

## **Ingo Scholz; Johannes Plagemann: Opportunities and Risks of Budget Assistance: The Example of Mozambique**

Within today's development policy, budget assistance is regarded as the new and the best method. In the *Paris Declaration on Aid Effectiveness*, both donor and receiving countries refer to the necessity of pursuing self-responsible strategies to fight poverty and to budget assistance as a tool of development cooperation. It even is to be the first choice wherever the conditions prevailing in the partner countries permit it. In Mozambique, one of the beneficiaries, the volume of budget assistance promised for 2008 amounts to about 435 million US dollars. Mozambique is a good example for demonstrating and evaluating the opportunities and risks of the 'budget assistance' tool.

One of the world's poorest countries, Mozambique may be regarded as underdeveloped even by the standards of sub-Saharan Africa. The reasons for this lie in the history, the economy, and the domestic policy of the country. Even in the eighties, Mozambique was largely dependent on foreign donors which in 1992, the year of the cease-fire, still provided a share of 87 percent of the gross domestic product by way of assistance. In 2007, the share of foreign aid came down to 54 percent of the national budget, and 56 percent are expected for 2008. By now, the donors and Mozambique's government have developed a modus operandi: When diverse bilateral donors agreed in 1999 to coordinate and harmonise assistance, they attached to it the condition that a single strategy of poverty alleviation should be agreed which the government would have to maintain in the long run. Today, budget assistance in Mozambique is regarded as the most convincing example of harmonisation and coordination worldwide. Some people even call it a 'success story of development cooperation'.

It is true that budget assistance offers many opportunities: One central argument in its favour is the concept of ownership. In contrast to classical project aid, the government of the receiving country is supposed to work out an individualised development strategy adapted to the conditions prevailing in the country. A government which is itself responsible for reducing poverty in its country is bound to pursue its strategy sustainably: More self-responsibility means more sustainability. Another advantage of budget assistance is that it increases the accountability of the receiving country's government towards its own voters, the parliament, and the press. If it is solely the receiving country that decides on the allocation, planning, and coordination of the funds provided, the consequence will be a learning effect or, in other words, capacity development. It is expected that the concept of budget assistance will markedly reduce transaction costs, and that administrative expenses will shrink on both sides. It is also conceivable that budget assistance will have a positive impact on the fight against corruption. Budget assistance might defuse the problem of strongly fluctuating assistance payments and contribute towards macroeconomic stability and/or more sustainable national-budget planning. And finally, budget assistance may be understood as an expression of partnership and equality in the receiving country.

However, budget assistance carries numerous risks: Thus, given the reduction of official influence, the ownership concept generates more self-responsibility, but assistance-related interference with the budgetary procedure also challenges the sovereignty of the nation state. In addition, foreign experts posted in the receiving country increase the degree of control over the negotiated package, which runs counter to the principle of ownership. As the principle of budget assistance strengthens the central government, this may counterbalance any incentives to control government activities more efficiently – through parliament, for example. Lastly, there is not much accountability in Mozambique: The former state party, FRELIMO, is still the strongest force, which also shows in the composition of the parliament, and it cannot be taken for granted that the appropriations

committee actually reviews the national budget. As society is not able to control the national budget process it is for the donors to make sure that funds are used correctly.

There are other disadvantages as well: One of them arises from the double function of the administration: Receiving countries are to manage their funds on their own so as to increase their human capital and their efficiency in the use of funds, especially in the management of public finances. Thus, however, funds management is both the objective of and the prerequisite for budget assistance. Another worrying aspect is the increased fiduciary risk caused by the pooling of funds that goes hand in hand with donor harmonisation. Yet another downside is the high costs related to introducing budget assistance which result from the necessary control and support of the central government, including the development of expertise by the donor and the coordination of donor institutions. The monopolisation of allocation promoted by budget assistance may be an incentive for corruption: The wider a receiving country's discretion in the use of funds, the higher the corruption potential. For not one single high government official or politician has ever been prosecuted for malpractice in Mozambique – despite a whole series of spectacular scandals and the pressure exerted by the donors.

A further negative aspect is the selective character of budget assistance which inevitably keeps this tool from being applied widely, as good governance and extreme underdevelopment coexist only rarely. Furthermore, it must be criticised that budget assistance entails a shift of decision-making competence to the central government, weakening a civil society that lacks adequate tools of participation. As the proportion of budget assistance within the receiving countries' budget is on the rise, donor countries have to face the question of an 'exit strategy'. If a receiving country does not comply with its obligations so that the donor country feels compelled to react, volatility increases. This, in turn, is associated with conditionality which, given the fiduciary risk of budget assistance in unstable countries, can only be avoided by losing credibility. In the medium term, budget assistance might also threaten the generation of tax revenues – one of the development goals and a prerequisite for lasting prosperity.

Budget assistance does indeed ask much of both sides. Even in the future, there will be no alternative to the presence of experts who know the country – even if project aid is largely replaced. We must not expect too much of the national elites' eagerness to reform. In Mozambique, for example, the elites are still refusing to tackle the problem of corruption. Analysing budget assistance by the example of Mozambique gives rise to questions. Is the tool as such practicable, after all, if even the 'star pupil' displays so many risks?

In the future, budget assistance should certainly be subordinated more strongly than before to the main objectives of development policy, such as the demand for good governance. Blatant deficits in the political system, the weakness of the judiciary, unfair elections, and widespread corruption are defects that must be corrected. While this is first of all the duty of the Mozambicans, other countries should also contribute their share – not least by intensifying their control.

Donor countries are facing a problem *sui generis*: Can they admit, if necessary, that budget assistance has failed? And what would be the consequences in such a case? Splendid isolation from the circle of donor countries would cause medium-sized donors such as Germany to lose their influence and reputation not only with the other donors but also with the receiving country. Joseph Hanlon, an expert on Mozambique, says that to the donor countries, political stability and maintaining 'successful' cooperation has always been more important than democratic and institutional progress. On the other hand, experience shows that the rulers of developing countries often prefer massive cuts in assistance to losing their own power.

The Overseas Development Institute states that the essential prerequisite for successful budget assistance is the willingness of a receiving country's leadership to assume political responsibility and to answer to parliament and the civil society. Mozambique still shows serious deficits in both respects.