As the long-term fiscal impact of the global financial crisis begins to bite, aid donors, including the UK Department for International Development (DFID), are pushing harder than ever before for clear evidence on the impact of their aid programmes.

Value for Money (VfM) is the new mantra for aid spending and dominates most aid debates. Motivated by an emphasis on results, donor agencies are reviewing the merits of different aid approaches.

This Project Briefing examines an attempt by the Overseas Development Institute (ODI) to develop and apply a framework to enhance measurement of the net benefits of different options for DFID aid delivery in Malawi: an options appraisal. It looks at why DFID has strengthened its economic appraisal and summarises the methodology and findings from Malawi. Finally, it considers the implications for operational practice and gives recommendations for the design of options appraisals in the future.

Not surprisingly, a recent report on GBS by the UK National Audit Office (NAO) noted that: ‘evidence on the extent to which budget support has yielded better value for money than other ways of delivering aid, or has had an impact on income poverty, is not conclusive’ (NAO, 2008).

As budget support has become the modality of choice for DFID over the past decade, there is a clear need for better evidence on its benefits. The NAO report recommended that DFID should appraise the different options for disbursing aid, assessing the comparative costs, risks and benefits of these options. It called for an ‘options approach’ that would become an integral part of standard DFID appraisals.

Three other developments emerged alongside the NAO recommendations. First, an increased emphasis on quantification in the analysis of different approaches to aid delivery. Second, greater focus on ‘ex ante’ appraisal of interventions to inform future choices. And third, renewed interest from Ministers and domestic oversight bodies to prove that aid spending provides VfM. That focus was clear in the maiden speech of the new UK Secretary of State for International Development and in the UK Public Accounts Committee report on DFID aid to Malawi (Committee of Public Accounts, 2009). In response to the NAO report, DFID published a guidance note on conducting economic appraisals (DFID, 2009).

The purpose of an options appraisal is to evaluate the net costs and benefits, including risks, of one aid modality in comparison with another, in response to a particular development objective. To date, DFID has completed pilot options appraisals in Malawi, Rwanda and Uganda. All three appraisals have tried to apply the new DFID guidance on economic appraisals.
to estimate the net benefits of GBS. Because there is no single DFID methodology, the appraisals were, therefore, successive efforts to develop a more rigorous and credible approach to measuring the benefits and costs of competing options.

**Options appraisal in Malawi**

**The context**

Between 2004/5 and 2008/9, GBS accounted for around one third of DFID’s total aid to Malawi. The proposed programme of Poverty Reduction Budget Support (PRBS) for 2009/10 included £25 million in direct financial support to the Government of Malawi.

ODI was commissioned to appraise this planned intervention against other options. The appraisal aimed to quantify the net benefits of continued GBS from DFID, as compared with providing the same resources in other ways.

**Alternatives to GBS**

The first task was to identify realistic and appropriate ‘options’ as credible alternatives to GBS funding. This was based on consultations with DFID Malawi and other budget support donors participating in Malawi’s Common Approach to Budget Support (CABS) group.

The options, including GBS, were selected on the basis that they would be mutually exclusive and capable of absorbing the entire planned DFID funding allocation for GBS:

- **Option 1** (the ‘base case’) was the continuation of the current rolling annual multi-donor GBS arrangement.
- **Option 2** was additional support to the multi-donor Sector-Wide Approach (SWAp) for health.
- **Option 3** was additional support for the National Water Development Plan (NWDP) via a Trust Fund arrangement with the World Bank.

The option to discontinue GBS and not channel the funds through another instrument – in other words the ‘no aid’ scenario – was not considered.

**Appraisal methodology**

The main question was: ‘Does GBS offer net benefits above and beyond the alternatives?’ The focus was on the marginal costs and benefits of switching DFID funding from the GBS ‘base case’ to each of the other scenarios.

The team mapped out a causal framework for the assumed influence for each scenario on the total volume of financial resources directed to priority areas in the Malawi Growth and Development Strategy (MGDS). The approach drew heavily on cause-and-effect evaluation frameworks for GBS (Lawson and Booth, 2004; IDD and Associates, 2006), DFID guidance on appraising GBS (DFID, 2008) and a recent evaluative review of SBS practices in sub-Saharan Africa (Williamson and Dom, 2010).

The two main challenges – analytical complexity and data gaps – made it difficult to attribute expected changes in net benefits to the use of specific approaches. Important assumptions were made for simplification so that the direction and scale of influence could be estimated. This limited the appraisal to modelling only those effects that could be readily quantified.

Table 1 outlines the five net benefits in the causal framework, and the assumptions against which costs were compared. The expected benefits of GBS that are not readily quantifiable, such as improvements in domestic accountability, ‘pro-poor’ policymaking and public sector capacity, were not fully represented in the analysis.

The analysis was similarly selective for the two sector instruments, and judgements on the expected results linked to each option carry the same limitations.

**Results**

The results show the net effect of switching away from GBS on the overall volume of budget resources allocated to priority areas of the poverty reduction strategy, expressed as a proportion of planned DFID expenditure. Results are shown using a ‘traffic lights’ colour code (Table 2).

It is apparent from the findings, shown in Table 3, that the ‘base case’ option of continuing GBS is preferable, marginally, to options 2 or 3. Switching to those options would have a net cost in terms of changes in priority spending, and shows a rating that is ‘moderately negative’.

This does not mean that GBS is without challenges, but that providing GBS produces incremental gains over and above the possible alternatives. The expectation is that GBS would result in more resources for priority areas of the MGDS after accounting for transaction costs, leakages in the general budget and the interest costs of domestic borrowing.

It is important to note that the analysis draws a distinction between net benefit streams for which there is a good evidence base (termed ‘Category A’), and those where a higher degree of judgement (‘Category B’) is needed. If 'Category B' estimates are excluded the preferred options become 2 and 3.

**Policy implications and lessons learnt**

The results have two clear implications for DFID operations in Malawi. First, the model is sensitive to DFID’s influence, both on minimising leakages and on increasing budget allocations to priority spending areas. This suggests that, to have maximum influence on ‘pro-poor’ spending patterns, GBS should be accompanied by strong and sustained dialogue between donor and recipient government on budget policy and public financial management issues.

Second, if CAB’s influence over allocations and leakages in the general budget increases year on year, rather than remains constant, the results indicate that a three-year GBS programme would become significantly rather than marginally preferable to the other options.
Table 1: Summary of net benefit streams and main assumptions underlying the model used in the Malawi options appraisal

<table>
<thead>
<tr>
<th>Net benefit stream</th>
<th>Assumptions underlying the model</th>
<th>Health SWAp</th>
<th>Water and Irrigation Programme</th>
</tr>
</thead>
<tbody>
<tr>
<td>Government of Malawi budget allocations to priority areas</td>
<td>Although resources allocated through GBS may not be fully used for MGDS priorities, GBS allows the Common Approach to Budget Support (CABS) donors to exert influence on the allocation of the budget to priority areas.</td>
<td>All expenditures allocated through the Health SWAp would be used for MGDS priorities.</td>
<td>All expenditures allocated through the Water and Irrigation project would be used for MGDS priorities.</td>
</tr>
<tr>
<td>Domestic debt and foreign reserves (excluding the costs of worsening debt and foreign reserve situations)</td>
<td>Domestic debt increases when expenditures are allocated to earmarked alternatives (e.g. the Health SWAp and the Water and Irrigation Programme), because unused balances held in accounts for the Health SWAp and the Water and Irrigation Programme cannot be used for Treasury management purposes, in contrast with the central Treasury account used for GBS.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Transaction costs on government and donors</td>
<td>Donors: consultancy costs continue for CABS reviews and related monitoring activities.</td>
<td>Donors: transaction costs associated with existing earmarked alternatives are fixed. As a consequence, the marginal increase in transaction costs from allocating additional resources to these programmes is negligible. Government: although harmonisation under the programme has helped reduce demands on government time and effort, it is unlikely that marginal effects would be significant.</td>
<td></td>
</tr>
<tr>
<td>Expenditure leakages</td>
<td>Level of leakage equivalent to current rate for the Government of Malawi budget. However, GBS allows CABS donors to exert influence on proportion of budget leakage.</td>
<td>Expenditures allocated to earmarked alternatives are subject to lower (or at least no greater) levels of leakage than resources going through GBS into the general budget due to additional procurement oversight.</td>
<td></td>
</tr>
<tr>
<td>Absorptive capacity</td>
<td>There are no significant differences between the absorptive capacity of the three options and resources are fully disbursed. As DFID is already an active partner, no significant gains in health or water and irrigation policy are expected.</td>
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</tr>
</tbody>
</table>

Source: Authors’ own analysis.

Table 2: Impact rates

<table>
<thead>
<tr>
<th>Rating</th>
<th>Highly negative</th>
<th>Moderately negative</th>
<th>Insignificant/neutral</th>
<th>Moderately positive</th>
<th>Highly positive</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net costs/benefits of switching away from GBS as % of DFID expenditure</td>
<td>-25%</td>
<td>-5 to -25%</td>
<td>-5 to +5%</td>
<td>+5 to +25%</td>
<td>&gt; +25%</td>
</tr>
</tbody>
</table>

Source: Authors’ own analysis.

Table 3: Incremental benefits of switching away from GBS as % of DFID expenditure: estimated changes in priority spending if DFID were to quit GBS

<table>
<thead>
<tr>
<th>Net benefit stream</th>
<th>Health SWAp</th>
<th>Water and Irrigation project</th>
</tr>
</thead>
<tbody>
<tr>
<td>Category A</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Government of Malawi allocations to priority areas</td>
<td>Direct &quot;allocative&quot; effect of increased DFID spending in Health and Water and Irrigation</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Direct &quot;allocative&quot; effect of withdrawal of GBS</td>
<td></td>
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<tr>
<td>Domestic debt and foreign reserves</td>
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<tr>
<td>Transaction costs on government and donors</td>
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<tr>
<td>Subtotal (Category A)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Category B</td>
<td></td>
<td></td>
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<tr>
<td>Government of Malawi allocations to priority areas</td>
<td>Indirect effect (CABS influence over budget allocations)</td>
<td></td>
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<tr>
<td>Expenditure leakages</td>
<td>Reduced leakages in the general Government of Malawi budget (CABS influence over the proportion of budget leakage)</td>
<td></td>
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<tr>
<td>Total (Category A and B)</td>
<td></td>
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</tbody>
</table>

Source: Authors’ own analysis.
Methodology trade-off

There is a trade-off in the appraisal methodology between the basic credibility of a comprehensive analysis that includes all assumed costs and benefits and the rigour and reliability of including only those costs and benefits that can be properly measured. This study attempted to follow the second approach, and it became clear that the assumptions used in the model are critical to the overall results.

The most significant benefit comes from the influence of donors on government spending allocations, inherent in GBS. By focusing primarily on quantifiable benefits and trying to avoid implausible assumptions, the model relies on a small number of factors to measure effectiveness. Marginal changes in these assumptions can have a significant impact on the net benefits of the different approaches. This focus on quantifiable results produces only a partial analysis of the net benefits of GBS and risks producing a skewed assessment that may be an unreliable guide for policy decisions. More work is needed, therefore, to understand better and explain more fully the assumptions underlying the analysis.

Ways must also be found to integrate quantitative and qualitative analyses. This would improve the comparison of different aid instruments and demonstrate their effects on priority spending allocations.

Overall, the options appraisal in Malawi has revealed some important assumptions that are crucial for decisions about whether to continue with GBS, as compared with other aid approaches. It also reveals some striking differences in the relative importance of different variables.

This appraisal model for Malawi provides a starting point to determine how to develop a more robust appraisal approach and which data must be included.

Ultimately, the appraisal process itself, and what it tests and exposes, may be as important as the conclusions reached about the net benefits, which are far more difficult to estimate.

References:

Written by Heidi Tavakoli, ODI Research Officer (h.tavakoli@odi.org.uk) and Edward Hedger, ODI Research Fellow (e.hedger@odi.org.uk). The authors acknowledge the invaluable contribution of Nick Highton, former ODI Programme Leader at ODI’s Centre for Aid and Public Expenditure to the research on which this Project Briefing is based and for his comments on the draft.

References and project information

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