Chapter 5. Support to Fiscal Management in the Crisis

This chapter reviews the quality of Bank support to developing countries in managing the fiscal challenges associated with the crisis—one of the four priority directions highlighted in the Bank’s crisis response strategy.¹ The World Bank was quick to reckon that the crisis would stress fiscal positions of most developing countries and the credit crunch would restrain the ability of emerging economies with market access to meet their gross financing needs. The Bank would play an important countercyclical role—through DPOs financed by IBRD and IDA—in helping countries meet their gross financing needs while they proceeded to adjust expenditure and revenue policies to the crisis conditions. At the same time, helping countries protect long-run investments in social development and infrastructure was identified as an overarching priority for Bank support in fiscal management. It was understood that the Bank’s support in fiscal management would be closely coordinated with the IMF and other development partners.

A guiding framework for the evaluation is the relevance and effectiveness of Bank support in strengthening medium-term fiscal positions in crisis-hit countries, while also helping protect spending that is pro-poor and promotes growth. IEG assesses Bank support in confronting the fiscal challenges countries faced. Most often, countries that entered the crisis with weak fiscal positions set fiscal consolidation as a key priority. By contrast, countries that entered the crisis from a position of fiscal strength were able to respond countercyclically, through fiscal stimulus. Although many countries fell into these two broad categories, several countries had to reprioritize expenditures, or introduce fiscal measures with a clear future payoff, to create fiscal space during the crisis for some measured stimulus or for spending to protect the poor. Uncertainty about the duration of the crisis, compounded by uncertainty about the size of distressed private sector liabilities that could possibly be assumed by the state as a result of the crisis, further complicated matters, thus making directions for Bank support less clear-cut.

The first section of the chapter reviews the patterns of Bank financial support and operation design according to fiscal policy constraints that recipient countries faced. The second section assesses the relevance of the objectives and design of Bank operations against country-specific fiscal challenges and reviews some preliminary results. Main findings are summarized immediately below; recommendations are outlined in chapter 7.
Overall Findings

About 54 percent of the Bank’s financing through DPOs that focused on fiscal management was allocated to countries with moderate fiscal stress. This pattern of financing was broadly aligned with the Bank’s exposure to client countries before the crisis, based on these countries’ pre-crisis fiscal positions. The Bank response to the crisis in fiscal management cushioned the sharp increase in financing needs associated with the crisis by incrementally augmenting the commitments of already programmed DPOs or by initiating new, stand-alone operations. Several countries that entered the crisis with low or moderate fiscal stress were able to initiate some countercyclical response that was partly financed with resources from the Bank’s DPOs.

Although there was a significant increase in commitments, the policy content of DPOs was often only partly relevant to the fiscal challenges of the crisis. Adjusting the content of programmatic DPOs was difficult in the midst of the crisis and sometimes was not achieved. In addition to fiscal management components, most crisis response DPOs included policy components with a different sector focus, and in half of the DPOs, there were components relevant to the crisis. In some cases, budget support was mainly provided through operations with no fiscal content, such as environmental DPOs, whose commitment amount was considerably augmented compared to initial plans.

Financing instruments pertaining to crisis situations, such as the Special Development Policy Loan option and DPL-DDOs, could have been used more often during the crisis. The Special Development Policy Loan option, relevant for IBRD-eligible countries confronted with crises, was made financially unattractive by the elastic use of DPOs on regular financing terms for crisis support. In countries with solid fiscal positions, the instrument was not used because of the requirement for the presence of an IMF program. DPL-DDOs have been used infrequently but have strengthened the credibility of country financing programs where fiscal positions were reasonably sound. In countries under fiscal stress, DPL-DDOs have served as regular financing instruments rather than precautionary credit lines.

Fiscal consolidation measures supported by the crisis response DPOs were often insufficient to help attain sound fiscal positions. In some cases this was because the economic and fiscal impacts of the crisis were underestimated. In other cases it was because potentially sensitive or demanding measures—such as reduction of subsidies or curtailment of low-priority investments—could not be tackled during the crisis, or because the supported fiscal measures were backward looking. In yet other cases, as the DPOs were not sufficiently modified to address the impact of the crisis; the measures supported were not necessarily called for from a stabilization perspective. Targets for the fiscal deficit, fiscal revenues and expenditures, or the public debt ratio were included in less than one-third of DPOs for countries under high or moderate fiscal stress. The relatively large number of cases in which the longer term perspective could not be reflected suggests the difficulty of using a medium-term development instrument for crisis response.

Around half of crisis response DPOs with fiscal content included provisions to safeguard or scale up social protection expenditures. Expenditures for education and health were protected in less than one-third of the DPOs, although more frequently in countries with adequate fiscal space. Similarly, public investments were safeguarded—and public works
programs scaled up—in DPOs for countries with low fiscal stress, but less frequently so where fiscal stress was more elevated.

When countercyclical policies were supported, there was not always close attention to the fiscal space required for affordable countercyclical spending. A majority of client country recipients of fiscal management-focused DPOs that entered the crisis with low or moderate fiscal stress emerged from the crisis with weaker fiscal positions. Although strong caveats apply to attribution, weak fiscal positions post-crisis tend to be associated with some weaknesses in the design of these DPOs.

Crisis response DPOs typically supported a broad array of public financial management reforms that should help attain stronger fiscal outcomes in the future. However, as such reforms require focused action over time to attain the expected results, stand-alone crisis response DPOs were not properly designed to follow up on this reform agenda. Moreover, some important structural fiscal reforms were sometimes disregarded to further fortify fiscal management in the future.

The Bank’s knowledge base in public finance was generally sufficient—with some gaps when lending had declined before the crisis. Diagnostic work was sufficient, especially in public financial management, an area where longstanding engagement had been maintained. However, there were noticeable knowledge gaps in countries where the Bank’s pre-crisis engagement had waned.

Country Fiscal Positions in the Crisis and the Response of the World Bank Group

This section first reviews the allocation of World Bank crisis response financing for DPOs with a focus on fiscal management, according to the fiscal positions and external vulnerabilities of recipient countries. It then reviews the objectives of those operations and key features of their content and design.

Patterns of Bank Crisis Response Financing Focused on Fiscal Management

A major part of the World Bank’s financial support to crisis-hit countries was channeled through DPOs with a focus on fiscal management. For this evaluation, these operations were identified by using the thematic codes of their components as selection criteria (appendix E, section 2, for details of the methodology). During FY09–10, the World Bank approved 100 DPOs with some policy content in fiscal management in 66 countries for a total commitment amount of $26 billion. This represented 63 percent of total commitments through DPOs in FY09–10.2

Crisis Response DPOs with a Focus on Fiscal Management

The majority of DPOs with fiscal management content were related to consequences of the crisis. DPOs with fiscal content that were approved in FY09–10 have been categorized as crisis response operations using the same criteria as elsewhere in this evaluation (appendix E, section 2). Based on these criteria, of the 100 operations approved in FY09–10, 67 were crisis-related, for a committed amount of $23.3 billion in 48 countries (table 5.1 and appendix table E.2).3 The remaining 33 DPOs, for a total amount of $2.7 billion, were allocated to 28
countries as noncrisis-related operations. The lion’s share of the crisis response resources (88 percent) was provided through IBRD, and the remainder through IDA.

The recipient countries were mainly in the Europe and Central Asia, Latin America and the Caribbean, and East Asia and Pacific Regions. Europe and Central Asia represented 46 percent of commitments, whereas Latin America and the Caribbean and East Asia and Pacific combined absorbed 42 percent of the resource transfer (table 5.1). The regional concentration of financial transfers partly reflects the impacts of the global economic crisis, which radiated from its epicenter in the financial sector of the developed economies to the middle-income countries, mainly in the Europe and Central Asia, Latin America and the Caribbean, and East Asia and Pacific Regions, through financial and trade linkages. It also reflects the larger headroom of these countries relative to the maximum World Bank Group lending exposure from IBRD. Countries from the Africa, South Asia, and Middle East and North Africa Regions received comparatively lower financial support through operations with a focus on fiscal management. About 60 percent of IDA allocations for such operations were absorbed by countries in the Africa Region.

Table 5.1. Allocation of DPOs with Fiscal Management Content to Crisis-Affected Countries

<table>
<thead>
<tr>
<th>World Bank Regions</th>
<th>Number of countries</th>
<th>Number of operations</th>
<th>Number of operations (% of total)</th>
<th>Committed amount (US$ millions)</th>
<th>Share of committed amount (%)</th>
<th>IBRD loans (US$ millions)</th>
<th>IDA credits (US$ millions)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Africa</td>
<td>14</td>
<td>19</td>
<td>28.4</td>
<td>1,905.6</td>
<td>8.2</td>
<td>150.00</td>
<td>1,755.60</td>
</tr>
<tr>
<td>East Asia and Pacific</td>
<td>5</td>
<td>9</td>
<td>13.4</td>
<td>4,450.0</td>
<td>19.1</td>
<td>4,000.00</td>
<td>450.00</td>
</tr>
<tr>
<td>Europe and Central Asia</td>
<td>14</td>
<td>19</td>
<td>28.4</td>
<td>10,745.9</td>
<td>46.2</td>
<td>10,555.49</td>
<td>190.40</td>
</tr>
<tr>
<td>Latin America and the Caribbean</td>
<td>12</td>
<td>17</td>
<td>25.4</td>
<td>5,366.2</td>
<td>23.0</td>
<td>5,366.20</td>
<td>0</td>
</tr>
<tr>
<td>Middle East and North Africa</td>
<td>1</td>
<td>1</td>
<td>1.5</td>
<td>300.0</td>
<td>1.3</td>
<td>300.00</td>
<td>0</td>
</tr>
<tr>
<td>South Asia</td>
<td>2</td>
<td>2</td>
<td>3.0</td>
<td>513.7</td>
<td>2.2</td>
<td>0</td>
<td>513.70</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>48</strong></td>
<td><strong>67</strong></td>
<td><strong>100.0</strong></td>
<td><strong>23,281.4</strong></td>
<td><strong>100.0</strong></td>
<td><strong>20,371.69</strong></td>
<td><strong>2,909.70</strong></td>
</tr>
</tbody>
</table>

Source: IEG review, with data from World Bank.

In most cases, crisis support was provided by augmenting commitments of DPOs that were programmed in the CPS or through new DPOs that were not previously programmed. Of the 67 crisis response operations with fiscal content, 21 were new operations not identified in the existing CPS that were initiated to address the consequences of the crisis. Seventeen were stand-alone operations, and 50 were part of a programmatic series that had either started before the onset of the crisis or were initiated during the crisis. Several of the programmatic DPOs received enhanced financing, with the amounts earmarked in the CPS increased in 26 of the 67 crisis response operations.
None of the disbursed crisis response DPOs with fiscal content was prepared under the Special Development Policy Loan Option.\(^5\) The lack of use of the Special Development Policy Loan partly reflects an elastic use of the standard DPO instrument for crisis-hit countries.\(^6\) The accelerated processing of standard DPOs, the increase in commitments compared to the original CPS lending programs, and the supplemental DPO financing often made available rendered the Special Development Policy Loan option financially unattractive. Moreover, the requirement for presence of an IMF program made the Special Development Policy Loan option irrelevant for IBRD-eligible countries that faced the crisis with reasonably solid fiscal positions, as in many of these countries no IMF-supported program was in place.

**Crisis Response DPOs and Lending Commitments According to Country Fiscal Positions and External Vulnerabilities**

Options for fiscal management of the crisis were, to a large extent, shaped by the strength of country fiscal positions. Countries with high debt, irrespective of the level of the fiscal deficit, were particularly vulnerable to the crisis: To the extent a high debt level created large gross refinancing needs (depending on the profile of maturing debt), the virtual vanishing of international credit at the outbreak of the crisis increased the risk of debt distress—a risk further exacerbated in countries with large fiscal deficits. Fiscal adjustment to attain debt sustainability was a priority in most of these countries. Options for countercyclical response in these countries were virtually nonexistent, unless policies could be introduced that would clearly improve the fiscal situation in the future. By contrast, some countries with a large fiscal deficit but a low level of debt could consider options for partial deficit financing, with some debt build-up, and could thus let the fiscal automatic stabilizers operate. Countries with low levels of debt and deficit could use their fiscal space more proactively for countercyclical response through fiscal stimulus.

The assessment of fiscal positions of the 48 countries that received DPOs with fiscal management content is based on the fiscal deficit and the level of public debt before the crisis. IEG constructed an indicator of fiscal stress for this evaluation as the average of two rank-nings of the 48 client countries (i) by the level of fiscal deficit (in percent of GDP) in 2007–08 and (ii) by the level of gross public debt in proportion to GDP in 2007–08 (appendix E).\(^7\) Based on their average scores, the 48 countries were categorized on a continuum of fiscal stress, divided, for illustrative purposes, into three zones:

- Low fiscal stress (lower third of scores)
- Moderate fiscal stress (middle third of scores)
- High fiscal stress (upper third of scores).

However, it should be noted that, at a time of crisis, gross refinancing needs associated with a given level of fiscal deficit and (maturing) public debt may entail different levels of fiscal stress for emerging economies with capital market access (such as IBRD borrowers) and low-income countries that mostly rely on financing from official sources (such as IDA borrowers). Emerging economies with market access may face a risk of sudden debt distress when credit flows evaporate, and rollover of maturing official debt of low-income countries may prove easier to handle. The Bank’s flexibility in scaling up IBRD financing during the crisis may thus have been valuable to some client IBRD countries—by covering part of gross refinancing needs or by augmenting reserves as an additional defense line to vanishing capital market
credit. An objective counterfactual scenario for the evaluation of such an impact is difficult to elaborate, however, and requires analysis of alternative scenarios country by country.

Forty-eight countries were identified to have received fiscal management–focused DPOs during the crisis. The majority of this group (25) fall into the zone of moderate fiscal stress; another 10 fall into the low fiscal stress zone; the remaining 13 fall into the zone of high fiscal stress (table 5.2). Countries within these categories entered the crisis from broadly varying fiscal positions: although countries in the low fiscal stress zone had, in 2007–08, a slight fiscal surplus and a public debt not exceeding 20 percent of GDP, countries in the high fiscal stress zone entered the crisis with an average fiscal deficit of 5.3 percent and public debt at 70 percent of GDP.

The majority of commitments of crisis response DPOs with a focus on fiscal management were concentrated in countries with moderate fiscal stress. Table 5.2 shows that the 25 countries in the moderate fiscal stress zone absorbed 54 percent of the total resources committed, through 37 of the 67 crisis response DPOs. The 13 countries in the high fiscal stress zone received about one-third of resources. The 10 countries in the low fiscal stress zone absorbed 13 percent of committed resources. Commitments in proportion to client country GDP varied, on average, from 1 percent in countries with “moderate” fiscal stress to 0.8 percent in countries with “low” fiscal stress to 0.9 percent in countries that were highly affected, with considerable variation among individual countries. Financing through DPOs with a focus on fiscal management broadly reflects the pattern of World Bank Group pre-crisis exposure to the 48 client countries based on these countries’ pre-crisis fiscal stress. The share of financing to the 10 countries with low fiscal stress slightly exceeded, by 3.2 percentage points on average, the share of outstanding IBRD and IDA debt of these countries before the crisis (at the end of 2007).

Table 5.2. Fiscal Positions of Countries Receiving DPOs with Content in Fiscal Management

<table>
<thead>
<tr>
<th>Fiscal position category</th>
<th>Number of countries</th>
<th>Number of operations</th>
<th>Number of countries (DPOs) with IMF facility</th>
<th>Committed amount (US$ millions)</th>
<th>Share of total commitments (%)</th>
<th>IBRD loans and IDA credits outstanding (end of 2007; % of total for the 48 countries)</th>
<th>Committed amount (% of country GDP, 2009-10)</th>
<th>Average fiscal deficit (% of GDP, 2007-08)</th>
<th>Average public debt (% of GDP, 2007-08)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Low fiscal stress zone</td>
<td>10</td>
<td>11</td>
<td>5 (6)</td>
<td>3,080.8</td>
<td>13.2</td>
<td>9.9</td>
<td>0.8</td>
<td>1.2</td>
<td>20.1</td>
</tr>
<tr>
<td>Moderate fiscal stress zone</td>
<td>25</td>
<td>37</td>
<td>15 (21)</td>
<td>12,650.0</td>
<td>54.3</td>
<td>56.6</td>
<td>1.0</td>
<td>-1.2</td>
<td>38.6</td>
</tr>
<tr>
<td>High fiscal stress zone</td>
<td>13</td>
<td>19</td>
<td>10 (14)</td>
<td>7,550.6</td>
<td>32.4</td>
<td>33.5</td>
<td>0.9</td>
<td>-5.3</td>
<td>70.1</td>
</tr>
<tr>
<td>Total</td>
<td>48</td>
<td>67</td>
<td>30 (41)</td>
<td>23,281.4</td>
<td>100.0</td>
<td>100.0</td>
<td>0.9</td>
<td>-1.8</td>
<td>43.3</td>
</tr>
</tbody>
</table>

Source: IEG review of crisis response DPOs.

Among the 67 crisis response DPOs, 41 coincided with IMF facilities (Stand-By Arrangement, Poverty Reduction and Growth Facility, or Flexible Credit Line) in 30 of the 48 reci-
pient countries. There was also cofinancing or parallel financing by other donors in about half of the 48 crisis-hit countries supported by the Bank. IMF facilities were in place in 77 percent of countries in the high fiscal stress zone and in 60 percent of those in the moderate fiscal stress zone. An IMF facility was present in about half of the countries in this sample with low fiscal stress (table 5.2).

Financing through DPOs with a focus on fiscal management broadly reflected the pattern of the Bank’s pre-crisis exposure to these countries. However, the pattern of Bank financing according to client country fiscal stress needs to be interpreted with caution. First, it takes time to formulate good policies, and thus it comes as no surprise that a significant part of financing was directed to countries with moderate and low fiscal stress. Moreover, the process may be easier in countries where there is significant engagement. Second, in countries with low or moderate fiscal stress, space existed for countercyclical response. Where fiscal stress was high, a main challenge was to help countries formulate appropriate policies to attain sustainable fiscal positions, although room for financing the deficit was limited.

Creditworthiness considerations may have also limited the room for lending in some of these countries. The presence of an IMF program may have had an ambiguous role. Most of the countries under high fiscal stress (10 of 13) had an IMF facility in place, which may have strengthened the Bank’s proclivity to lend or, conversely, may have reduced these countries’ need for incremental Bank financing. Also, as discussed in chapter 2, flexibility in the allocation of Bank resources to client countries depends on the financing window: In IDA countries, allocation is determined largely by IDA’s available resource and performance-based allocation system and there is limited scope for reallocation, although additional front-loading possibilities were offered by Bank management. By contrast, crisis-response financing could be significantly stepped up in IBRD countries and, as noted, the vast majority of financing through fiscal management-focused DPOs (88 percent) was provided through IBRD.

Countries that received DPOs with a focus on fiscal management entered the crisis with varying degrees of external vulnerabilities that generally reflected the soundness of their fiscal positions. For the purpose of this evaluation, the external vulnerabilities of the 48 countries were approximated by two metrics, measured at the end of 2008: (i) the import coverage, in months, of foreign exchange reserves, and (ii) the foreign-currency denominated debt in proportion to exports. A composite indicator of external vulnerability was constructed similarly to the indicator of fiscal stress, based on these two sub-indicators (appendix E, section 2). As fiscal imbalances often result in external current account imbalances that create external debt or reduce the adequacy of foreign exchange reserves, the indicator of external vulnerabilities at the onset of the crisis was positively and significantly correlated with the degree of fiscal stress (figure 5.1). Thus, the findings concerning the Bank’s fiscal management-focused DPOs apply broadly to categorizations according both to fiscal stress and to vulnerabilities of external positions of the recipient countries.
THE CONTENT OF CRISIS RESPONSE OPERATIONS IN FISCAL MANAGEMENT

A primary objective of crisis-response DPOs, though not always explicitly stated, was to provide budget support or ensure that short-term gross financing needs would be met at a time when international credit markets were closed. Financing of countercyclical programs was also an objective in countries that had the fiscal space for stimulus—either through the action of automatic stabilizers in the budget (Uruguay and Mexico) or through proactive stimulus packages (Indonesia, Peru, and Vietnam). In some cases, the Bank’s stepped-up financing allowed the refinancing of existing debt falling due (El Salvador and Jamaica). Sometimes the increase in the DPO commitment amount came at the expense of other investment lending programs in the CPS that were cancelled or postponed (Uruguay).

The 67 crisis-related DPOs with a focus on fiscal management most often included various subthemes. The fiscal subthemes occurred with varying frequency, ranging from 30 to almost 90 percent of the portfolio reviewed by IEG (figure 5.2). Three of these subthemes were most prominent: measures to strengthen macroeconomic management and ensure fiscal sustainability; structural reforms aimed at improving the cost-effectiveness of public expenditures; and public financial management reforms, including procurement. Program design around these three pillars was common and was often favored over more complex, and perhaps more sensitive, measures such as reforms in tax policy and revenue administration or civil service reforms.
However, often the crisis response DPOs included policy components unrelated to the fiscal incidence of the crisis. In addition to a fiscal management component, 90 percent of the DPOs included components with a different sector focus. And in about half of the DPOs these components were designed to address crisis-related issues (figure 5.2). Examples of crisis response stand-alone operations with components unrelated to the crisis include the DPOs in El Salvador (primary education, science and technology policy), Costa Rica (telecom sector, insurance, protection of intellectual property rights), Jordan (access to finance and business environment reforms), and Mexico (trade policy reform). In most cases, the fiscal measures supported by DPOs were part of an ongoing structural reform agenda, especially in tax administration and public financial management. However, in some cases, these measures were not necessarily called for from a countercyclical or consolidation perspective (for example, in El Salvador, Costa Rica, and Peru).

Figure 5.2. Content of Crisis-Related DPOs in Fiscal Management (in percent of operations)

![Bar chart showing the content of crisis-related DPOs in fiscal management](chart.png)

Source: IEG DPO portfolio review.

The fragmentation of policy components into sector policy agendas unrelated to the crisis was unwarranted in stand-alone operations designed with the aim of responding to the crisis. Content unrelated to the crisis could be justified in programmatic DPOs, as these operations typically support several objectives under the CPS pillars over time. However, stand-alone operations were ill designed to support structural policy reform agendas in other sectors, as there were neither follow-up actions nor tracking of progress over time.

Some DPOs that were part of programmatic series were not modified to address the consequences of the crisis. In Vietnam, for example, the 2009 Poverty Reduction Support Credit-8 was contemporaneous with the outbreak of the crisis and the government’s response to it through a significant stimulus package. It was approved under the IDA Fast-Track Facility, and the original amount of $150 million was augmented to $350 million—and supplemented
by as much as $240 million by other cofinanciers. Yet its content was unrelated to manage-
ment of the crisis. Similarly, the resources provided under the 2009 Public Investment
Reform DPL ($500 million) supported the financing of the stimulus package, but the pro-
gram was focused on strengthening the public investment project cycle.\textsuperscript{10} In Peru, the con-
tent of the second DPL in the series ($350 million) was not modified in response to the crisis,
and supplemental financing of $330 million was provided in the fall of 2008. Only the third
DPL, approved in the fall of 2009, was modified to include, ex post, key measures in the
government’s stimulus plan.

Only about half of crisis response DPOs with fiscal content included measures to protect
social expenditure programs and infrastructure programs. The absence of such measures in
half of the crisis response DPOs seems at variance with one of the stated strategic directions
of World Bank crisis support—protecting social programs and investments in infrastructure.
In some cases, as analyzed in chapter 6, the Bank provided crisis-related financial support to
social expenditure programs and infrastructure through investment lending operations or
DPOs in these sectors.\textsuperscript{11} However, in parallel with financing of specific social programs, the
crisis response DPOs with a focus on fiscal management would have been an important in-
strument to address trade-offs in the protection of spending in the social sectors and infra-
structure within an affordable medium-term fiscal envelope. This is because the larger the
share of public spending to be protected, the less effective any attempt to improve fiscal po-
sitions during a crisis is likely to be. In countries with adequate fiscal space this might have
been a secondary concern, but in fiscally stressed countries measures would have been
needed to ensure that countercyclical spending remained fiscally affordable. As further ana-
alyzed in the next section, there are differences among Bank DPOs regarding the extent of
protection of these expenditures that reflect the availability or lack of fiscal space.

Similarly to the fiscal management-focused DPOs with components unrelated to the crisis,
the Bank extended countercyclical financing through DPOs with sector focus unconnected
to the global crisis—with “environmental DPOs” a prominent example of such operations.
Eight DPOs with special focus on environmental management and climate change were ap-
proved during the crisis, in six countries, for a total commitment amount of $3 billion. In
four of these countries (Brazil, Colombia, Mexico, and Peru), these DPOs were recalibrated
in response to the financial crisis by advancing their schedule of preparation and increasing
the commitment amount, with no noticeable change in content—although in Brazil the pro-
gram was broadened to include reforms at the Ministry of Environment and the National
Water Agency (appendix E, section 3).

Environmental DPOs provided a financing safeguard in the face of the crisis and, to some
extent, facilitated the financing of fiscal stimulus. Had a different facility been available for
flexible countercyclical support to countries with solid fiscal fundamentals, the Bank might
have been able to avoid using sector operations that were seemingly unrelated to the global
crisis for crisis support. Moreover, it is doubtful that the crisis-driven increase in funding will
help achieve higher environmental objectives through these DPOs because their content was
not strengthened in parallel with the augmentation of their amount.
CHAPTER 5
SUPPORT TO FISCAL MANAGEMENT IN THE CRISIS

The Relevance of Operation Objectives and Design in Fiscal Management

This section reviews the relevance of objectives and design of crisis response operations in fiscal management from two angles: first, from the angle of strengthening fiscal positions, especially in countries that entered the crisis with fiscal vulnerability and, second, from the perspective of providing support to countercyclical fiscal policies, where fiscal space for stimulus existed or could be created. It then looks at fiscal outcomes in recipient countries in comparison to fiscal positions before the crisis. Finally, it reviews the focus areas of structural fiscal reforms supported by these operations, especially in public financial management, and concludes with a discussion of their analytical underpinnings.

Support to Strengthening Fiscal Positions

To help countries attain stronger fiscal positions, most of the crisis response DPOs aimed to improve the cost efficiency of public expenditures. The streamlined review of the 67 crisis response DPOs reveals that such measures were included in about two-thirds of the DPOs and in almost all the countries in the high fiscal stress zone (figure 5.3). Such measures included, for example, improvements in the targeting of social entitlements or cuts on low-priority administrative expenditures.

However, other potentially demanding or politically sensitive measures were included in these operations with much lower frequency. Such is the case of measures to better control the wage bill, reduce subsidies, or curtail low-priority public investments, which occurred in one-third or less of crisis response DPOs. Equally low was the frequency of tax policy and tax administration reforms to boost revenue collections (figure 5.3). Prior actions or triggers that required specific targets for the fiscal deficit, fiscal revenues and expenditures, or the public debt ratio were also less frequent. Such targets were included in less than one-third of the reviewed crisis response DPOs, with no noticeable difference in frequency regarding the strength of country fiscal positions.

The measures of fiscal consolidation supported by fiscal management–focused DPOs reflected only to a limited extent differences in countries’ fiscal positions. The streamlined review of the 67 crisis response DPOs reveals that the frequency of expenditure or revenue measures to attain a stronger fiscal position differed only to a limited extent across countries (figure 5.3). Measures to help better control the wage bill and reform the tax administration occurred more frequently in DPOs in countries with high fiscal stress—although their frequency remained generally low even in these countries. Prior actions to reduce subsidies or curtail low-priority public investments were used infrequently across countries, regardless of their fiscal stress at the onset of the crisis. It is notable that targets for the fiscal deficit, fiscal revenues, expenditures, or the public debt were not set frequently enough in DPOs for countries in the high fiscal stress zone, despite the more demanding fiscal challenges facing these countries and the higher surrounding risks as a result of their weak fiscal positions.
Reflecting the above patterns in the design of crisis response DPOs, measures to attain sound fiscal positions were often insufficient in the short run. The in-depth reviews conducted by IEG (appendix E, section 4) indicate that DPOs often did not support specific expenditure reforms to reduce or reprioritize spending on a sustainable basis (Costa Rica, Jamaica, Jordan, Mexico, and Serbia). In some cases, the operations focused on tax policy or tax administration reforms that were not sufficient to reduce the budget deficit as needed (Costa Rica, Jordan). Often, although support for fiscal consolidation was an objective of the DPOs, the measures focused on improving budget processes over the medium term rather than on actionable expenditure rationalization or revenue mobilization measures. For example, in Serbia the program supported some important medium-term reforms, especially in public financial management and pensions, but a nominal freeze of wages and pensions was included in the 2009 DPO as a benchmark, not a prior action. In some cases, the prior actions were backward looking, referring to realized fiscal targets, with no agreed measures that would have resulted in sustainable performance during the crisis and beyond (Ukraine). Yet in some other cases the DPOs supported potentially reversible expenditure reductions, such as the curtailment of the public investment program in Jordan in 2009.

In a few cases, however, the operations focused on bold fiscal measures deemed necessary to attain a sound fiscal position. For example, the 2009 DPO in Ghana supported a hiring freeze in the public sector and elimination of “ghost workers” through a public employment
audit in all ministries and government agencies. The government took additional measures to curtail investment and recurrent spending as way of reducing a deficit that had attained 14.5 percent of GDP in 2008. As a result, the deficit was reduced to 6.6 percent in 2009, in line with an ambitious target of 4.5 percent in 2011.

In several cases, the impact of the crisis on economic activity was underestimated, resulting in an increase in the fiscal deficit and public debt that surpassed projections (Costa Rica, El Salvador). In countries with reasonably sound fiscal positions, the Bank’s operations rightly accommodated the countercyclical worsening of the fiscal balance. However, the worsening of the fiscal balance was indefensible and in some cases required a swift fiscal tightening to maintain a sustainable fiscal position (Poland). In El Salvador, the government plans to submit legislation over the next two years to raise additional tax revenues equivalent to 3 percent of GDP over the medium term to attain a sound fiscal position. The 2009 loans from the World Bank Group and IDB, which were meant to refinance foreign debt falling due in 2011, were used to finance the larger-than-expected budget deficit. New foreign debt had to be issued in January 2011 to pay off the debt falling due in mid-2011 at high interest rates because of the downgrade of the country’s sovereign debt ratings.

Effectiveness of Operations with Deferred Drawdown Options in Strengthening the Credibility of Country Financing Programs

Some DPOs designed for precautionary purposes have succeeded in improving conditions to access credit markets during the crisis. Of the 67 crisis response DPOs with fiscal content, only 9 were designed as precautionary instruments with DDOs in 7 countries (Costa Rica, Guatemala, Indonesia, Mauritius, Panama, Peru, and Uruguay).

A good example of a DPL-DDO that served its purpose well is the Public Expenditure Support Facility of $2 billion for Indonesia, approved in March 2009, and complemented by another $3 billion from Australia, Japan, and ADB. The aim of the contingent support package was to provide a backstop for essential public expenditures in the 2009 budget, while reassuring markets about Indonesia’s ability to meet its financing needs at reasonable cost. Indonesia was able to access the market again by mid-2009, with larger issuance at long maturities and lower yields on new issues. The loan was thus neither drawn nor rolled over, and it was closed as planned at the end of 2010. It is possible that the significant improvement in market access for Indonesia reflects, to some extent, the positive impact on confidence of the contingent credit line provided by the DPL-DDO (appendix E, section 4).

Similarly, in Peru, the July 2008 DPL-2 was designed with a DDO and was followed, in November 2008, by supplemental financing of $330 million as a DDO. Although Peru had fairly strong balance of payments and budget positions, these operations were designed to signal to markets that the country had enough buffers to deal with the financial turmoil. The direct financial impact of the crisis on Peru was contained and the supplemental DPL-2 financing was not drawn. Peru was one of the first Latin American countries to issue sovereign debt in the second half of 2009.

In other cases, there was no impact of the contingent feature of DPOs on market access. The 2008 DPO-2 in Uruguay ($400 million) and the 2009 DPO in Costa Rica ($500 million) were also prepared as precautionary crisis response operations, with DDOs, as both countries
were vulnerable to capital outflows. The way these operations were handled differs, however, from the cases of Indonesia and Peru.

In Uruguay, the loan was drawn immediately following effectiveness, in January 2009, to cover the increasing financing needs of the budget.

In Costa Rica, the DPL-DDO was approved in April 2009, at the same time as a 15-month Stand-By Arrangement with the IMF in the amount of $726 million. Congressional approval of the loan was delayed until August 2010, but it was drawn immediately after approval. At the same time, the authorities continued to treat the IMF arrangement as precautionary. The DPL-DDO seems to have served in this case as a debt management instrument, to lengthen the average maturity of the increasing public debt, with the IMF Stand-By Arrangement serving as an insurance instrument against future market turmoil.

As suggested by the case of Indonesia, especially when there is no IMF contingency financing in place, DPL-DDOs can help improve the credibility of the government’s financing program if the commitment amount is substantial and the country’s fiscal position is reasonably sound. The Bank could consider using the DDO option more frequently in future crises, specifically in countries that meet these conditions. However, in Indonesia, the DPL-DDO was subject to certain restrictive drawdown conditions built in the financing strategy issued by the government—as one of the prior actions for its approval by the Bank. A more flexible design would have made the DPL-DDO more accessible to the authorities without the need for a waiver or a change in drawdown conditions that may have sent a negative signal to markets.

**Support to Countercyclical Fiscal Policies**

As with measures to strengthen fiscal positions (figure 5.3), there is variance across DPOs with fiscal content regarding the emphasis placed on countercyclical measures and the design of these measures (figure 5.4). These differences reflect, to a considerable extent, the fiscal space available to client countries at the onset of the crisis. There were also differences in the attention of these DPOs to the fiscal affordability of countercyclical measures, to ensure that a sound fiscal position would be maintained post-crisis.

**Attention to Public Expenditure Allocations for Social Protection Was Mixed**

Less than half of crisis-related DPOs included provisions to safeguard expenditures in the social sectors (figure 5.4). In particular, as found by the streamlined reviews of the 67 crisis response DPOs, expenditures for social safety net programs were protected or scaled up in about half of these operations. Other social protection programs were safeguarded less frequently through prior actions. Similarly, expenditures for education and health care were protected in less than one-third of the crisis response DPOs that had a focus on fiscal management. Ascertaining whether the level of expenditures in education and health was adequate in the countries where measures to protect these expenditures were not envisaged by the Bank’s DPOs is beyond the scope of this evaluation. Such an assessment was by and large missing in the operations reviewed.
DPOs in countries with adequate fiscal space more frequently included measures to protect or scale up social expenditures than did DPOs for countries that were fiscally constrained. In more than 60 percent of DPOs in countries in the low fiscal stress zone expenditures for social safety net programs were protected or scaled up—a significantly higher proportion compared to countries with moderate or high fiscal stress (figure 5.4). Expenditures for other social protection programs, such as pensions and disability, were protected even more frequently in countries with fiscal space (low fiscal stress) than in countries with moderate or high fiscal stress. Expenditures for education and health were also protected more frequently in countries in the low fiscal stress zone. However, even in these countries, these expenditure programs were safeguarded in only about one-third of the Bank’s DPOs with a focus on fiscal management—a proportion that was reduced to 20–25 percent in countries with high or moderate fiscal stress.

**Figure 5.4. Countercyclical Measures Supported by Crisis Response DPOs (in percent of operations, according to country fiscal stress zone)**

<table>
<thead>
<tr>
<th>Expenditure Program</th>
<th>Low fiscal stress</th>
<th>Moderate fiscal stress</th>
<th>High fiscal stress</th>
</tr>
</thead>
<tbody>
<tr>
<td>Expenditures for social safety net programs were protected or scaled up</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
</tr>
<tr>
<td>Other social protection programs (pensions, disability) were protected or scaled up</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
</tr>
<tr>
<td>Expenditures for education were protected</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
</tr>
<tr>
<td>Expenditures for health care were protected</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
</tr>
<tr>
<td>Civil service pay was protected</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
</tr>
<tr>
<td>The public investment program was re-prioritized</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
</tr>
<tr>
<td>A stimulus package scaled up expenditures for public works</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
</tr>
<tr>
<td>The operation supported establishing a contingency to recapitalize banks</td>
<td>[ ]</td>
<td>[ ]</td>
<td>[ ]</td>
</tr>
</tbody>
</table>

Source: IEG DPO portfolio review.
Note: DPO = Development Policy Operation.

The public investment program was reprioritized to maintain key growth-promoting investments in countries with fiscal space, but less frequently so when fiscal stress was more elevated. As found by the streamlined reviews of the 67 DPOs conducted by IEG, reprioritization of the public investment program occurred in 70 percent of the DPOs in countries with low fiscal stress (figure 3.4), so that key capital expenditures could be maintained or scaled up to support the economy during the crisis. Reprioritization occurred with lower frequency in 30 percent of DPOs in countries under moderate fiscal stress, where some
measured countercyclical response was possible. Only in a handful of DPOs in high fiscal stress countries could such measures be supported.

More than half of fiscal management–focused DPOs included provisions for scaling up public works in countries with fiscal space (low fiscal stress). The frequency of support to public works was much lower in DPOs for countries with moderate fiscal stress, whereas such measures were absent in DPOs where fiscal stress was high. Similarly, protection of civil service pay occurred with low frequency in DPOs for countries with moderate or high fiscal stress (figure 3.4). However, measures to safeguard civil service pay were present in about 30 percent of DPOs when country fiscal stress was low.

Fiscal measures to protect or scale up pro-poor expenditures in response to the crisis were often targeted with adequate cost estimates. In its in-depth reviews of fiscal management–focused DPOs, IEG found several examples of such measures in DPOs for El Salvador, Ghana, Georgia, Jordan, Poland, and Romania (section 1 of appendix E, section 3 on findings from in-depth operation reviews). In most of these countries, the DPOs helped expand or hold the line on the level of essential social expenditures, expanded and better targeted social spending, and supported efforts to increase the efficiency of spending in the future.

However, some DPOs that supported countercyclical policies or stimulus packages did not pay enough attention to the allocation of higher spending to specific expenditure programs—including for social protection or for public investment with high impact on employment and growth (Mexico in 2009 and Costa Rica). In some cases, the DPO supported frontloading of already programmed current and capital expenditures in the budget, with no attention to expenditure allocations (Mexico in 2009).

In Nigeria, for example, one of the key objectives of the 2009 Development Policy Credit was to help maintain sound fiscal policies in an uncertain environment. It sought to accomplish this by supporting a revised budget based on a conservative oil price assumption and continuing to save excess oil revenues in the stabilization fund (excess crude account). The program supported maintaining federal expenditures in 2009 within a range of 23–25 percent of GDP. This outcome was achieved by releasing savings from the excess crude account equivalent to 4.3 percent of GDP. However, the program contained no provisions for the protection of specific expenditure categories, including in the social sectors, or for reprioritization of expenditure allocations within a tighter budget envelope. A prior action to improve the execution of the capital budget was included in the program with the aim of increasing expenditure on labor-intensive projects, but capital expenditures declined to 3.8 percent of non-oil GDP in 2009, from 4.6 percent in 2008.

In other cases, DPOs provided implicit support to government countercyclical programs by assessing these programs—and the associated macro framework—as satisfactory, without including any of the countercyclical measures in their fiscal management components (Costa Rica, Indonesia, Uruguay, and Vietnam). A notable exception is Peru, where, although the 2008 second Fiscal Management and Competitiveness DPL and the 2009 Results and Accountability DPL did not contain provisions for expenditure allocations to safety net programs, the September 2009 third DPL for Fiscal Management and Competitiveness was modified to include measures in the government’s stimulus package. As a result of the government’s commitment to pro-poor spending during the crisis, programs targeted to the ex-
Extreme poor were scaled up from 1.4 percent of GDP in 2007 to 1.8 percent in 2010. The Indonesia Public Expenditure Support Facility supported provisions in the 2009 budget to sustain and, if necessary increase, critical public expenditures in the event of a pronounced growth slowdown, though without specifying thresholds below which such provisions would be triggered.

**Attention to Fiscal Space for Countercyclical Policies**

IEG’s in-depth reviews indicate that crisis response DPOs did not always pay due attention to expenditure allocations or the revenue mobilization measures needed to create fiscal space for countercyclical spending. As a result, in some cases, higher spending was concentrated on expenditures that were not easily reversed, such as civil service wages, and that may end up permanently worsening the fiscal position (Costa Rica). In other cases, especially in countries that did not have much room for deficit financing, the measures envisaged to help create fiscal space, especially in tax policy and tax administration, were modest and could not prevent a deterioration of the fiscal position (Costa Rica, El Salvador, Uruguay). In Uruguay, tax revenue performance was in line with targets in the crisis-response DPO, but the primary fiscal surplus fell short of the targets envisaged.

In El Salvador, for example, more emphasis would have been warranted on comprehensive measures to reduce general subsidies to finance the new social spending supported by the two crisis-related DPOs. The reduction in electricity subsidies for large consumers and some new indirect taxes were steps in the right direction to open up fiscal space. However, they were not enough to offset the impact of the crisis on the fiscal position, and a reduction in a transportation subsidy supported by the second DPO was later partly reversed as oil prices rose in 2011.

As with the use of the environmental DPOs, in some cases the Bank’s fiscal management-focused DPOs provided financing for countercyclical response without relevant policy content. An example of this approach is the Poverty Reduction Support Credit-8 and Public Investment Reform DPL in Vietnam, which provided financial resources for the government’s stimulus package, although the operations did not include any policy content to support or guide this package. In some cases, as in Peru, prior actions for countercyclical policy were an inherent part of the Bank’s DPOs. The design and fiscal affordability of countercyclical stimulus programs seems to have been more appropriate when these programs have been included in Bank DPOs (appendix E, section 4).

**Resilience of Fiscal Positions in the Aftermath of the Crisis**

A majority of client countries that received fiscal management-focused DPOs emerged from the crisis with weaker fiscal positions. In 28 of the 48 client countries, the fiscal deficit and public debt (in proportion to GDP) were higher in 2010 than their average levels in 2007–08, before the crisis (figure 5.5). A caveat applies, as countries resorted to borrowing in response to the crisis; thus, some increase in debt in proportion to GDP was to be expected in its aftermath. As complementary indicators of fiscal outcomes, for the 16 countries where IEG conducted in-depth reviews, the fiscal deficit and public debt projected during the crisis for 2011 were compared to the most recent post-crisis projections for the same year (appendix E, section 4).
In all these countries, either the public debt or the fiscal deficit projected post-crisis for 2011, or both, exceeded the pre-crisis projections. A higher public debt was expected in 13 countries, and larger fiscal deficit was expected in 11. As this analysis does not rely on cyclically adjusted fiscal deficits, which are available for only few emerging economies, it is impossible to assess whether the deterioration of fiscal positions was commensurate with the growth contraction that resulted from the crisis or reflected some fiscal stimulus that still persisted in 2010.\textsuperscript{14} Assessing whether the fiscal positions post-crisis are consistent with debt sustainability is beyond the scope of this evaluation. However, countries with a significant deterioration of their fiscal positions face the challenge of fiscal consolidation, so as to be prepared against the risk of a possible fading of the global recovery.

Weak fiscal positions after the crisis tend to be associated with some weaknesses in the design of fiscal management-focused DPOs. As noted in IEG’s streamlined and in-depth reviews, the Bank’s DPOs often paid insufficient attention to the available space for fiscal stimulus, to the reversibility of stimulus measures, and to forward-looking measures to attain fiscal sustainability. Often the impact of the crisis on fiscal positions was underestimated, as indicated by the larger than initially projected fiscal deficits and/or debt for 2011 in the countries where in-depth reviews were conducted. In some cases, DPOs provided counter-cyclical financing without policy content related to the crisis. Where such weaknesses in the design of the Bank’s DPOs were present, the deterioration in fiscal positions after the crisis was noticeable. In some cases this partly reflected ill-designed stimulus measures (Costa Rica, El Salvador, Vietnam); insufficient measures of fiscal consolidation and underestimation of the fiscal impact of the crisis (Poland, Romania, Serbia); or a combination of these factors. In Jamaica, measures supported were initially insufficient to reverse the dynamics of public debt, and in Nigeria the Bank’s support could not help manage the budget’s procyclicality resulting from the rebound in the price of oil after the crisis. In a few countries with high fiscal stress at the onset of the crisis, there is evidence of an overall improvement of the fiscal position (Ghana) or of a reduction in debt with only a moderate widening in the fiscal deficit (Jordan).

Associating fiscal outcomes with the Bank’s fiscal management-focused DPOs is subject to strong caveats, however, and is not amenable to evaluation. In addition to the noted limitations of the overall fiscal deficit as indicator of fiscal performance, the lack of counterfactual fiscal outcomes in the absence of Bank support calls for caution in the assessment of the results of this support. Also, the Bank’s support was often provided as part of joint support packages with other development partners—especially the IMF—thus further complicating attribution. Finally, many of the Bank’s crisis response DPOs that are part of programmatic series have yet to be completed, thus making the assessment of their results premature.
Figure 5.5. Change in Overall Fiscal Deficit and Gross Public Debt in Countries that Received DPOs with a Focus on Fiscal Management, 2010 Compared with Average for 2007–08 (in %)

Source: IEG based on data from IMF 2010.
Note: Negative (positive) signs are assigned to fiscal deficits (surpluses) in 2007–08 and 2010.

SUPPORT TO STRUCTURAL FISCAL REFORMS

Public financial management reforms were a key focus area of crisis response DPOs. Based on the streamlined portfolio reviews conducted by IEG, measures to improve budget planning, execution, comprehensiveness, and transparency were present in 88 percent of the 67 crisis-related DPOs. Public financial management reforms were supported in 15 of the 16 countries where in-depth operation reviews were conducted for this evaluation (appendix table E.3). Reform of budget processes was a common focus area in all 15 countries—with budget preparation attracting particular attention in 11 countries and budget execution in 9 countries. Cash management and public procurement were the next most common public financial management reform areas. Tax or customs administration measures, in some cases both, were included in DPO programs in 9 of the 16 focus countries. Reforms of external audit and debt management were pursued in fewer cases.

Some public financial management reforms, especially in financial management and budget comprehensiveness and execution, should pay off in the short term by assisting fiscal consolidation programs in countries with weak fiscal positions. Such is the case, for example, of the detailed quarterly fiscal outturns initiated in Ghana; the upgraded internal audit functions in Jamaica; the spending limits by line ministries, prior to budget formulation, introduced in Romania; and the medium-term expenditure ceilings and tighter budget control and monitoring arrangements in Serbia.

In many countries, reforms were part of an integrated approach to strengthening public financial management systems and institutions. Examples of an integrated approach to
strengthening public financial management systems and institutions include Indonesia, Jamaica, Poland, and Serbia—although priorities and results differed across these countries (appendix E, section 4). Crisis response DPOs have continued to support the introduction of medium-term expenditure frameworks that should help improve the predictability of the budget and its consistency with debt sustainability. Rolling out of such frameworks has been supported in Georgia (for the public investment program), Mexico, Poland, Romania, and Serbia, but progress in this direction has varied across countries. The introduction or implementation of fiscal rules, limiting the increase in public spending or the level of the fiscal deficit, was supported in some countries, notably in Peru and Poland.

However, in some cases—including in countries with weak fiscal positions or weak budget processes—reforms to strengthen budget preparation and execution were partial or piecemeal. In Jordan, for example, public financial management support in the 2008 DPL was limited to the adoption of an enhanced calendar for budget preparation. This could be a move toward a more strategic view of budget preparation, but, at the same time, an enhanced budget calendar is an administrative reform that is not embodied in a law or regulation and can easily be bypassed. In Nigeria, the program supported some important public financial management reforms (see below), but on the non-oil revenue side the program targeted an increase of federal tax collections in proportion to non-oil GDP, without including any measures for achieving this target, although it supported some limited tax administration reforms. Some of these difficulties may be due to the difficulties of engaging in a dialogue on medium term reform in the midst of a crisis.

Although some public financial management reforms were not necessarily called for from a countercyclical or a fiscal consolidation perspective, strengthened public financial management and revenue administration could improve fiscal outcomes for any given fiscal measures in place. Promoting the results orientation of the budget, supported by the DPOs in Costa Rica, Georgia, Indonesia, Peru, and Poland, is expected to help generate fiscal space for priority expenditures by increasing attention to spending outcomes in the formulation of the budget. When these reforms come to fruition, the capacity to protect priority expenditures in future crises would be expected to improve. However, these reforms have a long gestation period, with the introduction of performance budgeting still largely work in progress in all focus countries.

Because public financial management reforms typically require follow-up actions over an extended period to attain the expected results, stand-alone crisis response operations were not an appropriate design to support these structural reform agendas. This was the case for the implementation of public expenditure evaluation systems in Mexico and for results-based budget management in Costa Rica. In Nigeria, the stand-alone Development Policy Credit supported highly relevant measures to improve cash management, upgrade public procurement regulations to the highest international standards, and improve transparency of contract awards. However, the absence of DPO programmatic engagement in these areas will make it difficult to trace the medium-term results of Bank support and keep focus on the medium-term policy agenda. Some of these reforms are being supported through a technical assistance lending operation.
By contrast, Romania is an example of a country where the Bank initiated a crisis response operation in 2009 as part of a programmatic DPL series, cognizant that the implementation of the structural fiscal reforms to bring the fiscal position on a sustainable footing would require time. It would also require analytical and technical assistance in areas such as public pay, medium-term budgeting, and pension modeling. Building the knowledge base for this assistance should be facilitated by the programmatic engagement initiated in 2009.

Although the crisis response DPOs kept a consistent focus on strengthening public financial management systems and institutions, structural fiscal reforms in some important areas remained unaddressed (appendix E, section 4), reflecting the difficulties of incorporation of such elements during the crisis. In Nigeria, for example, the 2009 Development Policy Credit could have promoted better transparency and predictability in the operation of the Excess Crude Account. This would help meet expenditure priorities over time in a context where the high dependence of the budget on volatile oil revenues imparts procyclicality on spending. In Indonesia, the fall in energy prices triggered by the crisis could have provided an opportunity to the Bank’s DPOs and Public Expenditure Support Facility to help reduce the sizeable energy subsidies, using the resulting fiscal space to scale up pro-poor social programs and investment. In Vietnam, the 2009 Poverty Reduction Support Credit and the Public Investment Reform DPL could have addressed long-standing challenges in the design and execution of the federal budget on the basis of generally accepted international principles.

**ANALYTICAL UNDERPINNINGS OF CRISIS RESPONSE OPERATIONS IN FISCAL MANAGEMENT**

Despite stretching its administrative budget to support stepped-up lending during the crisis, the Bank maintained a steady flow of AAA with a focus on public finance (table 5.3). The Bank completed 102 AAA with public finance content during the crisis (FY09–10), a somewhat higher delivery rate than the 188 pieces in the four fiscal years preceding the crisis (51 AAA deliveries per year against 47 per year pre-crisis). Patterns of AAA among countries in the three fiscal stress zones were relatively balanced before the crisis, with somewhat higher AAA deliveries in countries with low fiscal stress. However, during the crisis, deliveries of public finance–related AAA to countries in the high fiscal stress zone were stepped up, compared with those for countries in the low and moderate fiscal stress zones.

<table>
<thead>
<tr>
<th>Categorization of fiscal position</th>
<th><strong>PRE-CRISIS: FY05–08</strong></th>
<th></th>
<th><strong>DURING CRISIS: FY09–10</strong></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Number of countries</td>
<td>PER</td>
<td>CEM and DPR</td>
<td>Other public finance</td>
</tr>
<tr>
<td>Low</td>
<td>10</td>
<td>8</td>
<td>11</td>
<td>24</td>
</tr>
<tr>
<td>Moderate</td>
<td>25</td>
<td>26</td>
<td>22</td>
<td>46</td>
</tr>
<tr>
<td>High</td>
<td>13</td>
<td>13</td>
<td>4</td>
<td>34</td>
</tr>
<tr>
<td>Total</td>
<td>48</td>
<td>47</td>
<td>37</td>
<td>104</td>
</tr>
</tbody>
</table>

Source: IEG, based on World Bank data.
Note: CEM = Country Economic Memorandum; DPR = Development Policy Review; PER = Public Expenditure Review.
Although in many countries the Bank’s knowledge base in public finance was sufficient to rapidly build a program tailored to country needs, knowledge gaps existed where the Bank’s pre-crisis engagement had waned. An adequate knowledge base existed where the Bank had maintained a strong partnership before the crisis, including through the full array of Bank lending and nonlending services. Georgia is an example where the Bank was actively involved in helping carry out key reforms, with the establishment of a credible fiscal framework, a drastic reduction in corruption, and an improvement in public services. In some countries, however, core diagnostic work in public finance was relatively outdated at the outbreak of the crisis. Examples include El Salvador; Jamaica; Vietnam, where the last pre-crisis Public Expenditure Review (PER) was completed in 2004; and Peru, with a PER dating back to 2003. No recent PER was available in Pakistan. Moreover, in countries with dwindling lending volumes over time, diagnostic work lagged. Examples include Poland and Mexico, where the last pre-crisis PERs were completed in 2003 and 2004. In Brazil, the Bank’s diagnostic work in public expenditure policy was concentrated at the subnational level.

When the Bank’s knowledge base was relatively weak, the Bank was not well prepared to lay out actionable and forward-looking policy programs in fiscal management to address the crisis. The absence of crisis-related content in fiscal management in several of the DPOs that were prepared to address the impact of the crisis, despite the sizeable increase in commitment amounts, testifies to the weak analytical base of some of these operations. The analytical underpinnings of the DPOs in Mexico and Romania are examples of such knowledge gaps (appendix E, section 4). To fill existing knowledge gaps, the Bank was often able to conduct analytical work in a very short time frame, as, for example, in Serbia, where a PER was initiated in the fall of 2008 and finalized in June 2009, providing needed underpinnings to a new programmatic series of public expenditure DPOs.

The analytical base in public financial management was generally adequate. Public financial management reforms supported by crisis response DPLs were typically part of long-standing policy dialogue and were underpinned by adequate diagnostic work (PERs and Financial Accountability reviews, Country Procurement Assessment Reports, and specific technical assistance). Full diagnostic public financial management work was conducted in 8 of the 16 focus countries for this evaluation (Georgia, Ghana, Indonesia, Jamaica, Jordan, Poland, Serbia, and Ukraine), and partial analytical work was available in 6 countries (Costa Rica, El Salvador, Mexico, Nigeria, Peru, and Vietnam). Analytical work in public financial management was lacking in Romania because of a retreating overall pre-crisis engagement with the Bank. Diagnostic work on tax administration and tax policy was conducted in Uruguay, although part of it was not publicly available.

Maintaining a strong knowledge base in public finance, through a steady flow of diagnostic work, is a condition for effective support, especially in countries with fiscal positions vulnerable to a global crisis. To ensure strong analytical engagement, sufficient resources need to be directed to AAA regardless of lending volumes. To that effect, some thought might be given to making qualification to a countercyclical support facility contingent on diagnostic work in public finance conducted on a regular basis.