budget support and project aid. However, since this is a country case study, no general conclusions on the (relative) effectiveness of the evaluated aid modality can be drawn from this evaluation. That would require analysis of a much larger number of individual case studies.

Executive summary

This study - commissioned by the German Ministry for Economic Cooperation and Development (BMZ) – evaluates the direct effects (i.e. the direct and induced outputs) of budget support (BS) in Zambia. In cooperation with the Government of Zambia, the present evaluation of BS in Zambia is a joint effort of the Policy and Operations Evaluation Department of the Netherlands Ministry of Foreign Affairs (IOB), the Evaluation and Audit Department of the German Federal Ministry for Economic Cooperation and Development (BMZ-E), and the Secretariat for Evaluation of the Swedish International Development Cooperation Agency (Sida). It is part of an initiative of the Evaluation Unit of the EU (Directorate-General for Development, External Relations and EuropeAid) which aims at assessing the effectiveness of BS and improving the methodology for evaluating this complex instrument of development cooperation.

Intervention logic

Programme-based approaches, including sector and general budget support (SBS/GBS), are core elements of the Paris/Accra Agenda for more effective aid, which emphasizes ownership, harmonization, alignment, managing for results, and mutual accountability (High Level Forum 2005). BS in its modern form is thought by many to represent the most suitable form of aid for implementing these principles in practice (Michel 2008, 22).

Clearly, a core ingredient of BS is financing which is provided with the aim of supporting the implementation of a comprehensive national development programme, such as a poverty reduction strategy (PRS), in the recipient country. In addition to financial resources, however, BS programmes commonly also encompass non-financial contributions in the form of:

- Policy Dialogue
- Conditionality
- Technical Assistance (TA) and Capacity Development

This is because the development partners do not use BS exclusively as a financing instrument for supporting the respective partner country's strategies for reaching the Millennium Development Goals (MDGs) in line with the principles of the Paris Declaration. In providing BS, development partners also aim at strengthening ownership, alignment, results orientation, and mutual accountability through a formalised policy dialogue between donors and partner governments – together with better political leverage for donors to bring about improvements in effectiveness, transparency, corruption control and democratic accountability in the management of public funds (Leiderer 2010, 2). Thus many donors also understand BS as a means of contributing to key reform processes in partner countries with the aim of building more effective public institutions.

Because of this multiplicity of inputs and multi-dimensional objectives of budget support, the effectiveness of BS depends on a complex interaction between financial and non-financial contributions as well as the recipient government's own capacities and dispositions. The present evaluation therefore understands BS in Zambia as a 'package' of financial and non-financial inputs and takes the complex interactions of effects and presumed causal links in the intervention logic of BS into account.

This part of the evaluation focuses on the inputs and the direct and induced output of BS in Zambia. The main evaluation questions (in the following: "EQ") are structured accordingly:

1. **INPUTS:** To what extent are BS mechanisms that have been put in place consistent with Zambia's strategic and policy framework, and how well has the design been adapted to the specific political, economic and institutional context?
2. **DIRECT OUTPUTS:** To what extent has BS in Zambia led to increased external funding subject to the government's own budgetary process, the establishment of a policy dialogue framework, and the harmonization/alignment of external assistance?

3. INDUCED OUTPUTS: Has BS had an impact on fiscal discipline and macroeconomic management, public finance management, public spending and governance, and democratic accountability?

To answer these evaluation questions, this component of the overall evaluation mainly relies on data from three different sources:

- Semi-structured interviews of key stakeholders and experts during two field visits (February – April 2010 and June 2010),
- Existing evaluation reports, reviews, other official documents and academic literature,
- Information on financial flows,
- Micro- and macro-economic data and indicators.

In addition, this report contains elements from a background report delivered by Prof. Oliver Saasa, the principal national consultant for this evaluation component. Moreover, where appropriate, evidence from the sector reports of the overall evaluation was used.

Inputs

EQ 1: To what extent are BS mechanisms that have been put in place consistent with Zambia's strategic and policy framework and how well has the design been adapted to the specific political, economic and institutional context?

EQ 1.1: What inputs have been provided by BS and to what extent do they correspond to the envisaged GBS/SBS inputs?

Financial support

First and foremost, budget support consists in the provision of direct, untargeted funding in support of the budget in general (general budget support – GBS) or specific sector budgets (sector budget support – SBS). In Zambia, Cooperating Partners (CPs) provide budget support in both forms: general Poverty Reduction Budget Support (PRBS) is provided by a PRBS group of six bilateral donors, the European Commission (EC), the African Development Bank (AfDB) and the World

Bank. Sector budget support, on the other hand, is provided by the EC in the sectors Roads and Health and in support of the PEMFA (Public Expenditure Management and Financial Accountability) reform programme, and by the United Kingdom in the health sector.

While the bilateral donors and the EC provide PRBS and SBS as grants, the AfDB and the World Bank give loans. For their part, CPs use different disbursement mechanisms ranging from fixed tranches only (Germany, Finland) to various forms of variable tranches based on overall government performance (UK, The Netherlands) or individual indicators (Norway, Sweden, EU) to floating tranches (WB, AfDB) which are disbursed only after particular policy actions have been taken. The largest share of BS in Zambia (84 % in 2007) is, however, provided in the form of fixed tranches committed on an annual basis.

Since 2007, PRBS CPs not only make annual commitments but also establish a disbursement schedule with monthly commitments in order to improve predictability and facilitate cash flow planning for the Government of the Republic of Zambia (GRZ).

Altogether, from 2002 to 2009, BS to GRZ has increased from US-\$ 65.4 million to US-\$ 248.2 million. Even though in absolute terms BS resources increased substantially over the past years, other aid modalities still play a much more important role in terms of aid volumes. The share of BS in total official development assistance (ODA) to Zambia is still comparatively low at 22.4 % (2008, up from 6.5 % in 2003). For OECD/DAC CPs, the share in 2008 was 30.3 % (2003: 9.4 %).

Policy dialogue

The policy dialogue structure around BS in Zambia is outlined in the joint Memorandum of Understanding (MoU) signed by all PRBS donors and GRZ. The main fora for the regular PRBS dialogue are the Joint Steering Committee (JSC), the Joint Executive Committee (JEC), and the bi-annual meetings taking place as part of the Joint Annual Review (JAR) process.

Joint Steering Committee (JSC): The JSC is the main steering body in the PRBS dialogue architecture and drives the joint GRZ/CP PRBS-agenda. The JSC is composed of both Government and CP representa-

tives, with the CP side represented by three lead donors on a rotational basis.

The JSC is co-chaired by GRZ and CPs and meets quarterly with the following agenda: to discuss progress made with respect to performance indicators agreed on in the PAF, to prepare for review meetings, to act as a forum for dialogue, and to mediate in dispute settlement.

Joint Executive Committee (JEC): The work of the JSC is co-ordinated by a small Joint Executive Committee consisting of three representatives from GRZ and two PRBS Group members. The members are selected by the members of the JSC from amongst themselves and rotate annually. The JEC is responsible for routine coordination activities as well as the preparation of joint reviews and the management of follow-up activities. In case any MoU Signatory wishes to raise a relevant issue for dialogue, the JEC convenes a meeting of both sides to agree upon the dialogue process on the issue in question.

Joint Annual Review (JAR): Besides the quarterly JSC and JEC meetings, GRZ and PRBS signatories meet twice a year as part of a structured annual review process. The JAR meetings are jointly convened by the government and the CPs and are open to the participation of parliamentarians and representatives of civil society.

In sum, the JAR dialogue covers:

- A review of performance, budget execution, and expenditure priorities on the basis of the indicators described in the PAF.
- A review of underlying principles.
- A review of action plans for policy priorities and the following year's national budget, including the link between poverty reduction priorities and inter-sectoral allocations.
- A discussion of the Medium Term Expenditure Framework (MTEF) of GRZ.
- A confirmation of the CPs' BS commitments for the following year.
- A follow-up on audits.

The JAR is also closely linked to other dialogue fora which do not exclusively cover the PRBS process. Most importantly, the review process builds on the sector dialogue conducted in the so-called Sector Advisory Groups (SAGs). In addition, the PRBS policy dialogue is closely linked to the annual High Level Policy Dialogue (HLPD) Meeting between the government and the CP Group (CPG), i.e. the signatories to the Joint Assistance Strategy for Zambia (JASZ).¹ The HLPD is chaired by the Minister of Finance and National Planning. The CPG is subdivided into two sub-groups, namely, the Heads of Cooperation (HoC) and the Heads of Mission (HoM).

There are no specific dialogue mechanisms related to sector budget support operations, since SBS-related issues are usually dealt with either in the context of GBS or within the dialogue structures linked to the SWApS.

Conditionality

As in most other countries receiving BS, the conditionality attached to the provision of budget support funding in Zambia is applied on two levels: the Underlying Principles (UPs) that frame the general mutually agreed-on basis for the provision of budget support; and the Performance Assessment Framework (PAF), which serves to regularly assess the performance of the government (and more recently the CPs as well) in implementing the programme.

PRBS is provided on the basis of a Memorandum of Understanding (MoU) between GRZ and the PRBS group that sets out the jointly agreed terms and procedures for direct budget support from the PRBS Group to the National Development Plan and serves as a co-ordinating framework for consultation with the government, for joint reviews of performance, for common procedures on disbursement, for reporting, and for audits. According to the MoU, PRBS is provided on the precondition of GRZ's commitment to "fight poverty, including through a

¹ All PRBS donors are members of the CPG. Currently included are Canada, Denmark, Finland, France, Germany, Ireland, Italy, Japan, the Netherlands, Norway, Sweden, UK, the United States, the African Development Bank, the European Commission, the IMF, the United Nations System, and the World Bank. Other CPs may attend as observers.

pattern of public expenditure consistent with poverty reduction priorities as identified in the National Development Plan” as a basic principle (GRZ / PRBS Group 2005, 5). In addition, the MoU identifies three Underlying Principles (UPs) for the provision of direct budget support:

- GRZ’s Commitment to peace, democratic principles, the rule of law, good governance and integrity in public life, including the fight against corruption;
- GRZ’s Commitment to public financial management reforms;
- GRZ’s Commitment to pursuing sound macro-economic policies, as evidenced by a positive IMF assessment of overall macro-economic performance.

The UPs are subject to continuous assessment by the PRBS Group as part of the annual review process. This assessment is to a large degree based on the judgement of each CP, meaning that a *perceived* violation of the UPs suffices to initiate the High Level Policy Dialogue prescribed by the MoU. At the same time, a positive assessment of the UPs is a precondition for PRBS commitments on the part of the CPs within the framework of the annual review process. The UPs thus constitute the core of PRBS conditionality and provide a key entry point for CPs into dialogue with GRZ on the overall reform agenda.

In addition, CPs condition their budget support commitments and to some extent their disbursements on progress achieved by GRZ in implementing the National Development Plan. This progress is to be measured according to jointly agreed-on performance indicators as described in a Performance Assessment Framework (PAF), which the MoU defines as “a multi-annual matrix of priority milestones, targets and indicators based on the National Development Plan, Public Expenditure Management and Financial Accountability reforms under the PEMFA programme and related initiatives over time, other components of public service reform, macro-economic stabilisation policy and debt sustainability” (GRZ / PRBS Group 2005, 4).

Since 2006 the PAF has evolved into a comprehensive framework of targets, policy measures and outcome indicators, with the current 2009-2011 PAF covering four main areas of the FNDP, namely: (a) reform

process and financial management (covering decentralization, public sector reform, public finance management, domestic taxation, financial sector); (b) wealth creation (agriculture, infrastructure incl. roads, energy and water, private sector development); (c) social equity (health, education); and (d) cross-cutting issues (HIV/AIDS, environment). Although there has been no major shift in the sector focus, which from the beginning was mainly on the first two pillars; i.e. reform process and wealth creation, the number of targets measuring GRZ performance has increased steadily since 2006, reaching 37 targets in the 2009-2011 PAF.

The use role of the PAF in determining disbursements varies widely between CPs: Two CPs (Germany and Finland) provide BS exclusively in the form of fixed tranches based on overall PAF performance; other CPs (The Netherlands, UK) use different mechanisms to link additional incentive tranches with overall PAF performance; others (Sweden, Norway, and the EC) also base fixed tranches on overall PAF performance, but link their variable tranches with selected PAF indicators; the World Bank and the African Development Bank provide their budget support in the form of floating tranches that are disbursed once a selected set of PAF indicators (prior actions) show successful implementation.

Technical Assistance and capacity building

In order to assist GRZ in improving the quality, efficiency, cost-effectiveness and delivery of public services to its people, CPs have engaged in a number of programmes and initiatives involving technical assistance and capacity development. These activities, partly conducted as accompanying measures of BS, are embedded in the GRZ's own reform agenda. GRZ has been implementing the *Public Service Reform Programme* (PSRP) since 1993. In line with this GRZ programme, the majority of BS donors provide funding to the PEMFA programme, the first component of PSRP. In addition a number of CPs support the government in building capacities at the Office of the Auditor General (OAG) and in Parliament or engage in other forms of BS-related technical assistance.

The objective of PEMFA is to contribute to the efforts of the Government in improving efficiency, effectiveness and democratic account-

ability in the management and utilisation of public financial resources at both the central and sub-national levels. All nine PRBS donors are among the 13 signatories to the PEMFA Memorandum of Understanding.

Contributions by the co-operating partners to the programme budget for the five-year period amounted to US-\$ 72.2 million, of which 55 % or US-\$ 39.7 million had been utilized by March 2009. The PEMFA Programme was (cost-neutrally) extended for one year and ended in 2010.

Over the last ten years, a number of donors including USAID, EU, Finland and Germany and Great Britain have targeted capacity-building projects for Members of Parliament (MPs). Another important TA programme not directly linked to but highly relevant for the PRBS programme is the assistance provided by Germany through GTZ to MoFNP. This programme, in implementation since 2006, aims at supporting MoFNP in integrating the Poverty Reduction Strategy in the budget process.

EQ 1.2: To what extent are BS operations put in place consistent with Zambia's strategic and policy framework and with the overall Development Partners' (DPs) development strategies?

Budget support has been declared as the preferred aid modality by GRZ. This preference is also acknowledged by the donors, who have committed themselves to work towards moving in the direction of this aid modality. First steps on the road to BS were already taken in the 1990s through sector-wide approaches (SWAp) and in 2003 through the Harmonization in Practice (HIP) initiative. In 2005, GRZ launched a Zambia Aid Policy and Strategy (2005) which called for direct BS as the main aid modality. With the formulation of a Joint Assistance Strategy (JASZ) signed by all major donors, the CPs explicitly acknowledged the government's preference for BS and committed themselves "to the extent possible increasingly deliver aid to the government sector through this modality to the extent that GRZ's systems meet established guidelines and standards, and that CP policies support such assistance."

Since then, BS operations in Zambia (i.e. financial and non-financial contributions) have been largely in line with the national strategic framework and priorities. There is no direct evidence that the principle of alignment has been voluntarily infringed on by CPs. With regard to the different budget support inputs, the evaluation found the following:

- *Funding* – Measured against the government’s regularly updated medium term financial plans, budget support in Zambia has provided fairly reliable funding. However, when measured against the estimated funding gap in the GRZ’s Fifth National Development Plan (FNDP), BS funding falls significantly short of what has been considered necessary to meet the ambitious poverty reduction and development goals formulated in the FNDP.
- *Policy Dialogue* – Altogether, it can be argued that the PRBS dialogue focuses mostly on reform programmes and sectors identified as GRZ priorities in the FNDP. However, the FNDP has been formulated in a rather broad way and is not very explicit when it comes to prioritization and concrete reform implementation. As a consequence, formal alignment for CPs towards the FNDP is relatively easy and does not exclude the possibility that concrete reform steps in specific sectors or even cross-cutting issues might not be driven by international agencies.
- *Conditionality* – By and large, the two major components of conditionality attached to the provision of BS in Zambia are consistent with the overall intervention logic implied in the provision of BS. However, a more detailed analysis of conditionality in the Zambian BS process reveals three major weaknesses:
 - The PAF has too many indicators. This complicates policy prioritization. Moreover, there is no inherent logic within the PAF, which explains the different use of process and outcome indicators.
 - Disbursement mechanisms related to the indicators and targets of the PAF do not correspond to a homogeneous incentive system but rather respond to the different logics of the individual CPs within the PRBS group.

- The conditionality of the UPs is formulated in such a way that it provides extensive manoeuvring space for individual CPs in interpreting the process of political reform in Zambia. This in turn creates a large potential for collective action problems among CPs when it comes to interpreting the course of reforms.
- *Technical Assistance* – BS-related TA and Capacity Building efforts are consistent with both GRZ and CP strategic frameworks:
 - The PEMFA programme is one of three pillars under the Public Sector Reform Programme of the FNDD. As such, CP support for the PEMFA programme is fully in line with GRZ’s strategy and policy framework.
 - Building on the Joint Assistance Strategy for Zambia in 2008, the CP Group developed and signed a Code of Conduct on Capacity Development aimed at improving “*the effectiveness, efficiency and impact of technical assistance from both project support and direct budget support to Zambia*”. This Code of Practice formulates 15 principles on how to provide TA, including the principle of supporting country-led programmes for capacity development and providing this support in a coherent, coordinated and programmatic manner.

EQ 1.3: How well was the design of GBS/SBS inputs adapted to the specific political, economic and institutional context of Zambia?

The PRBS-MoU formulates principles for the provision of budget support in Zambia. These Underlying Principles (UPs) do not impose any specific structures or policies on GRZ and allow the CPs to align their inputs with the existing political, economic and institutional context of Zambia. Therefore it can be argued in principle that BS inputs in Zambia are well aligned to the specific economic and institutional context in Zambia and thus allow for genuine democratic ownership of the processes involved.

However, some deficiencies with regard to institutional alignment, participation and democratic ownership in the policy dialogue exist: Even though the key dialogue processes are open to civil society participa-

tion, the involvement of CSOs or, for instance, parliamentarians, has been less than satisfactory in actual practice.

In addition, the political realities to some extent create incentives for CPs to sideline existing institutions, yet without the results hoped for. For instance, the structure for PRBS policy dialogue in principle builds on existing structures and is well integrated with other dialogue fora, such as the High Level Policy Dialogue conducted by the CP Group of signatories to the Joint Assistance Strategy (JASZ), or the sector dialogue taking place in the 21 Sector Advisory Groups (SAGs). The poor performance of some SAGs has led CPs to incorporate specific sector issues into the PRBS dialogue with the aim of bringing them to a higher level of policy dialogue. This strategy, however, requires a coherent policy formulation capacity on the partner side. In practice, however, the Ministry of Finance and National Planning has not been able to exercise its coordination function *vis-à-vis* all sector ministries effectively.

Moreover, serious weaknesses exist with regard to information management and record keeping for key PRBS processes. Despite the complexity of the PRBS and related dialogue processes there is no institutionalised and effective joint knowledge and information management system regarding these processes on either side of the aid relationship: MoFNP clearly has insufficient capacities for providing effective monitoring and information management for PRBS processes. This weakness negatively affects many aspects of GBS/SBS operations, but so far the CPs too have failed to remedy this by supporting the MoFNP in this particular capacity or by assuming this important function themselves in a harmonized way and without creating substantial transaction costs. In this respect, BS operations have not been fully adapted to the intervention logic that highlights the importance of the alignment principle.

- On the GRZ side, the Ministry of Finance’s Economic and Technical Cooperation (ETC) Unit, which has the prime responsibility for engaging and coordinating the CPs, was organised by donor desks up to the end of 2009. This setup did not facilitate sector or issue-related information management in support of PRBS dialogue processes.

- On the side of the cooperating partners, the lead donors represented in the key PRBS dialogue are responsible for preparing meetings and moderating discussions. However, they do not have specifically dedicated resources for engaging in joint and sustainable knowledge management. Thus, a large part of the preparatory and analytical work is done by the actors individually and often repetitively. This deficiency not only has created unnecessary administrative costs for both CPs and GRZ but has also hampered the emergence of common positions among the CPs of the PRBS group.

Direct outputs

EQ 2: To what extent has BS in Zambia led to increased external funding subject to government's budgetary process, the establishment of a policy dialogue framework and to harmonization/alignment of external assistance?

EQ 2.1: To what extent has BS contributed to an increased size and share of external funding subject to government's budgetary process and improved the predictability of overall flows of external assistance

Budget support has increased the size and share of aid subject to GRZ's budgetary processes, while also facilitating planning, accounting, and reporting procedures for the government with regard to aid inflows. However, this has not happened at a level where a substantial reduction of the overall transaction costs of development cooperation could be expected.

The extent to which budget support has increased the share of external support channelled through GRZ's own budget processes varies according to the data source employed: An analysis which uses IMF data on GRZ receipts of grants and budget support puts the proportion of budget support in total grants at an average of 29 % in the 2005-2009 period, compared to 19 % for the years 2002-2004. An analysis based on MoFNP data, on the other hand, shows a significantly higher share of budget support in total grants, with a peak in 2006, when PRBS grants accounted for 53 % of grants and total budget support (including SBS) accounted for 68 % of grants.

According to OECD/DAC data, the budget support share of total ODA receipts (excluding debt relief) has increased from 6.5 % to 22.4 % since 2003. For OECD/DAC donors only, the share of budget support in total ODA rose from 9.4 % in 2003 to 30.3 % in 2008.

The share of external support in public expenditure has been decreasing over the past years. This is not due to diminishing amounts of aid but is a consequence of the fact that domestic budget allocations have grown substantially faster than external funding: The share of domestic allocations in total allocations grew from a mere 62 % in 2003 to 85 % in 2009.

Depending on the data source, the share of BS resources in total government expenditures was a mere 5.4 % (IMF) or 6.17 % (GRZ) between 2005 and 2009. In comparison, project support accounted for an average 13.56 % of government expenditures over the same time span.

- Compared to many other BS recipient countries, GRZ's dependency on BS to fund its public expenditures is thus relatively limited.
- Increasing the share of aid resources that are subject to GRZ's own planning and budgeting processes has given budget support the potential to improve the allocative efficiency of public expenditures in Zambia. At the same time, however, no substantial reduction of transaction costs on either side of the aid relation can be expected from this, since the amount of off-budget aid requiring parallel planning, administration, and reporting processes is still substantial.
- Aid predictability in Zambia in general is fairly poor; this seriously undermines the effectiveness of GRZ planning and cash flow management. This applies in particular to project-based aid, but also to PRBS funding: In 2007, for instance, a mere 77 % of PRBS commitments were disbursed; in 2008, disbursements were 15 % higher than commitments.
- However, the main problem for PRBS predictability is with its timing rather than with the amounts disbursed. Late disbursements affect budget implementation, since unused funds must be returned from line ministries to the Treasury. PRBS funds were delayed on

average by 5.03 months in 2007, 0.78 months in 2008, and 3.11 months in 2009.

EQ 2.2: To what extent has BS contributed to the establishment of a framework of policy dialogue, focused on key government strategies and priorities?

A comprehensive dialogue structure has been established around the BS process; this provides the basis for regular and structured policy dialogue. This structure has helped in the discussion of conflicting interests on conditionality and funding. In this regard, the established structures have provided strong incentives against further fragmentation of the dialogue process. On the other hand, however, the dialogue process has been plagued with deficiencies that mainly relate to the persistent fragmentation on both sides of the dialogue process. Setting up complex dialogue structures with important functions for an ambitious aid instrument such as BS requires strong capacity and the political will to manage these dialogue structures in an effective and efficient manner. While both CPs and GRZ have continuously expressed their intention to do so in their rhetoric, the *de facto* capacity on both sides has been limited.

Even though there have been both periods of inactivity and accelerated progress, there is evidence that the policy dialogue in connection with budget support has helped alignment and harmonization processes. Importantly, the dialogue structures showed some institutional stress resistance at times when the operational effectiveness of the dialogue structures was put to the test during the corruption crisis in 2009.

For this reason, the established dialogue processes provided a valuable firewall against further fragmentation; the established mechanisms gave CPs and GRZ a platform for dealing with highly controversial issues. In this regard, the dialogue mechanisms were indeed fruitful in preventing the implosion of harmonization and alignment attempts during times of crisis, because they provided – at least to some extent - an institutional and organizational foundation for the intervention logic of budget support. Despite all the deficiencies of the dialogue process itself, this often implicit value of the dialogue structure should not be underestimated.

One important collective action problem, however, weakens the BS dialogue's focus on key government priorities: the specific sector interests of many individual CPs. A strong move towards harmonization and alignment, compatible with the intervention logic of BS, would weaken many CPs' special relations with sector ministries and would subordinate their sector interests to a coherent national planning system with the finance ministry as the prime player. In this regard, the sector interests of individual CPs and the interests of sector ministries to restrain the coordinating function of the finance ministry come together in an "unholy" alliance against the intervention logic of BS.

EQ 2.3 To what extent has BS contributed to the provision of non-financial inputs, such as technical assistance and capacity building, which are considered as strategic government priorities?

In line with the principles of the Paris Declaration, the PEMFA programme is using a multi-donor basket funding mechanism managed by a dedicated secretariat within the MoFNP; this mechanism should in principle ensure adequate ownership, alignment, and harmonization of the provided Capacity Building. However, budget support-related TA and Capacity Building in Zambia have been less effective than would have been hoped for. In practice, for example, PEMFA was perceived by some as being primarily an avenue for PRBS donors to control fiduciary risks, rather than as a genuine capacity development programme owned and led by GRZ. In particular, while MoFNP as a natural ally for most of the reforms supported by the PEMFA programme may actually exhibit sufficiently strong ownership at the top management level, this is not necessarily true at all lower levels and in all other parts of government. In addition, the programme's design may have been too ambitious in terms of coverage to be effectively managed by MoFNP.

EQ 2.4: To what extent has BS contributed to harmonization and alignment of external assistance, and reduced transaction costs over time?

Budget support has increased the size and share of aid subject to GRZ's budgetary processes; it has facilitated planning, accounting, and reporting procedures for the government with regard to aid inflows; however, this has not happened at a level where a substantial reduction of the

overall transaction costs of development cooperation could be expected.

With regard to non-financial contributions, however, coordination with CP activities not directly linked to the provision of budget support was insufficient to have a substantial effect on aid harmonization and alignment beyond the directly PRBS-related activities.

For instance, there is no coherent and harmonised approach to Capacity Development under which a formalized system of coordination and dialogue on TA activities could be established. As a consequence, the PEMFA programme was insufficiently coordinated with other TA activities, and while PEMFA provided a strong framework for donor coordination and harmonization within the programme and for PFM-dialogue with GRZ, CPs seem to have lost sight to some extent of its need for coordination with other TA outside PEMFA (and provided through other aid modalities). As a consequence, no formalised coordination and information exchange mechanisms with other TA activities have been established.

Induced outputs

EQ 3: Did BS have an impact on fiscal discipline and macroeconomic management, public finance management, public spending and governance and democratic accountability?

EQ 3.1: To what extent did BS contribute to the improvement in fiscal discipline and macroeconomic management?

Over the past years, GRZ has performed fairly well with regard to macro-economic management and fiscal discipline. However, these positive developments were predominantly due to strong economic growth (as a result of the resource boom) and debt relief, rather than to BS. Nonetheless, BS certainly helped to maintain fiscal discipline, in particular during the international financial and economic crisis. Prudent macroeconomic policies and significant structural reforms associated with HIPC/MDRI debt relief sparked the economic turnaround seen in the last decade: external and domestic debt has been brought

down to moderate levels, and international reserves have increased significantly.

EQ 3.2: To what extent did BS contribute to an improvement of budget management and overall PFM?

Notwithstanding repeated delays in the implementation of reforms and the continued need for further strengthening of the PFM system, PRBS has contributed to substantial improvements in the management of public finances in Zambia. The most recent PEFA assessment, conducted in 2008, confirmed that PFM performance in Zambia has improved in all dimensions of the PEFA indicators. This overall positive assessment of GRZ's efforts to strengthen its PFM system is largely shared by the IMF. Nevertheless, a broad consensus seems to exist among actors on both sides of the aid relation as well as within civil society that these achievements were predominantly due to the general focus of the PRBS dialogue and the Underlying Principles; in turn, PFM-related PAF conditionality is generally not perceived as a decisive factor in creating effective incentives for the government to strengthen its PFM.

At the same time, Zambia's PFM system continues to exhibit significant weaknesses, even in those areas that are arguably of particular relevance for PRBS effectiveness and the minimisation of fiduciary risks such as policy-based budgeting, budget variance, and expenditure controls.

With regard to external budget oversight, further improvements are necessary. In particular, even though the effectiveness of the Auditor General's Office has improved significantly, important challenges with regard to follow-ups of audit findings remain. In particular, follow-up actions by Government to remedy audit findings have not always been satisfactory.

EQ 3.3: To what extent did BS contribute to the level and composition of public spending?

In nominal terms, total budget allocations increased by 113 % or an annual average of 13.73 % between 2003 and 2009. This vast increase, however, needs to be weighed against an average annual inflation rate of about 15 % over the same period. The marginal contribution of

budget support to expenditure growth varied substantially over the period from 2004 to 2009. While the additional inflow of budget support resources in 2005 and 2009 contributed about a fifth of the year-on-year change in expenditures from 2004 to 2005 and from 2008 to 2009, the contributions for 2005/6 and 2006/7 were merely 3.76 and 5.70 %, respectively.

Exchange rates play an important role for the contribution of budget support to budget resources available to the government.

- BS facilitated the increase in GRZ budgets and expenditure between 2006 and 2009. Nevertheless, the contribution of PRBS increases to the total budget growth has been relatively modest: In current prices, year-on-year budget support increases contributed an average of 12.49 % to nominal expenditure growth. Of the 34 % increase in real expenditures between 2006 and 2009, 16.5 %, or 5.6 percentage points, can be explained by the increase in budget support resources.
- Nevertheless, despite the relatively small share of budget support in government expenditures and its poor performance against FNDP fiscal targets, there is evidence that the resources provided are decidedly more important for the government's fiscal leeway than their relatively small budget share would suggest. This is because domestic revenue barely covers – mostly statutory – recurrent expenditures. For discretionary spending, and in particular for capital expenditures, the government still relies heavily (if not exclusively) on loans and grants.

Additionality: Revenue side fungibility

At an average 18 % of government revenue (excluding grants) as per cent of GDP between 2004 and 2008, Zambia's revenue performance was consistently above the average of 16.3 % for the group of low-income countries in Sub-Saharan Africa. This is against a continued decline during the period from 2000 to 2006, when the tax-to-GDP ratio declined from 19.2 to 17.0 %. In 2008, revenue (excluding grants) reached 18.6 % of GDP, which is in line with the target set in the Fifth National Development Plan for a revenue-to-GDP ratio of more than 18 % by 2010.

According to data provided by the CPs, revenue grew in real terms by 23 % between 2002 and 2008. This was the result of a domestic revenue growth of 50 %, whereas total budget support and project grants shrank by 35 %. According to MoFNP data, tax revenue grew in real terms by 26 % between 2004 and 2008 alone.

- In view of the substantial increases in domestic revenue over the past decade or so, it seems safe to say that budget support funding in Zambia is predominantly additional to domestic financing. There is no evidence for substantial crowding out of domestic resources in the sense that the provision of budget support might have led to a reduction in domestic revenue mobilisation.
- Nonetheless, there is scope for further increasing the tax-to-GDP ratio by broadening the tax base and taxing the mining sector more heavily. However, it must be doubted whether the domestic tax effort would increase substantially in Zambia in the absence of budget support. In fact, with non-traditional donors (particularly China) playing an increasingly important role as providers of external funding in Zambia, it can be assumed that GRZ could relatively easily find sources of funding other than taxes should PRBS donors decide to reduce or stop providing budget support.
- Moreover, revenue-side fungibility in Zambia is not specific to any particular aid modality. Rather, the degree of fungibility could be expected to be substantially the same if the amounts of aid currently provided in the form of budget support were to be provided in project form instead.

Allocative efficiency

At an aggregate sector level, expenditures from 2006 to 2009 were only partly in line with FNDP sector priorities and fiscal targets for the domestic budget. It is noteworthy that performance was best in the social sectors health and education, where the government controls the most important share of resources. In education (health), the average deviation of expenditures from the domestic fiscal target was 0.84 (2.17) percentage points, or an average of 10.29 % (12.08 %) of the projected share in the domestic budget. In agriculture and roads, both

of which are ostensibly more politicized and, at the same time, receive relatively more support in form of projects, the variance between projected domestic budget shares and expenditure was larger (21.87 %, 39.20 %) and has been increasing over the past years.

- With regard to the social sectors, budget allocations and expenditures in Zambia are roughly in line with strategic priorities as set out in the Fifth National Development Plan and can be considered fairly pro-poor. Budget support resources – while certainly not decisive for this allocation pattern – can be argued to have facilitated significant increases in social sector spending.
- There is evidence that in these sectors BS did not crowd out (but rather crowded in) domestic resources, and that by and large budget support is financing the right priorities in Zambia. A continuous concern is the persistently high wage bill, which poses a potential threat to the implementation and continuation of (investments in) poverty reduction programmes.
- Notwithstanding the persistently large share of General Public Services in overall expenditures, at an aggregate level GRZ thus made fairly reasonable use of additional resources from a development and poverty reduction perspective: of the real expenditure growth of 29.1 % between 2006 and 2008, the largest share was spent on Economic Affairs (20.4 %), Social Protection (19.8 %), Health (14.2 %), and Education (12.8 %). Only 5.1 % of the additional resources were used for defence, and only 3 % for Public Order and Safety.
- Of the fiscal space in excess of statutory expenditures, which was created at least in part by budget support, roughly half was spent on pro-poor priority spending sectors.

Poverty orientation of the budget

Overall, the budget has become more pro-poor in past years. Total allocations to PRPs during the 2005 to 2009 period averaged 45.78 % of the total budget from all the sectors and provinces.

- However, infra-sector and sub-sector spending does not necessarily always reflect pro-poor priorities. For instance, in education a bias

towards urban over rural areas can be observed; in agriculture, the budget is found to be dominated by input subsidies that reach only about 15 % of the farmers, who, in addition, are among the financially better-off.

- An issue of concern with regard to the poverty orientation of the budget is the small and decreasing share of capital expenditure in total spending. This development poses a threat to the implementation and continuation of investments in poverty reduction programmes and already has contributed to a general deterioration in the infrastructure.
- Notwithstanding these developments, poverty-related expenditures did increase as a share of the total budget and as a share of GDP. This was in particular a result of the increases in expenditures for health and education, but also due to an increase in spending on agriculture, from 2 % in 2000 to 7.6 % in 2007.

EQ 3.4: To what extent did BS contribute to an improvement of policy processes and policy implementation (including ownership and transparency)?

The quality of policy processes, especially in relation to transparent and accountable, public financial management in Zambia, is still low due to serious capacity shortages, coordination problems, and several political challenges. Nevertheless, these processes have slightly improved between 2005/6 and 2008; since 2009, however, it has been difficult to maintain the momentum of this development. Nevertheless, at least a partial contribution of BS to some policy reform processes can be mentioned:

- The reform of the budget calendar approved by the end of 2009 and implemented in 2010 can be partly attributed to the BS High Level Policy Dialogue (HLPD). In the follow-up to the scandal in the health sector, the PRBS CPs put strong emphasis on the issue of reforming the budget calendar, and the subsequent reform by GRZ will most likely improve budget planning and policy implementation. However, the political cost to GRZ of implementing this reform is relatively low.

- Support for the decentralization process has also been an area where the PRBS had some, if limited, success. The overall political and fiscal decentralization process in Zambia has been weak, and has stagnated for several years despite some initiatives of GRZ. A constitutional reform necessary for strengthening both the political independence of local governments (direct election of mayors) and the ‘demand-side’ of decentralization seems currently politically unviable. There has also been little success in improving transparency and non-discretionary practices in the fiscal transfer system, mainly because of strong resistance on the part of sector ministries. Despite constant complaints from the PRBS group and other CPs about this slow progress, the Decentralization Implementation Plan (DIP) was not approved by the Cabinet until early 2010. Prior to this event, pressure to pass the DIP through Cabinet increased substantially in the context of both the health scandal and increasing rumours that a further report by the auditor general would reveal similar challenges in the road sector. Thus the BS HLPD was helpful in achieving this reform step, since at least some of the PRBS parties signalled to GRZ that they would consider further delay as an additional political sign of non-compliance with the Underlying Principles. As in the case of the reform of the budget calendar, however, the approval of the DIP by the Cabinet has not yet involved significant political costs because the implementation process has not yet gained strong momentum.

EQ 3.5: To what extent have there been improvements in governance and democratic accountability, particularly regarding the relative roles of parliament and civil society in relation to the budget?

When assessing the effect of BS on the quality of policy processes and governance, one has to keep in mind the difficult political environment in Zambia. Nevertheless, and with all due caution regarding remaining attribution problems, the existing evidence suggests at least mildly positive effects on policy processes and overall governance quality. However, the potential of the instrument has been constrained by three factors:

- First, while the period from 2006 to 2010 showed an overall upward trend regarding some core governance indicators, the *ownership for improving core governance dimensions* has decreased over the last two years.
- Second, *the internal construction of an effective overall incentive system of financial and non-financial BS components* has been limited due to collective action problems within the PRBS group in relation to policy dialogue, conditionality and disbursement procedures.
- Third, the overall deficient external incentive structure in which the financial and non-financial components of BS are embedded has limited the leverage of the instrument as a whole with regard to broader governance reforms. Overall, dependence on external aid from DAC-members has decreased due to the natural resource boom together with the rising importance of China as an external partner of Zambia.

Despite these problems, one can consider BS as one of the few remaining (external) factors that have built up certain leverage against further deterioration of governance in the last two years. The PRBS group – despite substantial harmonization deficiencies – is still the most coherent external constellation of actors and has partly functioned as a substitute for the weakness in domestic power-sharing arrangements.

There are two main reasons why BS – despite its weaknesses – is able to have some effect on governance-related issues in the long run, and to prevent further deterioration of transparency, accountability and democratic processes in the short run:

- First, the financial weight of BS for the government is still considerable when measured in terms of the “fiscal space” for development-oriented investments which are necessary for maintaining political support.
- Second, given the political competition in Zambia’s electoral democracy, receiving BS is politically important for the GRZ *vis-à-vis* the opposition. Thus GRZ is willing to make at least some concessions to the PRBS group because the suspension of BS would give the

political opposition an opportunity to further increase its electoral support, which has been rising during the period from 2009 to 2010.

EQ 3.6: To what extent has the rule of law improved in the country?

Zambia is ranked slightly above the Sub-Saharan African average with regard to various governance indicators, including corruption and the rule of law. With regard to corruption, the World Bank Governance Indicators also suggest an improving trend since 2004 (which nevertheless has slightly reversed since 2009). Given the only modest changes and remaining standard deviations, one should be very cautious in interpreting slight changes as robust evidence. Overall, one cannot say that the rule of law in Zambia has substantially improved. On the one hand, it could be argued that the strengthening of the General Auditor's Office and its increasing capacity to oversee public spending and to detect misbehaviour on the part of public officials is a sign of improving the rule of law. On the other hand, however, the consequences drawn from misappropriation scandals have been modest at best, given the fact that prosecution of the politicians involved has been very slow. This is a sign of either a lack of capacity on the part of the public prosecution entities or their lack of independence vis-à-vis political influence. While permanent violations of basic physical integrity are not a structural feature of the Zambian political system, intimidation of outspoken opposition candidates has occurred in the last two years and provides some evidence that the GRZ is at least partially attempting to inhibit free expression in the upcoming electoral competition. Moreover, access to justice for the large group of marginalized citizens is still very difficult and has not improved over the recent years. With regard to the effectiveness of BS, one can say that it has contributed in a narrow sense to an improvement of the rule of law by strengthening the General Auditor's office. However, there were little systemic effects of this instrument on the general situation of the rule of law in Zambia.

Political economy interpretation and conclusions

Despite positive developments in the harmonization and alignment of development policies in Zambia during the last decade, the non-financial inputs of BS to Zambia are not completely in line with the Paris

principles. An analysis of the design of policy dialogue, conditionality and technical assistance & capacity building shows several deficiencies that have hampered its effectiveness.

- The alignment of BS processes towards the national development plan and policies is generally provided for. As the preferred aid modality, BS is consistent with the *Zambian Aid Policy and Strategy* and the PAF indicators used for PRBS assessment tie in with the key performance indicators of the FNDP progress assessments.
- With respect to harmonization the non-financial inputs provided do not meet the requirements set out in the conceptual framework. According to the basic assumptions on the effectiveness of BS, Zambia belongs to the group of countries in which policies and political dialogue, along with performance assessment and disbursement mechanisms, must be coordinated and harmonized for the most part by the CPs themselves. CPs in Lusaka, for example, have made progress by setting up structures and coordination mechanisms for a harmonized BS approach and have even managed to more or less maintain a harmonized approach in times of crisis. On the other hand, recent events in the health sector and a scandal in the road sector have also shown the limits of harmonization. The variety of pretensions by individual CPs in Zambia impede the possibility of sending out a coherent signal to GRZ and therefore weaken the potential of aid as an instrument for building a coherent system of incentives for strengthening development orientation from within the *Zambian system*.
- With regard to government ownership, there are clear signs of differing intensities of CP dominance of the three areas of non-financial inputs. It is clear that there is an asymmetrical relationship between the government and the CPs which are signatories to the PRBS, with the latter exercising a predominant but often incoherent influence over the former. The asymmetrical relationships in the PRBS MoU have not facilitated clear opportunities for the government to be “in the driver’s seat”. In this respect, BS has demonstrably been ineffective in pushing the country ownership agenda. There is no ‘reprimand’ mechanism with regard to defaulting CPs under

the MoU currently governing the PRBS. All provisions under the MoU that are related to conditionality elements presuppose that defaulting will always take place within the government and that a reprimand for ‚wrong-doing‘ is thus applicable only to the government. This has adverse implications for the quality of dialogue under this BS arrangement - a state of affairs that is not in line with the tenets of the Paris Declaration. Existing evidence shows that, in certain important aspects, the government has been more compliant than the CPs.

- The observed incoherencies in disbursement mechanisms and the PAF and the responses to potential violations of the Underlying Principles are often driven by political considerations in the domestic headquarters of CPs, which respond more to political constellations at home than to local harmonization necessities . Since local aid managers in Lusaka, for example, are not confronted with a strong “pull” for alignment by GRZ, they have tended to react primarily to incentives arriving from individual CP headquarters, thus introducing centrifugal elements into both the dialogue process and the incentive mechanisms.

1 Introduction

This study – commissioned by the German Ministry for Economic Cooperation and Development (BMZ) – evaluated the direct effects (direct and induced outputs) of Budget Support (BS) in Zambia. The evaluation is embedded in the specific context of Zambia and is based on an explicit intervention logic covering financial and non-financial contributions of BS. As such, the evaluation focuses upon strategies of the cooperating partners in providing BS, the process and structure of donor harmonization and alignment with government policies and systems (outputs), and the effects of BS on induced outputs such as institutional performance, public financial management, and allocative and operational efficiency.

1.1 Context of the evaluation

This evaluation is part of an initiative of the Evaluation Unit of the EU (Directorate-General for Development, External Relations and EuropeAid) with the aim of assessing the effectiveness of BS and improving the methodology for evaluating this complex instrument of development cooperation. Guided by the principles of the Paris-Declaration, evaluation units of EU member states and the EC set up a management group in 2008 to accompany the overall evaluation process. Based upon an EC-commissioned “issue paper”, two preliminary papers on methodology were drafted, and different evaluation teams were set up to assess the effectiveness of BS in three African countries: Mali, Zambia and Tanzania.

In cooperation with the Government of Zambia, the present evaluation of BS in Zambia represents a joint effort of the Policy and Operations Evaluation Department of the Netherlands Ministry of Foreign Affairs (IOB), the Evaluation and Audit Department of the German Federal Ministry for Economic Cooperation and Development (BMZ-E), and the Secretariat for Evaluation of the Swedish International Development Cooperation Agency (Sida).

Different parts of the overall evaluation were carried out by the Amsterdam Institute for International Development (AIID), the German Development Institute (DIE), IOB, the evaluation unit of the KfW Development Bank, and Oxford Policy Management (OPM).

Hence, the present study is part of a larger set of assessments which aims at tracing the causal effects of budget support in Zambia from inputs through direct and induced outputs and outcome to the level of ultimate impact. Impact is assessed in different sectors; agriculture, education, health and infrastructure (see Table 1). The overall assessment also comprises an analysis of BS and macroeconomic stability and a study on service delivery, income and poverty reduction. The division of labour among the above-mentioned evaluation and research organizations is related to the ambitious goal of providing a comprehensive assessment of BS effectiveness in Zam-

Table 1: Content and organizational responsibilities of the overall evaluation		
Content / Area Evaluated	Organization	Level
Direct impact of BS on government policies	German Development Institute (commissioned by BMZ-E)	Focus on inputs and induced outputs of BS
Agriculture	Oxford Policy Management (commissioned by Sida)	Focus on outcomes and impact of BS in agriculture
Education	IOB and the Ministry of Education of Zambia	Focus on outcomes and impact of BS in education
Health	AIID, commissioned by IOB	Focus on outcomes and impact of BS in health
Infrastructure	KfW Development Bank	Focus on outcomes and impact of BS in infrastructure (roads; water and sanitation).
Macroeconomic Impact	AIID / MoFNP / Zambian consultant	Focus on the Induced Output of BS
Service delivery, income and poverty reduction	IOB / Zambian Consultant	Focus on Outcomes and Impact of BS
Source: Own compilation		

bia, ranging from the input level to the outcome and impact level in several sectors (see Table 1). To achieve this goal, and to advance methodological knowledge on how to best evaluate BS, the overall evaluation relies on different (qualitative and quantitative) comparative methods. These methods were selected according to their appropriateness for answering various evaluation questions, with a specific focus on different aspects of intervention logic.

1.2 Rationale and intervention logic of budget support

“I know that budget support is controversial. Although I can accept that there may be situations where this form of aid is impracticable, I am convinced that, where circumstances permit, budget support is the most effective instrument of development” (Louis Michel, European Commissioner for Development and Humanitarian Aid 2004-2009 (Michel 2008, 3)).

1.2.1 Rationale for budget support

Programme-based approaches, including sector and general budget support (SBS/GBS), are core elements of the Paris/Accra Agenda for more effective aid, with its emphasis on ownership, harmonization, alignment, managing for results, and mutual accountability (High Level Forum 2005). This agenda emerged from an intense international debate since the mid-1990s centred mainly on the modalities and instruments best suited to improving the effectiveness of international development aid (Leiderer 2010).

BS in its modern form is thought by many to represent the most suitable form of aid for implementing these principles in practice (Michel 2008, 22). Although definitions of BS used by aid agencies differ, they all share the notion of BS as a form of direct financial support to a recipient country’s budget with the aim of providing flexible funding for country-led poverty reduction efforts (Koeberle / Stavreski 2006, 7).² In current usage – although conceptually incomplete – BS refers to predictable, usually

2 Probably the most widely accepted definition is the one by the OECD/DAC that focuses on the financial aspects of BS and defines the instrument as “a method of financing a partner country’s budget through a transfer of resources from an external financing agency to the partner government’s national treasury. The funds thus transferred are managed in accordance with the recipient’s budgetary procedures” (OECD/DAC 2006, 26).

annual, aid flows that are disbursed in response to a – mostly low-income - country's progress in implementing a national poverty reduction strategy (PRS) (Koeberle / Stavreski 2006, 5).

As a *financing instrument* BS seeks to contribute to:

- (i) the promotion of government ownership and accountability through the use of recipient systems and procedures and a strict alignment of support with the recipient governments' own development strategies and programmes;
- (ii) the reduction of transaction costs of aid delivery;
- (iii) the harmonization of donor procedures through the establishment of joint mechanisms for monitoring, disbursement, etc.;
- (iv) the improvement of aid predictability in order to strengthen the ability of governments to plan with aid resources.

Importantly, however, development partners do not use BS exclusively as a financing instrument aimed at supporting national strategies for reaching the Millennium Development Goals (MDGs) in line with the principles of the Paris Declaration. In providing BS, development partners also aim at strengthening ownership, alignment with recipient governments' own development strategies and programmes, results orientation, and mutual accountability through a formalised policy dialogue between donors and partner governments – together with better political leverage for donors to bring about improvements in terms of transparency, effectiveness, and corruption control in the administration of public funds (Leiderer 2010, 2).

Thus many donors also understand BS as a way of contributing to key reform processes in partner countries with the aim of building more effective public institutions. In particular, they hope to use BS to improve transparency, accountability, and the effectiveness and efficiency of public administration and public financial management. Moreover, many bilateral aid agencies also link BS with the promotion of human rights, democratic participation, the rule of law, and gender equality (BMZ 2008, 8).

Beyond aiming at implementing the Paris/Accra Agenda, donors therefore formulate different objectives for their use of BS. Germany, for instance, has identified three objectives of BS: a governance objective; an effectiveness and efficiency objective; and – only in third place – a financing objective (BMZ 2008, 8).

Consequently, while the definition of BS as a form of direct financial support to a country's budget is appropriate for distinguishing BS from other modalities of financial cooperation, an evaluation of BS effectiveness clearly requires a more explicit conceptualisation of how BS is expected to work. BS in practice entails much more than the mere transfer of financial resources to the recipient government's treasury. Therefore BS also contains important *non-financial contributions*. Typically, poverty reduction BS links transfers of financial resources with a range of conditionalities as well as an intense policy dialogue, along with capacity-building measures aimed at strengthening the recipients' policies as well as implementing capacities (Hammond 2006, 92). At a conceptual level, BS can thus be interpreted as an attempt to combine *financial and non-financial inputs* in a mutually reinforcing manner in order to increase the effectiveness of external support for development processes in recipient countries.

While this (often implicit) interaction logic of BS makes good sense from a theoretical perspective, it significantly complicates matters from an evaluation perspective. This is because the various feedback loops expected to render BS more effective than other forms of development aid preclude evaluation according to a simple linear causal chain along a one-dimensional intervention logic. In this regard, it is noteworthy that the implicit logic is seldom made explicit in BS programme documents. However, the authors of this study believe that it is helpful to do so in order to frame the main challenges for evaluating BS.

1.2.2 Intervention logic of budget support programmes

In practice, BS programmes commonly encompass much more than mere financial support for government budgets. More specifically, aid agencies' inputs to BS operations also include:

- Policy Dialogue
- Conditionality
- Technical Assistance (TA) and Capacity Development

The core ingredient of BS is clearly the financing, which is provided with the aim of supporting the implementation of a comprehensive national development programme, e.g. a poverty reduction strategy (PRS), in the recipient country. Poverty reduction strategies aim to reduce poverty and

foster economic development mainly through the provision of public goods and services funded primarily through the national budget.

The impact of budget resources on poverty reduction and economic development, however, is determined by the quality of national strategies and policies, the government's resolve to actually pursue these policies, and the government's political and administrative capacities³ for efficiently and effectively using the resources to implement these policies. Since government systems for strategic planning, policy formulation, budget planning, formulation, and execution tend to be weak in most recipient countries, donors typically combine financial contributions with non-financial input aimed at strengthening these government systems.

By engaging in an intense policy dialogue with the recipient government donors aim at improving policy content (while respecting the principle of ownership) as well as the wider governance system, including the public financial management (PFM) system. An effective dialogue mechanism facilitates smooth coordination and better structured communication within the government system; between the government and its cooperating partners; and among donors themselves.

Policy dialogue as a non-financial input of budget support is thus expected to contribute to better policy choices and overall improved governance. In so doing, it is ultimately expected to make donors' financial contributions as well as domestic budget resources more effective in achieving development objectives.

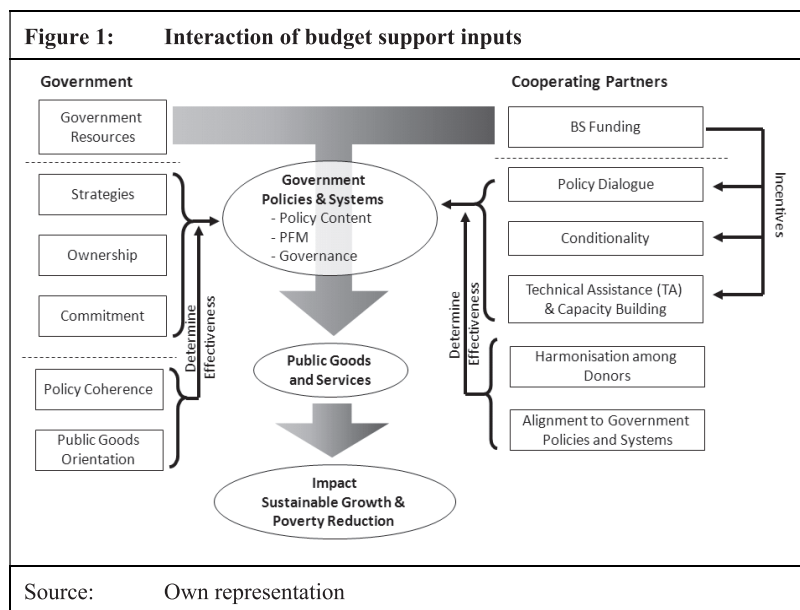
At the same time, by conditioning funding on policies and policy outcomes, donors use their financial contributions to augment the effectiveness of this dialogue by offering incentives for the recipient governments to undertake governance reforms and pursue better policies.

In addition, BS donors complement their financial contributions with specific technical assistance and capacity building programmes targeted at strengthening the government's capacity to manage available resources and to implement necessary reforms effectively and efficiently.

3 The political capacity of a government to implement pro-poor policies obviously also depends on the specific political power structures in the country. These determine whether the government can, for example, get new legislation or pro-poor budget allocations approved by parliament and/or other potential veto players.

In this intervention logic, non-financial contributions to BS programmes thus act as a lever to make financial contributions to the budget more effective in achieving poverty reduction and development objectives. At the same time, by linking policy dialogue and conditionality to funding, the financial contributions also serve to strengthen the effectiveness of non-financial inputs by creating incentives for governance reforms, improvements of policy content, and stronger PFM systems.

Figure 1 illustrates this multi-dimensional mechanism of mutual reinforcement of financial and non-financial BS inputs.



Ultimately, the expectation is that this mix of inputs, under the right conditions, will contribute to the realization of specific government outputs (Caputo / Lawson / van der Linde 2008, 14), such as:

- improved fiscal discipline and macroeconomic management;
- strengthened Public Finance Management (PFM) and procurement systems;

- improved public policy design and policy processes;
- increased funding for discretionary spending, resulting in an increase in the quantity and quality of goods and services provided by the public sector;
- enhanced allocative and operational efficiency⁴ of public expenditure;
- improved budget processes, including better links between government and parliament.

Cross-cutting to this list of government outputs is the expectation that an “adequate” mix of financial and non-financial inputs will improve transparency and democratic accountability; or, conversely, the assumption that factors such as corruption and a lack of macroeconomic discipline will impair the effectiveness of BS.

Cutting across this list of government outputs is the expectation that an ‘adequate’ mix of financial and non-financial inputs will create an incentive for the recipients to improve transparency and democratic accountability. Thus, the instrument not only aims to strengthen core supervisory functions with the state administrative body on the supply side of budget accountability. Moreover, by strengthening parliament’s and civil society’s engagement in the overall budget process, the instrument also aims to contribute to the demand side of democratic accountability. At the same time, this intervention logic implies that factors such as corruption and a lack of macroeconomic discipline will impair the effectiveness of budget support.⁵

At the level of budget allocations and expenditure management, three things are therefore important for the effectiveness of BS: additionality, allocative efficiency, and operational efficiency. All three are closely related to the inherent fungibility of aid resources and the associated fiduciary risks of budget support (see Box 1).

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- 4 Allocative efficiency represents the degree to which resources are allocated in accordance with the strategic priorities of the government. Operational efficiency is the rate at which resources allocated towards and spent on the government’s strategic priorities are actually translated into results, or in short the value for money of public expenditure (IDD and Associates 2007).
 - 5 In fact, this part of the intervention logic is related to the participatory elements in the creation of PRSPs, which are supposed to go beyond a narrow concept of government ownership through the participation of civil society groups (e.g. Booth 2003; Meyer / Schulz 2008; Faust 2010).

Box 1: Aid fungibility and efficiency: Fiduciary risks of budget support

Fiduciary risk in the context of BS means that the funds provided may be used inefficiently or for other purposes than those intended by the donors. This risk stems in part from the fact that aid resources, in particular BS resources, are fungible and thus cannot be effectively earmarked.

In the context of BS, fungibility matters mainly at two levels:

- Firstly, BS may reduce the incentive for recipient governments to mobilise adequate domestic revenue for financing goods and services to implement national poverty reduction and development strategies. Where this is the case, BS may simply crowd out domestic (e.g. tax) revenue instead of providing resources for additional expenditures, and hence cannot be expected to produce any positive effects through the provision of public goods and services. (Obviously, this can have both positive and negative, intended or unintended effects and impact through the reduction of the tax burden on certain sectors, firms, activities or individuals.)
- Second, recipients may use the provided resources for other purposes than those intended by the donors, i.e. in most cases the production of public goods and services in pursuit of a national poverty reduction strategy. What matters for the effectiveness of BS with regard to poverty reduction and development goals is thus the allocation efficiency of public expenditures.

Beyond these fungibility-related risks, there is also the obvious risk that resources may be used inefficiently by the recipient. Thus the operational efficiency with which public goods and services are produced is also crucial for the effectiveness of BS.

Source: own

1.2.3 Necessary conditions for effective budget support inputs

The effectiveness of BS clearly depends on a complex interaction between financial and non-financial donor contributions as well as the recipient government's own capacities and dispositions.

On the recipient side, it is important that governments should show a sufficient level of *policy coherence and public goods orientation*, which impact positively on ownership, development strategy and commitment to reforms. In this regard, important preconditions for the effectiveness of BS include:

- a commitment to improve transparency and democratic accountability;
- agreement between donors and the recipient government on policies and budget priorities;
- a demonstrated commitment and capacity to implement reform programmes;
- a clear strategy for prioritizing pro-poor expenditures;
- a transparent budget and commitment to strengthen the PFM system.

But whether the financial resources provided will effectively contribute to achieving the goals formulated in the PRS also depends on several factors on the supply side of the aid relation.

For one thing, it is of key importance that the financial resources are provided in a cost- efficient, timely, and above all, predictable way so as to enable the recipients to strategically plan the use of all available resources. In turn, whether the non-financial contributions are effective in strengthening government capacities to make good use of the financial contributions provided mainly depends on two conditions:

Most importantly, the way in which non-financial contributions are provided is crucial for their effectiveness. More specifically, it is of utmost importance

- how well donor contributions are coordinated and how well procedures and requirements are harmonized, and
- to what extent these contributions are aligned to the partner government's priorities, systems, and procedures.

Moreover, the effectiveness of non-financial BS inputs depends on whether the leverage of the financial contributions is strong enough to create an effective and coherent incentive structure: for example, the institutional context in which these inputs are provided and the degree to which these measures fit the government's priorities are of crucial importance for the recipient government's ownership and thus its receptiveness for capacity development measures. The effectiveness of conditionality tied to BS largely depends on how well the conditions are coordinated among the donors and how clearly these conditions are linked to the provision of financial resources. The same applies to the transaction costs involved in negotiating these conditions: BS-related policy dialogue can be expected to be

more effective if the donors agree on joint objectives and priorities and provide a harmonized and credible set of incentives.

1.2.4 Implications of a non-linear intervention logic for budget support evaluation

The non-linear intervention logic underlying the rationale for BS renders an evaluation of the instrument's effectiveness extraordinarily complex. Important factors that add to this complexity which must be taken into account in the evaluation of BS were identified in the Note on Approach and Methodology for a Joint Evaluation of BS (IDD Associates 2007):

- The initial inputs are themselves complex – a combination of funds with associated dialogue and conditionality, technical assistance and capacity development, harmonization and alignment. In addition, it can be difficult to distinguish between the non-financial components of BS programmes and other aid modalities.
- The desired ultimate effects are complex (poverty reduction in various dimensions), and changes in outcome and impact indicators will be partly (and sometimes predominantly) the effects of other causes (deliberate effects of non-GBS inputs, or exogenous factors).
- The assumed chain of causality is long, both conceptually and temporally. This applies particularly to effects expected from processes of institutional change. Also, many of the intermediate effects postulated are not in themselves open to straightforward measurement, let alone to proportionate attribution to multiple causes, particularly in a dynamic context in which BS is only one of the influencing factors in continuously changing systems.
- The logic of causation itself is often controversial; for example, even if it could be demonstrated that BS led to the adoption of a particular policy designed to reduce poverty, the appropriateness and efficacy of the policy – either generally or in the context of the particular country – might well be disputed).
- Last, but not least, the choice and the construction of appropriate counterfactuals (what would have happened if BS had not happened?) is both difficult and controversial.

1.3 Evaluation framework, evaluation questions and methodology

1.3.1 Evaluation framework and evaluation questions

In order to account for the described complexity of the presumed effects of BS, the present evaluation was based on a comprehensive causality map developed by a group of cooperating partners as part of a comprehensive evaluation framework.⁶

The evaluation takes the complex interactions of effects and presumed causal links in the intervention logic of BS into account. For guiding this part of the evaluation, which is mainly focused on inputs, direct outputs and induced output of BS in Zambia, the main questions and more specific sub-questions are structured accordingly.

1) **INPUTS:** To what extent have BS mechanisms put in place been consistent with Zambia's strategic and policy framework and how well has the design been adapted to the specific political, economic and institutional context?

1.1 Which inputs have been provided by BS, and to what extent do they correspond to the envisaged GBS/SBS inputs?

1.2 To what extent are the BS operations put in place consistent with Zambia's strategic and policy framework and with the overall Development Partners' (DPs) development strategies?

1.3 How well was the design of GBS/SBS inputs adapted to the specific political, economic and institutional context of Zambia?

2) **DIRECT OUTPUTS:** To what extent has BS in Zambia led to increased external funding subject to government's budgetary process, the establishment of a policy dialogue framework and to harmonization/alignment of external assistance?

6 The methodology group was formed on the initiative of the Evaluation Unit of the Europe Aid Co-operation Office of the European Commission. The Steering Group on BS further includes the evaluation departments of Belgium, Canada (CIDA), Denmark (DANIDA), Finland, France (AFD), Germany (BMZ), Ireland (Irish Aid), the Netherlands (IOB), Norway (NORAD), Sweden (Sida), The United Kingdom (DFID) and the OECD/DAC secretariat.

2.1 To what extent has BS contributed to an increased size and share of external funding subject to government's budgetary process and improved the predictability of overall flows of external assistance?

2.2 To what extent has BS contributed to the establishment of a framework of policy dialogue, focused on key government strategies and priorities?

2.3 To what extent has BS contributed to the provision of non-financial inputs, such as technical assistance and capacity building, which are considered as strategic government priorities?

2.4 To what extent has BS contributed to harmonization and alignment of external assistance, and reduced transaction costs over time?

3) INDUCED OUTPUTS: Did BS have an impact on fiscal discipline and macroeconomic management, public finance management, public spending and governance and democratic accountability?

3.1 To what extent did BS contribute to the improvement in fiscal discipline and macroeconomic management?

3.2 To what extent did BS contribute to an improvement of budget management and overall PFM?

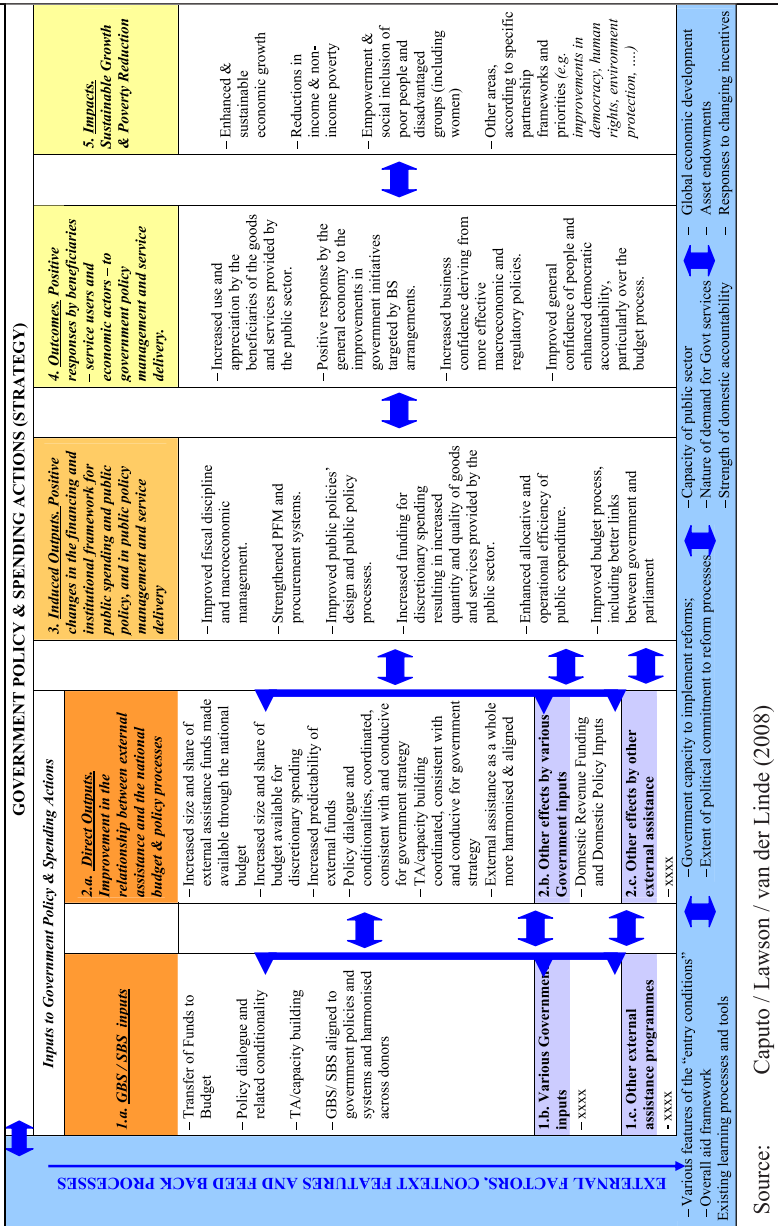
3.3 To what extent did BS contribute to the level and composition of public spending?

3.4 To what extent did BS contribute to an improvement of policy processes and policy implementation (including ownership and transparency)?

3.5 To what extent have there been improvements in governance and democratic accountability, particularly regarding the relative roles of parliament and civil society in relation to the budget?

3.6 To what extent did the rule of law improve in the country?

Figure 2: Causality map budget support



1.3.2 Data collection and methodology

Data for evaluation came primarily from three sources:

- Semi-structured interviews of key stakeholders and experts during two field visits (February – April 2010 and June 2010)⁷
- Existing evaluation reports, reviews, other official documents and academic literature
- Information on financial flows
- Micro- and macro-economic data and indicators

In addition, this report also contains elements from a background report delivered by Prof. Oliver Saasa, the principal national consultant for this evaluation component. Moreover, evidence from the sector reports of the overall evaluation was used where appropriate.

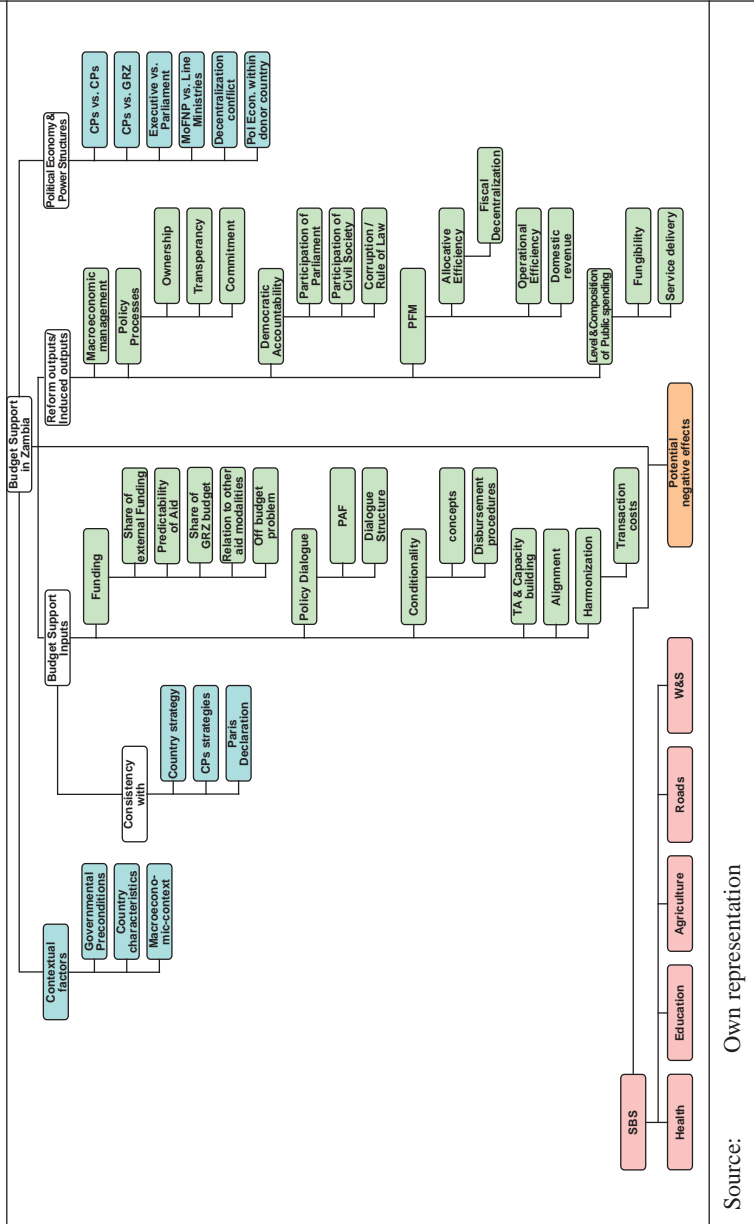
Most of this evaluation on the political economy and policy processes of BS in Zambia has been qualitative in nature. Given the challenges of qualitative research, the acquired data was coded using Atlas.ti®, a software package for textual analysis, in order to incorporate all available information in the evaluation team’s assessments and to help sustain the objectivity of judgments as much as possible. For this purpose key documents, interview minutes, the background report of the main consultant, and sector reports were coded in accordance with judgment criteria and sector indicators.⁸ Overall, the codes are linked through an “analytical grid” depicted in Figure 3. This grid corresponds to the evaluation questions at the input and output level within the intervention logic described above, with a particular emphasis on context and political economy factors.

This systematic coding process allowed for the triangulation of relevant findings. Once the coding was finalized, the software made it possible to

7 Key informants were selected from the following categories of stakeholders: government policy makers at the central and sector level, parliament (public accounts, budget, and sector committee), audit institutions, civil society organizations (incl. non-governmental organizations and academia/research organizations), international donors, project/technical assistance teams, private sector associations, and beneficiaries at the provincial and district levels.

8 Additional codes were used to capture further information (e.g. on illustrative evidence or unintended effects).

Figure 3: Analytical grid for qualitative data analysis



Source: Own representation

identify and compile all statements on any coded issue. Moreover, Atlas.ti® made it possible to attach analytical codes developed according to phenomena that occurred in these text segments. After completion of the coding process it thus became possible to see all statements and comments made by stakeholders or found in the documents analysed on any particular issue. This permitted a systematic and detailed comparison of statements and quotes. The quotations for every code were synopsisized and compared with each other. At the same time it was still possible to go back to the original transcript and see in which context a particular statement had been made (Leiderer et al. 2007).

Attribution of the direct and induced outputs to BS inputs then was established on the basis of the coded information, the background reports and analysis by the sector teams. Where possible, attribution was based on contribution analysis with performance measurement tools as described by Mayne (1999).

The analysis was then embedded in the overall intervention logic, distinguishing wherever possible between GBS and SBS contributions. Where appropriate, potential alternative explanations are discussed in order to reduce the risk of misattribution of observed effects. This approach explicitly acknowledges the attribution problem that arises “when one believes or is trying to claim that a program has resulted in certain outcomes and there are alternative plausible explanations” (Mayne 1999, 13).

Next to exploring alternative explanations for observed effects, another step taken to avoid misattribution was the establishment of appropriate counterfactuals. For most BS-related interventions, alternative aid modalities feature strongly among the possible counterfactuals (IDD and Associates 2007, 6). The dominant approach of this evaluation, however, was to evaluate budget support against the underlying intervention logic. As stressed in the note on methodology for the joint evaluation of GBS of 2006, (a) the appropriate counterfactual is a matter of conjecture, rather than an alternative scenario that can be reconstructed in detail; (b) a complete substitution of one modality for another is rarely seen as a realistic option; and in any case; (c) many of the more interesting observations are about interactions between the different aid modalities. In a pragmatic approach, this study thus does not establish a hypothetical counterfactual situation for each and every sub-enquiry in the overall study. Instead, the analysis is limited to counterfactuals for selected key issues.

2 Context and history of budget support in Zambia

2.1 Country context Zambia

2.1.1 Economic background⁹

Zambia, which until three decades ago was one of the most prosperous countries in Sub-Saharan Africa, today is one of the world's least developed countries. At the time of independence in 1964, Zambia's rich mineral resources were well developed, and during the first ten years, world market conditions were generally favourable. During this period, the pattern of government expenditure actually reflected the country's steady export receipts from copper. Zambia's fortunes were adversely affected by external shocks that came in quick succession starting in 1973, when oil prices quadrupled, and then in 1974, when copper prices declined considerably. For a country that depended on this product for more than 90 % of its export revenue, the economy experienced severe difficulties in adjusting to these shocks. By 1975, Zambia was faced with a sharp decline in government revenue and a serious balance of payments problem. Unsustainable budget deficits also set in. Declining ore reserves, inadequate foreign exchange earnings, and accelerating domestic inflation barred the mining companies from reinvesting in the spare parts and maintenance needed to sustain output levels. In spite of these difficulties, public spending remained high, financed by massive external borrowing. By the early 1980s, the economy was under serious stress.

Despite a major political regime shift in 1991, Zambia continued to register a poor economic record in the 1990s and the early 2000s. The economy remained undiversified and continued to exhibit heavy dependence on mineral resources, in particular on exports of copper. The country's growth record, from the long-term perspective, had been depressing. The GDP growth rate fell from an average of 1.5 % in the 1970s to 1.4 % in the 1980s and 0.3 % in the 1990s. Other economic indicators also pointed to declining trends. Inflation, for example, increased steadily over the years, rising on the average from around 10 % in the 1970s to about 70 % in the 1990s. This increase in inflation, coupled with a population growth which was above the GDP growth rate during the 1990s, resulted in a decline in real

9 This section draws heavily on a background report prepared by Saasa (2010b).

per capita income. The government's fiscal deficit averaged about 2 % of GDP over the period from 1995 to 2000. It stood at about 5.4 % in 2000.

Since 2000, Zambia has registered an encouraging macroeconomic trend. Following the sale of the Zambia Consolidated Copper Mines Limited (ZCCM), the GDP growth rate of 3.5 % in 2000 and 5.2 % in 2001 indicated a brighter economic outlook for the economy. According to GRZ sources (Central Statistics Office), inflation declined from 30 % in 2000 to 18.7 % at the end of 2001. In 2002, however, a region-wide drought dampened the emerging brighter outlook, and an increase in food prices significantly contributed to a rise in inflation to 26.7 %.

In the recent past, Zambia has registered significant improvements in the macroeconomic spheres. During the period from 2006 to 2008, the real GDP growth rate improved from 5.2 % in 2005 to 6.3 % in 2006 and dropped slightly to 5.7 % in 2008 (see Table 2). Consequently, substantial investments have been recorded in some of the major sectors, particularly in mining, manufacturing, tourism, and, in some years, in agriculture.

The performance of the monetary and financial sector during the last three years has been mixed, with fluctuations recorded in inflation and exchange and interest rates. According to GRZ sources, single-digit inflation was achieved at 8.2 % and 8.9 % in 2006 and 2007, respectively; this was above the FNDP target of 5 %. Notwithstanding this development, inflation in 2008 rose to double digits, ending the year at 16.6 %. It declined again to single digits (9.9 %) in 2009. However, it has picked up again since, reaching 10.2 % in March 2010. Interest rates also remained high, averaging above 20 %.

External sector performance has generally remained favourable, with external debt servicing maintained within sustainable levels and the overall balance of payments remaining positive. The balance of payments position improved remarkably in 2006, with an overall surplus of US-\$ 821.6 million, compared to the deficit of US-\$ 115.8 million the previous year. Export earnings grew by over 100 % to US-\$ 4876 billion in 2008 from US-\$ 2178 billion in 2005. In this regard, the gross international reserves build-up improved from 1.5 months of import cover in 2005 to 2.2, 2.5 and 2.8 months of import cover in 2006, 2007, and 2008, respectively. The favourable export earnings performance was a positive stride in achieving the FNDP strategy of promoting export development as one of the eco-

Table 2: Selected macroeconomic indicators for Zambia, 2000-2008

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
GDP growth (annual %)	3.6	4.9	2.7	5.7	5.4	5.2	6.3	6.2	5.7	6.3
GDP per capita (current US-\$)	309	339	339	390	473	610	890	937	1165	986
Population growth (annual %)	2.6	2.4	2.3	2.2	2.2	2.3	2.4	2.4	2.5	2.5
Inflation. consumer prices (annual %)	26.0	21.4	22.2	21.4	18.0	18.3	9.0	10.7	12.4	13.4
Exports of goods and services (% of GDP)	27.1	28.0	27.7	28.7	38.3	34.7	38.5	41.6	35.8	29.8
Copper. (US-\$ per metric ton; source: IFS)	1816	1580	1560	1779	2864	3677	6731	7132	6964	5165
Exchange rate (ZMK per US-\$)	3111	3611	4399	4733	4779	4464	3603	4003	3746	5046

Source: WDI, IFS

conomic growth drivers. Nonetheless, continued instability in the exchange rates is adversely affecting the export sector.

Notwithstanding positive macroeconomic trends, it is important to take a closer look at the structure of the Zambian economy. Starting from an undiversified economy based on the extraction of mineral resources, Zambia, to a certain degree, has managed to diversify its sources of economic growth. Today, the mining sector still makes up for 70 % of exports and 4 % of GDP (AfDB / OECD 2008, 618 ff.). While copper remains to be vital for the Zambian economy, other sources of productivity have been tapped. The major source of GDP in 2006 was the service sector, which provided 55.9 % of GDP. While industry put in another 29.5 %, the share of agriculture continued to decrease, from 18.3 % in 2000 to 14.6 % in 2006 (World Bank 2008b, 22). The diminishing weight of the agricultural sector is due to its relative underperformance, with negative growth rates in 2001 and 2002 followed by marginal improvements until 2006. Among the reasons for the stagnant situation are 1) a continuous low level of productivity caused by the sector's high weather-dependency, 2) limited access of farmers to agricultural inputs and credit, and 3) failure to push through land reforms (EIU 2008, 18). In the period from 2001 to 2006 the Zambian economy grew by 5.6 % on the average, with industry being the driving force. The three sub-sectors of construction, mining and manufacturing accounted for 1.2, 0.7, and 0.6 percentage points, respectively (World Bank 2008b, 23).

2.1.2 Democracy and political change in Zambia

In the last two decades, Zambia has experienced several major political changes. In 1990/91, reformist tendencies headed by the MMD (Movement for Multi-Party Democracy) peacefully led the country to democratic rule, thus ending the authoritarian one-party dominant regime under President Kaunda. While during its first years, the new regime under president Frederick Chiluba showed strong democratic elements, democratic accountability began to deteriorate in the second half of the 1990s. Political rights and civil liberties were curtailed to an extent that Zambia almost became an authoritarian regime again. In 2001, however, Chiluba – as a result of civil society protests, among other things – failed to gain sufficient political support for a third presidential term. After highly disputed elections, which were not considered as fair and free by many external observers, the MDD candidate Levy Mwanawasa became president in 2002. Despite concerns

that the MDD government would consolidate a non-democratic one party dominant regime, the 2006 presidential elections were regarded as free and fair. This has also been the case for the 2008 elections, when the current head of state, Rupiah Banda, achieved another victory for the MDD. Accordingly, since 2006, the country has been ranked as an electoral democracy by Freedom House. Still, most studies agree that severe deficiencies remain under the current administration. These deficiencies relate mainly to two core issues: First, a relatively low degree of checks and balances. According to the recent country report of the Bertelsmann Transformation Index (Bertelsmann Stiftung 2009), the dominance of the executive “clearly extends beyond the stipulations of the constitution”. Second, low levels of political transparency and continuous problems of patronage and corruption persist, even if there is some disagreement among external observers with regard to the dynamics of these challenges.

Overall, Zambia has experienced a political development which is rather typical for many African countries and has been ranked only slightly above the regional average on the Freedom House scale of political rights and civil liberties. The 1990s reflected a typical combination of a breakdown of a long-standing authoritarian regime together with structural economic reforms and the emergence of a democratic order. However, as in many other countries of the region, democratic progress did not speed up but rather showed concerning signs of stagnation. Thus, while being an electoral democracy, the citizenry is still far from enjoying a satisfactory level of political rights and civil liberties. Instead, Zambia can be accounted as one of a growing number of developing countries whose political regimes are characterized by both democratic and authoritarian elements.

2.1.3 Poverty profile

In spite of an existing comprehensive Poverty Reduction Strategy (PRS) and positive growth trends during the last decade, Zambia faces serious challenges with respect to a substantial reduction of its poverty level.

At first sight, aggregate poverty indices for Zambia show an overall improvement in poverty levels in recent years. According to the Human Development Index (HDI), Zambia has made continuous progress over the last decade, improving its absolute index score from 0.345 in 2000 to 0.360

in 2005 and 0.395 in 2010. Zambia currently ranks 150th out of 169 countries on the HDI-list of 2010.¹⁰

According to the 2008 Millennium Development Goals (MDGs) Status Report for Zambia, only one of the MDGs, namely that of integration of the principles of sustainable development into country policies and programmes and reversal of the loss of environmental resources, is not likely to be met.

Notwithstanding recent trends, the Living Conditions Monitoring Survey (LCMS) IV of 2004 states that 68 % of the population fell below the national poverty line. Although the overall poverty level was reduced to 64 % by 2006, the depth and severity of poverty remained high in the country; extreme poverty decreased only slightly and stood at 51 % in 2006.¹¹

Zambia's improved economic performance since 1999 has not significantly reduced poverty. One explanation for the weak growth/poverty relationship is that recent growth has been concentrated in mining, wholesale and retail trade and construction, which are mostly urban based and capital-intensive. These sectors have not generated sufficient employment due to weak linkages with the rest of the economy. If the country continues on its current growth path, it is projected that headcount poverty will only marginally decline to 62.3 % by 2010¹², from 68 % in 2004.

The spatial concentration of poverty reduction to the urban areas constitutes a major case of concern in Zambia. During the years of strong economic growth, the rural population in general and small-scale farmers in particular were mostly excluded. As shown in Table 3, headcount ratios in rural areas even increased: from 78 % in 2004 to 80 % in 2006. While poverty remained high in rural parts of the country, people living in the Copperbelt district, where the total poverty headcount decreased from 56 % in 1998 to 34 % in 2006, benefited most.

10 For further information see <http://hdr.undp.org/en/>.

11 Extreme poverty is measured on the basis of a lower poverty line that reflects the minimum requirements of spending for food and excludes some of the items included in the national 'basic' poverty line.

12 The poverty projections are based on a 2004 computable general equilibrium and micro-simulation model.

Table 3: Development of poverty in Zambia, 1996-2006 (percentage poor)				
	1996	1998	2004	2006
Urban	46	56	53	34
Rural	82	83	78	80
Total	69	73	68	64
Gini Ratio	0.47	0.49	0.53	0.53
Source: MoFNP, Central Statistics Office				

In light of the above, the weak growth of the agricultural sector explains why poverty incidence is still highest among the rural small-scale farmers. Analysis of income deciles reveals that income in Zambia is very unevenly distributed. According to government statistics, the bottom 50 % of the Zambian population claims a meagre 15 % of total income, while the top 10 % claim 48 % of the total income, which is more than three times the income share for the bottom 50 %.

About 55 % of the total population and 70 % of the poor live in rural areas. Furthermore, the majority of rural and urban households rely on incomes from agriculture and agriculture-related industries or consume domestically produced food. It is generally agreed that agriculture and related industries tend to be more labour-intensive and also have strong linkages with the rest of the economy. Growth in this sector is therefore expected to generate jobs and create employment opportunities for households. Rural and agricultural development is therefore important for accelerating pro-poor growth and reducing poverty in Zambia.

After a substantial overall reduction of poverty rates between 1998 and 2006 (see Table 3), poverty levels in the country dropped only marginally from 2006 to 2008. This recent trend is mainly due to a reduction in urban poverty levels, with rural poverty even showing a slight improvement.

2.2 The history of aid in Zambia

After a period of financial autonomy in the first decade of independence (Wohlgemuth / Saasa 2008, 1) the Zambian government had to resort to financial assistance from external donors. The undiversified economy, in combination with severe external shocks, caused serious problems regarding the balance of payments. In order to cope with the lack of revenue from the tarnished copper industry, Zambia entered into numerous financing agreements in the late 1970s. The aid boom experienced throughout the late 1970s and mid 1980s suddenly ended after the government shifted its political focus in 1987, thus abandoning the reform agenda prescribed by the International Monetary Fund (IMF). The United National Independence Party (UNIP) administration refused to adhere to the regulations of debt servicing made by the IMF; this led not only to Zambia's ineligibility for further IMF loans but made almost all bilateral donors refrain from further provision of urgently needed external finance. After the fruitless attempt of the government to detach itself from international finance institutions, the MMD, after winning the 1991 elections, resumed its focus on the reform model of structural adjustment, thus again attracting the donors' attention and goodwill. Indeed, the renewed commitment to structural adjustment by the MMD government disposed the donors to massively increase aid flows (White / Dijkstra 2003, 402). In the early 1990s, donors support rose on an unprecedented scale, averaging US-\$ 951 million annually between 1990 and 1994 (Wohlgemuth / Saasa 2008, 3).

Notwithstanding substantial fluctuations, Zambia has received remarkable amounts of aid over the last twenty years, resulting in an increased debt burden. Already in 1984, as a result of extensive non-concessional borrowing from the IMF and the World Bank, Zambia was the world's most indebted country relative to GDP (Fraser 2009, 305). Massive aid inflows in support of the democratically elected reformist government of the MMD were registered after 1991. After two years of broad and rapid liberalisation, programme aid abated, seemingly in part because of the bilateral donors' disenchantment with the MMD's waning commitment to reform (White / Dijkstra 2003, 406ff). In 2000, after the government finally completed privatizing the principal copper company ZCCM, Zambia was declared eligible for debt relief under the Highly Indebted Poor Countries Initiative (HIPC). In March 2005, when Zambia reached the HIPC completion point, its total foreign debt was reduced from US-\$ 7.1 billion to US-\$ 4.0 billion. Under the

Multilateral Debt Relief Initiative Zambia's debt stock was further reduced to around US-\$ 0.5 billion by the end of 2006 (Wohlgemuth / Saasa 2008, 2).

In the 1980s Zambia entered into an era of aid dependency, allowing its development partners to substantially influence domestic policies by attaching a variety of economic conditions. Especially in the forefront of debt relief in 2005/06, when the share of aid in the central budget was 43 % on the average (Wohlgemuth / Saasa 2008, 3), donors used their financial position to push for extensive conditionality, putting forward often unpopular economic and public sector reforms. In conjunction with the HIPC-Initiative, the IMF and World Bank geared up their conditionality, demanding comprehensive privatization, faster progress on civil service cuts, the removal of exchange rate controls, a liberalization of the strategic grain reserve, and an end to the distribution of fertilizers (Fraser 2009, 307).

In recent years, aid relations have evolved substantially. After debt forgiveness in 2005 and 2006, the contribution of aid to the national budget declined to 30 % between 2006 and 2007, followed by further reductions to 28 and 24 % in 2007 and 2008, respectively (Wohlgemuth / Saasa 2008, 3). In 2009 the downswing continued, and foreign assistance as a share of the government budget declined to around 20 % (Chigunta / Matshalaga 2010, 8). This trend is confirmed by Table 4, which shows a continuous downward trend in foreign aid as a percentage of GNI since 2004.

This decline in aid dependency in recent years can be explained for the most part by debt relief after the country reached the HIPC completion point, along with rising copper prices and strong economic performance (Chigunta / Matshalaga 2010, 8). According to the World Development Indicators, GDP (in current US-\$) has doubled between 2005 and 2008. Similarly, the government budget has increased and, due to their relative stability, the importance of external donor funds for the budget has decreased accordingly. In addition, the appearance of non-traditional donors, the limited effects of the global financial crisis, and the flourishing external sector have recently influenced the aid relations between international donors and the Government of Zambia.

2.3 The evolution of budget support in Zambia

In the 1990s, Zambia and its cooperating partners took their first steps on the road to BS with the introduction of sector-wide approaches (SWAs). In

Table 4: Total net aid to Zambia 2000-2009 (US-\$ millions)

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Grants	523	589	699	931	974	1,909	4,565	910	1,032	955
Loans (net)	272	-18	113	-157	156	-737	-3,116	98	84	
Total	795	571	811	775	1,130	1,172	1,449	1,008	1,116	1269
Aid (% of GNI)	25	17	23	19	25	20	20	11	9	10
Aid per capita (US-\$)	76	53	74	69	99	100	151	82	88	98

Source: OECD/DAC Stats, World Development Indicators

1993, they developed a SWAp for the health sector (Chansa 2008; Chansa et al. 2008). In the second half of the 1990s, GRZ and CPs agreed on a number of SWAPs, including one for the basic education sector for 1999-2002, an Agricultural Sector Investment Programme in 1996, and the Road Sector Investment Programme in 1998. Sector cooperation accelerated after the turn of the century when, based on investment plans in the education and health sector, contributions of donor funds had increased.

The SWAPs were part of a harmonization process that began to take shape in 2002. In response to the Declaration on Harmonization which was formulated at the first high-level meeting on aid effectiveness in Rome in 2003, seven CPs¹³ agreed to join forces in support of harmonization and alignment, marking the beginning of what became known as the Harmonization in Practice (HIP) Initiative. The donor group commissioned a study (Saasa / Claussen 2003) in late 2002 to recommend on aid harmonization. This study formed the basis of the *Joint Statement of Commitment by Donors and GRZ to increase aid effectiveness and reduce transaction costs for Zambia* through the adoption of OECD/DAC Guiding Principles and Good Practices. The Joint Statement was signed by the Zambian Government and the Directors-General of the seven aid agencies in March 2003. The parties to the MoU agreed (a) to harmonize their aid support and processes, including procurement processes; (b) to increase the share of BS they provide; and (c) to coordinate their policy inputs. Following the decision of all remaining major donors in Zambia to join the HIP Initiative, it was expanded in 2004 to create the Wider Harmonization in Practice (WHIP) group.

The Zambia Aid Policy and Strategy (2005) includes inter alia a call for direct BS as the main aid modality (GRZ 2005b, 19). In April 2007, the Joint Assistance Strategy for Zambia (JASZ) was signed by all the major donors¹⁴ and the Zambian Government. Complying with GRZ preferences, the cooperating partners agreed on the following:

13 Denmark, Finland, Ireland, the Netherlands, Norway, Sweden and the United Kingdom

14 The signatories to the JASZ are 12 bilateral donors, the European Commission, the United Nations, the World Bank and the African Development Bank. Five of the bilateral donors (Germany, Ireland, Norway, Sweden and the United Kingdom) will replace their current strategy for development cooperation with Zambia with the JASZ. The others will base their ongoing county strategies on the JASZ, which should lead to overall diminished transaction costs in terms of government consultations. For example, the European Commission's Country Strategy paper for 2008–2013 aligns well with the JASZ principles.

“CPs will respect GRZ’s preference for direct budget support and will to the extent possible increasingly deliver aid to the government sector through this modality to the extent that GRZ’s systems meet established guidelines and standards, and that CP policies support such assistance.”(Cooperating Partners 2007, 38)

The JASZ has cemented the new relations between donors and the Zambian Government. It is a unique document in the history of aid cooperation, representing the donors’ joint response to Zambia’s Vision 2030, the Fifth National Development Plan (FNDP) and the Zambian Aid Policy and Strategy Programme, which together constitute the national framework for reducing poverty and promoting sustainable development. JASZ also relates to the Paris Declaration in emphasizing local ownership of the development process and enhancing aid effectiveness and mutual accountability. In accordance with the Zambian Aid Policy and Strategy, the JASZ gives major responsibilities to the Government of Zambia, positioning it to take on ownership and aligning external assistance to Zambia’s policies, systems and procedures (Cooperating Partners 2007, 34). In turn, it also requests donors to collaborate in improving funding predictability and alignment with Zambia’s own financial management systems (Cooperating Partners 2007, 3; GRZ 2005b, 11ff).

In April 2005 GRZ and four cooperating partners (the European Commission, the World Bank, DFID and the Netherlands) signed a Memorandum of Understanding on the provision of *Poverty Reduction Budget Support - PRBS*. Later on, Sweden, Norway, Germany, Finland and the African Development Bank followed. The MoU sets out the jointly agreed terms and pro-

Table 5: Policy agreements for harmonization	
Year	Policy Agreement
2003	HIP
2004	WHIP
2005	PRBS MoU
2006	Zambia Aid Policy and Strategy
2007	JASZ
Source:	Saasa (2010b)

cedures for direct BS to the National Development Plan and serves as a coordinating framework for consultation with the government. The signatories have committed themselves to:

- enhance ownership and effective implementation of the National Development Plan;
- increase the predictability of aid flows;
- allow allocative efficiency in public spending;
- strengthen domestic accountability;
- increase GRZ’s institutional capabilities;
- reduce the administrative burden on the government and reduce transaction costs.

PRBS aims to offer funding directly to the government budget in support of programmes targeted at reducing poverty. Such a direct transfer allows the receiving government to determine how to apply the funds in line with its development priorities. Over the last couple of years, PRBS has remained one of the most instructive responses by donors in the country in terms of positive reaction to donor harmonization, coordination and joint programming in the spirit of the Paris Declaration and Zambia’s Aid Policy and Strategy (which specifically calls for aid to be channelled through the general BS mechanism).

3 Inputs: Implementation of budget support in Zambia

EQ1: To what extent are the BS mechanisms that have been put in place consistent with Zambia’s strategic and policy framework and how well has the design been adapted to the specific political, economic and institutional context?

1.1 Which inputs have been provided by BS and to what extent do they correspond to the envisaged GBS/SBS inputs?

1.2 To what extent are the BS operations put in place consistent with the Zambia’s strategic and policy framework and with the overall Development Partners’ (DPs) development strategies?

1.3 How well was the design of GBS/SBS inputs adapted to the specific political, economic and institutional context of Zambia?

As elaborated in Section 1.2.2, this evaluation is based on an intervention logic that conceptualizes BS as a combination of financial and non-financial inputs. While the financial inputs consist in the provision of direct budgetary support to the government's treasury, the non-financial contributions include policy dialogue, conditionality, technical assistance and capacity development. According to the conceptual framework developed in Section 1.2.2, the effectiveness of each of these inputs is to a large extent determined by the overall design of the programme, especially with regard to the Paris Declaration principles of ownership, harmonization and alignment. This chapter provides a description of BS inputs in Zambia, while Chapter 4 assesses *how* these inputs were provided, i.e. to what extent the budget support programme in Zambia is in tune with the principles of ownership, harmonization, and alignment.

3.1 Financial inputs

First and foremost, budget support consists in the provision of direct, untargeted funding in support of the general budget (general budget support – GBS) or specific sector budgets (sector budget support – SBS).

In Zambia, CPs provide budget support in both forms: general Poverty Reduction Budget Support (PRBS) is provided by the PRBS group of six bilateral donors (see Table 6), the European Commission (EC), the African Development Bank (AfDB) and the World Bank. Sector budget support is provided by the EC in roads, health and in support of the PEMFA (Public Expenditure Management and Financial Accountability) reform programme (see Section 3.2.3),¹⁵ and by the United Kingdom in the health sector (see Box 2).

15 The PEMFA programme is also funded through a joint basket mechanism (see Section 3.2.3.1). The EC's financial contribution to the PEMFA programme (2005: US-\$ 3.125 million, 2007: US-\$ 1.95 million) is not included in the further analysis of financial inputs, since these are dealt with in the same fashion as the basket funds. Even if the EC gave up formal earmarking of this PEMFA funding, *de facto* earmarking still seems to take place, although there is somewhat contradictory information on exactly how this SBS is channelled to the PEMFA secretariat: while the EC claims that it is disbursed to the Treasury as BS through Bank of Zambia (BoZ) (i.e. through the Control 99 Treasury Account) and transferred from there to the PEMFA secretariat, BoZ claims the EC disburses directly into the separate PEMFA account (Interviews with BoZ and EC representatives).

Box 2: Sector budget support in the health and roads sectors**Health sector budget support**

The EC and DFID are the only CPs which have provided support to the health sector through SBS. The EC initiated a pilot SBS programme from 2006 to 2008 and from 2009 on has implemented a larger SBS programme. DFID earmarked some US-\$ 5 million) of its general budget support (GBS) to the health sector from 2006-2007, although from 2008-2010 – whilst there was additional funding provided for health within the GBS allocation – this was only broadly earmarked for the Ministry of Health (MoH) and did not target any specific sub-programme in the sector.

The two CPs pursue a somewhat different course with their SBS in the health sector: the EC's target is to support GRZ's human resource retention scheme in the sector, while DFID aimed its SBS at supporting the elimination of user fees for basic health services and at improving MoH – MoFNP relations.

The SBS for health, similar to GBS, is channelled through the Bank of Zambia to the MoFNP, from where it is supposed to be transferred to the MoH. However, none of the two CPs imposes strict additionality requirements for this earmarked funding: While it was one of the EC's conditions for this SBS that a dedicated human resource retention budget line be established, the EC does not require any proof that the funds are actually spent for this purpose. DFID imposed a traceability requirement which requires proof that the money was spent on user fee elimination. DFID gave up this traceability requirement in 2008, and since then only broadly earmarks a portion of its PRBS to be transferred to the MoH, without any requirement for these funds to be additional to domestic funding.

Roads sector budget support

The EC has also provided SBS to the roads sector in support of the Road Sector Investment Programme (ROADSIP II) since 2006 (including a tranche due in 2005 but disbursed only in 2006). A second tranche was disbursed in 2008.

The overall objective of the programme is to contribute to the promotion of equitable economic growth and poverty reduction and the enhancement of food security. The specific objectives of the SBS are to improve accessibility, mobility and connectivity at the district, provincial and national levels by promoting basic access and regional integration for people and goods. SBS funding is channelled through BoZ and earmarked for the National Road Fund Agency (NRFA).

Source: ODI / Mokoro (2009); EC (2008b; 2008a)

While the bilateral donors and the EC provide their PRBS (and SBS) as grants, AfDB and the World Bank give loans. BS is provided in annual instalments, following a n-1, n+1 scheme, in which, based on annual appraisals, in a year n CPs make commitments for the upcoming period (n+1) based on their assessment of government performance in the previous year (n-1). In addition to its annual performance tranche the EC also provides BS tranches within the framework of its MDG contract scheme. In addition, in 2009, the EC disbursed an additional € 30 million (US-\$ 38.7 million) through its V-Flex mechanism.¹⁶

Since 2007, PRBS CPs not only make annual commitments but also establish a disbursement schedule with monthly commitments in order to improve predictability and facilitate cash flow planning for GRZ (see Section 4.1.2).

As for the amounts of budget support funding in Zambia, it is surprisingly difficult (if not impossible) to obtain consistent data on BS flows in Zambia, and figures from the different available sources tend to differ substantially. In fact, it proved impossible to determine the exact figures for all flows of funds even for recent years.¹⁷

Table 6 gives the consolidated data which the evaluation team deemed closest to the truth. These data had to be collected from different sources, and some doubts about the accuracy of individual figures remain.

16 The Vulnerability FLEX mechanism (V-FLEX) is a short-term instrument supporting the most vulnerable ACP countries in coping with the impact of the global financial and economic crisis and mitigating its social consequences (EU 2009).

17 Remarkably, MoFNP does not keep records of BS inflows. Data provided by CPs was clearly erroneous in some cases (e.g. figures not adding up to the totals given or apparently showing commitments instead of actual disbursements) and also contradictory between sources. From the annual PRBS reviews, only data for the past three years could be extracted, and except for 2009, these do not contain information on SBS. Moreover, as information provided to the evaluation team by individual CPs shows, figures in the annual reviews are sometimes incomplete. Data provided by BoZ on disbursements for most years is only preliminary or estimates, not actuals. It seems that exchange rate effects and even definitional differences cannot explain all the discrepancies, and that there are serious shortcomings regarding reporting, record keeping, and information sharing on BS flows on both sides of the aid relationship.

Table 6: Budget support disbursements by donor (million US-\$)

	2002	2003	2004	2005	2006	2007	2008	2009
Grants								
Finland						6.7	6.8	6.5
Germany						6.7	6.8	12.9
Netherlands					7.5	13.6	13.6	12.9
Norway		0.1		6.1	12.8	19.0	27.1	25.1
Sweden				0.5	6.9	14.2	17.2	
United Kingdom	0.1			28.3	41.1	49.5	51.7	48.6
o/w PRBS					36.1	44.5	51.7	48.6
o/w SBS Health ¹					5	5		
EC	65.3	32.7	52.1	65.4	63.1	48.9	87.5	109.6
o/w PRBS				31.9	39.5	39.7	37.9	86.9 ²
o/w SBS Roads				30.5	23.6		46.0	
o/w SBS Health						7.2	3.6	16.9
o/w PEMFA				3.0		2.0		5.7

Table 6: cont.										
Total PRBS grants	65.4	32.8	52.1	66.8	102.8	141.5	163.6	192.9		
Total GBS/SBS grants	65.4	32.8	52.1	100.3	131.4	155.7	213.2	215.6		
PRBS loans										
AfDB				9.0	8.8		30.6	23.0		
World Bank								9.6		
Total PRBS loans				9.0	8.8		30.6	32.6		
Total budget support	65.4	32.8	52.1	109.3	140.2	155.7	243.8	248.2		

Note: This table is the result of extensive cross-checking of different sources. Some doubts remain, especially with respect to 2002/3 figures. Minor discrepancies are explained by different exchange rates applied in different sources.

¹ Since DFID gave up its traceability requirement for its health SBS in 2008 and now provides it within its PRBS contribution without any specific arrangements for conditionality or TA, it is considered as part of DFID's PRBS funding after 2007. For 2006 and 2007, 5 million US-\$ are calculatory SBS.

² Including 38.4 million US-\$ V-FLEX; Sources: EU/GRZ (2008), OECD/DAC, MoFNP, CPG, BoZ, Gerster / Chikwekwe (2007), Whitworth (2010), EC (2007)

3.2 Non-financial inputs

3.2.1 Policy dialogue

According to the intervention logic on which this evaluation is based, policy dialogue as a non-financial input of BS is important as a contribution to better policy choices, overall improved governance, and ultimately, for making donors' financial contributions as well as domestic budget resources more effective in achieving development objectives. An effective dialogue mechanism should facilitate coordination and communication within the government system, between the government and its cooperating partners, and among CPs themselves.

The formal dialogue architecture for BS policy dialogue in Zambia involves different actors, fora and mechanisms. The dialogue mechanisms directly related to PRBS have their formal roots in Part 5 of the MoU of PRBS, which states that “regular consultation among the Signatories is considered critical to continued engagement by the PRBS Group and effective implementation of the National Development Plan and subsequent reform strategies” (GRZ 2005c, 9).

The main fora for regular PRBS dialogue are the Joint Steering Committee (JSC), the Joint Executive Committee (JEC), and the bi-annual meetings which take place as part of the Joint Annual Review (JAR) process.

Joint Steering Committee (JSC): The JSC is the main steering body in the PRBS dialogue architecture and the driver of the joint GRZ/CP PRBS-agenda. The JSC is composed of both government and CPs representatives, with the CP side being represented by three lead donors on a rotational basis.

The JSC is co-chaired by GRZ and CPs and meets quarterly to

- discuss progress made with respect to the performance indicators as agreed in the PAF
- prepare for review meetings
- act as a forum for dialogue as specified in Part 5 of the MoU
- mediate in dispute settlements as specified in Part 11 of the MoU.

According to the PRBS-MoU, any signatory “may at any time identify an issue which that Signatory feels is relevant to the implementation of the

MoU and is permitted to notify the JSC, through the Secretary to the Treasury, of its wish to enter into dialogue on that issue” (GRZ 2005c, 13).

Joint Executive Committee (JEC): The work of the JSC is co-ordinated by a small Joint Executive Committee consisting of three representatives from GRZ and two PRBS Group members. The members are elected by the members of the JSC from amongst themselves and rotate annually. The JEC is responsible for routine coordination activities as well as the preparation of joint reviews and the management of follow-up activities. In case any MoU Signatory wishes to raise a relevant issue for dialogue, the JEC will convene a meeting of both sides to agree upon the dialogue process on the issue in question.

Joint Annual Review (JAR): Besides the quarterly JSC and JEC meetings, GRZ and PRBS Signatories meet twice a year as part of a structured annual review process. The JAR meetings are jointly called by Government and CPs and are open to the participation of parliamentarians and representatives of civil society. The MoU provides for these meetings to take place in June and October every year.¹⁸

According to the MoU, the June meeting’s focus is that the signatories arrive at a joint view on performance; this serves as the basis for commitments for the following budget year. The main reference for the performance assessment is the jointly agreed-on Performance Assessment Framework, or PAF (see Section 3.2.2.2); the assessment itself is to be based on the National Development Plan’s Annual Reviews, the annual PEMFA progress reports, the Quarterly Budget Execution Reports, national audits, and any other prior analytical work agreed upon in relation to the PAF (GRZ 2005c).

The October meeting’s focus is on dialogue regarding forward planning and budgeting; it serves to update the PAF and to agree on indicators to be included in the PAF for the coming year. According to the MoU, this dialogue is to be based on the government’s “annual financial reports of the previous budget year, the annual PEMFA evaluation and the ceilings in the annual budget for the next budget year” (GRZ 2005c, 11).

18 The MoU also states that “the Signatories aim to merge the two review meetings into a single annual review meeting” (GRZ 2005c, 10).

In sum, the JAR dialogue involves:

- A review of performance, budget execution and expenditure priorities on the basis of the indicators described in the PAF.
- A review of underlying principles.
- A review of action plans for policy priorities and the national budget for the next budget year, including the link between poverty reduction priorities and inter-sectoral allocations.
- A discussion of the Medium Term Expenditure Framework (MTEF) of GRZ.
- A confirmation of CPs' commitments for BS for the following year.
- Follow-up on audits.

The JAR meetings are jointly called by Government and CPs and are open to the participation of parliamentarians and representatives of civil society.

The JAR also provides a close link to other dialogue fora, which do not exclusively cover the PRBS process. Most importantly, the review process builds on the sector dialogue conducted in the so-called Sector Advisory Groups (SAGs), which were set up as part of the National Development Plan formulation process. In principle, the SAGs continue to play a key role in monitoring the FNDP and reviewing sector outcomes and performance. In this function, the performance of the individual SAGs is crucial not only for the quality of Policy Dialogue but also for other processes such as the MTEF (Gerster / Chikwekwe 2007, 11ff.).

The 21 SAGs are chaired by the Permanent Secretaries of the leading ministries. The SAGs meet more or less on a regular basis, with the Government inviting all major stakeholders, including donors, civil society bodies, and members of the private sector to participate in the meetings.

In addition, the PRBS policy dialogue is closely linked to the annual High Level Policy Dialogue (HLPD) Meeting between Government and the Group of CPs (CPG) that are signatories to the Joint Assistance Strategy (JASZ).¹⁹ The HLPD is chaired by the Minister of Finance and National

19 All PRBS donors are members of the CPG. Currently included are Canada, Denmark, Finland, France, Germany, Ireland, Italy, Japan, the Netherlands, Norway, Sweden, UK, the United States, the African Development Bank, the European Commission, the IMF, the United Nations System and the World Bank. Other CPs may attend as observers.

Planning. The CPG is subdivided into two sub-groups, namely, the Heads of Cooperation (HoC) and the Heads of Mission (HoM).

While the HoM are responsible for general strategic and political dialogue at the highest level, the HoC mainly address operational multi-sector issues as well as strategic development policy issues. The HoC is led by a troika consisting of two bilateral donors and one multilateral agency.²⁰ The troika members convene at least once a month and also meet on a monthly basis with the Secretary to the Treasury at the Ministry of Finance and National Planning to discuss a diversity of issues (usually defined by the troika).

The overall purpose of the HoC is to facilitate regular and open policy dialogue within the CPG between CPs and Government, thereby promoting overall coordination and aid effectiveness.²¹ The HoC group also coordinates and prioritizes CPs' policy positions for the HLPD with Government.²²

Upon invitation, representatives of civil society can attend the annual HLPD meetings. In practice, however, this rarely seems to happen.

Besides the regular dialogue process taking place at the regular meetings of the JSC, the JEC and within the framework of the JAR and the HLPD, the PRBS-MoU also provides for any signatory to initiate a dialogue process on particular issues of concern at any time. The MoU does not prescribe a particular process for this non-routine dialogue, but allows substantial flexibility as to how to frame this issue-driven dialogue. In particular, the MoU states that:

“Any Signatory may at any time identify an issue which that Signatory feels is relevant to the implementation of this MoU (including concerns regarding Underlying Principles), and may notify the JSC of its desire to enter into dialogue on that issue, by writing a letter to the Secretary to the Treasury for forwarding to the JSC. On receipt of notification that a Signatory wishes to enter into dialogue, the Chairs of the JSC will pass the letter to the Joint Executive Committee to convene a meeting of the JEC to agree a process for dialogue on the issue in question. In convening such a meeting, the JEC will also invite PRBS Group members to identify other issues of a similar nature

20 In order to ensure continuity, each donor/agency in the troika serves as a member for 18 months: six months as an incoming member, six months as chair, and six month as an outgoing member.

21 See CPG website: www.cpg.org.zm

22 In preparation for the annual HLPD meetings, both the government and CPs prepare position papers in which the latter usually responds to the former's submission.

which might usefully be discussed in the same process of dialogue, so as to reduce transaction costs for all concerned between the Review meetings described above” (GRZ 2005c, 13).

Importantly, the MoU does not formulate any requirement for consensus or a majority among the PRBS CPs to initiate such a dialogue.

There are no similar dedicated dialogue structures for sector budget support operations. SBS-specific issues are routinely dealt with either bilaterally or within the formats of PRBS policy dialogue or within the dialogue structures linked to SWAPs. This might be related to the fact that SBS is provided by only two CPs (UK and the EC) in the health sector and only by the EC in the roads sector (see Box 2). To a certain extent, this might also be an expression of the fact that SBS is provided mainly with the aim of providing funding to specific sector activities and puts less focus on improving overall GRZ governance and policy making.²³

3.2.2 Conditionality: Underlying Principles & Performance Assessment Framework

Closely interlinked with the PRBS policy dialogue is the conditionality attached to the provision of budget support funding. In Zambia, budget support conditionality is applied on two levels, namely the Underlying Principles (UPs) that frame the general and mutually agreed-on basis for budget support, and the Performance Assessment Framework (PAF), which serves to assess the government’s (and more recently also the CPs’) performance in implementing the programme.

3.2.2.1 Underlying Principles

PRBS is provided on the basis of a Memorandum of Understanding (MoU) between GRZ and the PRBS Group that “sets out the jointly agreed terms and procedures for direct budget support from the PRBS Group to the National Development Plan and serves as a co-ordinating framework for consultation with the Government, for joint reviews of performance, for common procedures on disbursement, for reporting and for audits” (GRZ / PRBS Group 2005, 4).

23 For a more extensive discussion of CP’s different objectives in providing budget support see Chapter 6.

According to the MoU, PRBS is provided on the precondition of GRZ's commitment to "fight poverty, including through a pattern of public expenditure consistent with poverty reduction priorities as identified in the National Development Plan" as a basic principle (GRZ / PRBS Group 2005, 5). In addition, the MoU identifies three Underlying Principles (UPs) for the provision of direct budget support:

- GRZ's Commitment to peace, democratic principles, the rule of law, good governance and integrity in public life, including the fight against corruption
- GRZ's Commitment to public financial management reforms
- GRZ's Commitment to pursuing sound macro-economic policies, as evidenced by a positive IMF assessment of overall macro-economic performance

The violation of a UP is understood as being above and beyond concerns raised about under-performance against indicators and targets expressed in the PAF (see Section 3.2.2.2). In case of perceived violation of an UP, the MoU prescribes an escalating dialogue process. If despite this dialogue process the PRBS Group still feels that the government is making no serious attempt to improve the situation in spite of remonstrations, the PRBS Group may consider suspending disbursement of the agreed-on instalments, reducing levels of budget support for future years, or terminating the agreement fully (GRZ / PRBS Group 2005, 19).

The UPs are subject to continuous monitoring by the PRBS Group as part of the annual review process. It is important to note that the UP assessment (in particular that of 'commitment to good governance') is to a large degree based on each CP's judgement, which means that a *perceived* violation of the UPs suffices to initiate the High Level Policy Dialogue prescribed by the MoU.²⁴ At the same time, positive assessment of the UPs is a precondition for CPs PRBS commitments within the framework of the annual review process. The UPs thus constitute the core of PRBS conditionality and provide a key entry point for CPs for the dialogue with GRZ on the overall reform agenda.

24 Regarding the macro-economic stability requirement, CPs rely on a third party (IMF) assessment. Progress with regard to financial management reforms is in practice assessed according to progress in implementing the PEMFA programme, which can be argued to be a comparatively objective measure. The commitment to poverty reduction is mainly assessed on the basis of PAF performance and FNDP implementation progress.

3.2.2.2 Annual performance assessment

In addition to the Underlying Principles, CPs condition their budget support commitments and – partly – their disbursements on GRZ progress attained in implementation of the National Development Plan. This progress is to be measured through jointly agreed-on performance indicators as described in a Performance Assessment Framework (PAF), which the MoU defines as “a multi-annual matrix of priority milestones, targets and indicators based on the National Development Plan, Public Expenditure Management and Financial Accountability reforms under the PEMFA programme and related initiatives over time, other components of public service reform, macro-economic stabilisation policy and debt sustainability” (GRZ / PRBS Group 2005, 4).

The PAF developed in Zambia is a mixture of policy measures and outcome indicators. Progress on PAF targets and indicators is at the centre of the joint GRZ / CPs annual PRBS Review.²⁵ The PAF is thus updated annually with the formulation of new targets and the elimination and/or introduction of new indicators.

Since 2006 the PAF has evolved into a comprehensive framework of targets and indicators, with the current 2009-2011 PAF covering four main areas or pillars, namely: (a) public sector reform (decentralization, public sector management, public finance management, domestic taxation, financial sector development); (b) wealth creation (agriculture, infrastructure incl. roads, energy and water, private sector development); (c) social equity (health, education); and (d) cross-cutting issues (HIV/AIDS, environment).

The distribution of targets across these pillars is given in Table 7. The PAF for 2009-2011 contains 38 targets.²⁶ Although there has been no major shift in the sector focus, which from the beginning was mainly on the first two pillars Public Sector Reform and Wealth Creation, the number of targets for measuring GRZ performance has increased steadily since 2006. The 2010-

25 Apart from the PAF reports, the reviews include *inter alia* the National Development Plan's Annual Reviews, the annual PEMFA progress reports, quarterly budget execution reports, and the results of national audits.

26 The target for the third of three Private Sector Development indicators on labour productivity was to be determined during the first quarter of 2009. It was later found that no common definition could be agreed on; the indicator was not assessed, and it was recommended that it be dropped in the June 2010 Review. (For this reason Table 4.2 shows only 37 indicators for 2009.) The PAF for 2010 and 2011 was revised in late 2009 and narrowed down to 25 indicators.

2012 PAF was revised in late 2009 and narrowed down to 25 indicators. The number of indicators for public sector reform was reduced from 15 to 10; for wealth creation the number of indicators was brought down from 10 to 5.

It is important to note that even though it can be argued that all PAF indicators are in line with these FNDD pillars, they do not all have an equivalent among the Key Performance Indicators (KPIs) identified in the FNDD for monitoring purposes. For instance, of the 37 indicators used to measure GRZ performance in the 2009 PAF (see Table 7), only 19 have a more or less direct equivalent in the FNDD KPIs (see Section 4.2.2.2).

Based on the assessment of each indicator, an overall PAF score is computed as an aggregate measure of GRZ performance (cf. Figure 6: PAF performance 2006-2009 in Section 4.2.2.2).

Since 2007 the framework has also included a “Donor PAF” which assesses the CPs’ performance with regard to the target alignment and predictability of their support.²⁷

The indicators linked to measuring the government’s progress in meeting the targets can be divided into process indicators and outcome indicators. The majority of indicators and targets in the PAF are outcome-oriented and quantitative in nature, in that they set quotas and benchmarks or milestones that are to be reached by the government without prescribing any specific policy actions. However, process indicators have also been integrated from the very beginning, primarily in the areas of Public Service Management, Public Financial Management, and Agriculture.

Overall, the number of process indicators has remained relatively constant and small. Starting with seven in the 2006 PAF, the number of such policy measures has been reduced in 2007 and 2008. The PAF for 2009 contains an increased number of indicators, of which seven are policy measures.

The PAF is a centrepiece of PRBS conditionality, since CPs link their commitments as well as their disbursements of budget support to it. However, the mechanisms by which the individual CPs link their disbursements to the PAF vary substantially;

27 The targets in the Donor PAF are: (a) the proportion of ODA given as BS (showing an alignment with the government’s preferred aid modality), (b) the amount of PRBS disbursed as a percentage of commitment, (c) the weighted average deviation of the months of disbursement against the months of commitment. (MoFNP 2008, 15).

Table 7: Number of PAF targets and indicators 2006-2009				
	2006	2007	2008	2009
Public sector reform	13	11	11	15
Decentralisation			1	2
Public Service Management	3 (1)	4	3	3
Public Finance Management	4 (1)	4 (1)	4 (1)	7
Macroeconomic	3			
Domestic Taxation		1	1	1
Financial Sector Development	1 (1)	1	1	1
Public Service Pension Fund	2	1	1	1
Wealth creation	9	9	10	10
Agriculture	3	3	3	3 (1)
Infrastructure	4	4	4	5 (2)
Private Sector Development	2	2 (1)	3	2 (1)
Social equity	7	8	8	8
Health	4	4	4	4
Education	3	4	4	4
Cross cutting	2	3	4	4
HIV / Aids	2	3	3	3
Environment			1	1
Total indicators GRZ	34	33	34	41
Total targets GRZ Performance	31	31	33	37
Targets Cooperating Partners		3	3	3
Note: Monitoring indicators with no target are in brackets.				
Source: PAF Progress Reports				

- **Germany and Finland** disburse their budget support as a fixed tranche based on an overall positive assessment of PAF performance as a measure for the Underlying Principle of government commitment to poverty reduction.
- **The Netherlands** disburse a fixed tranche based on overall positive PAF performance and commit an additional ‘incentive tranche’ to be disbursed if the overall PAF score exceeds 80 %.²⁸
- The **UK** also disburses a fixed tranche based on overall positive performance and commits an additional performance tranche linked to overall PAF performance, but with different thresholds: no performance tranche is disbursed for an overall PAF score below 50 %, and a linear disbursement rule (rounded up to the nearest £ 0.5 million) is applied for PAF scores between 50 % and 80 %.²⁹ At a PAF score above 80 %, the full variable tranche would be disbursed.³⁰
- **Sweden and Norway** also both operate a fixed and variable tranche. While the fixed tranche is based on overall PAF performance, the variable tranche is linked to performance as measured by selected PAF indicators (with performance in year n-1 determining disbursement in n+1).
- The **European Commission**, in addition to its fixed tranche, operates two variable tranches which are linked to specific PAF indicators: an annual performance tranche that is determined by the annual performance assessment; and a performance tranche under the 6-year MDG-Contract scheme, where performance over the first three years of the arrangement determines disbursement in years 4 to 6.
- The **World Bank** and the **African Development Bank** do not use a fixed tranche but rather operate floating tranches which are disbursed once a set of selected PAF indicators (prior actions) has been met.

28 For 2009, the incentive tranche would have been € 3 million, on top of a € 10 million fixed tranche. So far, however, this incentive tranche has never been disbursed due to PAF performance below the threshold.

29 For example, a PAF score of 65 % would trigger a disbursement of 50 % of the variable tranche.

30 The UK applies this approach since 2009. In both 2009 and 2010 the variable tranche accounted for 13 % of the UK’s budget support commitment. In 2009, 62.5 % percent of the variable tranche was disbursed.

The share of the variable tranche in overall commitments also differs among the CPs: Norway and Sweden reserve 50 % of their commitments for their variable tranches, the UK only 13 %. The Netherlands in 2009 would have been able to disburse an additional 30 % as incentive tranche. The EC, in turn, has reduced its performance tranche continuously from an initial 91 % to 25 % in 2010. In 2009, no variable tranche was foreseen by the EC. In 2007, the combined fixed tranches made up 84 % of the overall PRBS commitments (Gerster / Chikwekwe 2007, 17).³¹

3.2.3 Technical assistance and capacity building

In conjunction with the provision of BS, the cooperating partners acknowledge the importance of effective government institutions, legislation and regulations that facilitate improved management of national resources and external funds. In order to assist the GRZ in improving the quality, efficiency, cost-effectiveness and delivery of public services to its people, CPs have engaged in a number of programmes and initiatives of technical assistance and capacity development. These activities, partly conducted as accompanying measures of BS, were embedded in the context of the government's own reform agenda. The GRZ has been implementing the *Public Service Reform Programme* (PSRP) since 1993, which was recently re-formulated as PSRP II.³² In line with this GRZ owned programme, the majority of BS donors provide funding in support of the PEMFA programme, the first component of PSRP. This funding is provided through a dedicated basket mechanism.³³ In addition, a number of CPs support the Government in

31 For a synopsis of the use of the 2009 PAF for disbursement decisions see Table 12 in Section 4.2.2.2.

32 The PSRP II encompasses three distinct areas of reform: (a) Public Expenditure Management and Financial Accountability (PEMFA), a programme implemented by the MoFNP; (b) Public Service Management (PSM), implemented by the Cabinet Office (CO) under the Management Development Division; and (c) Decentralization, entailing fiscal devolution through the development and consolidation of intergovernmental fiscal architectures with a focus on different transfer modalities of grant funds to the local level. Decentralization is implemented by the Ministry of Local Government and Housing (PEMFA 2010, 1).

33 Formally, the EC supports the PEMFA programme through SBS, but from the BoZ/GRZ side these funds are treated as basket contributions too (see Section 3.1).

building capacities at the Office of the Auditor General (OAG) as well as in Parliament or engage in other BS-related technical assistance. A selection of BS-related capacity building activities is listed in Box 3.

Box 3: Budget support-related capacity building activities

U.K. Department for International Development. Providing support to the Anti-Corruption Commission. Strengthening of political parties. Offering technical assistance to the Secretary to Cabinet. Supporting professionalization of the public service.

Millennium Challenge Account. Providing support to the Anti-Corruption Commission and Zambia Revenue Authority. Helping government implement provisions of the National Corruption Prevention Policy and Strategy (setting up of integrity committees in a few ministries). Re-engineering work processes in the Department of Immigration, Patents and Company Registration, Zambia Revenue Authority, and the Ministry of Lands.

U.S. Agency for International Development, DFID, EU and others. Providing support for the implementation of parliamentary reforms.

Norway and Netherlands. Supporting the Office of the Auditor General in implementing reforms in audit practices and effectiveness.

Norway, UNDP, Denmark and others. Supporting access to justice and judicial reforms. Building courts and supporting the recently set up Governance Secretariat.

European Union. Supporting capacity development in civil society organizations. Supporting the government in electoral reforms

Consortium of donors. Providing financial and capacity development support to the Task Force on Corruption.

Source: World Bank (2008a)

3.2.3.1 The Public Expenditure Management and Financial Accountability (PEMFA) Programme

The objective of PEMFA is to contribute to the efforts of the government in improving efficiency, effectiveness and accountability in the management and utilisation of public financial resources at both the central and sub-national levels in order to improve public expenditure management and to strengthen financial accountability overall. With regard to BS, positive results of the programme would increase CPs' confidence in GRZ's own

country and PFM systems (Hedvall et al. 2007, 6). The programme is supported by the signatories to the PEMFA MoU, including all nine PRBS donors: Norway, The Netherlands, Germany, Sweden, Finland, Ireland, Denmark, United Kingdom, the US, the European Commission, the World Bank (IDA), the United Nations, the African Development Bank (AfDB). GRZ also provides counterpart funding to meet recurrent costs (PEMFA 2010, 1).

The PEMFA Programme was initially a five-year programme (2005-2009) with 13 components, namely: (1) a Commitment Control System (CCS) and Financial Management System (FMS); (2) IFMIS (Integrated Financial Management Information System) implementation; (3) Improved Fiscal Policy and Economic Planning; (4) Reformed Budget Preparation and Budget Execution; (5) Improved Debt Management; (6) Improved Internal Audit; (7) Better External Finance and Coordination; (8) a Legal and Regulatory Framework; (9) Strengthened External Audit; (10) Enhanced Parliamentary Oversight; (11) Accountancy Training and Regulation; (12) Public Procurement Reform; and (13) a Centralized Computer Services Department (Hedvall et al. 2007, 6).

Contributions to the budget for the programme for the five-year period by co-operating partners amount to US-\$ 72.2 million. By March 2009, 55 % or US-\$ 39.7 million had been utilized (MoFNP 2009, 3). The PEMFA Programme was (cost-neutrally) extended for one year and will end in 2010 (PEMFA 2010).

3.2.3.2 Technical assistance and capacity building at the Office of the Auditor General and in parliament

One particular element of PEMFA is the strengthening of oversight systems. On the basis of the National Governance Baseline Survey Report published in August 2004, a series of measures were introduced to reduce the occurrence of corrupt practices, including a process of strengthening the Office of the Auditor General (OAG). In 2004, the Government approved the restructuring of the OAG, which included the decentralization of the Office to all districts in the country.

Norway and the Netherlands engage in a programme to assist the OAG, a programme purposely de-linked from the wider PEMFA in order to guarantee independence of the Auditor General (NORAD 2007, 56). Moreover,

budget support CPs are involved in a variety of corruption-fighting activities that are not necessarily part of the PEMFA programme (NORAD 2007; DFID 2008).

In the last 10 years, a number of donors, including USAID, EU, Finland and Germany and UK, have initiated capacity building projects targeting Members of Parliament (MPs). USAID operates a five year support programme through the Economic Association of Zambia (EAZ). The EU programme consists of three phases: Phase one provides capacity building for MPs, Phase two provides hardware and office construction, Phase three will establish constituency offices. For the last five years, MPs have received regular capacity building through technical assistance and training. For instance, the EAZ has developed budget literacy guidelines, conducted training courses, and advised MPs and relevant Parliament Committees before, during and after budget execution every year. Besides this, MPs are entitled to issue calls for expertise aid from the public. In addition, parliamentary committees were enabled to adopt different consultation forms in order to attain different opinions from the public in the decision-making process. The problem with the support for MPs however, is the high turnover rate of MPs in elections, which means that only a minority of MPs stay long enough to gain significant experience.

Another important TA programme not directly linked to but highly relevant for the PRBS programme is the assistance provided by Germany through GTZ to MoFNP. This programme, in effect since 2006, aims at supporting MoFNP in incorporating the Poverty Reduction Strategy into the budget process by providing TA to various MoFNP departments (Monitoring and Evaluation, Central Statistics Office, Planning and Economic Management, Budget Office). In addition to building capacities in relation to the national budget processes, this programme contributes to PRBS processes by generating and improving the data for the monitoring and evaluation of government performance (Larizza / Marten / Pain 2009).

4 Direct outputs

EQ2: To what extent has BS in Zambia led to increased external funding subject to the government's budgetary process, along with the establishment of a policy dialogue framework and the harmonization/alignment of external assistance?

2.1 To what extent has BS contributed to an increased size and share of external funding subject to government's budgetary process and improved the predictability of overall flows of external assistance?

2.2 To what extent has BS contributed to the establishment of a framework of policy dialogue with a focus on key government strategies and priorities?

2.3 To what extent has BS contributed to the provision of non-financial inputs, such as technical assistance and capacity building, which are regarded as strategic government priorities?

2.4 To what extent has BS contributed to harmonization and alignment of external assistance, and reduced transaction costs over time?

4.1 Budget support's role in aid transparency and predictability

4.1.1 Has budget support increased the size and share of aid subject to the government's budgetary process?

Budget support has increased the size and share of aid subject to GRZ's budgetary processes; it has facilitated planning, accounting, and reporting procedures for the Government with regard to aid inflows; however, this did not happen at a level where a substantial reduction of overall transaction costs of development cooperation could be expected.

The extent to which budget support has increased the share of external support that is channelled through GRZ's own budget planning, execution and control processes varies according to the data source employed. An analysis by DFID in Lusaka conducted in 2010 (Whitworth 2010) on the basis of IMF data on GRZ receipts of grants and budget support puts the proportion of budget support in total grants at an average 29 % in the 2005-2009 period, compared to 19 % for the years 2002-2004 (see Table 8).

MoFNP data on grants from the annual financial reports and the figures on budget support disbursements collected from various sources (see Table 6)

Table 8: Budget support as share of total grant receipts, ZMK billions									
	2002	2003	2004	2005	2006	2007	2008	2009	
DFID analysis, based on IMF data									
Grants	1.350	1.424	1.433	1.825	1.797	2.104	2.069	2.790	
Budget Support	324	229	258	543	423	582	642	879	
BS / Grants	24%	16%	18%	30%	24%	28%	31%	32%	
MoFNP and authors' data on budget support disbursements									
Grants			1668	1880	699	1461	1503		
PRBS Grants	288	155	249	298	370	566	613	973	
Budget Support Grants	288	155	249	448	473	623	798	1088	
PRBS Grants / Total Grants			15%	16%	53%	39%	41%		
Total BS/ Total Grants			15%	24%	68%	43%	53%		
Source: Whitworth (2010), MoFNP, CPs and others									

show a significantly higher share of budget support in total grants. According to this data the share of budget support in grants peaked in 2006 when PRBS grants accounted for 53 % of total grants and total budget support (including SBS) for 68 % of grants receipts (Table 8). In the following two years, the share of total budget support received fell 43 % and 53 % of grant receipts.

However, these figures overestimate the relative role of budget support in total aid receipts, since they include only aid flows that are recorded in the government budget. Taking OECD/DAC data on ODA flows since 2003 puts the relative importance of budget support in a more realistic perspective: as a proportion of total ODA receipts (excluding debt relief), budget support has continuously risen since 2003 from 6.5 % to 21.9 % in 2008, before it fell again to 19.7 % in 2009. For OECD/DAC donors only, the share of budget support in total ODA (excluding debt relief) rose from 9.4 % in 2003 to 31.0 % in 2009.

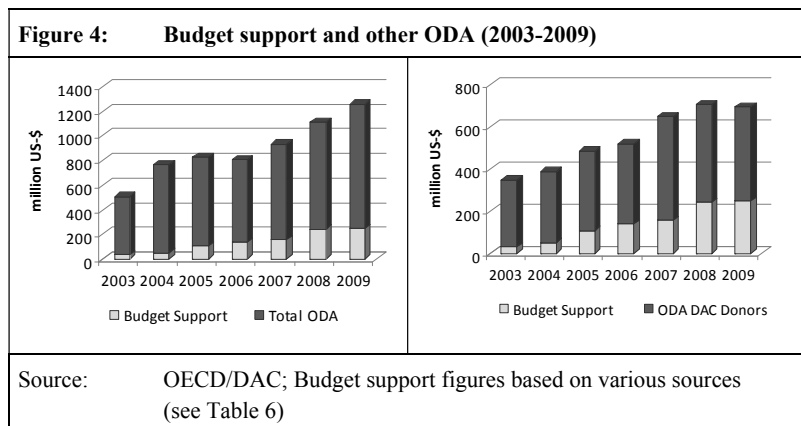
Even when including basket funding which is channelled at least partly through government systems as well, the proportion of “through-budget” funding in total ODA (all donors) never exceeded 30.3 % (2007; 2009: 28.1 %).³⁴

For PRBS donors alone, the share is even higher: data on the share of PRBS disbursements in total ODA is reported for the last three years in the 2010 PAF Progress Report (see Table 9). According to this data, the share of budget support for PRBS CPs (including sector budget support) as a proportion of ODA disbursements to GRZ from PRBS donors increased from 40.2 % in 2007 to 58.7 % in 2008, but dropped again to 53 % in 2009.

It is clear from these figures that increasing the share of aid resources that are subject to GRZ’s own planning and budgeting processes gave budget support the potential to improve the allocative efficiency (Box 1 in Section 1.2.2) of public expenditures in Zambia. At the same time, no substantial reduction of transaction costs on either side of the aid relationship can be expected from this, since the amount of off-budget aid requiring parallel planning, administration, and reporting processes is still substantial.³⁵

34 According to data on SWAp disbursements collected by IOB (not reported here).

35 The difficulties posed for MoFNP planning, implementation, and reporting procedures by aid provided directly to sector ministries poses has been stressed by various GRZ interview partners.



4.1.2 Has budget support improved the predictability of aid flows?

Aid predictability in Zambia in general is fairly poor; this seriously undermines the effectiveness of GRZ planning and cash flow management.

This applies especially for project-based aid. According to one CP's internal analysis, for instance, only 58 % of the planned donor funded investments recorded in the budget in 2007 were actually disbursed. However, as Figure 5 shows, PRBS predictability has been relatively poor as well: in 2007, actual disbursements were a mere 77 % of commitments, while disbursements in 2008, were 15 % higher than commitments. This finding is in line with the 2008 PEFA assessment, which gives direct budget support predictability in Zambia a grade of D+.³⁶

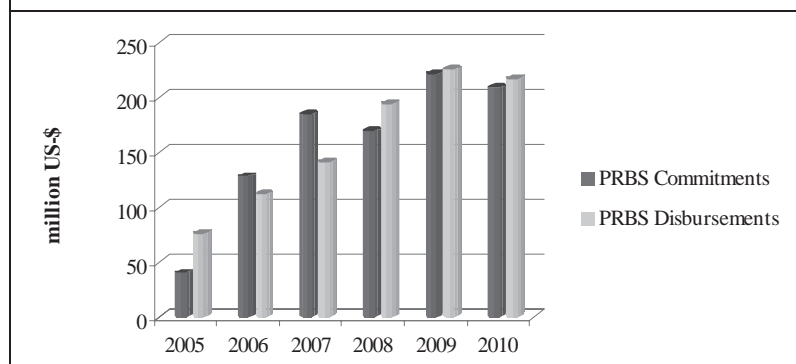
Moreover, even though it may seem from Figure 5 that PRBS predictability in 2009 had improved significantly, the aggregate figures mask substantial variance between the commitments and disbursements of individual CP's.

³⁶ The PEFA (Public Expenditure and Financial Accountability) performance measurement system grades government performance on the basis of 28 high-level indicators in 6 dimensions of public financial management and donor performance on the basis of three indicators, including the predictability of direct budget support. The grades given for each indicator range from A (best) to D (worst); see PEFA (2005).

Table 9: Budget support as proportion of ODA disbursements from PRBS donors 2007-2009			
	2007	2008	2009
Grants			
EC	71.7 %	66.9 %	57.37 %
Finland	39.8 %	46.9 %	35.17 %
Germany	24.4 %	24.3 %	33.73 %
Netherlands	25.1 %	17.4 %	36.86 %
Norway	39.6 %	67.1 %	74.95 %
Sweden	20.6 %	33.0 %	0.00 %
United Kingdom	83.5 %	74.1 %	91.66 %
Credits			
AfDB	61.4 %		53.07 %
World Bank	0.0 %		0.00 %
Total	40.2 %	58.7 %	53.00 %
Note: The budget support figures underlying this analysis are not the same as those reported in Table 6, since some disbursements (e.g. a World Bank disbursement of US-\$ 9.6 million in December 2009) were not recorded in the PRBS reviews.			
Source: MoFNP (2010)			

This was particularly pronounced in 2009, when Sweden did not disburse its PRBS (against a commitment of US-\$ 18.3 million) as a reaction to the corruption scandal in the health sector (see Box 4), whereas the EC (with the addition of a € 30 million V-FLEX allocation) and the AfDB (disbursing US-\$ 23 million against a commitment of US-\$ 11.5 million) disbursed considerably more than what they had committed. As a result, the total amount disbursed was only slightly higher than the amount committed; this provided some form of predictability for the national budget (MoFNP 2010, 21).

Figure 5: Predictability – PRBS commitments and disbursements (2005-2010)



Notes: 2007 includes a small portion of DFID sector budget support (health). PEFA figures on commitments for 2007 differ from PAF progress reports (US-\$ 193.9 million versus US-\$ 184.52 million).

Source: 2005-06: 2008 PEFA Assessment, 2007-09: PAF Progress Reports, various sources on disbursements

According to one MoFNP official, however, the main problem for predictability over the past three years from the Ministry’s perspective was more with timing than with the amounts disbursed. Late disbursements affect budget implementation, since unused funds must be returned from line ministries to the Treasury.³⁷

Through 2007, CPs provided reports on their disbursements of budget support semi-annually, but not quarterly. From 2008 on, CPs agreed to provide monthly estimates (GRZ 2008, 38). Since 2008, CPs regularly negotiate a disbursement schedule with GRZ that is used for GRZ’s annual cash flow plan as well, thus underscoring the importance of timely disbursements.

Since its introduction in 2007, the ‘Donor PAF’ (see Section 3.2.2.2) includes an indicator for measuring the delay of BS disbursements against

37 According to the same official, the cabinet can allow sector ministries to keep unused funds if they are intended for capital expenditure.

the commitments made at the time of the November review. The average delay of disbursements per donor during each year as well as the total average is given in Table 10. The figures show that donor performance varies substantially between donors as well as across years.

A number of agencies experienced important delays in releasing resources. The CP with the longest delays among those which actually disbursed was the European Commission (with an average of 5.6 months in 2009, 3.0 in 2008, and 6.61 in 2007). Finland performed best in 2007 and 2008, with no delay; in 2009 (when some CPs withheld disbursement after the corruption scandal in the health sector) only the UK, Norway and the AfDB disbursed without delay.

The Strategic Partnership with Africa's Budget Support Working Group conducts a regular survey of budget support operations across Africa. The surveys include information provided by donors concerning the reasons for delayed disbursements. Table 11 shows the information provided in the 2005, 2007, and 2008 surveys for Zambia.

Table 10: Average delay (in months) of budget support disbursements 2007-2010				
	2007	2008	2009	2010
Finland	0.00	0.00	4.00	0.0
Germany	6.00	2.00	3.00	4.0
Netherlands	1.00	0.00	1.00	0.0
Norway	3.31	1.00	0.00	0.0
Sweden	3.00	0.00	8.00*	
United Kingdom	1.37	0.28	0.56	1.0
EC	6.61	3.00	5.60	9.0
AfDB	12.00*	0.00	0.00	3.0
World Bank	12.00*			4.0
Total	5.03	0.78	3.11	3.7
*no disbursement				
Source: MoFNP (2010)				

In contrast to 2009, as the reasons given in Table 11 suggest, most delays in the first years of PRBS were related to administrative problems on both sides of the aid relationship. This could be regarded as an unavoidable learning process on both sides. As Table 10 shows, the total average delay improved significantly in 2008, suggesting that PRBS processes had begun to run more smoothly.

This positive development, however, was disrupted by various corruption-related issues in 2009. Preliminary data for 2010 suggest that some CPs disbursed on schedule or even ahead of schedule in the first three quarters of 2010, whereas the EC, for example, delayed disbursement of a fixed and variable tranche totalling US-\$ 42.7 million, which had been scheduled for March, until October. Germany, in turn was withholding disbursement of € 10 million at the time of writing, pending a decision on how to assess recent developments with regard to GRZ's demonstrated commitment to fight corruption.

4.2 Non-financial contributions: Ownership, alignment & harmonization

As elaborated in Section 1.2.3, the effectiveness of non-financial contributions to budget support programmes does not depend solely on the quality of the individual contributions (input level). To an important degree, their potential effectiveness is also determined by the extent to which the provided inputs respect the principles of the Paris agenda for more effective aid, in particular the principles of ownership, harmonization, and alignment (direct output level). Accordingly, the following sub-sections assess the extent to which the provision of non-financial contributions has been guided by these principles. Where relevant, the question is also assessed of whether these budget support inputs have promoted the principles of ownership, harmonization, and alignment beyond budget support contributions, thus affecting the effectiveness of other aid contributions as well.

4.2.1 Policy dialogue

Over the last couple of years, as described in Section 3.2.1, a comprehensive dialogue structure has been established around the BS process, in continuation of previous efforts at harmonization and alignment of development aid to Zambia. In doing this, CPs and GRZ have provided the basis for a regular and structured policy dialogue. Nonetheless, following the inter-

Table 11: Reasons for delayed budget support disbursements		
Cooperating Partner	GBS Commitment (million US-\$)	Reason given by CP for delay
2007		
Sweden	14.24	IMF review delayed.
Netherlands	10.96	In 2007 the signing of the bilateral agreement took a longer than expected.
Germany	6.85	Delay due to late signing of documents.
EC	37.14	Delays were mainly of administrative nature, with a number of additional supporting documents requested by EC HQ.
AfDB	45.91	The first and major reason was delayed submission of the PRBS June review report, as agreed at inception. In addition, there was a delay associated with supply of wrong account details for holding the funds. Disbursement was indeed effected soon rectification of these two issues.
World Bank	10	The government advised that they would rather have the credit disbursed in 2008 than in late 2007 as was planned. Thus negotiations were deferred to 2008.
2006		
Norway*	12.98	An extra allocation was made from HQ in Norway that facilitated an additional disbursement of NOK 35 million late in 2006. However flexibility was expressively given and GRZ could have requested to transfer this amount to 2007 so as to not disturb the cycle of planning and expenditure in 2006 unduly.

Table 11: continued		
United Kingdom	35.56	PRBS CPs disburse upon written request from the Government. DFID received a late disbursement request for the Q3 payment.
World Bank	9.86	The Bank was committed to disburse against the new PAF and the new PRSP. However, government launched its PRSP only in early SDR 2007. 6.7 million are equivalent to circa US-\$ 10 million.
2005		
Norway	6.13	The bilateral agreement between Zambia and Norway was signed in the 4th quarter 2005 and linked to this the first disbursement was made in the same quarter. Initially an amount of NOK 30 million was planned but additional availability of funds on the Norwegian aid funds in 2005 led to a reallocation exercise leading to an additional NOK 9.5 million for Zambia that was channelled as GBS.
World Bank	20	The government delayed in meeting the milestones.
*no delay, but additional funding		
Source: SPA (2008)		

vention logic described in Section 1.2.3, the effectiveness of this dialogue also depends on whether it is structured and conducted in line with the principles of ownership, alignment, and harmonization.

The evaluation team's assessment of whether this has been the case in the past is ambiguous: on the one hand, the described structures certainly helped to discuss conflicting interests on conditionality and funding. In this regard, the established dialogue structure has provided strong incentives against further fragmentation of the negotiation process. Even though there

have been periods of both inactivity and accelerated progress, there is evidence that the BS related policy dialogue has promoted alignment and harmonization (Gerster / Chikwekwe 2007). Importantly, the dialogue structures showed some institutional stress resistance at times when the operational effectiveness of the dialogue structures was put to the test during the corruption crisis in 2009.

For this reason, the established dialogue provided a valuable firewall against further fragmentation, because the established mechanisms gave CPs and GRZ a platform for dealing with highly controversial issues. In this regard, the dialogue mechanisms indeed were fruitful in preventing the implosion of harmonization and alignment attempts during times of crisis; they at least partly provided institutional and organizational backing for the intervention logic of budget support. This often implicit value of the dialogue structure should not be underestimated despite all deficiencies of the dialogue process itself; these will be described in the following paragraphs.

Box 4: The 2009 corruption scandal in the health sector

The dialogue mechanisms and their effectiveness have been put to the test by the recent corruption and theft scandal in the MoH involving the disappearance of more than K27 billion in 2008-2009 and estimated at more than K64 billion since 2006. The actual figures are yet to be established, and the case is currently before the courts of law. Many donors, including the most important in the health sector - the Netherlands, Sweden, the GAVI Alliance, and the Global Fund to Fight AIDS, Tuberculosis and Malaria – immediately made a decision to suspend and/or delay aid disbursements. Aid flows to the Ministry of Health at one time dried up completely.

Consequently, Sweden and the Netherlands suspended funding. Resumption of disbursements was made dependent on an action plan, including recovery and repayment of misappropriated funds, prosecution of the officials involved, and preventive measures. Sweden and the Netherlands proposed a joint Swedish-Dutch (Sida/DGIS) position on the conditions to be met by GRZ before a resumption of gradual release of committed funds for the MoH could be considered. The route proposed for both embassies was as follows:

- To adopt an action plan as the basis for lifting the suspension of disbursements to the MoH.
- To make a first tranche available if and when all benchmarks of the immediate actions of the Action Plan have been met and verified, based on a revised and prioritised MoH work plan and a liquidity plan for the remainder of this year.

The second and third tranches are to be released upon full completion of the stated benchmarks, taking into account MoH's reporting on implementation of the Action Plan.

- Corrective measures should include the recovery and repayment of misappropriated funds based on the outcome of the Auditor General's Forensic Audit.
- Preventive measures should include additional oversight and safeguards by the Office of the Auditor General, in the form of continuous pre- and post-audits with quarterly reporting. This should be complemented by the immediate strengthening of key departments such as procurement, accounts, and internal auditing.
- Structural measures should include strengthening MoH's financial management capacity, e.g. the revival of the Audit Committee, the annual external performance audits, and the institutionalisation of core values of integrity and good management practices within the MoH.

Source: de Kemp / Faust / Leiderer (2010); Saasa (2010a)

On the other hand, however, the dialogue process has been plagued with deficiencies that mainly relate to the persisting fragmentation on both sides of the dialogue process. Setting up complex dialogue structures with important functions for an ambitious aid instrument such as BS requires both the capacity and the political will to manage these dialogue structures in an effective and efficient manner. While rhetorically CPs and GRZ have continuously expressed their intention to do so, the *de facto* capacity on both sides has been limited.

On the side of the GRZ, overall ownership of the dialogue process, as is revealed by almost all interviews and previous assessments on this topic, is still weak, and the level of fragmentation on the side of GRZ has made it difficult to provide strong incentives for the CPs' alignment. While the MoFNP has relatively strong ownership of the overall PRBS dialogue, ownership of other agencies of GRZ has been rather weak, as has been the participation of civil society, sub-national entities, and parliamentarians.

- The MoFNP has emerged as the actor within GRZ with the strongest ownership for the dialogue process. The reason for this is related to the preference structure of the MoFNP: the MoFNP perceives the policy dialogue as a means of strengthening its coordinative function within the government and reducing transaction costs vis-à-vis a situation in which it must individually negotiate with a diverse set of actors both within the

government itself and within the community of CPs. At the same time, however, the capacity and political strength of the ministry for carrying out its coordinating functions within the dialogue process has been limited (MoFNP 2007, 6), and other components of BS or traditional aid have not been sufficiently effective to alter this situation substantially (Box 5 shows the findings of the recent JASZ evaluation on this issue). In addition to its relatively limited political strength, MoFNP's coordinating capacity has also been constrained in the past by its own organisational structure: Until the end of 2009, the MoFNP's Economic and Technical Cooperation (ETC) Unit, which has primary responsibility for engaging and coordinating with CPs, had been exclusively organised according to donor desks (with some also having a particular sector responsibility). This setup evidently did not facilitate coordination and issue-oriented engagement with the CPs as a group. In particular, there is no well-equipped PRBS secretariat or similar entity that could effectively prepare, structure, and follow-up on the policy dialogue. Beginning in 2010, a desk officer has been assigned to each sector and line ministry to facilitate easier dialogue/communication between CPs and the government. At the time of writing, it was unclear whether this had led to significant strengthening of MoFNP's coordinating capacity.

- With regard to other agencies of the central government, the ownership of the existing dialogue structures has been heterogeneous, and the collaboration between MoFNP and sector ministries has been weak in the dialogue process. The participation of sector ministries in the core dialogue mechanisms of BS has been uneven at best.
- Beyond a lack of capacity by several ministries to fulfil their role in the complex dialogue structure, political interests acted as a stumbling block. From the sector ministry perspective, accepting the dialogue structure and the underlying intervention logic of BS would also have meant acceptance of the finance ministry as the core state agency in regulating the distribution of external and domestic funds – with serious implications for the existing formal and informal distribution mechanisms that increased the political weight of the leadership of these ministries. Accordingly, sector ministries aligning to the logic of BS would have had to give up their privileged position in negotiating and receiving resources directly from CPs. As a result, the sector ministries had an understandable motive for not seriously

trying to overcome the collective action problems of organizational fragmentation with GRZ. Not surprisingly, the ministries most willing to integrate themselves at least rhetorically into the dialogue process were those which were projected to profit over-proportionally from budget support in relative terms, namely Education and Health.

- This inability of the incentive structure to overcome deeply rooted collective action problems within GRZ has resulted in a weak division of labour across the SAGs and between the SAGs and the PRBS group. There is a consensus among observers that dialogue at the sector level has not been working well. The SAGs have not been significantly involved in reviewing sector outcomes and performance. Contributions from the SAGs for the preparation of the annual reviews have been limited. Many SAGs have met very infrequently and usually in the context of planning and reviewing donor-funded sector programme operations rather than as part of the MTEF/Budget process (Gerster / Chikwekwe 2007, 13). Consequently, many technical issues related to the assessment of sector performance could not be clarified prior to the PRBS review. As a result, the SAGs as well as the annual joint SAG conference have not functioned properly in building a link between specific sector issues and the core mechanisms of the BS dialogue.
- These weaknesses of the SAGs have had implications for the government's ability to steer the dialogue processes. Weakly coordinated SAGs, unable to properly contribute to the annual reviews, have reduced the government's capacity for taking the lead in setting new sector targets for the Performance Assessment Framework. In principle, the processes are organized and chaired by GRZ with CPs taking a rather supporting position. In real terms, however, the frequency of setting the agenda and determining its contents is primarily influenced by CPs.³⁸
- These weaknesses of the SAGs have provided an incentive for CPs to direct the strategic dialogue fora of PRBS to specific sectors issues, thus often overloading the core BS dialogue mechanisms. In

38 For instance, each individual PRBS-CP is technically authorized to call for a HLPD in the case of a perceived non-compliance of GRZ with one of the underlying principles.

the period under consideration, policy dialogue has frequently served the purpose of resolving technical problems which hinder the CPs in making disbursement decisions. Political issues, including the topics covered by the Underlying Principles, often have not been subject to open, regular discussions within the framework of the policy dialogue structure. Although the institutional setting is given – the JSC was set up in 2005 in order to meet on political issues at least quarterly – there has only been a low level of continuity in the dialogue on such cross cutting aspects. Instead, politically sensitive topics have been dealt with in an ad-hoc manner.

Box 5: JASZ evaluation findings on MoFNP coordinating capacity

One critical aspect revealed by the present evaluation is the evident weakness of the government system in guiding aid coordination and alignment functions - a state of affairs which has had serious adverse effects on the ability of the JASZ to achieve its objectives. The challenges are both structural/organizational and systemic. At the structural level, the government has failed to put in place and/or support an effective system within which external support could be received and utilised effectively. Perhaps the greatest weakness is revealed by the institutional and organizational weaknesses of the current structures that have been set up to discharge this responsibility. Firstly, the ETC of MoFPD is supposed to be the main entry point of CPs to the Ministry. In contrast, the ETC organization is far removed from the emerging aid architecture that calls for a more harmonized and coordinated system in which the government is expected to assume a more proactive leadership role. In fact, the ETC was recently down-graded from a department with a Director to a section that reports to a multi-tasking department. This has resulted in a reduction of the ETC's authority for carrying out an effective dialogue with CPs without the need to refer issues to higher authorities. A number of donors have realised this frailty and tend to circumvent it by dealing with officials at levels higher than that of the ETC.

Source: OPM (2010, 27f.)

- Beyond the level of central government, the participation of parliament, subnational entities, and civil society in the BS mechanisms has also been uneven or even absent. Another weakness in the design of policy dialogue in Zambia is the low level of third party integration into the process. Civil society organisations (CSOs), parliamentarians, and private actors are not participating in the SAGs on a regular basis. As regards the PRBS review, representation of CSOs and parliamentarians has been weak. Even though

a broad participation of parliamentarians, representatives of sub-national entities and civil society organizations can easily overburden the dialogue process and create a tension between inclusiveness and efficiency, this has not been the case in Zambia. Despite substantial contributions based on their increasing work in budget support-related issues and their willingness to participate in the dialogue processes more intensely, CSOs attendance at the PRBS reviews has been scarce (Gerster / Chikwekwe 2007, 27f.). One major reason for this may well be the circumstance of late invitation by GRZ/CPs to the review sessions as well as poor information-sharing between the PRBS group and Civil Society actors in the context of the PRBS review (CSPR 2008, 32). Sub-national actors have mostly been absent from the dialogue process, reflecting the overall (political) weakness of sub-national entities and/or their coordinating mechanisms such as the Local Government Association of Zambia. Similarly, participation of members of parliament in the dialogue process has been modest at best.

On the side of CPs, there have been regular attempts to strengthen the dialogue process; however, persistent fragmentation among CPs has created challenges to harmonization, alignment, and mutual accountability.

- Most importantly, PRBS in Zambia is perceived as an important, yet “merely complementary” mode of aid delivery by most CPs. As can be seen from the relative weight of BS (Section 4.1.1), it is still far from being the dominant mode of aid delivery. This has created a situation in which CPs must not only coordinate the complex and bureaucratically demanding BS instrument but must also individually ensure that their traditional project- or sector-interests are compatible with BS – or vice versa. This situation of managing two different worlds of development aid delivery – one aiming at harmonization and alignment, the other at individual visibility and project success – has increased the transaction costs of dialogue extensively. Moreover, the contradicting purposes of these two different approaches to aid has been characteristic for almost all CPs involved in PRBS and therefore has come at the expense of transparency and mutual accountability of the dialogue process. For GRZ it has been almost impossible to determine what kind of incentives are behind the dialogue strategies of many CPs – incentives for providing aid in a harmonized and aligned manner, or incentives related to individual visibility and the maintenance of aid projects outside the official budget structure.

- Another reason, why the transaction costs of the dialogue process are perceived as increasingly burdensome by many CPs is the absence of joint knowledge management of the PRBS process. In this regard, CPs have failed to compensate for the weakness of the MFNP in building an effective controlling and knowledge management system. Even if progress has been made, the problem is illustrated by the fact that even such simple issues as keeping a consistent data base of actual BS disbursements has proven to be a real challenge (see Section 3.1). While joint analytical work and monitoring has been improving, the bulk of this work is still done individually, with no institutionalized memory mechanism in place. This lack of a joint knowledge management system negatively affects the dialogue process because of two structural challenges of joint aid management, which have become even more relevant: first, the high level of fluctuation among aid managers within aid agencies tends to have a negative effect on the continuity and long-term perspective of the process; second, the heterogeneity of analytical capacities among different CPs tends to reduce the technical quality of the dialogue and to obstruct the *de facto* division of labour among CPs.

These deficiencies on the donor side have made it difficult to compensate for weaknesses on the part of GRZ. Moreover, these deficiencies have contributed to a certain volatility within the process; this is typical of management structures beset by weaknesses with regard to delegation and the division of labour.

Despite the fact that all stakeholders in the dialogue process knew about the structural challenges described above, they have spent most of their resources on specific technical issues. Thus, partly because of the malfunctioning linkage between the SAGs and the more strategic dialogue fora, the dialogue process has not yet developed the potential needed for it to be an effective instrument for the discussion of strategic challenges at the political level. For instance, the annual reviews mainly discuss the targets and indicators of the PAF, resulting in a policy dialogue that is dominated by operational issues at the cost of a real political dialogue and a focus on systemic and strategic issues such as governance, PFM, or decentralization. In times of open crisis, however, CPs have tended to change their positions focusing on core political issues and showing a tendency to band together in response to conflictive issues. The policy dialogue after the scandal in the health sector described in Box 4 illustrates this point.

On the one hand, the 2009 crisis led at least temporarily to a more strategic approach of CPs towards GRZ. After the misappropriation of funds in the health sector, the PRBS group was able to respond almost uniformly signalling its unease about the corruption cases and the overall slow pace of reforms (see Box 4). By temporarily suspending PRBS disbursement and basket funding to the health sector and by jointly initiating a HLPD on the Underlying Principles as stipulated in the PRBS MoU, CPs were able to bring long-overdue reforms back to the discussion table. In the same vein (though arguably easier due to the smaller number of donors involved), cooperating partners dealt with the recent problem in the roads sector. In response to high unit rates for contractors and over-commitments of ZMK 1 trillion in 2008, cooperating partners suspended disbursements and requested an audit by the Auditor General to look into the sector's financial, technical and procurement behaviour (Terberger et al. 2010, 13). In his report, the Auditor General pointed to severe procurement deficits, linked to weak supervision by the Road Development Agency. Cooperating Partners suspended disbursements of ongoing funding and negotiated a common Remedial Action Plan with GRZ that focused on the implementation of corrective measures to address the audit findings and guaranteed that similar shortcomings would not be repeated.

This kind of dialogue during testing times between GRZ and cooperating partners had a warning effect and some of the recent reform steps – such as the approval of the Decentralization Implementation Plan and, to a lesser degree, the Reform of the Budgetary Cycle – can be at least partly attributed to the recent dialogue process. Another example is the approval of the public service pay reform by the Cabinet, one day before the PRBS review in November 2009. Therefore, the ability to set up an emergency dialogue and to handle pressing issues in the aftermath of the corruption scandals has shown to a certain extent that the established policy dialogue structures have been capable of providing a valuable platform for dealing with tense situations.

At the same time, however, the 2009 governance crisis clearly revealed weaknesses concerning the effectiveness of current dialogue mechanisms. As such, it also highlighted the need for more efficient dialogue and a better division of labour in order to lift dialogue to a higher (i.e. more political) level and enable the government to take ownership of consultation processes.

Finally, finding a common ground among CPs has not always been easy; this has reflected substantial differences among CPs with regard to the interpretation of the recent scandals in the health and roads sector.³⁹ The more sceptical CPs have argued that those scandals are not acceptable in principle and should prompt a (temporary) suspension of budget support and a demand for full clarification of the issues, together with an increased pressure on GRZ to implement pending structural reforms in key areas. This group of sceptical CPs had the impression that Zambian procedures and agencies involved in dealing with the problems were incapable of resolving the scandals in a proper manner and in accordance with the law; they therefore advocated a more interventionist approach. Other CPs, however, took a more moderate position on these issues. While also demanding full disclosure, they interpreted the scandals as the result of success in strengthening national supervisory bodies, the Office of the Auditor General (OAG) in particular. This group of CPs was at least partly convinced that the course of dealing with the scandals, however slow and stony, was moving in the right direction overall and was driven by improved national procedures and agencies. These different interpretations have led to certain conflicts of interests within the PRBS groups on how to adequately respond to misappropriation of funds in the health and roads sectors. Moreover, these different interpretations have also aggravated differences among CPs about the critical level of ownership of GRZ, which is an Underlying Principle for the provision of PRBS.

4.2.2 Conditionality

As explained in Section 3.2.2, budget support conditionality in Zambia is applied on two levels; the Underlying Principles and the Performance Assessment Framework. However, there are divergences in understanding as regards the use of these two elements of conditionality. The importance given to the UPs varies among CPs. For some, the UPs, i.e. with regard to the general reform process and governance context, are the most important part of a *de facto* conditionality that determines financial contributions. For others, the relative priority of UPs and PAF indicators is reversed. Finally, there is also divergence with regard to relevant indicators within the PAF inasmuch as several donors link their individual disbursements only to a selected number of indicators.

39 Also see Section 4.2.2.1 on diverse interpretations with regard to the Underlying Principles.

It seems that this divergence can at least partly be attributed to the different emphasis put by individual CPs on the different objectives of the budget support programme: while some CPs apparently understand BS primarily as a poverty-reduction-oriented financing instrument, other CPs seem to put more emphasis on using BS as an instrument for promoting public administration and governance reforms.

To establish a clearer picture of whether BS conditionality has been implemented in line with the principles of ownership, alignment, and harmonization outlined in the Paris Declaration, and how this has affected its effectiveness, the subsequent sections assess the two levels of conditionality individually.

4.2.2.1 Underlying Principles

The MoU's relatively open formulation of the role of the UPs as the core conditionality for the BS programme has two main implications, in particular with regard to harmonization.

For one, the MoU's formulation leaves open a wide range of autonomy and flexibility to the individual members of the PRBS-Group in how to use the UPs to determine their disbursement decisions: some CPs link their disbursement exclusively to their overall assessment of government performance and governance dynamics, while others have made the PAF their central reference point for disbursement decisions.

In addition, since the MoU does not identify objective criteria for assessing the UPs, the decision whether the UPs are respected is left to the individual judgement of each CP. This has led to substantial heterogeneity within the PRBS-Group with regard to explicit or implicit criteria and interpretation of whether the UPs are being respected. This interpretational flexibility has impeded harmonization and coordination processes among CPs to a certain extent.

The variety of coping strategies adopted by CPs in the aftermath of the 2009 corruption crisis revealed the heterogeneity of the PRBS group. The different ways in which CPs dealt with the government showed the lack of a coherent strategy in the case non-compliance with the UPs. Even now, CPs have still not developed a harmonized or joint fall-back scenario or a "plan B" for dealing with unsatisfactory adherence to these principles. This has led to a (perceived) lack of results and hindered an effective joint approach in times of crisis. Notwithstanding the success of CPs in setting up a high-

level policy dialogue (HLPD) following the corruption cases in the health sector, this dialogue and the discussions within the PRBS group regarding the scandals also demonstrated the continuing fragility of the harmonised approach. While recent misappropriation scandals have been accompanied by substantial efforts on the part of the CPs to maintain a harmonized approach, these events have also highlighted frictions among CPs in providing PRBS. These different notions of fundamental conditionality have been reflected at times in the difficulties of engaging in the dialogue process with a common position. As one representative of a bilateral aid agency put it straightforwardly: “We have different constituencies, different incentives and do respond to different political masters back home. I get demoted when I overlook a corruption scandal; others get promoted when they meet their disbursement targets.”⁴⁰

This argument is well illustrated by the different reactions of Sweden and the EC in response to the 2009 corruption case in the health sector. The Swedish decision to suspend disbursements was based on the view that the UPs had been violated. In contrast, the EC assessed the fact that the case was brought to the attention of the OAG by members of the administration and followed up as positive signs for the successful functioning of domestic institutions in fighting corruption. Accordingly, in the same year, the EC actually augmented its disbursements through the Vulnerability Flex Support in 2009.

These different reference points with regard to the UPs have caused some conflict between CPs during the dialogue process. For the Zambian government, in turn, these differences make it difficult to anticipate reactions among the donor community as a whole.

4.2.2.2 The Performance Assessment Framework

The PAF represents the focal point of PRBS policy dialogue on GRZ performance and connected conditionality. It also provides a good means for measuring how well these non-financial BS inputs are aligned with government priorities and processes.

The PAF is set forth in a document which explains the relationship of each of its indicators with the FNDFP, the central GRZ strategic framework which the CPs intend to support with their PRBS. Judging from these explana-

40 The implications of the underlying incentive structures on the effectiveness of BS in Zambia are analysed in more detail in Chapter 6.

tions, by and large, the PAF is fairly well aligned with the FNDP. However, the very broad scope of the FNDP means that as a matter of fact it would be rather difficult to find indicators that are not in line in any way with any of the areas identified by the FNDP. In addition, the majority of PAF indicators are rather ‘weakly aligned’ in the sense that they are in line with FNDP priorities but are not included in the list of FNDP Key Performance Indicators (KPIs) and thus require separate monitoring. In fact, among the 41 indicators included in the 2009 PAF, of which 37 formulate targets, a mere 19 are identical to FNDP KPI’s (or arguably do not require separate monitoring processes), albeit in some cases with different targets or in different formulations or aggregations.

This seemingly weak alignment was evidently not due to the FNDP being partly outdated by 2009. Certainly, some of the KPIs, in particular those applied for the agricultural sector, focus merely on government inputs and do not meaningfully reflect GRZ performance. In these cases, it can also be argued that the more appropriate PAF indicators reflect the progress made since the formulation of the FNDP in defining meaningful performance targets, partly as a result of the PRBS-related policy dialogue. However, as was already the case in the 2006 PAF, the share of indicators with a more or less direct equivalent in the FNDP was roughly similar, with 15 out of 34 PAF indicators (and 31 targets) identical to individual KPIs or arguably not requiring separate monitoring processes.⁴¹

This of course does not imply that the remaining PAF indicators were not in alignment with GRZ priorities at all; nor that they required additional monitoring and assessment efforts in all cases: The FNDP itself explicitly provides for the inclusion of process indicators not included in the list of KPIs (GRZ 2006, 376); and a number of PAF indicators are in line with indicators monitored within other frameworks, e.g. those used as part of PRGF monitoring or sector strategies, such as the ROADSIP for the Road Sector.

It can thus be argued that the PAF is sufficiently well aligned to government priorities and monitoring processes,⁴² even if individual indicators have been – at least in part correctly – criticised for being unrealistic or not meas-

41 It is noteworthy that alignment in this sense is best with regard to the indicators for performance in health, education, and HIV/AIDS.

42 Note that this assessment does not contradict the view that CPs tend to sideline established but partly ineffective dialogue structures (such as the SAGs) by inflating the PAF with additional (sector) indicators (see below).

urable. In principle, this should have provided for substantial GRZ ownership of the activities and outcomes underlying the PAF. Nonetheless, judging from overall scores since 2006, GRZ performance as measured by the PAF score has weakened over the years: As Figure 6 shows, PAF scores have diminished continuously, from 70.0 % in 2006 to 58.3 % in 2009.

This weakening performance has led to serious concern among CPs, which have expressed doubts about GRZ's commitment to reform and poverty reduction. Especially after the 2008 review, CPs raised concerns about deteriorating performance and the low PAF score of 65.6. In particular, the weak performance with regard to the delivery of services to rural areas – where GRZ repeatedly missed the PAF-targets in 2007 and 2008⁴³ – has caused dissatisfaction within the PRBS group.

While these concerns must be taken seriously, some caveats are in order against oversimplified comparisons of PAF scores over time as a measure for the improvement or deterioration in GRZ ownership and reform orientation.

First, some of the indicators included in the PAF, as well as the respective targets, change from year to year. In other words, a similar overall score in two different years does not necessarily imply the same degree of effort by GRZ. Nor do differences in the score necessarily mean that GRZ's commitment or efforts changed. The poor results for the health indicators in 2009 were mainly the result of incidental factors that were partly related to the corruption scandal in the sector (see Chapter 9). In 2010, the sector had a much higher score. However, results hardly improved for one indicator (immunization), but the target had been lowered. A third indicator that was not met in 2009 was deleted in 2010. Only the third indicator (on district releases) made real progress. For education, the only indicator that was not fully met in 2009 was deleted in 2010. Moreover, while the PRBS indicators for education had a score of 100 %, several cooperating partners decided not to disburse because of a lack of progress in the sector (see Chapter 9). For the environment, the results improved from 50 % to 100 %, because the (single!) target that was initially set for 2009 was subsequently

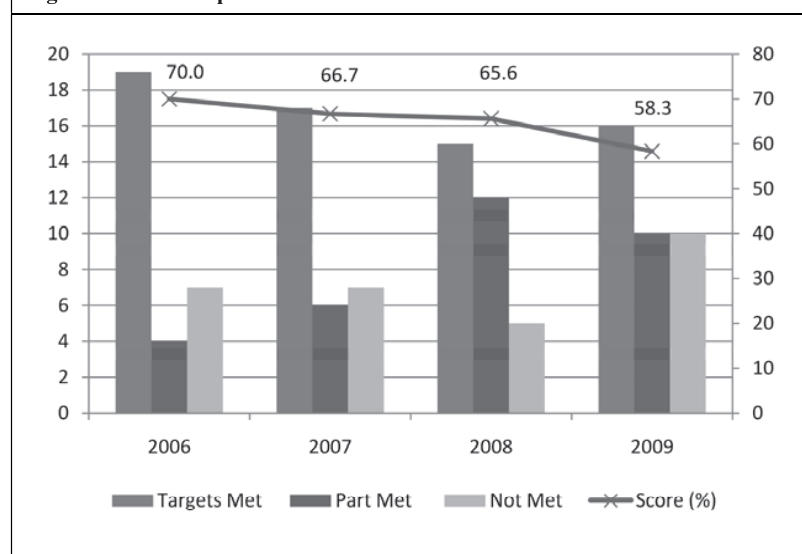
43 In 2007 only 36 % of the rural targets were achieved. Rural performance increased slightly to a score of 40 % in 2008 and improved further in 2009. Despite slight improvements, the low level of performance in rural service delivery is of major concern to the Cooperating Partners (MoFNP 2010, 18).

transferred to 2010 (MoFNP 2011, 38). On the other hand, results for PFM were not as good in 2011 as in 2010. The main reason is the large expenditures on the purchase of the record maize surplus (see Chapter 8). At the same time, results for agriculture improved, mainly because unrealistic indicators (such as those for irrigation) were removed from the PAF.

Second, the examples show that the PAF consists of a heterogeneous set of indicators. Given the dynamics that led to their inclusion, it does not go without saying that if one indicator is equal in weight to another they are necessarily equally important for measuring government commitment.

Third, the assessment of indicators as having been ‘met’, ‘partly met’, or ‘not met’ leaves a great deal open to interpretation. The assessment of an individual indicator in any given year may to an extent depend on the wider policy dialogue agenda and the cooperating partners’ perceptions of issues other than those measured by the indicator.

Figure 6: PAF performance 2006-2009



Columns: Number of indicators (left axis); line: per cent of indicators met (right axis).

Source: MoFNP (2010)

Notwithstanding these caveats, there is some evidence that GRZ's ownership of the PAF has indeed weakened in some respects. In part, this seems to be due to GRZ's perception (as well as some of the cooperating partners) that individual indicators have been imposed rather than negotiated in the past.⁴⁴ In addition, in some instances the inclusion or exclusion of specific indicators seems to have followed a rationale to use the PAF as a tool to control fiduciary risks rather than a GRZ-owned instrument to assess its performance against FNDP-related indicators.

The former perception in particular is linked to the fact that there is no real consensus among cooperating partners, nor between cooperating partners and GRZ as to the appropriate size and substance of the PAF. Clearly, cooperating partners have not managed to harmonize their different expectations under this central PRBS monitoring tool. Despite cooperating partners' awareness of the PAF's shortcomings and their general willingness to move forward in harmonizing their approaches, the prevalence of diverging preferences amongst cooperating partners regarding the focus of the PAF indicators is contentious:

- Some CPs argue that the PAF indicators should focus mainly on core reforms, in particular in the area of PFM, leaving the measurement of progress in specific policy areas to the sector working groups. The idea behind this approach is to increase policy leverage by earmarking the disbursement of funds or the amount of further commitments based on a reduced number of performance indicators.
- Others, however, consider the PAF as an instrument derived from an encompassing development plan and therefore conclude that the PAF should also include sector indicators. This argument gains additional weight when the sector advisory groups perform in an unsatisfactory way, so that the inclusion of sector indicators of the PAF secures CPs' visibility and ensures them of a degree of political leverage regarding sector performance.

44 A characteristic of the PAF target for water supply in rural areas, for instance, is that many of the projects are (directly) funded by cooperating partners and foreign NGOs. GRZ's contribution to the sector is modest. This raises the question what this indicator assesses. Given the relatively limited domestic resources reserved for safe water and sanitation in rural areas, and the slow pace of improvements, GRZ ownership does not seem to be high.

One important reason for this divergence is related to a similar collective action problem on the part of GRZ (see Section 4.2.1) regarding the specific sector interests of many individual CPs. A strong move towards harmonization and alignment in line with the intervention logic of BS would weaken many CPs' special relations with sector ministries and would subordinate their sector interests in the context of a coherent national planning system in which the finance ministry would be the prime player. For this reason, the sector interests of individual CPs and the interests of sector ministries in restricting the coordinating function of the finance ministry come together in an "unholy" alliance against the intervention logic of BS.

Given the weak performance of the SAGs, individual CPs have an incentive to introduce specific indicators into the PAF, thus side-lining the formal structures for sector policy dialogue, with the expectation that this will provide political leverage for achieving their individual sector-related (project) targets. Unfortunately, if all CPs behave in this way, the PAF tends to get overloaded, reflects no clear policy priorities, and leads to a policy dialogue that is more concerned with discussing specific sector issues than tackling the general challenges of reform and stagnation. Thus, one must also assess the weakness of the SAGs and the composition of the PAF from a CP perspective.

Consequently, the PAF as a whole involves a large number of indicators covering a wider range of sectors and government activities than would seem manageable for GRZ to monitor effectively and lead a substantive policy dialogue on.

Presumably even more problematic than the mere number of indicators and targets in the PAF is the incoherent use made by CPs of these indicators in determining the disbursement of their individual PRBS tranches. Table 12 shows the usage of the PAF indicators for disbursement decisions by individual CPs, based on a PRBS inventory compiled by CPs in early 2010. Not only do CPs tend to apply very different approaches in determining their PRBS disbursements (see Section 3.2.2.2) but also, and more importantly, the conditionality linking variable and floating tranches to indicators is very widely spread out across the entire PAF. For example, given that the combined variable tranches in 2007 accounted for only 16 % of total PRBS commitments,⁴⁵ the incentives generated for GRZ to try to meet specific

45 Gerster / Chikwekwe (2007, 17); see Section 3.2.2.2.

indicators cannot be expected to be very strong. What is more, prior to the PRBS inventory exercise conducted in 2010, there was evidently no clear understanding on the GRZ side (or even within the PRBS-Group) of how exactly the individual CPs linked their tranches to the PAF.

On balance, PRBS conditionality is thus not fully in tune with the notions of ownership, alignment and harmonization. The main weakness consists in the insufficient harmonization of the various CPs' approaches. This leads to a weak and inconsistent incentive structure for GRZ on both levels of conditionality (UPs and PAF). Even with recently improved transparency, the overall complexity of disbursement arrangements remains high, and GRZ is confronted with weak and inconsistent incentives from individual CPs that can be expected to lead to confusion rather than to foster ownership and commitment.

The reason for this inconsistent application of conditionality seems to be rooted in the co-existence of different interpretations within the PRBS group concerning the interlinkages and hierarchies of various objectives or functions of PRBS. In particular, there seems to be a fundamental (albeit not explicit) disagreement about whether PRBS should be understood primarily as a funding instrument or as an instrument for promoting governance reforms and good policy making.⁴⁶

4.2.3 Technical assistance and capacity building

In 2008, building on the Joint Assistance Strategy for Zambia, the CP Group developed and signed a Code of Conduct on Capacity Development that aims at improving *“the effectiveness, efficiency and impact of technical assistance from both project support and direct budget support to Zambia”* (CPG 2008, 1).

Budget support-related technical assistance (TA) and capacity building activities in Zambia focus on key capacity constraints that are of utmost relevance for the effectiveness of financial contributions (see Section 3.2.3). In particular, the PEMFA programme and the support to the Office of the Auditor General helped to develop crucial capacities for strengthening the use and control of aid resources which are channelled through the gov-

46 For a more comprehensive elaboration of this interpretation, see Chapter 6.

ernment's budget system. What is more, in line with the principles of the Paris Declaration, the PEMFA programme is using a multi-donor basket funding mechanism managed by a dedicated secretariat within MoFNP, which – in principle – should ensure adequate ownership, alignment, and harmonization of capacity building resources.

Notwithstanding this generally positive assessment of non-financial inputs, budget support-related TA and capacity building in Zambia have been less effective than might have been hoped for given how it is provided.

Among the main factors restricting the effectiveness of BS-related TA is the fact that – despite the joint PEMFA programme framework and the provision through country systems – the principles of ownership, alignment, and harmonization are adhered to only to a limited extent. In particular, various interlocutors stressed with respect to the PEMFA programme that, while representing a comprehensive programme with a large number of components and activities, the main rationale behind launching the programme was that it was conceived by CPs as a pre-requisite for the provision of BS.

As such, the programme is perceived by some as being primarily an avenue for PRBS donors to control fiduciary risks, rather than as a genuine capacity development programme owned and led by GRZ. In particular, while MoFNP as a natural ally for most of the reforms supported by the PEMFA programme may actually exhibit sufficiently strong ownership at the top management level, this is not necessarily true at all lower levels and in all parts of government.⁴⁷

At the same time, some interview partners also argued that the programme design may have been too ambitious in terms of coverage to be effectively managed by MoFNP.⁴⁸

47 To a certain extent, of course, this is not confined to TA in Zambia alone but rather applies to PFM reforms in general, independent of the country context. A case in point seems to be the slow progress on introducing an Integrated Financial Management Information System (IFMIS) in all Ministries, Provinces and Spending Agencies, or MPSAs (see Section 5.2). According to a number of interview partners, there are strong reservations against this reform in parts of the public administration, apparently for fear of becoming obsolete or of losing control over resources as a result of the IFMIS.

48 This view was underscored by a comprehensive evaluation of all components undertaken in 2010. To be fair, it must be stressed that CPs in general seem to share such criticisms and were discussing avenues for improvement in a next phase of joint PFM support to GRZ at the time of writing.

Table 12: Use of the 2008-2010 PAF indicators for PRBS disbursement decisions

Indicator	World Bank	AfDB	European Commission	Sweden	Norway	United Kingdom	Netherlands	Germany	Finland
Incl. DEC 1									
Incl. FPM 1									
Incl. FPM 2	PA								
Incl. FPM 3									
Incl. PFM 1				VAR	VAR				
Incl. PFM 2	PA		VAR-APT	VAR	VAR				
Incl. PFM 3			VAR-APT	VAR	VAR				
Incl. PFM 4			VAR-APT	VAR	VAR				
Incl. PFM 5			VAR-APT	VAR	VAR				
Incl. PPF 1	PA								
Incl. DTR 1				VAR	VAR				
Incl. FSD 1	PA								
Incl. AGR 1				VAR	VAR				
Incl. AGR 2									
Incl. AGR 3	PA								
Incl. INF 1									
Incl. INF 2									
Incl. INF 3				VAR	VAR				
Incl. INF 4									
Incl. INF 5									
Incl. PSD 1		PA							
Incl. PSD 2		PA							
Incl. PSD 3	PA	PA							
Incl. HEA 1				VAR	VAR				
Incl. HEA 2				VAR	VAR				
Incl. HEA 3									

Table 12: Use of the 2008-2010 PAF indicators for PRBS disbursement decisions									
Indicator	World Bank	AfDB	European Commission	Sweden	Norway	United Kingdom	Netherlands	Germany	Finland
Ind. HEA 4				VAR	VAR				
Ind. EDU 1			VAR-MDGT	VAR	VAR				
Ind. EDU 2a									
Ind. EDU 3									
Ind. EDU 4			VAR-MDGT	VAR	VAR				
Ind. HIV 1				VAR	VAR				
Ind. HIV 2									
Ind. HIV 3			VAR-MDGT						
Ind. ENV1									
PA = Prior Action; must be achieved before floating tranche is released.				Fixed tranches: linked to overall satisfactory progress; no specific threshold for PAF score.			Used for disbursement decision of variable tranche; tranche linked to individual indicators or overall PAF score; APT = Annual Performance Tranche, MDGT = MDG-Tranche (three-year basis).		
Source: Information provided by CPs; Note: The list in the PRBS Inventory is not fully consistent with the indicators listed in the 2009 PAF and 2010 PAF Annual Review.									

Added to this comprehensiveness of the PEMFA programme is its insufficient coordination with other TA activities: while PEMFA provided a strong framework for donor coordination and harmonization within the programme and for PFM-dialogue with GRZ, CPs seem to have lost sight of coordination with other TA outside PEMFA (and provided through other aid modalities).⁴⁹

As a consequence, no formalised coordination and information exchange mechanisms with other TA activities have been established. In the case of one GTZ project which provided two advisors in MoFNP (see Section 3.2.3), for instance, this almost certainly meant that potential synergies – not only with the PEMFA programme in particular but with the wider PRBS processes in general – were not tapped. The analytical capacity and knowledge generated in this project almost certainly could have supported PEMFA and PRBS processes in various cases without necessarily compromising the project staff's role as neutral advisors to GRZ.

The root of this problem is that – beyond the above-mentioned Code of Practice on Capacity Development (CPG 2008) that formulates 15 principles on how to provide TA⁵⁰ – there is no coherent and harmonised approach to capacity development in which a formalized coordination and dialogue process could be established.⁵¹ One remedy suggested by some interview partners for this might be to develop a joint GRZ/CP capacity development strategy and establish a formalized dialogue and coordination framework in line with the SAG arrangement in the sectors.

Naturally, such a strategy and dialogue framework would not by itself solve all problems with regard to ownership and alignment of BS-related TA and capacity building. But better coordination and information exchange could

49 At the same time, according to one CP representative, most individual projects (GTZ support to MoFNP, USAID support of the single treasury account reform, support by Norway and Netherlands to the Office of the Auditor General) all benefited from resources going into the PEMFA programme.

50 Linked to this, CPs have reached agreement on the use of harmonized scales for allowances and salaries in CP-funded programmes, although occasionally CPs and GRZ have to be reminded of the agreement. (OPM 2010, 31).

51 The existing CP Capacity Development Working Group, established as an ad-hoc working structure in 2007 (CPG 2007, 1), seems not to have developed into an effective mechanism for ensuring this coordination and joint discussion of TA-related content.

certainly contribute to a better understanding of reform impediments and thus contribute to a better design of reforms and more effective TA in support of these reforms.

4.3 Conclusions on direct outputs

Despite positive developments in the harmonization and alignment of development policies in Zambia during the last decade, non-financial BS inputs to Zambia are still not completely in line with the Paris principles. The analysis of the design of policy dialogue, along with conditionality, technical assistance, and capacity building has shown some deficiencies in the design of the BS programme that hamper the effectiveness of the instrument.

- Alignment of BS processes with the national development plan and policies is widely provided for. As the preferred aid modality BS is consistent with the Zambian aid policy and strategy and the indicators used for the PRBS assessment in light of the PAF's tie-in with the key performance indicators of the FNDP progress assessments. Nevertheless, the share of budget support in total official development assistance (ODA) flows to Zambia is still comparatively low (accounting for 22 % of ODA in 2008).
- With respect to harmonization, the non-financial inputs provided do not meet the requirements set out in the conceptual framework. According to the basic assumptions on the effectiveness of BS, Zambia belongs to a group of countries in which the political and policy dialogue as well as performance assessments and disbursement mechanisms must be mainly coordinated and harmonized by the CPs themselves. CPs in Lusaka, for example, have made progress by setting up structures and coordination mechanisms necessary for a truly harmonized BS approach. CPs have even managed to more or less maintain a harmonized approach in times of crisis. On the other hand, recent events in the health sector and a scandal in the road sector have also shown the limits of harmonization. The variety of pretensions by individual CPs impede the possibility of sending a coherent signal to GRZ, thus weakening the potential of the aid instrument to for creating incentives to strengthen development orientation within the Zambian system.

- With regard to ownership, there are clear signs of differing intensity of CP dominance across the three non-financial inputs. It is clear that there exists an asymmetrical relationship between the donor signatories to the PRBS on the one hand and the government, on the other, with the former clearly being in the stronger position. The asymmetrical relationship in the PRBS MoU has not facilitated clear opportunities that allow the government to be in the driver's seat. In this respect, BS has demonstrably been ineffective in pushing the country ownership agenda. There is no 'reprimand' mechanism in place against defaulting donors under the MoU which currently governs the PRBS. All provisions under the MoU that are related to conditionality elements presuppose that only the government can default and a reprimand for 'wrong-doing' is thus only applicable to the government. This state of affairs has adverse implications for the quality of dialogue under this BS arrangement - a state of affairs that is not in line with the tenets of the Paris Declaration. Existing evidence shows that in certain important aspects the government has been more compliant than the donors (Saasa 2010b, 53).

5 Induced outputs

EQ3: Has BS had an impact on fiscal discipline and macroeconomic management, public finance management, public spending and governance and democratic accountability?

3.1 To what extent has BS contributed to the improvement in fiscal discipline and macroeconomic management?

3.2 To what extent has BS contributed to an improvement of budget management and overall PFM?

3.3 To what extent has BS contributed to the level and composition of public spending?

3.4 To what extent has BS contributed to an improvement of policy processes and policy implementation (including ownership and transparency)?

3.5 To what extent have there been improvements in governance and democratic accountability, particularly regarding the relative roles of parliament and civil society in relation to the budget?

3.6 To what extent has the rule of law improved in the country?

5.1 Macroeconomic management and fiscal discipline

Over the past years, GRZ has performed fairly well with regard to macroeconomic management and fiscal discipline. Although these positive developments are predominantly due to strong economic growth (as a result of the resource boom) and debt relief rather than BS, BS certainly helped to maintain fiscal discipline, in particular during the recent international financial and economic crisis.

According to the most recent IMF assessment, prudent macroeconomic policies and significant structural reforms associated with the HIPC/MDRI debt relief sparked the economic turnaround seen in Zambia in the last decade: external and domestic debt has been brought down to moderate levels, and international reserves have increased significantly (IMF 2010d, 10). Inflation fell significantly from its 2005 levels in 2006 and 2007, but rose sharply during 2008 due to the depreciation of the kwacha in the wake of falling copper prices during the economic crisis.⁵² By end-2009 it had declined to single digits again, and has declined further in the first five months of 2010 despite a 15 % domestic fuel price increase in January 2010 (IMF 2010d, 4). At the time of writing, inflation had been brought down towards the authorities' end-2010 target of 8 %, and the Bank of Zambia is targeting a further reduction in inflation to 7 % by end-2011 (IMF 2010c).

Foreign reserves rose to their highest level in years in 2010 and stood relatively high at US-\$ 1.9 billion by end-2010, the equivalent of about 3.3 months of imports (IMF 2010c; IMF 2010b).

After its most recent mission to Zambia, the IMF commended the Bank of Zambia for having managed monetary policy well with a view to reducing inflation while at the same time maintaining conditions for facilitating economic growth (IMF 2010c). The key macroeconomic policy challenge ahead identified by the IMF assessment is to create fiscal space for spending to enhance economic diversification and reduce Zambia's dependence on copper exports. This will require mobilizing more revenues, including those from mining; containing current spending, including that on the wage bill; and improving overall spending efficiency (IMF 2010d, 16).

52 Copper prices declined 60 % between July 2008 and January 2009, but have recovered since. The nominal exchange rate depreciated 42 % between end-June 2008 and end-March 2009. It has since appreciated by 11 % through June 1, 2010 (IMF 2010d, 4).

With respect to the near-future, the IMF states that *“the 2011 budget is consistent with the maintenance of sound macroeconomic policies. The envisaged revenue enhancement is appropriately ambitious and stems from new tax policy measures, administrative improvements, and payments of tax arrears. The expenditure mix shifts clearly towards capital and social spending, though there is some residual upward pressure on wages despite tight limits on new hiring.”*(IMF 2010c).

All in all, the macro-economic outlook for Zambia looks rather positive, potentially further reducing the role of budget support in ensuring good macroeconomic management and fiscal discipline. In addition, the IMF also projects a reduction in external budget support, arguing that in the future an increased proportion of infrastructure spending (particularly in the electricity and road sectors) will have to and can be financed nonconcessionally, while preserving debt sustainability (IMF 2010c).

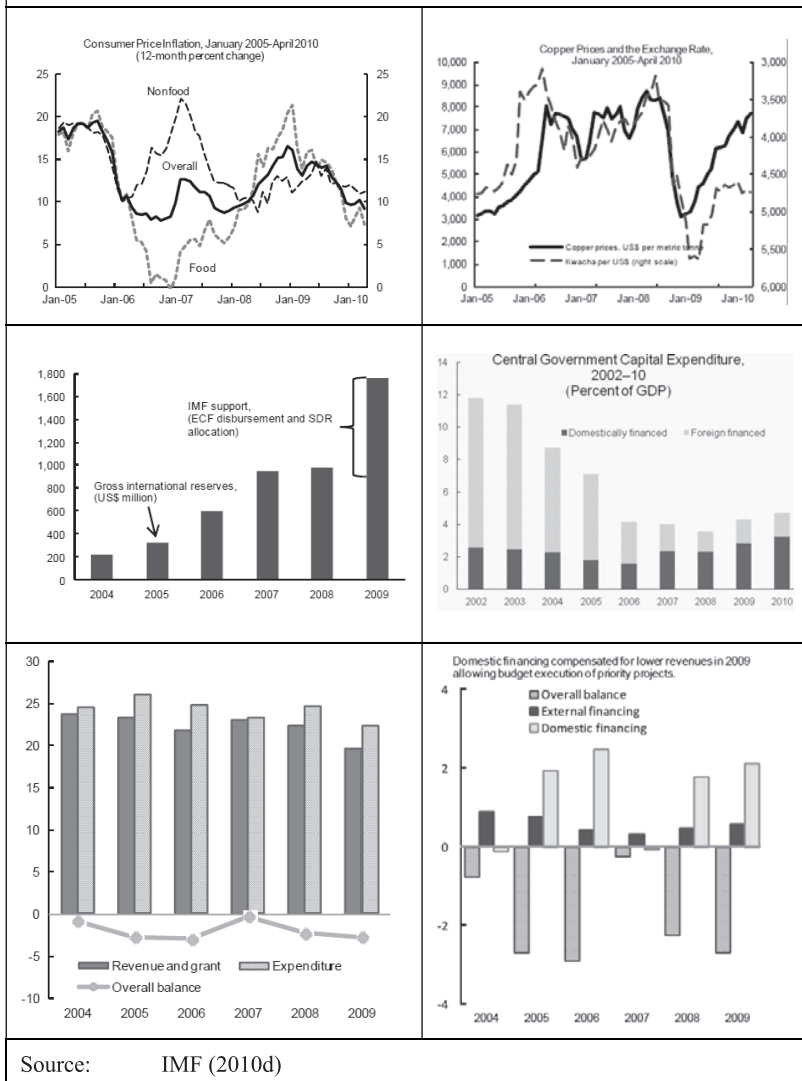
5.2 PRBS and Public Financial Management

Notwithstanding repeated delays in the implementation of reforms and the continued need for further strengthening of the Public Financial Management (PFM) system, PRBS has contributed to substantial improvements in the management of public finances in Zambia. A broad consensus seems to exist among actors on both sides of the aid relation as well as within civil society that these achievements were predominantly due to the general focus of the PRBS dialogue and Underlying Principles; in turn, PFM-related PAF conditionality is generally not perceived as a decisive factor in creating effective incentives for the government to strengthen its PFM.

PFM performance is among the key focus areas of policy dialogue, conditionality, and capacity building within the framework of PRBS in Zambia: for one thing, progress of the PEMFA programme is one of the underlying principles of the PRBS MoU, and PEMFA is supported by most PRBS donors through a joint funding mechanism.⁵³ In addition, PFM indicators are part of the PAF and thus of the annual PRBS performance review.

53 The MoU on external support for PEMFA was signed by UK, the European Commission, the Netherlands, Ireland, Denmark, Norway, Sweden, the World Bank, Finland, Germany, and the UN country team (see Section 3.2.3.1).

Figure 7: Macroeconomic management and fiscal discipline



Source: IMF (2010d)

Some PRBS donors also provide additional project support in the area of PFM, e.g. Germany for MoFNP and Norway for the Office of the Auditor General (see Section 3.2.3.2).

The PAFs for the years 2006 to 2008 included 5 PFM indicators, of which 4 were included in the respective annual performance assessment.⁵⁴ The 2009 PAF initially included 8 PFM indicators, of which 4 were subsequently subsumed under the heading ‘oversight’, leaving 4 “core” PFM indicators for the annual review. Of these 4 oversight indicators, one (“*proportion of audit queries acted upon*”) was only included to provide a baseline for future assessments, while all 4 PFM indicators were included in the 2009 assessment. Table 13 summarizes GRZ performance against these indicators over the years.⁵⁵

	2006	2007	2008	2009 (PFM)	2009 (Oversight)
Achieved	1	4	2	2	2
Partially achieved	1	0	1	0	1
Not achieved	2	0	1	2	0
Score (%)	37.5	100	62.5	50	88.3
Source: Annual PAF progress reports; own compilation					

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- 54 In 2006 expenditure variance was reported but not considered in the performance assessment. In 2007 and 2008 the PFM-1 indicator, which measures the percent of MPSAs whose budget releases are between 95 % and 105 % of their budget allocation, was included in the PAF merely for monitoring purposes and did not form part of the performance assessment. From 2008 on, PFM-1 was limited to non-personal emolument releases only. Together with the planned development for each MPSA of a quarterly expenditure allocation plan (excluding releases for Personal Emoluments and Grants), the stated intention of this limitation was to shift the focus of this indicator from assessing the credibility of the budget to measuring the regularity of releases.
- 55 The deterioration from 2007 (100 %) to 2008 (62.5 %) is due to large unexpected expenditure for the elections (PRBS Group 2009b, 1).

5.2.1 Performance and recent dynamics in Zambia's PFM system

Notwithstanding remaining weaknesses Zambia's PFM performance has improved substantially since 2005. To date, two performance assessments of Zambia's PFM system using the PEFA indicators (PEFA 2005) have been conducted. The first assessment, in 2005 (GRZ 2005a), served as a first-year evaluation of the PEMFA programme and a baseline for future assessments. The second PEFA assessment, conducted in 2008, measured progress against this baseline. It notes significant improvements in various dimensions of PFM (GRZ 2008, ix), in particular an improved basis for strategic budgeting, greater comprehensiveness of fiscal information (including systematic reporting of arrears), improvements in internal audit, and improved oversight through better coverage and an improved methodology for external audits and better public access to the Public Accounts Committee hearings.

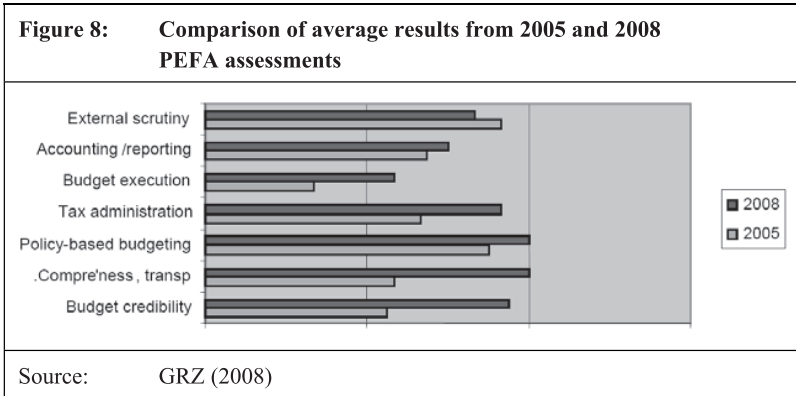
In fact, a comparison of average scores for the various dimensions of PFM indicates improvements on all fronts except on external scrutiny of the budget (Figure 8).⁵⁶ Even there, however, as the 2008 PEFA assessment confirmed, external budget oversight has been strengthened significantly in the past years, too (see Box 6).

The overall positive assessment of GRZ's efforts to strengthen its PFM system is largely shared by the IMF. Box 7 gives the IMF's assessment (in its most recent Article IV consultations) of the most important recent and ongoing PFM reforms:

The biggest impediment to efficient budget performance identified by the 2008 PEFA report was the constitutional provision that the budget had to be presented 90 days after the beginning of the fiscal year. This provision

56 There has been improvement in 2 out of 10 sub-indicators in measuring external scrutiny; no change was recorded for 7 indicators, and only one indicator (timeliness of submission of audit reports to the legislature) saw deterioration from A to B. This, however was not due to later submission of the Office of the Auditor General's (OAG) report to Parliament (early January) but to earlier submission of the Financial Statement by the Office of the Accountant General to the Auditor General, thus widening the gap between the two submissions to more than 4 months. Nevertheless, the OAG has been able to submit its report within 5 and 7 months respectively of its receipt of the Financial Statements for the budget years 2005 and 2006.

resulted in appropriations being approved only in March or April of the same year as the proposed budget, adversely affecting budget implementation performance (Bird 2009, 21). This issue was addressed with a constitutional amendment in September 2009 requiring the National Assembly to pass the budget by the end of December. The resulting new budget calendar was applied for the first time in the preparation of the 2010 national budget.⁵⁷



Another important reform is the implementation of a single treasury account system: according to the Accountant General’s office, GRZ formerly operated some 3000 active government accounts, leading to severe difficulties with cash management and unnecessarily high interest payments. At the time of writing, the number of government accounts had already been reduced to 1700, the ultimate objective being to establish a system with only four accounts for donor funds, salaries, and recurrent and capital expenditure.⁵⁸

57 Notably, this reform at the same time addresses the issue of Presidential warrants, which were necessary to authorize expenditures prior to parliamentary approval of the budget. The problem of substantial supplementary budgets which alter initially approved budget priorities, however, has still not been resolved by this reform (see Section 5.3).

58 According to the same official, one challenge in moving forward with this reform is that only 33 % of Zambians have access to banking services, thus complicating the payment of salaries through a single government account.

Box 6: PEFA 2008 assessment of external budget scrutiny and audit

The efficiency of the Office of the Auditor General (OAG) has improved due to substantially increased staff levels, more systematic training, introduction of new and computer-assisted audit methods, and the adoption and successive application of international auditing standards. The timing of the annual report has met constitutional requirements during the last three years. Through PEMFA, the OAG has also been able to establish five regional offices to facilitate effective auditing of provinces and districts.

The reforms of the OAG have continued to be implemented since the last PEFA evaluation in 2005. Training of staff is ongoing on a permanent basis, more professional audit methods, including computer-supported methods, have been introduced and are being implemented. International auditing standards (INTOSAI) are being adopted and implemented through training and supervision. The OAG has also introduced performance audits, although these are still in their early stages. The OAG has increased its staff budget and now has 530 employees (cf. 300 in 2005), of whom 350 are auditors; this has enabled the OAG to extend its coverage.

The OAG's mandate covers all institutions receiving grants from central government; local governments are audited by auditors engaged by the local councils. In terms of coverage, all Ministries, Provinces, and Spending Agencies (MPSAs) are covered annually for an audit certification of financial statements, but the OAG is still not able to cover its complete mandate annually. In terms of expenditures, the audits cover about 75 %; in terms of entities/accounts the coverage is now more than 50 %. However, the OAG is sequencing its audits so that all MPSAs are covered over a period of two to three years. As part of the reforms, the OAG has recently been able to establish its own offices in the remaining 5 provinces, of which 3 are already functioning; this will facilitate better audit coverage of provinces and districts. The 2008 work plans already include 36 districts (out of 74) for audits.

Parliament's involvement in the budget process has improved, although its role is still limited with respect to the whole budget framework. When it comes to *ex post* approval of supplementary budgets, the parliament continues to play a more passive role.

Parliament's oversight operates through PAC for external audit follow-up, and the Estimates Committee has been assigned additional supporting staff through the parliament's Reform Programme. PAC has eliminated the backlog of reports and is delivering its reports to the House within 8 months of receiving the annual report from OAG. While the Executive makes a formal response to the Auditor General's and PAC's recommendations, there is little systematic follow-up of remedial actions taken.

Source: PEFA Assessment (GRZ 2008)

Probably the most important ongoing PFM reform is the roll-out of the Integrated Financial Management Information System (IFMIS) as a key component of the PEMFA programme. However, this reform has experienced serious delays for a number of reasons. Some of these delays are certainly rooted in GRZ's choice of a highly sophisticated system for which implementation capacities, particularly those of the line ministries, are limited. At the same time, ownership for the roll-out at the technical level and in sector ministries seems to be limited, and MoFNP's restricted political weight *vis-à-vis* certain sector ministries (see Section 4.2.1) certainly does not help swift implementation of the reform either.

Zambia's PFM system also continues to exhibit significant weaknesses, even in those areas that are arguably of particular relevance for PRBS effectiveness and the minimisation of fiduciary risks, such as policy-based budgeting, budget variance, and expenditure controls.

With regard to external budget oversight, further improvements are necessary. In particular, even though the effectiveness of the Auditor General's Office has improved significantly (see Box 6), important challenges with regard to follow-up of audit findings remain: as CPs emphasised in their 2009 statement on PAF performance (PRBS Group 2009b), follow-up actions by the government in order to remedy audit findings has not always been satisfactory. In particular, the CPs stated that "GRZ's overall control systems are not robust enough, and imply that PFM systems need further strengthening." At the same time, they find that the Anti-Corruption Commission is functioning well (PRBS Group 2009a, 1).

Box 7: Recent and ongoing PFM reforms

Considerable progress has been made in implementing public financial management reforms. After consultation with stakeholders, the government has altered its budget cycle to ensure parliamentary approval of the budget in advance of the fiscal year. This is expected to improve budget execution and the legislature's participation in the budgeting process. In addition, the government is expected to introduce a planning and budgeting act in 2010 in order to clearly define the budgeting process and key deliverables by the government as part of the budget (structural benchmark for end-June 2010).

The government is in the advanced stages of finalizing its implementation strategy for the establishment of a Treasury Single Account (TSA). A draft strategy was approved in early 2009 and various modalities of implementation

have now been addressed. The implementation will commence with trial runs at the Ministry of Finance and National Planning, followed by a full pilot in early 2010, with other MPSAs being added to the pilot in due course. The full introduction of the Treasury Single Account will be phased in gradually, commencing in 2010, when six MPSAs will adopt the TSA (structural benchmark for end-December 2010), and all MPSAs will be expected to use the TSA subsequently.

Implementation of the integrated Financial Management Information System (IFMIS) will gather significant momentum in 2010, with the first full pilot commencing in January 2010. Comprised of thirteen technology modules, the IFMIS project will create substantial efficiency gains all across government institutions, providing for improved financial information flows and improved accountability and control. The first pilot site will be the Ministry of Finance and National Planning, which will operate all thirteen modules starting in January 2010. Over the course of the year, additional MPSAs will be included, with a full rollout expected by end-2011 (IMF 2010e, 38).

Source: IMF (2010e)

5.2.2 The role of budget support in PFM improvement

As Section 5.2.1 describes, the performance of Zambia's PFM system has improved in virtually all dimensions, even though much still remains to be done. And although some key PFM reforms predate the provision of PRBS,⁵⁹ it can be argued that budget support has at least partially contributed to these improvements.

It appears to be a common perception among PRBS and non-PRBS CPs that this positive influence is neither directly attributable to the PEMFA programme nor to financial incentives directly linked to individual PFM indicators in the PAF. Instead, it seems that the main catalyst for PFM improvements consisted in the general financial incentives of PRBS together with policy dialogue on the UP and the PAF indicators, rather than capacity

59 The adoption of a Medium Term Expenditure Framework (MTEF) and the introduction of Activity Based Budgeting (ABB) with MPSA budgets broken down according to programme and activity levels, were first considered in the late 1990s. ABB was piloted in 2000 and rolled out to all MPSAs by 2004; the MTEF was formally introduced in 2004 (Bird 2009, 10)

building in the PEMFA framework or PFM-specific conditionality attached to the PAF.⁶⁰

In fact, a number of interview partners voiced concerns that one PFM indicator in the PAF could even create perverse incentives with regard to government reporting: according to the Public Finance Act the controlling officer (in this case the Secretary to the Treasury) is entitled to withhold funds if a ministry fails to meet its reporting obligations. The PFM-1 indicator, on the other hand, requires that 70 % of MPSAs'⁶¹ actual releases be within the bandwidth of 95-105 % of budgeted resources.⁶² This, in effect, could undermine one important sanctioning mechanism which enables the MoFNP to hold line ministries accountable for the orderly and timely submission of their financial returns in future.

However, some of the most relevant recent reform steps can be at least partly attributed to the High Level Policy Dialogue initiated in the wake of the 2009 health scandal. In particular the approval (by constitutional amendment) of the new budget calendar in September 2009, one of the measures included in the HLPD 'road map', is being attributed by many to the HLPD.⁶³ Even though most interview partners agree that HLPD most likely merely accelerated this reform, for which there already seems to have been substantial government ownership (and which was planned as part of the wider constitutional review), this reform must be regarded as a signifi-

60 This assessment was confirmed to the evaluation team by various GRZ officials as well as PRBS and non-PRBS CPs. The general perception seems to be that the pronounced interest of CPs in PFM issues, in particular in budget transparency, credibility, execution, and reporting, and the inclusion of these topics in the PRBS policy dialogue, have induced the government to improve performance in at least in some of these areas. There is also some evidence that PRBS policy dialogue and PEMFA resources have positively impacted on the effectiveness of not directly PRBS-linked (off-budget) TA to strengthen PFM capacities.

61 Ministries, Provinces and Spending Agencies. There are currently 40 Ministries and spending agencies, plus 72 local authorities that receive some (albeit very little) central government funding.

62 Note that the relevant indicator PFM-1 was included in the assessment for the first time in 2009 when it was not met (25 % against a target of 40 % of all MPSAs). For the same year, Sweden and Norway had linked the disbursement of their variable budget support tranche to this and other indicators (see Section 3.2.2.2).

63 Other core PFM issues such as progress on the IFMIS implementation were addressed in the HLPD as well.

cant step towards a more effective PFM system. The late approval of budget appropriations in March or April and the compressed budget preparation process, which resulted from the old budget calendar, was identified as the single biggest impediment to efficient budget performance in the 2008 PEFA assessment (GRZ 2008, viii).

Another important development with regard to budget oversight that is attributable to (sector) budget support is the recent audit in the roads sector. After CPs had been informed of substantial over-commitments of more than ZMK 1 trillion by the Road Development Agency (RDA) in April 2009, they proposed that the Auditor General should carry out a fully-fledged audit covering financial, technical and procurement aspects. This audit report was submitted to the foreign donors in a preliminary version at the end of April 2010 and later as an official document (KfW 2010, 12). The findings of this special audit ultimately led to the removal of a number of senior officials at the RDA.

However, there is also evidence that important areas of PFM tend to escape the CPs' focus. In particular, it seems that CPs' bias towards the control of fiduciary risks of PRBS undermines any potential leverage PRBS might have on key areas of PFM: For instance, a comprehensive evaluation of the PEMFA programme conducted in 2010 clearly indicated that weaknesses in the programme's design impacted negatively on ownership and thus on the overall effectiveness of the reform programme. Various interview partners on both sides of the aid relation stated the view that the main reason for these design flaws were rooted in the fact that CPs primarily regarded the PEMFA programme as a precondition for the provision of PRBS and were predominantly interested in the control of fiduciary risks, and less so in designing a comprehensive, sustainable, and government-owned PFM capacity development programme (cf. Section 4.2.3).

In a similar vein, there is little evidence that CPs particularly push for greater budget transparency and participation of Parliament and civil society in the budget process when this does not directly benefit the donors' fiduciary interests.⁶⁴ A case in point is the lack of PRBS conditionality that

64 As one civil society representative put it bluntly: "The donors use the requirement to have civil society participation only when they need it, not otherwise." With regard to strengthening the parliament's capacities to exercise its role in external budget oversight, it seems that due to the political sensitivity of this kind of capacity development donor assistance in this field does not always focus on the most relevant needs (prioritizing, for instance, infrastructure instead of dialogue and training).

would enhance opportunities for civil society to scrutinize the in-year budget performance of the government. That this is another area in need of reform is demonstrated by the poor rating of budget transparency in Zambia in the 2010 Open Budget Index: Out of a possible 100, Zambia scores a dismal 36, meaning that minimal information is provided to the public in its budget documents during the year (IBP 2010).⁶⁵

5.3 Budget support contributions to levels and composition of public spending

Although budget support is becoming more important as a percentage of total aid to Zambia (see Section 4.1.1), its share in total public spending is not very large. Calculations by Whitworth (2010) based on IMF data give an average of 5.4 % between 2005 and 2009, with the highest share of 6.5 % in 2005 (see Table 14).

Given that data collected by the evaluation team suggests that the figures used in Table 14 underreport budget support disbursements (see 3.1), Table 15 shows the results of a similar analysis with data taken from GRZ's financial report and the data on budget support disbursements shown in Table 6 in Section 3.1.

These figures show a higher proportion of budget support funds in government expenditure. Total BS disbursements averaged 6.17 % of expenditure, reaching 9.05 % in 2009. BS grants had an average share of 5.73 %, reaching 7.86 % in 2009; PRBS grants still accounted for only 7.04 % in 2009, averaging 4.83 % between 2003 and 2009.⁶⁶

While the figures for the BS share in public expenditure in Table 14 are thus almost certainly too low, it can be expected that the data given in Table 15, at least to some extent, represent an upper boundary for the true figure: as GRZ officials in the Accountant General's Office stressed, MoFNP's difficulties in obtaining comprehensive and reliable information on direct donor funding to sectors make it seem safe to assume that actual expenditure in a

65 The Ministry of Education is the only Ministry to publish actual disbursements (according to the same civil society representative, this is only due to pressure by one CP, as evidenced by the fact that no other ministry is doing it). Only recently, RDA followed.

66 An important reason for the increase in 2009 consisted in exchange rate effects. The exchange rate in 2009 was on the average 30 % higher than in 2008 (see Table 15).

Table 14: Share of BS in revenue and expenditure 2002-2009 (ZMK billion), IMF data									
	2002	2003	2004	2005	2006	2007	2008	2009	
Total revenue	2 906	3 680	4 740	5 642	6 618	8 522	10 220	10 315	
Budget support	324	229	258	543	423	582	642	879	
Project	1 026	1 195	1 175	1 282	1 374	1 522	1 427	1 911	
Total revenue and grants	4 256	5 104	6 173	7 467	8 415	10 626	12 289	13 105	
Domestic expenditure	3 578	4 508	5 239	6 646	8 049	10 450	12 402	14 065	
Donor-funded capital expenditure	1 508	1 828	1 681	1 702	1 002	760	695	983	
Total expenditure	5 086	6 336	6 920	8 348	9 051	11 210	13 097	15 048	
Domestic expenditure / Total expenditure	70 %	71 %	76 %	80 %	89 %	93 %	95 %	93 %	
Budget support / Total expenditure	6.4 %	3.6 %	3.7 %	6.5 %	4.7 %	5.2 %	4.9 %	5.8 %	
Project support / Total expenditure	20.2 %	18.9 %	17.0 %	15.4 %	15.2 %	13.6 %	10.9 %	12.7 %	

Source: Whitworth (2010); 2009 data provisional; calculations by IOB (authors' exchange rate update for 2009)

Table 15: Share of BS in revenue and expenditure, 2003-2009 (ZMK billion), MoFNP and CP data								
	2003	2004	2005	2006	2007	2008	2009	
Total revenue	5 355	7 674	9 168	7 597	11 081	12 424		
PRBS grants	155	249	298	370	566	613	973	
Total BS grants	155	249	448	473	623	798	1088	
Total BS	155	249	488	505	623	913	1252	
Other grants (grants less BS)		1616	1780	567	1305	1290		
Government expenditure	5 171	5 993	7 267	7 728	9 799	12 349	13 832	
PRBS grants / Expenditure	3.00%	4.15%	4.10%	4.79%	5.78%	4.96%	7.04%	
Total BS grants / Expenditure	3.00%	4.15%	6.16%	6.13%	6.36%	6.47%	7.86%	
PRBS loans and grants / Expenditure	3.00%	4.15%	4.66%	5.20%	5.78%	5.89%	8.23%	
Total BS / Expenditure	3.00%	4.15%	6.71%	6.54%	6.36%	7.39%	9.05%	
Other grants / Expenditure		26.96%	24.50%	7.34%	13.32%	10.44%		
Exchange rate ZMK / US-\$ (WDI)	4733	4778	4463	3603	4002	3745	5046	
Source:	MoFNP financial reports; authors' own collection of BS data; exchange rate: World Development Indicators; other grants are grants reported by MoFNP minus disbursed budget support grants; Authors' calculations							

given year will have been at least as high as stated in the annual financial reports.

The share of all recorded grants in public expenditure fell from 31.12 % in 2003 to 17.84 % in 2008. Given this limited and diminishing role of external funding for Zambia's public expenditure, it is not clear what the appropriate benchmark should be for assessing whether BS has contributed to an adequate level and composition of public spending. One indication, however, is provided by the PRBS Underlying Principles, which require that GRZ demonstrate commitment to the fight against poverty, "including through a pattern of public expenditure consistent with poverty reduction priorities identified in the National Development Plan" (GRZ 2005c).

5.3.1 Budget support performance against fiscal targets

When the Fifth National Development Plan was formulated, the overall funding need for reaching its targets was estimated at ZMK 62,623.22 billion (US-\$ 17.4 billion) for the 2006-2010 period (GRZ 2006, 354). The FNDP fiscal targets include projections of the expected inflow of external aid resources in the form of budget support and projects.⁶⁷

Table 16 compares FNDP (and MTEF) projections with actual budget and project support realizations. As a share of GDP, GBS was expected to average 1.8 % (2.1 % including budget support loans) for the 2006-2010 period (1.6 % for 2006-2009). FNDP projections were based on an assumed annual growth rate of 7 % during the implementation period. Given that actual growth rates in the first four years of the implementation period were considerably lower (2006: 6.2 %, 2007: 6.3 %, 2008: 5.7 %, 2009: 6.3 %)⁶⁸, this implies that budget support as well total aid resources fell significantly short of levels deemed necessary to fund the FNDP.⁶⁹

67 To estimate the resource gap for meeting its objectives, the FNDP identifies two scenarios: a baseline extrapolating actual resource flows from 2005 and projections of revenue and expenditure outlining the financial requirements of the FNDP. One criticism of the FNDP is the lack of a detailed macro-fiscal framework, which has made it difficult to analyse the realism of assumptions and spending proposals *ex ante* (Bird 2009, 9).

68 Sources: Ministry of Finance and National Planning, IMF.

69 In fact, budget support levels remained much closer to the level of the FNDP baseline scenario, which extrapolated current funding levels in 2005. The FNDP also includes projections for budget support loans at 0.3 % of GDP for all years except 2006. The actual figures were 0.08 % (2006), 0 % (2007), 0.21 % (2008), and 0.25 % (2009).

Table 16: Budget support targets and realization as per cent of GDP		2006	2007	2008	2009	2010	Average 2006-2009
FNDP target	Budget Support	0.8 %	1.3 %	2.0 %	2.2 %	2.5 %	1.6 %
	Project Support	3.3 %	3.3 %	3.6 %	3.9 %	4 %	3.5 %
MTEF projection	Budget Support	N/A	1.26 %*	1.21 %*	1.35 %** (1.25 %)*	1.30 %*** 1.23 %*** (1.17 %)*	1.27 %***
	Project Support	N/A	2.42 %*	2.62 %*	3.64 %** 2.30 %*	2.96 %*** 2.27 %*	2.89 %
Outturn	Budget Support	0.94 %	1.23 %	1.11 %	1.48 %	N/A	1.21 %
	Project Support	3.50 %	3.29 %	2.59 %	3.22 %	N/A	3.07 %
Source:		Projections: GRZ (2006); actual projects and GDP Whitworth (2010); actual GBS: same as Table 6; *MTEF 2008-2010, **MTEF 2009-2011, ***MTEF 2010-2012; project figures include SWApS; budget support targets are GBS grants only (authors' calculations).					

Comparison with MTEF projections show that the rolling 3-year planning process provides more realistic (and regularly updated) estimates of external support. The 3-year rolling MTEF planning, which is designed to provide a link between the FNDP and annual budgets, projects much lower budget support receipts averaging 1.28 % of GDP over the 2007-2010 period (adjusted upwards in the course of rolling planning).⁷⁰

Hence, if measured against the government's medium term financial plans, budget support in Zambia provides fairly reliable funding as a contribution for implementing the FNDP. However, when measured against the estimated funding gap in the FNDP, the level of funding provided through budget support falls significantly short of what was deemed necessary to meet the ambitious poverty reduction and development goals formulated in this strategy.

5.3.2 Budget support contribution to levels of public spending

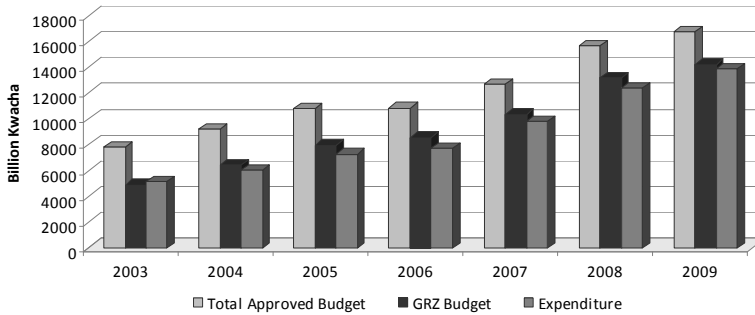
As indicated by Table 14, the share of external support in public expenditure has been decreasing over the past years. This is not due to diminishing amounts of aid but is a consequence of domestic budget allocations having grown substantially faster than external funding. As a consequence, the share of expenditure that is subject to MoFNP's control and processes has increased as well.

Figure 9 shows the development of total and domestic⁷¹ budget allocations and expenditure since 2003. In nominal terms, total budget allocations increased by 113 % or by an annual average of 13.73 % between 2003 and 2009. This vast increase, however, must be weighed against an average annual inflation rate of about 15 % over the same period.⁷²

70 This implies that with regard to GRZ's medium term planning budget support provides a fairly predictable source of funding (more predictable in any case than project support). See Section 4.1.2.

71 GRZ's domestic budget is the portion of the budget financed by domestic resources, including general budget support (grants and loans) and domestic financing.

72 The large discrepancy between total budget and expenditure is explained by the fact that the government's financial reports do not mirror budget presentation. The former exclude expenditure financed by external funds, which are not channelled through the Treasury Account, although these funds are included in the budget proposals (Yellow Book). The result is that an analysis of budget execution (both regular in-year reports and annual financial statements) shows relatively low levels of budget implementation (GRZ 2008, 22).

Figure 9: Budgets and expenditure 2003-2009, current prices

Source: See figure 10

Table 17 shows relative developments in real terms of total approved budgets and domestic budgets (originally approved and including supplementary budgets) as well as GRZ releases and reported expenditure, taking 2003 as the base year.⁷³ For the originally approved budgets, i.e. excluding supplementary budgets approved during the fiscal year, domestic allocations were 52 % higher in 2009 than in 2003, compared to an only 4 % rise in total budget allocations. Including supplementary budgets (and counting them fully as domestic allocations), growth in allocations is 38 % for the GRZ budget against 1 % for total budget allocations from 2003 to 2009. In constant 2008 prices, total budget allocations (including supplementary budgets) thus remained remarkably constant (and evidently unrealistic) from 2003-2005 at about ZMK 15,300 billion. After a real decrease of more than 11 % between 2005 and 2006, budget allocations grew constantly in real terms to ZMK 15 279 billion in 2009 (14 133 billion in 2008 prices). GRZ's domestic budget (including supplementary allocations) has constantly

73 Releases capture only the domestically financed budget, which passes through the Government Consolidated Account, unlike foreign financed expenditures, which are generally disbursed directly to spending agencies. Reported expenditures are primarily domestic. Expenditure above GRZ releases is funded through balance brought forward from previous years; appropriation in aid; or donor funding. Line ministries can only carry unspent funds for capital expenditure into the next fiscal year.

Table 17: Real increases in budgets, releases, and expenditures 2003-2009 (indices)							
	2003	2004	2005	2006	2007	2008	2009
Originally approved budgets							
Total budget	100	101	101	93	98	102	104
GRZ budget	100	119	126	126	138	145	152
Including supplementary estimates							
Total budget	100	98	99	88	92	102	101
GRZ budget	100	111	117	111	120	138	138
Releases	100	98	108	104	117	129	135
Expenditures	100	98	101	95	108	122	127
Shares (including supplementary budgets)							
GRZ budget / Total budget	62 %	70 %	74 %	79 %	81 %	84 %	85 %
Releases / Expenditures	82 %	83 %	88 %	90 %	90 %	87 %	88 %
Releases / GRZ budget	87 %	77 %	80 %	81 %	85 %	82 %	86 %
Expenditure / GRZ budget	106 %	93 %	91 %	90 %	95 %	94 %	97 %
Source: Same data as Figure 10; authors' calculations							

increased year by year since 2003, with the exception of 2006 when, in real terms, domestic allocations fell by 5 %.⁷⁴

Due to the stronger increases in domestic budgets, the share of domestic allocations in total allocations (including supplementary budgets) grew from a mere 62 % in 2003 to 85 % in 2009. Releases as a share of GRZ budget – following a drop from 87 % in 2003 – increased again from 77 % in 2004 to 86 % in 2009. In-year releases as a share of reported expenditure increased from 82 % in 2003 to 90 % in 2006 and 2007 and fell to 88 % again in 2009, meaning that a somewhat larger share of actual expenditure is subject to MoFNP control and cash flow management. With the exception of 2003 (106 %), expenditure was between 90 % and 95 % of domestic allocations until 2008 and even increased to 97 % in 2009.

A key question is, of course, to what extent these increases in domestic budgets and expenditure can be attributed to budget support. Table 18 gives a marginal analysis of the contribution of year-on-year budget support increases (GBS and SBS, grants and loans) to the annual increases of domestic budget allocations and expenditure.

As Table 18 shows, the marginal contribution of budget support to expenditure growth varied substantially over the period 2004–2009. While the additional inflow of budget support resources in 2005 and 2009 contributed around a fifth of the year-on-year change in expenditure from 2004 to 2005 and from 2008 to 2009, the contribution for 2005/6 and 2006/7 was a mere 3.76 and 5.70 %, respectively.

74 The substantial drop in total and domestic allocations from 2005 to 2006 was partly due to the high inflation rate in 2005 of 18.3 %. In current prices, total budget allocations still grew by 0.6 %; the domestic budget in 2006 by 7.7 %. In addition, in 2006 a much smaller supplementary budget of 655 billion (ZMK 810 billion or 216 million US-\$ in 2008 prices) was approved as compared to ZMK 1 000 billion (ZMK 1 406 billion or 375 million US-\$ in 2005). Not accounting for this change in supplementary allocations, the originally approved GRZ budget was even 13.8 % higher in 2006 than in 2005 in current prices. In real terms, however, this made for a marginal increase of 0.34 % of domestic allocations prior to supplementary allocation. Total allocations, excluding supplementary estimates, nominally grew by 4.2 %. Real expenditure also dropped by more than 6 %, while growing by 6 % in nominal terms. However, the reduction was not only an effect of inflation, but also an effect of large nominal reductions in budgets for investment programmes and economic programmes. The budget for loans and investments decreased from ZMK 1.9 trillion in 2004 (US-\$ 820 million in constant prices) to ZMK 1.1 trillion in 2005 (US-\$ 420 million in constant prices). The main reasons were reduced contributions from the budget to (planned) investments in transport improvement, fiscal transparency, tourism and water, which demonstrated important underspending in 2004 and 2005. The overall decrease on the expenditure side of the budget in this period coincided with a substantial drop in external borrowing as well (see Section 5.3.3).

	Marginal budget support contribution to nominal budget growth					
	2004-2005	2005-2006	2006-2007	2007-2008	2008-2009	
Nominal increase domestic budget (billion kwacha)	1494	610	1780	2856	1006	
Nominal annual growth rate domestic budget	23.15%	7.66%	20.8%	27.62%	7.62%	
Nominal increase expenditure (billion kwacha)	1273	461	2071	2550	1483	
Nominal annual growth rate expenditure	21.25%	6.34%	26.80%	26.02%	12.01%	
Year-on-year budget support increase (million US-\$)	57.2	30.91	15.49	88.06	4.42	
Year-on-year percentage change	109.77%	28.29%	11.05%	56.56%	1.81%	
Year-on-year budget support increase (billion kwacha)	239	17	118	290	339	
Year-on-year percentage change	95.94%	3.56%	23.36%	46.51%	37.16%	
Contribution of budget support increase to nominal domestic budget increase (percentage points)	15.99% (3.70)	2.85% (0.22)	6.63% (1.38)	10.15% (2.80)	33.73% (2.57)	
Source:	Same as Figure 10; authors' calculations					

Table 18 also shows quite clearly the important role of exchange rate effects for the contribution of budget support to budget resources available to the government: While the year-on-year change of budget support provisions in 2005/6 in US-\$ translated into a more than 28 % increase, in current kwacha this represented an increase of only 3.56 %. In 2008/9 the US-\$ increase in budget support was a mere 1.81 %, whereas in local currency, this meant that GRZ had more than 37 % more budget support resources available in 2009 than in 2008.

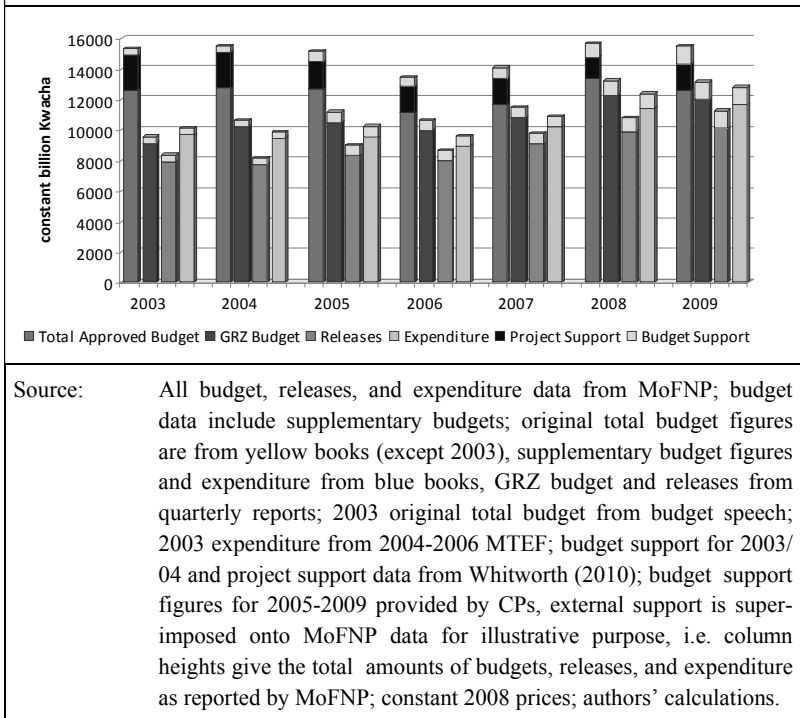
In current prices, year-on-year budget support increases contributed an average of 12.49 % to nominal expenditure growth. Annual budget support increases contributed a mere 12.8 % or 16.7 percentage points to a total nominal expenditure growth of 130.8 % between 2004 and 2009. Budget support between 2006 and 2009 still contributed 12 %, or 10 percentage points to a nominal expenditure growth of 79 %.

In real terms, the contribution of budget support to budget and expenditure increases was slightly more important. Figure 10 shows the same data underlying Table 17 for total approved estimates, domestic allocations, MoFNP releases, and reported expenditures. For illustrative purposes, budget and project support are superimposed onto the columns in order to show the amounts of budgets, releases and expenditure.

The figure shows that while the rise in budget support certainly facilitated the increase in GRZ budgets and expenditure between 2006 and 2009 in real terms, this effect should not be overrated. The contribution of GBS increases to the total budget growth was relatively modest over this period: of the real domestic budget increase between 2006 and 2009 of 24 %, 21 % (or 5 percentage points) may be explained by the increase in budget support. Of the 34 % increase in real expenditure over the same period, 16.5 %, or 5.6 percentage points can be explained by the increase in budget support resources.⁷⁵ The decrease of budget support resources by 8.7 % in real

75 Figure 10 also suggests that estimates of budget allocations have become more realistic since 2006, in particular with regard to estimates of external funding. Despite the introduction of activity-based budgeting in 2000 and its complete rollout by 2004, it appears that until 2005 annual estimates were still mostly carried forward from previous years in the form of incremental budgeting with little significant bearing on actual expenditure. However, the predictability of “on budget” project-based aid continues to be a major problem. According to one internal CP document, a mere 58 % of planned (on budget) donor investments was actually disbursed in 2007.

Figure 10: Budgets, releases, and expenditure 2003-2009, constant prices



terms from 2005 to 2006 meant that the nominal year-on-year increase of 31 million US-\$ was not enough to compensate for the drop in real expenditure in 2006, however.⁷⁶

Nevertheless, despite the relatively small share of budget support in government expenditure and its poor performance against FNDP fiscal targets, there is evidence that the resources provided were decidedly more important for the government's fiscal space than the relatively small budget share

⁷⁶ At the same time, as argued in Section 5.3.3, budget support did not crowd out domestic revenue but rather compensated in part for a drop in external borrowing.

would suggest. This is because domestic revenue barely covers – mostly statutory – recurrent expenditure.⁷⁷

Table 19 gives an estimate of non-discretionary and discretionary expenditure. Spending on wages and salaries, domestic and foreign interest, and arrears repayments amounts to almost half of domestic revenue, and wages alone account for more than a third of total expenditure. Discretionary spending calculated in this way, however, does not necessarily reflect the actual fiscal space of GRZ: combined personal emoluments and recurrent departmental charges accounted for 58.1 % of the budget in 2006. By 2008 this had risen to 70.9 %, leaving little space for developmental expenditure (Ngoma / Sichinga 2010, 11). These figures suggest that for discretionary spending, and in particular capital expenditure, the government still relies heavily (if not exclusively) on loans and grants. In fact, according to an analysis commissioned by the Civil Society for Poverty Reduction (CSPR), almost the entire capital budget is financed from external sources (Ngoma / Sichinga 2010, 9).⁷⁸

5.3.3 Additionality: revenue side fungibility

A key concern regarding the effectiveness and efficiency of budget support has to do with the fungibility of the provided resources, and in particular with the resulting fiduciary risks (see Box 1 in Section 1.2.2).

In view of the substantial increases in domestic revenue over the past decade or so, it seems safe to argue that budget support funding in Zambia is predominantly additional to domestic financing. In other words there is no evidence for substantial crowding out of domestic resources in the sense that the provision of budget support may have led to a reduction in domestic revenue mobilisation. At an average 18 % of government revenue (excluding grants) as per cent of GDP between 2004 and 2008, Zambia's revenue performance was consistently above the average of 16.3 % for the group of low-income countries in Sub-Saharan Africa (IMF 2010a, 75), in

77 Estimates of the share of domestic expenditure reserved in this way naturally vary, but estimates from CPs and sources within MoFNP put the figure at 80 % at the least.

78 Although it is difficult to determine the exact extent of the government's actual fiscal space, this point was confirmed by various CP and GRZ interview partners, including those in the Budget Office. See also Section 5.3.4 on the sector allocation of discretionary budgetary resources.

Table 19: Discretionary and non-discretionary expenditure as a share of total expenditure 2002-2009									
	2002	2003	2004	2005	2006	2007	2008	2009	
Domestic Interest	12.58 %	12.49 %	14.24 %	11.00 %	8.56 %	6.90 %	7.10 %	6.93 %	
Foreign Interest	5.87 %	5.08 %	2.90 %	2.00 %	0.75 %	0.52 %	0.56 %	0.41 %	
Wages	36.36 %	38.33 %	38.40 %	36.94 %	35.20 %	33.79 %	36.00 %	37.50 %	
Arrears Repayments	4.11 %	1.15 %	1.60 %	3.82 %	3.07 %	3.08 %	4.78 %	1.98 %	
Total Non-Discretionary	58.92 %	57.05 %	57.15 %	53.76 %	47.57 %	44.29 %	48.44 %	46.82 %	
Domestic Interest	12.58 %	12.49 %	14.24 %	11.00 %	8.56 %	6.90 %	7.10 %	6.93 %	
Discretionary Balance	41.08 %	42.95 %	42.85 %	46.24 %	52.43 %	55.71 %	51.56 %	53.18 %	
Source: Whitworth (2010)									

contrast to a continued decline during the period 2000-2006, when the tax-to-GDP ratio declined from 19.2 to 17.0 % (ILO 2008, 134). In 2008, revenue (excluding grants) had reached 18.6 % of GDP, which is in line with the target set in the Fifth National Development Plan for reaching a revenue-to-GDP ratio of more than 18 % by 2010.⁷⁹

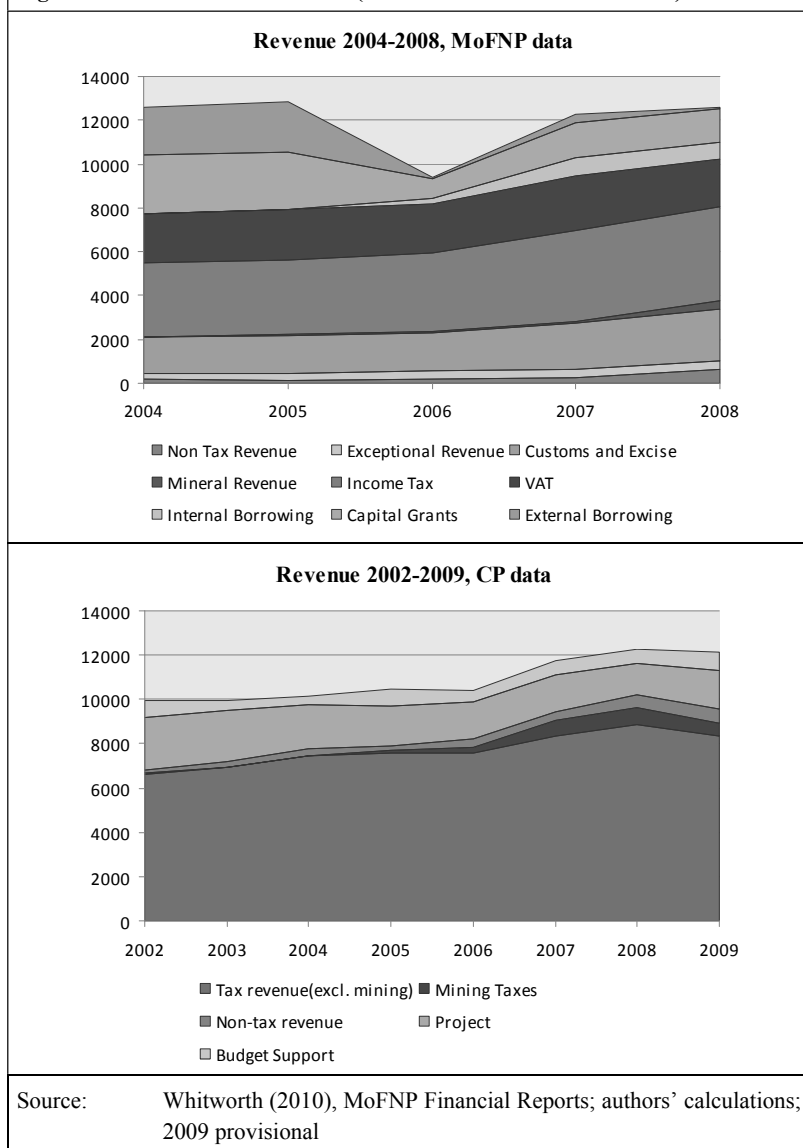
Figure 11 shows the development of revenue according to different data sources. Both data sources confirm that domestic revenue has been increasing in real terms since at least 2002. The main source of government revenue is from domestic taxes, with the largest share coming from PAYE (pay as you earn) income tax, followed by import VAT and customs and excise taxes. Capital grants from co-operating partners are only in fourth place (Ngoma / Sichinga 2010, 9).

According to data provided by the CPs (Whitworth 2010), revenue grew in real terms by 23 % between 2002 and 2008. This was the result of domestic revenue growth of 50 %, whereas budget support and project grants shrank by 35 %. According to MoFNP data, tax revenue grew in real terms by 26 % between 2004 and 2008 alone. Non-tax revenue grew by 254 %, albeit from a very low base of a mere 1.4 % of total revenue in 2004. Capital grants, however, fell by 45 %. According to an IMF analysis, the apparent revenue shortfall in 2009 was mainly due to import-related indirect taxes (IMF 2010d, 6).⁸⁰

79 According to provisional IMF data, the ratio dropped to 15.7 % in 2009, which would be below the FNDP target and below the regional average for low-income countries of 16.3 % in that year. However, the same caveats as mentioned above regarding 2009 revenue and expenditure data apply.

80 This drop was mainly a consequence of the international financial and economic crisis, which had a heavy impact on Zambia's tax revenue. For example, copper prices declined by 60 percent between July 2008 and January 2009, but have recovered since then. The nominal exchange rate depreciated by 42 percent between end-June 2008 and end-March 2009. It has since appreciated by 11 percent through June 1, 2010. (IMF 2010d, 4). However, the data presented for 2009 on the left hand side in Figure 11 are merely provisional and could not be verified on the basis of GRZ data. According to ZRA figures, the initial revenue target for 2009 has been adjusted upwards from ZMK 9 581 billion to 1 019 billion, representing a further rise in domestic revenue of 5.5 % against actual domestic revenue in 2008.

Figure 11: Sources of revenue (in billion constant 2008 kwacha)



Box 8: The Zambia Revenue Authority

In 1991, the new Movement for Multiparty Democracy (MMD) announced an ambitious, donor-backed programme of liberalisation, stabilisation and privatisation. A prominent part of the reform package was the strengthening of the tax administration.

On 1 April 1994, the government launched the Zambia Revenue Authority (ZRA), a semiautonomous agency, and transferred revenue collection from the traditional public administration office, which was under direct control of the Ministry of Finance, to this new entity. This strengthening of Zambia's tax administration was also a donor requirement: at the beginning of the 1990s, the IMF made the strengthening of internal revenue collection one of its conditionalities for the provision of new loans (Hill 2004, 141; Gloppen / Rakner 2002, 32).

The ZRA has also been strongly supported by technical assistance. Up to 2004, the British DFID as the main bilateral donor had provided technical assistance worth £ 15.8 million through its Zambia Revenue Authority project.^a The rationale for this was to finance technical equipment such as computers, to provide expertise through short-term advisors, and to support staff training (Hoover / McPherson 2004, 392; Kasanga 1996, 20). Most important was the provision of a foreign management team for the ZRA. This has been described as follows:

[...] The computerisation of Zambia's tax administration has been one of the focal areas for donor support. In conjunction with training programmes for tax officers, the drive to improve the collection and processing of taxpayer data has largely been successful. Through consistent training, the project has built up technical expertise within the ZRA to use the information technology which has been installed.

One of the ZRA's biggest achievements has been the separation of recruitment of low and middle level staff from Zambia's political environment. A major factor in this was the donor-funded employment of a strong expatriate management team, which found acceptance both within the revenue authority and in the Zambian government.

In February 2002, almost nine years after the creation of the tax agency, the expatriate Commissioner General, the last manager from abroad, left and was at last followed by a Zambian.

[...] Tax officers today belong to the best-paid employees in Zambia and – together with the central bank's staff – form the administrative elite of the country.

^a The scope of DFID intervention has expanded considerably beyond mere support of the ZRA. Since 2000, the DFID has also supported the Tax Policy Unit within Zambia's Ministry of Finance and National Planning and has assisted local NGOs in building knowledge on taxation issues. Therefore the sum was not awarded to the ZRA alone; Sources: quoted from von Soest (2008, 26, 29), von Soest (2006, 17, 18)

Domestic taxes are administered by the Zambia Revenue Authority, or ZRA (see Box 8). According to MoFNP data, the strongest growth among domestic revenue sources in absolute terms between 2004 and 2008 was registered in income tax, which grew by ZMK 909 billion (in constant 2008 prices), or 27 %. The second strongest growing source of revenue is domestic borrowing, which grew from zero in 2004 and 2005 to 823 billion in 2007 and 812 in 2008. Third come Customs and Excise, which grew by ZMK 684 billion, or 40 %. The substantial reduction in external borrowing was partly offset by an increase of internal borrowing to about 6 % of total revenue in 2009.

Box 9: Development agreements in Zambia's mining sector

Zambia's copper and cobalt industry sold minerals with a value of over US-\$ 13 billion and benefited from nearly US-\$ 4 billion of foreign direct investment in the period from 2003 to 2008 [...].

Zambia [...] negotiated a number of "development agreements" when it privatised its copper sector in the late 1990s. This was done at a time of historically low world copper prices, declining copper production and an unsustainable debt burden. The "development agreements" included a reduction in the corporate tax rate from 35 to 25 per cent, exemption from customs duty, the reduction of the mineral royalty from 2.0 to 0.6 per cent, exemption from excise duty on electricity, an increase in the period over which losses could be carried forward and exemption from withholding tax on interest, dividends, royalties and management fees (di John 2008, 44-45). [...] After these agreements had been concluded, the then President, Frederick Chiluba, was found guilty of corruption by the High Court in London in 2007 (BBC 2007).^a The former head of the state-owned Zambia Consolidated Copper Mines and a local businessman were jailed in 2008 for corruption (The Independent 2008). A World Bank report also referred to "grave irregularities" in the sale of the mines (Reuters 2008), and the IMF has advised Zambia to renegotiate these agreements to provide a "quick and substantial boost" (IMF 2008, 16) to the fiscal contributions of the extractive sector.

^a Former President Chiluba was subsequently acquitted in August 2009 of corruption charges after a six-year trial by the Lusaka magistrate's court (The Independent 2008).

Source: quoted from Stürmer (2010, 7, 19); authors' note

In relative terms, the strongest growth was recorded for Mineral Revenue which grew from ZMK 7 billion in 2004 to 75 billion in 2007 and to 364 billion in 2008. This observation is particularly relevant inasmuch as the contribution of the economically important mining sector to the public

budget continues to be a highly contested issue in Zambia (Dymond 2007; Fraser / Lungu 2007). Many actors, especially civil society and donors, argue that this contribution is too small and not in line with the sector's potential to contribute to the public budget (Lungu 2009, 18).

Mining in fact contributes little to government revenues, partly because of favourable tax concessions granted at the time of privatization (IMF (2010d, 12), see Box 9): Copper exports accounted for roughly three quarters of export earnings in 2008 and 2009 (IMF 2010d, 22); according to one estimate, were Zambia to apply an implicit tax rate to the mining sector similar to that of Australia, total tax revenue from the extractive sector could have amounted to 2.5 billion US-\$ between 2003 and 2008, or 37 % of ODA (Stürmer 2010, 9). In fact, however, the entire sector's tax contribution to overall domestic revenue was a mere 3 % in 2004; since that time, this increased steadily to 15 % by 2008.

Nonetheless, as Figure 12 shows, tax revenue from the mining sector has increased substantially since 2000. The sector's main contribution is through PAYE income tax and company tax, which together accounted for two thirds of revenue generated by the sector in 2008 and nearly 80 % in 2009. Company tax picked up from virtually zero until 2005 to ZMK 464 billion in 2008 (2009: ZMK 401 billion).

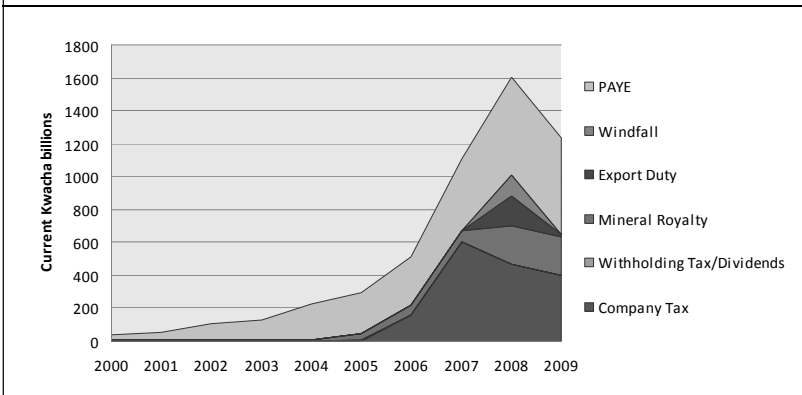
Mineral royalties, which during the nineties were the main contributor to mining revenue, declined from ZMK 29 billion in 1995 (not shown) to merely 4 billion in 2000. Since 2004 (4 billion), revenue from royalties increased significantly to ZMK 235 billion in 2009.⁸¹

In 2008, the GRZ introduced a windfall tax on mining companies' profits that yielded 126 billion kwacha or 7.9 % of sector revenue. However, only three out of eight mining companies actually paid windfall taxes (Ngoma / Sichinga 2010, 6), and revenue fell significantly short of expectations.⁸² Following protests by mining companies and other actors, parliament voted to abolish the windfall tax again in March 2009 in order to compensate for the impact of the international financial and economic crisis.

81 Zambia's copper export earnings climbed sharply in the fourth quarter of 2009. At the time of writing this increase seemed not to have been accounted for in the data reported by ZRA (<http://www.zra.org.zm>).

82 According to a ZRA official, projected revenue from the tax (which was applied in three stages with respective rates of 25 %, 50 %, 75 %) was US-\$ 900 million against a realized US-\$ 350 million.

Figure 12: Mining sector tax revenues 2000-2009



Source: Zambia Revenue Authority

According to ZRA officials, the main obstacle – besides strong political resistance – to taxing profits in the mining sector more effectively in Zambia lies in the complex cost structure of mining operations in Zambia. Zambia’s extractive industry features some of the world’s deepest mines as well as surface mining, leading to presumably very heterogeneous profit margins. In contrast, the capacity of the ZRA to assess mining companies’ claims of profits and losses is very limited.⁸³

Besides taxing mining profits more heavily, the main challenge for domestic revenue mobilisation in Zambia (as in all African LDCs) is to broaden the tax base. According to ZRA officials, income tax is currently paid by a mere 500 000 tax payers in the formal sector. In contrast, the number of people employed in the informal sector grew from a negligible level in 1994 to an estimated 3.5 million today. Capacity and responsiveness of the ZRA, in turn, have not grown to the same extent to effectively capture the informal sector.

A number of proposals have been put forward to improve capture of the informal sector, such as a 3 % presumptive tax charged on business income for small-scale businesses below an annual turnover threshold of ZMK 200 million and a presumptive tax on minibuses and taxis. However, it seems

83 The ZRA is currently establishing a dedicated mining unit with the support of NORAD.

that the ZRA does not yet have sufficient capacities to effectively collect this type of taxes.

As a result, there certainly is scope to increase the tax-to-GDP ratio even further by broadening the tax base and by taxing the mining sector more heavily. However, the political will to do so has been limited (or reversed) in the recent past, and it is questionable whether in the absence of budget support this willingness would change substantially, given the comfortable growth of domestic revenue, positive economic developments in recent years, and the relatively small share of budget support in total revenue.

It therefore must be doubted that in the absence of budget support domestic tax effort would increase substantially in Zambia. In fact, with non-traditional donors, in particular China,⁸⁴ playing an increasingly important role as providers of external funding in Zambia, it can be assumed that the GRZ could relatively easily find sources of funding other than taxes, should PRBS donors decide to reduce or stop providing budget support.

It is important to note that – as the amount of budget support is significantly smaller than the amount of capital expenditures – it can be argued that revenue side fungibility in Zambia is not specific to any particular aid modality. Rather, the degree of fungibility could be expected to be substantially the same were the amounts of aid currently provided in the form of budget support provided in project form instead.

5.3.4 Allocative efficiency: budget and expenditure composition

Another fiduciary risk commonly associated with budget support is related to the fungibility of budget resources on the expenditure side of the budget (see Box 1). Therefore, key questions for the effectiveness of budget support are whether the resources provided are allocated to priority sectors, whether these resources are additional to domestic resources, and whether budget support resources merely crowd out domestically funded allocations in these sectors, thus freeing up resources for other uses.

84 For instance, in March 2010 Zambia was granted a 1 billion US-\$ concessional loan from China for infrastructure and development projects. For a general discussion of Chinese lending to Zambia, see Dahle Huse / Muyakwa (2008).

Budget allocations and expenditure in Zambia, at least with regard to the social sector, are roughly in line with strategic priorities as set out in the Fifth National Development Plan; they can thus be considered fairly pro-poor. Budget support resources – while certainly not decisive for this allocation pattern – can be argued to have facilitated significant increases in social sector spending. There is evidence that in these sectors budget support did not crowd out (but rather crowded in) domestic resources, and that by and large budget support finances the right priorities in Zambia. A continuous concern is the persistently high wage bill, which poses a potential threat to the implementation and continuation of (investments in) poverty reducing programmes.

Figure 13 shows budget allocations and expenditures by government function⁸⁵ in constant 2008 US-\$.⁸⁶ The figures confirm the finding of Section 5.3.2 that total budget allocations have risen since 2006 and, more importantly, that the domestic share of expenditures has also been continuously rising over the past years.

Growth of total and domestic allocations was mainly driven by increased allocations to Economic Affairs (total growth: 33.5 %, domestic growth: 42 %), Education (26 %, 30 %), and Health (22 %, 18 %).⁸⁷ The most significant change between 2006 and 2008, however was the substantial reduction in allocations to General Public Services, which fell by more than 12 % (total budget) and 10 % (domestic), accounting for -41 % and -25 % of the overall growth, respectively.⁸⁸

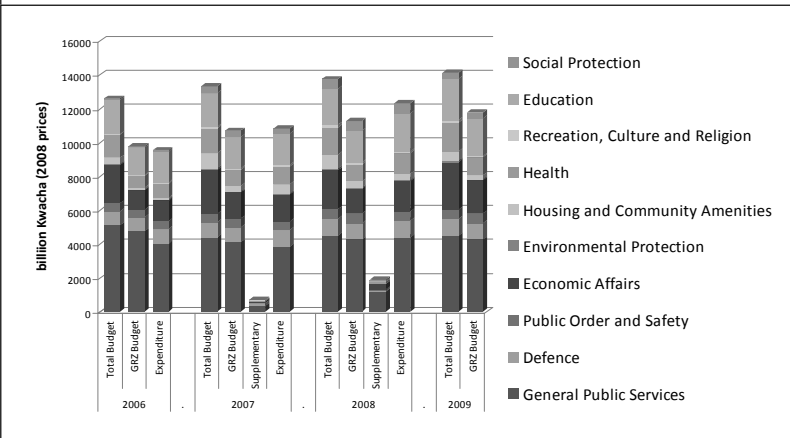
85 The UN classification of functions of government (COFOG) distinguishes ten main functions, divided into groups and classes. The COFOG budget classification was first introduced in Zambia in 2006.

86 Total budget figures as reported in the annual national budget (Yellow Book) include on-budget donor contributions. The GRZ budget is exclusive of on-budget resources but does include ‘through-budget’ resources such as budget support (from 2006 on, educational SWAps are included in the GRZ budget). The annual Accountant General’s report (Blue Book) reports only resources that are managed through-budget. It is important to note that the GRZ regularly puts forward supplementary budgets within the fiscal year, which can account for a quarter of budgeted allocations. However, since supplementary budgets are available in functional classification only for 2007 and 2008, they are not included in Figure 13. This explains why domestic expenditures were higher than domestic budget allocations in 2007 and 2008.

87 Excluding supplementary budgets.

88 Whitworth (2010) gives a good overview of the payment of arrears between 2003 and 2009.

Figure 13: Budgets and expenditure by function 2005-2009



Notes: Only domestic expenditures are reported by functional classification in the Accountant General’s reports. For 2005 only domestic budget and releases are reported by functional classification in the Quarterly Reports and almost certainly are subject to serious reporting errors (see Footnote 90). The financial report for 2009 was not yet available in functional classification at the time of writing; budget figures for 2006 and 2009 are originally approved budgets excluding supplementary budgets, which are only available by functional classification for 2007 and 2008.

Source: Zambia Revenue Authority

Actual expenditure shares given in Table 20 show a somewhat different pattern: economic affairs also accounted for the largest share of total growth between 2006 and 2008,⁸⁹ with more than 20 % of the total increase. The second-largest contributor was social protection, which accounted for almost another fifth of total expenditure growth, followed by health (14.2 %) and education (12.8 %).

89 Unfortunately, the 2009 financial report was not available by functional classification at the time of writing.

Between 2005 and 2006, releases for general public services fell from ZMK 4 693 billion to ZMK 2 724 billion (in current prices), or almost 49 % in real terms. This reduction of expenditures for general public services was largely an effect of the reduction of debt service payments (and other statutory expenditures). In 2006 debt cancellation resulted in a large reduction of the external debt (from ZMK 28 000 billion in 2005 to ZMK 3 500 billion in 2006). This contributed to a decrease of the external debt service from ZMK 470 billion in 2005 to ZMK 227 billion in 2006.⁹⁰

Between 2006 and 2008, however, general public expenditures actually increased again by 8.5 %, contributing 12.4 % to overall expenditure growth over the same period. The share of general public services in total expenditures thus remains relatively high at 37.8 %. The main explanation for this is the payment of arrears, including salaries. A large part of these arrears are accounted for under the subheading of “Financial Management and Accounting”. In 2008, this subheading accounted for almost 8.5 % of government expenditure. Almost 90 % of these expenditures were for arrears, including salaries.

Supplementary budgets, which only require ex post parliamentary approval, could be expected to reflect actual government spending priorities even more clearly than regular budget estimates. Interestingly, supplementary budgets (which are only available by functional classification for 2007 and 2008 and are reported separately in Figure 13) mainly provide additional estimates for general public services (51 %) and (64 %). A closer analysis of actual expenditure, however, indicates that the additional resources from supplementary budgets were actually not used for this category. Instead,

90 Part of the reduction, however, may be due to refinement of reporting by functional classification, as the figures for 2005 in Figure 13 suggest. The information for 2005 is from the Quarterly Reports and not from the audited Accountant General’s financial report. According to this information, general public services, with ZMK 5 575 billion in 2005, accounted for more than 80 % of GRZ allocations and 71.4 % of releases, which seems extraordinarily high, even accounting for high debt service payments. In 2006, domestic allocations in this category fell to ZMK 3 860 billion, or 42.4 % of the domestic budget. It seems likely that to some extent this reflects not only a reduction in debt service and other payments in this category but also the learning curve with regard to budgeting and reporting by functional classification. It cannot be completely ruled out that this effect might play a role in subsequent years as well. The relatively strong growth of the education budget between 2005 and 2006 was caused in turn partly by the inclusion of SWAp budgets (pooled fund) for this sector in the government accounts from 2006 onwards.

Table 20: Expenditure shares and changes 2006-2008; functional classification						
	Share 2006	Share 2007	Share 2008	Average share 2006-2008	Change 2006-2008	Contribution to 2006-2008 total increase
General Public Services	42.4 %	35.5 %	35.6 %	37.8 %	8.5 %	12.4 %
Defence	8.9 %	9.1 %	8.0 %	8.7 %	16.6 %	5.1 %
Public Order and Safety	5.0 %	4.8 %	4.5 %	4.8 %	17.4 %	3.0 %
Economic Affairs	13.0 %	14.5 %	14.6 %	14.0 %	45.8 %	20.4 %
Environmental Protection	0.2 %	0.4 %	0.4 %	0.3 %	156.7 %	1.0 %
Housing and Community Amenities	1.3 %	5.2 %	3.0 %	3.2 %	204.3 %	8.8 %
Health	8.8 %	9.8 %	10.0 %	9.5 %	47.1 %	14.2 %
Recreation, Culture, Religion	0.4 %	0.8 %	0.9 %	0.7 %	175.7 %	2.5 %
Education	19.6 %	16.9 %	18.0 %	18.1 %	19.0 %	12.8 %
Social Protection	0.6 %	3.0 %	4.9 %	2.9 %	933.7 %	19.8 %
Total	100.0 %	100.0 %	100.0 %	100.0 %	29.1 %	100.0 %
Source: MoFNP, authors' calculations						

they helped to fund expenditure above original domestic estimates in housing and community services (189 % over-expenditure), health (81 %) and defence (76 %) in 2007, and economic affairs (35 %), education (35 %) and health (23 %) in 2008.⁹¹

Nevertheless, apart from the persistently large share of general public services in overall expenditures, on the aggregate the GRZ thus made fairly reasonable use of additional resources from a development and poverty reduction perspective. Of the real expenditure growth between 2006 and 2008 of 29.1 %, the largest share was spent on economic affairs (20.4 %), social protection (19.8 %), health (14.2 %) and education (12.8 %). Only 5.1 % of the additional resources were used for defence, and only 3 % for public order and safety.

Whether the overall allocations are in line with the strategic priorities formulated in the FNDP is more difficult to assess. The FNDP's fiscal projections do not follow a COFOG functional budget classification, thus making direct comparison of annual budgets and expenditures with FNDP targets difficult.

The FNDP does, however, identify the areas for priority pro-poor spending, namely health, education, agriculture, HIV and AIDS, rural infrastructure development, rural financing, and small and medium-scale employment promotion (GRZ 2009, 40).

In this respect, it is noteworthy that budget increases in the sectors of health and education cannot be explained with budget support alone but stem over-proportionally from GRZ contributions. In fact, growth in allocations to these sectors has been higher than budget support increases. This is a strong indication that no crowding out of domestic resources by budget support is taking place in these sectors. On the contrary, given the CP's strong focus on these sectors (also with regard to PRBS conditionality, see Section Inputs) one can presume a certain degree of *crowding in* for health and education.⁹² The same is true for allocations to the ministry of local govern-

91 Average variance between domestic budget and expenditure for all 10 functions was 11 % in 2006, 17 % in 2007, and 13 % in 2008.

92 There is evidence, however, that the shift from basket funding to SBS in the health sector by the UK and the EC did in fact lead to a reduction in domestic releases to MoH in 2007. The MoFNP has argued that since the MoH already had sufficient unspent balances available in its own bank accounts, it was ineligible for additional funds during budget execution. From an allocative efficiency perspective, this is a valid argument. DFID gave up its earmarking of health SBS after finding that it did not fit the GBS principles (ODI / Mokoro 2009, 40).

ment and housing and the ministry of works and supply, whose budgets cover the water & sanitation and roads sub-sectors. In the agriculture sector, GRZ contributions grew by 75 % between 2005 and 2009, yet CP contributions grew even more. Relatively large increases were budgeted for agriculture, education and health. For agriculture, the total growth surpasses the growth of the domestic budget.⁹³

For some of these priority sectors, the FNNDP sets aggregate expenditure targets. Figure 14 shows FNNDP targets and actual outlays for selected sectors (as a percentage share of total budget, domestic budget, and domestic expenditures respectively). Figure 14 shows that expenditures overall during the 2006-2009 period were only partly in line with FNNDP sector priorities and fiscal targets for the domestic budget.

It is also noteworthy that performance was best in the social sectors of health and education, where the government controls the most important share of resources. In education, the average deviation of expenditures from the domestic fiscal target is 0.84 percentage points, or an average of 10.29 % of the projected share of the domestic budget. For health, these figures were respectively 2.17 percentage points and 12.08 %. In agriculture and roads, both of which are ostensibly more politicized and, at the same time, receive relatively more support in the form of projects, the variance between projected domestic budget shares and expenditures is greater (21.87 %, 39.20 %) and has increased over the past years.

Figure 14 also illustrates that in the water and sanitation sector, which is predominantly financed through donor projects,⁹⁴ the government exercises little control over whether overall FNNDP spending priorities are realized or not. With a projected share of GRZ spending of just 6.54 % of an overall identified financing need of ZMK 1 208 billion for the sector (GRZ 2006, 357), there is even an average deviation of more than 100 %.

93 This analysis is based on a budget classification by headings and sub-headings as provided by the MoFNP. Due to space limitations allocations by heading are not reported in detail here.

94 The projected average share of water and sanitation in the domestic budget between 2006 and 2010 is a mere 0.2 percent, against an average 8.02 percent of projected donor funding and an average 2.00 percent of projected total expenditures.

Figure 14: FNNDP fiscal targets and domestic expenditure as budget shares

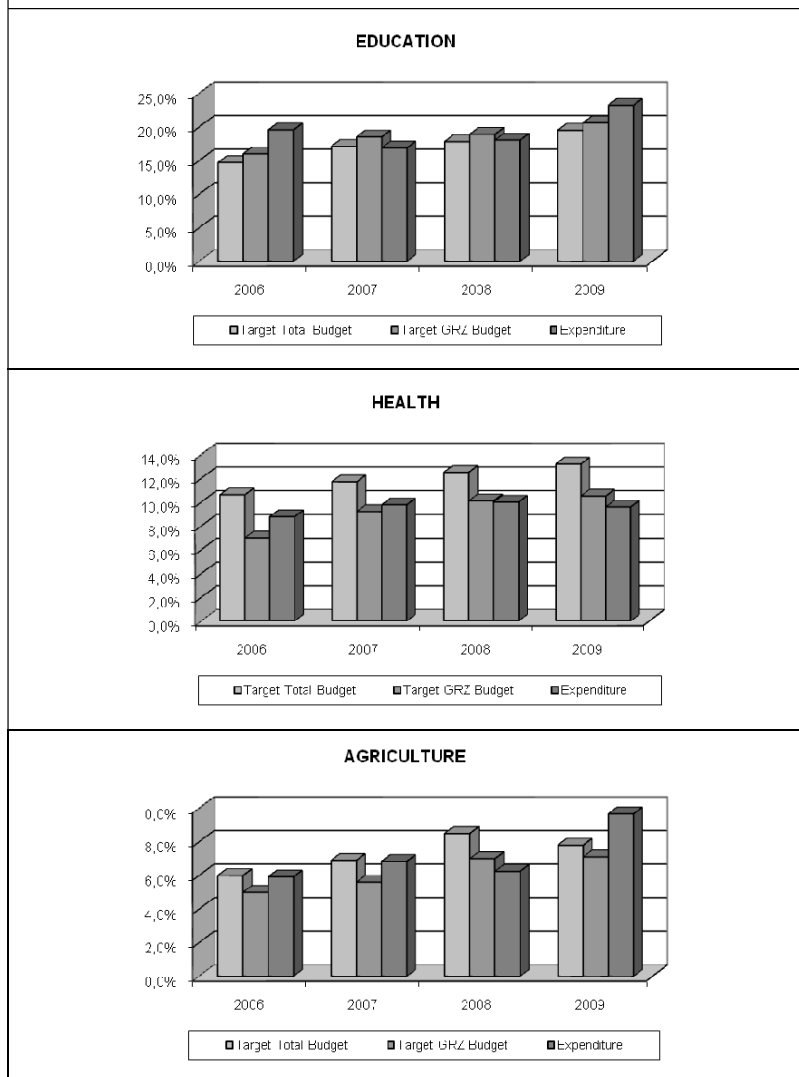
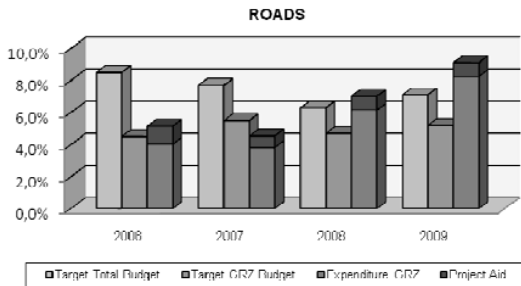
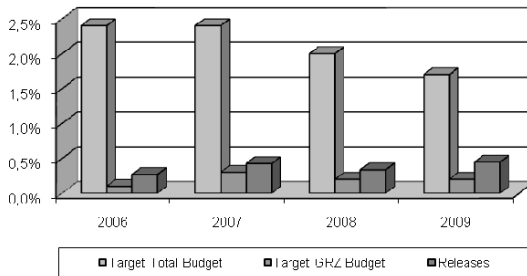


Figure 14: continued



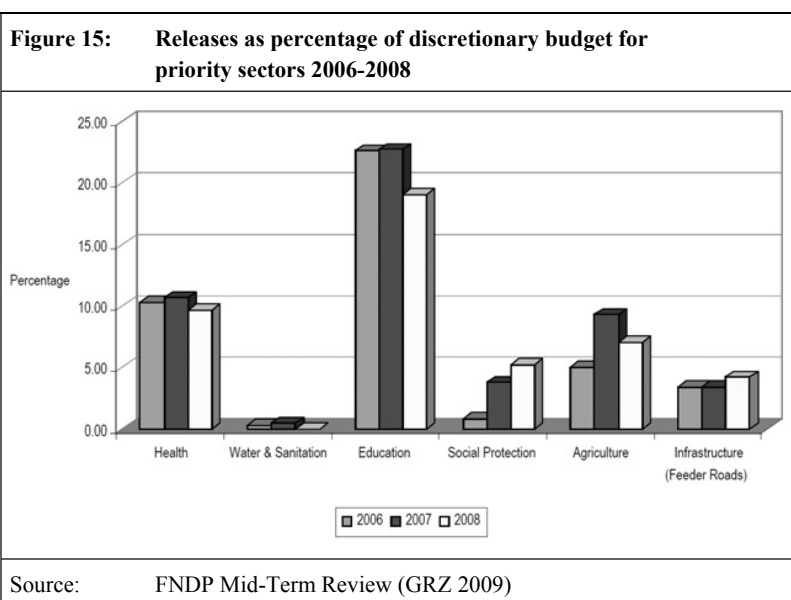
WATER & SANITATION



Notes: No expenditure data by functional classification is available for agriculture and water and sanitation. Agricultural expenditure figures are from the Ministry of Agriculture and Cooperatives budget only (for 2006-2009, releases to MACO account for 99 % of releases for agriculture); Water and sanitation actuals are releases by MoFNP as provided in MoFNP quarterly reports.

Sources: FNDP, MoFNP Quarterly Reports, MoFNP Financial Reports, GRZ (2009), KfW

Unfortunately, the FNDP does not provide more detailed guidance for determining more inter-sectoral and sectoral resource allocation priorities; this would permit a more comprehensive *ex-post* comparison of MPSA's budget allocations with the original plan (Bird 2009, 1). An analysis of the use of discretionary spending conducted for the FNDP mid-term review (GRZ 2009), however, seems to confirm that a considerable share of available resources is spent on priority sectors: of the fiscal leeway in excess of statutory expenditures which is arguably created at least in part by budget support, roughly half is spent on pro-poor priority spending sectors (see Figure 15).



5.3.5 Poverty orientation of the budget

A key question for the effectiveness of budget support in reducing poverty is the poverty orientation of the budget, which in turn is closely related to the amount of fiscal leeway which is available and the balance between recurrent and capital expenditures in the budget.

One potential benefit of budget support is that it enables recipient governments to better balance recurrent and capital expenditures than in the case of project aid, which is usually focused on capital investment, often in an off-budget form. In contrast to many other sub-Saharan African countries, Zambia operates a unified budget planning system with current and capital spending combined within a common set of budget estimates. This reflects international good practices (Bird 2009, 10) and should in principle enable the GRZ to plan for an adequate balance of recurrent and capital expenditures.

Table 21 compares the shares of recurrent and capital expenditures with overall expenditures. It is noteworthy that capital expenditures had already decreased significantly before the introduction of PRBS: from their peak of 11.9 % of GDP in 2001, capital expenditures fell to 8.0 % of GDP in 2006. However, the relative drop was even greater in 2007, when capital expenditures were around 4.3 % of GDP (MoFNP 2008).

The figures in Table 21 show a slightly increasing share of personal emoluments and a substantial increase in other recurrent departmental expenditures. The share of capital expenditures in turn fell from a high of 20 % in 2003 to a mere 9 % in 2008. In principle, this would not need to be an altogether negative development, if under traditional project-based aid recurrent expenditures were neglected in favour of investment projects. Most observers and analysts in Zambia seem to agree, however, that this development poses a threat to the implementation and continuation of investments in poverty-reduction programmes (IMF 2010e, 36) and already has contributed to a general deterioration in the infrastructure (Ngoma / Sichinga 2010, 25; IMF 2010e, 36).

At the same time, the low share of capital expenditure figures is partly due not to actual allocations but to weak implementation capacities (ILO 2008, 134), which until 2009 were also adversely affected by the compressed budget cycle (Bird 2009, 19).

Notwithstanding these developments, poverty-related expenditures have increased as a share of the total budget and as a share of GDP. In particular, this was due to increases in expenditures for health and education, as well as to increased spending on agriculture, from 2 % in 2000 to 7.6 % in 2007.

Below the level of sector allocations, the budget classification system makes it possible to track allocations targeting poverty-related expenditures

Table 21: Expenditures by subheading 2002-2008 (per cent)								
	2002	2003	2004	2005	2006	2007	2008	
Personal emoluments	34	31	33	34	33	36	36	
Recurrent departmental charges	17	15	16	22	25	29	35	
Grants and other payments	14	10	14	13	18	17	18	
PRP (HIPC)	3	3						
Capital expenditures	19	20	12	11	14	10	9	
Constitutional and statutory expenditures	13	21	25	20	10	8	2	
Total	100	100	100	100	100	100	100	
Source: MoFNP (Financial Reports); calculations by IOB								

somewhat more specifically, since the activity-based annual budget (yellow book) identifies poverty reduction programmes, or PRPs (see Table 22).⁹⁵

Table 22: Wages and poverty reducing spending 2005-2009					
In per cent of domestic revenue	2005	2006	2007	2008	2009
Wages and salaries	44	43	42	44	51
Poverty Reducing Expenditures	35	36	47	45	
PRP allocations to budget (%)	42	43	47	47	
In per cent of GDP					
Wages and salaries	7.6	7.2	7.7	8.1	8.1
Poverty Reducing Expenditures	6.1	6.0	8.3	8.3	
PRP allocations (%)		7.2	8.2	8.8	
Source: CSPR (2005); GRZ (2009); IMF (2010e); Ngoma / Sichinga (2010)					

Total allocations to PRPs during the 2005-2009 period averaged 45.78 % of the total budget from all the sectors and provinces. In 2006, a total of ZMK 2 343.7 billion (or 42.57 % of the budget) was released to programmes classified as PRPs. During 2007, a total of ZMK 5 645.7 billion (or 46.9 % of the total budget) was allocated to poverty-reduction programmes while the 2008 PRP budget allocation was ZMK 6 488.8 billion, representing 47 % of the total budget for the year. The bulk of PRP allocations were for capi-

95 This classification has its difficulties however. Until 2006, the classification included a PRP 1, PRP 2, and PRP 3 code, standing for a direct, indirect, and remote impact on the poor. The PRP classification of a number of expenditure items has been criticised by civil society in the past (CSPR 2005) and seems to have changed repeatedly: Traditionally, these expenditures included health, education and social services; since 2007, development programmes in the productive sectors such as agriculture and infrastructure upgrading are also included. These changes in definition had an upward effect of about 7 percentage points on poverty-reducing expenditures as per cent of domestic revenue, and of 1.2 percentage points on poverty-reducing expenditures as per cent of GDP (de Kemp / Faust / Leiderer 2010, 18).

tal programmes, especially for road and other infrastructure development (GRZ 2009, 42).⁹⁶

Overall, the budget thus has become more pro-poor over the past years. According to a review of public expenditure reviews in Zambia, however, infra-sector and sub-sector spending does not necessarily always reflect pro-poor priorities. For instance, in education the review finds a bias towards urban against rural areas; in agriculture, the budget is found to be dominated by input subsidies that reach only about 15 % of the farmers, who are better off anyway (Chiwele 2009). This issue is more closely studied in the various sector reports prepared as part of this evaluation.

5.4 Budget support and the quality of policy processes and governance

Most CPs regard BS not only as an instrument for financing pro-poor policies but also as a means of improving the overall quality of policy processes and strengthening democratic accountability, corruption control, and the rule of law. This is made explicit in the non-financial components of Budget Support, namely in the Underlying Principles, which require an overall positive trend in these areas as a *conditio-sine-qua-non* for the disbursement of financial resources. Since dialogue mechanisms and – at least partly – the contents of the PAF are also related to governance reforms, BS support – due to its potential for harmonizing donor incentives and its combination of financial and non-financial components – is therefore often perceived as bearing a huge potential for effectively promoting democracy and good governance in general. Given these expectations, this section tackles the questions whether and to what extent BS in Zambia has had a positive effect on improving policy processes and the quality of core governance dimensions.

96 According to CP information, pro-poor programmes in the budget are not protected *de jure* against cuts; *de facto*, however, certain other programmes are indeed protected: when donor funding was withheld after the 2009 health sector scandal, health, education and roads Infrastructures were protected from cuts, and money was taken from other sectors to ensure funding for these sectors. In Health, the MoFNP released funds amounting to 25 % over budget in order to protect basic health services.

5.4.1 Democracy and governance in Zambia

As mentioned in the introduction, Zambia again became an electoral democracy in 2006. Accordingly, the political regime is currently characterized by the core element of democracy, i.e. competitive and relatively free and fair elections. As the indicators in Figure 16 show, Zambia is ranked slightly above the Sub-Sahara African average. This also holds for two other governance indicators such as corruption and the rule of law. With regard to corruption, the World Bank Governance Indicators also suggest an improving trend since 2004, which nevertheless has slightly been reversed since 2009.

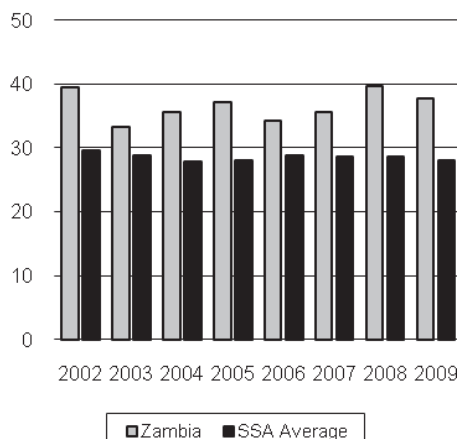
Despite these relatively positive developments, the Zambian democracy is fragile, and overall governance is relatively weak. While there have been competitive elections, other key features of democracy are fragile. There is a strong concentration of power in the hands of the executive *vis-à-vis* the legislative, the judiciary and civil society, all of the latter being relatively weak with regard to their oversight and control functions. Moreover, civil society is relatively weak in terms of being able to bring its core interests to the attention of political decision-makers, and the political parties within parliament have at best only partly fulfilled their function of incorporating societal interests into coherent political programs.

Additionally, the political influence of sub-national units (namely the district councils) is also limited, and the decentralization process has been slow at best. This also hampers the emergence of vertical checks and balances. Most importantly, the constitution does not yet allow for direct elections of mayors or integrate members of parliament into the political decision-making process at the district level. Both factors tend to promote centralist policy-making and act as barriers to the emergence of strong and independent political figures who might act at the district level as counterweights to highly centralized policy-making. Additionally, the process of fiscal decentralization has been slow, and attempts to establish a clear and transparent formula for transferring central resources to the subnational level have often been undermined, giving the central government a great deal of freedom in discretionally allocating resources at the local level.

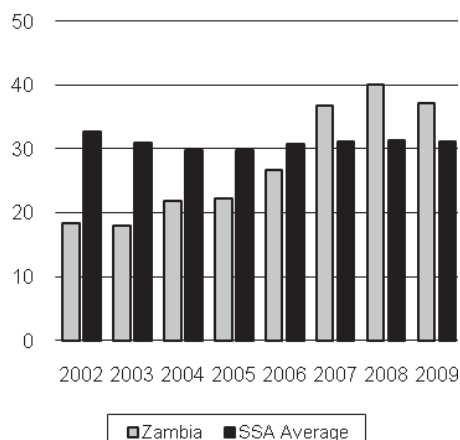
This lack of substantial checks and balances, and the dominant position of the executive, have limited incentives for strengthening democratic accountability and overall political transparency. In combination with the

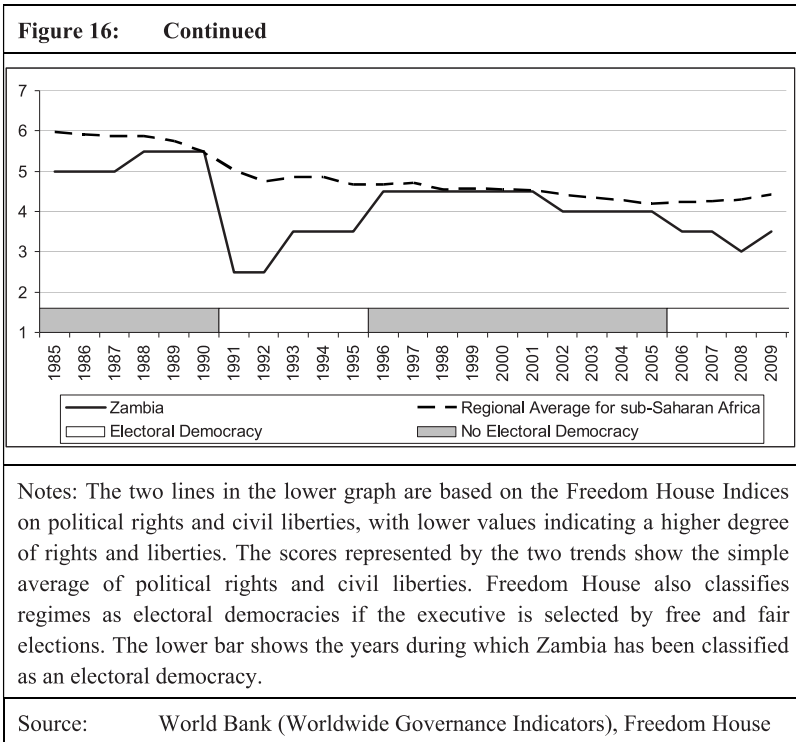
Figure 16: Governance and democracy development in Zambia

Rule of law (percentile rank)



Control of corruption (percentile rank)





historic pattern of one-party dominant regimes organized according to centralist patronage systems, the fragile system of checks and balances has created incentives and opportunities for the ruling party to undermine electoral competitiveness whenever its position is threatened by increasing popularity of the opposition. This explains why the GRZ has only shown limited ownership in advancing core governance reforms since 2009. Instead, in an increasingly politicized environment and with an increasingly popular opposition, several initiatives of the GRZ have been designed to hamper political transparency, to reduce the influence of critical NGOs, and to shield politicians involved in corruption scandals from judicial prosecution. This limited impartiality has also led to controversies between the DAC CPs and the GRZ, with the latter accusing the PRBS group of illegitimate intervention in domestic affairs.

5.4.2 Impact on policy processes and governance

When assessing the effect of BS on the quality of policy processes and governance, one must keep in mind the difficult political environment described in the previous paragraphs. Nevertheless, and with all caution in relation to remaining attribution problems, the existing evidence suggests at least mildly positive effects on policy processes and overall governance quality. However, the potential of the instrument has been constrained by three factors:

- First, while the 2006-2010 period shows an overall upward trend regarding some core governance indicators, the *ownership for improving core governance dimensions* has decreased over the last two years
- Second, *the internal construction of an effective overall incentive system of financial and non-financial BS components* has been limited due to collective action problems within the PRBS group with regard to policy dialogue, conditionality and disbursement procedures.
- Third, one must remember that the overall external incentive structure in which the financial and non-financial components of BS are embedded has limited the leverage of BS as a whole with regard to broader governance reforms. Overall, the dependence on external aid from DAC members has decreased due to the boom in natural resources together with the rising importance of China as an external partner of Zambia.

Despite these problems one may regard BS as one of the few remaining (external) factors that has built up a certain leverage against further deterioration of governance in the last two years. The PRBS group – despite substantial harmonization deficiencies – is still the most coherent external constellation of actors who have partly filled the gaps created by weak domestic power sharing arrangements.

There are two main reasons why BS – despite its weaknesses – has been able to have some effect on governance-related issues in the long run (4 years) and prevent a further deterioration of transparency, accountability and democratic processes in the short run (2 years):

- First, the financial weight of BS for the government is still considerable when measured in terms of “fiscal leeway” for the development-oriented investments required in order to maintain political support.
- Second, BS is politically important for the GRZ *vis-à-vis* its political opponents. Thus the GRZ is willing to make at least some concessions

to the PRBS group because suspending it would give the political opposition an opportunity to further increase its electoral support (which was rising in the period from 2009 to 2010).

As already described, the quality of policy processes, especially those which concern transparent and accountable, public financial management in Zambia, is still low due to serious capacity shortages, coordination problems, and political challenges. Although these processes improved slightly between 2005/6 and 2008, it has been difficult to maintain the momentum of this development since 2009. Nevertheless, at least a partial contribution of BS to some reform processes can be mentioned:

- The reform of the budget calendar approved by the end of 2009 and implemented in 2010 can be partly attributed to the BS High Level Policy Dialogue (HLPD). In the follow-up to the scandal in the health sector, the PRBS CPs put strong emphasis on the issue of reforming the budget calendar, and the subsequent reform by GRZ will most likely improve budget planning and policy implementation. However, the political cost to GRZ of implementing this reform is relatively low.

**Box 10: The 2009 reform of the budget calendar:
one reform, two interpretations**

In the context of the 2009 road map following the scandal in the health sector, the PRBS CPs agreed to jointly demand a reform of the budget calendar which had been pending for several years. Prior to the reform, the annual budget was approved only in March or April of a given year. Thus, in the first three to four months of a year, budget allocations could only be made by direct presidential approval. According to the interpretation of external observers, this procedure even further broadened the executive's discretionary leeway regarding budget allocations. The reform reduced this presidential leeway by forcing the government to hand in its budget draft earlier to the legislative in order to obtain parliamentary approval expeditiously. As a consequence, budget allocations now require majority approval by the parliament for the whole budget calendar and not – as was the case before – only for eight to nine months.

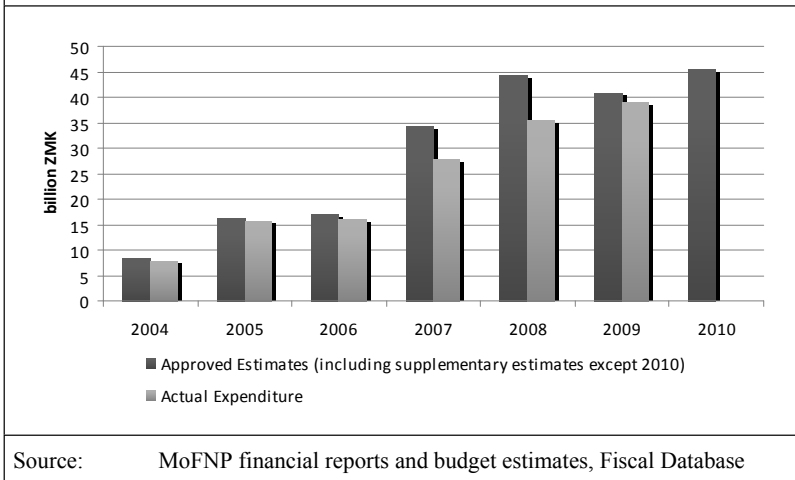
According to administration sources, however, the delay of the reform was mainly related to the fact that the GRZ wanted to put all reforms requiring constitutional amendments into a single constitutional reform package instead of bringing them one by one before the legislative. According to these sources, the 2009 constitutional amendment on reform of the budget calendar was added because of the increasing pressure of the PRBS group. However, the reform itself had little political weight due to the strong overlap between the executive and the legislative arms of the government.

- Support for the decentralization process has also been an area where the PRBS had some, if limited, success. The overall political and fiscal decentralization process in Zambia has been weak, and has stagnated for several years despite some initiatives of GRZ. A constitutional reform necessary for strengthening both the political independence of local governments (direct election of mayors) and the ‘demand-side’ of decentralization seems currently politically unviable. There has also been little success in improving transparency and non-discretionary practices in the fiscal transfer system, mainly because of strong resistance on the part of sector ministries. Despite constant complaints from the PRBS group and other CPs about this slow progress, the Decentralization Implementation Plan (DIP) was not approved by the Cabinet until early 2010. Prior to this event, pressure to pass the DIP through Cabinet increased substantially in the context of both the health scandal and increasing rumours that a further report by the auditor general would reveal similar challenges in the road sector. Thus the BS HLPD was helpful in achieving this reform step, since at least some of the PRBS parties signalled to GRZ that they would consider further delay as an additional political sign of non-compliance with the Underlying Principles. As in the case of the reform of the budget calendar, however, the approval of the DIP by the Cabinet has not yet involved significant political costs because the implementation process has not yet gained strong momentum. Overall, while the 2004 Decentralization Policy and the 2010 Decentralization Implementation Plan are important formal political articulations, the concrete implementation of political, administrative and fiscal decentralization measures has been slow, thus conserving the centralist character of policy-making in Zambia.
- The strengthening of the Auditor General’s external auditing capacity probably has been one of the more substantial achievements of the PRBS. While still faced with serious capacity problems, the Office of the Auditor General (OAG) has been strengthened in recent years in terms of the coverage, quality and timing of its reports. While there remain some problems with issues of independence – for instance, budget independence and the fact that auditor has to deliver her report to the executive (president) before delivering it to the parliament – the de facto independence of the institution has increased. This positive development is also documented by the substantial increase of OAG’s budget, which

almost doubled from 2004 to 2005, and almost tripled since 2005 in current prices (see Figure 17).

In contrast to other political reforms, the major external and domestic players involved – the PRBS group and the finance ministry – had a very concrete interest in strengthening the Auditor General’s office. From the PRBS group’s perspective, the prime concern regarding the fiduciary risks of BS made the office of the Auditor General a crucial target of their governance support, very difficult to neglect from the side of the GRZ. Moreover, the MoFNP, as the ministry with primary responsibility for the PRBS process, has also had an interest in strengthening the role of the Auditor General, inasmuch as the MoFNP perceives this institution as an ally in better controlling other state agencies. In this regard, the role of the Auditor General’s

Figure 17: Budget and expenditure Office of the Auditor General 2004-2010



office in the health and road sector scandal has been crucial and – in principle – has followed the procedures established by the Zambian system. The PRBS group and other DAC CPs have carefully observed these two processes and thus provided a certain “watchdog” function in the process.

- Strengthening the oversight functions of the parliament as a complementary process to promoting the authority of the Auditor General, how-

ever, has been much more difficult. Only limited improvements have taken place with regard to strengthening the oversight and control functions of the parliament. While the – mostly anecdotic – evidence shows a slight increase in the activities of the parliament with regard to its budget oversight activities, most of the structural underlying causes for a weak parliament remain. Given the fact, that almost 40 % of the MPs have positions as ministers or vice ministers in government, the overlap between the executive and the parliament is extremely strong and has negatively affected an independent role of the parliament. Interfering with these – partly constitutionally regulated – affairs has been politically too sensitive for the PRBS group. The fact that improving the parliament's political oversight role would inevitably have come with strengthening the role of the opposition has made this topic even more sensitive. Thus, most CPs have reduced their support to a mainly infra-structural nature and some capacity building instead of tackling the root causes of the legislature's weakness. Thus, the overall imbalance between the executive and the parliament has remained, and the legislative has had limited space to manoeuvre in demanding appropriate political consequences in the context of the corruption/misappropriation cases investigated by the Auditor General (Chiluba case, health case, etc.). Thus, while the strengthening of the Auditor General has increased that independent agency's potential to uncover illegal activities within the executive, the remaining weakness of the parliament has been a serious barrier for holding actors accountable in case of misbehaviour.

- The effectiveness of the PRBS process with regard to increased participation on the part of civil society in the BS process in order to strengthen monitoring capacities has also been limited. All civil society groups involved in poverty reduction and political monitoring are heavily dependent on external resources. Thus the endogenous power of these groups is weak, which in turn has provided the GRZ with an argument for questioning the legitimacy of these groups. Despite this general weakness, the involvement of these groups in monitoring the budget process has increased during the last years. Although this cannot be directly traced to the PRBS process, since most capacity building was not financed through BS related activities, the process has nevertheless provided a legitimizing argument for the activities of civil society with its formal emphasis on civil society participation. Beyond general calls for civil society inclusion, on the other hand, the PRBS group has only

made sporadic attempts to directly promote participation by these groups in the different dialogue mechanisms. As several interviewees of civil society organizations have suggested, PRBS members were sometimes unwilling to push for stronger civil society inclusion because this might have complicated the nature of government-to-government negotiations between PRBS CPs and the GRZ.

Overall, the existing evidence suggests that the PRBS process has had some effects on improving policy processes and the overall quality of governance but that it has failed to realize its full potential due to the described problems of developing a coherent incentive structure.

- In times of crisis and controversies, the PRBS group has been able to promote some highly visible reform steps (e.g. reform of the budget calendar, approval of the Decentralization Implementation Plan). The PRPS pressed hard to achieve such results in order to assure the GRZ of continued authority with regard to the UPs and to deliver credible reports on the ongoing reform process to their headquarters. However, these politically visible achievements have not been transformed into a sustainable reform process on these issues: partly because of a lack of authority on the part of the GRZ, partly because of failure by the CPs failure to provide more continuous incentives. This again reflects the differences among CPs in interpreting BS primarily as an instrument of democracy support and good governance or as an instrument primarily focused on financing poverty alleviation measures.
- Moreover, little emphasis has been put on crucial deficiencies of the political system in relation to weak checks and balances in Zambia's political system. Because this overall weakness has deeply rooted political origins and would require substantial political reforms – including constitutional changes – such issues have been perceived as being too sensitive to tackle with the instrument of BS.
- The most continuous efforts have been made with regard to strengthening independent state agencies that have oversight functions. In this regard, it is important to mention that PRBS CPs themselves have a strong self-interest in strengthening the institution of the Auditor General in monitoring the budget process and uncovering illegal behaviour. Because the CPs were mainly concerned about fiduciary risks of BS that could easily backfire on aid agencies in their home parliaments and over-

sight institutions if cases of corruption and/or misappropriation were to become evident, the CPs had a strong interest in strengthening the Auditor General and receiving potential information on illegal behaviour as soon as possible. This self-interest also partly explains the pressure of some CPs to get access to reports of the Auditor General before the Zambian parliament itself did so, thereby potentially disturbing formal procedures and the proper chain of procedures in the oversight process.

6 The political economy of budget support in Zambia

This section interprets the findings on Budget Support in Zambia described in the previous chapters from a political economy perspective. According to intervention logic, BS has the potential to promote poverty reduction and institutional reforms through an effective combination of financial and non-financial components. However, even a view of BS as useful for promoting institutional capacities, democratic accountability, and poverty reduction does not automatically make it an effective instrument. What is crucial for its effectiveness is the extent to which CPs adapt to a partner country's systemic capacity for addressing its development barriers.

Based on the common intervention logic of BS, one might argue that it is crucial for the effectiveness of the instrument that a recipient country not only has a substantial level of effectiveness of poverty reduction policies and institutional reforms but also possesses the institutional capacity to craft and implement complex development plans. Moreover, the intervention logic requires that a recipient country strongly support the alignment of a heterogeneous set of CPs according to its reform strategies and priorities. Consequently, with an increasing level of the recipient country's systemic capacity to address development issues – that is with increasing levels of democratic accountability, transparency, and administrative capability – the endogenous collective action problems of CPs are resolved by the recipient. Since recipient countries with such systemic capacities will have not only ownership for development oriented processes but also the capability to formulate and implement development-oriented reforms, the responsibility for harmonizing and aligning donor countries will tend to shift relatively smoothly to the partner country's government.

Zambia's systemic capacity, like those of many other countries in the region, is relatively weak. The country has not yet developed the level of systemic strength that allows it to effectively harmonize and align CPs according to a coherent strategic framework. Especially in recent years, the GRZ has not shown a substantial will to engage in far-reaching institutional reforms, nor has it shown much administrative capacity for coordinating complex development plans and aligning CPs accordingly. In such a scenario, the CPs themselves become much more responsible for contributing to coherent policy-making and institutional strengthening.

Thus the Zambian case requires CPs to take on far more responsibility for a harmonized approach towards political dialogue and the different types of conditionality of BS than in a setting with a strong recipient government. This makes harmonization and alignment a more ambitious goal, given the fact, that during past decades harmonization and alignment were often not achieved due to major collective action problems among CPs which were often driven by special political, economic and bureaucratic interests.

Moreover, CPs must not only overcome their own collective action problems, that is, harmonization efforts should not lead to a donor-driven process characterized by a simple imposition of policy measures and conditions upon the partner side. As a consequence, effectively implementing BS in a relatively weak recipient country like Zambia becomes even more challenging. CPs will have to walk the thin line between the advantages of a harmonized political dialogue and conditionality on the one hand and the danger of simply imposing policy obligations on the other. Furthermore, mutual accountability cannot be easily demanded if the partner country is characterized by systemic weakness.

Given the evidence concerning BS inputs, outputs and induced outputs presented in the previous chapters, one may conclude that CPs in Zambia have not yet succeeded in establishing policy dialogue mechanisms and conditionality in a harmonized way that might compensate for the weaknesses of the Zambian state. This does not speak against the instrument of BS as such but rather questions the political will of CPs to cope with the challenges of the instrument's intervention logic, namely the challenge of harmonization and alignment in the absence of a strong, coherent and reform-oriented partner government.

6.1 Systemic weaknesses in Zambia

In spite of the fact that the CPs, together with the GRZ, have managed to set up some fundamental structures necessary for providing effective PRBS, this process has been hampered by domestic weaknesses in Zambia. These weaknesses have been depicted in the previous chapters and can be summarized as follows:

The National Development Plan: Like many other countries, Zambia is crafting a broad development plan which is intended to present a coherent strategy on how to effectively combat poverty and promote economic development. Although the Fifth National Development Plan (FNDP) is more realistic than many of its predecessors, it has not provided sufficient guidance for determining inter-sector and sector resource allocation priorities. Strategic goals and the respective indicators are too broadly defined, and crucial issues of how to address goal conflicts, how to define relative priorities, and how to allocate public resources accordingly are only vaguely dealt with. Given the very broad nature of the FNDP, it has been difficult to see how ministry and public service agency budgets are linked to the plan. Consequently, the FNDP has served only as a very broad framework for aligning CPs to the government's priorities. In this regard, the FNDP and its specific sector considerations have been focused more on analysing past developments than in setting out well-defined scenarios for future policies that could serve as guidance for adapting strategic goals and indicators to changing context factors.

Inter-ministerial incoherency: Given the broad setting of the FNDP, the plan has not functioned as an instrument for creating a more integrated set up of sector ministries and promoting the relative strength of Ministry of Finance and Planning *vis-à-vis* powerful sector ministries. In contrast to several of its counterparts in the region, the Zambian finance ministry is relatively weak politically and, as a consequence, has not been able to involve the sector ministries in an effective reform of public financial management. On the contrary: many sector ministries have been successfully obstructing attempts by the finance ministry to develop transparent and integrated reforms that would enable a more integrated approach towards budget allocations, spending priorities and performance assessment.

This weakness has become especially conspicuous with regard to the SAGs. Unfortunately, many SAGs have often not fulfilled their function of pro-

viding a dialogue mechanism for reviewing sector outcomes/performance and subsequently paving the way to integrated MTEF preparation. They have met infrequently and usually only in the context of planning and reviewing donor-funded sector operations rather than in the context of the MTEF/Budget process. Moreover, many SAGs have failed to promote the alignment of individual sector strategies to that of the FNDP. While some ministries - the Ministry of Education, for instance - have tried to align their internal program structures more closely with that of the FNDP, others have subordinated their internal programs to the department/unit level, thus making it difficult to link budgets to the programs identified in the FNDP. This reveals the weak linkages between the MFNP as the crucial coordinating entity and the sector ministries when it comes to building up an integrated scheme for budget planning and implementation.

Aid Management: As a consequence of the above-mentioned weaknesses, strategic aid management in Zambia has been weak. There is no clear mechanism within the government that deliberates, in a formalised manner, on the management of aid beyond the more routine government systems and structures. This situation mirrors inter-sector incoherencies and the relatively weak collaboration between the MFNP and the sector ministries, the latter being afraid of losing part of their spending autonomy and their privileged access to the sector activities of the CPs. Moreover, the discourse between government and non-state actors in the area of aid effectiveness is also weak at best, meaning that there is no overall strategy of the government for effectively including NGOs in the process of aid management. As a consequence, the strategic capabilities of aligning – and sometimes disciplining – a huge set of aid agencies have been modest.

Declining political will for political reforms: Political development since 2008/2009 casts some doubts on the GRZ's willingness to advance crucial political reforms that are defined in the Underlying Principles. Public sector reforms related to decentralization, public service, or budget reforms have been advancing very slowly. Moreover, the questionable character of some legislative initiatives aimed at regulating NGOs and ensuring the financial transparency of political decision-making have cast further doubts on the government's political will to advance reforms in favour of democratic accountability. In this regard, the current government seems to face a political dilemma. On the one hand it is increasingly under pressure from the opposition, and electoral victory for it in the 2011 presidential elections

is far from secure. This development is related to the fact that despite macroeconomic growth and stability in recent years, little has been achieved with regard to effectively combating poverty and growing social inequality. Faced with the possibility of electoral defeat, the GRZ has been acting defensively in the last two years with regard to institutional reforms. Instead of opting for a strategy of institutional reforms in core areas, including constitutional change towards more democratic accountability, the government has attempted to drown out the calls of NGOs and the opposition for greater transparency, accountability and decentralized state structures.

6.2 Resulting deficiencies in harmonization and alignment

These weaknesses in relation to the lack of administrative capacity and coherence as well as a decline in political clout have made it impossible for the CPs to rely on a purely alignment-based harmonization strategy. On the one hand, CPs have partly taken the challenge of harmonization seriously. Substantial progress has been made in setting up dialogue structures and a common conditionality framework. However, a closer look at conditionality, disbursement mechanisms, the dialogue process and knowledge management reveals substantial deficiencies in the harmonization and alignment process. In sum, one must thus conclude that CPs in Zambia have repeatedly failed to adapt to the specific context of a relatively weak recipient country, so that problems of harmonization and alignment have persisted.

Conditionality and disbursement: The PRBS process in Zambia is characterized by continuing deficiencies in setting up a harmonized incentive system that links the financial and non-financial components of BS in a coherent manner.

The CPs have not managed to establish a cohesive *Performance Assessment Framework* (PAF) in cooperation with the GRZ. Instead, the current PAF involves too many indicators from different sectors and is indecisive about how to measure progress. Both of these elements reflect the absence of a common priority framework among the CPs, among whom different understandings prevail about the proper focus of the PAF. Some CPs argue that the PAF should mainly focus on core reforms, in particular in the area of PFM, leaving the measurement of progress in specific policy areas to the sector work groups. Others, however, consider the PAF as an instrument

derived from an encompassing development plan and therefore conclude that the PAF should also include sector indicators. Beyond this, differences remain among CPs about how to measure performance and progress. While some CPs prefer outcome indicators, others rely more on process indicators and government actions. Overall, this unresolved discussion about the size and the contents of the PAF also reflects the specific, disparate sector interests of particular CPs which have attempted to include indicators in the PAF as a means of strengthening their sector activities by bringing them to the table in the PRBS dialogue fora. This incentive for including particular sector indicators in the PAF was reinforced by weak SAGs. When SAGs have performed in an unsatisfactory way, the inclusion of sector indicators in the PAF has been part of a strategy for securing political leverage regarding sector performance. Thus the GRZ's limited ability to promote a more coherent PAF has not been counterbalanced by the CPs. Instead, an inconsistent understanding of how to build a coherent PAF, along with the specific sector interests of particular CPs, have tended to aggravate the problem.

Closely related to the inconsistency of the PAF is the failure of CPs to harmonize their *disbursement mechanisms*. CPs have very divergent modes of disbursement. CP disbursements differ mainly with regard to the level of fixed and variable tranches of the respective disbursement and how they are linked to the PAF. This divergence of disbursement mechanisms adds to the differences in understanding the Underlying Principles and the PAF indicators. Altogether they show that some CPs attach more importance to the predictability of BS funding while others attach more weight to a performance-based approach in which disbursements are made against an assessment of *ex ante* and jointly defined performance criteria. These diverse disbursement mechanisms make it more difficult to send a coherent signal to the GRZ about the relative priorities of the CPs.

Above and beyond incoherency with regard to the PAF and the related disbursement mechanisms, there have been different understandings among the CPs about violations of the *Underlying Principles*. This became especially manifest in 2009 and 2010, when the General Auditor's office found evidence of a misappropriation of funds and fraud by members of the public sector in two strategic sectors (Health & probably Roads/Transportation). On the one hand, the PRBS group at the official level was – until now – able to respond almost uniformly to this challenge. By temporarily suspending further disbursements for Budget Support and by jointly initiating

a high level dialogue on the Underlying Principles of BS as stipulated in the PRBS MoU, CPs were able to signal their unease about the misappropriation of funds in the health sector and the overall slow pace of reforms. Some reform steps – such as the approval of the Decentralization Implementation Plan and – to a lesser degree - the Reform of the Budgetary Calendar – can be at least partly attributed to this dialogue during times of discomfort (2009).

These dynamics were mainly caused by two counteracting effects:

On one hand, the CPs' expression of discomfort with overall governance performance, along with reflections on their part about suspending BS, had a signalling effect. This signalling effect was especially relevant in the second half of the political cycle, given GRZ's rising concern about losing the general elections in 2011. In this regard, a joint suspension of disbursements would have been viewed by the critical press, civil society and by the opposition as evidence for the government's weak performance. Moreover, BS funding still plays an important role in given the government's fiscal leeway, making the weight of the funding dimension of PRBS in Zambia politically important.

On the other hand, however, this leverage effect was limited because of the remaining fragility of the harmonized approach. While uniformly signalling concern to the GRZ during the 2009 health scandal, the subsequent actions of individual CPs partly differed. While Sweden and the Netherlands considered suspending BS at least temporarily, and Sweden in fact did temporarily withdraw from the consensus not to suspend BS, the EU decided to continue its disbursements, and one CP even augmented its disbursements during the course of events. This highlights the ongoing collective action problems within the PRBS group. Therefore, while the recent misappropriation scandals have been accompanied by substantial efforts of CPs to maintain a harmonized approach, the same events have also highlighted frictions among CPs in providing PRBS.

Joint knowledge management: Related to different interpretations among CPs about how to craft and implement conditionality and disbursement mechanisms, the potential for joint knowledge management including joint monitoring and learning has received too little attention. While the CPs have made substantial progress in systematic information exchange and have provided an institutionalised dialogue structure for such exchange,

joint knowledge management has been weak - a fact that has undermined the quality of the dialogue process. Overall, more than ten bilateral and multilateral CPs have been directly or indirectly involved in providing PRBS to the GRZ. Yet almost no resources have been spent to set up a common information basis for long-term-oriented assessment of the PRBS progress. Instead, relevant information such as that contained in budget analyses, sector assessments, and disbursement activities has been mostly disseminated on an ad hoc basis and has been widely dispersed among CPs. This situation has caused a huge duplication of work by individual CPs and the GRZ and obstructs a more efficient use of invested human capital. Given the high turnover of staff amongst the CPs, the absence of a permanent "PRBS secretariat" has further threatened the institutional memory, the depth of understanding of the issues at hand, and consistency in the dialogue. The absence of a permanent "PRBS secretariat" responsible for joint knowledge management can be seen as a significant roadblock to the establishment of a more solid, fact-based dialogue process. Interestingly, the CPs so far have rejected proposals by the GRZ for establishing a more effective aid coordination entity that could provide strategic overview information not only on the overall PRBS process but also on individual donor activities. In this regard, it is also worth mentioning that the present endeavour of jointly evaluating the instrument's effectiveness in recent years has been paralleled by uncoordinated ad hoc evaluations and assessments on the part of individual CPs. These parallel evaluations and assessments have created an additional administrative burden for the GRZ.

Mutual accountability: Given the weakness of a common, strategically oriented monitoring system and the divergence of perspectives on crucial elements of a joint incentive system for guiding the PRBS process, the CPs have also been rather reluctant to engage actively in a process that aims at providing joint accountability for their support.

In this regard, the CPs have responded in a lukewarm manner to several efforts by the GRZ to generate more transparency in the overall assistance activities undertaken by the international donor community. The CPs have rejected demands from MFNP to list all (off- and on-budget) aid activities according to several criteria (volume, disbursement, mode of delivery, etc.) and to make this information public. This rejection was based on the argument, that the criteria established by the MFNP were not optimal and would create too many transaction costs. Another somewhat informal argument

was that several CPs did not want to explicitly reveal the amount of their concrete support to civil society groups. While these arguments may not have been without substance, the CPs nevertheless did not follow up on the GRZ's initiatives and did not attempt to offer an improved initiative by themselves.

A similar reluctance on the part of the CPs to facilitate the GRZ's efforts to improve its capacities for aid management effectively characterised the final preparation of Zambia's Aid Policy and Strategy, an aspect that seriously compromised the establishment and strengthening of an effective dialogue architecture in the country. For example, during the development of the Aid Policy and Strategy, considerable time was spent on the preparation of two important chapters, namely (a) *Framework for Implementation of Aid Policy*; and (b) *Aid Coordination Framework*. These chapters were removed from the final Aid Policy and Strategy document at the insistence of the two CP representatives who sat in on the meetings of the Reference Group (the body chaired by the ETC Director which superintended the development of the Aid Policy and Strategy). The position of the CPs was that the two chapters should be 'revisited' after the Policy was approved by Cabinet. Such a 're-visitation' never took place, and the Aid Policy and Strategy was approved by Cabinet in May 2007.

A positive move was made recently in Zambia to address some of these aspects. It was decided at the time of the formulation of the PAF for 2007-2009 that a number of indicators for assessing the nine PRBS Cooperating Partners in their provision of budget support should be included. Three indicators specifically dealt with the proportion of ODA given as budget support, the amount of PRBS disbursed as a percentage of commitment, and the average delay. Not surprisingly, the overall picture reveals a high degree of heterogeneity among the CPs. In combination with the rejection of several GRZ initiatives for making aid flows more transparent and establishing a joint coordination and monitoring system, the strategic heterogeneity among CPs has tended to exacerbate the GRZ's weaknesses in coordinating and aligning foreign assistance rather than helping to overcome them.

6.3 Root causes of harmonization and alignment deficiencies

As this evaluation has shown, the process of giving BS to GRZ has produced some significant progress with regard to building common incentives systems, information exchange and dialogue structures.

This progress is important because harmonization is required for effectively implementing BS in Zambia (and elsewhere). However, the analysis has also shown that this progress has not been sufficient to cope with the specific challenges of the political context in Zambia and that harmonization, alignment and mutual accountability have been plagued with continuous deficiencies. The absence of a long-term oriented joint strategy and the resulting ad hoc dialogue on important issues tends to create unpredictability for both the CPs and the GRZ. Moreover, disagreement about the contents of the PAF and the relative importance of the Underlying Principles makes it difficult for the CPs to send clear signals about their overall priorities, thereby undermining a more thorough policy dialogue with the partner. Finally, the rather opaque and sometimes ad hoc structure of the PAF creates a predictability problem for the respective partner, stands in contrast with the principle of mutual accountability, and undermines the already limited capacities for the GRZ for alignment. Taken together, these problems impose a burden on any attempt to carry out a strategically oriented policy dialogue; they reduce the predictability of reactions of the PRBS group *vis-à-vis* the GRZ, and they diminish the potential leverage of BS for promoting policy reforms oriented towards poverty reduction, increased governance effectiveness of the administration, and democratic accountability. The following paragraphs provide an explanation for this finding and argue that there have been mainly two interrelated root causes for the above-mentioned insufficiencies.

- 1) First, the CPs continue to have different understandings about the hierarchies of the two strategic goals embedded in the intervention logic of BS, namely the goal of funding for poverty reduction and the goal of promoting deep-reaching institutional reforms.
- 2) Second, harmonization efforts by local aid agencies have been repeatedly disturbed by specific interventions on the part of various national CP headquarters, which have responded more to political necessities in the respective donor countries than to harmonization requirements in the recipient countries.

Ad 1): According to one possible interpretation, BS is primarily an instrument for channelling resources through a recipient country's budget into sectors that are most relevant for poverty reduction in order to more effectively and efficiently finance policies for poverty reduction. Alternatively, BS can also be primarily interpreted as a set of incentives combining finan-

cial and non-financial components that can promote deeply rooted institutional change towards transparency and democratic accountability. While the common intervention logic assumes that both goals can be mutually reinforcing, this parallel achievement is not a given. Especially in times of crisis, CPs will have to rank the relative importance of these two goals in order to decide whether to continue with disbursements or not. As the case of Zambia shows, this potential conflict of interest has been existent but has not been made explicit. The relative priority given to governance promotion as opposed to financing poverty alleviation has differed among the CPs and has complicated a joint approach of the CPs in the dialogue process.

The differences in goal priorities also partly explain why for instance Sweden temporarily suspended BS in 2009 while the EU increased its disbursements significantly through its V-Flex mechanism around the same time. It also explains why different CPs have given different importance to the UPs. For some, these underlying principles – referring to the general reform process and governance context – are the most important part of a de facto conditionality. For those CPs that give high priority to governance promotion, every disbursement has at least implicitly to be made against an assessment of these principles. For those CPs, indicators of the PAF play only a supplementary role, while the fulfilment of the Underlying Principle is a key factor in triggering disbursements. For others, the relative priority of Underlying Principles and PAF indicators is just the opposite. For instance, the EU also regards BS as a “dynamic” instrument that can be implemented in countries with relatively weak governance structures because the instrument is assumed to be apt for improving those weaknesses. This interpretation can easily conflict with the interpretation of several bilateral donors such as Germany and Sweden. The latter CPs perceive budget support only as a suitable aid instrument for countries which have already reached a certain level of political transparency and accountability. These different interpretations of the instrument’s intervention logic also partly explain the still fragmented analytical mechanisms. Individual CPs prefer to define the concrete terms for analysis according to their specific interpretations of the instruments’ intervention logic, which is not necessarily identical with that of other CPs. As one representative of a bilateral aid agency has put it, the core problem is straightforward (as was confirmed in several other interviews):

“We have different constituencies, different incentives and do respond to different political masters back home. I get demoted when I overlook a corruption scandal; others get promoted when they meet their disbursement targets.”

Ad 2): The prior citation points not only to different priorities with regard to strategic goals related to BS but also provides us with the central explanation for why these different interpretations exist. While the principles of the Paris Agenda and intervention logic points to the necessity of harmonized and aligned interventions in order to counter the negative effects of donor fragmentation, the individual actions of particular CPs with regard to their BS- related activities in Zambia are driven primarily by domestic considerations. The Zambian experience suggests at least that when the alignment capacities of the recipient country are weak, the impact of the political constellation back home is very high.

When harmonization and alignment became prominent guiding principles in the first half of the past decade, many CPs embarked upon BS as an instrument that promised to deliver the desired degree of harmonization and alignment. In what might be called the "first generation" of harmonization the CPs put emphasis on establishing dialogue, harmonization and alignment structures in the respective partner countries in order to organize a more coordinated way of delivering BS. Zambia represents this approach and has had some success in establishing the organizational structures that would have enabled CPs to enter a harmonized dialogue and funding strategy. Yet, these structures established by the PRBS group in cooperation with the GRZ have been frequently undermined by standards, procedures and interference originating from the different CP headquarters and their respective political constituencies. Since local officials from aid agencies have to respond to their headquarters' demands, they will eventually introduce a plurality of interests into both the local dialogue and the harmonization structures, thereby substantially reducing the collective action capacities of the PRBS group. In the Zambian case, this challenge became evident with regard to several aspects.

The differences already described in prioritizing poverty alleviation and governance reforms are often a function of different interests and constellations in the respective donor countries. In countries in which parliaments and oversight institutions have shown a higher level of scepticism with regard to the instrument of budget support, the national headquarters have become more sensitive to questions of corruption and potential misappropriation of funds. Accordingly, they tend to give more weight to the Underlying Principles and prefer performance-oriented disbursements to predictability in disbursements. Consequently, attempts to establish a harmo-

nized approach within the PRBS group in Zambia have also been a function of different political constellations in the respective donor countries, and domestic political changes have had an impact on the level of heterogeneity within the PRBS group. For instance, recent government changes in several European countries, such as the Netherlands, the U.K., and Germany were accompanied by different perceptions of BS as an adequate instrument of development cooperation. When aid managers on the ground in Lusaka had to respond to the – democratically legitimized – political changes in their home countries, they found themselves in a difficult situation. While they were expected to jointly implement a harmonized and aligned approach, they were at the same time receiving orders from headquarters that could easily change over time due to alterations in the political situation at home. Again, the impact of the resulting volatility and heterogeneity on harmonization and alignment tends to increase inversely to the weakness of the recipient governments in aligning the CPs to their respective governance priorities.

Given these circumstances, one can interpret it as a relative success that CPs on the ground have managed to maintain a certain level of harmonization during the last two years. However, this will continue only if the different agency headquarters, i.e. their constituencies and oversight institutions, embark on a second generation of harmonization efforts; only then will the problems of incoherent disbursement mechanisms, the overloaded PAF, and differences about the hierarchy of objectives be reduced to a level at which BS in Zambia will develop its full potential. This of course is the political dimension of harmonization and alignment, which often remains escapes consideration.

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Annex

Annex: List of interview partners			
Last name	First name	Institution	Function
Banda	Saul	Ministry of Education	Policy and Research Advisor
Beaume	Eric	European Commission	Head of Operations
Blokhuis	Frans	GIITEC	Team Leader, Resident Engineer
Botterweck	Gerd	Friedrich-Ebert-Stiftung	Resident Director
Bowden	Andrew	Irish Aid	Governance Advisor
Bwalya	Samuel	Ministry of Finance and National Planning	FMS Officer
Chanza	Collins	Ministry of Health	Chief Planner of Development Cooperation
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Chundu	Benny	Ministry of Energy and Water Development	Director of Planning

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Hara	Matthew	Office of the Auditor General	Director Provinces
Harris	Clare	DFID	Economic Development Advisor
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Kapinka	Kelly M.	Ministry of Works and Supply	Assistant Director of Planning
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Kaunda	Emmanuel	National Road Fund Agency – M&E Department	Monitoring and Evaluation Manager
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Kressler	Robert	GTZ	Office Manager

Annex (cont.): List of interview partners			
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Krimmel	Thomas	KfW	Consultant
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Lubambo	Peter	Ministry of Local Government and Housing	Director
Mabenga	Raphael	National Road Fund Agency	Director and CEO
Mandohs	Andy	Ministry of Energy and Water Development	Programme Manager, Water Advisor
Maape	n/a	Ministry of Works and Supply	Chief Engineer of RDA
Matengu	Mbala	Ministry of Local Government and Housing	n/a
Meiz	Masce	Ministry of Works and Supply	Assistant Director (Technical)
Mendamanda	Davison K.	Office of the Auditor General	Deputy Auditor General CSD
Meyke	Frank	German Embassy	Ambassador
Misale	Cetty	KfW	Financial Specialist Macro Economics and Public Expenditure

Annex (cont.): List of interview partners			
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Mubita	Kaalu	Economics Association of Zambia	Economist
Mukungu	Ashie	AfDB	Senior Country Economist
Mulanga	Daniel	Road Development Agency	Principle Engineer
Musuku	Steven	Bank of Zambia	Senior Economist, Balance of Payments and Debt Division; Economics Department
Mwansa	Louis	Office of the Auditor General	Director Planning
Mwila	Alfred	Zambia Revenue Authority	Assistant Director Research and Planning
Nkunika	Bizwayo N.	Ministry of Works and Supply	Permanent Secretary
Nyambe	Vincent	National Road Fund Agency	Fund Manager
Nyawali	Lazarous	RDA	Regional Road Engineer Livingstone
Pain	Chris	GTZ	Macroeconomic Advisor MoFNP, M&E
Palale	Patricia	World Bank	Public Sector Management Specialist

Annex (cont.): List of interview partners				
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Tumbwe	Boniface	Ministry of Finance and National Planning	Chief Accountant, BEA	
von Rabenau	Kurt	KfW	Consultant	
von Schönhoven	Christian	KfW	Economist, Road Sector Expert	
Watae	Sydney	USAID	Governance Expert	
Whitworth	Alan	DFID	Economic Advisor	
Zanotta	Alessandro	European Commission	EU Advisor Macroeconomic and Public Finances	
Zgambo	Peter	Bank of Zambia	Senior Economist – Research Division; Economics Department	
Zyambo	Rachel	Ministry of Finance and National Planning	Deputy Accountant General	

Annex (cont.): List of interview partners			
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Sverken	Karin	Swedish Embassy	First Secretary BS and Public Sector Reform
Tumbwe	Boniface	Ministry of Finance and National Planning	Chief Accountant, BEA
von Rabenau	Kurt	KfW	Consultant
von Schönhoven	Christian	KfW	Economist, Road Sector Expert
Watae	Sydney	USAID	Governance Expert
Whitworth	Alan	DFID	Economic Advisor
Zanotta	Alessandro	European Commission	EU Advisor Macroeconomic and Public Finances
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Zyambo	Rachel	Ministry of Finance and National Planning	Deputy Accountant General

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