

Aid instruments for peace- and state-building: Putting the New Deal into practice



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About the g7+

The g7+ is a voluntary association of countries that are or have been affected by conflict and are now in transition to the next stage of development. The main objective of the g7+ is to share experiences and learn from one another, and to advocate for reforms to the way the international community engages in fragile and conflict-affected states.

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New Deal case study

The European Union's State Building Contracts (SBCs) for providing budget support to fragile states

1. Budget support and EU State Building Contracts – Background and context

During the 2000s budget support – financial assistance direct to a government's budget – became an increasingly common instrument for providing aid to developing countries. This expansion in its use emerged due to concerns about the ownership, sustainability and impacts of project aid, as well as in response to the imperative of helping to finance the scale-up in spending required to achieve the Millennium Development Goals (MDGs) and other development priorities.

Budget support as an aid instrument has attracted a great deal of debate. On the one hand its aid effectiveness credentials have been confirmed (at least in part) by a range of evaluations, and it has supported a significant scale-up in service delivery (IDD and Associates 2006; Lawson 2014). On the other hand, its critics have been eager to highlight its vulnerability to corruption, and evaluations have identified its limited contributions to date in helping to improve governance (IOB 2011) and the quality of service delivery (Williamson and Dom 2009).

In recent years, concerns about the effectiveness of budget support have come into sharper focus due to constraints on donor public finances and aid budgets following the global financial crisis. As a result a number of donor governments have cut their bilateral budget support programmes. However, European member states have continued to provide budget support multilaterally through the European Commission (EC). The EC's budget support fell by just over 20% in 2011, but has since remained stable and its budget currently constitutes around 50% of the total budget support provided by OECD Development Assistance Committee members (OECD 2015).

Fragile states have been amongst the largest beneficiaries of budget support from the EC. Under the 9th European Development Fund (2001-07) half of budget support commitments¹ were made to twenty countries on the current OECD list of fragile states. These countries were also programmed around 40% of budget support under the 10th European Development Fund (2008-13) (ECA 2010). This assistance has built on the EU's long-standing political commitments to support fragile states, initiated by its 2001 Programme for the Prevention of Violent Conflicts.

2. Introducing the State Building Contracts (SBCs)

SBCs are an instrument the EC has introduced to guide its provision of budget support to fragile and conflict-affected countries. The EU utilises this instrument alongside Good Governance and Development Contracts (GGDC), which provide general budget support (support to the general budget) to countries with stronger institutional and policy environments, and Sector Reform Contracts (SRCs), which provide sector budget support (support to sector budgets) in pursuit of sector development priorities (EC 2012).

A number of characteristics distinguish SBCs from traditional budget support programmes:

- **Focus on countries facing fragility** – these countries are identified on the basis of assessing the nature of their fragility, a process which also helps to guide implementation and assist efforts to ensure that SBCs are strategically oriented towards supporting state building objectives
- **A flexible and forward-looking approach to assessing fundamental values and eligibility criteria** – GGDCs require a positive assessment of adherence to the fundamental values of human rights, democracy and the rule of law, as well as other eligibility criteria (e.g. the strength of financial management systems); in contrast SBCs require that there merely be signs that progress can be made in these areas in the future (e.g. commitment to relevant reforms); such an approach recognises the political and institutional challenges inherent in situations of fragility
- **Short-term duration and rapid deployment** – SBCs were initially to be implemented over the course of 1-2 years, with the possibility of extension for a similar period (GGDCs and SRCs are typically in operation for 3 to 6 years); SBCs have also been deployed relatively rapidly in order to ensure they can respond to the urgent political and developmental challenges found in fragile states

Another important element of the EU's reformed approach to budget support is **a strengthened approach to assessing and managing risk,**

¹ Data on EU budget support disbursements across these countries are not readily available and may differ from commitment figures; in addition, not all of these countries would have been considered FCAS throughout this period, so these figures are not a totally accurate picture of the historical trends in EU budget support

including formal recognition of the risks of inaction from donors. Recognising such risks represents a unique innovation of SBCs amongst budget support instruments.

Other important characteristics of SBCs (as well as GGDCs and SRCs) include **the use of variable as well as fixed tranches, with variable tranches linked to programme conditions; and funding for complementary technical assistance.**

As of the end of 2014 SBCs operations had been approved in 15 countries, 10 of which were in sub-Saharan Africa. Funding disbursed through these operations totalled €1.369 billion, equivalent to around 12% of total EC budget support since the introduction of the new instruments. The average level of funding provided through individual SBCs has to date been €91.3 million, which is considerably larger than the average budget support instrument (at €47.5 million). In 2015 an additional eight SBCs are planned for approval, seven of which will be in west and central Africa (EC 2015).

3. What were the drivers of the introduction of SBCs?

Following the global financial crisis in 2007/8 and the subsequent squeeze in public spending across donor countries, aid budgets have come under greater scrutiny and been cut in many cases. This context has also led to greater scrutiny over and cuts to budget support operations, including amongst European Governments, who have historically been amongst the strongest supporters of budget support (Tavakoli and Hedger 2012). Questions about the EC's budget support operations have also been fuelled in part by a 2011 European Court of Auditors (ECA) Report on the EC's management of general budget support, which concluded that this aid instrument had not been effectively adapted for use in diverse country contexts, such as fragile states (ECA 2011).

In response to this scrutiny in 2011 the EC introduced a new policy framework to guide the management of its budget support – 'The Future Approach to EU Budget Support to Third Countries'. One of the main objectives of this policy framework is to ensure that the EU's budget support is better adapted to country contexts, including

fragile situations. This objective was pursued through the introduction of State Building Contracts (SBCs) to provide budget support to fragile and post conflict states, alongside GGDCs and SRCs (see section 2).

4. How the instrument addresses the New Deal principles

SBCs address a range of the New Deal principles, especially those in the TRUST pillar, as outlined below:

- **Risk-sharing** – By applying a risk assessment process for SBCs which takes into account the risks facing partner countries from donor decisions not to provide assistance alongside the risks for the donor in providing assistance SBCs support a strong (and somewhat unique) approach for promoting the sharing of risk in the provision of development assistance
- **Use of country systems** – In providing budget support through SBCs these instruments make maximum use of country systems, helping to facilitate efforts to strengthen them
- **Strengthen capacities** - A key element of the SBC package is technical assistance which is targeted at supporting countries to strengthen government systems and institutions

SBCs have also attempted to promote many of the peacebuilding and statebuilding goals, largely through the conditions attached to the variable funding tranche in these areas. Almost all of the SBCs implemented to date include conditions relating to **revenue and services** (mainly through strengthening public financial management and promoting domestic resource mobilisation), five include conditions related to promoting **justice** and three include conditions related to promoting **security**.

Finally, it is also important to note that amongst the pre-conditions for South Sudan's SBC (which was ultimately postponed due to the outbreak of conflict) was agreement on the countries' **New Deal Compact**. This approach was pursued in an effort to ensure that these processes complemented and leveraged each other.

5. Impacts of SBCs

The first SBCs began disbursing in 2013 and this instrument therefore has some (albeit limited) track record of implementation from which to identify some initial general impacts of SBCs. The following insights on the initial impacts of SBCs draws on both official (EC 2014) and external (Hauck et al 2013; Bernardi et al 2015) reviews of early implementation of this instrument.

The first point to note is that SBCs have provided very significant levels of funding in fragile high risk contexts, where most donors have been unwilling to provide substantive support, especially through governments. SBCs have also been important vehicles for pursuing the New Deal for engagement in fragile states, especially in addressing the TRUST principles. SBCs therefore add notable value to the international community's response to the challenges facing fragile countries.

The EC has also displayed the ability to relatively rapidly (certainly compared to other donors) approve, design and begin implementation of SBCs, which has provided it with the opportunity to respond quickly to emergencies and crises. For example, in the case of Mali only five months elapsed between the initial identification mission and the first disbursement. This allowed the SBC to support the Malian Government to maintain civil service pay and hold successful elections, both of which were vital to stabilisation efforts (Bernardi et al 2015).

In addition, the Mali case also illustrates that the ambitious levels of funding provided by SBCs to countries in emergency situations provide an opportunity for the EC to leverage reforms vital to improving the effectiveness of and accountability of governments. Following a corruption scandal which emerged during the early stages of implementing the SBC, the EC was able to secure reforms to the public procurement code and commitment to a formal follow-up process, measures which will help to improve accountability for public spending into the future (Bernardi et al 2015). The experience of budget support does though suggest that in general deep and sustained governance reforms may be beyond the reach of SBCs (IOB 2011).

6. Lessons learnt

This section also utilises official and external reviews of the initial experiences with SBCs to identify lessons for improving the design and implementation of this instrument. It is hoped that these insights will also be useful for informing implementation of other similar support programmes in fragile states. The following lessons emerge from the initial implementation experience of SBCs:

- **Pursuing shared approaches to risk** – SBCs have helped to promote a shared approach to risk by incorporating a focus on the risk to the partner country of non-intervention. This principle of “sharing risk” has been promoted in a number of international aid forums, but this is one of the few practical examples to emerge of donors pursuing it.
- **Pursing short and long term objectives coherently** – The Mali and South Sudan SBCs attempted to address both short term goals of promoting stability, as well as longer term goals relating to state-building and governance. There has been some degree of tension between these goals, which has created challenges for better focussing their implementation (Bernardi et al 2015). This experience highlights the importance of budget support/aid programmes addressing immediate development challenges within a complimentary long-term strategy and partnership.
- **More objective and transparent approaches to the selection of recipients** – It has been noted that there is limited clarity on the criteria which are used to select countries to receive SBCs, and that developing clearer and objective criteria for country selection will help to build confidence in this instrument and more effectively target its support (Hauck et al 2013).
- **Better targeting of technical assistance** – The technical assistance component of SBCs is vital given the weak levels of human capacity in many fragile contexts, and it is therefore important that SBCs routinely provide significant levels of support to building such capacity. However, technical assistance hasn't yet been adequately deployed across all phases of the SBC programme cycle

(Hauck et al 2013). Analysis of the Mali and South Sudan SBCs also found that the levels and content of technical assistance wasn't adequately tailored to the specific challenges being faced in each of these countries (Bernardi et al 2015).

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