

The EU's State Building Contracts

Courageous assistance to fragile states, but how effective in the end?

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Key messages

State Building Contracts appear to be a smart and flexible response to past criticisms of EC budget support in fragile, transition and conflict-affected environments, but the effectiveness of this form of budget support, which was formalised in 2012, remains to be seen.

Officials within EU institutions and EU member states have different expectations about the strategic and developmental role that State Building Contracts should play in partner countries. Stakeholders will need to avoid overloading the modality with too many objectives and demands.

Capacity requirements for implementing budget support require greater attention in fragile contexts. More flanking measures for capacity development to effectively accompany the implementation of State Building Contracts are needed as well as extra expertise at the level of the EU delegations.

State Building Contracts conceptually support the New Deal's peacebuilding and statebuilding goals, but to accomplish them, EC officials and partners implementing the State Building Contracts will have to keep the New Deal's ambitions in close sight.

About this note¹

This Briefing Note takes a closer look at the purpose and key features of State Building Contracts (SBCs) and presents initial experiences and views of stakeholders working with this budget support modality. Little has been written about this particular form of budget support. The analysis aims to contribute to the growing body of knowledge on effective peacebuilding and statebuilding and illuminate what the EU as a strong supporter of the New Deal (Box 2) can do to further improve its practices towards these objectives. It addresses those who would like to know more about this budget support modality as well as officials from EU institutions and EU member states who deal with policy and the operational steps involved in assisting fragile and post-conflict countries in moving towards resilience and development.

For the executive reader, we have summarised in section 6 the principal points emerging from this Briefing Note.

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In May 2012, the Council of the European Union (EU) adopted a new policy statement entitled *The Future Approach to EU Budget Support to Third Countries*. These “Conclusions”, as they are called in EU parlance, followed a similarly titled Communication issued by the European Commission (EC) in October 2011 (EC 2011b; UN 2012). In that Communication the EC proposed that budget support contracts be differentiated to tailor responses to the context of the partner country concerned. Three types of general budget support contracts were distinguished: Good Governance and Development Contracts (GGDCs), Sector Reform Contracts (SRCs) and State Building Contracts (SBCs). These last were to address situations of fragility and support transition processes. This move towards differentiation in budget support was in large part a response to a critical report by the European Court of Auditors in 2010 regarding the EC’s management of budget support (ECA 2013). At about the same time, EU member states were expressing concerns about the EC’s budget support strategy as well (Capacity4Dev 2013 and Faust et al, 2012). Formulation of the Communication was timely, as it coincided with international discussions on aid effectiveness that stressed the need for more differentiation in support to partner countries and greater attention to fragile and conflict-affected situations. Against this backdrop, the EU foreign ministers in their Council Conclusions also noted that the SBCs should bring into practice the “New Deal” for engaging with fragile states. This New Deal was endorsed by the EU and member states at the Fourth High-Level Forum on Aid Effectiveness in Busan, South Korea (Busan 2011, paragraph 26).

Underlying this Note is an analysis of EU policy papers and guidelines and studies on budget support in fragile and conflict-affected settings. The Note furthermore draws extensively on interviews with officials from EU institutions and member states, subject-matter specialists and partner-government representatives.² A range of questions is raised: What is the rationale of the SBCs? What are the fundamental differences between SBCs and other modalities of budget support? Does this modality produce more effective and strategic decision-making within EU institutions for addressing fragility and conflict-affected environments? What are the expectations of stakeholders in EU institutions and in EU member states?³ To what extent do SBCs promote the New Deal?

The Briefing Note is structured in six sections. Section 1 is informative and highlights a number of generic issues related to the provision of budget support in fragile and conflict-affected environments. Section 2 provides technical information about the purpose and design of the SBCs. Section 3 presents initial experiences in working with SBCs. Section 4 summarises several political and operational questions that have emerged during interviews and should be taken into account in future work with SBCs. Section 5 reflects on the added value of SBCs for promoting the peacebuilding and statebuilding goals of the New Deal. Section 6 concludes this Briefing Note by summarising its principal points.

Box 1: Abbreviations

BSSC – Budget Support Steering Committee
DEVCO – Directorate General for Development and Aid of the European Commission
EC – European Commission
EEAS – European External Action Service
EU – European Union
GGDCs – Good Governance and Development Contracts
SBCs – State Building Contracts

Box 2: The g7+ and peacebuilding and statebuilding goals of the New Deal

The g7+ (www.g7plus.org) is a self-selected group of 19 fragile states that first came together in 2010 to seek parameters for a new approach to international engagement with fragile and conflict-affected countries. The discussions were held under the umbrella of the International Dialogue for Peacebuilding and Statebuilding (IDPS), which was established in Accra in 2008 as an international forum for political dialogue among countries affected by conflict and fragility, their international partners and civil

² A total of 23 were interviewed: 6 from the EU Directorate General for Development and Cooperation (DEVCO), 2 from EU delegations, 5 from the European External Action Service (EEAS), 1 from the EU Directorate General for Financial and Economic Affairs (ECFIN), 4 from EU member states, 2 partner-government representatives and 3 subject-matter specialists. SBC programme documents were unfortunately not available to the authors.

³ We also recorded expectations of some partner-country officials, though their expectations for SBCs are the same as for other forms of general budget support that they have received in the past. SBCs are broadly seen as a concept internal to the EU.

society. In Monrovia in 2011, the group agreed on a set of five peacebuilding and statebuilding goals. Further discussions later that year culminated in the "New Deal" for engagement with fragile states (New Deal 2011). Endorsed by countries at the Fourth High-Level Forum on Aid Effectiveness in Busan, the New Deal has three main components.

1. Five peacebuilding and statebuilding goals: (i) **legitimate politics** to foster inclusive political settlements and conflict resolution, (ii) **security** to establish and strengthen people's sense of safety, (iii) **justice** to address injustices and increase in people's access to justice, (iv) **economic foundations** to generate employment and improve livelihoods and (v) **revenue and services** to manage revenue and build capacity for accountable and fair service delivery.
2. FOCUS elements, intended to clarify the process that a country and its development partners will undertake: a **Fragility** assessment; agreement on **One** vision, one plan; formulation of a **Compact**; monitoring **U**sing peacebuilding and statebuilding goals; and **S**upport for political dialogue and leadership.
3. Principles of mutual **TRUST**, with **T**rust being based on **R**isk-sharing, **U**se and strengthening of country systems, **S**trengthened capacities, and **T**imely and predictable aid.

Implementation of the New Deal began on a trial basis in 2012. Five countries volunteered for the pilot: South Sudan, Timor-Leste, Liberia, Sierra Leone and the Democratic Republic of Congo (DRC). These countries have now all conducted a fragility assessment consultation and are at different stages of finalising the reports and preparing a compact. Somalia recently launched its New Deal Compact with the EU as the leading international partner.

1. Budget support in fragile and conflict-affected situations

This section was written for readers who are not fully familiar with budget support and the particularities of working with this aid modality in situations of fragility. It reviews some key issues that are taken up throughout the rest of the paper.

A. Setting the scene

The EU has committed itself to work more effectively in fragile environments. Budget support is a tool that few donors are willing to use in such countries, though this form of aid can contribute to stabilising an already fragile environment. Bilateral donors have found it difficult to continue to provide budget support in developing countries, let alone in fragile environments. Increasingly, they find it hard to implement budget support and to justify its relevance to critical constituencies when applied in countries marked by corruption, human rights violations or political volatility and fragility.

The EU was and is an exception in that it provided and continues to provide budget support – at the country level, in particular sectors, and in countries experiencing fragility or are conflict-affected. It does this often in close collaboration with the International Monetary Fund (IMF). Yet the EU also experiences pressures. There was pressure from a number of EU member states to substantially reduce the scope for using budget support. There were questions from the EU Court of Auditors. And there have always been questions among EC and EU aid practitioners about how to best use budget support to generate real added value as part of a wider "package" that includes policy dialogue and capacity development measures. These pressures have affected the design of the three budget support contracts of the EC, and also influence their implementation in the field.

On the basis of evaluations, studies and ongoing experience, the EU has argued that budget support as an aid package remains relevant and has a lot of potential, also in fragile environments, certainly when it is part of a clever overall engagement strategy. Part of that package and the overall approach is that donors work together to lessen the burden on partners and to gradually strengthen country systems, including accountability relations and partner ownership. This has proven to be very difficult in "normal" developing countries and even more so in fragile contexts. Experience has shown how difficult it is for donors to combine aid tools, to work together, to divide labour, to play second fiddle, to share notes, to refine knowledge about successes and failures and to adapt approaches and timing accordingly (Andrews et al. 2012).

EU budget support can only be effective to the extent that the EU is enabled or empowered to combine all of its aid tools, to facilitate partnerships and to use all its policy instruments coherently (including trade, security, diplomacy, etc.). Such basics of good donor practice are even more important in fragile environments because usually, there is little domestic institutional or state capacity to make up for donor errors, or to make corrections.

B. Learning from recent work on budget support

Recent studies and literature on budget support in fragile and conflict-affected situations offer key findings and messages that enable us to better understand the intricacies involved in this approach to aid. Some of the points raised apply to the provision of budget support in general. Others address the specificities and problems posed by fragile contexts.

How to distinguish fragile situations? No firm definitions exist of “country fragility” or “state fragility” (GSDRC 2013). Nonetheless, empirical patterns of fragility are found and these can help to inform policy and operational responses to contexts described as “fragile”, “in stable” or “in transition” (Gravingholt et al. 2012). The EC’s 2007 Communication “Towards an EU Response to Situations of Fragility”, refers to fragility as “weak or failing structures and ... situations where the social contract is broken due to the State’s incapacity or unwillingness to deal with its basic functions, meet its obligations and responsibilities regarding service delivery, management of resources, rule of law, equitable access to power, security and safety of the populace and protection and promotion of citizens’ rights and freedoms” (EC 2007a).

How to understand general budget support? As an aid modality, budget support allows for the use of country systems, therefore strengthening country institutions. Today’s understanding defines general budget support as a package of inputs combining the transfer of financial resources to central financial institutions to fill a financial gap with policy dialogue, a conditionality framework and accompanying capacity development measures, as well as a commitment on the part of donors to provide more aligned and better harmonised support. Moreover, general budget support is premised on the state having the lead role in multiple ways, and on the fact that the government and donors are willing and able to engage in a partnership form of relationship (Dom & Gordon 2011).

Rationale for using budget support in fragile countries. According to a Common Approach Paper formulated by the World Bank and African Development Bank, with active participation by the EC,⁴ the basic rationale of budget support in fragile countries is to intervene quickly in order to address basic needs and maintain state functions. Emphasis is placed on ‘seizing a “window of opportunity” for starting reforms and reviving the delivery of essential public services (and safety nets) by governments; avoiding deterioration of the economic and political environment that underpins stabilization; and supporting social stability’ (AfDB & WB 2011).

Can budget support work everywhere? A differentiation is proposed, for instance, between states with weak or strong capacity to manage budget support. In addition, states can be differentiated between those with weak or strong legitimacy of the government, which also has implications for the likelihood of budget support delivering the intended results. Where both legitimacy and capacity are weak, the provision of budget support will be difficult but should not be excluded up front. The decision should be based on a careful assessment of opportunities and risks. Where governments are unwilling to reform, budget support should not be provided at all (De Catheu de 2013).

⁴ The EC did not sign the Common Approach Paper since it was still finalising its Green Paper on budget support at that time.

Risks and benefits. Table 1 presents some of the supposed benefits and potential risks involved in using budget support. These are gathered from the literature and from donors' arguments for engaging in budget support operations – or refraining from doing so.

Table 1: Perceived benefits and risks of using budget support

<i>Perceived benefits</i>	<i>Perceived risks</i>
<p><i>For all partner countries</i></p> <ul style="list-style-type: none"> • Uses and strengthens country systems • Strengthens country ownership • Contributes to domestic accountability • Reduces transaction costs and offers incentives for donors to harmonise their support • Increases predictability of funding <p><i>Specific to fragile contexts</i></p> <ul style="list-style-type: none"> • Provides financing for pressing needs, filling a resources gap 	<p><i>For all partner countries</i></p> <ul style="list-style-type: none"> • Elite capture, fraud and misuse of funding • Concentrates power in the government • Conditionality often lead to lack of aid predictability • Conditionality may challenge the sovereignty of the partner country <p><i>Specific to fragile contexts</i></p> <ul style="list-style-type: none"> • Lack of government policies to guide partners • Weak legitimacy of government and leadership • Lack of long-term predictability and link with medium-term objectives • Limited capacity within partner country systems as well as partner country civil society • Limited or lacking domestic accountability, civil society organisations often absent or very fragile

In practice, budget support has a mixed track record both in fragile and in non-fragile environments. The 2012 budget support evaluation of the Dutch Ministry of Foreign Affairs (Ministry of Foreign Affairs of the Netherlands 2012) and an earlier OECD evaluation (OECD 2011) note that budget support has had limited impact on poverty reduction and that donor expectations have often been unrealistic. The Dutch evaluation notes that where political and governance reforms were the objective, budget support has been marginally able to promote policy change. But it has been more successful in public financial management reforms. A review of external assistance to Mozambique (a formerly fragile and post-conflict country) credits budget support with strengthening policy implementation and reducing aid dependency, even leading to a rise in domestic tax revenue.⁵ The risk of overloading the agenda of budget support has also been noted, as well as the need to clarify the objectives being pursued, particularly with regard to fragile states (Dom & Gordon 2011). Budget support operations have been found to be more effective in sectors where objectives are spelled out and supported by government policies.

Political conditionality and policy dialogue. The OECD's Development Co-operation Directorate (DCD) recommends that 'political conditionality should not be specifically linked to budget support or any individual aid instrument, but should rather be handled in the context of the overarching policy dialogue between a partner country and its donors' (OECD 2006). Yet despite this recommendation, most donors have continued to consider budget support to be a lever for technocratic reform and democratic governance reform (Molenaers 2012). At the same time, donors offer little proactive strategic thinking about how budget support could actually strengthen or support democratic reform (*idem*). Furthermore the amount of aid provided through budget support is fairly limited (Dom & Gordon 2011). Therefore, donors should be careful to avoid too high expectations of achieving leverage through this instrument.

The Common Approach Paper of the World Bank and African Development Bank notes that decisions and policy dialogue on budget support in fragile situations are insufficiently informed by analysis. The paper recommends that political economy analysis be undertaken to understand the root causes of conflicts, the drivers of elite behaviour, politics of exclusion, regional and global influences and citizen expectations (AfDB & WB 2011). This approach could help donors (possibly in collaboration with other development partners and dialogue with partner countries) to tailor the provisions of budget support to specific cases of fragility.

⁵ For instance, in the case of Mozambique budget support reportedly had positive effects in terms of improving the country's tax income and thus reducing aid dependency (Gerster 2013).

How to pursue domestic accountability? In fragile environments, budget support can take the form of an emergency “one-off” stabilisation initiative or a policy-oriented programme to support the development of a country over time. A commitment to development, understood as a commitment to good political governance (or “good enough” governance), is one of several qualifying conditions used for budget support. Yet the establishment of more transparent systems is enormously challenging in fragile environments, given the generally weak capacities of civil society organisations, parliaments, courts of audit/local auditors and the media and the absence, or incompleteness, of published public budgets and accounts. Moreover, donors’ own lack of transparency makes an already complex relationship with the recipient country even more difficult (Dom & Gordon 2011).

Capacity challenges for donors and recipients. On the part of the partner government, fragile countries face a series of capacity problems, often translated into limited absorptive capacity at the institutional level as well as within civil society (OECD 2009). Donors experience capacity issues as well. For instance, limited knowledge about the country or sector and frequent staff rotations that limit donors’ ability to engage in downstream service delivery (ODI 2011). The European Court of Auditors report notes that the EC had not made full use of budget support’s potential because it lacked expertise in priority areas and was weak in managing dialogue with partner countries (ECA 2010).

2. Policy and guidelines

A. Innovations applicable to all budget support operations

The adoption by the EU Council of the EC’s Communication on the use of budget support marked a leap forward in implementing the development policy set out in the EU’s “Agenda for Change”.⁶ That policy, accompanied by the budget support guidelines issued by the EC in September 2012 (EC 2012a), builds on experiences in provision of budget support in different contexts. It also responds to criticisms raised regarding the previous focus on technocratic governance reforms in recipient countries. The policy furthermore redresses the former neglect of the prevailing political situation in the recipient country. While the 2012 guidelines do not represent a radical departure from the previous ones, published in 2007 (EC 2007b), six innovations do warrant mention (Box 3).

Box 3: Innovations of the 2012 budget support guidelines

Process innovations

Fundamental values assessment. EU delegations (EU embassies in partner countries) are requested to assess adherence and commitment to human rights, democracy and the rule of law at the programming stage and throughout the provision of budget support. A positive assessment is a precondition only for the Good Governance and Development Contracts (GGDCs), though other budget support operations are encouraged to pay attention to the findings on fundamental values and try to promote them. For an SBC, the assessment should be forward-looking and take into account whether there are clear signs of commitment, for example, the signing of a peace accord, a political settlement and any confidence-building measures undertaken.

Risk assessment and management framework. The risk assessment and management framework consists of five dimensions and draws on previously used tools that have now been formalised. A key innovation is the inclusion of (i) political risks, in addition to (ii) macroeconomic, (iii) developmental, (iv) public finance management and (v) corruption/fraud risks (see also Box 6). The aim of the framework is to provide an overview of the risks of inaction and the opportunities of intervention.

Four eligibility criteria. A new eligibility criterion, “transparency and oversight of the budget”, has been added to the three criteria set in the previous guidelines, those three being “a national policy/strategy”, “a stability-oriented macroeconomic framework”, and “a public finance management programme”. For SBCs, the specificities of countries in situations of fragility or transition are taken into account. For instance, a country might not have a reform strategy supporting the objectives of the SBC, but it might have an agreed transition compact that could serve as the basis of the eligibility assessment.

Assessment of the eligibility criteria. The 2007 guidelines required a national policy or strategy, a stability-oriented macroeconomic framework and a public finance management programme to be in place or under implementation at the time of approval of budget

⁶ “Operationally, the EU and Member States should make use of aid modalities that facilitate joint action such as budget support (under a ‘single EU contract’), EU trust funds and delegated cooperation” (European Commission 2011a: 11).

support operations and upon each disbursement. The 2012 guidelines require, in addition, that EU delegations check whether those strategies, policies and programmes remain credible and relevant.

Institutional innovations

Budget Support Steering Committee (BSSC). The BSSC meets approximately twice a month and is composed of senior management of the EU Directorate General for Development and Cooperation (DEVCO) and relevant representatives of the European External Action Service (EEAS) and EU Directorate General for Economic and Financial Affairs (ECFIN)⁷, chaired by the Director-General of DEVCO. The BSSC was created to ensure coherence in the provision of budget support across countries and regions and to provide a broader base from which to take decisions. Past operations were criticised for the high degree of discretion granted to geographic directors in complex country contexts. The BSSC provides strategic oversight, offering a forum for discussing key decisions such as whether to engage in budget support and disbursing tranches, in particular for operations in riskier environments. Decisions to suspend budget support are also addressed by the BSSC, with discussions based on the updated risk assessment framework matrix.

Regional budget support teams or hubs. The guidelines envisage creation of teams or hubs to advise and support EU delegations, the EU Head of Delegation (EU ambassador) and EU Headquarters, in the design and formulation of programmes and in conduct of the dialogue with the partner countries. The teams are to fill gaps in capacity and expertise, in particular, at the EU delegation level. As of October 2013, these posts had not yet been filled.

Budget support to fragile and conflict-affected countries is not new to the EC. However, awareness of the need to work differently in these countries became fully institutionalised with the formulation of the revised guidelines in 2012.⁸

B. Key features of SBCs

The three budget support modalities all have the same overall objective, that is, to assist the government of a partner country in eradicating poverty, promoting sustainable and inclusive growth, and consolidating and improving democratic and economic governance. This is followed by specific objectives for each modality. See Table 2 for Good Governance and Development Contracts (GGDCs) and SBCs.

Table 2: Specific objectives of GGDCs and SBCs compared

	<i>GGDC</i>	<i>SBC</i>
Specific objectives	<ul style="list-style-type: none"> - Improve the financial capability of the government to achieve its policy objectives. - Strengthen core government systems and support broad reforms including macroeconomic management, public finance management, public-sector reform and domestic resource mobilisation. - Address constraints on sustained and inclusive growth. - Foster domestic accountability and strengthen national control mechanisms to improve governance. - Improve crosscutting service delivery aspects. 	<ul style="list-style-type: none"> - Improve the financial capability of the government to restore peace and macroeconomic stability and to achieve short-term policy objectives. - Foster a transition process towards development and democratic governance. - Support government efforts to ensure vital state functions (especially maintenance of peace and security, payment of civil service salaries, provision of core administrative functions and minimum basic services to population).

Source: Adapted from European Commission 2012a.

Comparing them reveals one distinct way that Sector Reform Contracts (SRCs) differ from GGDCs and SBCs. SRCs give access to policy dialogue at a sector level or for a set of interlinked sectors. The dialogue, thus, focuses on supporting sector policies and reforms, improving related governance and enhancing service delivery. GGDCs and SBCs allow for higher-level political and policy dialogue with the partner country. Box 4 summarises the distribution of budget support funding across the three contract modalities.

⁷ The BSSC includes the responsible DEVCO geographic directors, representatives of the EEAS (geographic/horizontal, for programming and fundamental values and political aspects), relevant thematic/horizontal DEVCO directors, representatives of geographic and thematic services concerned, one representative from ECFIN (Globalisation, Trade, Development Unit).

⁸ The current guidance on "State Building Contracts for Fragile Situations" (EC 2012a: Annex 9) builds on an internal note from 2009 that became a methodological annex to the previous 2007 guidance document.

Box 4: Distribution of budget support funding

The EC runs some 240 budget support operations in third countries, amounting to some 20% of EC aid. Roughly 80% of the operations are Sector Reform Contracts (SRCs) (or old sector budget support operations), 5% are Good Governance and Development Contracts (GGDCs), 6% are State Building Contracts (SBCs), with the remaining 9% being old budget support operations (the so-called Millennium Development Goal Contracts).⁹ The small amount of EC budget support going to fragile countries should come as no surprise. A 2011 analysis of trends in aid and budget support flows from donors to a selected group of fragile countries¹⁰ notes that general budget support and balance-of-payment operations make up just 4.8% of total official development assistance (ODA), therefore being of limited volume relative to the total aid received.¹¹

According to the guidelines, the decision to move ahead with an SBC is based on an assessment of the opportunity of intervention through budget support, which should include five elements usually conducted by the EU delegation for the country concerned (Box 5). If this assessment is positive, then the eligibility criteria (see Box 3) will be assessed as part of the preparation of the main project documents, that is, the action fiche and supplementary documents.

Box 5: Elements used to assess the opportunity of intervention with an SBC

The decision on whether to move ahead with an SBC is taken based on the following five assessments:

1. Whether the partner country can be considered fragile, in a fragile situation or in transition
2. Risks and benefits, including the risks of not providing budget support (see Box 3)
3. A clear purpose of the SBC linked to statebuilding objectives
4. An indication of the government strategy for SBC support (this could take the form of a compact formulated as part of New Deal implementation)
5. An indication of wider international support for the provision of budget support, particularly from the World Bank (WB) and International Monetary Fund (IMF)

Source: Adapted from EC 2012a.

Technically, the GGDC and SBC are quite similar, including in the areas of implementation and disbursement. On the basis of the EC guidelines, four main characteristics set SBCs apart from GGDCs.

The first, as noted above, is the different **specific objectives** of the two modalities (Table 2). SBCs focus on restoration of peace and macroeconomic stability, ensuring vital state functions and supporting a transition to democratic governance. The underlying rationale is that budget support can prevent deterioration of the social and economic situation and enable basic service provision, thus countering social tension and perpetuation of instability.

A second characteristic that distinguishes SBCs from GGDCs is that SBCs carry no fundamental values **precondition for budget support** (EC 2012a: 28-29 & tables 58-59). In contrast, a positive assessment of the fundamental values situation in the country is a precondition for the GGDC. A fundamental values assessment does need to be carried out to provide information about the opportunity of intervention, but it has no mandatory weight in decisions on whether to grant an SBC.^{12 13}

⁹ The 2013 EuropeAid report notes that around 22% of EC aid is given in the form of budget support, food aid or other modalities (EC 2013).

¹⁰ The short list includes Afghanistan, Burundi, the Central African Republic, Chad, Congo, Côte d'Ivoire, DRC, Eritrea, Guinea, Guinea Bissau, Haiti, Liberia, Nepal, Niger, Sierra Leone, Somalia, Sudan, Timor-Leste, Yemen, and Zimbabwe.

¹¹ Dom & Gordon 2011. It is important to note that this study's calculations were done on the basis of the OECD's ODA database, which has several weaknesses. In particular, as stated by the authors, the data do not distinguish between balance of payments and general budget support.

¹² "The risk of inaction should be balanced with the development and basic needs implications of not engaging in fragile states." P. 28. EC 2012a.

¹³ This precondition regards the decision to start the process of granting budget support. During the identification and formulation phase, four eligibility criteria are nonetheless assessed for SBCs as well as other modalities (see Box 3). See also Chapter 6. EC 2012a.

Third, while a GGDC can be granted to any country fulfilling the precondition for fundamental values, an **SBC may be granted to any country in a fragile or transition situation.** Decisions on whether to utilise an SBC are taken on a case-by-case basis.¹⁴

Box 6

lists countries that currently have or are supposed to soon receive an SBC.

Fourth, **SBCs last one to two years** with the possibility of an extension, typically of one additional year.¹⁶ An SBC can be renewed in due circumstances and when the transition to an SRC or GGDC is not yet feasible.

The usual length of a GGDC is between three and six years. The shorter term of the SBCs is due to the specific rationale of the instrument. It is understood to be a flexible intervention measure to provide tailored assistance for a limited time and which can be adapted once the situation changes.

3. Early experiences

Full implementation of the EC's new guidelines on budget support started relatively recently, in January 2013. Earlier, in 2012, a number of ongoing budget support operations in fragile situations were transformed into SBCs. Other new SBCs began in 2012 and 2013 or are in preparation, including those for Côte d'Ivoire, Mali, Burundi, Togo, Mauritania, Tunisia and South Sudan. It is too early to review the full effects of the SBCs and the extent to which they have helped countries achieve specific objectives like macroeconomic stability, fostering transition processes towards development and ensuring vital state functions. Nevertheless, some initial experiences and observations can be recorded to indicate the extent to which certain flaws noted in past experiences with budget support have or have not resurfaced.

A. There seems to be no widely shared vision on the purpose of the SBCs and what they can realistically achieve

By adopting the EC guidelines and recommendations on budget support, the European Council, representing the EU member states, recognised the SBC as an aid modality suitable for addressing fragility and post-conflict environments and for helping countries make a transition towards development and democratic governance. Despite this recognition, there seems to be no widely shared vision on the purpose of the SBCs and what they can realistically achieve.

Box 6: Countries with a current or planned SBC, by region, and the amount of funding and period provided¹⁵

West Africa

- Côte d'Ivoire: €115.4 million agreed in 2012 for the period 2012-2015
- Liberia: no details available
- Mali: €220 million agreed in 2013, for the period 2013-2014
- Mauritania: €40 million agreed in 2012, for the period 2013-2015
- Sierra Leone: €29.6 million, for the period 2013-2014
- Togo: €22.5 million agreed in 2012, for the period 2013-2015

East Africa

- Burundi: €42 million, for the period 2013-2015
- South Sudan: €80 million planned, for the period 2013-2014

North Africa

- Tunisia: SBC under preparation, for the period 2013-2014*

Caribbean

- Haiti: €112 million agreed in 2013, for the period 2013-2015

Sources: * Van der Linde & Willemsen 2013; various DEVCO sources and interview transcripts

¹⁴ The EU delegation concerned assesses whether a country should be considered fragile or in transition according to criteria in use among international organisations and characteristics listed in the 2007 EC Communication on fragility (EC 2007a) and in the EU Council Conclusions on fragility of that same year (Foreign Affairs Council 2007). The presence of the country on lists of fragile or conflict-affected countries can be referenced in the assessment. But a country that does not appear on any of these lists may still receive an SBC if sufficient evidence of fragility or transition is presented. See Annex 9. EC 2012a.

¹⁵ Several others are under discussion but not yet approved.

¹⁶ The length of the SBC refers to the years in which disbursements are planned. This is different from the operational duration of the contract, which is the implementation time of the contract (i.e. including monitoring and evaluation), which is usually more lengthy, for instance amounting to 48 months for an SBC provided in 2013-2014.

EEAS officials point to the value of the SBC as an immediate intervention measure to respond to emergencies and, in their mind, to help stabilise politically fragile situations.¹⁷ According to one official, an SBC should help to operationalise political decisions in contexts requiring quick, visible and credible EU action. Developmental goals should come second and follow the political goals where needed. This position neglects lessons from the past that budget support operations should not be made conditional to political reform processes, as brought out by an OECD review of budget support programmes.¹⁸

EC representatives indicate appreciating the ability to operate “more freely” in a transition context, with fundamental values and political risk assessments not disregarded but carrying less weight because a positive assessment on human rights, democracy and the rule of law is not a precondition for funding. Moreover, they value the ability to fill fiscal gaps to guarantee basic functions of the state.

EEAS, DEVCO and EU member-state representatives share the perception that the SBC allows for quicker intervention, even though the procedural requirements are the same as for the other modalities of budget support.¹⁹ The case of Mali is likely to have influenced this perception, because roughly six months passed from the decision to engage in budget support (February 2013) to the first disbursement (June 2013).

A number of EU member-state representatives are generally supportive of the Commission's approach. This is related to the somewhat “schizophrenic” situation that some member states find themselves in. While both member states and the Commission are required to meticulously account for international cooperation expenditures, domestic constituencies hold their national governments more directly accountable for the political implications of providing budget support. Hence member states tend to be more risk-averse in their bilateral assistance, refraining from engaging in budget support in riskier countries. But these same member states are nonetheless convinced of the need for pragmatic approaches to stabilisation in certain fragile and conflict-affected environments. They therefore agree on the EC's use of budget support for such countries.

Other member states view SBCs only as a mechanism for extreme situations of political and social instability, like the current situation in Mali, to be used for comparatively short periods. For these cases, they would like to see a more risk-sensitive approach, with political conditions attached to some phases of SBC formulation and implementation, for instance, to the disbursement of budget support tranches. According to these member states, countries like Côte d'Ivoire and Tunisia should not receive SBC support, because of their lag of compliance with fundamental values. A country like South Sudan would also be excluded, according to these member states representatives, due to the nearly complete absence of functioning state structures that can meaningfully process budget support.

B. Within the EU institutions, the new policy on budget support and institutional innovations are seen as a positive development

The creation of the Budget Support Steering Committee (BSSC) (see Box 3), which meets approximately twice a month, is viewed as a particularly positive institutional innovation. The role of the BSSC is to help establish a shared institutional view and decision-making process on provision of budget support. It functions as a platform for systematic discussion of the often intricate issues involved in providing budget support in fragile and transition environments, including questions about fundamental values and the appropriateness of budget support. The establishment of the BSSC was a response to past criticisms of

¹⁷ Looking at the countries listed in Box 6, they noted that 50% of the countries receiving an SBC do not fall in this category.

¹⁸ This was mentioned during an interview with a DEVCO official. See also OECD (2011: page 4), ‘Budget support programmes have proved once more unable to “buy” reform.’

¹⁹ According to the Annex 9 of the guidelines, the identification phase could be conducted together with the formulation phase. Some stakeholders have remarked, however, that in practice this does not happen, therefore the procedures are the same.

the inappropriately high degree of discretion granted to DEVCO geographic directors in making complex and ultimately political decisions. Its creation also recognises that member states have very different views on budget support, which requires careful consideration of decisions. Moreover, budget support is a potentially very political and strategic instrument that merits shared decisions by senior staff across institutions. Following normal procedures, the BSSC discusses each SBC at least three times,²⁰ based on the information collected by the EU delegation and the risk assessment and management framework.

Within its short lifetime, the BSSC has grown into a key decision-making body determining the strategic direction of cooperation with a range of countries. Detailed technical questions are set aside in favour of discussions about the most appropriate form of budget support, alternative aid modalities, the costs of inaction and mitigating measures to reduce risks that could be taken when working with a partner country. Questions were raised during interviews about whether the potential strategic importance of the BSSC is sufficiently felt throughout the different ranks of the EEAS and whether the matters discussed by the BSSC are seen as primarily technical or political. Interviewees from the EEAS suggest that more attention could be given to this organ within their institution.

C. More attention to political risks is valued but development and implementation of operational tools to assess these risks are lagging behind

The decision on whether to move ahead with formulation of an SBC (or other form of budget support) is based on a number of components (see Box 5). One of them is the risk management framework (Table 3). Officials from DEVCO and the EEAS are positive about the institutionalisation of this framework, which goes beyond technocratic governance reforms to include sensitive questions about political risks and risks of inaction. Questions were raised about whether EU Headquarters and EU delegations have sufficient information, human resources and tools to appropriately assess the political economy and conflict situation of a country. Opinions were split among interviewees across and within the different institutions (EEAS, DEVCO and the EU delegations). Some feel that enough information is already available from within DEVCO and the EEAS, as well as from other development partners operating in-country and from public sources. Others, also spread across the different institutions, agree with the Common Approach paper (AfDB & WB 2011) and see benefits of more in-depth insights about the political situation of a country, the actors driving or hindering reform, the interests and incentives of key decision makers to engage in change as well as the institutional capacities.

Several EC officials remarked that the EC provides little guidance on how to conduct political economy analyses and how to incorporate them into decision processes. However, the EEAS and EC did recently launch an in-depth and systematic conflict assessment tool for fragile and conflict-affected settings and recommends using it to assess risks and opportunities (EEAS & EC 2013a; EEAS & EC 2013b). Some officials and experts from civil society commented that risk assessments,

Table 3: Risk management framework

<i>Risk category</i>	<i>Dimensions</i>
Political	- Human rights - Democracy - Rule of law - Insecurity and conflict
Macroeconomic	- Macroeconomic policy and financial sector - Debt sustainability - Vulnerability and exogenous shocks
Developmental	- Public policy - Government effectiveness
Public finance management	- Comprehensiveness of the budget - Controls in budget execution - Procurement - External audits
Corruption/Fraud	- Corruption and fraud

Source: Adapted from Annex 7 of EC 2012a.

²⁰ The higher risk of failure in fragile and transition environments requires involvement of the BSSC at least three times in the process: when an opportunity to engage through a budget support operation is identified, in the review and approval of the action fiche and in taking the decision to disburse payments.

especially for SBCs, should become more conflict sensitive and include more systematic use of the EU's own in-house expertise on fragility and conflict.

D. Early SBCs have produced intense dynamics and interactions among the EU institutions and member states, though these dynamics have not always been positive

The political crisis in Mali in early 2013 created a strong sense of urgency that resulted in a decision-making process to deal with the crisis that EU and member state officials describe as positive (though noting that this assessment relates only to the moment when the decisions were made, as we do not know how the crisis will further unfold). Interviewees from all of the institutions consulted in this study emphasised that the EU was able to act quickly and jointly and, with the SBC, it had an adequate instrument with which to take a visible lead and exercise political leverage. Whether this dynamic can be repeated in less politically urgent cases remains to be seen. In Côte d'Ivoire, the EU has considerable clout for engaging the partner government in political dialogue due to the substantial funding it provides for macroeconomic stabilisation, for security and justice sector reform and for financing social services. Furthermore, its division of labour with the IMF (which focuses on macroeconomic support) and the World Bank (which focuses on private-sector development) allows the EU to act as one of the major players in the country. Member states are closely following the EU's work in this case, with some considering provision of bilateral budget support in the future. The case of South Sudan has been less smooth so far. Most member states consider the provision of budget support there as premature, given the country's unstable political situation, its tense relationship with Sudan and the fragility of its government administration. The SBC is still under preparation due to unresolved issues related to implementation. Observers commented that the approach taken by the EU delegation was "pushy" in coordinating the SBC with other development partners. Lessons should be learnt from this case for other contexts where an SBC is proposed.

E. Staffing of EU delegations strongly impacts the implementation of budget support in fragile and conflict-affected countries

Implementing an SBC requires specialist knowledge on budget support, a savvy understanding of the political and economic context where the intervention is to take place, strong monitoring, and the ability to engage effectively in political dialogue and policy dialogue. EU delegations, in particular in fragile and post-conflict states, face a shortage of human resources. The creation of regional budgets for support teams could fill some of the capacity gaps, particularly in the technical domain. But it is doubtful whether an expert working from a distance could follow the political and institutional developments of a country closely enough to fully understand the more sensitive issues that need to be considered during policy dialogue, and even more so during political dialogue. Ability to effectively implement SBCs, and even plans to engage more through SBCs, are thus currently severely hampered by these capacity gaps. A further bottleneck reported by some EU delegations is the lack of a communication and cooperation flow between the political sections staffed by EEAS officials and the operations sections staffed by EC officials. This has led, in some cases, to a disjointed conduct of political and policy dialogue with partner countries, negatively impacting implementation of SBCs.

4. Questions and concerns

The interviews brought out several questions and concerns about current and future budget support provision to fragile and conflict-affected countries. They relate to emerging trends as well as to perceptions among different stakeholders. These warrant careful monitoring in relation to the EU's overall development policy and its commitment to implement the peacebuilding and statebuilding goals of the New Deal.

A. Are SBCs also provided to countries lacking a firm political will to reform?

As noted previously, SBCs can be granted to fragile and transition countries, as assessed by a set of loosely-defined criteria. This approach appears pragmatic and flexible, but nonetheless makes it difficult for

outsiders to understand for which country situations an SBC can be used. Some interviewees from EU member states and the EEAS expressed the view that SBCs should be used only for countries coming out of an acute crisis and in need of immediate stabilisation. The argument for an SBC was said to be less clear for cyclically fragile countries and countries that have been structurally fragile for years, many of them showing political unwillingness to reform. On the list of countries that currently receive SBC support (Box 6) several are perceived as having lacked the political will to reform for many years. The EC guidelines recommend that an SBC be considered when fragility is not due to 'unwillingness', thus raising the question of whether the guidelines are being followed to the letter (EC 2012a: Annex 9).

B. Is there a risk of SBCs being used too widely?

The potentially wide breadth of use of SBCs is led by the indication in the guidelines that an SBC is appropriate for both fragile and transition countries.²¹ The latter term was added to the budget support guidelines at a time when the Arab Spring was unfolding in Tunisia, yet the guidelines provide no further definition or clarification about what type of countries fall into this category.²²

A safeguard against the inflationary use of SBCs is the BSSC, as it is designed to provide strategic oversight and ensure consistent and coherent budget support provision. The BSSC thoroughly screens proposals made by geographical desks and EU delegations. When such support to a partner country is being considered, its discussions focus on the specific aim of the SBC. This role of the BSSC is borne out by the presently low percentage of SBCs (6%), compared to SRCs (80%) as a proportion of total budget support. Given the recent introduction of the SBC, however, this is an early figure, as requests for this modality were said to be arriving in higher numbers than originally anticipated. Moreover, some member-state interviewees foresaw the EC providing budget support in situations where their own government is more constrained due to more critical and risk-adverse national constituencies. Finally, the Commissioner publicly stated the intention to increase the use of budget support, which again raises the spectre of wider use of SBCs.²³

Some member-state officials expressed concern that the EC might use SBCs too widely, including in highly instable situations where concerns about fundamental values may be downplayed in favour of political considerations. No positive assessment on fundamental values is required for the decision to go ahead with an SBC. The modality could therefore be used for country contexts that do not allow for a GGDC and for which provision of one or several SRCs would be considered inadequate or too cumbersome to manage.

It is too early to tell at this stage what the answer to this question will be. Some observers point out that the weak government capacity in many fragile contexts does not allow the use of an SBC. Moreover, EU member states will remain critical about the use of budget support, which could even result in a more modest use of this aid modality. All interviewees agreed that the further use of SBCs should be monitored and embedded in a process of regular exchange and learning.

C. Can SBCs be used for long-term engagement?

Experience with budget support in fragile and low-capacity African contexts shows that it can take years for basic structures to be built and the first tangible results to become evident. Prominent examples are Sierra Leone and Liberia. Trust and patience are needed to set up meaningful policy dialogue and to accompany

²¹ "The State Building Contracts is not limited to fragile States however and situations of fragility may arise, inter alia, in partner countries during political transition to democracy and establishment of the rule of Law" EC 2012a: Annex 9, p. 141).

²² The only reference is provided by the European Neighbourhood Policy, which refers to "democratic transition countries", meaning that partner countries like Morocco, Albania and Ukraine could all potentially be considered for an SBC.

²³ At a public ODI event in 2011 Commissioner Piebalgs indicated his ambition to increase budget support, not to reduce it, from the present target of 25% to perhaps 50% (Maxwell 2011).

the partner government's own reforms in a well-informed manner. The need for long-term engagement in such contexts is also stressed by the 2011 World Development Report (WB 2011).

The guidelines for SBCs indicate a duration of two years with the possibility of extending the contract for one additional year. The guidelines note that the contract could potentially be renewed after the first SBC expires, if conditions for GGDCs and SRCs are not met. Whether a longer series of SBCs would be possible in a country is not clear, however, and interviewees from all EU institutions noted that what comes after the first or second SBC should be clarified. Interviewees noted that EU member states in the EDF committee, in particular, could question more than two subsequent SBCs for a country, since fundamental values would then be less prominently addressed over a longer period, comparable to that of a GGDC.

Interviewees from DEVCO and the EEAS presented three possible scenarios. The first is to use the timeframe of the first and second SBC to assess whether the partner country has established a good track record in terms of human rights and fundamental values. This would signal the government's commitment to values and provide a basis for granting a GGDC. The current track record of budget support in fragile situations, however, suggests that in most cases such a scenario is remote at best. A second scenario is that the EC stops providing general budget support after the first and second SBC period and scales down to SRCs, leaving the provision of general budget support to other international or bilateral agencies. This scenario is rather unlikely, given the relative loss of opportunities to engage in high-level policy and political dialogue as some interviewees mentioned. The current SBC for Côte d'Ivoire demonstrates the effectiveness of a dialogue at the highest levels combined with dialogue within particular sectors. A third scenario is a series of SBCs, assuming a clarification on the allowance of such longer series, which would be a pragmatic solution to the issue of long-term engagement.

D. Is there enough knowledge about the effects of mitigating measures?

Following past experiences with EU budget support, member states expressed concerns about risks and how to respond. They adopted the EC Communication on budget support in the expectation that more attention would be given to risk management and that measures to reduce risks would have traction.

The EC's risk management framework, outlined in Table 3, attaches high importance to risk response and mitigation for all forms of budget support. The guidelines refer to a variety of measures available to the EC when designing a budget support programme. These include a range of capacity development measures, such as technical assistance, political dialogue, policy dialogue and support to actors and processes to enhance transparency, accountability and participation in the budget process. Depending on the assessment, citizens and civil society might be involved, as well as parliaments, courts of auditors, public finance departments (e.g., for publishing budget figures) and the media.

These mitigating measures are applicable to SBCs but rather difficult to implement in fragile and conflict-affected settings, particularly where fragility is structural and rooted throughout society and in all regions of a country (Weijer & Kilnes 2012). Evidence from governance support in low-capacity fragile situations suggests that considerable resources and long-term commitment are required before functioning and effective endogenous processes are in place that can counter spillage, corruption and elite capture of public spending (OECD 2007).

So far, very little is known about the effects of risk response measures and how to deal with the residual risks of providing SBCs. DEVCO and EU delegation officials interviewed expressed concern about overly optimistic estimations of the effects of mitigating measures in the risk assessment framework. They suggested greater investment in learning about the effects of such measures so that more realistic prognoses could be given about the time likely to be needed before such measures show results and what type of support would be required.

E. How to approach capacity development for effective delivery?

Interviewees from EU delegations and DEVCO pointed out that decisions about the implementation of SBCs do not take sufficient account of the immense human capacity gaps in fragile states that make effective and timely implementation so challenging. They mention that EU decision makers appear to underestimate the level of fragility outside of the capital city and on what will be needed to implement an effective and timely delivery system. In South Sudan, as one EC official explained, the planned €5 million capacity development support to implement the SBC, which is worth €80 million in total, will be enough to provide assistance to the public finance management system, but more investments are needed to make the payment for health workers and teachers sustainable. In fragile states, a balance needs to be found between the need for quick delivery, perhaps requiring a considerable amount of technical assistance, and structural investments to develop capacity in the medium term (Petersen 2013). Some interviewees recommended that during assessment and design of SBCs more attention should be paid to effective flanking measures and that the BSSC should take a broader look at capacity and institutional issues in fragile states. Suggestions were made that the BSSC adopt a portfolio approach when providing SBCs, which means deciding on a balanced portfolio for the fragile country that includes a range of interventions to address capacity needs, and risks, at different levels.

F. How to deal with civil society in the context of SBCs?

Interviewees from civil society and member states stated that more attention should be paid to the role of civil society organisations in the context of an SBC. Some suggested following DFID's example and structurally committing an amount equal to 5% of budget support operations to the promotion of domestic accountability, from which support to civil society can also be funded (DFID 2011). But they also acknowledged that each country context is different and civil society actors will not in all cases be able to provide meaningful support to shaping domestic accountability. Practitioners, not linked to the EU, point out that an engagement with civil society and domestic accountability – while politically correct – might further complicate operations. Confrontational approaches, using civil society organisations as “watch dogs”, should be avoided in favour of accompanying measures to facilitate dialogue. However, capacities in fragile states, in both government and in the EU delegation, are generally highly stretched. Dedicated engagement with civil society might add too much complexity and divert attention from other priorities in a context of limited capacities.

The EC does have a reference document on engaging with non-state actors that includes recommendations on working with such actors when providing budget support (EC 2011c). Furthermore several funding instruments can be used to involve civil society, such as the European Instrument for Democracy and Human Rights (EIDHR) and the Instrument for Stability (IfS), as well as thematic budget lines. Two interviewees mentioned that there is limited knowledge within the EU on how this support to civil society can be effectively linked to budget support in fragile environments. At the delegation level, support to civil society and SBCs are generally dealt with by different desks (or often regionally in the case of the IfS). Moreover, funding instruments for civil society follow their own programming cycles and procedures, which might not match the timeframe of the design and implementation of the SBC. Interviewees from EU delegations as well as member states called for greater investment in civil society involvement in the context of SBCs and suggested building a knowledge base from where the most appropriate approach per country context can be formulated.

5. SBCs and the New Deal

So far, there is little evidence from practice to indicate how SBCs have been used in countries where the New Deal is being implemented. We limit this section to reflections based on an analysis of the EC's budget support guidelines, a reading of the New Deal and comments made about initial experiences in

implementing the New Deal. We consider this issue pertinent because the EC and member states have stated their strong support of the New Deal.

The strength of the New Deal is its ownership by a group of self-declared fragile countries (the g7+, see Box 2). The process leading to the adoption of the New Deal in Busan in 2011, was a highly participatory one in which representatives from the g7+ stressed the need for a different approach when engaging with fragile countries. According to the New Deal, external support should be based on priorities formulated by the fragile countries, and it should strengthen national systems and processes in a timely and predictable manner. Furthermore, risks should be shared and five priority areas comprehensively addressed. These five areas are formulated as “legitimate politics”, “security”, “justice”, “economic foundations” and “revenue and services”.

An SBC should be understood as one of several possible aid modalities to support a fragile country. It ought to be evident that an SBC cannot be overloaded and cannot be seen as a cure-all to stabilise an environment. Yet, the modality can provide certain leverage, in particular, if the EC intervenes with a hefty financial injection in a situation of very low own revenues and scarce state capacities to use the funding effectively.

Comparing the focus of the SBC with the five peacebuilding and statebuilding goals of the New Deal, the SBC seems to target statebuilding in particular. The funding can help stabilise the fiscal situation of a country, allowing a partner government to pay salaries and purchase equipment for providing basic services, while building and strengthening country systems and providing funding in a predictable way. Government officials from partner countries interviewed for this Briefing Note highly valued this EC support. However, questions were raised on whether SBCs are linked smartly enough to instruments that support peacebuilding, understood as processes to strengthen society from the bottom up and to help reconcile the interests of the state with those of its citizens while diffusing tensions within civil society. It is a difficult question that requires highly tailored responses, as pointed out in the earlier discussion about engagement with civil society.

The FOCUS elements of the New Deal (see Box 2), which clarify the process to be followed by a country and its development partners, are generally coherent with the steps spelled out in the SBC guidelines. The SBC requires an indication of the partner government's strategy. That could be embedded in the New Deal's “one vision, one plan”, followed by a compact, dialogue and country leadership. Less clearly linked are the New Deal's fragility assessment and the SBC fragility assessments. The latter is to be ‘conducted by the EU Delegations, in close coordination with member states and other donors active in the partner country’ (EC 2012a: Annex 9, p. 142). The guidelines do not spell out whether attempts should be made to include national partners in this process, or whether the New Deal's fragility assessment (or any other joint assessment between the partner country and the international community) should be done prior to the EU delegation's fragility assessment for the SBC. Key questions can also be raised about the division of labour. What effects will the SBC have where the EU is (or is not) the lead donor in the New Deal? How will harmonisation with other donors unfold when it comes to fragility and risk assessments?

These rather donor-centric elements of the SBC can also be seen in the budget support guidelines (“road map” for budget support in situations of fragility states). “The road map is the instrument used to identify whether a country is eligible or to identify the steps by which it could be eligible. ... In order to get the dialogue with the authorities under way as soon as possible and to inform them of the steps and conditions leading to eligibility, it is recommended that the road map be shared with them. It is also recommended that the road map be discussed with [international] partners” (EC 2012a: Annex 9, pp. 144-145). There is no doubt that partner governments' capacities in fragile countries are generally low. Nonetheless, given the

g7+ ambition to follow a new approach and to avoid repeating the mistakes of past aid management, attempts should be made to work more inclusively and provide facilitative means to involve the partner countries up front.²⁴

Finally, the SBC can support the TRUST principles of the New Deal, provided it gets a number of things right. Provision of budget support is intended to empower country systems and build national capacities. A long-term commitment is necessary, and this calls for a clarification of what comes after the first or second SBC. Risks need to be shared and disbursements need to be timely and predictable. To share risks requires a joint understanding of what the risks are. Hence, the EC and its partners will need to conduct joint risk assessments and have joint risk mitigation strategies involving dialogue as well as mechanisms to deepen the analysis over time.

The larger overall challenge for the EC and other donors, as well as for the g7+, lies in the “how” and whether implementation of an SBC, in combination with other aid modalities, can be done with consideration of and support for ongoing endogenous processes of reconstruction, however fragile they might be. This requires a cultural change within the EU and willingness to do business differently, as stressed by two officials from the EEAS and DEVCO.

6. A courageous response, but the proof of the pudding is in the eating

Provision of budget support for post-conflict, fragile and conflict-affected countries is not new for the EC. But a critical assessment by the European Court of Auditors in 2010 and tough questions raised by member states about the EC's budget support practices led to a new policy and revised guidelines to strengthen EC budget support implementation capacity. The new policy, issued in 2012, is a compromise aiming to respond to the various expectations and preferences of EU member states while accommodating the recommendations of the Court of Auditors. The policy distinguishes three types of budget support: GGDCs, SRCs and SBCs, which have been implemented since 2012-2013. This Briefing Note looked at initial experiences with the design and implementation of SBCs and questions raised by interviewees regarding the future provision of budget support in fragile contexts. From these interviews and document analysis, we extract seven principal points.

First, officials from the EEAS and DEVCO see the split into three budget support modalities as a realistic and better response to the different contexts in which budget support is provided. EC officials value budget support as it uses and strengthens country systems and is most in line with the political principles of partnership and alignment that the EC promotes, as formulated in the Agenda for Change (EC 2011a). Officials have welcomed the SBC modality, as it allows the EU to pragmatically engage with local actors in fragile environments. The added value of the modality is the provision of assistance to stabilise a country, and in a surprisingly quick way, as noted in the case of Mali. The policy is also viewed as better grounded in reality with regard to issues of governance and human rights. Fundamental values are assessed for an SBC, but adherence to human rights, democracy and the rule of law is not a precondition for approval of this type of budget support to fragile and transition countries. What matters is the partner country's expression of willingness to adhere to these values in the course of the further development of the country.

²⁴ The EC has promoted ideas for working more creatively with capacity development support and technical assistance in the context of its Backbone Strategy on Technical Cooperation and PIUs. But the budget support guidelines don't refer to it explicitly (EC 2008).

Second, EU member states differ in their expectations about the role that SBCs should play in fragile and transition countries. Some member states view SBCs only as a mechanism for use in extraordinary situations of political and social instability on a very short term basis. Other member states, however, recognise the need for longer-term engagement to help fragile states in their transition towards resilience and development. They also recognise that it may be important to work through country systems, however fragile these may be. These member states would apply the same logic for emergency situations or for structurally fragile countries. Still other member states expect EU institutions to impose political conditions to budget support for fragile countries, even though past budget support evaluations have indicated that budget support cannot be used to leverage big political reforms. Their strength is elsewhere, such as in supporting public finance management systems or reforms, and contributing to service delivery in particular sectors. Evidence and experience with different forms of budget support call for realism rather than inflated expectations.

Third, some EU officials promote SBCs as one of several “developmental” instruments to address fragility and transition, while others see SBCs as one of several “political” instruments to address geostrategic concerns for stability. Strategic planners within the EEAS argue that the leverage of providing considerable funding through an SBC should be linked to political dialogue with the country concerned and used to promote fundamental reforms such as elections and negotiations with rebel groups. Implementation of SBCs, led by EU delegations, can also lend visibility and credibility to EU external action in unstable environments, redressing the hitherto fragmented and uncoordinated nature of the EU response in such situations. Their perceptions that more funding can lead to more political influence are countered by the more “developmental” view of SBCs. This promotes predictability, technical reforms in the area of public finance management and non-conditionality, to be pursued in collaboration with the partner government and other development actors. DEVCO officials support this latter line of thinking, giving priority to poverty reduction and provision of basic services to populations. They add caution about the potential for leveraging support for political change and fundamental institutional reforms. Meanwhile, some SBCs have become an important element in the discourse within the EU institutions on how to strategically engage within fragile and transition environments.

Fourth, outsiders find it difficult to understand the choice of SBC countries. The European Council states that the decision on whether to go ahead with an SBC should be taken on a case-by-case basis, following a thorough assessment of the partner country's fragility or state of transition. Referring to the list of countries that currently get SBC of which several are perceived as lacking political will to reform for years (Box 6), EEAS officials questioned whether this modality should also apply to countries that are structurally weak and to those displaying political unwillingness to substantially reform for years. Due to this wide formulation, many countries could potentially be considered, creating a risk of inflationary use of SBCs. It is in the hands of the inter-institutional BSSC to assure that SBCs are employed only in circumstances where the aims are supportive to statebuilding objectives. The modality is too young to determine how extensively it will be used. But interviewees across institutions reckon that a very limited use might be difficult to maintain, given the expectations of some EU member states that budget support for stabilisation and statebuilding should be provided in situations where they cannot act bilaterally. Moreover, higher than anticipated numbers of requests for SBCs are being received from EU delegations, which might increase pressures to formulate SBCs.

Fifth, the sequencing of SBCs and when to exit is unclear for officials from DEVCO and the EU delegations. Past experience with budget support in structurally fragile countries indicates that long-term accompaniment is required on macro-reforms as well as political and policy dialogue at the highest level. SBC can be granted for two years with a potential extension of one additional year and the possibility for a renewal of the SBC if the conditions for the other budget support modalities are not met. Whether a series

of SBCs could be considered is unclear to many interviewees. They emphasised that the EU and its member states will need to clarify this matter, potentially along the lines of the three scenarios depicted earlier in this note (section 4, point C).

Sixth, capacity requirements for budget support in fragile contexts need considerably more attention during the preparation process, the formulation and implementation. Officials from DEVCO and the EU delegations are concerned that the vast human capacity gaps, as well as the weak partner government institutions in fragile environments, may be underestimated. More attention should be given to capacity support throughout the preparation and implementation of SBCs. These might require deployment of considerable complementary flanking measures to enable trust building and stronger ownership through dialogue and capacity building. Some suggested that the BSSC can play a conducive role in ensuring that different modalities are combined and the right partnerships with other donors are explored. Also at the level of the EU Delegations there are serious capacity constraints in terms of amount of human resources and their context-specific expertise. Several EU delegations in fragile countries currently have staff shortages that prevent an effective accompaniment of the implementation of SBCs.

Seventh, SBCs as an aid modality is in line with the statebuilding goals and principles of the New Deal. Still, questions remain on whether in the implementation of the SBC, the EU will sufficiently apply these principles in a particular context. The rationale underlying SBCs is to strengthen country systems, empower national leadership and capacities and ensure predictability for national execution. The EU, in collaboration with the other international partners that have endorsed the New Deal, will need to ensure that SBCs promote the ways of working proposed under the New Deal framework, in particular with regard to listening to the partner countries, working through national systems to the extent they exist, including civil society into dialogue to the extent possible and ensuring harmonised and joint approaches with other development partners. Experts comment that this is of paramount importance as the provision of an SBC is more than a technical issue and can influence changes beyond statebuilding. Given the relatively small funding amounts channelled through SBCs, their potential to lever change should not be overstated. But they can have an impact on the political and economic context of a partner's institutional landscape and on its further development path. Where applicable, active buy-in from national leaders and key stakeholders from civil society should therefore be solicited as early as possible and remain part of the ongoing implementation process for the duration of the SBC.

In conclusion, it is still too early to tell whether this form of budget support and the way it is implemented can add value for countries trying to leave behind a period of structural fragility, political instability or conflict. **The creation of SBCs as one of several budget support modalities appears to be a smart response by the EC to criticisms of the EU's budget support in fragile contexts.** The Commission has saved the instrument as integral part of its toolbox in fragile countries. The new instrument is more flexible than its predecessor. It allows for provision of budget support in a wide variety of contexts, ranging from countries emerging from conflict to those that are in transition or are structurally fragile. SBCs also seem to be developing into a modality that enables different EU institutions to exchange information and dialogue internally, to anchor a decision more firmly through a newly created institutional mechanism, the BSSC, and to extent the dialogue and communication to those member states and other donors who seek to respond in adapted ways to quite distinct and increasingly difficult country situations.

But the modality should not be overloaded with too many expectations and demands. SBCs cannot be seen as the principal modality to bring about stability and support transition. SBCs will need to be embedded in a wider portfolio of aid modalities and combined with a broader set of interventions (including in other policy domains) that complement one another strategically. Future evaluations of SBCs should take this into account, as emphasised by several of our interviewees.

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