

not given proper incentives to the recipients to assume fundamental responsibility for funding. Although institution building is the catchword of the day, the fact remains that many aid programmes take the shape of short-term projects in specific fields with concrete goals specified.

If sustainability is seen in the larger context of institution building, we should be talking about the viability of entire systems rather than attempting to rescue the capacities built in individual projects after aid support has been withdrawn. This does not exclude that also entire systems or programs demand proper recurrent cost financing, which has to be budgeted for.

When a donor decides how to deal with the sustainability of an individual project, the contribution of the project should be weighted against the national development strategy in general and the ongoing institution building process defined in terms of entire systems. This means that the time perspective in aid engagements has to be extended and that institutions might be deemed reasonably sustainable even if there is a need for a continued aid flow.

If aid can be placed in a clearly defined developmental context there is little reason to uphold the principle that aid has to be terminated or minimised in the near future. Under such circumstances the validity of the entire notion of aid dependence might be questioned.

Some policy implications

- All costs – capital as well as recurrent – should be taken into account when planning aid financed activities. The principle of cost sharing in each individual project case should be abandoned.
- The value of a project should be measured against the contribution it makes towards the development of larger systems.
- All aid involvement should be based on an overall development strategy defined by

the recipient country. This strategy should have clearly specified target areas, against which the recipient governments can be made accountable and to which donors are committed.

- The other side of this is that aid should in principle not be given to countries where governments are not held accountable to their citizens and where the rule of law is not adhered to.
- Development co-operation is a long term activity and cannot be carried out with short term incentives or instruments.

The Expert Group on Development Issues, EGDI, was established by the Swedish Government in 1995 with the objective of contributing to an increased understanding of development issues in a global context and increasing the effectiveness of development cooperation policies.

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EGDI

Studies in brief

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Capacity building, institutional crises and the issue of recurrent costs

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Why are governments unable to finance recurrent costs of projects when development assistance is withdrawn? Under what circumstances is it justifiable to continue development assistance when the recipient is unable to finance its recurrent budget? These are some of the questions discussed in the study, which synthesises reports from an EGDI project, investigating the links between the micro and macro levels of aid financed capacity building.

How did the recurrent cost problems emerge?

In the early periods of development co-operation it was assumed that the host country should finance its own recurrent budget, whereas the donor undertook to finance investments and technical assistance. This principle was based on the development thinking at the time, identifying a budget or balance of payments gap as the main obstacle to more rapid economic growth and development. With rapidly increasing number of aid projects many governments in countries receiving development assistance found it difficult to finance recurrent costs, once the investments were made. With the oil price increase

and subsequent debt crisis in the early 1980s the situation deteriorated in many countries. The micro aspect of the problem concerns the sustainability of individual aid projects, whereas the macro aspect comes out as a deficit in government budgets and national accounts.

Declining real wages and high inflation characterised the period. Inability to pay and retain skilled personnel and maintain basic infrastructure and equipment, resulted in deteriorating quality of the services supplied from the projects.

When shall donors continue to finance total costs?

The recipient partner in development co-operation is normally a government organisation. Aid dependence becomes manifest at the point when the local partner in the project is unable to take over and finance all responsibilities. For individual donors this poses a specific problem: How should they behave to make sure that the capacity built can be maintained, while at the same time not allowing for aid dependence to be perpetuated? For the recipient governments the problem is similar,

namely how to construct feasible strategies when their own national resources are insufficient to uphold recurrent operations in all donor supported capacity building projects.

The main question addressed in the study is: *Under what circumstances may it be justifiable to continue giving support to a project that is financially unsustainable in the sense that the recipient is unable to finance its recurrent budget?*

Two options are open to the donor partners. Either to accept full cost responsibility, knowing that at least in the short run aid dependence will tend to increase, or to withdraw completely, even if the services rendered by the project might seem to exist.

This problem can be analysed in two ways. One is the strict donor perspective that is concerned principally with the sustainability of each specific project. The other is to take a broader view and to analyse the sustainability of a project in light of its place in the larger system. In the first approach the donors make decisions from case to case on how to handle the recurrent cost issue; in the second approach the costs of a project have to be measured against its overall welfare contributions.

The former perspective is the traditional one, it is seen as a donor dilemma and it forces the donors to adopt ad hoc solutions in order to rescue already made investments. The latter perspective focuses on the role of the recipient governments in formulating a strategy that can form a basis for sustainable capacity building and includes a commitment with respect to long-term funding. A systems approach to capacity building requires not only longer time horizons and an integrated approach to aid projects but also a different system for sharing responsibilities and commitments.

The study argues that sustainability of aid cannot be analysed solely as a problem of survival of individual projects and thus mainly as a technical issue. In order to overcome the micro-macro dichotomy every decision made by a donor with regard to cessation or continuation of individual projects should be placed in the context of the overall development strategy and institutional reform process in the recipient country. The notions of capacity building and institution building are of particular importance in such assessments.

The financial gap in government budgets can be overcome either by increasing the development assistance or by an up-

surge in government revenue. Before deciding how to handle recurrent costs, the donor would have to assess whether the project has a potential to be revenue generating and eventually self-financing. The project has to be assessed in the perspective of institution building in general, meaning that every project should be measured against its place in the larger system.

High social value of the services may justify total financing

One fundamental aspect that should guide the choice is the value of the services produced in the project. If a project provides services that are of high social value or of great importance in some other respect, the donor might consider providing total financing. This would guarantee that the capacity built into the project is not foregone. Sustainability is maintained, but aid dependence increases.

This leads to the question how "a highly valuable service" should be defined. Is it the very end product as such, or the more indirect contribution of the service to social welfare? In reality, a financially unsustainable project may continue as a result of pressure from those in the field or within the organisation itself. A successful donor-led project actually may even extract capacities from other activities that may be equally valuable from a societal point of view. The local skills accumulated remain within the donor sphere, and if one donor drops out, others are queuing to recruit the skilled personnel available.

One problem is that the recipients are offered an escape route from making choices of their own. Given the incentive structure, with a myriad of projects available, the recipients can choose to regard all projects as more or less equally valuable. Thereby the responsibility for solving the recurrent cost crisis is transferred to the donors. Many donors find this extremely unsatisfactory, since they find themselves trapped in having to take full funding responsibility for what is regarded as their "own" projects. The donors are also prevented from adopting an integrated systems approach to aid, since the recipients have few incentives to make the necessary priorities. Thus, a fundamental change in attitudes is necessary so that the recipient governments are made responsible for the priorities made and the targets set in the aid programmes.

If basic capacities in education and health care can only be upheld by means of aid, it makes little sense to put pressure on recipi-

ent governments to take over recurrent costs. The point is that capacities should not only be maintained but also developed, and in order to achieve this the government needs to raise larger funds than before.

NGOs are not always the solution

Insufficient administrative capacities on the part of the recipient government are often assumed to be a key reason for unsustainability. However, the financial sustainability on micro level is not necessarily improved if the recipient partner is a NGO. If the development of social services depends heavily on aid projects run by NGOs, who will then take responsibility for the totality of these systems? Why should governments be enticed to do so if they are by-passed? With this strategy, time perspectives might even be shortened. What mechanism is there to ensure that long-term perspectives on development policy are maintained when the actors involved can be seen as individual entrepreneurs?

The problem of low salaries

That low salaries are a major incentive problem is unquestionable. If higher salaries should play a role in capacity building it is important that these salaries are offered in ways that ensure that the staff is retained within the sector. The development of a new privileged class, i.e. to a large extent those working for the donor agencies, should be avoided. This is already part of the problem of deficit civil service capacity in Africa today. Donor driven projects already hire many qualified people and in a sense these make up a new privileged class.

This process is also draining the system of local professional capacities. If that is to be changed the donors must adopt an entirely new attitude towards institution building. It appears that professionals are increasingly working outside the public sector, whereas administrative capacities have not been enhanced to any noticeable extent. The attitude that downsizing or dismantling of the state as such will solve the efficiency problem is little more than wishful thinking.

The importance of legal authority

The problem of insufficient institutional capacity is not only one of lacking administrative capacities, but more so one of lacking legal authority for the regulatory framework including the civil service. Thus, if institution building is to be a major field for deve-

lopment assistance it cannot be treated only as an administrative issue. The first principle in institution building is to make sure that the rule of law applies. It provides a fundamental principle for guaranteeing unbiased exchange and legal authority. A key element in institution building is the eradication of patrimonialism, as it has been in all other successful cases of modernisation.

The argument that modern development presupposes efficient institutions rests upon the assumption that there is a difference between personal and impersonal rule, so that human interaction is protected by law and the state is a neutral enforcer of the legal system. So, the fundamental difference referred to is the one between personal rule and the rule of law.

Institutions refer to entire systems of social arrangement such as the system of government and public administration from central to local levels, the educational system, the police force, the military, the judicial system, and the system regulating the economy. Within such institutions various forms of organisations are operating.

Changing administrative capacities will not automatically bring about development. Today, many individual projects are called institution-building efforts, while in reality they remain isolated interventions in small geographical areas, or are concerned with specific technical tasks within the public sector sphere and sometimes in co-operation with private companies. If, instead, institution building is analysed as interventions in the larger context of entire systems, the concept of institutions can be concretised from case to case. It has to be made clear what is the anticipated role of a specific intervention in its larger institutional setting. In doing so, the sustainability of an aid involvement has to be analysed as a long-term undertaking and the costs involved should be regarded as a totality. Such an approach must be based on a broadly based agreement between donor and recipient countries, so that a consistent strategy for institutional system development can be followed.

Don't split financing between investment and recurrent costs

A major conclusion is that the recurrent cost constitutes a major problem that has tended to increase aid dependence over time. The splitting of costs between investments and recurrent costs is a technical and narrow practice that in combination with the project approach has perpetuated aid dependence. It has