Using PEFA to Support PFM Improvement

Volume 4 of the PEFA Handbook
Guidance objectives

Provide a practical guide on:

• How PEFA assessment reports can be used to improve PFM performance
• The issues that need to be considered in developing effective reform initiatives

Design PFM reform initiatives that:

• Have government commitment, ownership and input
• Are based on clearly desired PFM outcomes
• Consider and address potential constraints
• Reflect government priorities and capacities
• Are sequenced in accordance with the desired outcomes, potential constraints and government priorities
Things to consider in developing PFM reform

• Use PEFA assessment findings in the country context:
  • There is no “one size fits” answer to sequence and design reforms
  • Reforms must be tailored to country’s situation

• Practical guidance is not prescriptive

• Government is responsible for PFM reforms prioritization and implementation

• PFM reform not always linear

• Different approaches to reform should be considered from formal, structured plans to more iterative reform methodologies
Design principles for PFM reform

• Understand role of non-technical factors
• Involve broader stakeholders groups when designing, implementing, and monitoring reforms
• Agility and speed are crucial for relevant and impact
• Ongoing monitoring, learning, and adjustments are key to countering foreseeable constraints
Seven stages of PFM reform

1. Identify PFM strengths and weaknesses
2. Determine underlying causes
3. Agree desired PFM outcomes
4. Design and prioritization
5. Identify and address constraints
6. Implement reforms
7. Monitor progress and impact
**Using PEFA to support PFM improvement: Key stages and questions**

<table>
<thead>
<tr>
<th>Key stages following the PEFA report</th>
<th>Main questions</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Stage 1: Identify PFM strengths and weaknesses</strong></td>
<td>What problem or problems that need to be addressed that are impacted by PFM? What are the findings of the PEFA assessment?</td>
</tr>
<tr>
<td><strong>Stage 2: Determine the underlying causes of strengths and weaknesses</strong></td>
<td>What are the causes of strong and poor PFM performance identified by the PEFA assessment?</td>
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<td><strong>Stage 3: Agree on desired PFM reform outcomes</strong></td>
<td>What are the government's desired outcomes of PFM reform?</td>
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<td><strong>Stage 4: Develop and prioritize PFM reform initiatives</strong></td>
<td>Which initiatives can bring about the desired outcomes? What are the most important reforms and how do we sequence them?</td>
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<td><strong>Stage 5: Identify potential constraints to reform</strong></td>
<td>What are the constraints to reform? How are the constraints addressed?</td>
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<tr>
<td><strong>Stage 6: Implement reforms or reform action plans</strong></td>
<td>What are the actions, deliverables, responsibilities and timelines?</td>
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<td><strong>Stage 7: Monitor and evaluate reform implementation</strong></td>
<td>Are reforms being implemented? What are the next steps for reform? Has reform had the desired impact on the identified problem?</td>
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Stage 1: Identify PFM strengths and weaknesses

- What is the problem?
- What are the main findings of the PEFA assessment?
- PEFA may/may not be the driver of reform
- Identify broader policy issues
- Take stock of relevant analytical work
- Consider the matrix of PFM strengths and weaknesses
Stage 2: Determine the underlying causes of strengths and weaknesses

• What are the causes of strong and poor PFM performance identified by the PEFA assessment?

• Further analysis may be needed including:
  • Informal enquiry;
  • Formal technical analysis;
  • Using other PFM diagnostic tools

• Underlying causes also act as constraints or enablers to developing and implementing reform
# Case study

<table>
<thead>
<tr>
<th>PI</th>
<th>PEFA score</th>
<th>Strengths and weaknesses</th>
<th>Underlying causes</th>
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| PI-1 | D | Aggregate expenditure outturns exceeded original budget by more than 20% in last three years | • Overoptimistic economic and fiscal projections  
• Unavailability of economic and fiscal forecasting models  
• Lack of capacity in economic and fiscal forecasting  
• Political involvement in setting fiscal projections |
| PI-2.2 | D | Significant variation in budget composition by function undermining the predictability and availability of budget allocations to key service delivery agencies. |
Stage 3: Agree on desired PFM reform outcomes

- What are the government’s desired outcomes of PFM reform?
- What would the government like to achieve over the short term, medium term and long term?
- Helps guiding prioritization and sequencing
- Drawing on national policy objectives enables practical alignment reform/national objectives
## Case study

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• Improved predictability of budget allocations to service delivery ministries. |
| PI-2.2 | D | Significant variation in budget composition by function undermining the predictability and availability of budget allocations to key service delivery agencies. | | |
Stage 4: Develop and prioritize PFM reform initiatives

- **Which initiatives can bring about the desired outcomes?**
- **What are the most important reforms and how do we sequence them?**

- **Initiative/action:** intended result, timeframe, responsibility
- **Appropriate reform design and optimum sequencing is country-specific**
- **Costs and available financial resources**
- **Sometimes priorities causally & sequentially linked**
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<th>Desired outcomes</th>
<th>Proposed reform activity and priority</th>
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<td></td>
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<td>Unavailability of economic and fiscal forecasting models</td>
<td>Improved predictability of budget allocations to service delivery ministries.</td>
<td>• Implementing cash flow forecasting (medium)</td>
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<td>Lack of capacity in economic and fiscal forecasting</td>
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<td>• Updating budget processes and procedures (high)</td>
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Stage 5: Identify potential constraints to reform

- What are the constraints to reform?
  - Capacity
  - Institutional
  - Political economy

- How are the constraints addressed?
  - Can the constraints be mitigated, if so, how?
  - Are constraints such that they will preclude implementation of reform?
  - If so, should the reform be deferred until such time as the constraint can be addressed?

- Non-technical factors vary across countries and overtime
- No consensus on how to address non-technical factors
- Identify alternative technical solutions
<table>
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<tr>
<th>CONSTRAINT</th>
<th>MANIFESTATION</th>
<th>POTENTIAL IMPACT</th>
<th>RISK (H, M, L)</th>
<th>MITIGATION STRATEGY</th>
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<tr>
<td>Political environment</td>
<td>Unwillingness of senior politicians and/or senior bureaucrats to support reform implementation</td>
<td>Critical. Inability to effectively implement and/or embed reform. Lack of cooperation or resistance among key stakeholders. Lack of adherence to new processes and procedures.</td>
<td>High. Few reforms will be successful without the commitment of senior levels of government.</td>
<td>Seeking endorsement of political leadership. Raising awareness of the benefits of reform. If endorsement is not achieved it may be necessary to defer reform and pursue other priorities that are endorsed and supported by government.</td>
</tr>
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<td>Government and development partner engagement</td>
<td>Reform design is not internally driven.</td>
<td>Reform design is undertaken by development partners and reflects their priorities rather than the governments.</td>
<td>Variable: The risk depends on the extent of commitment and engagement of the government. The less engagement, the higher the risk that development partners will engage in technical assistance that does not reflect the government’s priorities.</td>
<td>Reform initiatives should be tailored to the specific administrative and political circumstances of a country.</td>
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<td>Technical capacity</td>
<td>Staff lack specific competencies to develop and/or support implementation.</td>
<td>Significant. Both short and longer-term impact on the ability to implement the reform.</td>
<td>High. An understanding of the reform, and its application is essential.</td>
<td>Capacity development</td>
</tr>
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<td>Institutional environment</td>
<td>Institutions and/or organizational structures are not sufficient or appropriate for supporting reform implementation</td>
<td>Significant. Inadequate supervision, and workflow management and monitoring</td>
<td>Moderate. It may be possible to establish alternative management and workflow arrangements.</td>
<td>Organizational restructuring to support reform initiative.</td>
</tr>
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<td>ICT systems capacity</td>
<td>The administration lacks systems hardware and software to support reform initiative.</td>
<td>Moderate. Some reforms require more advance systems and software, e.g. FMIS.</td>
<td>Moderate. Manual processes and procedures can be used pending the acquisitions of software and systems.</td>
<td>Development partner support and technical assistance.</td>
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<th>PI</th>
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<th>Main weaknesses identified</th>
<th>Underlying causes</th>
<th>Desired PFM outcomes</th>
<th>Proposed reform and Priority</th>
<th>Constraints to proposed reform</th>
<th>Addressing constraints</th>
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<td>Strengthen fiscal discipline through greater adherence to fiscal targets. Improved predictability of budget allocations to service delivery ministries.</td>
<td>Strengthening macro-fiscal forecasting (high) Implementing cash flow forecasting (medium) Updating budget processes and procedures (high)</td>
<td>Lack of capacity in economic modeling and analysis. Political interference in setting macro-fiscal projections. Unwillingness of line ministries to adhere to budget processes and procedures</td>
<td>Recruitment and training of macro-economists. Strengthening the legal framework underpinning budget planning and preparation.</td>
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### PI-1

**Aggregate expenditure outturns exceed original budget by more than 20% in last three years**

- **Underlying causes**
  - Overoptimistic economic and fiscal projection;
  - Unavailability of economic and fiscal forecasting models;
  - Lack of capacity in economic and fiscal forecasting;
  - Political involvement in setting fiscal projections

**Desired PFM outcomes**

- Strengthen fiscal discipline through greater adherence to fiscal targets.
- Improved predictability of budget allocations to service delivery ministries.

**Proposed reform and Priority**

- Strengthening macro-fiscal forecasting (high)
- Implementing cash flow forecasting (medium)
- Updating budget processes and procedures (high)

**Constraints to proposed reform**

- Lack of capacity in economic modeling and analysis.
- Political interference in setting macro-fiscal projections.
- Unwillingness of line ministries to adhere to budget processes and procedures

**Addressing constraints**

- Recruitment and training of macro-economists.
- Strengthening the legal framework underpinning budget planning and preparation.

### PI-2.2

**Significant variation in budget composition by function undermining the predictability and availability of budget allocations to key service delivery agencies.**

- Underlying causes
  - Lack of capacity in economic and fiscal forecasting
  - Political involvement in setting fiscal projections

- Desired PFM outcomes

- Proposed reform and Priority

- Constraints to proposed reform

- Addressing constraints
Stage 6: Implement reforms or reform action plans

• What are the actions, deliverables, responsibilities and timelines required to successfully implement the reform initiatives?

• Developing a PFM reform plan
  • Desired outcome
  • PFM reform
  • Key tasks/actions
  • Responsibilities
  • Timeframe
  • Outputs
  • Capacity needs
  • Cost implications
Stage 7: Monitor and evaluate reform implementation

• Are reforms being implemented?

• What are the next steps for reform?

• Has reform had the desired impact on the identified problem?

• Continuous process
  • Learning
  • Adjusting

• Accountability

• Impact evaluation
# Key elements of a PFM reform plan

<table>
<thead>
<tr>
<th>Desired Outcome</th>
<th>PFM Reform</th>
<th>Key Tasks/Actions</th>
<th>Responsibility</th>
<th>Time Frame</th>
<th>Key Milestones/Outputs</th>
<th>Capacity Development Needs</th>
<th>Cost and Funding Source</th>
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<tr>
<td><strong>State the govt's intended outcomes</strong></td>
<td>Specify the reform priorities or initiatives</td>
<td>Set out the individual tasks required to implement the reform</td>
<td>Identify institutional and individual responsibility for completion of each task</td>
<td>Set out the deadline for each task</td>
<td>Identify milestones</td>
<td>Set out required capacity development needs</td>
<td>Estimate cost and funding source</td>
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*PEFA*
Key lessons

• A PEFA report will highlight PFM strengths and weaknesses
• But further analysis may be required to understand underlying causes
• Important to define desired PFM outcomes but also be aware of potential constraints to reform
• Prioritization and sequencing of reform needs to take into account specific country circumstances
• Important to continually monitor progress impact of PFM reforms
Learn more about PEFA

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