The Limits of Institutional Reform in Development

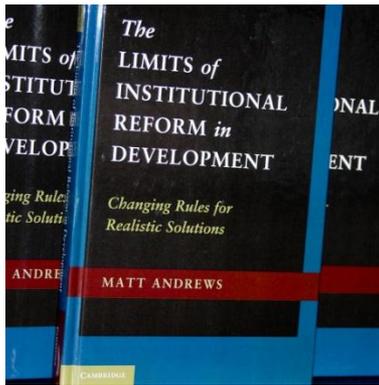Matt Andrews

Harvard University

Startling evidence

- Institutional reform is pervasive
  - Billions of dollars, thousands of projects, all countries
- Reforms reflect a common model
  - Business-friendly, disciplined, modern states
  - Built on best practice
  - Reflect in indicators
- But results are not common, and often disappoint
  - Donors own indicators show 40-70% failure rate
  - And 'successes' come with implementation gaps
    - Laws etc. exist but do not function
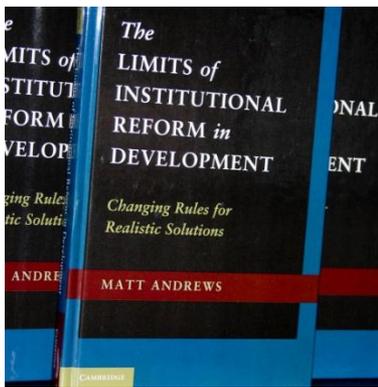
A new explanation

- Old excuses don't explain the limited results
  - Countries did what they were told, through mostly successful projects; results are not improving with time
  - And we had indicators to guide, motivate, monitor
- A new explanation: reforms as signals
  - Institutional reforms introduced to get credibility
    - Move money, improve indicators
  - But this is a short-run gain with negative long-run implications
    - Reforms cannot be implemented, and problems persist
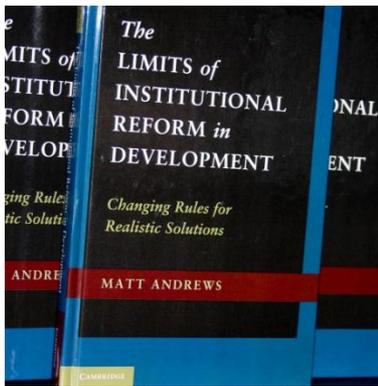
The problem with reforms as signals

- They are adopted with little reflection on context
- They promise complex best practices but do not provide all that these practices require
- They involve champions but not the distributed agents who implement the new institutions

They deliver 'results' but 'what you see is not what you get'
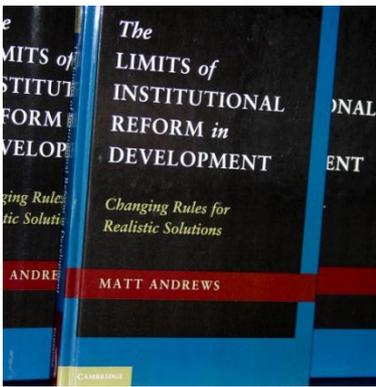
The context problem in a picture: The hole is too small, but dang it I don't care!
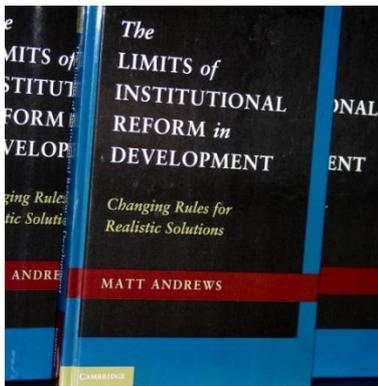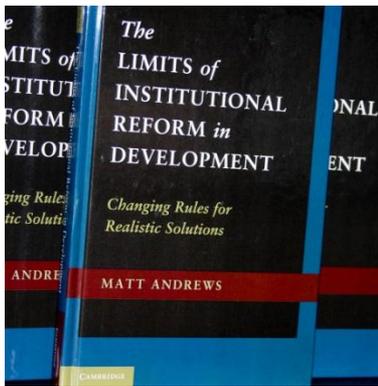
The content problem in a picture

We build a lot of the regulative mechanisms we can see and evaluate

But we do not build the unseen norms and cultural cognitive mechanisms that form the foundation for the new rules of the game

The result: Producing Iceberg Tips
(That sink)

The agency problem in a network diagram

Working from the outside (as agent E)
We emphasize engaging with those who are
Formally at the center of the network in
governments (like the Minister of Finance)
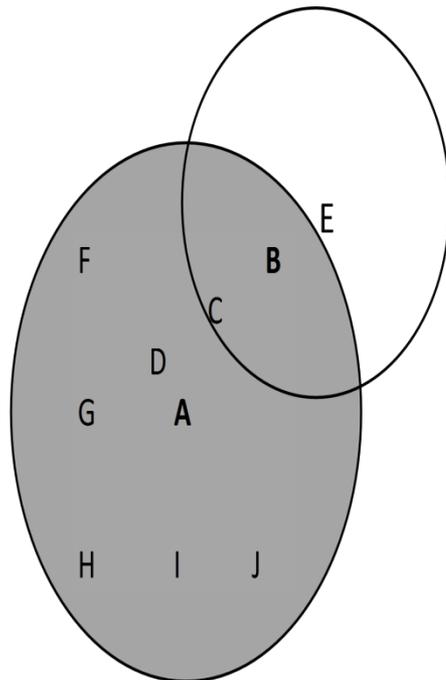
At best this gets access to agent A (but it may
get agent B)

The agents who still need to get engaged are all
over the network, from C to D to F,G,H, I ad J

Failing to engage them means failing to deal
with their opposition, learn about their
contributions, etc.
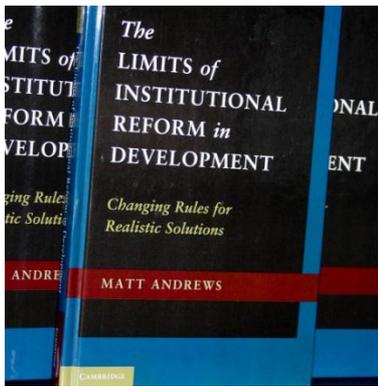
An alternative Problem Driven Iterative Adaptation: PDIA

- Where institutional reforms make governments more functional, they are not adopted as signals
- Rather:
  - They emerge in response to problems
  - Through iterative processes of experimentation, learning
  - Involving multiple agents
  - Producing hybrids that are locally owned, understood, and implemented
- This is how 'best practice' reforms actually emerged in developing countries
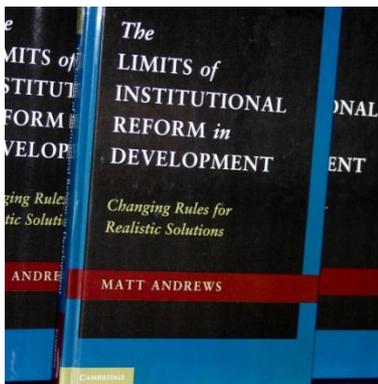
Sweden's story in short

- The country came back from major financial crises in 92
- And implemented a range of reforms: fiscal rules, multi-year budgets, etc.

P110730-1 Source: Convergence Program for Sweden, Govt. Offices of Sweden
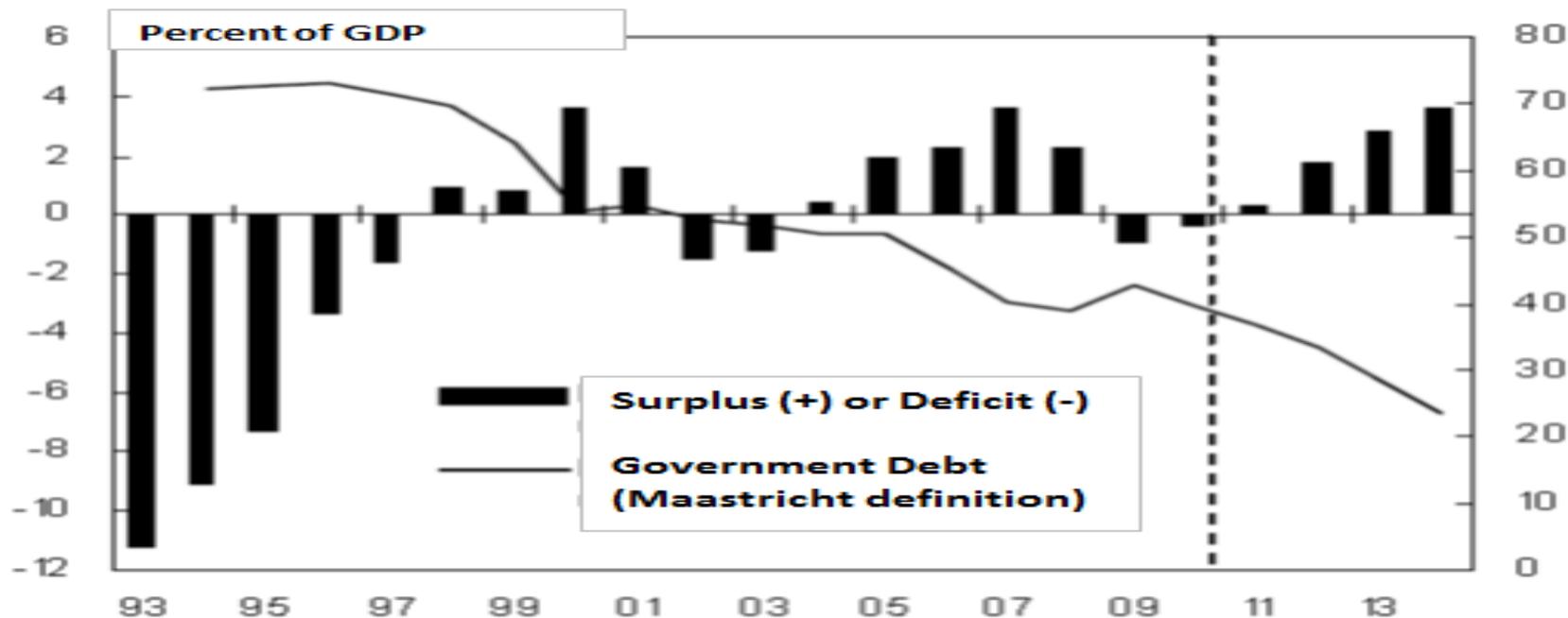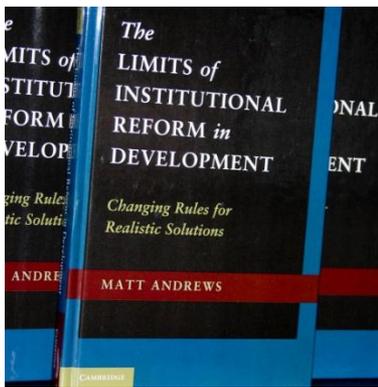
It is so successful that other countries want to learn from the Swedes

- But countries are looking to copy the wrong thing
  - Fiscal rules, multi-year budgets
  - The form….
- Countries like the USA and Ireland have had these forms in place before
  - And they did not work or fell into disuse
  - Because of the context
- **Instead, we should be learning about how Sweden did it**
  - **Choosing reforms that actually worked, with few gaps between form and function**
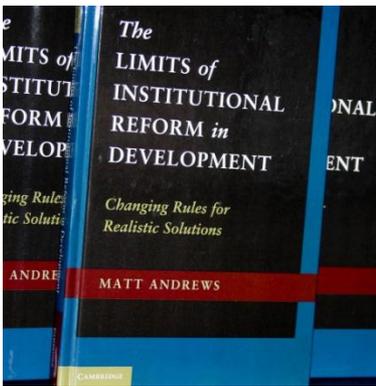
First observations

- From 1960s Sweden was a difficult public financial management (PFM) context
  - Soft budget constraint, lots of spending
 - Growing deficits and growing public sector
- PFM staff were concerned, and tried 'best practice' reforms routinely
  - Program budgeting in the late 1960s
  - Much more in the 1980s
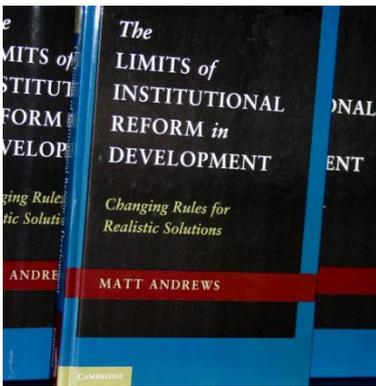
# Mostly lessons of failure in these reforms; and crisis in 1992

- After all these reforms, most PFM specialists believed their system was deeply flawed
  - No budget calendar
  - No procedural authority to the MOF
    - Parliament did what it wanted
  - No expenditure controls
  - No real accounting and reporting mechanisms
- Crisis in 1992 came from financial sector meltdown
  - But the public sector deficit became a noose
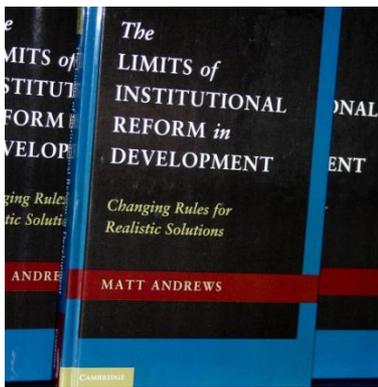
1992 as a crucial point in time

- Government responded with austerity program
  - Cut spending, Deal with banking system, Etc.
- But group of technocrats in the MoF took advantage of the situation and showed that the problem was also related to PFM
  - Using data to show Sweden=2nd worst PFM system in Europe
- The data turned a 'condition' into a political problem that had to be addressed
  - 'We don't want to be like Italy'
  - Minister of Finance made it a central focal point
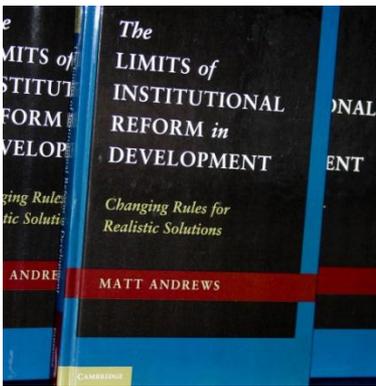
From 1992 to 1997

- Built on many of the ideas from 1980s
  - Note all the ways they 'learned'
- And proceeded through entry points that the 'problem' allowed
  - Budget calendar first, Clarification of local government responsibilities, And others
- Building political support and developing more understanding of what context would allow
  - Experimenting with new ideas like multi-year budgeting, gathering lessons about what works, when and why, adapting and making the 'solutions' work
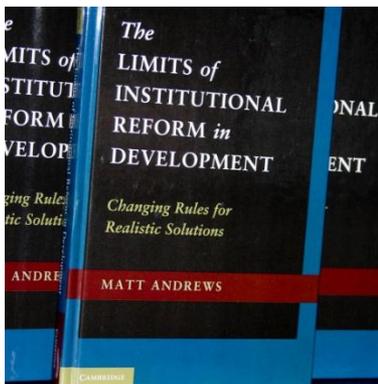
By 1996/1997

- Politicians had seen results from the early steps
  - Problems were being resolved
- Technocrats had a clearer idea of alternatives and had created contextual space to act
  - New laws changing power relationships, New fiscal rules
  - Ceilings, Multi-year framework
- The new reforms could mostly get implemented as they were introduced
  - And they have been expanded thereafter
  - Following a sequence that is driven by problems (a new way of sequencing)
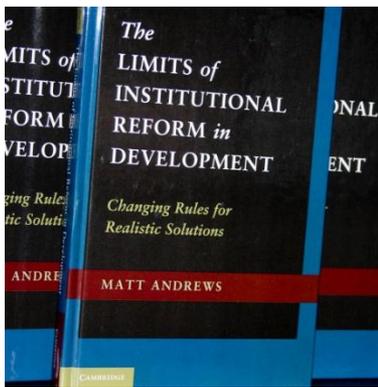
Some Lessons

- Reforms were influenced by context
 - Took off in 1990s when there was disruption… and the incumbent PFM structures were politically discredited…and there were alternatives to build on… and there were a growing group of agents of change
- But reformers used the context
  - Constructed the problem
    - The crisis was about PFM, but they needed to use data to show this…to the politicians (politicizing the reform)
  - They bought in the alternatives (drawing on past lessons, with ideas that other agents had been using)
  - They built the teams and coalitions throughout the public sector and political regime
- In a process that reflects what I call 'purposive' muddling
  - Experiment, learn, adapt…Experiment, learn, adapt
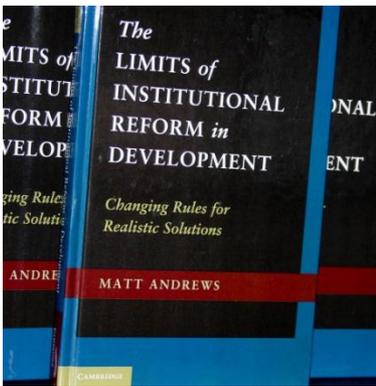
Why problems are an entry point to change

- Prospect theory in economics
  - People accept change at the prospect of loss more than the prospect of gain
- Organizational theory
  - In bureaucracies, risk aversion undermines change
  - You need to show that 'staying where you are' is a bigger risk than 'changing'
- Coalition building in politics
  - Problems are the basis of the coalition development
- But there is a difference between conditions and problems
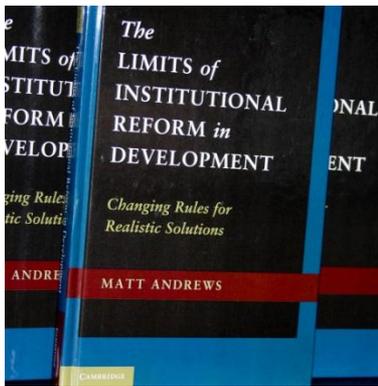
problem driven, iterative adaptation as step by step 'purposive muddling'

The goal:
High functionality
And high legitimacy

More legitimacy
We have improved support after reforms

The problem
In development, muddling is perceived as a negative thing, and learning and adaptation are not encouraged or rewarded

The assumption
Each step allows one to learn and build support and capacity for the next steps...ultimately leading to institutional forms that are legitimate because they are functional
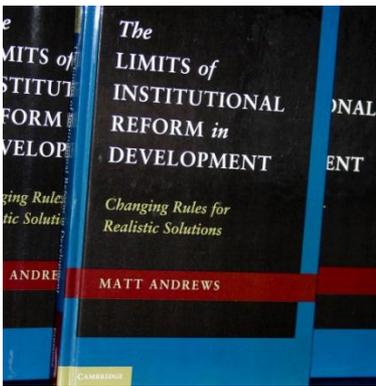
The PDIA strategy
Identify problems and take first experimental steps to get some quick wins. Learn, build support and capacity. Take the next step in a problem drive, iterative process that promotes adaptation.

The starting point:
Low functionality
And low legitimacy

More functionality
Problems are solved after the reforms

Implications for institutional reform in development, and the role of indicators

- Focus on sparking, supporting local change processes
  - Instead of hawking global change products as solutions, draw awareness to problems
- Foster 'purposive muddling' finding and fitting processes
  - Instead of reproducing 'best practice' forms
- Build change communities, not just champions
  - Minister plus team plus academics and beyond

Thank you

Find me at matt_Andrews@hks.harvard.edu

And @governwell on twitter