The capabilities of finance ministries

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List of acronyms

DST	Deputy Secretary to the Treasury
GDP	gross domestic product
HIC	high-income country
IMF	International Monetary Fund
IT	information technology
LIC	low-income country
MDGs	Millennium Development Goals
MIC	middle-income country
NPM	New Public Management
OECD	Organisation for Economic Co-operation and Development
PEFA	Public Expenditure and Financial Accountability
PFM	public financial management
PPP	purchasing power parity
PS	Permanent Secretary
SOE	state-owned enterprise
UK	United Kingdom
UMIC	upper-middle-income country

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1. Introduction

All countries have a finance ministry. If one organisational feature defines what makes a state a state, it is a central unit that handles income and expenditure – or aspires to. This remains remarkably consistent irrespective of the huge variations in the purpose and institutional shape of government. Finance ministries are also at the centre of many current policy discussions, whether on how to respond to the 2008 financial crisis, how best to fund global development goals, or how an emerging economy should go about establishing a welfare state. Virtually every policy decision that involves the raising and spending of public money involves a finance ministry at some stage. Yet despite their almost self-evident importance, very few studies focused on finance ministries as objects of study.

How do finance ministries go about performing their tasks, what do they look like as organisations, and does it matter how they are organised? What makes a finance ministry capable of doing its job? Is it a strong legal mandate to run public finances as it sees fit? Is it a set of instruments that allow it to run public finance systems according to international best practices? Is it a group of highly trained, well-managed, diligent and dedicated people who keep the rest of the public sector in check? Is it a powerful minister who commands respect in cabinet and can overrule colleagues?

We have investigated these questions using multiple in-depth case studies: Germany, United Kingdom, Mexico, South Africa, Uganda, Nepal, and Sierra Leone. Each of the case studies covers institutional context, organisational features, and fiscal and social outcomes, as well as an analysis of capabilities. The cases were selected not randomly but to provide insights into what capability means in different contexts. Specifically, Uganda, Nepal, and Sierra Leone are all noted for having achieved considerable reform progress under difficult circumstances; South Africa, Germany, UK and Mexico were each considered at different times in the last two decades to be quite successful managers of fiscal performance; and South Africa's National Treasury is a notable case of a newly established ministry successfully taking charge of fiscal policy. The report also draws on detailed country-level case research from Viet Nam and Chile.

2. What is a capable ministry of finance?

Capability is more than capacity, defined as the total resource endowment of people and money, and manifests itself only in how it performs its tasks. Many reasonably well-endowed organisations fail to turn capacity into performance, while some manage to perform well on the basis of very scarce capacity. Underlying each task or function are four generic capabilities that, in varied combinations, make up an organisation's capability to perform these functions. These are (1) analytical, (2) delivery, (3) coordinative and (4) regulatory:

1. **Analytical capability**: the ability to understand and analyse information and research in order to inform decisions. In the case of finance ministries, this capability is in frequent demand in the recurrent formulation of all aspects of fiscal policy, as well as numerous more specific policy issues regarding the financial aspects of government activities. Many finance ministries pride themselves on the ability of their staff to master new policy briefs and counter the sectoral expertise of the ministries with which it negotiates funds. This capability is traditionally at the centre of many international efforts to provide technical assistance in developing countries, where the belief persists that better forecasting capability alone leads to more sensible fiscal policy.
2. **Delivery capability**: the ability to produce goods and services and get things done. For a central ministry that does not directly provide public services, this capability is less important than it would be in, say, the post office. Almost every finance ministry does, however, produce a set of landmark deliverables each year, in particular a complete budget according to (in most countries) a specific calendar. There are also more administrative tasks, such as revenue collection and cash management, which essentially rely on the ability to produce certain outputs – and often funding – across government.
3. **Coordinative capability**: the ability to orchestrate the activities of different actors in pursuit of a common objective. Coordination is a critical function of a finance ministry from its location at the centre of government. A vast range of policy activities can come together only if the finance ministry is able to assemble and use

specialist inputs from other ministries and bodies as well as non-government actors. Again, the best example is the setting of fiscal policy culminating in formulating the annual budget. This could not be achieved in a modern government without the organisation of vastly complex procedures involving many different actors who have to deliver, analyse and move along many components before the budget is complete.

4. **Regulatory capability**: the ability to control the production of particular services provided by others. Salient regulatory domains for many finance ministries include the oversight of state-owned enterprises (SOEs) and financial markets, but in a broader sense, regulation is also involved when finance ministries set the financial framework of spending ministries. In many countries, the finance ministry also has a major role in overseeing subnational entities in various aspects of public finance including debt management, performance management and fiscal aggregates. In countries heavily influenced by New Public Management (NPM), governments have sought to retreat from the direct provision of goods and services towards a more regulatory stance, which has affected finance ministries in various ways. Notably, it has led to a substantial increase in subordinate agencies reporting to finance ministries, accompanied by a downsizing of those ministries.

Finance ministries cannot perform their functions in isolation given that they are in charge of but seldom spend public money. The vast bulk of government financial operations happen elsewhere, so without means of interacting with and reaching into other organisations, it is impossible to exercise control from the centre, however powerful the formal mandate.

Finance ministries in the structure of government

No ministry is independent of the government and the institutions that surround it. This especially applies to finance ministries, which are mandated to exercise broad control over government financial operations rather than having their own expenditure. The relationship between organisation and environment is inevitably complex.

There is generally a strong correlation between per-capita income and virtually any measure of the quality of government. An assessment of capabilities therefore needs to take into account broad income levels. At the same time, the challenges facing the finance ministry also change with income. This was certainly the case historically, but it also seems to apply to countries today. For instance, the allocation choices facing a mature industrial economy with large entitlement programmes, ageing populations and entrenched bureaucratic interests are not the same as those facing a fast-growing middle-income country (MIC) without a fully developed welfare state. Given a certain income level, the precise shape and form of the institutional environment determines how much space a ministry has to develop its functions. Clearly, a weak legislature is much less likely to constrain a finance ministry's ability to set the terms of the fiscal policy process, for good or bad.

Ultimately, these institutional qualities are likely to affect how the ministry of finance is organised and how effectively it can perform its functions. Very rarely is a finance ministry so constrained in its mandate that it would be considered a backwater. Limited mandates on their own also do not make it hard to maintain capability. This seems to be generally true even in countries where the finance ministry has severely constrained powers, such as in the United States. The functional core of the finance ministry always appears to be sufficiently strong to merit a degree of executive attention.

Finance ministries as organisations

Without understanding how finance ministries function as organisations, they tend to be seen as 'black boxes' – poorly defined entities that mediate between the instruments of public finance and the institutional framework. What are the formal responsibilities of the ministry of finance, and what functions are shared with, or delegated to, other institutions? Fragmented functions are not always a sign of institutional weakness or lack of capability. Indeed, for some functions, prevailing global 'good practice' actively encourages separation of powers or responsibilities. This is often done in the spirit of NPM and has long been followed by finance ministries in Anglo-Saxon OECD countries. Delegation to agencies is often intended to achieve more efficient specialised services, such as the use of semi-autonomous revenue agencies and regulatory bodies for the financial sector. There are also cases where functions are split in order to restrain the powers of the central government.

Attribution of responsibilities and organisational arrangements are clearly related. It is reasonable to assume that a finance ministry that collects revenues directly would have more employees than one that does not, perhaps outsourcing to an autonomous revenue authority instead. These forms of delegation are focused on the delivery function of finance ministries, but the operational core of the ministry of finance – made up mostly of the groups and functions responsible for delivering and regulating the national budget – tends to be much more stable and smaller among the case studies. In many countries this is recognised in the voting structure of the appropriation act – with specific votes for departments that deal with revenues, customs, internal audit, treasury and stores, among others – even if formal reporting lines continue to be to the minister or chief administrator of the finance ministry. However, it also dramatically shrinks the size of some finance ministries.

One important factor is how many staff work in particular functions, their education, training and experience. Furthermore, the characteristics of the (senior) civil servant: do they have tenure? Are they promoted on merit? Are the key technical and managerial positions occupied by people who came up through the civil service or from the outside? To what extent is the civil service open or closed, and does that affect the finance ministry? How is the ministry structured: is it a traditional bureaucracy or a more professional organisation? How are the hierarchies organised, and how do professional staff relate to managers?

Despite differences in organisational arrangements there are remarkable similarities. Whatever the staff size, most ministries adopt a four-tiered bureaucratic structure of directorates, departments, units and sub-units. In practice, there also seems to be a limit on the size of a ministry of finance, at least excluding accountants and auditors cadres. Perhaps this indicates a threshold beyond which there is relatively little to be gained by taking on additional staff or doing so exceeds the tolerable opportunity costs for politicians.

Nearly all the ministries studied have found ways to attract and retain essential staff. The larger economies do it predominantly through salaries, while Nepal, Uganda and Sierra Leone use allowances and other benefits (monetary and in-kind) to offer adequate levels of remuneration. This may be a rational reaction to rigid salary and recruitment systems in the civil service more widely, and is supported to some degree by international donors. Unsurprisingly, there are always difficulties in attracting or developing some skills. South Africa's National Treasury must compete with a vibrant financial sector for talented analysts, and has identified upper-middle and lower-upper management skills as particularly challenging to develop internally. In Uganda, the analysis suggests that while it is possible to recruit suitable economists, it is harder to attract those with IT skills.

There is also a strong preference for continuity in leadership and internal promotion. The tenure of recent ministers and top civil servants in most of the ministries studied averages around four years, though some incumbents have exceptional periods in office. The evidence suggests that these ministries rely more prominently on the influence of specific personalities – ministers, top bureaucrats, or even directors – to build the organisation's capability. There is little doubt that such features contribute to more limited institutional capability. So while bureaumetrics are unlikely to be the main drivers of finance ministry capability, they do matter.

3. The evolution of capabilities

Within the broad term of delivery, two functions are worth distinguishing. The central finance function includes a range of administrative delivery functions, where large-scale operational units produce certain products on a regular basis. These are most importantly the administration of tax, customs and other revenues; the administration of cash flows and procurement; and the production of regular reports, audits and other checks on the financial operations of government. Apart from these administrative delivery functions, there is a more complex policy delivery, specifically in the preparation of the budget and related products.

There is a striking difference in the way delivery capability manifests itself in low-income countries (LICs), as opposed to upper-middle-income countries (UMICs) and high-income countries (HICs). For LICs, some aspects of the finance ministry's delivery function pose challenges, whereas in richer countries, delivery is so routine that it seems almost invisible.

As a consequence, many finance ministries tend to start delegating and outsourcing administrative delivery functions. Nearly all of the case-study countries have semi-independent revenue and customs agencies under the ministry of finance, a trend that now extends well beyond the OECD. Germany never had a central tax administration under the finance ministry to begin with, since states and not the federal government collect revenues. Audit and control functions are increasingly delegated to line departments and ministries.

A significant minority of mostly LICs start and conclude budget negotiations much later than the average and submit the budget very shortly before or even after the start of the fiscal year, with negative consequences for its credibility and implementation. Budget crises are not, however, the prerogative of LICs, and especially in the USA a succession of crises, extensions and missed deadlines has almost become the norm. But the ability of the Office of Management and Budget to deliver the budget to the legislature on time is not in question.

The overall trend suggests that administrative delivery capabilities are increasingly outsourced or delegated, and that most ministries of finance have policy delivery capabilities. There seems to be a transition as countries approach UMIC status, at which point these delivery outputs and the capability to run such administrative processes so seldom fail that they are simply assumed to function. There also seems to be a measure of system credibility. As has been observed elsewhere, many weak public financial management (PFM) systems suffer a gap between formal and informal practices, which limits the credibility of the budget and in turn the ability of central ministries to exercise control.

It is reasonable for finance ministries to be reluctant to release control over administrative delivery functions when the credibility of the overall system is in doubt, because it is very closely tied to the flow of funds and therefore the most crucial part of PFM. For ministries at the other end of the spectrum, the distance of administrative delivery from the core policy activities makes these easy functions to delegate.

From analysis to coordination

Finance ministries need to engage in a wide range of analytical activities. The analytical demands broadly fall into four somewhat overlapping categories.

- Aggregate fiscal policy analysis, which is needed to decide the framework of revenues and expenditures, most importantly in the context of budget preparation.
- Specific fiscal policy analysis, which relates to the analysis of particular policy proposals and any short-term issues that may arise during the course of the fiscal year.
- Analysis of departmental spending, both through regular budget negotiations and policy discussions and more tailored reviews of spending requests that reach the ministry of finance.
- Analysis of any other policy or operational question that the finance ministry might take up, which could involve anything from reforms to the accounting system to the rescue of an SOE.

In many LICs, the analytical capability of fiscal policy matters, especially aggregate fiscal policy, is given very high priority. This is understandable for two reasons. Internally, control over aggregate figures underpins many other choices and enables the ministry to control the distribution of resources throughout the government. Externally, international organisations concerned with fiscal sustainability have long invested resources in and paid attention to technical assistance and other forms of support for fiscal analysis capability. From the perspective of a finance ministry in a weak PFM system, developing its fiscal policy analysis capability is a matter of both control and stability in an often-volatile fiscal environment. Outside observers may view this centralising tendency as a source of abuse and long-term instability if the technical objectiveness of the analytical outputs is in doubt.

At the same time, analysis of sectoral policies, very broadly defined, is often weak in LICs. The clearest indicator for the strength of sectoral analysis capabilities is the staff profile in budget departments' sector desks. If the ministry's focus is on achieving and maintaining delivery capability in sectoral spending, then staff often have accounting, legal or administrative training, whereas an emphasis on analytical capability is reflected by employing economists, sector specialists or public policy generalists.

In many HICs and MICs, the tendency is to outsource or share at least some fiscal analysis capability. In part, this is due to the broader international trend of setting up different kinds of fiscal council that take on some form of responsibility for the formulation of aggregate fiscal policy. A related reason is that in countries with very well developed public sources of economic analysis there is less reason to maintain tight control over aggregate fiscal figures because it would be hard to sustain excessive departures from the consensus figures. In Germany, for instance, independent research institutes make macroeconomic forecasts and the government uses the consensus forecast.

Sectoral policy analysis capability, on the other hand, appears as a core function of the finance ministry. Once acquired, this capability is not outsourced or delegated, and investment is maintained even when other functions are shed. In the United Kingdom (UK) the Treasury has been reorganised several times since the mid-1990s, and policy analysis, broadly defined, has become increasingly central to the ministry.

Almost every major function of finance ministries involves coordination. For budget formulation and approval, policy inputs need to be submitted, and positions need to be reconciled and consolidated, so that the resulting draft budget is able to move through the machinery of government. The budget process itself is probably the most consequential and complicated co-ordinative process in government – at least in countries where the budget is a credible indicator of future public spending and government intent. This sets finance ministries apart from many other parts of government, even central government, where core functions can be performed in relative separation.

In LICs, there is often a mismatch between analytical capability and the legal mandate to enforce policy decisions; and the capability to coordinate the performance of central finance functions. In the literature, this has often been cast as the distinction between formal and informal practices, where the latter do not match what the former appear to promise. This divide is of particular concern in countries where the informal budget process is deliberately used to facilitate illicit practices. In several of the case-study countries, however, most public organisations seem to aspire to follow the formal rules of government, but are hampered by the lack of coordinative capability.

Regulatory capability does not refer only to the policy regulation of particular sectors, such as banking and financial sector regulation. For finance ministries it also includes the ability to shape the financial behaviour of other parts of government. This has traditionally been done by command and control, i.e. hierarchical oversight of financial operations, sometimes of one transaction at a time. In such contexts finance ministries do this by supplying a steady flow of financial transaction outputs – approvals, cheques and tenders. When these delivery capabilities are outsourced or delegated, the function of the finance ministry shifts towards regulation. This shift significantly changes the demands on the ministry, as controls disappear and staff are expected to define the operational framework rather than being involved in the details.

The biggest impact on finance ministries of a shift towards regulation is on the number of employees. Existing regulatory agencies as well as more policy-oriented regulatory units employ fewer but more senior staff, as the direct processing of transactions gives way to the setting of guidelines and frameworks. This reduces the number of lower-ranking staff who used to process transactions. At the same time, concerns about a possible identity crisis that might overwhelm budget offices as they let go of detailed control and shift towards policy and regulation seems to be unfounded.

There is a clear difference between LICs on the one hand, and MICs and HICs on the other. Finance ministries in LICs focus more on transactions and control, while those in higher-income countries emphasise policy functions, regulation and coordination. This is broadly consistent with a general OECD-wide trend towards NPM and delegation. The reasons for these changes are complex, reflecting both changing budgeting fashions as well as evolving challenges as countries develop, but also an evolution of capability. For whatever reason, some finance ministries reach a stage where the transactional focus of many delivery functions assumes less importance for the leadership of the ministry, which precipitates a shift towards increasingly policy-oriented analytical, coordinative and regulatory functions.

There is no necessary transition from a control to a policy focus, however. In Western Europe alone, the institutionalisation of policy advice at the centre of government has taken quite different forms. The case studies suggest that finance ministries pay uneven attention to coordination and policy-oriented analysis, and often pay a price for a lack of coordination and for an inability to engage in policy discussion. Especially in aid-dependent countries, much of the policy analysis function is effectively outsourced to international organisations. There does not seem to be any inherent reason for LICs to prevent finance ministries from doing this and investing more in their policy analysis and coordinative capabilities.

What do capabilities mean for policy?

There are no simple lessons for how best to strengthen the capabilities of finance ministries. The findings from the broader literature on institutions, fiscal or otherwise, are highly relevant here. The external environment enables and constrains finance ministries in many different ways. The size and composition of the public sector, as well as the level of economic development, among many other factors, shape the challenges facing the ministry, with important implications for how it engages with the rest of the government. Institutional arrangements, such as the political and electoral system, the balance between the legislature and the executive, and the administrative legacy – create the space in which the ministry operates. This space might be extraordinarily broad and allow a large amount of discretion to the minister and the ministry, as is the case in Chile and the UK. But more often there is a range of constraints that need to be addressed before making any changes to the way the finance ministry operates.

Although it is a truism in international policy discussions, political leadership matters for capability. Most finance ministries see themselves as critical advisers to politicians. The work of the ministry ultimately determines how far any government's political agenda is funded and implemented. Many finance officials point to their ministers as providers of political cover, which enables them to do their work – whether this entails the largely transactional delivery of administrative functions or the provision of policy-driven analysis and coordination. If this political protection fails or the relationship becomes more antagonistic, problems appear quickly and noticeably.

One particularly important factor is the stable tenure of ministers and senior officials. Many finance ministries, at very different income levels, with sustained capability did so under very stable terms in office of both the political leaders and their senior civil servants. In the absence of stable political leadership a consistent senior management group can still provide stability for the organisation to perform and evolve. If the senior management also experiences rapid turnover, capabilities seem to suffer over the long term.

Given a certain degree of institutional space, matters such as organisational structures, pay and other civil service details affect the performance of finance ministries. These issues remain poorly researched. There is very little comparative information on organisational structures, civil service pay, promotions and incentives, and ways in which finance ministries perform their functions to which officials or advisers could turn. In short, finance ministries, especially in LICs, are poorly served by the lack of research and evidence on which to draw. Public administration and organisational research have examined such issues in great detail, and the international PFM community could readily tap into the available research and apply it to ministries of finance.

The findings from this report and from the nascent literature on finance ministries could form the basis of a practical approach to strengthening the capabilities of finance ministries.

Two immediate changes appear particularly worth exploring:

First, a reform agenda, whether it is part of a broader PFM reform plan or specifically tailored towards the finance ministry, should not be narrowly focused on PFM but should draw upon public management research, as well as the broader evidence on government institutions. This might start to fill the 'missing middle' in the current analytical toolkit.

Second, the analyses presented in this report could provide the basis of a capability bottlenecks assessment. A combination of (1) fiscal institutions, (2) central finance functions, (3) organisational structures, and (4) tenure and civil service features could be used to identify the most critical constraints on the ability of a ministry to perform its specific tasks.

There is still the need for a dose of realism because the evidence suggests that finance ministries cannot wholly escape the institutional environment that sustains and constrains them. Nonetheless, they could still position themselves better to make the most of this institutional context.

1. Introduction

Finance ministries are ubiquitous. If there were one organisational feature that defines what makes a state a state, it would have to be a central unit that handles money going in and out – or aspires to. There is a remarkable consistency across time and place, even as the purpose and institutional shape of government varies tremendously. Countries as different as Japan (Hartcher, 1998) and the United Kingdom (UK) (Roseveare, 1969) have finance ministries with origins going back a millennium.

Finance ministries are also at the centre of many current policy discussions, be they on how to respond to the financial crisis of 2008, how best to fund global development goals or how to go about establishing welfare states in emerging economies. Virtually every policy decision that involves the raising and spending of public money involves a finance ministry at some stage. Yet for all their almost self-evident importance, finance ministries as objects of study are curiously absent.

For the most part, analysts look at finance ministries indirectly or when they are at the margins of attention focused elsewhere. Such perspectives provide useful insights but risk missing crucial aspects of how finance ministries work and why they matter. There are broadly three camps of 'not seeing' finance ministries.

The first perspective sees the finance ministry as an invisible helper. This is the case in much of fiscal policy research. Whether fiscal policy matters has been hotly debated since Keynesianism first gained prominence (Blinder and Solow, 1973), and how fiscal policy relates to desirable outcomes such as growth continues to attract attention (Cottarelli and Jaramillo, 2013; Easterly and Rebelo, 1993). These discussions share the assumption that once policy decisions are taken, they will be implemented. Furthermore, when information about better policy choices becomes available, it will be taken into account. A variation of this perspective is often found in media reports on fiscal matters, where it tends to be the minister who takes decisions and drives policy, not the ministry.

In the second view, which is of more recent origin, the finance ministry is a malleable mass. In the fiscal institutions literature, authors have started to investigate how politics and institutions shape the way fiscal policy is made (Hallerberg et al., 2009b; Hallerberg, 2004; Poterba and von Hagen, 1999; von Hagen, 1992, 2004). The idea that governments operate in an environment that enables and constrains them is an important advance. Research into fiscal institutions proposes, for instance, that it is much easier for governments to delegate power to a strong finance ministry in countries with competitive electoral systems that produce single-party governments.

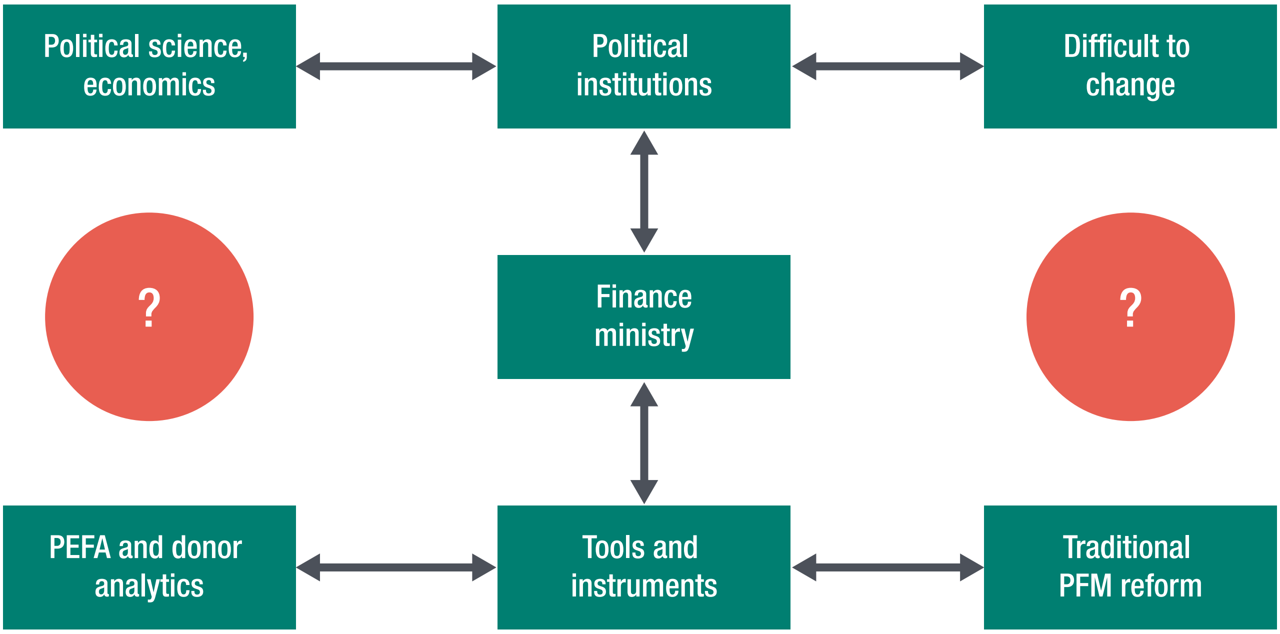
In places where these conditions do not exist, alternative models need to be found: for instance, cross-party agreements to commit to certain fiscal objectives (Hallerberg, 2004). This literature is driven by the theoretical observation that public finances suffer from a common pool problem, whereby everyone in government has an incentive to spend more than the government as a whole should spend. Finance ministries act as a counterbalance. It is this role that explains why they are so common. The nature of the institutions that shape the ministries – what they actually look like – remains unexplained.

The third perspective can be seen in the discussions among public financial management (PFM) practitioners that tend to look at finance ministries as empty shells looking for tools. Proposals for how best to manage public money are abundant, but they take the form of tools and instruments that describe what governments in general and finance ministries should do, but do not offer much insight into what they look like (Brooke, 2003; Holmes, 1998; PEFA Secretariat, 2005). There have been vocal critiques of this body of work in recent years (Andrews, 2010, 2013; Andrews et al., 2014).

The problem with these three perspectives is not that they are wrong or irrelevant as such, but that they are the closest approximations of mainstream research relevant for understanding finance ministries and yet they all fall short of looking at the ministries themselves (see Figure 1). The first two perspectives, which draw directly on academic economics and political science, outline the high-level fiscal and institutional environments within which finance ministries operate. Both environments are very difficult to change in the short run, which limits their direct utility for policy and reform. While it is important to understand external constraints, voting systems and even major fiscal institutions like budget laws do not change very often.

At the other extreme, the literature on tools and instruments is well developed, in terms of both analytical frameworks to assess the status quo, such as Public Expenditure and Financial Accountability (PEFA), and the set of tools and instruments that make up the canon of current PFM reforms. There is, however, a missing middle around finance ministries as organisations, with a dearth of solid analytical literature, let alone a set of operational approaches or advice on how to improve ministries themselves (the first notable exception is Allen et al., 2015).

Figure 1: Finance ministries as the missing middle



Source: Authors

The literature on finance ministries as organisations is surprisingly slim. There is a small body of comparative and conceptual work (Allen et al., 2015; Allen and Krause, 2013; Dressel and Brumby, 2009; Krause, 2009a; Schick, 2001; Wanna et al., 2003), as well as case study material for budget offices or finance ministries in Organisation for Economic Co-operation and Development (OECD) countries (Allen and Kohnert, 2012; Hartcher, 1998; McKinnon, 2003; Tiihonen, 2012; Tomkin, 1998). The UK Treasury in particular has been the subject of several in-depth case studies over the years (Allen, 2014; Heclo and Wildavsky, 1974; Lipsey, 2000; Parry et al., 1997; Roseveare, 1969; Thain and Wright, 1995). These studies provide a starting point for looking at finance ministries more closely, but they do not give systematic answers to the most important questions about them.

How do finance ministries go about performing their tasks, what do they look like as organisations, and does it matter how finance ministries are organised? In particular, what makes a finance ministry capable of doing its job? Is it a strong legal mandate to run public finances as it sees fit? Is it a set of instruments that allow it to run public finance systems according to international best practices? Is it a group of well-trained, well-managed, hardworking, dedicated people who keep the rest of the public sector as much in awe as in check? Is it a powerful minister who commands respect in cabinet and can overrule his colleagues?

This report aims to chart a path in three ways. First, it will situate finance ministries as organisations in the existing body of knowledge on PFM. It will then discuss in detail the organisational features that could matter for the capability of finance ministries. Finally, it will analyse the implications for policy – is this all idle description for description's sake, or does it amount to something of an agenda?

Apart from the available secondary literature, the report relies heavily on publicly available data on fiscal performance and institutions. The core of the empirical foundation is provided by a series of in-depth case studies covering: Germany, UK, Mexico, Chile, South Africa, Uganda, Nepal and Sierra Leone. Each of the case studies covers institutional context, organisational features, and fiscal and social outcomes, as well as an analysis of capabilities. The cases were selected not randomly but to provide insights into what capability means in different contexts. Specifically, Uganda, Nepal and Sierra Leone are all noted for having achieved considerable reform progress under difficult circumstances; South Africa, Germany, UK and Mexico were each considered at different times in the last two decades to be quite successful managers of fiscal performance; and South Africa's National Treasury is a notable case of a newly established ministry successfully taking charge of fiscal policy. The report also draws on detailed country-level case research from Nepal, Viet Nam and Chile.

In other words, each of the cases is considered to have had a degree of success in handling at least some of the important challenges they faced. The findings of this report are not meant to be representative of all countries or to be generalisable, but rather an exploration of how best to approach the capabilities of finance ministries.

2. What is a capable finance ministry?

Much like *obscenity*, *capability* is a term that is hard to define, but it is recognisable: 'I know it when I see it' (Stewart, 1964). In order to approximate the capability of a finance ministry, five discrete areas need to be both defined and connected: (1) the results it would aim to achieve; (2) the institutional context that enables and constrains its operations; (3) its specific functions; (4) its organisational structures and staff; and (5) its ability to actually perform its tasks. Without having a sense of the objective, the space for manoeuvre, and the job description, an analysis of capabilities would remain both narrow and vague. In this section, each of these areas will be discussed in turn.

2.1 The purpose of a central finance function

In a very basic sense, finance ministries are the custodians of public money. They serve to pursue the fiscal policy objectives of the government of the day and ultimately the entire policy agenda, insofar as it relates to the use of public funds. The classic definition of the objectives of public finance proposes three interrelated objectives: the pursuit of aggregate fiscal discipline, allocative efficiency and operational efficiency (Musgrave and Musgrave, 1989; Schick, 1998a). In practice and over time, the emphasis placed on each objective will vary, but none will ever disappear entirely as a concern. It has also long been argued that there is at least an implicit hierarchy and priority to the objectives, whereby fiscal discipline is the first and logically the fundamental priority (Schick, 1966).

In practice, an overriding concern with fiscal discipline and macroeconomic stability is common to all mainstream efforts to define the scope and nature of PFM. This is only logical – once a government is threatened with bankruptcy, concerns with efficiency become moot. Schick makes this argument in the context of US budgetary reforms in the 20th century as well as more broadly about the evolution of budgetary institutions (Schick, 1966, 1998b). In earlier centuries, the institutional evolution of modern finance ministries came about through a constant struggle over the control of the public purse, which, at least in countries influenced by Western Europe, led to modern legislative and executive institutions (Krause, 2013; Wehner, 2010). Fiscal discipline, as defined by the fiscal balance and debt levels, is the easiest objective to measure and define, as it has a direct (though not simple) relationship to what finance ministries do.

This is not to say that operational efficiency is not important. The same impulse towards spending discipline, and similar tools and instruments, drives finance ministries towards pursuing efficient spending, with the ultimate purpose of keeping aggregate spending under control (Hemming, 2013). It is ultimately the purview of spending ministries, departments and agencies – nationally as well as locally – to manage funds efficiently. Change in operational efficiency, let alone the overall state, at any point in time, is notoriously difficult to define and ultimately hinges on a government's ability to measure inputs as well as results.

In practice, efficient allocation is not always at the forefront of budgeting, and its pursuit differs notably depending on the complexity, composition and consistency of public spending. For very long stretches of history, allocation decisions were relatively unimportant for governments because the vast bulk of expenditure was always military. It was not uncommon for 18th-century European governments to dedicate upward of 80% of public spending to the military, much of the rest going to the royal household. Naturally, the central government bureaucracy in charge of public money focused its capabilities on keeping spending under control (Krause, 2013).

In modern government, public spending is vastly more complex, and conflict over allocation decisions – who gets what, when and how – is inherent in the nature of modern politics (Lasswell, 1958). Many mature industrial countries enjoyed periods of long stability during which the allocation process was incremental: predictable annual increases were steadily distributed in an almost ritual fashion (Wildavsky and Caiden, 2004). In the golden age of incrementalism, finance ministries were not known for their innovation. It is only since the period of austerity that affected most OECD countries in the 1970s and 1980s that allocation decisions entered a period of both profound uncertainty and active innovation. As pressure on expenditures from secular trends such as demographic change increased, revenues became more volatile and less bountiful, making incrementalism less viable (Schick, 1983).

This almost permanent state of fiscal stress has been driving a range of innovations in the public sector (many of them associated with the New Public Management) that have affected the role of finance ministries with regard to allocation decisions. For finance ministries, allocation decisions have become a critical part of their function, and many of the recent innovations, such as performance budgeting and medium-term budgeting, are at least in part about better allocation. In 2001, Schick argued that this change was causing an identity crisis of finance ministries in their public spending role, as they retreated from their old control mandate towards an uncertain, performance-oriented future. More than a decade and one global financial crisis later, it seems that many finance ministries have held on quite successfully to their focus on spending discipline. Whether there is an established way of making sound allocation choices under stress is much less clear.

No finance ministry today will be able to disregard a concern for any of the three objectives – priorities in this case are a question of emphasis, not choice. Fiscal discipline (and macroeconomic stability) remains fundamental in a way that the other two objectives are not (Welham and Hadley, 2015), but it is hard to imagine a government doing well for long without an institutionalised concern for allocative efficiency and operational efficiency. Not one of the three is associated with a very clear set of tools and instruments, however. It is very much a question of context and choice around how these objectives are pursued.

2.2 The institutional context: enabler and constraint

As much as the existence of finance ministries seems to be a constant in modern government, their environments vary tremendously. There are many ways to dissect institutional arrangements, from the more formal institutional comparisons that used to dominate political science and economics (Lijphart, 1999; Persson and Tabellini, 2005) to the varieties of capitalism literature (Hall and Soskice, 2001) to more recent work looking at aggregate institutional orders (Acemoglu et al., 2001; North et al., 2009). In any given country, the potential institutional forms relevant for any one government body are limitless, but two of these patterns are particularly relevant for finance ministries. These are the balance of budgetary powers between the legislature and executive and, related to this, the ability of executives to centralise power and delegate it to a finance ministry.

Legislative arrangements are much more varied than the simple distinction between parliamentary and presidential governments suggests. In public finance terms, the authority of the legislature to be involved in budgetary matters can differ a great deal, and this diversity exists amongst both presidential and parliamentary governments. The United States Congress is known to be perhaps the most powerful legislature, where executive budget proposals are mere suggestions that the legislature has both the authority and the capacity to completely redraft if it so chooses. At the other end of the spectrum there is more than one country resembling Chile, where the legislature changes little of what the executive proposes. Similarly, not every parliamentary government follows the Westminster model of the UK. Scandinavian legislatures, for instance, are very powerful and resourceful bodies (Wehner, 2006, 2010).

Figure 2: Legislative budget authority versus executive control

Sources: Wehner (2006) and Krause (2009)

For finance ministries, the balance of power between legislatures and executives is at least in part a zero-sum game (Figure 2). If one branch has the last word on spending, the other cannot have it. This is notwithstanding the important informal and indirect influence that a legislature may wield, for instance via budget committees. But the power of the finance ministry depends on other factors besides the power of the legislature. The literature on fiscal institutions posits that budgeting is driven by a common pool resource problem, by which each government minister has an incentive to spend more money than the government as a whole would be able to raise in taxes without upsetting voters so much that the next election is in peril (Velasco, 1997). The finance ministry serves as the counterbalance to the spending impulses of the rest of government and is empowered by the head of government to enforce spending discipline. In the literature, this is found to work well where governments are more internally coherent (by having either single-party or ideologically coherent coalition governments), where electoral systems produce stable and competitive elections and, for the most part, where legislative budgetary powers are weak (Hallerberg and Marier, 2004; Hallerberg et al., 2009b; Hallerberg, 2004).

The institutional power of a finance ministry can take many forms but is usually seen as its ability to centralise decisions over budgetary matters and exercise control over how other parts of government take budgetary decisions. At least in formal-institutional terms, different indices measuring this power exist for a large number of rich and middle-income countries (MICs) (Hallerberg et al., 2009b; Krause, 2009b; Poterba and von Hagen, 1999; Scartascini and Filc, 2007; von Hagen, 1992). It can be further disaggregated into different kinds of power and authority, for instance whether ministries rely more on hierarchical oversight over individual decisions of budgetary inputs, or whether ministries follow a more delegated approach of controlling the macrobudgetary framework and outcomes (Krause, 2009b, 2012). In practice, the way finance ministries interact with their institutional environments is much more nuanced, through a multitude of both formal mechanisms and informal practices (Hallerberg et al., 2009a, 2009b).

These institutional factors present an important part of what matters for the capabilities of finance ministries. If certain powers are located elsewhere in government, then for all the effort of budget officials, some things just will not work. For instance, trying to maintain a medium-term ceiling on ministerial spending is something a finance ministry can never even try to do on its own if the legislature has the power to increase ministerial allocations. On the other hand, finance ministries can also be tremendously empowered by their institutional environments – as evidenced by the very active reforms carried out in countries where legislatures are weak and executives very centralised, such as Chile or the UK. It is worth noting that the literature on fiscal institutions covers Europe and Latin America reasonably well but the rest of the world very poorly. As a consequence, issues that affect OECD countries only a little but other countries quite a bit – for instance the influence of separate planning ministries on the budget process – are as yet under-studied and poorly understood.

2.3 A portfolio of functions

As deceptively simple as it is to say that finance ministries exercise control over public finances, in practice they have taken on – and often discarded – a broad portfolio of functions. They cover a very varied set of activities (Table 1), which range from the straightforward administrative work of controlling expenditures and managing cash going in and out, via a range of policy functions, to the regulation of banks and oversight of state-owned enterprises (SOEs) (Allen and Krause, 2013).

Table 1: Central finance functions

Macrofiscal forecasting and analysis	Accounting policy
Fiscal policy formulation	Debt management
Fiscal risk analysis	Tax administration
Interface between monetary and fiscal policy	Customs administration
International economic and financial relations	Intergovernmental financial relations
Tax policy	Regulation of banks and other financial institutions
Budget preparation	Management of public assets, including public enterprises
Treasury and cash management	Public procurement
Internal control	Monitoring and management of performance
Internal audit	Strategic planning

Source: Adapted from Allen and Krause (2013)

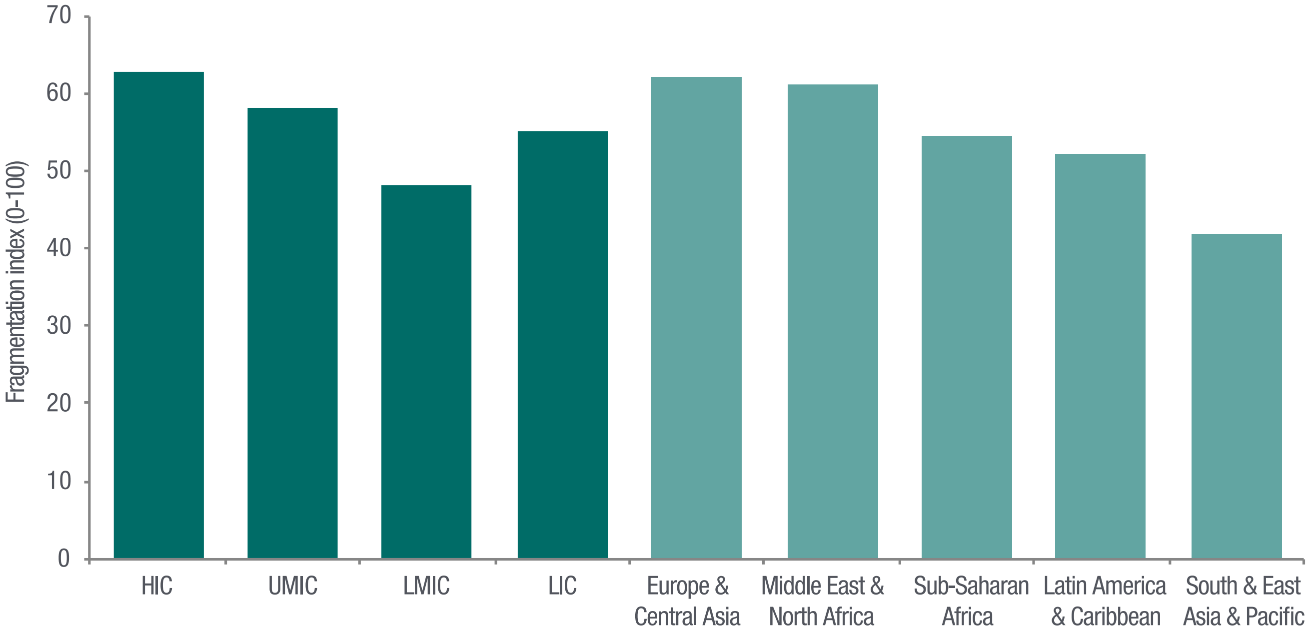
What exactly constitutes a government body carrying out a function is subject to some interpretation. Most straightforwardly, a ministry could either be in sole charge of something or not. However, it is also possible that a function is somehow shared between ministries, either by design or default. Even when the function might lie outside a ministry in another body, that body may be in a subordinate relationship – as is the case with many regulatory bodies or delivery agencies that ultimately report to the ministry of finance.

There does not seem to be much of a regional or income-based pattern to how these functions are distributed. A recent survey showed that, on aggregate, countries were grouped together relatively closely (see Figure 3). The aggregate conceals differences in composition, but the only slight trend seems to be that both high-income countries (HICs) and low-income countries (LICs) display slightly higher degrees of fragmentation, whilst MICs are more concentrated. It also seems that Asia (defined as South, South-East and East Asia, as well as the Pacific Island states) has lower fragmentation than other regions of the world. LICs are relatively fragmented, reflecting perhaps general challenges of institutional coordination and reform in low-capacity environments, but also the political incentives of these environments that actively seek to reduce the prospects for, and impact of, reforms that might strengthen formal rules-based systems of financial governance. This has been characterised as taking the form of 'capricious heads of state' who often deliberately aim to 'divide-and-rule' in expenditure and budgetary governance. Governments centralise initially fragmented functions as they develop over time, and then delegate some functions out to semi-independent agencies in the spirit of the New Public Management (Allen and Grigoli, 2011).

It is important to note that fragmentation of function does not necessarily equate to strength or weakness for a finance ministry. Some areas, such as tax and customs administration, are routinely delegated to agencies in many OECD countries, because their routine nature – as opposed to the associated policy function – is not considered central to the ministry's work. Other functions, such as public procurement, oversight of state-owned enterprises (SOEs) or banking regulation, are very important but are not an integral part of the finance ministry's budgetary role. Its power vis-à-vis spending ministries will not be affected by whether the financial regulator is part of the ministry or not. Other functions, however, clearly are crucial. If the finance ministry does not control budget preparation, either because that role is mostly held by the legislature in collaboration with line ministries or because the capital budget is prepared by a separate planning ministry, one cannot speak of a centralised budget process, with all the associated implications.

For a finance ministry, the precise portfolio of tasks will matter less than how empowered it is to carry them out by its environment, and whether it has the capacity to actually implement everything it is tasked with. A relatively narrowly mandated ministry might be highly capable in performing its functions, whereas another might be endowed with a wide range of functions without being able to do any of them well. The latter is a great risk when international best practices are imported without regard for the capacity to staff and implement new tasks – an important critique to current international reform support (Andrews et al., 2012; Andrews, 2013; Haque et al., 2012; Welham et al., 2013).

Figure 3: Fragmentation of central finance functions



Source: Allen and Grigoli (2011)

2.4 Organisational structures and staff

The structure of an organisation is an important determinant of its capability. The public sector is no exception. There is a large body of literature that analyses bureaucratic form and investigates the links between bureaucratic structure and policy-making (Heclo and Wildavsky, 1974; King and Rothstein, 1993; Weir and Skocpol, 1985; Marier, 2005; Dahlström et al., 2010). Particularly in the 1960s and 1970s, writing on public administration discussed the internal organisational structure of governmental actors and its effects on legitimacy and performance (Pugh et al., 1968). This discussion traces its origins back to Max Weber and his original depiction of an ideal-typical rational bureaucracy driven by formal rules and professional, specialised staff (Weber, 1980 [1921]).

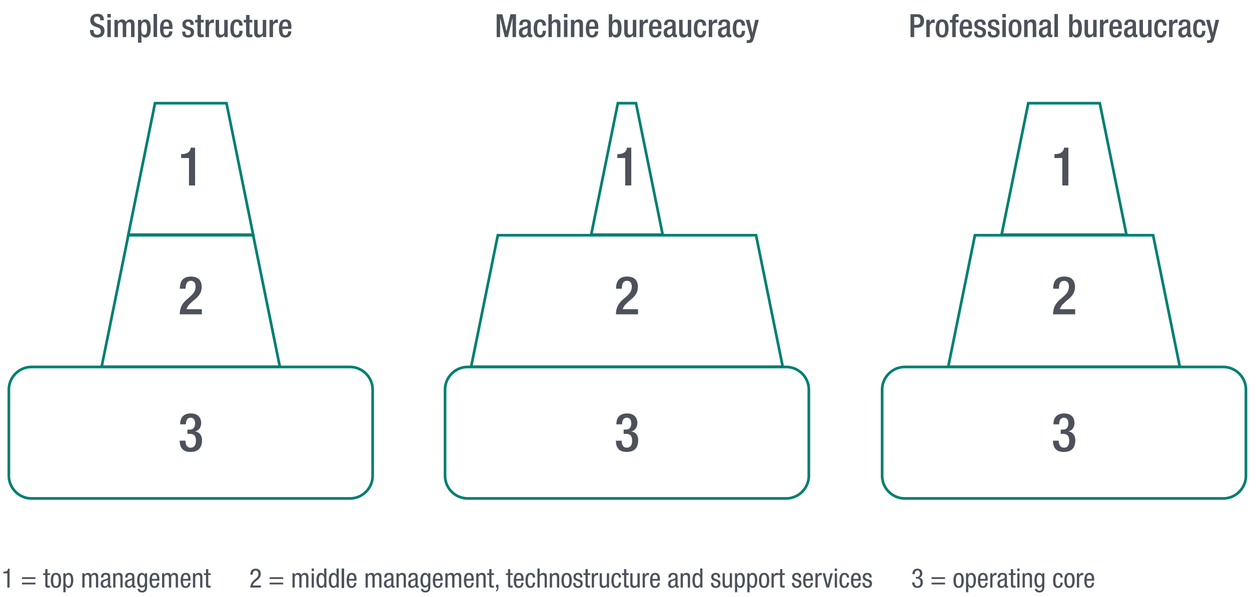
It is fairly uncontroversial that a capable bureaucracy is a crucial ingredient if central governments are to work properly, but there isn't much agreement on precisely what form might be most appropriate, and bureaucratic models differ tremendously between countries and over time. In principle, there are two related questions that arise in the context of organisational structures of finance ministries. First, are there certain features that consistently show themselves to be relevant to organisational capability? Second, are there any features that an organisation needs to take control of at certain stages of development? For public administration in development, the best-known treatment is Schick's warning that developing countries need to 'look before they leapfrog' towards a New Public Management mode of organisation. He proposes both that organisations first need to establish a Weberian foundation of formal rules and bureaucratic stability, and that ultimately a model relying on market mechanisms, delegation and flexibility would be more efficient (Schick, 1998b).

The different challenges they face, the institutional environments they interact with and the precise functions they take on all affect how finance ministries structure themselves internally. This applies both to the potentially most appropriate or effective internal structures and to the dysfunction and problems that could arise in response to external influences. There are three broad dimensions that could usefully be investigated in order to shed light on finance ministries as organisations: the role of the political leadership and the relationship between bureaucracy and politics; organisational structures; and staff roles and pay.

Frequently highlighted in the literature on public administration is the degree to which the civil service is influenced by politicians. For the finance and economics portfolio, autonomous and politically shielded but technically capable bureaucracies have long been discussed in the context of states' ability to facilitate growth and successfully implement macroeconomic policies (Whitfield, 2011). On the other hand, there is also a need to ensure accountability – by being responsive to elected politicians or by hiring staff who are representative of the society they serve. The final compromise between the opposing objectives of independence and accountability is a key feature of public bureaucracy.

There are many different ways to analyse the structure of organisations. One influential typology identifies, among others, three ideal types of organisational structure (Mintzberg, 1979 – see Figure 4). In each case, the organisation has three broadly defined parts: it is led by its top management; its actual day-to-day functions are

Figure 4: Typology of organisations



Source: Adapted from Mintzberg (1979)

carried out by the operating core, where the rank-and-file staff are found; and these two parts are intermediated by middle management, support units (IT, catering and facilities) and the technostructure (the part in charge of standardising the operations of others, such as human resources, audit and compliance, and legal).

The first ideal type is the 'simple structure', where few support units and other back-office functions exist. Coordination typically occurs in the form of direct supervision between senior managers and staff, with little differentiation and specialisation. The key part of the organisation is the top management, where important decisions are centralised. The organisation is usually so simple that a single person, or group of people, can stay in more or less direct charge of the day-to-day operations of the organisation. In public finance, this is the stereotypical finance ministry in a very small or very poor country, where bureaucratic structures are simple because a more complex organisation could not be supported.

The second ideal type is the 'machine bureaucracy', which resembles the classic image of a sophisticated, and cumbersome, bureaucracy. The operating core consists of large and specialised units, driven by detailed formal procedures and rules. Coordination takes place by standardisation of processes, and the middle layer of the organisation is the key part of the organisation. All the different possible compliance and oversight functions are very well developed and located within the organisational structure. Staff in the operating core have little discretion over how to approach their work, and they follow the rules and standards laid out for them. Top managers are quite far removed from the operational activities of the rank and file. In many ways this is the typical image of any traditional government ministry, especially in continental European countries. One can easily imagine a finance ministry operating as a machine bureaucracy, where staff are concerned with controlling inputs, processing financial operations, and other simple tasks, overseen by a large hierarchy of managers and controllers.

The third type is the 'professional bureaucracy', which relies not on the standardisation of procedures but on highly developed skills. The operational work is carried out by specialists who are given considerable discretion in how they pursue their goals and objectives. It is therefore a much leaner and flatter organisation, where the operating core emerges as key. The middle layer of the organisation is smaller and simpler, as fewer support units are held in-house and fewer compliance and supervision mechanisms are needed. In principle, this is the image of a finance ministry after having gone through New Public Management reforms, where routine tasks and functions are outsourced or delegated and the ministry is left to focus on its macrobudgetary and policy roles.

2.5 Capability as the ability to perform

Ultimately, the institutional context, portfolio of functions and organisational structures will not have much bearing on any kind of outcome if the finance ministry is not able to carry out the tasks it sets for itself. It needs people, an organisational structure, a budget and the skills and means to get things done; in other words, it needs capability. Capability is more than the total resource endowment of people and money (i.e. capacity); it manifests itself only in its performance against tasks (Dressel and Brumby, 2009). There are many reasonably well-endowed organisations that that fail to turn capacity into performance, and conversely there are some that manage to perform well on the basis of very scarce capacity.

There is a risk that this definition of capability, whilst more precise than capacity on its own, becomes rather tautological. If a ministry does something well, however defined, it is capable; if results do not materialise, it is incapable. The term needs more precision. Schick (2001) focuses on a dichotomy between a traditional and a policy role for the central budget office. Allen et al. (2015) distinguish between policy, regulatory and transactional functions. A ministry capable of performing one function need not be equally capable in other areas as well. Underneath every task or function, there are four more generic capabilities that, in varied combinations, make up an organisation's capability to perform these functions. These capabilities are (1) analytical, (2) delivery, (3) coordinative and (4) regulatory (Lodge and Wegrich, 2014):

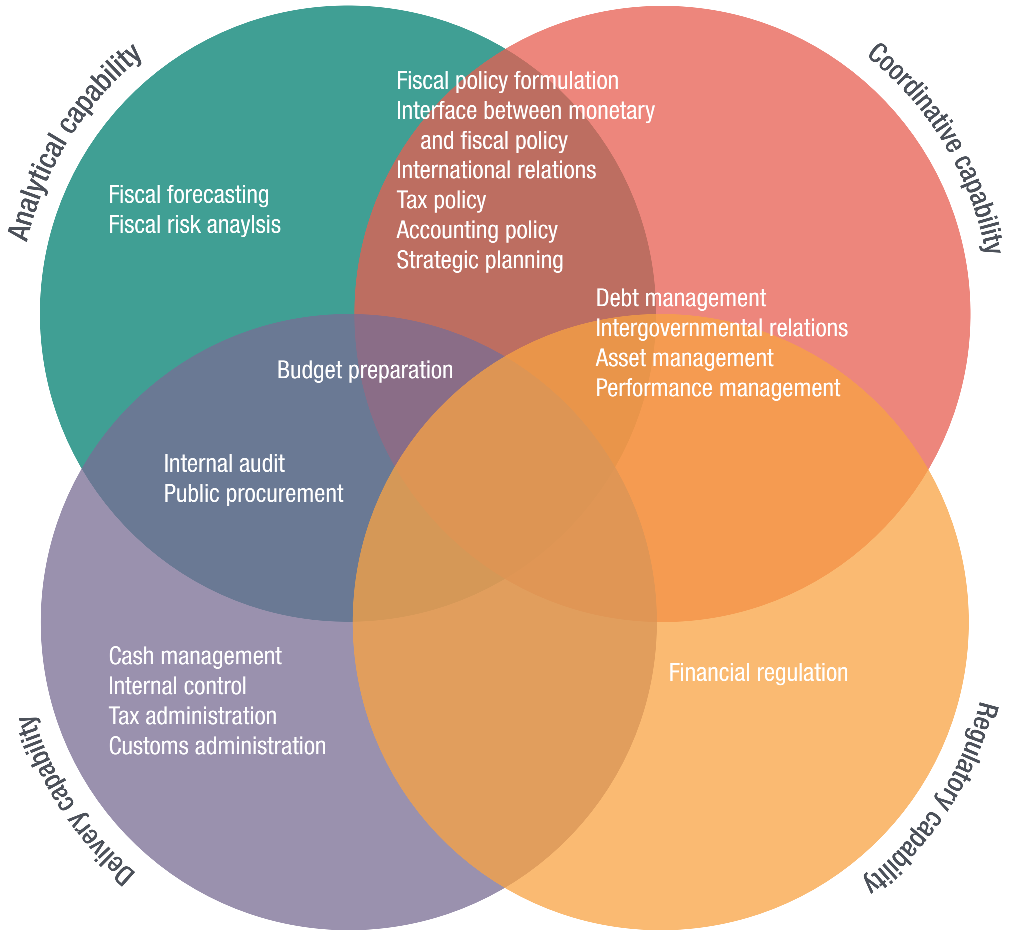
1. **Analytical capability**: the ability to understand and analyse information and research so as to inform decisions. In the case of finance ministries, this capability is in frequent demand in the recurrent formulation of fiscal policy in all its aspects, as well as numerous more specific policy issues that might arise in regard to the financial aspects of government activities. Many finance ministries pride themselves on the ability of their staff to master new policy briefs quickly and counter the sectoral expertise of the ministries with which it negotiates over funds. It is also the capability that is traditionally at the centre of many technical assistance efforts in developing countries, where the belief persists that better forecasting capability alone leads to more sensible fiscal policy.
2. **Delivery capability**: the ability to produce goods and services and get things done. For a central ministry not involved in direct service delivery to citizens, this capability is less important than it would be in, say, the post office. However, almost every finance ministry does produce a set of landmark deliverables each year: most importantly the delivery of a complete budget according to (in most countries) a specific budget calendar. There are also some more administrative tasks, such as revenue collection and cash management, which essentially rely

on the ability to produce and deliver certain outputs – often quite literally money – across government.

3. **Coordinative capability**: the ability to orchestrate the activities of different actors in pursuit of a common objective. Coordination is a critical element of what a finance ministry does from its location at the centre of government. A vast range of policy activities can only come together if the finance ministry is able to assemble and utilise specialist inputs from other ministries and bodies as well as non-government actors. Again, the best example is the setting of fiscal policy culminating in the budget formulation every year, which could not be achieved in a modern government without the organisation of a vastly complex procedure involving many different actors who have to deliver, analyse and move along many components before the budget is complete.
4. **Regulatory capability**: the ability to control the production of particular services delivered by others. Salient regulatory domains for many finance ministries include the oversight of SOEs and financial markets; but in a broader sense, regulation is also involved when finance ministries set the framework of the financial operations of spending ministries. In many countries, the finance ministry also has a big hand in overseeing subnational entities in various aspects of public finance including debt management, performance management and fiscal aggregates. In countries heavily influenced by the New Public Management, governments have sought to retreat more and more from the direct delivery of goods and services towards a more regulatory stance, which has affected finance ministries in various ways. Notably it has led to a substantial increase in subordinated agencies reporting to finance ministries, accompanied by a downsizing of the ministries themselves.

For the performance of any given function, a combination of different capabilities will usually be necessary, but they are not evenly distributed. Some central finance functions are very clearly based much more on one capability than others – for instance financial regulation. Others lie at the intersection of different capabilities, but none simply involves all of them in equal measure (Figure 5). Looking at the distribution of capabilities and functions, a few more patterns become apparent.

Figure 5: Mapping of capabilities and functions



Source: Authors

Overall there is a strong cluster at the intersection of analysis and coordination, as well as the intersection of analysis, coordination and regulation. There are very few areas that only involve analysis without coordination, and no coordinative activities without analysis – meaning that finance ministries drive certain cross-government processes, but never without adding their own inputs. There is also a cluster of delivery activities that do not involve other capabilities, and they are quite distinct from many other functions in that they are rather repetitive administrative functions without much of a policy dimension. Each of them is highly likely to have been hived off into specialist bodies and agencies in many OECD countries, as they would not be considered critical to those ministries' core responsibilities.

One implication stands out from this discussion: finance ministries cannot perform their functions on their own. This is perhaps obvious given that finance ministries are in charge of public money but spend hardly any of it themselves. The vast bulk of government financial operations happen elsewhere, so without means of interacting with and reaching into other organisations, it is impossible to exercise control from the centre, no matter how powerful a mandate is in theory.

2.6 Conclusion

Four areas need to be considered in order to frame the capabilities of finance ministries: purpose, institutional environment, portfolio of tasks and capabilities. In the absence of the others, each presents an incomplete picture; but even taken together, they still leave out many details. In any given country, there are many aspects – the finance ministry's priorities, how it fits into the larger public sector, what exactly it does and how – that are highly complex and likely to change over time.

The following sections will unpack each of these issues in more detail in the context of the case studies, as well as looking at patterns across cases. For the purpose of generalisation to the universe of all countries, the analysis is limited by the small number of case studies. However, it will serve to test and validate the ideas proposed in the context of countries that have dealt with (or struggled to deal with) a broad range of issues recognisable to a large number of countries not discussed in this report.

The next section discusses the changing priorities of finance ministries in the context of both economic and social challenges. These challenges form the backdrop against which central governments carry out their work, and politicians can retain or lose their jobs over them.

3. Measures of performance

Whether reasonably or not, governments regularly claim credit for economic performance and other socioeconomic outcomes, and get punished at the ballot box if the economy performs poorly. The emphasis on macroeconomic management at the expense of administrative control clearly reflects the perspective of ministers themselves, who both during and after their term in office tend to portray themselves as stewards of the economy, not as austere penny-pinchers[1] (Darling, 2012; Flassbeck, 2003; Jenkins, 1998). Finance ministries are centrally involved in both the macroeconomic and social agendas of any government that has them, usually as the lead agency in macroeconomic policy, tasked with funding most of the activities that could deliver socioeconomic outcomes.

Sustained underperformance is likely to prompt a response by government, even if the finance ministry is not causally responsible for a particular outcome. Should a ministry be criticised for not delivering on a certain outcome and this perception is deemed relevant for the government's electoral success, then over time the finance ministry ought to respond by trying harder, at least within the space allowed to it by its institutional environment.

This section discusses how ministries of finance interact with their institutional environments. Countries display a wide variety of formal legal endowments through constitutional powers, laws and administrative regulations that they can call upon in order to deliver their objectives. However, surrounding these formal rules are a wide number of informal practices, understandings and agreements that also affect the degree to which finance ministries can achieve their objectives. In some cases, widely differing formal institutional contexts operate with similar features regarding informal powers and influence.

3.1 Fiscal and macroeconomic outcomes

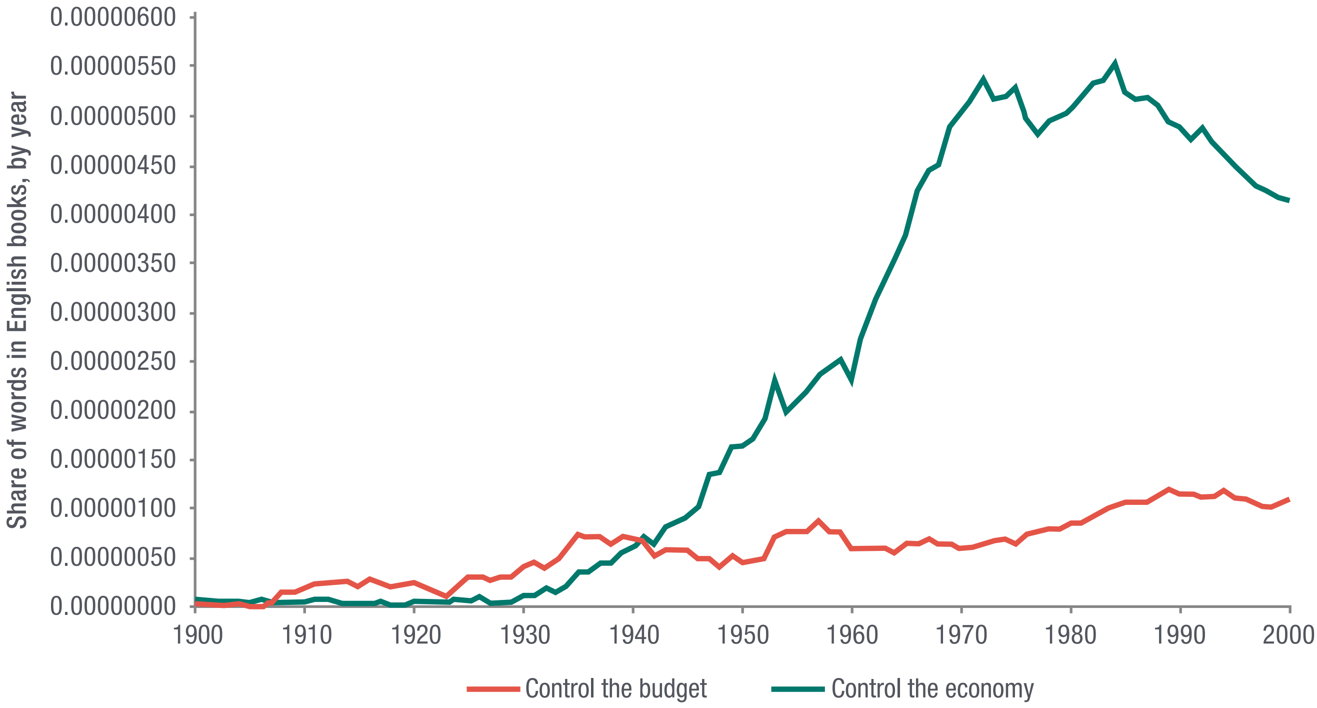
Over the course of the 20th century, the role of the stewards of public finance progressively expanded from controlling public spending and debt to controlling the economy. From the start of the century until the early 1940s, English-speaking sources mention control over the budget more often than control over the economy (Figure 6). Economic control rose steadily from the 1930s and surged ahead dramatically from the 1960s onwards, neatly matching the rise of Keynesianism in economic policy-making (Hall, 1989). Given these shifting priorities, it is worth considering how finance ministries have fared with regard to delivering better outcomes on key economic and fiscal policy parameters, such as the fiscal deficit, public debt, rate of inflation and economic growth.

In more recent decades, a steady improvement in fiscal performance has been a key characteristic of many LICs. Contributing factors include better policy and economic management, a favourable external environment (especially terms of trade improvements) and official debt relief (Lombardi, 2005). In fact, public debt levels are now at relatively low levels in the majority of LICs, with the debt levels in Nepal, Sierra Leone and Uganda falling below the LIC average for the period 2011-2013 (see Table 2). This has been helped not only by comprehensive external debt relief but also by strong economic growth and low interest rates. Overall, these three countries do not deviate from these trends, although there is some degree of cross-country heterogeneity, especially as regards the fiscal balance. Fiscal deficits have started to widen in recent years in Sierra Leone and Uganda (exceeding the LIC average over the period 2011-2013, as shown in Table 2), while Nepal has actually enjoyed fiscal surpluses, partly due to the under-execution of its capital expenditure (Krause et al., 2013).

The fiscal performance of the two upper-middle-income countries (UMICs) (South Africa and Mexico) and the three HICs (Chile, Germany and the UK) appear to follow even more closely the broad trend for their respective income groups between 2000 and 2013. The fiscal balance and debt levels generally improved in the first half of the period, but then sharply deteriorated at the start of the financial crisis in 2008. However, in the past three to five years, most of these economies have shown signs of recovery, with fiscal deficits shrinking due to appropriate policy responses (see Box 1). Debt levels have also somewhat stabilised following the slight upward trend since mid-2000, and are seen as prudent by international standards. The main exceptions are South Africa and the UK, where public debt dynamics are yet to stabilise, with the UK (88%) lying significantly above the HIC average of 62% (IMF, 2014b).

1 One notable exception was German finance minister Hans Eichel (1999-2005), who was famous for keeping a collection of piggy banks in his office.

Figure 6: From budgetary to economic control



Source: Adapted from Google Ngram (2015)

Box 1: Effectiveness of policy responses to the global financial crisis and other recent shocks

Chile: Since 2008, Chile's economy has successfully withstood two large adverse shocks – the global financial crisis and a devastating earthquake in February 2010. Its resilience was underpinned by solid policy frameworks (including a fiscal rule, inflation targeting and exchange rate flexibility), a sound banking system and a strong policy response, facilitated by the existence of large fiscal buffers (IMF, 2010).

Germany: Germany was hit exceptionally hard by the crisis, but strong policy support helped Germany emerge from the deep recession. Financial sector measures mitigated systemic stress and supported credit. Automatic stabilisers and significant fiscal stimulus contained the downswing and supported the recovery. Moreover, Germany has achieved the deficit goals at the federal level under the national debt brake rule introduced in 2009 well ahead of schedule, and the general government balance is already in line with commitments under the Fiscal Compact of the Economic and Monetary Union (IMF, 2013).

Mexico: Mexico implemented an effective counter-cyclical policy response to the global crisis (IMF, 2011). Moreover, its very strong fundamentals and policy track record proved crucial for withstanding the fallout from the global crisis and for recovery. The strong rule-based policy framework introduced in Mexico over the past decade includes the inflation targeting and flexible exchange rate regimes, the balanced-budget fiscal rule and a sound, prudential system.

South Africa: The turnaround in the overall fiscal position initiated in 1996 (which brought the deficit down to the target of 3% of gross domestic product (GDP) in 1999/2000) was critical in creating the fiscal space for the government to respond to the global financial crisis and its fallout in a counter-cyclical manner.

UK: In response to the financial crisis the government announced a package of fiscal consolidation measures that helped reduce the overall deficit from 11% of GDP in 2009/10 to 5.8% by the end of 2013/14 (IMF, 2014b).

Source: Excerpts from IMF Article IV consultation reports

With the exception of Sierra Leone and, to a lesser extent, Nepal and Uganda, the rest of the countries have enjoyed single-digit inflation rates in most years since 2000. Among the LICs, inflation has been on a declining trend since 2000, albeit with temporary reversals triggered by spikes in food and fuel prices (IMF, 2014a). Tighter monetary policies, facilitated by reduced fiscal dominance, have been central to achieving this trend decline. Inflation rates have remained high in Nepal, Sierra Leone and Uganda compared to the LIC average, as shown in Table 2, although Uganda's inflation rate was close to its 5% target level in 2013, while Nepal's and Sierra Leone's fell only slightly below 10%. In the case of Sierra Leone, high inflation rates have been the result of expansionary monetary and fiscal policy, currency depreciation and global price shocks, while Nepal's inflation rate closely mirrors that of India due to the currency peg and close trade relations. Ultimately, the struggle against inflation appears to be more of a challenge for the poorer countries than the richer countries, with the trends in the HICs closely mirroring one another and remaining below 4% in most years since 2000.

Finally, with regard to economic growth, all eight countries enjoyed positive growth rates for most of the 2000-2013 period. Growth rates have been especially high in Uganda and Sierra Leone following the end of their respective conflicts (in 1986 and 2002 respectively). In contrast, growth rates in Nepal, while positive, have been perceived as disappointing, failing to accelerate after the country's decade-long conflict ended in 2006 (Government of Nepal, 2014). Other than these three LICs, the five remaining countries suffered from negative growth rates at the start of the global financial crisis in 2009, though they quickly rebounded in subsequent years. The impressive resilience of LICs during the global economic crisis was facilitated by the limited direct linkages between domestic financial systems and international financial markets (IMF, 2014a). On the other hand, the post-2009 positive growth rates of South Africa, Mexico, Germany and the UK are still subdued relative to their peers and/or potential, with only Chile's average growth rate exceeding the average of its income group over the period 2011-2013 (see Table 2).

Ultimately, overall economic management of each of these eight countries has been mixed but generally sound. The more advanced economies of Chile, Germany and the UK appear susceptible to common external shocks, with trends in fiscal and macroeconomic outcomes showing a clear picture of two halves – before and after the financial crisis. On the other hand, there is greater heterogeneity among the LICs (and UMICs to a lesser extent), especially with regard to the size of the fiscal deficit and the rate of inflation. Among the four fiscal and macroeconomic outcomes considered in this section, stimulating and sustaining economic growth is a common concern for most of these eight countries, while curbing inflation rates is more of a policy challenge in the LICs.

Table 2: Key macroeconomic indicators, average 2011-2013

	Overall fiscal balance	General government debt	GDP growth)	Inflation
Low-income countries				
Nepal	0.15	32.90	4.02	9.27
Sierra Leone	-4.07	37.43	5.54	14.03
Uganda	-3.37	31.23	5.34	12.57
LIC avg.	-2.85	40.40	6.16	7.65
Upper-middle-income countries				
Mexico	-3.62	44.27	3.03	3.77
South Africa	-4.23	42.03	2.65	5.50
UMIC avg.	-2.02	46.89	5.33	5.46
High-income countries				
Chile	0.48	11.97	5.10	2.71
Germany	-0.18	79.80	1.36	2.08
United Kingdom	-7.20	88.00	1.34	3.29
HIC avg.	-0.66	61.59	1.53	2.70

Source: World Economic Outlook October 2014 and World Development Indicators

3.2 Socioeconomic outcomes

This section focuses exclusively on the three LICs and two UMICs, where socioeconomic development is part of the international development agenda and is monitored using comparable figures. Looking at specific Millennium Development Goals (MDGs) and their corresponding targets, Table 3 provides a snapshot of what has been achieved. Notably, all five countries have made impressive socioeconomic gains, either achieving or being on track to meet several of the MDG targets that have eluded most LICs, namely reducing under-five mortality rates and improving access to safe drinking water (IMF, 2014a). Moreover, among these five countries, only Sierra Leone did not halve the proportion of people whose income is less than one dollar a day by 2015, while the other four countries have already achieved this MDG. Similarly, Uganda is the only exception with regard to successfully halting the spread of HIV and AIDs.

Nepal's achievements, illustrated in Table 3, are particularly remarkable given its difficult context of recent armed conflict and persistent political instability. Despite these constraints, Nepal is the only country among the five that is rated as having achieved or likely to achieve all six of the MDG targets listed below. Among these achievements, Nepal's large-scale reduction in maternal mortality (fell by over 50% since the early 1990s) is noteworthy given that this goal has tended to be one of the most off-track MDGs in most countries, including Uganda, South Africa and Mexico. While the available evidence does not explicitly link improvements in the MDGs to the capabilities of the finance ministry per se, it does partly attribute Nepal's success to a consistent policy focus and sustained financial commitment by the Nepali government and donors over the past two decades. Health policy became an area of political contestation following the 1990-1991 political transition and the return of multiparty politics, thereby providing political space for substantial reforms of the health system and for doubling health expenditure per capita between 1995 and 2010, 40% of which was aid (Engel et al., 2013).

Under-five mortality and life expectancy at birth are two other health outcomes that are worth examining in greater detail. These two indicators measure the general health status of a population and also reflect the quality and efficiency of a country's health system. While Table 3 demonstrates that each of the five countries is likely to achieve the under-five mortality target, some further insights emerge from Figure 7. First, it reveals that sharp reductions in child mortality have been observed at all levels of national income, with all countries except South Africa exhibiting a clear downward trend since 1990. Second, the rate of improvement appears to be

Table 3: Progress on selected MDGs

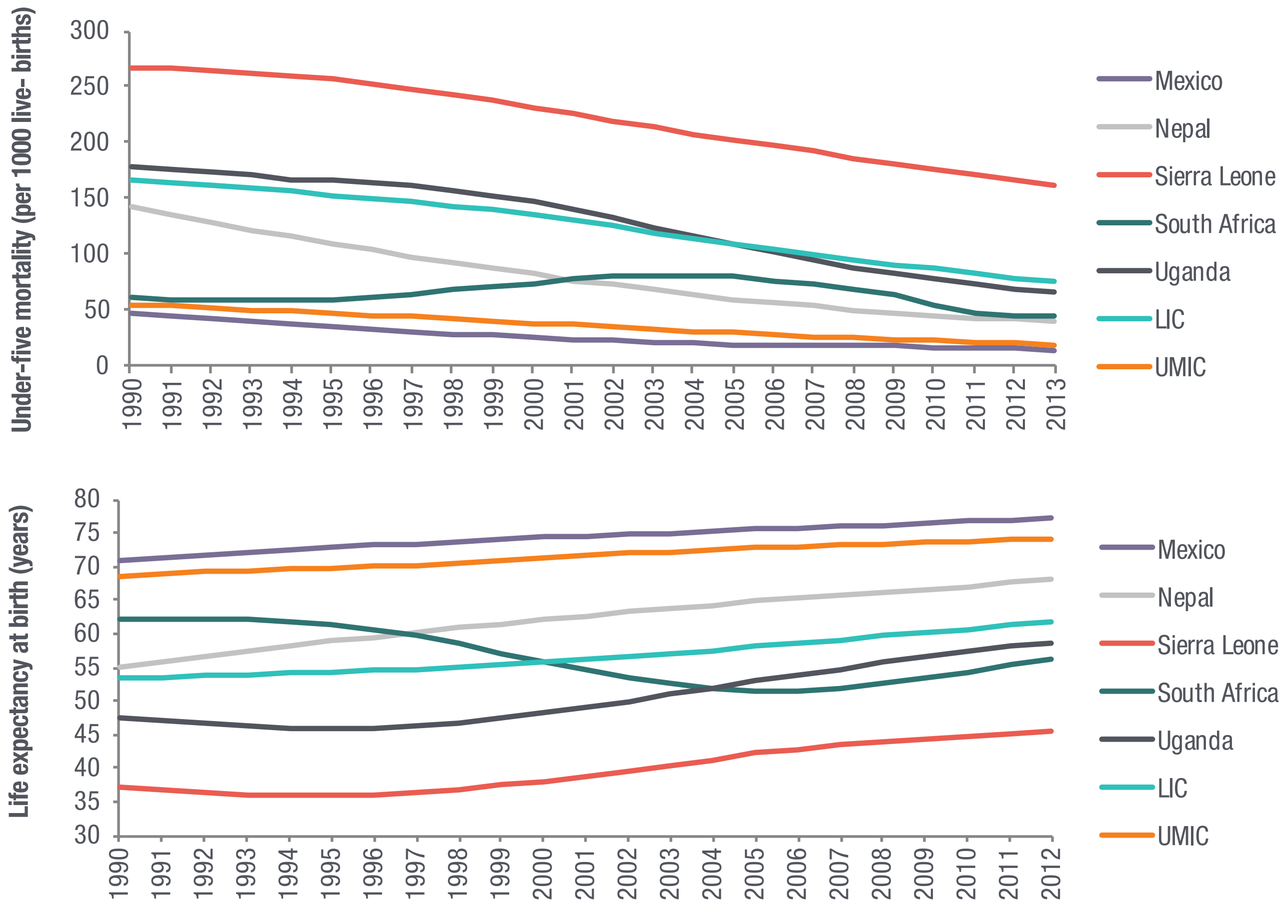
GOAL	Nepal (2013)	Sierra Leone (2010)	Uganda (2013)	South Africa (2013)	Mexico (2013)
Halve, between 1990 and 2015, the proportion of people whose income is less than one dollar a day	Achieved	Unlikely/Off-track	Achieved	Achieved	Achieved
Ensure that, by 2015, children everywhere, boys and girls alike, will be able to complete a full course of primary schooling	Likely/On-track	Inconclusive	Likely/On-track[i]	Likely/On-track	Achieved
Reduce by two thirds, between 1990 and 2015, the under-five mortality rate	Achieved	Likely/On-track	Likely/On-track	Likely/On-track	Likely/On-track
Reduce by three quarters, between 1990 and 2015, the maternal mortality ratio	Achieved	Likely/On-track	Unlikely/Off-track	Unlikely/Off-track	Unlikely/Off-track
Halt by 2015 and be reversing the spread of HIV/AIDS	Likely/On-track	Likely/On-track	Reversal	Likely/On-track	Achieved
Halve, by 2015, the proportion of people without sustainable access to safe drinking water	Achieved	Likely/On-track	Likely/On-track	Achieved	Achieved

Source: Extracted from respective Millennium Development Goals progress reports
Notes: i. Progress has been slow, but with effort Uganda may still achieve this goal (UNDP, 2013).

highly dependent on initial conditions, with the countries starting from the weakest position – like Sierra Leone – experiencing the fastest rate of improvement. At the same time there remains substantial room for improvement, with Sierra Leone's under-five mortality rate of 161 per 1,000 live births in 2013 being more than twice the LIC average of 76. South Africa also lies consistently above the UMIC average (since 1990) and was in fact the only country that experienced a prolonged increase in this indicator (1994-2003) due the impact of HIV and AIDS. Thereafter, this indicator improved in South Africa due to the introduction of the PMTCT[2] programme and the pneumococcus and rotavirus vaccines.

A similar story emerges for life expectancy at birth. This is unsurprising given that infant mortality and child mortality have a profound effect on life expectancy. Whilst mortality at younger ages reduced life expectancy in the earlier years of the 2000s in South Africa, evidence suggests gains in life expectancy from 2006. Nonetheless, both Sierra Leone and South Africa fall below the LIC average.

Figure 7: Under-five mortality (per 1000 live births) and life expectancy at birth (years) for selected countries



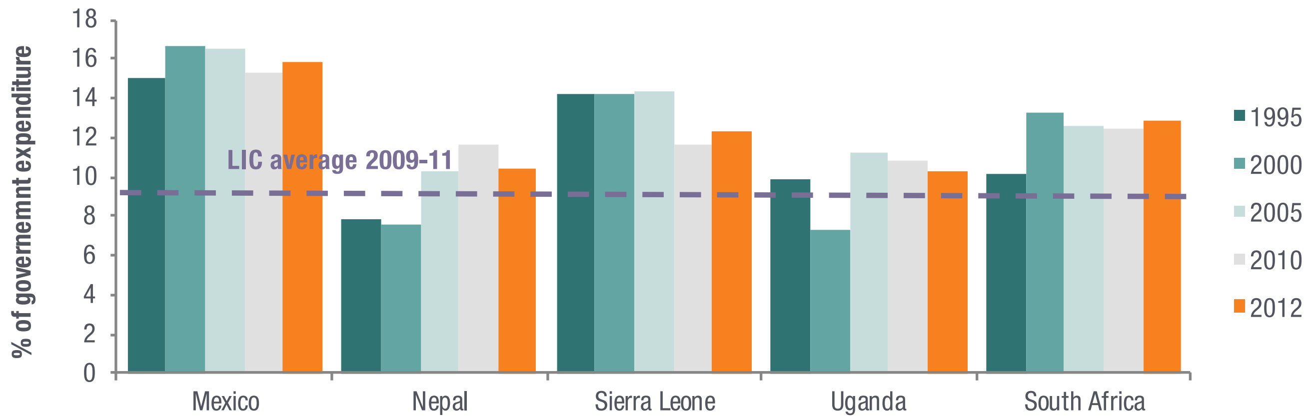
Source: World Development Indicators

2 This programme prevents transmission of HIV from mother to infant, through antenatal HIV testing and provision of antiretroviral prophylaxis or treatment for mothers and infants.

The logical question that then emerges is how far public expenditure has been instrumental in bringing about the progress in health status experienced in developing countries. Indeed, Figure 8 shows that with the exception of Sierra Leone, these improvements have generally coincided with an increase in public health expenditure as a percentage of total government expenditure between 1995 and 2012 (particularly Nepal). Moreover, all five countries have been spending more than the LIC average in recent years. However, from this data, it is impossible to infer causality with any degree of certainty. For example, the South African experience clearly shows that a significant increase in its health spending does not automatically translate into better outcomes, with above-mentioned health outcomes initially deteriorating despite increased spending. Nepal's experience with maternal health over the past 20 years suggests that the causal chain is even more complicated, with political commitment being just as important as financial commitment, and with several actors beyond the finance ministry playing critical roles. Health – with maternal health as a core priority within the sector – was politically important in Nepal, even in the midst of conflict, and this prioritisation was guided by a capable cadre of top-level officials in the Ministry of Health and Population and backed by donors.

In the wider empirical literature, health care expenditures and health outcomes have been a subject of an ongoing debate (see for example: Burnside and Dollar, 1998; Filmer and Pritchett, 1999; Bokhari et al., 2007). A number of these studies conclude that public spending and health outcome are tenuously related. Nonetheless, all of the negative or ambivalent findings on the effect of public spending on outcomes could potentially be a reflection of differences in the efficacy of spending, which could arise for a variety of reasons, including corruption and patronage. Thus, simply increasing public expenditure in the health sector may not significantly affect health outcomes if the efficiency of this spending is low.

Figure 8: Health expenditure, public (% of government expenditure), 1995-2012



Source: World Development Indicators

3.3 Conclusion

It is noteworthy that the macroeconomic situation and outlook is generally regarded as sound across all case studies, albeit with some important caveats. In particular, there is some concern over public debt dynamics in the UK and South Africa, about moderating inflation in Sierra Leone and Nepal, and about stimulating economic growth in most case study countries (Nepal, South Africa, Mexico, Germany and the UK). It is also striking that the five non-HICs have made impressive progress towards the MDGs, though Sierra Leone and South Africa still lag behind the average performance of their respective income groups for under-five mortality and life expectancy.

Overall trends in most of these outcomes for each country closely follow the trends of the respective income group, suggesting that there are common phenomena driving these trends. This is not to say that country-specific factors are not important. For example, in most LICs, the ministry of finance plays a pivotal role in negotiating and meeting the preconditions for debt relief and/or adhering to IMF programmes and advice. Identifying the relative importance of such factors with a reasonable degree of certainty is difficult owing to the high-level nature of these indicators and the fact that country-specific factors like institutional quality are themselves strongly correlated with income. Further complicating matters are the difficulties in separating the role of officials in providing advice and the role of ministers in making decisions that may be only partly based on the advice given. The subsequent sections attempt to resolve these complications by explicitly highlighting case study findings regarding the quality of the broader institutional environment, as well as the organisational features of the ministry of finance itself, and their relation to the ministry's ability to carry out its core functions effectively.

4. Finance ministries within the structure of government

No single ministry is independent from the government and the institutions that surround it. This especially applies to finance ministries, which are mandated to exercise broad control over government financial operations without spending much money directly themselves. The relationship between organisation and environment is inevitably complex. Several issues are worth highlighting.

First, there is generally a strong correlation between per-capita income and virtually any measure of the quality of government. An assessment of capabilities therefore needs to take into account broad income levels. At the same time, the challenges facing the finance ministry also change with income. This was certainly the case historically, but it also seems to apply to countries today. For instance, the allocation choices facing a mature industrial economy with large entitlement programmes, aging populations and entrenched bureaucratic interests are different from those facing a fast-growing MIC without a fully developed welfare state.

Second, given a certain income level, the precise shape and form of the institutional environment determines how much space a ministry has to develop its functions. Most clearly, a weak legislature is much less likely to constrain a finance ministry's ability to set the terms of the fiscal policy process, for good or bad.

All the countries studied in more detail were selected for their finance ministries showing elements of capability and performance, given their level of income. Organisation and environment are mutually reinforcing; therefore it is not very productive to ask whether the organisation caused the environment to score highly, or vice versa. This section will instead seek to outline the variety of external contexts that finance ministries operate in, and thereby define some of the structural challenges and opportunities they face.

4.1 Quality of government

As is to be expected, the finance ministries in the LICs operate in a more difficult institutional environment than those of the richer countries, based on measures relating to corruption and government effectiveness. Moreover, while these indicators have generally deteriorated for most of the countries, the governments of Sierra Leone, Mexico and Chile were perceived as becoming slightly more effective between 2000 and 2012, while only Chile was rated as slightly less corrupt (see Table 4). A similar pattern in terms of a positive correlation with income emerges if we look at an index that provides an aggregate measure of key features of public policies.[3] The exception is South Africa, which together with the three HICs lies above the sample mean of 1.94,[4] whereas Nepal, Sierra Leone, Uganda and Mexico fall below.

Nonetheless, in terms of the extent to which the public administration is professional rather than politicised, both Nepal and Uganda score higher than the two UMICs, the UMIC average and even Chile. In fact, Nepal has the second-highest score after the UK, which outperforms Chile and Germany in both areas. On other hand, the public administration of these two LICs is perceived as much less impartial compared to the richer countries and to the LIC average. South Africa and Mexico also fall below the UMIC average in both dimensions.

3 The policy index was created based on the six variables (decisiveness; stability; coordination; implementation and enforcement; efficiency; and public regard) and has a scale of 0-4.

4 Mean for a sample of 188 observations.

Table 4: Quality of government

Country	Impartiality	Professionalism	Control of corruption (by 2012)[i]	Government effectiveness (by 2012)[ii]	Policy index
Nepal	-0.92	4.80	Weak	Weak	1.13
Sierra Leone	–	–	Weak	Weak	1.15
Uganda	-0.54	3.90	Weak	Weak to intermediate	1.89
LIC avg.[iii]	-0.54	4.06	–	–	–
South Africa	-0.76	2.95	Intermediate	Intermediate	2.30
Mexico	-0.64	2.89	Weak to intermediate	Intermediate	1.89
UMIC avg.[iv]	-0.29	3.54	–	–	–
Chile	0.67	3.82	Very strong	Strong	2.92
Germany	0.54	4.52	Very strong	Very strong	3.10
United Kingdom	1.06	5.40	Very strong	Very strong	3.23
HIC avg.[v]	0.54	4.62	–	–	–

Source: Teorell et al. (2015), Chuaire et al. (2014) and World Governance Indicators

Notes: i. Rated as very strong if above 90th percentile; strong if 75th to 90th percentile; intermediate if 50th to 75th percentile; weak to intermediate if 25th to 50th percentile; weak if 10th to 25th percentile; and extremely weak if below 10th percentile.

ii. See previous footnote.

iii. LIC average based on 10 countries.

iv. UMIC average based on 30 countries.

v. HIC average based on 35 countries.

Given that governance scores are generally strongly positively correlated with income levels, the quality of each of the eight countries' broad institutional environments (corruption and government effectiveness) matches what would be expected for their respective income levels. However, when we focus on specific areas of the institutional environment, such as the quality of civil service, some noticeable anomalies emerge. In particular, both Nepal and Uganda appear to have a highly professionalised civil service, surpassing those of several of the richer countries. South Africa also appears to have an effective public policy environment.

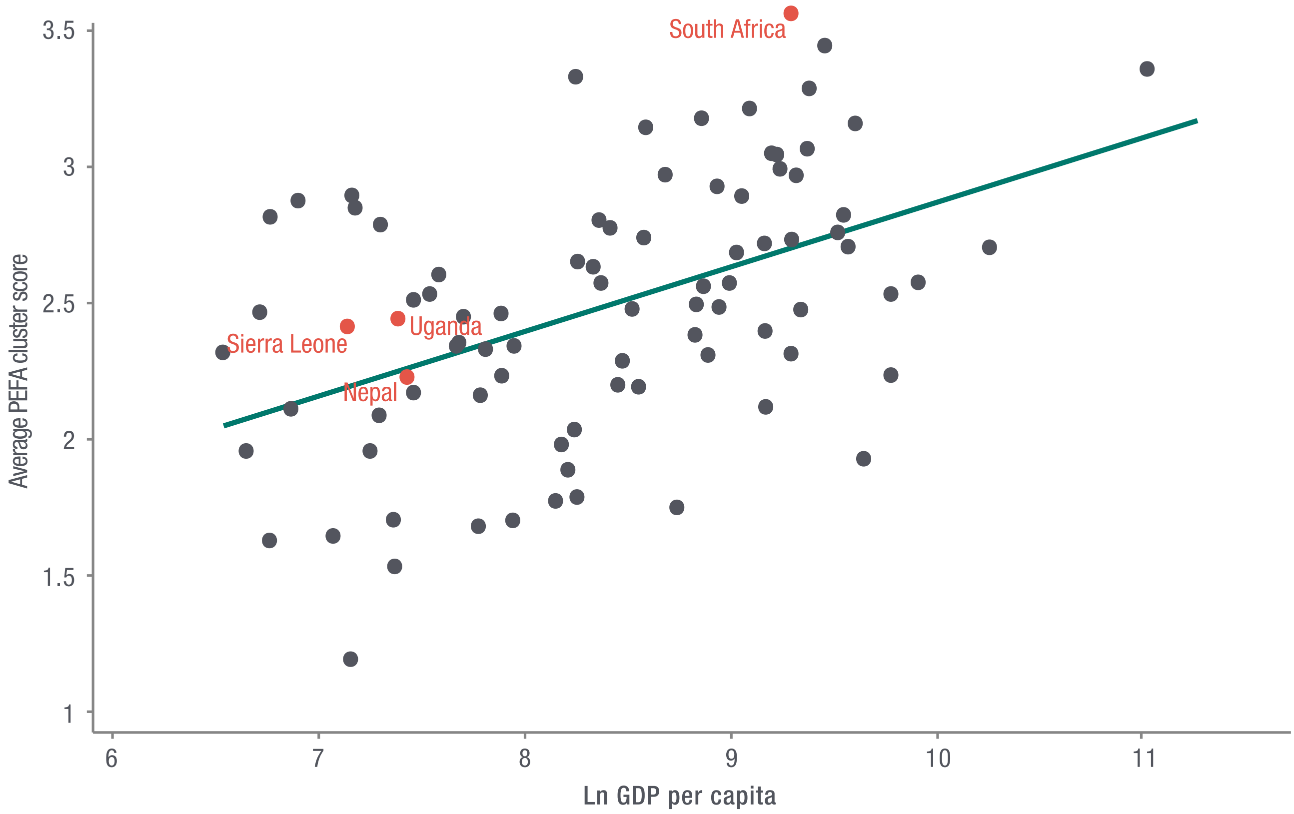
Income levels and the quality of PFM systems are similarly correlated (Figure 9). Using the PEFA indicators as a basis, richer countries unsurprisingly tend to manage their public finances better. The scores are generally accepted as a reasonable proxy for the quality of PFM systems, in spite of well-known limitations (de Renzio, 2009; de Renzio et al., 2011; PEFA Secretariat, 2005; Sweet et al., 2014). Unfortunately, PEFA scores are available for very few HICs and UMICs, leaving an inevitably stunted distribution. There are many countries that deviate quite far from the trend, however, and it is worth noting how these cases of stronger finance ministries compare to their income-level peers.

Keeping in mind the very limited sample available, three out of the four countries with such available data enjoy PEFA scores above what would be predicted by their income level. This is particularly pronounced in the case of South Africa, which scores an 'A' in 18 of the 28 PEFA dimensions (in 2008), and a 'B' or higher in all six clusters. In contrast, Nepal is the exception, finding itself much closer to the income/quality trend line. Nepal's PEFA assessment, however, was carried out at the height of its civil conflict and a more recent assessment is on the verge of completion. Three countries do not make a trend, but the detailed evidence from those cases suggest that the finance ministries are to some extent leading reform programmes that over time manage to improve the quality of PFM. It also suggests, however, that in each of these three countries, the system as a whole to some extent lags behind the progress that the ministries have already made.

4.2 Legislative and executive authority

The eight case studies show a wide range of legal frameworks that underpin the operation of budgetary and expenditure management, with no clear and obvious link between income level and any particular approach. For the LICs there are number of notable legal system features. In both Uganda and Sierra Leone a large part of their formal PFM rules governing economic and budgetary functions have grown out of donor-funded PFM programmes. In this way, they have adopted some elements of international best practice in formal PFM rules, although this is not universal (for example, Sierra Leone's legal framework

Figure 9: Average PEFA score by GDP per capita



Source: Adapted from PEFA assessment portal and World Development Indicators

still contains constitutionally mandated – and regularly used – 'overrides' for presidential spending). Uganda's legal systems are identified as having been used to normalise practice that was already in place, rather than lay foundations for new procedures. However, in each of these studies there were examples of required practices not being followed to the letter. For example, in Sierra Leone, supplementary budgets have not consistently been brought to Parliament for approval. Similarly in Uganda, there have been clear examples of maladministration of public resources but little in the way of follow-up, investigation and sanction.

Among the MICs and HICs, legal frameworks again vary considerably. In Mexico, there is a strong reliance on formal legal authority being necessary to operate public expenditure systems, whereas in Chile extensive use is made of administrative decisions by officials authorised by a broad legal framework. Germany's system operates within a clear legal framework, but the informal realities of coalition government and a practice of decision-making by consensus reduces the need for the ministry of finance to invoke some of its more sweeping legal powers, such as cabinet veto over financial matters.

One outlier can be identified within the entire legal framework debate. The UK operates much of its expenditure management without a consolidated legal framework. Indeed, official guides to public spending quite openly note that expenditure management is done partly on the basis of convention, partly through interpretation of broad ministerial powers, and also by extensive use of precedent. Together, these examples may well support existing arguments that the informal bureaucratic and political culture surrounding formal legal frameworks are more important in determining actual budget practice than the legal framework itself (see for example Andrews, 2008).

In all the cases studied, and seemingly regardless of legal frameworks, a pattern of relatively strong executives and weak legislatures emerges. The issue of legislative power over the budget process is well studied among HICs (e.g. Wehner, 2006), although less extensively investigated among LICs and MICs. All countries operate with the convention that the legislature has the sole power to authorise expenditure (even if this is done retrospectively in the case of some expenditure in certain countries); and yet in practice the case studies found only limited examples of the legislature playing an important role in expenditure and budget management.

In the LICs, there are clear examples of legislative procedure simply being ignored in practice by the executive; as well as legislatures being ill-equipped to meaningfully engage in policy debate. In Chile and Mexico, the legal framework combined with significant amounts of legislatively mandated expenditure substantially reduces the ability of the legislature to meaningfully amend the budget. However, the political system of Mexico – with a relatively powerful legislature budgetary authority combined with a three-party system that ensures that presidents do not command a legislative majority – constrains the executive far more than that of Chile.

In the UK and Germany, the budget is subject to significant discussion and debate among various factions (formal or informal) within ruling coalitions during the budget preparation stage, but with little expectation that during formal parliamentary debate there will be any significant changes made by either government or opposition. There were no examples raised in the studies of parliaments consistently and substantively amending budget proposals year after year, even if there were isolated examples of occasional legislative activism on one-off issues.

In some cases, the real role of the legislature over the public purse comes in after-the-fact scrutiny. In the Westminster-based systems (UK, Sierra Leone, Uganda) there is a more obvious role for the Public Accounts Committee or equivalent in using its investigatory and interrogative powers to challenge government spending, often with an eye to public exposure. This was less prevalent in the non-Westminster environments of the other cases, but appears to be a more realistic method for formal legislative engagement with the budget process than the universally acknowledged – but effectively symbolic – role of legislatures in 'approving' all spending.

The majority of finance ministries in the sample are perceived as strong within the executive, but they differ notably in how this strength is defined. In the two high-income cases, the UK Treasury is often seen as a 'model' for a ministry of finance that has embraced a New Public Management model of delegating detailed controls over inputs in favour of macrobudgetary controls over aggregates and outcomes. Over time, it has actively divested itself of day-to-day oversight and control of spending decisions and instead focuses on managing a number of interrelated systems that taken together provide the basis for spending control in the context of substantial delegation to other actors. The German system offers a contrast. For the German ministry of finance, significant micro-level controls are the tools by which it directs and manages spending units, with relatively less focus on the macro control toolkit (Figure 10).

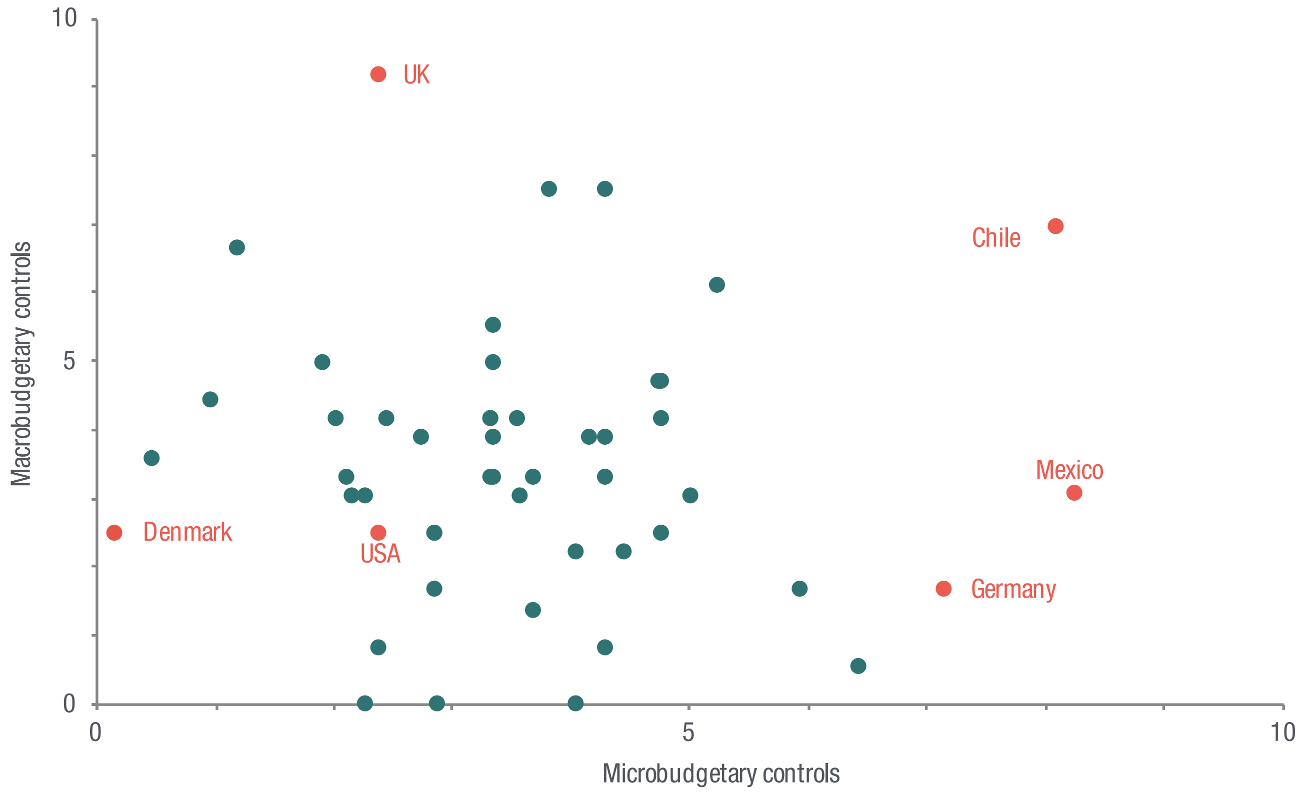
In contrast to the UK and Germany, which appear to have chosen either micro- or macro-level control as a guiding approach, the MICs in the sample – notably Mexico and Chile – appeared to show a tendency for both strong microbudgetary controls alongside significant macrobudgetary control. Indeed, in an index of such control, Mexico and Chile (as well as Germany) rank in the top three MICs and HICs surveyed for degrees of micro- and macro-level control (Krause, 2009a). As a concrete example of this in practice, formal rules require ministries in Mexico and Chile to continually approach the ministry of finance to 'make the case' for movements between different spending lines, and in some cases individual payments can be tracked centrally by the ministry of finance. This 'double control' would, all things being equal, suggest a particularly strong ministry of finance in terms of formal powers.

LICs have not been scored extensively against this micro/macro control framework. However, the evidence from the case studies would suggest some strong evidence for the importance of micro-level controls. In Sierra Leone and Uganda, cash was released in monthly (sometimes weekly) instalments to individual agencies based on individual ministry of finance decisions, and in certain circumstances the ministry of finance had a role in determining which individual suppliers to pay. The picture in Nepal is less clear, with substantial institutional fragmentation perhaps making micro-level controls harder to operate. In the two low-income African countries, this level of micro control offers significant prospects for oversight over spending, but it also absorbs a large amount of senior officials' time and it limits the amount of time that can be spent considering higher-level ('macro') budgetary issues.

Interestingly, within the sample were certain 'dogs that did not bark' in terms of the formal powers of the ministry and how they enable – or otherwise – the institution to deliver against its mandate. In none of the studies was the role of, and relationship with, subnational governments raised as a particular issue relating to capability.

The sample contains a mixture ranging from long-standing federal states (e.g. Mexico, Germany, South Africa) to unitary states with an evolving subnational fiscal framework (e.g. UK, Uganda, Sierra Leone), allowing for significant divergence of institutional models that could potentially have an impact on the capability framework. However, in the course of the studies, the role of subnational government in affecting – positively or negatively – the capabilities of ministries of finance did not appear significant. In some cases this may be because the subnational fiscal settlement is well established and uncontroversial; in others it may be because the federal or central ministry of finance does not feel particularly challenged either by the policy area of subnational governments or by subnational governments themselves. In any case, the capabilities of the ministries of finance surveyed in this series appear to have no particular relationship with subnational governments and their particular policy debates.

Figure 10: Microbudgetary versus macrobudgetary controls



Source: Krause (2009a)

4.3 Conclusion

In sum, given that governance scores are generally strongly positively correlated with income levels, the quality of each of the eight countries' broad institutional environments (corruption and government effectiveness) matches what would be expected given their respective income levels. However, when we focus on specific areas of the institutional environment, such as the quality of civil service or the PFM system, some noticeable anomalies emerge. In particular, both Nepal and Uganda appear to have a highly professionalised civil service, surpassing those of several of the richer countries. South Africa also appears to have an effective public policy environment.

Furthermore, the PFM systems of Sierra Leone, Uganda and South Africa (and to a lesser extent Nepal) appear to be well developed when assessed in terms of their compliance with international best practices (the PEFA assessment). Finally, comparisons of the budgetary powers highlight the considerable heterogeneity in the configuration of the PFM system across HICs in general, lending credence to the hypothesis that there is no one ideal structure that fits all countries equally well.

Ultimately, these institutional qualities are likely to have implications for how the ministry of finance is organised and how effectively it is able to perform its functions. In none of the cases is the finance ministry so constrained in its mandate that it would be considered an outright backwater, and neither do limited mandates themselves makes it hard to maintain capability. This seems to be a general observation that applies even to countries where the powers of the finance ministry are severely constrained, as for instance is the case in the United States (Tomkin, 1998). The functional core of the finance ministry appears to be strong enough that it always merits a degree of executive attention.

5. Finance ministries as organisations

Without understanding the insides of finance ministries as organisations, we are bound to see them as black boxes – poorly defined entities that intermediate between the instruments of public finance and the institutional framework. This section looks more deeply within this important context at how the eight finance ministries organise themselves internally.

What are the formal responsibilities of the ministry of finance, and what functions are shared with, or delegated to, other institutions? Fragmentation of function is not always a sign of institutional weakness or lack of capability. Indeed, for some functions, prevailing global 'good practice' actively encourages separation of powers or responsibilities. This is often done in the spirit of New Public Management and a shift towards macrobudgetary control, and has a long-standing record with regard to finance ministries in Anglo-Saxon OECD countries (Parry et al., 1997). Delegation to agencies often takes place in pursuit of efficiency for specialised services – such as the use of semi-autonomous revenue agencies and regulatory bodies for the financial sector. There are also cases where functions are split in order to restrain the powers of the central government. In the UK and Germany, for example, economic forecasts are outside of the core responsibilities of the finance ministry.

Attribution of responsibilities and organisational arrangements are clearly related. It would be reasonable to expect that a finance ministry that collects revenues directly would have more employees than one that does not, perhaps using an autonomous revenue authority instead. These forms of delegation are focused on the delivery function of finance ministries. However, the operational core of the main ministry of finance – made up mostly of the groups and functions responsible for delivering and regulating the national budget – tends to be much more stable and smaller across cases. In many countries this is recognised in the vote structure of the appropriation act – with specific votes for departments that deal with revenues, customs, internal audit, treasury and stores, among other functions – even if formal reporting lines continue to be to the minister or chief administrator of the finance ministry.[5] However, it also dramatically shrinks the size of some finance ministries.[6]

One important factor is the staff themselves. How many people work in particular functions? What education, training and experience do they have? A second factor is the characteristics of the (senior) civil service. Do they have tenure? Are they promoted on merit? Are the key technical positions, as well as managerial positions, taken up by people who came up through the civil service or by people from the outside? To what extent is the civil service open or closed (Dahlström et al., 2010) and does that affect the finance ministry? Third, how is the ministry structured internally: is it a traditional machine bureaucracy, or more of a professional organisation? How are the hierarchies organised, and how do professional staff relate to managers?

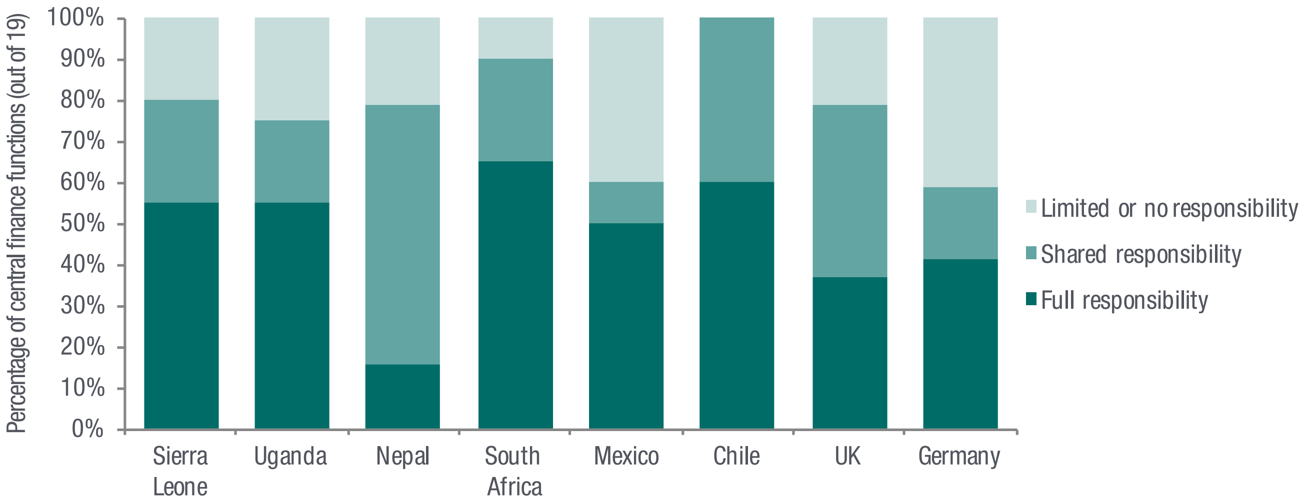
5.1 Distribution of functions

The existing research suggests empirically that centralisation and fragmentation of finance ministry functions follow a pattern relating to income per capita. Centralisation follows a 'hockey stick' distribution. LICs are relatively fragmented, reflecting perhaps general challenges of institutional coordination and reform in low-capacity environments, but also the political incentives of these environments that actively seek to reduce the prospects for, and impact of, reforms that might strengthen formal rules-based systems of financial governance (World Bank, 2011; Allen and Grigoli, 2011). MICs tend to centralise functions and reduce fragmentation as they develop; while HICs are seen as moving back towards a lower degree of centralisation and higher degree of fragmentation, although typically in the context of 'delegated' frameworks, where the central ministry of

5 A 'vote' is the administrative unit which Parliament authorises to spend up to the level in the appropriation act, or similar legislation

6 For example, in December 2012, the Ministry of Finance and Economic Development of Sierra Leone had 242 staff, while the vote for the Accountant General employed 226 staff. In Nepal, the Ministry of Finance employed around 172 staff in 2014, excluding nearly 5,000 staff in the Financial Comptroller General's Office.

Figure 11: Distribution of central finance functions



finance retains oversight and authority but chooses to devolve day-to-day management of activities to other units.

The cases reviewed in this paper do not fit easily into the broader patterns expected of their income groups. Uganda, Nepal and Sierra Leone, as the LIC grouping, show very different degrees of fragmentation (see Figure 11). Uganda and Sierra Leone have relatively centralised ministries. In contrast, Nepal displays a high degree of fragmentation, its finance ministry sharing many responsibilities with other ministries and commissions, as well as delegated agencies subordinated to the minister of finance. Chile, Mexico and South Africa show contradictory degrees of fragmentation, while the UK and Germany (as the two HICs) also demonstrate different levels of fragmentation. It is not clear, therefore, that the pattern identified in the wider literature regarding income level and centralisation of functions plays out in this more limited sample.

Within the sample, there is a trend with regard to the establishment of 'fiscal councils' in wealthier countries. These are institutions that have the effect of introducing additional constraints on macroeconomic policy-making, with the ultimate aim of improving a longer-term fiscal position at the expense of shorter-term political decision-making (Scartascini and Filc, 2007; IMF, 2013). Overall, the higher and middle-income cases within the study have gone furthest in setting up such bodies. The exact models of these councils vary considerably, and some (such as the UK's 'Official Budgetary Responsibility') are relatively new, whereas others (for example the German reliance on external economic forecasting institutes) are long-standing. This voluntary and increased reliance on external fiscal councils among HICs is not matched in the lower-income cases. Perhaps, the 'fiscal council' effect is achieved instead through the involvement in macroeconomic policy-making of the IMF, which remains a key stakeholder in Sierra Leone and Uganda.

Importantly, the role of the ministry of finance in engaging in policy debates beyond its 'core' responsibilities of economic and financial policy is also evident. In the UK, Mexico, Sierra Leone and South Africa, the voice of the ministry of finance is heard in many aspects of domestic public policy. In lower-income contexts, the absence of a well-developed policy development function reduces the ability of the ministry of finance to engage in policy debate, but it does allow for the (blunt) power of the purse to be brought to bear on issues of public policy, meaning that the ministry of finance cannot easily be excluded from significant policy issues.

5.2 Political leadership and autonomy

The ability of the ministry of finance to interact with the political environment was noted as an important factor behind the positive (or negative) performance in many of the case studies. This may play out through the status of the ministry or key personalities. For some of the countries it was the minister who influenced the direction and drive of the ministry; in others it was the top civil servants. Remarkable continuity of leadership has been evident in a number of the countries. Even in the UK and Germany, where leadership was not a central theme of the analysis of capability, the governments appear to value stability of ministers and top officials at the ministry of finance. Importantly, this ability transcends the formal politicisation of the civil service in all the countries under review, except Nepal.

Perhaps unsurprisingly, almost all the case studies made reference to the relationship between politics, institutions and budgetary management. The idea that national politics matters to the effectiveness of budget institutions and therefore the quality of outcomes is certainly not a new observation (see for example Caiden and Wildavsky, 1974). The literature certainly notes the negative impact that political decision-making can have in countries' central finance agencies, particularly in LICs (World Bank, 2011). In more recent times, an extensive literature has emerged that aims to relate more clearly cross-country differences in fiscal institutions to differences in fiscal outcomes (Hallerberg and von Hagen, 1999; Hallerberg et al., 2009b). This academic discussion relates predominantly to HICs, with relatively less attention given to LICs and MICs, but some key outcomes emerge. These studies suggest that countries that give strong 'delegated' authority to a finance minister to 'do the job' (often single-party government systems) or which have clear mechanisms of commitment to bind all actors into a budget agreement (particularly in coalition government systems) tend to perform better on fiscal outcomes.

The case studies seem to agree that the political power of the ministry of finance to deliver key budgetary outcomes appears more variable in low-income contexts. This may well reflect the less institutionalised and more personalised systems in these environments. Cross-country evidence suggest that in LICs, presidential power is typically misused with regard to expenditure and budget policy, and central finance agencies are deliberately fragmented for political gain (World Bank, 2011; Allen and Grigoli, 2011). Some of these issues are evidenced in the varying capability of the LICs in the study. In Uganda, the strength of the ministry of finance and the minister in controlling and directing expenditure has waxed and waned according to high-level presidential interest in maintaining an effective formal – rather than informal – budget process. Still, there has been fairly consistent support for the ministry of finance to deliver aggregate fiscal discipline. Sierra Leone has also seen success in handling the overall macroeconomic fundamentals of the post-war era, but relatively less on managing the disciplines of sub-aggregate budget credibility. Again, this can be linked to the political dynamics of the environment having a direct impact on budgetary practice. Nepal's example also shows how the politics of 'divide and rule' and frequent changes of minister reflect the fragmentation of the wider political system. Together, these examples agree that the informal power of the ministry of finance in low-income environments is particularly contingent on the shifting politics of the national context.

The MICs and HICs appear to show a more consistent pattern of politically powerful ministries of finance, with some relationship to the findings of the literature in this area. In Mexico, the Minister of Finance has usually come from the President's inner circle (meaning a greater possibility of 'delegated' authority), and in South Africa the minister of finance has historically been granted significant political autonomy to achieve budgetary objectives. In Chile, by contrast, it is the politically appointed – but not elected – Budget Director who is empowered (and therefore provided with delegated authority) to ensure budgetary discipline by virtue of a close relationship with the President.

In Germany and the UK, too, the Minister of Finance is seen as a powerful political position, beyond being 'one-among-many' at cabinet level, and not simply an administrative position that makes the numbers add up. Indeed, examples from the UK and Germany show just how crucial and influential the minister of finance can be during a moment of economic and financial crisis. For example, during the financial crisis of 2007/08, in both countries the ministry – and minister – of finance took a clear policy leadership role across government and operated with a great deal of autonomy and independence. This may indicate the use of a 'delegation' model to ensure fiscal discipline, although the nature of coalition government (long-standing in Germany but relatively new in the UK) may also put a premium on the 'contracting' approach to enforcing fiscal control.

The role of key personalities and leadership emerges differently in the case studies. Certainly, leadership is believed to have played an important role in raising the status and capability of the ministry of finance in Uganda and in South Africa. This appears to be less the case in the other countries reviewed. In Uganda, the former Permanent Secretary, Tumusiime-Mutebile, was identified as a key personality in establishing the ministry of finance as a centre of excellence in the Ugandan public sector in the 1990s before he became Governor of the Bank of Uganda in 2001. A member of the National Resistance Movement's struggle against Idi Amin, Tumusiime-Mutebile had strong political credentials within government and with the President, who reportedly allowed him significant autonomy in managing the economy and donor relations. He promoted a number of young and talented staff members into senior positions and was willing to back their judgement when challenged by external parties. Similarly, the longevity and influence of South Africa's minister of finance, Trevor Manuel, was seen as a main factor behind the National Treasury's success. Leading the National Treasury from 1996 to 2009, he fostered a spirit of critical thinking and open discussion that remains today. Like Tumusiime-Mutebile in Uganda, he used his political clout to reduce the budget deficit and reallocate expenditures, and remains an influential figure in South African politics.

The case studies of Mexico, Chile and Sierra Leone did not identify similarly influential characters, though they may well have existed or continue to exist. The case studies did, however, point to the personalisation of critical positions at the level of director. Most of the senior staff in the ministry of finance in Sierra Leone are former local technical assistants, hired by donors. These officials are generally young and highly qualified, and they work closely together to perform most of the core functions of the ministry. They are also the main points of contact for donors and the IMF, adding to their influence. But their powers did not appear to be delegated down the hierarchy, which raised important questions about who would succeed them.

The relevance of leadership raises important questions over stability and succession. Concerns over succession of influential personalities were raised in discussions with officials or external observers in Mexico, South Africa and Sierra Leone. Yet even beyond these ministries, a noticeable feature of the case studies is an emphasis on ministry of finance experience when determining the succession of key ministers and permanent secretaries. In some cases this has effectively become institutionalised, regardless of other institutional arrangements.

Having experience of working in public administration or economics is not always thought of as a prerequisite for being finance minister. Yet many of the case study countries place some value on such experience, and on continuity. In Mexico and Chile, ministers of finance generally have extensive experience in public administration. In the UK, Gordon Brown was well known as an economist, and was succeeded by Alastair Darling, who had previous experience as a junior minister in the Treasury. In South Africa, Minister Trevor Manuel was succeeded by Pravin Gordhan, who previously headed the revenue service. Gordhan has since been succeeded by the deputy minister of finance, Nhlanhla Musa Nene.

The preference for leaders with ministry of finance experience does not end there. The Ugandan Ministry of Finance is headed by the Permanent Secretary (or Secretary to the Treasury), aided by a Deputy Secretary to the Treasury (DST). There has been remarkable continuity in the leadership since the ministry was formed in 1992. Emmanuel Tumusiime-Mutebile was Permanent Secretary of the Ministry of Planning until he became the Permanent Secretary of finance when the two ministries were merged in 1992. Chris Kassami served as DST during this period and replaced Tumusiime-Mutebile in 2001 when he was appointed Governor of the Bank of Uganda. Keith Muhakanizi was promoted to DST, and later succeeded Kassami as Permanent Secretary in 2013.

Though not as striking as the Uganda case, some of the other countries have demonstrated similar patterns. The South African National Treasury is headed by the Director General. Internal observers have noted that recent directors general have been promoted from the Asset and Liability Management division. In the UK, the former Permanent Secretary Gus O'Donnell was succeeded by the Director – Budget, Tax and Welfare. O'Donnell, like his predecessor, has become the Cabinet Secretary. His successor, Nicholas Macpherson, retired in 2016 after holding the post since 2005. These are not truly institutionalised practices, or informal traditions, but suggest that ministries of various levels of capability and development benefit from (or at least prefer) continuity in internal leadership.

Tenure of top officials and politicians in all the case studies appears to be relatively similar, on average. Figures 12 and 13 look at the tenure of the previous five ministers of finance and top administrators. Though not perfect comparisons, they do reinforce the notion that all ministries have some degree of preference for continuity and stability. It may also point to the desire in more newly formed ministries to extend the tenure in order to build an organisational culture.

For nearly all elements of this discussion, Nepal presents a notable contrast, with exceptionally high turnover rates

Figure 12: Tenure of ministers and top officials

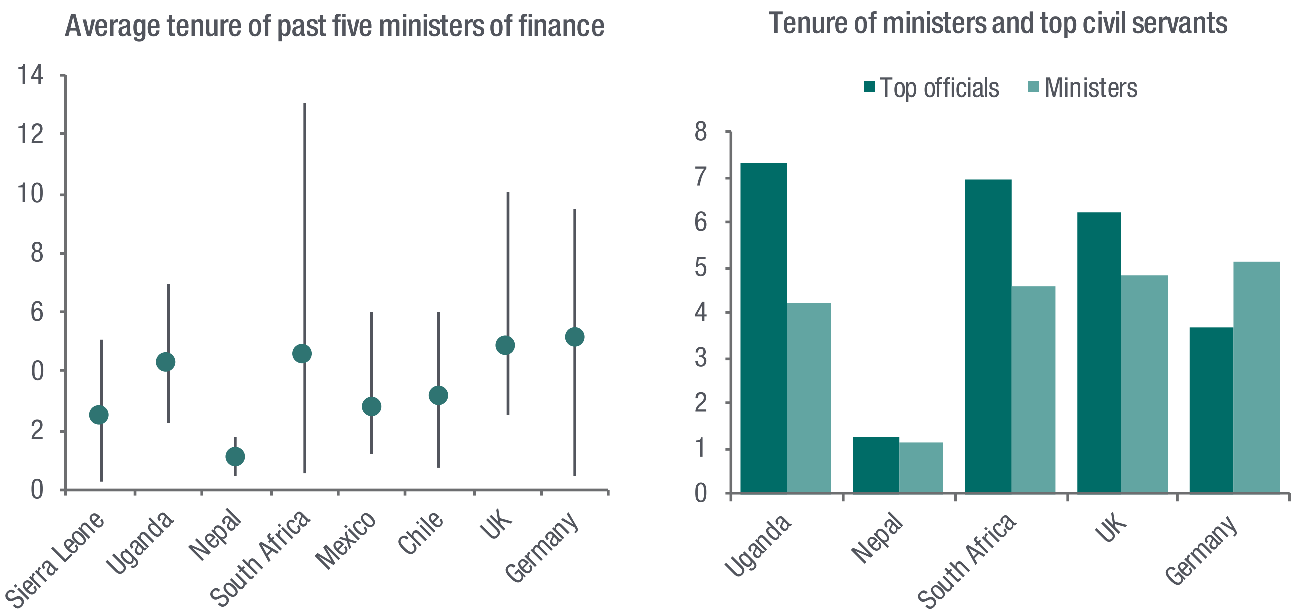
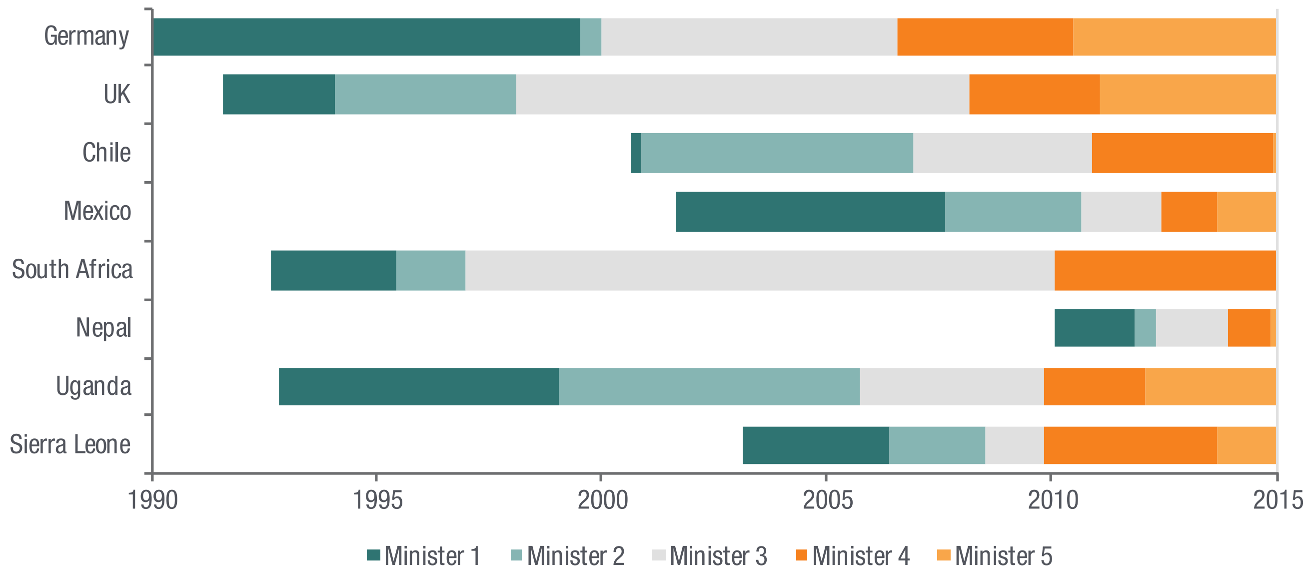


Figure 13: Tenure of the past five finance ministers



in the positions of both finance minister and permanent secretary. The average tenure for these two positions is around a year. Of the five most recent ministers, none has been in post for more than two years – with only one of the five permanent secretaries exceeding that benchmark. These changes – often rotations – are politically motivated and extend to the other central finance agencies as well. Together with the substantial fragmentation of responsibilities, this was noted as a major hindrance to the capacity of the ministry.

A final consideration is the politicisation or autonomy of the bureaucracy. Considering the eight finance ministries on these grounds, it seems that there are three broad groups. In Chile, Germany and Mexico, civil servant appointments are *formally politicised* within an established set of rules. In the UK and South Africa, appointments are *mostly autonomous* of politicians, who exact some degree of influence on the highest positions, possibly through mutual agreement or a shared sense of 'mission'.[7] This leaves a middle group that are *informally politicised*. This group includes all the LICs (Nepal, Uganda and Sierra Leone), which have formal rules to preserve independence but which are nonetheless influenced through political channels. There is an important connection between politicisation and the leadership dynamics at the top of the ministry; for instance, if politicians and senior bureaucrats share political affiliations, they can forge strong links that shape how the rest of the organisation relates to the political leadership.

In Chile, Germany and Mexico, politicisation is included in the formal rules of appointment. The Chilean Budget Director is considered a critical role and is appointed by the President directly. In Germany, Administrative State Secretaries are the most senior civil servants in the Ministry of Finance. They, together with division heads, are recruited as political civil servants with the approval of the federal government.[8] There is also space for more junior partisan officials, though these are not recruited in the same way. Mexico also politicises management positions. At the start of each new administration in Mexico's government, new personnel are appointed to political positions in the civil service, including the Under Secretaries, Heads of the Administrative Central Unit, and Heads of Units. In some cases politicisation may even extend to the Directors General and Deputy Directors General, despite being formally part of Mexico's professional civil service.

In contrast, bureaucracies in South Africa and the UK are highly autonomous, with only a limited degree of informal politicisation. Formally, appointments in the

7 In the UK, ministerial influence may only extend informally by requesting a permanent secretary to volunteer for a 'managed move' to another position, though the government is currently considering whether to give ministers a more formal role in appointing their permanent secretaries (Paun et al., 2013). In South Africa, commentators have reported on the politicisation in the top tier of the civil service. Some have speculated that this may be happening intentionally through the use of the affirmative action policy; but equally it may be that the division between the state and the African National Congress (ANC) is being blurred by the indoctrination of civil service officials by ANC policy. (Maphunye, 2005)

8 This political cadre is known as politische Beamte, and has existed in the federal bureaucracy since 1848.

UK have been made by the Civil Service Commission, though this changed slightly under the 2010 Constitutional Reform and Governance Act. Now, power of appointments for all civil servants is vested in the Prime Minister, but for all intents and purposes it remains with the Civil Service Commission, which sets the recruitment principles. Similarly, in South Africa appointments are made officially through the Public Service Commission. However, it has been suggested that politicians in both countries have a degree of informal influence at the top of the bureaucracy.

Finally, the experiences of the UK and South Africa suggest a third category – one where the civil service is formally independent but informally politicised. Nepal, Uganda and Sierra Leone all appear to fit these features to varying extents. All three countries have maintained formal civil service models established under British colonial rule – with recruitment overseen by an independent public service commission. However, in practice, appointments may be politicised or subject to patronage. The Nepalese civil service is generally regarded as highly professional, though the top ranks are more likely to be perceived as 'political' (Krause et al., 2013). In Uganda, only the ministers are politically appointed, although senior civil servant appointments are believed to require unofficial State House approval. The situation in Sierra Leone is not clear – partly because of reliance on donor-funded staff at management level – though it seems likely that patronage plays a role.

Importantly, the case studies suggest that bureaucratic autonomy is not an important determinant of the finance ministry's capability, nor does it seem to limit or enhance its ability to interact with the external political environment.

Overall, this review cannot confirm the expectation that ministry of finance functions are expected to be fragmented in LICs, be more centralised in MICs, and then fragment again as income per capita increases. It is particularly true for the LICs. However, the reasons for fragmentation or centralisation of powers may be important: some of the fragmentation is initiated by the government in the name of efficiency, while other constraints are imposed to enhance aggregate macroeconomic performance. Equally, Chile has centralised powers in response to earlier failures to manage expenditures financed predominantly from volatile revenues.

There is also evidence that the influence and stability of leadership plays an important role in the capability of the ministry, and perhaps more so for ministries that are still building an organisational culture. Even where institutions are well established, as in Germany and the UK, tenure for ministers and permanent secretaries is clearly desired. In contrast, the turnover rates in Nepal for the Permanent Secretary and Minister have been unusually high, which was raised as a significant barrier to building a more capable ministry of finance.

Despite the importance of the minister and top senior officials in many of the case studies, the level of bureaucratic autonomy does not appear to be a significant constraint on capability. The case studies present a range of bureaucratic models. Yet in each case the ministry has emerged as relatively capable.

5.3 Typologies of organisational structure

How a ministry organises itself internally is expected to influence its capability. For example, it is reasonable to expect the size and structure of the ministries of finance to vary with the level of institutional maturity, the complexity of the work, and the style of internal decentralisation and coordination. After all, it would be unlikely that the Sierra Leone Ministry of Finance employs as many people and has as many internal structures as the UK Treasury. Reading across the case studies suggests that this is partly true. Yet, the lack of clear correlation between sheer size of a ministry of finance and its capacity is well noted in the literature (Allen and Krause, 2013; Allen and Grigoli, 2011.

Many of the case study country ministries look remarkably alike, with a bureaucratic structure with four levels of administration – i.e. directorates, departments, units and sub-units. However, there are notable differences in organisational size and in the degree of horizontal fragmentation: in other words, some ministries have a lower ratio of managers to professional staff than others. This may confirm differences in the prime coordinating mechanism or style of decentralisation. To consider these high-level observations in more detail, this section considers the number and distribution of staff, organisational structure, and the flexibility of movement within the ministry.

Underpinning the logic of Mintzberg's typology is a Weberian notion that some forms of organisation are more developed than others. It may be possible to consider the period of establishment as a crude proxy for organisational maturity – specifically, the time that the institution has existed in its modern form. Among the case study countries this varies considerably from a couple of decades to a couple of centuries. This imprecise approach suggests three or possibly four useful groups.

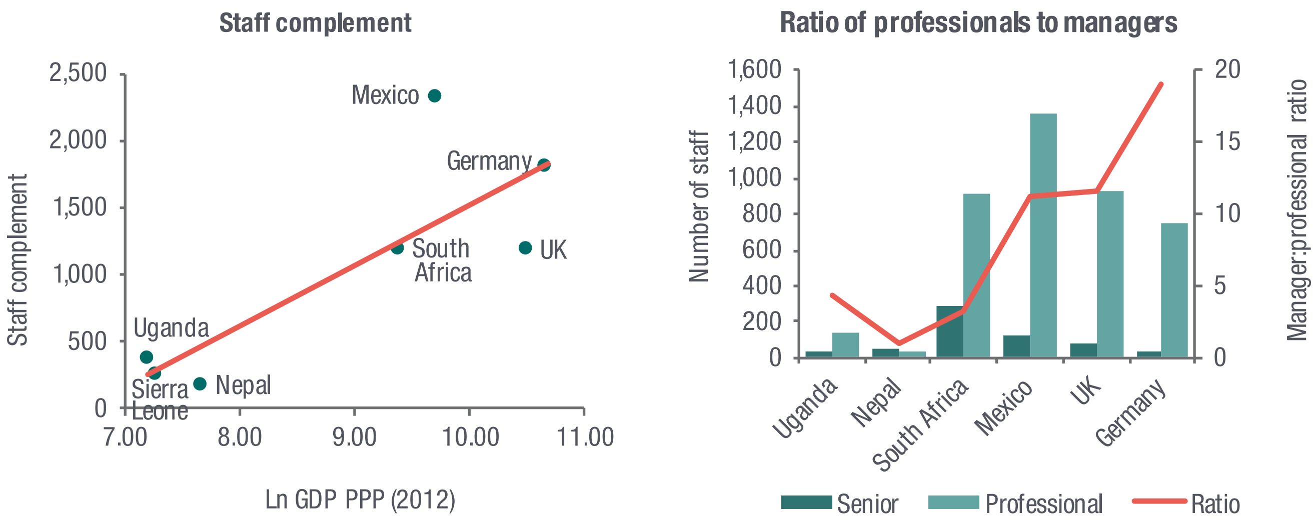
The first is the two European nations. These have deeply embedded institutions stretching back centuries, which have been established in relatively modern form for around 150 years. The second captures the two Latin American nations, whose PFM institutions emerged around 100-150 years ago but gained their central standing in the first half of the 1900s. It may also be relevant to include South Africa's National Treasury in this group. Though the National Treasury has changed significantly in the post-apartheid era, the foundations have arguably been in place much longer. The final group is represented by the former British colonies of Nepal, Uganda and Sierra Leone. Post-independence conflict and political instability mean these countries have PFM institutions largely developed since the 1980s, and in the case of Sierra Leone mostly since 2000. Given that institutional and economic development are closely intertwined (Acemoglu et al., 2001), it should not be entirely surprising that these groupings for the most part reflect the state of human and economic development.

As expected, the ministries vary considerably in size (Figure 14). The number of staff ranges from under 250 in the Ministry of Finance and Economic Planning in Sierra Leone to over 2,300 in Mexico's Ministry of Finance and Public Credit. This roughly excludes the accounting cadre. Perhaps unsurprisingly, countries with larger economies (in absolute or per capita terms) generally have larger finance ministries. South Africa and Mexico have particularly large ministries of finance in this regard.[9] The reasons for this are not immediately clear. Perhaps this reflects limited PFM capacity in line ministries or local governments that are compensated through the central finance agencies. Alternatively, these institutions may have wider responsibilities or operate greater microbudget controls, requiring more staff. At the other extreme, Nepal's Ministry of Finance is relatively small, mainly due to the high degree of fragmentation of its central finance functions.

While the internal hierarchies look similar, the horizontal allocation of responsibilities does not. Looking specifically at responsibilities for budgeting shows how some of these differences are tied to their unique PFM systems. For example, the UK Budget, Tax and Welfare department coordinates the annual budget but is not responsible for managing the budgets of line ministries. This is because the Spending Review sets expenditure ceilings for ministries for a fixed three-year period. Therefore, the annual budget deals mainly with changes to tax rates and welfare spending. As a result, expenditure has been the responsibility of the Public Services and Growth Department, while tax and welfare spending fall in the mandate of the Budget, Tax and Welfare Department. On the other hand, there appear to be some functions that are usually divided. These include specialised disciplines like accounting, auditing and financial services, but also some functions such as the responsibility for the macro-fiscal framework and managing line ministries.

Another striking difference can be found in the management structure (Figure 14). The finance ministries of Germany and the UK have the highest ratios of managers to professional staff, and Nepal has by far the lowest.[10] Again, the significant differences between these organisations means conclusions are highly speculative. However, it is likely that in the finance ministries of the UK and Germany there is less reliance on direct supervision of professional staff by the top tier of managers than in the other ministries, and that the main operating core conducts most of the work. These are classic traits of a professional bureaucracy. It may also suggest that in the other ministries, responsibilities for delivery are held at a

Figure 14: Number of staff and the ratio of professionals to managers



9 Including the Central Administrative Unit, Mexico's Ministry of Finance and Public Credit employs more than 5,800 staff, which is more than the Ministry of Foreign Affairs, Ministry of Labour, Ministry of Social Development and other policy-oriented ministries. Excluding the Central Administrative Unit halves that number and makes the ministry more comparable to departments with similar functions, such as Public Administration and Agrarian, Territorial and Urban Development.

10 This ratio in Uganda is higher in practice than in the budget because of a high vacancy rate for professional positions – at the time of research, as much as a third of these positions were unfilled, while most management positions were occupied.

more senior level, so relying more on middle and senior managers.

The case studies appear to support this broad conclusion. For example, in Sierra Leone many of the basic functions of the budgeting process were delivered at the director level. This included compiling and amending the budget as well as handling day-to-day claims on treasury resources from suppliers and line ministries. Despite the existence of a formal reporting structure within the ministry, it was also clear that directors would regularly follow directions from the Financial Secretary himself. Uganda does not operate with the same degree of direct supervision from the Principal Secretary, but in the past, commentators have noted just how important the position can be: one donor official suggested that when Tumusiime-Mutebile (Permanent Secretary from 1992 to 2001) left the country on official visits, donors would panic because all their projects went through him (Harrison, 2001). In contrast, there were no such suggestions in the case studies of Germany, the UK, Mexico or South Africa. A more subtle reading could suggest that the more institutionalised ministries rely less on individual personalities.

Between the two HIC examples, there is also interesting variation in the institutional manner in which policy engagement occurred. In the UK, the spending control and policy engagement functions are merged in combined 'spending teams', whereas in Germany, financial control and policy development functions are separated into different parts of the institution. Overall, it seems that the UK Treasury resembles much more the ideal type of a professional bureaucracy, whereas the German Ministry of Finance still retains many elements of the machine bureaucracy ideal type (Figure 15). Neither of these organisational forms seems necessarily much better suited to their tasks than the other, but the differences are very notable.

The distribution of staff suggests that the ministry of finance may evolve as institutions develop, shifting away from characteristics of a simple structure to a machine bureaucracy and then a professional bureaucracy. In Sierra Leone, a smaller number of staff and reliance on a group of directors for delivery implies that the ministry relies more on direct supervision by the Minister and Permanent Secretary to coordinate internal activities. In Uganda, direct supervision still plays a role, but there is certainly greater evidence of standardisation and delegation consistent with a machine bureaucracy. The similar ratio of professionals to managers in South Africa suggests that the National Treasury is also demonstrating characteristics of a machine bureaucracy. The case of Mexico is less clear: dependence on a large number of support staff is more indicative of a machine bureaucracy than a professional bureaucracy, yet the ratio of professional to managerial staff is similar to the UK, which more clearly demonstrates the features of a professional bureaucracy – with a relatively independent operating core of policy advisers.

5.4 Staff roles and salaries

A critical similarity across the case studies is that senior officials of the ministries studied were broadly content with their ability to attract and retain the right quality of staff. The ways in which they achieved this were also remarkably similar. Key differences lie along a number of lines. Firstly, remuneration was seen as generally adequate to attract and retain staff, but it varied in the use of non-salary benefits and in the gaps between top and bottom salaries. Secondly, recruitment and promotion were supported by meritocratic principles, even in more politicised (or patronage-based) environments. Finally, positions were generally filled using internal promotion, with minimal use of external recruitment or consultants.

As a primary means to attract, incentivise and retain staff, salaries and other benefits form an important dimension of the bureaumetrics of an organisation. Overall, interviews and secondary sources suggest that nearly all the ministries in this small sample have been able to offer sufficient remuneration – monetary and other – to attract and retain the staff needed to perform. Surprisingly, this was the case for the finance ministries in Sierra Leone, Nepal and Uganda, despite the low salaries of some officials. More in-depth comparisons reveal a number of interesting similarities and differences.

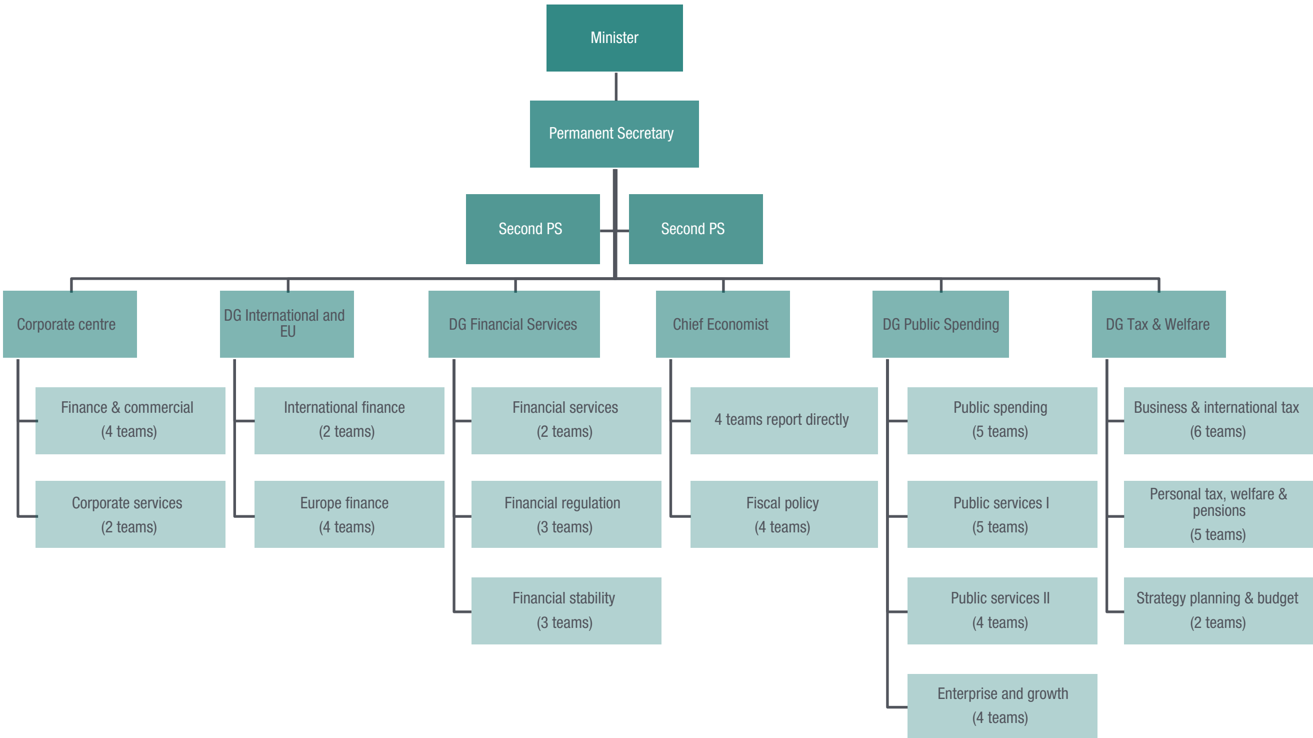
The first observation is that the ratio of salaries of entry level staff to average GDP per capita is inversely related on a purchasing power parity (PPP) basis for most countries (see Figure 16). This should not be surprising as more advanced economies will have greater access to the skills needed to conduct the core functions of the ministry of finance. However, this contrasts markedly with the salaries of the permanent secretary or other top-level administrator (the CEO), which exhibits a weaker trend. As a result, the salary differential between entry level staff and the top administrator varies enormously – from less than 2 in Nepal to nearly 18 in Mexico (Figure 17).

However, this observation needs to be treated with caution. Salary information for Sierra Leone and Chile were not available at the time of writing, and the data are not all directly comparable. In particular, salaries in LICs make up a smaller proportion of overall remuneration than in HICs. Entry positions may also come with different levels of responsibility.

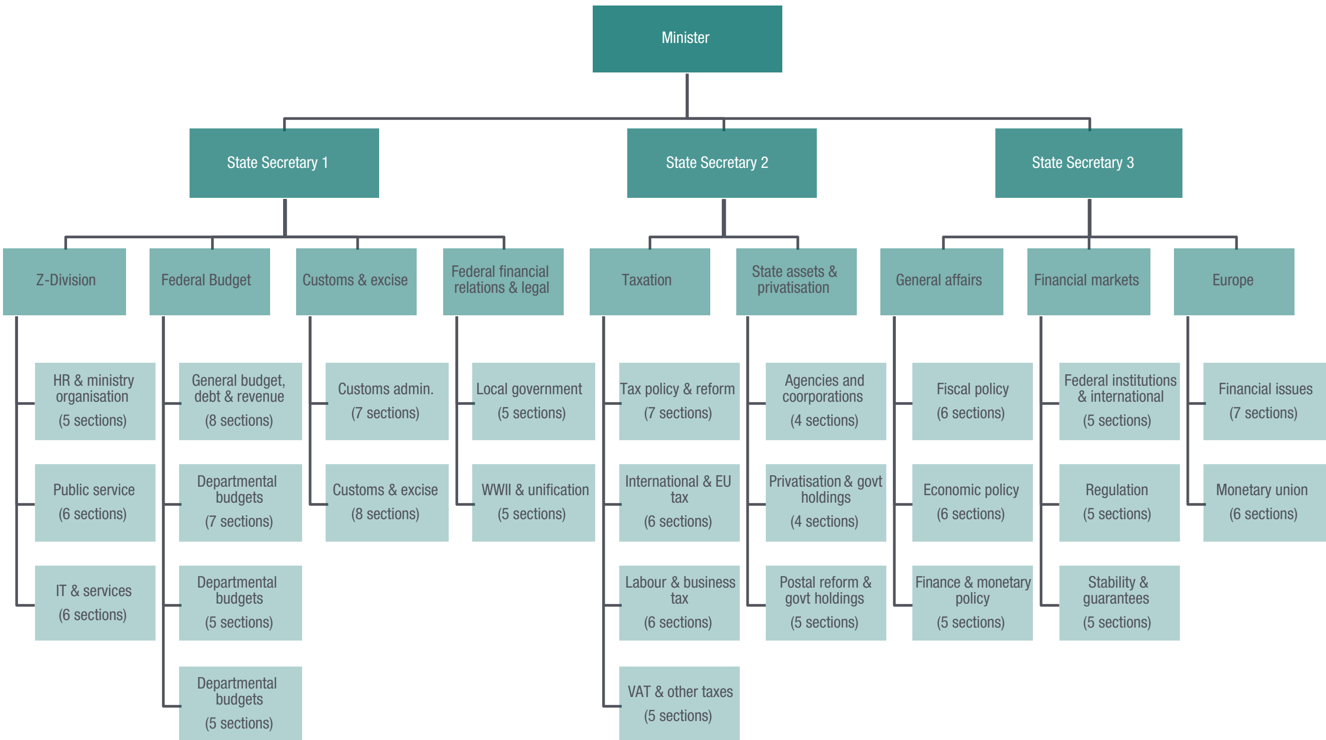
A second, related, generalisation is that ministries of finance in MICs and HICs rely less on allowances and other benefits. Data are more difficult to find and standardise than data for salaries, but anecdotal and

Figure 15: Organisational structures of German and UK finance ministries

UK Ministry of Finance



German Ministry of Finance



Source: Bundesfinanzministerium and Her Majesty's Treasury, respectively budget information suggests that staff in the finance ministries in Uganda and Sierra Leone benefitted considerably from allowances, 'per diems' and in-kind benefits. One explanation for this finding is that these ministries are embedded in bureaucracies that tend towards standardisation, including of salaries. The rational reaction has been to find alternative ways to remunerate staff sufficiently to retain them. Donor organisations have also played their part. In the 1990s, Uganda supplemented salaries with donor top-ups. More recently, in post-war Sierra Leone, salaries for some ministry of finance posts were fully paid by donors until being absorbed into the domestic payroll in the late 2000s. This has resulted in a binary structure for pay – with former local technical assistants earning many times more than their counterparts who had progressed through the civil service system.[11] Overall, nearly all the ministries have found one way or another to attract and retain the staff they need.

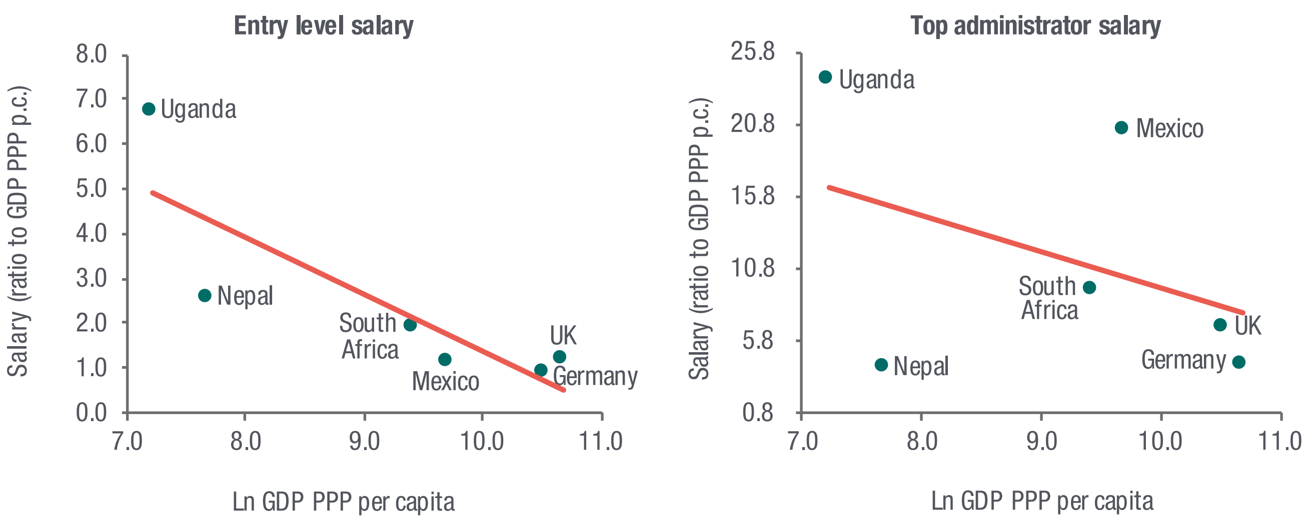
One significant exception is the UK. Turnover rates in the UK Treasury are exceptionally high among professional staff, averaging over 25% per annum. This is also not a new feature of the organisation, but one that has persisted over several decades and is closely linked to opportunities for promotion and salary levels, which are on average lower than in other central government departments. Inaction by the organisation suggests that this has now become the Treasury's business model – with a stable group of senior civil servants supported by a young, mobile operating core.

Finally, though most of the case studies suggest that salaries are adequate in general, most ministries of finance experience difficulties attracting and retaining some skill sets. There were some particularly notable examples. South Africa's National Treasury identified which of its financial analysts who are able to move to better paid jobs in the financial sector. Uganda faced particular challenges recruiting IT professionals, and has resorted to using contractors instead. It is important to qualify that entry level wage rates remain considerably lower in LIS and MICs than in the UK and Germany. This is true even when adjusting for purchasing power, which will be greater in most LICs (Figure 17).

Recruitment and promotion practices can also be used to build an organisation. This raises important questions about the availability of key skills and the culture of an organisation. Should promotion acknowledge seniority or political affiliation or be purely merit based? Are staff trained and promoted from within, or are they picked from the external labour market? When should permanent civil servants be hired, and when are temporary contracts preferred? The case studies touched lightly on each of these issues, providing a number of useful insights.

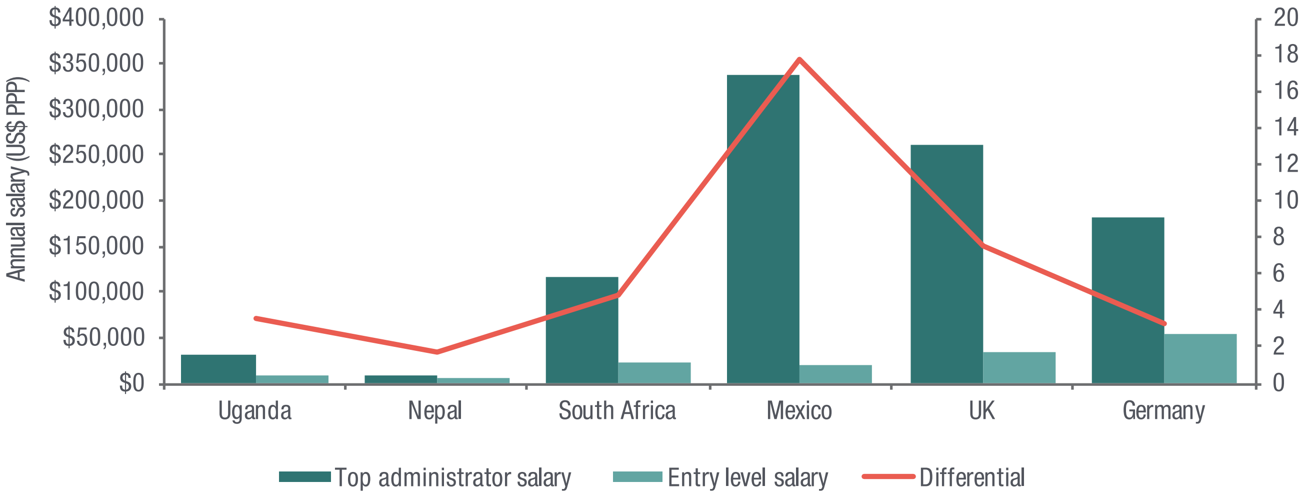
One was that, regardless of the level of formal politicisation or patronage, these ministries of finance appear to recruit and promote most staff on the basis of merit. At the more established end of the scale, Germany's political system continues to accommodate 'political civil servants' with a known party affiliation. But this system provides means of permitting that political involvement,

Figure 16: Salaries of entry level staff and the top administrator



11 In a similar study on Sierra Leone, Viñuela et al. (2014) found that six departments of the Ministry of Finance and Economic Planning were headed by local technical assistants (LTAs), and in total the number of LTAs exceeded professional civil servants. On average, LTAs are younger and more qualified than their counterparts and earn considerably more. On a monthly basis, they estimated that professional grades in the civil service earned between US$119 and US$1,391, while contract staff received between US$1,744 and US$2,500.

Figure 17: Wage compression (US$ PPP)



while at the same time maintaining the merit basis of their initial appointment (Derlien, 1996). The case study in Mexico notes that having professional experience in the Bank of Mexico, or in the ministry of finance itself, has become the rule for the finance ministry's personnel and even for its political appointees. While Chile's Budget Director is appointed directly by the President, candidates are usually strong technocrats, who commonly have experience within the ministry. Interestingly, donor involvement in the staffing of the Ministry of Finance in Sierra Leone also means that most of the professional staff have been selected (and managed) on a meritocratic basis (Viñuela et al., 2014). This provides further support for the earlier suggestion that each country's elite regard the ministry of finance as an important department. It may also be behind the relatively strong performance of these ministries compared to the line ministries they manage – building a reputation and organisational culture of excellence.

This common storyline reflects another tendency: the preference to promote from within rather than hire externally. The stability of the Permanent Secretary and Minister were notable features in many of the case studies. Data are more limited for lower levels. However, the case studies suggested that all the ministries generally promoted staff internally and used consultants sparingly. Interviews with staff in the South African National Treasury noted that this was not always straightforward, because the skill sets of technical and managerial staff are different. The UK Treasury faced a very specific problem when the financial crisis struck in the late 2000s. Lack of internal knowledge of financial sector management forced the organisation to hire externally to quickly acquire the skills needed. In general, these practices were tied to specific skills or events, rather than being a common feature of the finance ministry.

An interesting point of divergence for some ministries was the vacancy rate. Though data were not available for all the case studies, there appear to be significant differences between the countries. Vacancies in the UK appear to be minimal, though data were only available for senior civil servants. On the other hand, Uganda's Ministry of Finance has struggled to fill a large proportion of its official establishment (see Table 5 for a recent snapshot). In between, Mexico's Ministry of Finance and Public Credit had a vacancy rate of around 12% in May 2014, while officials in the South African National Treasury noted that the vacancy rate has fallen considerably in the

Table 5: Vacancies in the Uganda Ministry of Finance (2011)

Department	Filled positions	Approved positions	Share filled
Ministers/senior management	17	21	81%
Directorate of Budget	53	72	74%
Directorate of Economic Affairs	101	129	78%
Accountant General's Office	114	185	62%
Support departments/units	89	149	60%

past decade, to around 8%. They also claimed that the National Treasury was usually able to fill positions within a year. The higher vacancy rates in some ministries may be related to periods of expansion (as in South Africa) or rigidities in the hiring process (as in Uganda). Overall this suggests that these ministries may be operating within their own potential capability, or it could signify that these organisations rely more heavily on the middle line and strategic apex for delivery.

One striking feature common to almost all countries reviewed was the relatively high calibre of staff working in ministries of finance compared to other public institutions, and the degree to which this allowed the ministry of finance to wield additional authority above and beyond its formal powers. This appeared across the income spectrum, with the possible exception of Nepal where there was no explicit discussion of the relative quality of staff compared to line ministries.

In the LIC examples of Sierra Leone and Uganda, donors had played a significant historical role in providing salary top-ups to attract and retain effective staff. In both cases, staff have transitioned onto the more regular payroll; and when direct salary enhancement ceased in Uganda, most skilled staff elected to remain in the institution. In Chile, Mexico and South Africa, the esteem in which the finance ministries are held attracts strong recruits, partly on the basis that a period at the respective ministry of finance offers the prospect of employment in the private sector at later date. The high quality of staff entering the UK and German ministries of finance is noted elsewhere in the literature (Allen and Krause, 2013).

The relatively high skill level of ministry of finance staff compared to other public sector workers is not immediately relatable to length of tenure of staff in the institution or to the overall numbers of staff in the institution. While the ministries in Sierra Leone, Uganda, Mexico and South Africa reported that staff stayed with the institution for a long period, this is less the case in the UK and Nepal, where relatively high turnover of staff is the norm. While turnover is lower for professional staff than senior management in Nepal, the opposite is the case in the UK Treasury. In this way, it appears that the UK has established a fairly unique approach to maintaining a workforce of competent technical staff – including by having first pick (together with the Cabinet Office) of graduates recruited centrally through the annual 'Fast Stream' process.

All countries under review have organised their staff into a number of cadres. In most there are designated positions for accountants, auditors, procurement specialists, statisticians and other specialised fields. These often reflect divisions in mandate, or even boundaries between organisations. However, the case studies also reveal that some countries may have encouraged greater specialism within the core ministry of finance than other countries. This is partly evident in the degree that staff are able to move laterally across the organisation – because the easier it is to move to other departments, the less specialised they are likely to be in practice.

Anecdotal evidence suggests that the UK allows a high degree of rotation between departments in HM Treasury. Professional staff members in entry level grades usually change post every two to three years, with greater stability for each grade above. However, it is not uncommon for officials to move between sectors, or shift from the budget department to a team responsible for international or financial services. This suggests the Treasury's operating core is a team of generalists, at least at lower levels. The case study of Germany's ministry of finance suggests that staff members are less mobile than their counterparts in the UK. Though junior officials are expected to change section every three years in order to be eligible for promotion, they are generally expected to become specialists within a given department. In this regard, South Africa's National Treasury is similar – encouraging some rotation, but often looking for officials to become specialists in their field. So is Mexico's Ministry of Finance and Public Credit. The case study notes that 'There is some personnel rotation, but people tend to stay in financial areas'. In contrast, Sierra Leone and Uganda appear to be more tightly confined. In Uganda, for example, desk officers may change from one sector to another but are likely to make their career within a given department. There was no evidence in the case study of Sierra Leone to suggest that finance staff changed departments, even on promotion.

It is not clear how differences in this internal job market influence the capability of the ministry. The UK Treasury has sought to encourage longer postings, which have previously been as short as six months, suggesting that too much movement is a barrier to capability. On the other hand, the growth of the South African National Treasury has led to less flexibility, lamented by some of senior staff as having a damaging effect on the working culture. Certainly, finding the right balance appears to be a key aim in both institutions.

Overall, the ministries have shown remarkable consistency in their ability to attract and retain staff necessary to build a capable ministry of finance. This is regardless of the large differences in pay and wage compression. All appear to favour the skills acquired working within the ministry of finance, and all promote internally for the majority of positions. However, the ministries have taken different approaches to building the capability of their workforce – with a notable struggle to get the right balance between specialism in a policy field and the generalism needed to understand policy issues across the ministries' respective portfolios.

5.5 Conclusion

As with other chapters, caution is needed when generalising across this diverse set of case studies. Yet despite their differences, the organisational arrangements within these ministries of finance are surprisingly similar. This is especially true when contrasted with the significant differences in the distribution of central finance functions across agencies – and even the way that functions within the ministry are delegated.

Clearly, these ministries have distinct features that depend on their institutional environments. Chile, Mexico and Germany have permitted a degree of formal politicisation. In contrast, the UK remains a highly independent civil service, while Nepal, Sierra Leone, South Africa and Uganda appear to have adopted systems of informal politicisation for the top tier of civil servants at least. Despite this, recruitment and promotion in all the case studies is described as predominantly meritocratic, even in the case of politicised posts. This may be a key element of establishing a ministry of finance as an island of excellence in the public sector.

The ministries are also at very different stages of institutional maturity. While the PFM systems of the UK and Germany have been embedded over hundreds of years, Chile's and Mexico's have been formed predominantly over the past decade. The systems of Nepal, Uganda and Sierra Leone have their roots partly in colonial administration but have been disturbed by political and economic instability. These broad groups are also reflected in the organisational typology suggested by Mintzberg (1979). The younger ministries appear to be more dependent on their strategic apex and direct supervision to deliver. In South Africa, the burden may instead have fallen to the middle management line, while Mexico operates a more machine-like bureaucracy than the UK and Germany, where the operating core is responsible for most of the delivery of ministry of finance functions. This may be why the ratios of professionals to managers differ. Certainly, Germany and the UK have fewer managers than South Africa and Uganda. Whether this is matched by higher levels of capacity for the ministry remains speculative.

Perhaps the nature of the economy also plays a part in the size and staffing of the ministry. A more complex economy may require a larger ministry of finance. In this set of case studies, that does seem to be the case, though comparisons are muddied by differences in data and functional responsibilities. Ministries in the more advanced economies are also probably more able to recruit skilled staff. Certainly, the UK and Germany do not have to pay a significant premium over and above GDP per capita (on a PPP basis).

Yet despite these differences there are remarkable similarities. Staff size varies, but most of the ministries have adopted a four-tiered bureaucratic structure – with directorates, departments, units and sub-units. There also seems to be a limit on how big a ministry of finance can become in practice – excluding cadres for accountants and auditors, anyway. Perhaps this indicates a threshold beyond which additional staff add relatively less value or exceed the tolerable opportunity costs for politicians.

Nearly all the ministries studied have found ways to attract and retain the staff they need. The larger economies do it predominantly through salaries, while Nepal, Uganda and Sierra Leone use allowances and other benefits (monetary and in kind) to offer adequate levels of remuneration. This may be a rational reaction to ridged wage and hiring systems in the civil service more widely, and certainly is supported to some degree by international donors. Naturally, there are always challenges in attracting or developing some skills. South Africa's National Treasury must compete with a vibrant financial sector for talented analysts, and has identified upper-middle and lower-upper management skills as particularly challenging to develop internally. In Uganda, the analysis suggests that while suitable economists can be hired, attracting IT skills is more challenging.

There is also a strong preference for continuity in leadership and promoting staff internally. The tenure of recent ministers and top civil servants in most of the ministries studied averages around four years, though some incumbents have exceptional periods in office (such as Gordon Brown, Trevor Manuel and Emmanuel Tumusiime-Mutebile). The case studies for Uganda, South Africa, the UK, Germany, Mexico and Chile all highlighted preferences for promoting internally, to the extent that some promotion practices appear almost institutionalised – such as the progression to Permanent Secretary in Uganda, or Director General in South Africa. This may be particularly important in ministries that are developing their organisational cultures, such as in Uganda, South Africa and Sierra Leone. Certainly, the case studies suggested that these ministries rely more prominently on the influence of specific personalities – ministers, top bureaucrats, or even directors – to build the organisation's capability.

The Ministry of Finance in Nepal is a notable outlier throughout. Highly fragmented responsibilities are coupled with considerable turnover in staff and leadership. Salaries were believed to be adequate, and the organisation considered itself to be a relatively strong performer in the public sector, but there was considerable political interference, particularly regarding the rotation of staff. The organisation is also exceptionally top-heavy, with almost as many managers as professionals. There is little doubt that these organisational features contribute to more limited institutional capability. So while bureaumetrics are unlikely to be the main drivers of finance ministry capability, they do appear to matter.

6. Conclusion

This report outlines an approach to understanding the capabilities of finance ministries and provides evidence from eight country cases to outline the variation found in practice, as well as the key emerging issues and patterns. Section 2 reviews the purpose that finance ministries serve in government, their institutional context, and the functions they take on. It then outlines a definition of capability. Section 3 discusses the fiscal and socioeconomic performance of the eight case study countries and finds that while finance ministries are often held responsible for aggregate outcomes, it is essentially impossible to establish any causal relationship between capable finance ministries and aggregate economic performance. It concludes that finance ministries are a key ingredient of good performance – but more in the sense of a necessary condition for policies to be implemented than a sufficient condition for good performance to be achieved.

Section 4 discusses the relationship between finance ministries and their institutional environment, concluding that government institutions create the space in which finance ministries operate, both enabling and constraining them. Section 5 reviews the key ingredients of finance ministries as organisations, looking at the specific tasks a ministry takes on, the role of political leadership, and organisational structures, as well as staff roles and salaries. It finds that there are many things we do not know about the internal workings of finance ministries. The evidence from the cases suggests that there are many different ways in which finance ministries structure themselves in response to external challenges, which are very particular to the institutions, administrative legacies and politics of a given country.

The case study countries were chosen with a view towards examples of capability even in conditions that make it difficult for capable institutions to emerge or sustain themselves. It is therefore not surprising that none of the case study finance ministries is completely incapable of performing against its assigned tasks. At the same time, there are important differences in how this capability is achieved in different contexts, and in where the biggest challenges arise. The remainder of this section will discuss each of the four capabilities – delivery, analysis, regulation and coordination – in turn, and conclude by outlining some of the implications for international policy.

6.1 Analysis of capabilities

Within the broad term of delivery, two different functions are worth distinguishing. The central finance function contains a set of broad administrative delivery functions, where large-scale operational units produce certain products on a regular basis. These are most importantly the administration of tax, customs and other revenues; the administration of cash flows and procurement; and the production of regular reports, audits and other checks on the financial operations of government. Apart from these administrative delivery functions, there is a more complex policy delivery, which manifests itself specifically in the preparation of the budget and its assorted suite of products (the budget itself, a pre-budget statement, accompanying policy statements, the minister's budget speech, and so forth).

There is a striking difference in the way delivery capability manifests itself in the LICs in the sample (Sierra Leone, Uganda and Nepal), as opposed to the UMICs and HICs. For each of the LICs, some aspects of the finance ministry's delivery function pose challenges, although not necessarily in the same way, whereas for the richer countries, delivery becomes so regular that it almost seems invisible to the observer and to officials themselves.

As a consequence, many finance ministries tend to start delegating and outsourcing administrative delivery functions. Nearly all of the countries in the sample have semi-independent revenue and customs agencies under the ministry of finance, a trend that now extends well beyond the OECD. Germany never had a central tax administration under the finance ministry to begin with, since revenues are collected by the states and not the federal government. Audit and control functions are increasingly pushed out to line departments and ministries, a move consistent with a shift towards more macrobudgetary control.

At the same time, most countries do not struggle with the delivery of the core finance ministry policy products, most notably the budget. A comparison of 95 countries has shown that more than 80% of countries keep to a budget calendar that allows budgets to be submitted to legislatures at least two months before the start of the fiscal year (Figure 18). A significant minority of mostly LICs starts and concludes budget negotiations much later than the average and only submits the budget very shortly before or even after the fiscal year starts, with negative consequences

Figure 18: Budget delivery capability

Source: Krause et al. (2013)

for budget credibility and implementation (Krause et al., 2013). It is worth noting that budget crises are not the prerogative of LICs, and especially in the United States a succession of crises, extensions and missed deadlines is quickly becoming the new norm (Wang, 2013). But the ability of the Office of Management and Budget to deliver the budget to the legislature on time is not in question.

The overall trend seems to show that administrative delivery capabilities are increasingly outsourced or delegated, and policy delivery capabilities have become commonplace. There seems to be a transition taking place roughly when countries reach UMIC status, at which point these delivery outputs and the capability to run such administrative processes fail so rarely that they are assumed to just work. A measure of system credibility also seems to be at work. It has been noted elsewhere that many weak PFM systems suffer from a gap between formal and informal practices, which limits the credibility of the budget and in turn the ability of central ministries to exercise control (Andrews et al., 2012). It is reasonable for finance ministries to be reluctant to release control over administrative delivery functions when the credibility of the overall system is in doubt, because administrative delivery for finance ministries is very closely tied to the flow of funds and therefore the most crucial part of PFM. For ministries at the other end of the spectrum, the distance of administrative delivery from the core policy activities makes these easy functions to delegate.

Finance ministries need to engage in a wide range of analytical activities on a regular basis. Without simplifying matters too much, the analytical demands broadly fall into four somewhat overlapping categories. First is aggregate fiscal policy analysis, which is needed to decide the framework of revenues and expenditures, most importantly in the context of budget preparation. Second is specific fiscal policy analysis, which relates to the analysis of particular policy proposals and any short-term issues that may arise during the course of the fiscal year. Third is the analysis of departmental spending, both through regular budget negotiations and policy discussions and more tailored reviews of spending requests that reach the ministry of finance. Finally, there is the analysis of any other policy or operational question that the finance ministry might take up, which could involve anything from reforms to the accounting system to the rescue of an SOE.

In many LICs, the analytical capability of fiscal policy matters, especially aggregate fiscal policy, is given very high priority. This is understandable for two reasons. Internally it is reasonable to assume that control over aggregate figures underpins many other choices and enables the ministry to control the distribution of resources throughout the government. Externally, international organisations concerned with fiscal sustainability have long invested resources in and paid attention to technical assistance and other forms of support for fiscal analysis capability. From the point of view of a finance ministry in a weak PFM system, developing fiscal policy analysis capability inside the ministry is a matter of both control and stability in an often volatile fiscal environment. For outside observers, this tendency to centralise can be seen as a source of abuse and long-term instability if the technical objectiveness of the analytical outputs is in doubt.

At the same time, analysis of sectoral policies, very broadly defined, is often weak in LICs. The clearest indicator for the strength of sectoral analysis capabilities is the staff composition of budget departments' sector desks. If the focus of the ministry is on achieving and maintaining delivery capability in sectoral spending, then staff often have accounting, legal or administrative training, whereas an emphasis on analytical capability is reflected through economists, sector specialists or public policy generalists.

In many HICs and MICs, including Chile, Mexico, the UK and Germany, the tendency is to either outsource or share at least some fiscal analysis capability. In part, this is due to the broader international trend of setting up different kinds of fiscal councils, which take on some form of responsibility over the formulation of aggregate fiscal policy (Hagemann, 2013). The establishment of the Office of Budget Responsibility after the 2010 election in the UK is one example. Another related reason is that in countries with very well developed public suppliers of economic analysis there is less of a reason to maintain tight control over aggregate fiscal figures because too egregious departures from the consensus figures would be difficult to sustain. In Germany, macroeconomic forecasting is carried out by independent research institutes, and the consensus forecast is then used by the government.

Sectoral policy analysis capability, on the other hand, appears as a core function of the finance ministry. These capabilities, once acquired, are neither outsourced nor delegated, and investment is maintained even as other functions are shed. The UK Treasury, clearly the most consistently self-reviewing finance ministry in the sample, has undergone several reorganisations since the mid-1990s, and policy analysis, broadly defined, became more and more central to the ministry over time. The organisation of this capability can differ markedly between countries. In the UK, Treasury staff across a broad range of teams work on policy issues, with an increasingly high portion of them trained as economists. In Germany, this capability is concentrated in the budget department, where most staff are generalists with legal backgrounds, although economists are increasingly hired. In Chile, there are the traditional sector desks as well as a monitoring and evaluation team that carries out evaluations and monitors non-financial performance. In contrast, South Africa employs sectoral specialists in its sector teams, which sets it apart from other countries in the sample. Most finance ministries rotate generalists from desk to desk, even if they remain with the budget department for extended parts of their careers. They become specialists in budget policy and analysis rather than in the analysis of a particular sector.

Almost every major function of finance ministries involves coordination. For budget formulation and approval, policy inputs need to be submitted and received, and positions need to be reconciled and condensed, so that key outputs can be delivered and the budget is able to move through the machinery of government. The budget process itself is probably the most consequential and complicated coordinative process in government – at least in those countries where the budget itself is a credible indicator of future public spending and government intent. This sets finance ministries apart from many other parts of government, even central government, where core functions can be delivered in relative separation. For instance, independent central banks have policy interfaces with other parts of the executive, but they can operate monetary policy with a fraction of the coordinative demands of fiscal policy put on the finance ministry.

In many finance ministries, coordination is organised at two different locations: the minister's office for the high-level coordination with the political leadership, and the budget office for the coordination of the budget process. In South Africa, one chief directorate in the budget office deals with budget coordination – although, somewhat unusually, the sector desks are not part of the budget office. The German finance ministry has a division in its budget directorate-general in charge of budget coordination, which seems to be the most common arrangement (having budget sector desks and budget coordination both located in the central budget office).

Coordination failure is endemic in government, as is the quest for more joined-up operations (Bogdanor, 2005; Pollitt, 2003). There are sound theoretical reasons to think that coordination failure cannot be fully overcome, only ameliorated. The common pool resource problem suggests that the interests of spending ministries and the centre of government diverge; it is therefore built into the architecture of central government that coordination does not work seamlessly. The findings of the literature on fiscal institutions apply: coordination is easier when governments are more stable and coherent, when they consist of single parties rather than coalitions. There is a direct link between the ability of spending ministries to appeal to cabinet or other political mechanisms and the ability of finance ministries to coordinate critical processes. Yet even in countries where budgetary authority is centralised – most pronounced in Chile and the UK – budget offices invest considerable resources in coordination.

In many developing countries there is instead a mismatch between, on the one hand, analytical capability – especially of aggregate fiscal policy – and the legal mandate to enforce policy decisions, and on the other hand, a lack in the capability to coordinate the delivery of central finance functions. In the literature, this has often been cast as the distinction between formal and informal practices, where the informal practice does not keep what the formal rules appear to promise (Andrews, 2009; Rakner et al., 2004). The formal/informal divide is certainly an issue of concern, especially in those countries where the informal budget process is used deliberately to facilitate illicit practices. However, in several of the case study countries, most public sector organisations seem to aspire to follow the formal rules of government, but outcomes fall short because of a lack in coordinative capability.

Regulatory capability does not just refer to the policy regulation of particular sectors, such as banking and financial sector regulation. For finance ministries it includes, in the most basic sense, the ability to shape the financial behaviour of other parts of government. Traditionally, this is done by command and control, i.e. hierarchical oversight of financial operations – sometimes of one transaction at a time. Finance ministries in traditional settings do this by delivering a steady flow of financial transaction outputs – approvals, cheques and tenders. When these delivery capabilities are outsourced or delegated, the stance of the finance ministry shifts towards regulation. This shift changes the demands on the ministry considerably, as control levers disappear and staff are asked to define the framework of operations rather than being involved in the details.

In the UK, the Treasury has been very active in delegating day-to-day operations to spending departments and focusing its attention on policy questions and the macrobudgetary framework instead. Most other finance ministries are not comfortable with letting go of detailed control to the same extent, whether rightly or not. In LICs, the finance ministry is more likely to assume that regulation rather than detailed control is unrealistic. In South Africa and Mexico, subnational fiscal relations are often a cause for concern for the central finance ministry, and the ability of governments to reach into subnational entities to obtain intelligence and enforce regulations is quite limited. In Germany, the situation is quite different – there is a presumption that the states can handle their own affairs and are constitutionally empowered to keep the federal government out. In unitary states like Chile and the UK, the dynamics are different: the finance ministry is less encumbered by constitutional limitations, but that does not seem to have slowed down a trend towards more regulation.

The biggest impact on finance ministries of a shift from delivery towards regulation is on the number of staff employed. Both actual regulatory agencies as well as more policy-oriented regulatory units employ fewer but more-senior staff, as the direct processing of transactions gives way to the setting of guidelines and frameworks. The case study countries show a correlation between country size and the staff complement of the finance ministry. But changes over time are difficult to track. The sporadic evidence is that staff numbers at central finance ministries tend to fall over time, which has certainly been the case in the UK (Allen, 2014). The staff numbers added to the analytical, regulatory and coordinative teams do not make up the losses in lower-ranked staff who used to process transactions. At the same time, the concern over a possible identity crisis that might overcome budget offices as they let go of detailed control and shift towards policy and regulation (Schick, 2001) seems to be unfounded.

There is a temptation among public finance analysts to find stages of development – from the stages of budget reform in the 1960s to the platform approach of PFM reform of the 2000s (Brooke, 2003; Schick, 1966). Finance ministry capabilities do not quite lend themselves to such an approach. It is broadly correct that richer countries have more capable ministries, which is not just a function of a better endowment of human and financial resources, but also a reflection of a more complex set of tasks and challenges, most visibly expressed in the size and composition of public spending. But even though the challenges of the day require finance ministries to respond in different ways, the underlying suite of finance ministry functions does not change dramatically. It is very difficult to conclusively disentangle actual changes over time that might reflect a stage-wise evolution from changes in response to changes in the environment or different public sector trends and fashions.

Yet there is a clear difference between LICs on the one hand, and MICs and HICs on the other. Finance ministries in LICs focus their efforts more on transactions and control, while those in MICs and HICs emphasise policy functions, regulation and coordination. This is broadly consistent with a general OECD-wide trend towards New Public Management and delegation, or, in budgetary terms, from microbudgeting to macrobudgeting. The drivers of these changes are complex: they reflect the changing fashions of budgeting as well as evolving challenges as countries develop. But they also reflect an evolution of capability. For whatever manifold reasons, some finance ministries reach a stage where the transactional focus of many delivery functions becomes less and less of a visible concern for the leadership of the ministry, which precipitates a shift towards more and more policy-oriented analytical, coordinative and regulatory functions.

This control–policy transition does not have to be destiny, however. In Western Europe alone, the institutionalisation of policy advice at the centre of government took quite different forms (Fleischer, 2009). It seems quite clear from the case studies that finance ministries pay uneven attention to coordination and policy-oriented analysis, and often pay a price for a lack of coordination and for an inability to engage in policy discussion. Especially in aid-dependent countries, much of the policy analysis function is effectively outsourced to international organisations. There does not seem to be anything inherent in the nature of LICs that would keep finance ministries from changing this and investing more in their policy analysis and coordinative capabilities.

6.2 Implications for policy

There are no simple lessons for how best to strengthen the capabilities of finance ministries. The findings from the broader literature on institutions, fiscal or otherwise, are highly relevant here. The external environment enables and constrains finance ministries in a multitude of different ways. The size and composition of the public sector, as well as the state of economic development, among many other factors, shape the challenges the ministry has to tackle, with important implications for how it engages with the rest of government. Institutional arrangements – such as the political and electoral system, the balance between the legislature and the executive, and the administrative legacy – create the space in which the ministry operates. This space might be extraordinarily broad and allow a large amount of discretion to the minister and the ministry, as is the case in Chile and the UK. But more often the space throws up a multitude of constraints that need to be taken into account before making any changes to the way the finance ministry operates.

Although a truism of international policy discussion, political leadership matters for capability. Most finance ministries see themselves as critical advisers to politicians. The work of the ministry ultimately determines how a large proportion of any government's political agenda gets funded and implemented. Many officials point to their ministers as providers of political cover, which enables them to do their work – be that largely transactional delivery of administrative functions or the provision of policy-driven analysis and coordination. If this political protection fails or turns into a more antagonistic relationship, problems appear quickly and noticeably.

One particularly important factor is the stability in tenure of ministers and senior officials. Many finance ministries, at very different income levels, that experienced sustained capability over time did so under very stable terms in office of both the political leaders and their senior civil servants. In the absence of very stable political leadership a consistent top management group of senior officials can still provide stability for the organisation to perform and evolve. If the senior management also suffers from rapid turnover, capabilities seem to suffer, at least over the long term.

Given a certain degree of institutional space, details still matter. Organisational structures, pay and other civil service details do affect the way finance ministries perform against their tasks. These areas are very poorly researched at the moment. There is little to no comparative information on organisational charts and structures, civil service pay, promotions and incentives, and modes of operation of finance ministries that officials or advisers could turn to. In short, finance ministries, especially in LICs, are poorly served by the lack of research and evidence available to them. Public administration and organisational research have investigated all of these issues in great detail, and it would be well within the reach of the international PFM community to tap into the available research to try and apply it to ministries of finance.

The emerging findings from this report, as well as the nascent literature on finance ministries, could form the basis of a practical approach to strengthening the capabilities of finance ministries. Two immediate changes appear particularly worth exploring. First, a reform agenda, whether it is part of a broader PFM reform plan or specifically tailored towards the finance ministry, should draw upon a broader range of research and evidence. Instead of being narrowly focused on PFM, it should draw upon public management research, as well as the broader evidence base on government institutions. These ingredients would effectively start to fill the 'missing middle' in the current analytical toolkit. Second, the analytical features presented in this report could provide the basis of a capability bottlenecks assessment. A combination of (1) fiscal institutions, (2) central finance functions, (3) organisational structures, and (4) tenure and civil service features could be used to identify the most critical constraints for a ministry to be capable at performing against the tasks it sets itself. A dose of realism remains in order, because the evidence suggests that finance ministries will not be able to escape the institutional environment that sustains and constrains them. They would, however, be in a much better position to make the most of the position they are in.

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