Reimagining Public Finance

Managing public resources for development outcomes

A Framing of the Initiative

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Introduction

Public finance is among governments' most important policy tools for promoting development. Across most countries, governments represent between a quarter and a half of the whole economy, and act both through the direct and indirect delivery of goods and services and the regulation of economic activities across many sectors. The ways in which governments raise and spend public resources have an impact on most aspects of a country's development, from economic growth to income distribution, and from service delivery to crisis response. Harnessing the powers to tax and spend in the pursuit of positive development outcomes is therefore one of the key challenges and responsibilities facing governments the world over, especially as we approach the end date for the United Nations' 2030 Agenda and the Sustainable Development Goals (SDGs).

Over the past few decades, much progress has been made in using public finances for promoting development, but important challenges remain, and new ones have (re)surfaced. In the 21st century, governments in lower and middle- income countries have been successful in reducing poverty and expanding their citizens' access to infrastructure and services. However, governments have struggled to improve the quality of health, education, and other important services. Access remains inequitable. Regulation is often ineffective. Jobs and livelihoods are insecure. Recent reversals are also putting prior gains at risk and countries remain exposed to crises. In more recent years, economic crises, global pandemics, conflicts and increasing threats from climate change have made the job of managing public resources for development outcomes more challenging. Fiscal policy choices are constrained by growing levels of debt and economic uncertainty, and public financial management (PFM) systems are struggling to deliver on governments' fiscal policy objectives, including properly channeling and providing resources for service delivery.

The 'Reimagining Public Finance' initiative aims to open a conversation on what an approach with a stronger focus on the role that the management of public resources can play in

promoting better development outcomes could look like. It defines public finance as the combination of *fiscal policies*—what governments intend to do through the raising and spending of public resources—and *PFM systems*—how governments manage these resources through different processes and mechanisms, including along the various stages of the budget cycle. It argues that both these elements are in need of some rethinking and reconnecting. Over the past few decades, the fields of fiscal policy and PFM have partly grown apart from each other, driven by different approaches, disciplines, and communities of practice, and have drifted in directions that might ultimately undermine their objective of contributing to better development outcomes. Debates around fiscal policy have tended to focus on the need for ensuring fiscal discipline and promoting economic growth, assuming that these would lead to improved development outcomes. At the same time, part of the PFM community has devoted considerable effort to measuring the compliance of country PFM systems with international good practice standards, as well as promoting reforms that might not be well suited to countries' specific problems and contexts, again thinking that this would lead to better fiscal policy performance. While of course these are all relevant and important efforts, they would benefit from being framed within broader objectives. Focusing on development outcomes—i.e. on measures of how well countries are progressing against their own (and global) development goals—consolidates the recognition that fiscal discipline and economic growth are means and not ends in themselves, and that PFM systems should support the achievement of policy objectives rather than simply strive to resemble established models of good practice. Moreover, the two need to be looked at jointly if public finance is to become a more effective tool for achieving development outcomes.

The initiative is driven by two main questions. The first one is: 'what is the role of public finance in achieving better development outcomes?' This means looking at how governments can best use the tools of raising and spending public resources to support public policies that contribute to positive development impact across various sectors. The second question is: 'what are the key public finance bottlenecks that need to be addressed for that to happen?' This means focusing on identifying and removing the obstacles that are preventing governments from being more effective and impactful across both policy and delivery. Focusing on these two questions has the potential to encourage different actors and stakeholders—from governments to donors, and from oversight actors to citizens—to think differently about the role and importance of public finance in achieving development outcomes, and to help reframe the support that the World Bank and other international actors provide to governments in this area.

This framing paper provides an initial snapshot of the initiative. In the sections that follow, it provides the overall background and rational for the initiative, discussing lessons that have been learned over the past 25 years of public finance interventions, and sketches out the broad outlines of a possible approach, detailing some of the next steps that are being taken to more fully develop the initiative.

Background

Across the developing world, efforts to support reforms in fiscal policies and PFM systems are by no means new, and have often been controversial. The international community, including

United Nations agencies, international financial institutions, and bilateral donors have been supporting developing countries in improving their use of public finance tools to promote development outcomes for decades. In the early years of development cooperation, after many countries gained independence (1960s and 1970s), these efforts focused mostly on putting in place adequate planning and budgeting systems and financing public investments that governments could deploy in charting their own development path and narrowing the gap with richer countries.[1] In the years that followed (1980s and early 1990s), a global debt crisis, the end of the Cold War and the rise of the neoliberal order in the Western world shifted the focus to more general policy and fiscal reforms aimed at reducing the role of governments *vis-à-vis* private markets and at ensuring strict fiscal discipline. So-called 'structural adjustment programs' promoted by international financial institutions also faced significant backlash, as many saw them as contributing to what has been referred to as a "lost decade for development" (Singer 1989).

In the mid- to late 1990s attention shifted to the systems and institutions underpinning the formulation and implementation of fiscal policies. This was driven by a growing recognition that countries' development performance depends heavily on the quality and strength of their institutions—drawing on the pioneering work of people like Douglass North.[2] In the realm of public finance, this came with a recognition that fiscal performance is a function not only of economic circumstances, but also of the quality of PFM systems—or the "institutional arrangements for budgeting", as discussed by Jon Blondal in a review article on budget reforms in OECD countries (Blondal 2003). Better PFM systems, in other words, enable governments to more effectively pursue their fiscal policy objectives. Blondal pointed out how certain reforms including the introduction of medium-term budget frameworks, a stronger focus on results, budget transparency and modern financial management practices underpinned governments' capacity to improve their fiscal performance. In developing countries, a similar shift happened due to a number of interlocking factors, including: (a) a parallel increase in the interest and focus on the role of institutions in promoting development, manifested by the adoption of the "good governance" agenda and by the promotion of so-called "second-generation reforms" by many international organisations[3]; (b) the need to ensure that adequate systems were in place to ensure that resources freed by debt cancellation through the Highly Indebted Poor Countries (HIPC) initiative would be effectively used to reduce poverty; and (c) a growing consensus around the fact that foreign aid, in order to be more effective, needed to support and strengthen recipient countries' own policies and systems. This led to initiatives like the Comprehensive Development Framework (Wolfensohn 2000), the Poverty Reduction Strategy Papers (IMF/WB 1999), the Paris Declaration on Aid Effectiveness (OECD 2005), and the growth of General Budget Support (GBS) as an aid modality. As the international community rallied around this new approach, the importance of assessing and improving the quality of the systems through which governments manage public resources gained increasing recognition. This was also related to the

[1] The difficulties inherent in this enterprise were aptly captured in 1980 by Naomi Caiden, a budget scholar and keen budget reform observer, who famously said: "if there was ever a subject which has been over-written, over-analyzed and over-theorized with so little practical result to show for the effort, it is budgeting in poor countries" (Caiden 1980:40).

[2] See North (1990).

[3] See, for example, Grindle (2004) and Camdessus (1999). This shift was also motivated by some of the more disappointing results from the experience with structural adjustment policies and programs.

need to ensure that there were adequate fiduciary safeguards in place for GBS funds flowing directly to recipient countries' treasuries.

The publication of the World Bank's *Public Expenditure Management Handbook* in 1998 can be seen as an important milestone in this process. The broad contours of emerging thinking recognizing the importance of strengthening PFM systems in developing countries were brought together in the World Bank's Public Expenditure Management Handbook, the first—and arguably the most influential—of a series of similar publications by a host of other international institutions that were published at around the same time.[4] Looking at how governments manage public spending, the Handbook set out three levels at which budget institutions influence budgetary outcomes, namely: (a) ensuring aggregate fiscal discipline; (b) allocating resources in accordance with strategic priorities (allocative efficiency); and (c) promoting the efficient and effective use of resources (operational efficiency).[5] As explained in the Handbook: "The total amount of money a government spends should be closely aligned to what is affordable over the medium term and, in turn, with the annual budget; spending should be appropriately allocated to match policy priorities; and the spending should produce intended results at least cost" (World Bank 1998:3). It also identified a series of principles of sound budgeting, including comprehensiveness, predictability, transparency, and accountability. Finally, it emphasized two areas deserving particular attention: the need to strengthen the links between policy, planning and budgeting through the formulation of Medium-Term Expenditure Frameworks (MTEFs), and the need to put in place Integrated Financial Management Information Systems (IFMIS) to support resource management and expenditure controls and reporting. The Handbook also emphasized the political nature of budgeting and the importance of political commitment to reform.

The PFM field has grown significantly since then, and has generated both significant advances and some controversy and skepticism. The years between the late 1990s and the global financial crisis of 2008-2009 saw a huge expansion and consolidation of PFM as a field.[6] Funding for support to PFM systems and reforms grew about tenfold, in tandem with GBS operations (de Renzio et al. 2011). Building on previous efforts linked to the HIPC initiative, a comprehensive framework to assess the quality of PFM systems was developed based on international good practice benchmarks—the Public Expenditure and Financial Accountability (PEFA) framework—which has been used more than 700 times across more than 150 countries. Similar assessment tools have been developed for other areas of PFM, like fiscal transparency, tax administration, public investment management and debt management, for example.[7] The accounting community started work on establishing accounting standards for the public sector, setting up the International Public Sector Accounting Standards (IPSAS) Board in 2004. Finally, the use of Information Technology in the management of public finances has expanded hugely. In recent years, however, the conventional approach to PFM systems diagnostics and reform efforts has

[4] See, for example, Potter and Diamond (1999), ADB (1999), and Allen and Tommasi (2001).
[5] The original formulation of the three levels, however, was in Campos and Pradhan (1996).
[6] The original PEM label was soon replaced by PFM, to signal a broader focus on all of governments' financial flows and transactions, and not just those related to public expenditure.
[7] A recent stocktaking by the PEFA Secretariat counted 64 different PFM assessment tools (PEFA 2023).

come under increasing criticism for becoming too focused on technical details and somewhat insulated from broader public management, concerns about policy objectives, and the political nature of the budget cycle, and for promoting a 'one-size-fits-all' approach that does not take the specific context and the main problems faced by each country adequately into account (Box 1).

Box 1. PEFA and its critics

Over more than 20 years, the PEFA Framework has become the standard tool for PFM evaluations and has been extensively and repeatedly used across the developing world with support from a group of international development partners, both to assess the quality of PFM systems and to inform PFM reform efforts at country level, in partnership with country governments. The Framework consists of a detailed set of multi-dimensional indicators measuring various aspects of the quality of PFM systems in seven broad areas: (1) budget reliability; (2) transparency of public finances; (3) management of assets & liabilities; (4) policy-based fiscal strategy and budgeting; (5) predictability & control in budget execution; (6) accounting & reporting; and (7) external scrutiny and audit. The framework was originally launched in 2005, and subsequently revised in 2011 and in 2016, and scores countries based on their performance vis-à-vis internationally recognized good practice standards.

Despite its clear importance and usefulness, the PEFA framework has come under criticism for two main reasons. The first relates to the framework itself, and the fact that it suffers from three main limitations: (a) it has a centralized bias, as it focuses primarily on processes within central finance agencies and not enough on the organizations who are responsible for overseeing and delivering services; (b) it largely measures *de jure* aspects of budget systems (i.e. their form, or what they look like on paper) and not enough their *de facto* aspects (i.e. their function, or how well they work in practice); and (c) it does not adequately address political economy issues, the domestic institutional set-up and important interactions between different actors.

The second criticism is about how the framework can get used in practice to inform PFM reform processes and priorities. Improving PEFA assessment results often becomes the focus of reform design, without giving adequate attention to the rationale behind specific results or proposed reforms, to the actual objectives that PFM systems are supposed to serve—in terms of both PFM system functionality and contribution to fiscal policy goals—and to the specificities of each country context. This is of course quite different from what the original intention behind the PEFA framework was. In doing so, PFM reforms tend to look quite similar across countries. While some level of similarity can be expected, given the commonalities (and common weaknesses) of country PFM systems, PFM reforms which are primarily based on standardized assessments using international good practice standards and benchmarks may not adequately respond to the context-specific problems that prevent governments from achieving certain policy objectives.

Sources: www.pefa.org; Hadley and Miller (2016); Andrews et al. (2014); NYU/Wagner (2020).

Twenty-five years on, it is a good time to take stock and consider how debates around fiscal policies and PFM systems have evolved, what lessons have been learned, and what the implications are for the way forward. The fiscal policy environment has been very volatile for a good part of the past 25 years, stretching public finances to their limit, and debates around appropriate fiscal policy responses are characterized by significant disagreements. The growth and consolidation of PFM as a field has benefitted many governments that have undertaken efforts to improve their PFM systems, and many lessons have been learned. Yet, the strength of the link between PFM reforms and improved fiscal policy outcomes continues to be questioned. With so much in flux, this is a good time to improve and refine the approach that has evolved in practice over the past quarter century, taking into account the ways in which the context has changed and the lessons that have been learned. The importance of public finance for promoting development outcomes needs to be restated and reemphasized, and made more directly relevant to the challenges that governments face today and are likely to face in the future. Some efforts in this direction have already been undertaken and should be built on.[8]

Looking back: What has changed? What have we learned?

The broader context for public finance has changed considerably over the past 25 years and is currently in turmoil. While the late 1990s and early 2000s were a period of relative stability and growth, with an environment that could be seen as favorable to reforms, more recent years have seen a series of interlocking and compounding crises (i.e. the global financial crisis, the Covid-19 pandemic, conflicts, climate change, etc.) which have created new challenges and made the job of managing public finances more complex and difficult. Governments are currently faced not only with sluggish growth and constrained revenues, but also with increasing demands for spending and services. Recent upsurges in inflation and the subsequent monetary squeeze in advanced countries have also affected lower income countries' ability to finance their deficits at reasonable costs.

The debate around how governments should conduct fiscal policy in response to the many crises they are facing continues unresolved. Three contested issues need to be mentioned here. The first one revolves around the need for and the benefits of fiscal austerity measures in response to fiscal crises. While the necessity for governments to ensure the long-term fiscal sustainability of public finances is widely recognized and accepted, much debate still exists around how deep and fast so called 'fiscal consolidation' should be to bring governments back on a growth path after economic downturns throw public finances off-balance. In a widely cited article, Ostry et al. (2016) argue that the short-term costs of fiscal consolidation have often been underplayed, and that the widening of inequality that austerity often brings can undermine future economic growth. These lessons were certainly in evident display during the Covid-19 pandemic, when governments scrambled to provide assistance to households and firms, borrowing heavily to boost spending. Once the effects of the pandemic wore out, however, calls for fiscal restraint were renewed, especially in response to ballooning debt levels across many developing countries. The second issue relates to the need to address growing levels of inequality across many countries, and the role that governments can play in those efforts through the redistributive potential of both taxation and spending.[9] The third and final issue is linked to the multiple and increasing demands on public finances that governments are likely to face in the medium- to long-term. These include first and foremost the impact of climate change, but also

[8] See, for example, NYU/Wagner (2020).
[9] See, for example, Clements et al. (2015), Inchauste and Lustig (2017) and Granger et al. (2022).

issues related to persistent poverty and aging populations, raising questions about where and how governments can find the resources to adequately respond.

Recent research on institutions and governance has highlighted the need to recognize that different institutional arrangements can lead to desired outcomes. The last 25 years have seen a proliferation of interest and research on the role of institutions and governance arrangements in explaining countries' development trajectories.[10] While it would be too ambitious to attempt to summarize such varied scholarship here, one lesson seems particularly relevant for the purposes of the initiative. It stems from the research of Dani Rodrik and others on the basic tenets of the contemporary economics discipline and the varied strategies that countries that have achieved substantial and enduring economic growth have pursued. In an interesting essay for *Boston Review*, Rodrik and colleagues argue that:

> "*Economics does have its universals, of course, such as market-based incentives, clear property rights, contract enforcement, macroeconomic stability, and prudential regulation. These higher-order principles are generally presumed to be conducive to superior economic performance. But these principles are compatible with an almost infinite variety of institutional arrangements with each arrangement producing a different distributional outcome and a different contribution to overall prosperity.*"
>
> (Rodrik et al. 2019)[11]

Applying this insight to public finance means questioning the assumption that all countries need to put in place uniform institutional arrangements to achieve positive fiscal policy outcomes, or that all governments who face similar fiscal challenges should pursue identical institutional reforms. Rather, institutions can—and should—look different, as what matters is not how they look (their *form*) but how they work (their *function*), which in turn is related to various factors that are specific to the context in which they exist and evolve. Focusing on the functionality of institutional arrangements means choosing as a starting point a problem to be solved, rather than a good practice to be emulated.[12] The ballooning 'good governance' agenda, as described by Merilee Grindle (Grindle 2016), with its increasing—and increasingly demanding—list of good practices that governments are supposed to comply with, has created not only an impossible task for many developing country governments with weak capacities, but also strengthened the often misleading assumption that the simple mimicking of good governance practices copied from elsewhere will inevitably lead to development success.

Existing evidence on the impact of PFM reform interventions reports contradictory results, and is marred by data issues. Over the past three decades, there have been substantial investments and many achievements in PFM across the world, but overall improvements in the quality of PFM systems have been at best incremental. Evidence on how the quality of PFM systems has evolved over the past 25 years is relatively scant for the years before PEFA assessments became

[10] See, for example, Acemoglu and Robinson (2012) and World Bank (2017).
[11] For a more detailed discussion of these ideas related to growth strategies, see Rodrik (2005).
[12] This is related to the Problem-Driven Iterative Adaptation (PDIA) approach promoted by Andrews (2013).

widespread, but is more readily available for more recent years.[13] A comparison of 16 low-income countries from 2001 to 2007 shows half of the countries improving the overall quality of their PFM systems, while the other half either saw no change or a worsening trend (de Renzio 2011). A study covering a much broader set of countries for the period 2001-2014 also shows only a small aggregate improvement, with low-income countries doing better than middle-income countries—albeit starting from a weaker base—and countries in the ECA and SSA regions faring better than those in SAR and EAP, for example (Fritz et al. 2017). A more recent review bringing together average scores for PEFA assessments shows a very modest increase throughout the period 2005 – 2018, but with wide variations across regions and from country to country.[14] A recent IEG evaluation of World Bank support to PFM reforms looked at the impact of US$ 18.3 billion spent by the Bank on PFM interventions in the period FY08-17, and found that "improvements were mostly limited". Some areas, like arrears prevention, production and structuring of budget data, and accounting systems saw clear improvements, but others like budget credibility and IFMIS coverage were characterized by less satisfactory results (World Bank 2021). Similarly, "despite significant investments in IT for PFM, the prevailing paradigm has struggled to deliver successful digital transformation"[15]—many common PFM challenges persist after automation. Faced with total investments by donors of more than US$ 50 billion over the period 2002-2016 (Alphabeta 2018), some could argue that these results are somewhat disappointing. Others may respond that institutional change takes time and that such investments need persistence to show progress and results.

Evidence on the extent to which better PFM systems have led to expected benefits in PFM outcomes is also lacking and inconclusive. Only very few studies exist linking the quality of PFM systems and the budgetary outcomes outlined in the original PEM Handbook—fiscal discipline, resource allocation and operational efficiency, for short. Fritz et al. (2014) investigate the effect of the quality of PFM systems on fiscal balances and aggregate budget execution rates (fiscal discipline), on the sectoral composition of actual expenditure compared to the original approved budget (resource allocation), and on the cost-effectiveness of health and education expenditure (operational efficiency). They find evidence that stronger PFM systems are associated with better budget credibility, at both aggregate and sectoral levels, but not with lower deficits. Furthermore, they find no clear evidence regarding operational efficiency. A more recent study using a more extensive set of control variables reports somewhat similar findings, although the effect on aggregate budget credibility is lost (Mustapha 2019). These results sound a cautionary note on the often-assumed link between the quality of PFM systems (again, as measured by existing tools and approaches) and budgetary outcomes at different levels.

A persisting problem in efforts to strengthen the link between PFM systems and fiscal policies is the definition of the relevant outcomes and their operationalization. Much of the literature on fiscal institutions, which among other things attempts to link characteristics of PFM systems and processes with fiscal policy outcomes, has had an oversized focus on fiscal balances as the

[13] Inevitably, using PEFA data to assess the success of PFM reforms seems contradictory, given some of the limitations of the PEFA Framework identified in Box 1. Yet, the results can still provide us with a partial picture of the broad trajectory of PFM reforms.
[14] See 'Is PFM Performance Improving?', IMF PFM Blog, February 5, 2023.
[15] See Long et al. (2023).

key outcome of interest.[16] This may reflect one of the main preoccupations of policy makers in recent decades—i.e. the need to overcome the natural tendency of public spending to grow over time and surpass available revenues—but it also speaks to the emphasis that many economists and policymakers have put on fiscal discipline as the main objective that governments should pursue at all costs. It should therefore come as no surprise that most of the PFM reform areas covered in an IMF book on “PFM and its emerging architecture” (Cangiano et al. 2013) are about promoting fiscal responsibility. The adoption of fiscal rules, the creation of fiscal councils, the management of fiscal risks and the introduction of medium-term budgetary frameworks are all analyzed based on their contribution to fiscally responsible government behavior. While aggregate fiscal sustainability is clearly a very important public finance objective, it does not mean that the other main goals are not equally important and should not receive appropriate attention. This bias may also stem from the lack of adequate ways to operationalize and measure other budgetary outcomes. In particular, the concepts of allocative and operational efficiency, despite their intuitive clarity, are not easily turned into clear indicators like fiscal balances, and therefore not easy to investigate through empirical analysis.[17] The downside of this is the scarcity of evidence and analysis on the actual role of public finance in promoting specific development outcomes, or even more intermediate policy outcomes, such as those linked to the delivery of public services.[18]

There is debate in the public finance community as to whether there are shortcomings in the established PFM paradigm or problems lie more in the way it has been applied. A recent, comprehensive review of existing approaches to PFM reforms, for example, highlighted the need to move from a conception of PFM as a “closed” system, in which “the PFM processes and conventions that drive operational performance are considered to be unchanging ends in and of themselves”, to one that views PFM instead as an “open” system that “interacts more fluently with all aspects of public policy—namely, government policy choices, government actions (especially service delivery), and development results” (NYU/Wagner 2020:iv). Yet other practitioners dispute these criticisms and claim that any problems are not with the substance of the established approach and toolkit writ large—where substantial progress has been made—but with the need for “refinement of the technical design of the institutions […] where bad ideas prevail” and for strengthening the quality of their application with “better tailoring of institutional design to the circumstances of particular developing countries” (Robinson 2024).

The progress, lessons, challenges and debate highlighted above point to the need to re-examine how governments think about and use public finance as a tool for promoting development outcomes. This process should start from an assessment of conventional approaches to public finance reform that have been developed in recent years, building on

[16] For an overview of this literature, see Wehner and de Renzio (2013).
[17] An interesting exception here is provided by World Bank (2013), where an effort is made to assess the impact of MTEFs on both resource allocation and operational efficiency.
[18] For exceptions looking at the health sector, see Piatti-Fünfkirchen and Schneider (2018) and Welham et al. (2017).

ongoing efforts to move beyond the shortcomings that have been identified in both fiscal policies and PFM systems and involve:

a) Using development outcomes as the starting point and the end goal that public finance reforms should aim to contribute to, rather than just focus, in an isolated manner, on intermediate results.
b) Recognizing the important linkages and complementarities that exist between fiscal policies and PFM systems, and the need for them to work together in order to better contribute to development outcomes.
c) Allowing for institutional flexibility and diversity in the ways in which governments attempt to use public finance as a tool for promoting development, and focus instead on the problems that they face in making their fiscal institutions and PFM systems functional, and the specific bottlenecks that prevent them from being more effective.
d) Identifying and understanding the evidence and data gaps that have undermined previous efforts at operationalizing and measuring important aspects of public finance reforms, and purposefully address them.

These are some of the key starting points for the “Reimagining Public Finance” initiative.

Reimagining Public Finance

The ‘Reimagining Public Finance’ initiative aims to open a conversation on possible approaches for reflecting on the role that public finance can play in promoting better development outcomes. The approach outlined in this section is just a starting point for discussion, as part of an effort to address some of the limitations of conventional approaches to public finance reforms, and to gradually remodel the way in which different actors and stakeholders in the realm of public finance—from governments to donors, and from oversight actors to citizens—think about the management of public resources as a tool for promoting development. The proposed approach is based on the recognition that public finance—fiscal policies and PFM systems—is part of broader public policies and related delivery systems that governments put in place to achieve public sector results, which in turn contribute to development outcomes. It also recognizes that these achievements are shaped by the broader institutional context in which governments operate (see definitions of key terms used in the proposed framework in Box 2, and a visual depiction of it in Figure 1 below).

The initiative also seeks to explore how the support that the World Bank and other international actors provide to governments in this area could be improved, promoting more effective reforms that could result in better development outcomes. International support for country-level reforms in the area of public finance has come under increased scrutiny in recent years, from policy discussions on fiscal responses to the Covid-19 pandemic to concerns around the effectiveness of existing approaches to PFM reforms and their ability to deliver on budgetary outcomes. The initiative aims to build on lessons and knowledge obtained from extensive past experience and suggest ways to improve the quality and effectiveness of support that the World

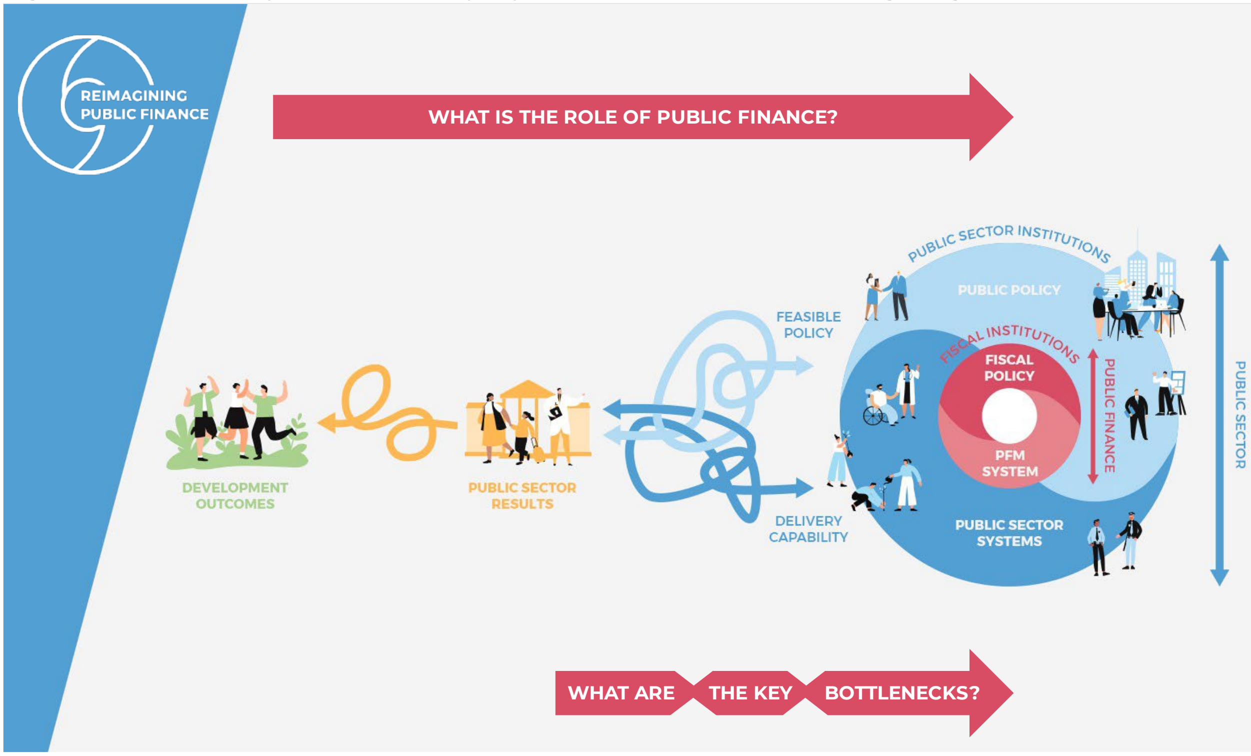
Bank and other actors provide to governments in the broad area of managing public finances. This might include producing guidance for governments, donors and practitioners on how to design, implement and support public finance reforms, plus sector-specific resources, problem-solving tools and training materials aimed at putting this approach into practice and improving the effectiveness of PFM reforms.

Box 2. Definitions of key terms

The Reimagining Public Finance initiative uses the following definitions for the different elements of the proposed framework:

- **Development outcomes** are measures of how well countries are progressing against their own (and global) development goals.
- **Public sector results** are measures of what governments actually do to contribute to development outcomes.
- **Feasible policies** are policies that are politically acceptable, financially affordable and consistent with delivery capabilities.
- **Delivery capabilities** refer to governments' ability to turn policies into public sector results.
- **Public policy** includes both ‘the what’ that governments are trying to achieve (e.g. universal health coverage or primary education) and the broad set of decisions and actions that governments take to try and achieve it, including through both direct and indirect interventions.
- **Public finance** is the part of public sector interventions that deals with the management of public resources, and it consists of fiscal policy and PFM systems.
- **Fiscal policy** relates to the subset of public policy relating to revenue, borrowing and spending.
- **Public Financial Management (PFM)** is the way in which governments mobilize and manage public resources to support the delivery of public policy, through functions including budgeting, procurement, accounting, reporting, and auditing.
- **Public sector systems** are ‘the how’ (e.g. the various processes and mechanisms) that governments use to deliver public policies.
- **Institutions** are humanly devised constraints (informal and formal) that shape individual behavior and structure the interactions between different actors i.e. the rules and the organizations that manage them.
- **Public sector institutions** structure the interactions between the various actors involved in public policy and delivery. They include public sector rules and processes, and the organizations of different types (e.g. ministries, agencies, etc.) that are mandated to oversee and implement them.
- **Fiscal institutions** structure the interactions between the various actors involved in public finance. They include public sector organizations with specific mandates in the management of public resources (e.g. finance ministry, parliament, supreme audit institution as well as sector ministries and frontline providers) and the associated policies, rules and processes.

Figure 1. Preliminary sketch of the proposed framework for Reimagining Public Finance



An approach to managing public resources for development outcomes needs to start by focusing on the long-term policy objectives that governments want to pursue, and that public finances might help achieve (see Figure 1). There are of course many different development outcomes that government policies are designed to help achieve, and the choice of which outcomes and policies governments prioritize at any given moment will inevitably differ from country to country, reflecting domestic priorities, capabilities and context. A useful starting point for discussion could be to focus on the list of development outcomes that have been agreed at global level and that can be assumed to be common across all or most countries (e.g. the Sustainable Development Goals). To take the education sector as an example, education outcomes could be related to achieving universal literacy and learning for different age groups (as illustrated in Table 1).

Table 1: Illustrative Relationships for Education: Part 1 – Public Policy and the Public Sector[19]

What are the desired Outcomes, Public Sector Results, Policies and Systems?		What are the Common Policy and Delivery Challenges?
Development Outcomes and Public Sector Results	**Outcome:** Universal numeracy and literacy	Low numeracy and literacy rates of children
	Public Sector Results: Ensuring universal access to quality basic education.	Inequitable access to quality education, especially low for poorer households.
		Often low quality of education received by students.
		Poor school infrastructure and teaching/learning materials undermine teaching and learning.
		Education is costly to access and this limits attendance.

[19] Tables 1 and 2 are illustrative only. An education study will elaborate and apply the framework for education and provide an evidence-based elaboration of the public policy, systems, interactions, challenges and bottlenecks.

What are the desired Outcomes, Public Sector Results, Policies and Systems?		What are the Common Policy and Delivery Challenges?
Public Policy and Public Sector Systems	**Feasible Policy:** Basic Education policy and delivery modalities can feasibly achieve universal access – they are affordable, involve delivery modalities and curricula for which there is capacity to deliver and are accepted by politicians and citizens.	Policies of free education, combined with unrealistic staffing and school infrastructure norms are not always feasible given prevailing costs.
		Professional development policy is missing or low quality, so teachers are not prepared to effectively teach at the right level and school leaders are directed to focus on the wrong priorities.
		Infrastructure norms are not appropriately prioritized for affordability and infrastructure decision mechanisms are over-centralized.
		Curriculum beyond the capability of teachers to apply.
		Policy focuses on public delivery as the primary delivery mechanism and does not facilitate the role and appropriate regulation of the private sector.
		Policy objectives are insufficiently focused on deprivation to ensure policies are feasible for deprived children.
		Policy ignores the de facto cost of accessing education.
	Delivery Capability: The government has in place the education professionals and operational inputs to deliver the curriculum, school infrastructure and equipment for the learning environment, and systems to manage them which can deliver policy and achieve public sector results.	Inadequate number of teachers are poorly motivated, and do not have skills to effectively teach the curriculum to most learners.
		Insufficient and inappropriate instructional materials, equipment and infrastructure.
		Management and oversight of teachers and schools is weak or focuses on the wrong priorities.
		Information and accountability mechanisms are oriented to the center rather than the service delivery end.
		Too little de facto delivery autonomy. Too little supported devolution to empower school and local managers
		Major disparities in school performance across and within jurisdictions.
		Weak regulation of the private schools sector.

The next step is to identify the public sector results that are the focus of government efforts in achieving specific development outcomes, and understand how the public sector is organized to deliver them. Development outcomes (in green in Figure 1) are affected by a number of factors that are often beyond the reach of government influence (e.g. social and cultural context, economic shocks, natural disasters, etc.). What governments can do is formulate and implement policies that are aimed at generating public sector results (in yellow in Figure 1), which in turn contribute to those development outcomes, although often in complex ways (thus the convoluted arrow). Taking again education as an example, public sector results would relate to the quantity and quality of schooling that governments provide to or regulate for citizens. To achieve these results, the public sectors of different countries (depicted in blue in Figure 1) need both policies that are feasible—both financially and politically—and adequate capabilities to deliver on all key aspects of these policies. In many developing countries, free universal primary education policies may be politically appealing but difficult to afford financially without compromising on the quality of education services. Levels of decentralization, support to private providers, effective teacher training opportunities, and management arrangements for public investment in education infrastructure are but a few of the many public sector systems that play a role in determining how effectively a government will be able to deliver the services that can generate the expected public sector results. In addition, both public policy decisions and the functioning of public sector systems are affected by the broader institutional context, in which people, power and politics help shape and determine the outcomes of government interventions. Public sector institutions play an important role in achieving coherence between public policy and public sector systems, by structuring the interactions among the various actors involved, and through different kinds of organizations with disparate sets of resources (people, money, information and management systems).

Only then can the discussion turn to how public finance can contribute to public sector results. Public finance (in red in Figure 1) is the part of public sector interventions that deals with the management of public resources. Fiscal policy can be considered to be a subset of broader public policy, and PFM systems a subset of overall public sector systems. Fiscal institutions are also a subset of public sector institutions, those that frame and structure the interactions among the various actors involved in public finance decisions. Fiscal policy decisions affect and are affected by public policies through their focus on three broad objectives: (a) overall fiscal sustainability; (b) resource mobilization and allocation; and (c) effectiveness and efficiency in the use of public resources.[20] PFM systems support both the formulation and implementation of fiscal policies through various functions like budgeting, procurement, accounting, reporting and auditing. At the same time, they interact with other public sector systems to deliver public policies. Ultimately, it is the combination of PFM and public sector systems that determine a government's delivery capability to achieve public sector results. Once again looking at the education sector, relevant public finance aspects will include both fiscal policy interventions—e.g. efforts to mobilize additional resources to fund higher education spending, choices around resource allocation among different education levels (primary, secondary, etc.)—and the use of PFM systems to pay teacher salaries on time, allocate resources fairly across and within jurisdictions, purchase school materials and other inputs efficiently, and ensure that money gets to where it is supposed to. These interventions and the results they are able to achieve will inevitably vary from country to country, depending on broader public policy choices around public vs. private provision of education, and levels of decentralization in the education sector, for example.

Table 2: Illustrative Relationships for Education: Part 2 – Public Finance

What is the role of Public Finance?		What are the common Public Finance bottlenecks?
Public Policy and Fiscal Policy	Fiscal Policy contributes to feasible education policy by causing collective prioritization of affordable, costed education policies and associated choices of modalities service delivery within the context of competing priorities.	Education policies are poorly prioritized, and are not disciplined by likely available resources.
		Government/donor preference for free publicly delivered education crowds out alternative delivery models.
		Fiscal space limited or additional fiscal space not allocated to public education due to competing priorities.
		Inefficient composition of funding across subsectors including bias toward tertiary education; and inefficient spending on ministry overheads, salaries, and new infrastructure.

[20] This is a reformulation of the three levels originally included in the PEM Handbook, broadening them to include: (a) concerns beyond fiscal discipline; (b) revenue collection; and (c) performance.

What is the role of Public Finance?		What are the common Public Finance bottlenecks?
	Fiscal Policy delivers adequate and equitable and efficient resources that enables delivery of education policy.	Over-optimistic macro fiscal projections results in inadequate resources to deliver the budget as planned, especially for operational non-wage inputs, maintenance and investments.
		Shifts in expenditure policy priorities over time crowd out education sector expenditures.
Fiscal Policy and the PFM System	Policy commitments on service delivery are realistic and affordable, supported by costing over time in a way that can be easily translated into a budget framework.	Inaccurate, inflated, or outdated costing of policies and delivery norms contribute to their infeasibility.
		Costing takes place in a way that is not easily translated into budget allocations and therefore is not adhered to.
	The budget process delivers decisions on allocations to key delivery inputs, and management and oversight are aligned over time to the costs of achieving delivery commitments.	Gaps in the planning and budget process contribute to a mismatch between objectives, norms, costing, budget allocations, and available funding.
		Inertia and a lack of technical or political interest to align budget allocations to costs especially operational aspects of delivery funding.
		Ad hoc and often political decisions outside the budget process on the location and distribution of resources and investments contribute to disparities and undermine the objective allocation of funds across and within jurisdictions.
		Budget virements during the budget execution stage undermines the planning process and the expected resources for implementation of projects and operational activities in educational centers.
The PFM System and Public Sector Systems	Education systems provide information that informs the equitable allocation of resources to schools and facilities.	A lack of information means teachers and operational inputs are not deployed in line with norms and needs; equipment and infrastructure are not adequately maintained and investments cannot be targeted to locales where infrastructure gaps are highest.
	Teacher human resource and payroll systems inform equitable teacher deployment, promotion and transfer, and enable timely payment of teachers.	Poor information on the deployment of teachers constrains the equitable distribution of teachers.
		Fragmented payroll systems not linked to HR systems contribute to delays in payment of teachers.
	The PFM system delivers reliable and adequate resources to spending agencies for frontline infrastructure and service delivery and the systems of management and oversight of delivery.	Fragmented, parallel, absent, and uncoordinated funding sources for delivery inputs and facilities which are misaligned with priorities.
		Funding for school infrastructure and inputs and frontline providers is unpredictable in timing and in quantity and may be delayed or diverted. Service and infrastructure providers do not have the authority to retain revenues and/or spend them.
		Poor procurement skills and oversight constrains development of quality education infrastructure and services.
		Management and oversight of schools and associated systems such as information for school managers and effective training, are not adequately and reliably resourced.

Adopting an approach based on the framework depicted in Figure 1 would potentially imply a significant advancement in regard to conventional PFM reform approaches. First, the proposed approach reverses the logic behind many existing PFM interventions. Rather than starting from an isolated focus on the quality of PFM systems, it considers first the development outcomes that governments are pursuing and that public finance can help achieve. It then identifies the public policy results that can contribute to them, how these are supported by the combination of public policies and delivery capabilities, and finally asks how public finance—fiscal policies and PFM systems—can contribute to bringing about the desired results and outcomes, taking the institutional context in which they work into account. While the ultimate purpose of this approach is still to help governments improve the functionality of their PFM systems, its focus is quite distinct. It considers PFM systems as working alongside other public sector systems and within a broader institutional environment. As a consequence, their contribution to policies and results is often complex and indirect. Again, the two key questions that this approach focuses on—represented by the two red arrows running from left to right— are:

a) What is the specific role that public finance (fiscal policy and PFM systems) plays in shaping public sector results and achieving development outcomes, and how can this role be played most effectively?
b) What are the specific problems that need to be solved to ensure that happens? What are the specific bottlenecks at different stages of the results chain that need to be addressed in order to ensure that fiscal policies and PFM systems can best contribute to positive outcomes?

Asking these questions strengthens the focus on the results and outcomes that public finance is supposed to help achieve, focusing and linking the reforms to relevant problems that matter for governments, therefore increasing their awareness and engagement, rather than on PFM systems themselves (i.e. avoiding PFM reforms *per se*). This means focusing on the key bottlenecks that need to be addressed to improve public sector results, and as a consequence development outcomes, rather than on more abstract notions of what PFM systems should look like.

Two important challenges in elaborating this approach and making it operational relate to defining clear linkages between the various elements of the framework, and to identifying specific public finance bottlenecks. Given the complexity of the proposed framework, it might be impossible to apply it wholesale to a broad set of development outcomes across many countries. Rather, it is probably better used to analyze the contribution of fiscal policies and PFM systems to specific development outcomes in individual country contexts, so as to inform debates around public policy and public finance reform agendas that will be relevant to each specific context. Depending on the outcome of interest and the country context, it might also be necessary to address gaps in available data, information and indicators to get a complete enough picture of the various elements of the framework. Nonetheless, the analysis should eventually lead to the identification of at least some of the specific public finance bottlenecks that need to be addressed in order to enhance the results that governments can achieve in a particular sector, and which reform efforts can target. Box 3 provides an illustration of a pilot study that was carried out to identify financial bottlenecks hindering service delivery in the education sector in Myanmar.[21]

Box 3. FinEd in Myanmar

The FinEd study in Myanmar was undertaken to help the Ministry of Education improve its capacity to ensure that massive increases in education funding did result in improved sectoral outcomes. It started from a recognition that important PFM challenges specific to the education sector have not been systematically identified and assessed, as the national PFM reform agenda did not address specific sector needs. The study was aimed at identifying key systemic weaknesses or 'bottlenecks' within the Ministry of Education's financial management system that impede service delivery in the education sector.

The study identified a series of bottlenecks hampering service delivery, from inadequacy of existing formulas for ensuring equitable school financing to fixed unit costs for construction projects, and from limited fiscal decentralization to weak financial management skills across the sector. It then classified these bottlenecks based on whether the education ministry could address them directly or required other actors to take action, and on whether the bottlenecks were sector-specific or affected all sectors. This facilitated the identification of possible ways to address and remove (or loosen) the bottlenecks, and promoted a better understanding of where the responsibilities for delivering on the necessary reforms lied.

Source: OPM (2019).

While this framing paper has described the proposed approach and what it tries to do, it is also important to state some things that the proposed approach is not and does not do:

a) It is not about reinventing the technical discipline of PFM and the associated norms, tools and practices that have developed over time. It does not question the role of government budgets in allocating funds or the importance of accounting or audit. Rather, the initiative aims to strengthen the role of PFM systems in supporting the formulation and execution of fiscal policies and in contributing to public sector results, and identify where they fail to play this role and why.
b) It is not about promoting performance budgeting as a PFM technical solution. While the focus of the initiative is indeed on achieving results at different levels of government action, the initiative is focused on identifying, addressing and removing obstacles and bottlenecks preventing governments from achieving those outcomes, rather than promote a specific form of "doing PFM".
c) It is not about dictating which policies governments should adopt to achieve development outcomes. Rather, the initiative is based on the understanding that PFM systems and fiscal and public policies are inextricably linked and should be looked at together. This implies the need for linking up with other players who look at fiscal and sectoral policies, for example, and helping them recognize the importance of considering the role that fiscal institutions play in achieving positive outcomes.

[21] While this exercise was not done using the framework proposed here, it provides some interesting and relevant insights that can be built on.

Planned work program

Over the coming months, the World Bank's Global Governance Practice is convening a collaborative process to discuss and revise this proposed framework and approach. This process will engage a number of stakeholders in helping to revisit and redefine the role that public finance can play in achieving development outcomes, better understand the linkages that exist the various elements of the framework, and reflect on how to improve public finance reforms.

The global work agenda for Reimagining Public Finance will focus on two overlapping phases and five complementary elements:

Phase 1: Reviewing and Reimagining Public Finance (September 2023 – March 2025)

1. **A Global Conversation**. Critical to building consensus on any need to reimagine public finance will be to facilitate conversations on different aspects of the future of public finance and a proposal for a more outcome-based framework across practitioners and thinkers within the Bank, with clients, and with external partners engaged in PFM reform. A series of structured conversations will be convened, including face-to-face convenings, regional events, online webinars, blogs, etc. with various sets of stakeholders. The process will culminate in a global conference on the future of public finance with leading academics and practitioners in early 2025. An external website will be prepared to host and document this conversation.

2. **Supporting Research**. A series of background research has already been commissioned, including five sectoral/thematic papers (Health, Education, Economic Resilience, Gender and Climate Change) that are elaborating the outcome-based framework set out in this document and testing its validity using country-level evidence, and a paper tracing the history of public finance reforms over the past 25 years. Additional sectoral and thematic papers (e.g. on digital PFM) may be commissioned as well. Depending on feasibility, a dashboard will be prepared and integrated into the online platform and an approach to PFM story telling developed to trace the evolution of PFM qualitatively and quantitatively.

3. **Global Report**. A global report on Reimagining Public Finance which traces out the evolution of public finance and related reforms over time in different contexts, identifies successes and areas for improvement, and makes the case for any needed changes to the approach to public finance reforms (where appropriate)—focusing on the achievement of functional change and contributing to development outcomes—will be published 25 years on from the foundational PEM Handbook.

Phase 2: Setting out and implementing a Renewed Approach (Late 2024 to end 2025)

4. **Resources: An online platform, existing and new resources.** Building on the outcome of phase 1 (and the external website), an online global public platform will be developed to set out the approach to making public finance work for development outcomes and provide complementary tools for practitioners, for example including problem solving guides and

training courses. If deemed appropriate, from the first phase, a handbook or equivalent will be prepared setting out how to implement the mentioned approach to public finance reform processes. If not, then the platform would act as a repository for relevant existing tools.

5. **Country-level engagements**. As the approach is developed, the Bank will support its pilot application in specific technical areas in countries where opportunities present themselves. This will complement or be part of engagements under the Future of Government and GovEnable initiatives which will also apply the framework in World Bank governance and sector engagements.

The work will be led by the Public Finance Governance Global Unit (EGVPF) and the PFM and PIM Global Solutions Group in the World Bank. A reference group of leading public finance practitioners and thinkers will be formed from inside and outside the World Bank. A core team of staff and consultants is managing the exercise.

For further details or submitting comments, please contact:

Tim Williamson (twilliamson@worldbank.org), Paolo de Renzio (pderenzio@worldbank.org), Richard Sutherland (rsutherland@pefa.org), Abdulaziz Almuzaini (aalmuzaini@worldbank.org), and Jordi Baños-Rovira (jrovira2@worldbank.org) and reimaginingPFM@worldbank.org.

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