

Taking Action for the World's Poor and Hungry People

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SPEAKER SUMMARY NOTE

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Title: Fiscal Policy Instruments and the Political Economy of Designing Programs to Reach the Poorest

It is important to identify the poorest groups in society, particularly those that might not benefit from formal programs of social protection or employment generation. These groups are often disadvantaged individuals who are unable to participate in the labor market or from extended family support. Information on these groups and individuals is often available to communities, though not necessarily to higher levels of government.

In some countries, central government programs are designed to provide support to the poorest—this includes the *Oportunidades/Progressa* in Mexico. However, such programs function on the basis of wide targeting, and are demanding in terms of administrative capabilities. The replication of the Mexican program in other Latin American countries has been disappointing—not just because of cost and administrative limitations.

The alternative is for local governments to carry out the targeted interventions themselves. This was the case with the (largely rural) *wu bao* (five guarantees) program in China. With tight targeting, the support generally worked well. However, this depends on the resources available to the localities—and there has been much greater variance in these resources over time. A similar pattern has been observed with the urban *di bao* program.

Ensuring adequate resources for local governments is important so that they can finance the key programs for the poorest and the hungry. This can be achieved partly by own-source taxes that also engender greater accountability and responsibility on local governments. This is a major constraint, as relatively little attention is given to the development of local own-source revenues (where the local administration is able to raise rates in case of additional need) in many developing countries. And, since own-source revenues can vary considerably, any system of own-source revenues has to be supplemented by transfers.

Another major constraint is that central programs tend to over-ride the preferences or interests of local officials and politicians who may have other priorities. An alternative is to provide targeted financing to local governments so that they are able to carry out the requisite programs. The difficulty is that the local governments may have incentives to divert the resources to issues that rank higher in the preferences of the local officials—particularly investments—as the central government implicitly assumes a degree of responsibility for the target groups.

The solution to the problem lies in introducing competition for the resources among the local governments and over time, and introduction of cross-conditionality in program design. Thus, some of the investments financed by the center might also be made conditional on the local government providing support to the poorest. This is because a threat to withhold financing for a program for the poorest may not be credible—but one for an investment program valued by the local government may be effective.

An effective program that involves local implementation with central financing will require a number of measures to be included in the budgeting processes and procedures:

- The definition of target groups and programs should be as precise as possible, including the specification of results that are monitorable.
- The budget should be set in an intertemporal framework, and comparable information on sources and uses of funds should be available to senior and comparable governments in a transparent and timely manner.
- There should be a feedback mechanism that affects future budget allocations depending on the use of funds in the current and past periods.
- In more advanced countries, moves towards actionable contracts and performance budgeting should be considered.
- In the longer term, the respective responsibilities of levels of government could be clarified, together with adequate own-source revenues and objective "equalization" transfers. This would be an efficient mechanism to build on local preferences and information.