

LEGISLATIVE ALERT

Vol.01 No.10 ISSN 0855-2452 A Publication of the Institute of Economic Affairs --- October 2001

THE MEDIUM TERM EXPENDITURE FRAMEWORK: A CASE STUDY OF GHANA

by

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Rationale for Ghana's MTEF

This paper evaluates the MTEF budgetary process based on Ghana's experience. It highlights the strengths and weaknesses of the MTEF in the Ghanaian context and makes recommendations for improvement.

The MTEF was introduced in Ghana to provide a tool for better deficit management through realistic revenue projections, and to identify priority objects of expenditure. Prior to its introduction in 1998, Public Expenditure Reviews (PERs) undertaken in 1993, 1994 and 1995 had revealed that the policy objectives and priorities spelled out in the government's development plans did not find expression in the annual budgets. Furthermore, the old budgetary process did not link the achievements of the objectives of Ministries Departments and Agencies (MDAs) to the level of available resources. Moreover, there was little attempt to re-prioritize activities as resources declined. As a result, low priority activities were accorded the same level of fiscal importance as high

priority activities. In addition, the classification of the budget did not indicate the purpose of expenditures (e.g., provision of extension services) but only types of expenditure (e.g., traveling); this made it difficult to evaluate the cost effectiveness of expenditures.

Although attempts had been made to address several of the above problems through the preparation of Sector Investment Programs (SIPs) in the Roads, Health and Education sectors in Ghana, such programs are sector specific and hence, do not take into account inter-sectoral trade-offs. The MTEF approach takes the SIP process a few steps further by taking into explicit account inter- and intra-sectoral trade-offs and links, sectoral choices to an albeit rudimentary macroeconomic framework that provides an indication of the overall resource envelope.

The MTEF Budgeting Process in Ghana

The MTEF process in Ghana is both a *top down* and *bottom up* process. It is a top down process because the Ministry of Finance

Legislative Alert is a monthly publication of the Institute of Economic Affairs, Ghana, a non-profit research institute and co-sponsored by the Center for International Private Enterprise in Washington D.C., U.S.A. and DANIDA, Ghana. Subscriptions to **Legislative Alert** are made available to those who make contributions to the IEA. Address all correspondence to: The Editor, Institute of Economic Affairs, P.O. Box OS 1936, Accra. Tel. 244716 & 7010714.

(MoF) estimates the total resources available and cabinet decides how these resources should be allocated between the five broad sectors based on government priorities.

MTEF can also be described as bottom up because MDAs in the preparation of their Strategic Plans estimate the actual requirements or inputs needed to realize their sectoral objectives. The top down process of allocating resources to MDAs is guided by a policy review process, where the MDAs review their strategic plans and policies in the context of the total resource envelope. Following the policy hearings, sectoral ceilings are developed and communicated to all MDAs in the Budget Guidelines, which indicate the total resources to be available for the forthcoming three years, including donor resources.

The Macroeconomic Framework

The budgetary allocation process begins with the Ministry of Finance (MoF) formulating the macro-economic framework. It was originally envisaged that a macro-economic model would be employed to estimate the total resource envelope, taking into account relevant variables including GDP growth, inflation rates, money supply growth etc.,. The operational reality is that the macro-economic model is yet to be employed in estimating the resource envelope. Currently, the estimation of the "revenue envelope" is based on incremental projections by the Ministry of Finance, in consultation with the IMF. This narrow interpretation of the macro-framework has resulted in systemic weaknesses in the estimation of MDA expenditure ceilings.

Issues

Resource Envelope is Not Credible

The macro-framework has consistently overestimated the nation's total resource envelope and as a result, actual allocations to MDAs have fallen short of their expenditure ceilings. This development has undermined the credibility of the MTEF process. The absence of an explicit model to estimate the

macro-economic framework is a key reason for this development.

Internally Generated Funds and Earmarked Donor Funds not Captured

Contributing to the poor estimation of the resource envelope is the failure to accurately report MDAs' "internally generated funds" and donor funding. Substantial components of "earmarked" donor assistance and internally generated funds are not captured in MTEF. A major reason for this trend is the concern by MDAs that full disclosure would lead to a corresponding reduction in their share of Government of Ghana (GoG) funds. However, failure to include all elements of funding within MTEF obviously compromises Government's ability to frame a comprehensive and consistent planning and budget process.

Forecasting inaccuracies have also been exacerbated by the failure to plan for external shocks. In particular, Ghana's macro-economic indicators took a turn for the worse in the mid-1999, as the economy suffered from the adverse shocks of rising crude oil prices and declining prices of her major commodity exports. The grave situation was further compounded by delays in donor disbursements, which account for a significant portion (almost a third) of total discretionary expenditure. These trends resulted in slower than projected increases in both expenditure and revenue.

In sum, difficulties in estimating the total resource envelope invariably undermine the credibility of the sector ceilings and consequently, the ability of MDAs to fund the activities necessary for the realization of their objectives. This can in turn breed frustration among MDAs by undermining the credibility and, consequently, the successful implementation of the MDAs' program of activities.

Setting MDA Ceilings

The MTEF process stipulates ceilings for MDAs in the broad sectors of Administration,

Economic Services, Infrastructure Services, Social Services and Public Safety. The indicative ceiling for MDAs for the three-year period includes total (i.e., both recurrent and development and both donor and Government of Ghana) expenditures, and is apportioned between the various cost centers (i.e., the level or place where the budget is prepared and managed: Departments, Divisions, Regions, and Agencies).

Issues

Prioritizing Allocations

MDA budgets for investment, services and to a lesser extent personnel emoluments are the first to be cut when revenue ceilings are not realized. With the exception of personnel emoluments, disbursements to MDAs were below their sectoral ceilings in both 2000 and 1999. In 1999 for instance, MDAs only received their allocations for the first two quarters of the year. The situation was worse in 2000 when they only received allocations for just one quarter. In some cases, the timing of the release was so late as to be counter-productive. For instance, in the case of the agricultural sector, where the timing of releases is crucial due to the agricultural cycle, the erratic disbursement of funds to MDAs seriously undermines the realization of sectoral objectives.

Monitoring

Furthermore, monitoring of the MTEF process has been constrained by the lack of funds since MDAs charged with monitoring responsibilities, have also been under-funded or have received their funds in a period when the effectiveness of their monitoring is compromised.

Defining Missions, Objectives, Outputs and Activities

Prior to the MTEF, program proposals from the sector ministries tended to be mere extensions of past programs, which had nothing to do with new approved policy issues under

the national development framework. However, under the MTEF process, MDAs use a strategic planning approach to define their mission, objectives, outputs and activities. The overall goal, mission and objectives of an MDA must however, fit into the national goals and objectives as articulated by the NDPC.

Issues

Superficial Links Between National Goals and Sectoral Plans

The operational reality however, is that there has been little horizontal coordination of effort between the NDPC and the MOF. The MTEF process appears to be controlled by the MOF, leaving the NDPC effectively sidelined. One possible reason for this development is that although the strategic plans of the MDAs were supposed to be formulated in the context of sector plans developed by NDPC, these plans were not available at the time that the MTEF initiative was being implemented. As a result, the sector plans from the MDAs have tended to be inconsistent or only superficially linked with the sectoral plans articulated in the national planning document formulated by the NDPC.

Limited Prioritization

There are also indications that MDAs lack flexibility, within any given year, in re-allocating resources to reflect changing priorities arising out of funding and other related shocks. The rigidities apply largely in respect of prioritization within the spending categories (or items) of "services" and "investments". Furthermore, as alluded to in the previous section, prioritization is done largely across items of expenditure (i.e., personnel emoluments, administration, services and investment). Because expenditures on personnel and emoluments are "non-negotiable", this item of expenditure receives the highest priority followed by expenditures on administration. To the extent that personnel emoluments account for almost half of total discretionary expenditures, there is very little left, by way of resources, for strategic planning.

Costing of Activities

In line with MTEF, the Government of Ghana moved the budgeting process from an incremental regime to an explicit focus on costing of activities and policies. Originally, the intention was to restrict the introduction of the costing part of the MTEF process to three pilot Ministries: Health, Education, and Roads and Transport. However, the response of the MDAs was presumably so enthusiastic that this component was extended to all ministries. Consequently, all ministries were trained to produce three-year estimates, and all ministries prepared their 1999 expenditure estimates in the MTEF format.

Issues

Concentration of Costing in a Few Centers

There are however, some constraints that have arisen with respect to computerized costing in Ghana. The country currently uses the ACTIVATE software for costing MDA activities. However, due to funding limitations, there are currently not enough computers, software licenses or trained users of the software for each MDA to undertake its own computerized costing activities at their respective cost centers. Consequently, with the exception of a handful of ministries with access to the software as part of a pilot programme (Health, Agriculture, Education, Roads and Transport, Defense, the Office of the President), costing is being undertaken at a few central locations. The goal is to expand access to the software in future.

Logistics and Delays in Costing

Besides overburdening personnel at the designated central locations, the current situation also slows the budgeting process and may increase the tendency for errors in data entry, since only a few central locations are responsible for coding information from several cost centers. The process is further slowed down because expenditure estimates/returns at the regional and district levels are physically transported to the MDAs in the

capital for coding. This is a result of inadequate computer facilities and the absence of a computer network linking the MDAs in the various regions and districts.

Cost Effectiveness

Most importantly, the amount of time and effort devoted to detailed costing appears disproportionate to the benefit gained from the process, especially given the unpredictable funding for service and investment activities.

Budget Classification and Integration

Ghana's MTEF reclassified the pre-existing nine expenditure categories into four broad areas to ensure greater transparency in the functional allocation of funds. The four categories are personnel and emoluments (item 1), administration (item 2), services (item 3) and investment (item 4). Currently, unlike items 3-4, overhead costs (items 1-2) are not linked directly to the objectives of respective MDAs due to methodological difficulties in attributing or mapping various aspects of such costs to specific objectives.

Issues

Mapping Overhead Expenditures to Poverty Reduction

It is expected that over time, consideration will be given to linking items 1-2 to their corresponding objectives. However, until this is done, identifying the components of wages and administrative costs that are devoted to poverty reduction will be impossible. As poverty monitoring gains prominence in the context of initiatives to minimize its incidence, such information will be vital for assessing the country's progress in achieving its poverty benchmarks.

Identifying Productive Investments

The "investment" category is too highly aggregated to distinguish investment activities that are directly productive from expenditures on social infrastructure. At present, this

distinction is only implicit and can only be inferred from the investment objective. However when objectives are too broadly defined, it is difficult to make such inferences.

Accomplishments of the MTEF in Ghana

The MTEF process in Ghana has yielded some notable achievements. It has been associated with an increased coverage of donor funds in the budget, despite the lapses discussed above. Prior to the MTEF, a substantial portion of donor funds was not captured in the budget. The initiative has also transformed the MoF's role from detailed control of line items to one of ensuring that MDAs allocate and use their resources in line with their stated objectives and priorities. The Development and Recurrent Budgets have been integrated as a result of MTEF. Operationally, this was accomplished through the merger of the Budget Division (responsible for the recurrent budget) and the Investment Policy Analysis Division (responsible for the development budget). Furthermore, the process has resulted in increased emphasis by MDAs on performance through the achievement of objectives and production of outputs. Concurrently, the new initiative has facilitated the devolution of responsibility for budget preparation and management down to the cost center level. This has nurtured a participatory approach to budgeting.

Challenges of Ghana's MTEF

On the other hand, the MTEF has also experienced constraints. Besides issues relating to poor coordination, weaknesses in quantifying the resource envelope, and resource constraints relating to costing discussed above, the MTEF process in Ghana has had other problems. For instance, the process has been described as very technical, time-consuming, and not easily internalized by the implementing bodies. This issue raises the question of whether the process is worth the effort, particularly in the context of unpredictable resource flows and limited human resource capacity.

The training period for the MTEF process was also inadequate. While it took approximately three weeks to train the facilitators of the MTEF process, the subsequent training of the MDAs by the facilitators only lasted three days.

The links between policy objectives set out in the medium term development plan and the budget priorities costed by MDAs, tend to be superficial. This may persist in the absence of effective monitoring and coordination between the planning and budgetary institutions.

Lessons from Ghana's Experience

Budgeting and Planning Ministries Must Collaborate

Ghana's experience with MTEF has generated several useful lessons. Key among these lessons is the importance of harmonizing national goals and objectives with the objectives and policies of MDAs. To this end, institutions responsible for the formulation and articulation of national plans must work closely with the institution charged with budgetary allocations. Since MDAs view the MoF as their source of funds, they are more likely to shift their allegiance to the MoF in the event of deterioration in relations between the planning institution (NDPC) and the MoF.

Resource Envelope Must be Credible

Furthermore, Ghana's experience shows that the failure of the macro-framework to provide realistic estimates of the resource envelope breeds frustration and undermines the credibility of the MTEF process. There is the need to maintain credibility, by ensuring that budgetary ceilings are realistic, and that resource flows are predictable. This will involve cooperation of donors in respect of the speed at which they disburse committed funds; greater transparency in the disclosure of both donor and internally-generated funds; and improvements in accuracy at the level of macro-economic modeling.

To reduce the budgetary impact of external shocks, the government could set up a

contingency fund exclusively for the purpose of addressing any over-estimation of the resource envelope. Furthermore, to avoid the possibility of the contingency fund degenerating into a “slush” fund, there must be explicit rules for its allocation.

Rushing Reforms May be Counterproductive

Another lesson from the Ghanaian experience with MTEF is that sweeping reforms must be implemented gradually if they are to be effective. The rapid introduction of the MTEF process has compromised the quality of implementation, as reflected in the formulation of strategic plans. The key reason is that the technical complexity of the process requires that more time is needed for it to be internalized. In this regard, it was not unusual for MDAs to “appropriate” mission statements and objectives directly from training manuals, even where they were irrelevant to their mandate. This places a greater burden on the Policy Review aspect of the MTEF process, particularly with respect to line ministries, which may have had difficulties internalizing the new thinking.

MTEF Needs Planners as Well as Accountants

These developments highlight the importance of cultivating and nurturing a cadre of planners

at the line ministries, to lead the strategic planning process. Accountants, normally in charge of the old budgeting process, are not well suited to assume the role of planners required by the MTEF process.

Effective Monitoring is Imperative

Ghana’s MTEF experience also highlights the importance of monitoring budgetary outcomes to ensure consistency in at least two levels: internal consistency between MDA activities and outputs and their stated goals and objectives; consistency between MDA goals and objectives and national goals and objectives.

In conclusion, it is important to note that, unless addressed, the identified weaknesses in Ghana’s implementation of MTEF will be magnified when the country attempts to implement the poverty reduction strategy through the MTEF process. Will the goals and objectives of the Ghana Poverty Reduction Strategy (GPRS) be effectively captured in the MDA strategic plans, and to the extent that they are captured, will the links between activities and outputs of the MDAs have substantive or merely superficial links with the GPRS?

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