An Evaluation of Political-Economic Analysis in Support of the World Bank’s Governance and Anticorruption Strategy

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Raj M. Desai
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Raj M. Desai
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# TABLE OF CONTENTS

Abbreviations ........................................................................................................................................ iii

Acknowledgements ...................................................................................................................................... v

summary .................................................................................................................................................... vi

1. INTRODUCTION .................................................................................................................................... 1

2. POLITICAL-ECONOMIC ANALYSIS IN THE CONTEXT OF GOVERNANCE .................................. 3
   - Political-Economic Analysis Prior to the World Bank’s GAC Strategy .................................................. 4
   - Three Decades of Political Analysis: A Brief Historical Assessment ............................................... 4
   - Governance, Public Sector Management, and the PRSP Process ......................................................... 7
   - Toward “New Generation” Political-Economic Analysis ................................................................ 9
     - General Outlines ................................................................................................................................. 10
     - Regional Themes ................................................................................................................................. 15
     - Other Donor Activities ....................................................................................................................... 18

3. THE NEW ENVIRONMENT FOR POLITICAL-ECONOMIC ANALYSIS ........................................ 20
   - New Political-Economic Diagnostics ................................................................................................. 21
     - “Problem-Driven” Governance and Reform Diagnostics ................................................................ 21
     - The Evolution in Political-Economic Approaches ............................................................................. 23
   - New Financing, New Frameworks ........................................................................................................ 24
     - The Governance Partnership Facility ................................................................................................. 24
     - The Operational Risk Assessment Framework .................................................................................. 24
     - The Political Economy Community of Practice ................................................................................ 25

4. APPLIED POLITICAL-ECONOMIC ASSESSMENTS: A REVIEW ............................................... 26
   - A Review of Political-Economic Analytical Inputs .............................................................................. 26
     - Three Themes from Political Diagnostics .......................................................................................... 26
     - Some Operational Implications Summarized ..................................................................................... 29
   - Political-Economic Content in Economic and Sector Work ................................................................ 31
     - Five Dimensions of Political Analysis ............................................................................................... 31
     - Some Remaining Challenges ............................................................................................................. 38

5. INTEGRATING POLITICAL ECONOMY IN BANK OPERATIONS ............................................. 42
   - Political and Institutional Analysis: Evidence from a Review of Projects ....................................... 42
     - Evidence from a Staff Survey .............................................................................................................. 45

6. CONCLUSIONS ....................................................................................................................................... 49
   - Consistency, Coverage, and Relevance .............................................................................................. 49
   - Mainstreaming .................................................................................................................................... 50
   - The Uses of Political Economic Analysis .......................................................................................... 51

REFERENCES ............................................................................................................................................ 53

Figures
Figure 2.1: Governance and Political Economy in World Bank Public Documents, 1982–2010.................................................................................................................................................................................. 9
Figure 5.1: Distributions of Analytical Tools Usage for Projects .................................. 43
Figure 5.2: Distributions of Analytical Tools Usage by GAC Responsiveness .......... 44
Figure 5.3: Pre-GAC versus Post-GAC Distributions for Highly GAC-Responsive Projects.................................................................................................................................................................................. 45
Figure 5.4: Staff Self-Assessments of Political-Economy Competence by Region ...... 47

Tables

Table 2.1: Three Eras, Three Governance Perspectives .................................................. 6
Table 4.1: ESW Scoring .................................................................................................. 32
Table 5.1: Use of Political Analysis in Projects (Pre- and Post-GAC Averages)......... 43
Table 5.2: Self-Assessments of Political-Economy Competence (percent of responses) 46
Table 5.3: Program Results by Political-Economy Competence in Country Teams ...... 47
### ABBREVIATIONS

<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Full Form</th>
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<tbody>
<tr>
<td>ASEAN</td>
<td>Association of Southeast Asian Nations</td>
</tr>
<tr>
<td>CAS</td>
<td>Country Assistance Strategy</td>
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<tr>
<td>CDD</td>
<td>Community-driven development</td>
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<td>CEM</td>
<td>Country Economic Memorandum</td>
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<td>CFAA</td>
<td>Country Financial Accountability Assessment</td>
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<td>CGAC</td>
<td>Country Governance and Anticorruption</td>
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<tr>
<td>CIS</td>
<td>Commonwealth of Independent States</td>
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<td>DAC</td>
<td>Development Assistance Committee</td>
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<td>DIID</td>
<td>Department for International Development</td>
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<td>DoC</td>
<td>Drivers of change</td>
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<td>DPR</td>
<td>Development Policy Review</td>
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<tr>
<td>ECA</td>
<td>Europe and Central Asia Region</td>
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<td>EAP</td>
<td>East Asia and Pacific Region</td>
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<td>EITI</td>
<td>Extractive Industries Transparency Initiative</td>
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<tr>
<td>EU</td>
<td>European Union</td>
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<td>ESW</td>
<td>Economic and sector work</td>
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<td>GAC</td>
<td>Governance and Anticorruption</td>
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<td>GPF</td>
<td>Governance Partnership Facility</td>
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<td>GTZ</td>
<td>German Society for Technical Cooperation</td>
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<tr>
<td>IBRD</td>
<td>International Bank for Reconstruction and Development</td>
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<td>ICA</td>
<td>Investment climate assessment</td>
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<td>IDA</td>
<td>International Development Association</td>
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<td>IEG</td>
<td>Independent Evaluation Group</td>
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<tr>
<td>IFC</td>
<td>International Finance Corporation</td>
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<td>IGR</td>
<td>Institutional and Governance Review</td>
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<tr>
<td>LAC</td>
<td>Latin America and Caribbean Region</td>
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<td>LICUS</td>
<td>Low-income countries under stress</td>
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<td>MENA</td>
<td>Middle East and North Africa Region</td>
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<tr>
<td>MIGA</td>
<td>Multilateral Investment Guarantee Agency</td>
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<tr>
<td>NGO</td>
<td>Nongovernmental organization</td>
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<tr>
<td>OECD</td>
<td>Organisation for Economic Co-operation and Development</td>
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<td>ORAF</td>
<td>Operational risk assessment framework</td>
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<td>PCF</td>
<td>Post-Conflict Fund</td>
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<td>PDG</td>
<td>Problem-driven governance</td>
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<tr>
<td>PEA</td>
<td>Political-economic analysis</td>
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<td>PECoP</td>
<td>Political Economy Community of Practice</td>
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<tr>
<td>PEFA</td>
<td>Public Expenditure and Financial Accountability</td>
</tr>
<tr>
<td>PEPR</td>
<td>Political Economic of Policy Reform</td>
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<tr>
<td>PER</td>
<td>Public Expenditure Review</td>
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<tr>
<td>PIU</td>
<td>Project Implementation Unit</td>
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<tr>
<td>PREM</td>
<td>Poverty Reduction and Economic Management</td>
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<td>PRSP</td>
<td>Poverty Reduction and Strategy Paper</td>
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<td>PSIA</td>
<td>Poverty and Social Impact Assessment</td>
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<td>Abbreviation</td>
<td>Full Form</td>
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<tr>
<td>SIDA</td>
<td>Swedish International Development Agency</td>
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<td>SPF</td>
<td>State- and Peace-Building Fund</td>
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<tr>
<td>USAID</td>
<td>United States Agency for International Development</td>
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<tr>
<td>USSR</td>
<td>Union of Soviet Socialist Republics</td>
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<td>WDR</td>
<td>World Development Report</td>
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SUMMARY

Political economy analysis (PEA) has a long history in World Bank analytical work. The World Bank in recent years has repeatedly stressed the importance of PEA for governance and anticorruption (GAC) efforts, including in its 2007 GAC strategy and implementation. This paper—written as a background paper for an IEG evaluation of GAC efforts—reviews World Bank political economy analyses since 2004, and evaluates the frameworks provided to Bank teams as guidance in the context of GAC implementation. It then reviews both stand-alone political assessments and the political analysis contained in economic and sector work (ESW) as part of its examination of how systematically PEA work has addressed the problem that political incentives of borrowers sometimes conflict with good-governance imperatives. The paper also summarizes evidence from a review of projects and a staff survey undertaken as part of the broader IEG evaluation, to identify whether clients and country teams made greater use of PEA, and whether they have helped improve the “fit” of Bank operations to country context. The paper offers some lessons for mainstreaming PEA in future World Bank analytical work.
1. **INTRODUCTION**

1.1 This paper is an input into the Independent Evaluation Group’s (IEG) governance and anticorruption (GAC) evaluation. The objective of this review is to assess the content and operational relevance of political-economic analytical work that has been conducted in the context of the World Bank’s 2007 governance and anticorruption framework and strategy. The GAC Strategy—while attempting to remain within the boundaries imposed by the World Bank’s Articles of Agreement’s general limitation on interference in a member's political affairs and on basing decisions on a member's political character—underscored, among other matters, a need to understand better the interactions between political motives and economic policies that, alternatively, prompt or obstruct governance reforms. Consultations on the implementation of the GAC Strategy have emphasized the mutually reinforcing nature of poor governance and political incentives that reward such things as: corruption and graft, weak enforcement of existing laws, policy making based on special interests rather than public welfare, the private diversion of public assets, and so on. Increased financing, moreover, has been made available to diagnose the underlying political constraints that client countries face, to identify appropriate entry points, and to develop innovative instruments that can ameliorate these constraints, thereby mitigating the governance risks that World Bank-supported programs and projects face. Finally, the Operational Risk Assessment Framework (ORAF) in place since July 2010 incorporates political-economic risks at multiple levels in its template.

1.2 Political analysis has a long history in World Bank economic work in general. In recent decades, political analysis has become the norm in economic and sector work (ESW) and in risk assessments for project documentation, mostly involving institutional and or governance assessments. In recent years, analyses have more explicitly considered the gap between the World Bank’s goal of supporting policies and programs that reduce poverty and the political reality that the governments at the center of the Bank’s borrower relationships often have diverging objectives. More likely, some individuals within governments may support these aims, and others may oppose them. Individuals or groups within government and society have their own objectives—status, power, incumbency, wealth—for which they may use governmental machinery to achieve, and reward their supporters and penalize their opponents accordingly. To the extent that deviations from World Bank-supported projects are likely, project risks are closely linked to these political incentives. The objective of political-economic analysis (PEA) is to highlight the sources of these incentives, assess their impact on programmatic outcomes of interest, and devise mechanisms to mitigate these factors.

1.3 This suggests that standard problems of governance—corrupt public management and financing, administrative bribery, state capture, expropriation or theft of public assets, and so on—cannot be fully addressed by efforts to seek “reform champions,” build institutional capacity, empower key constituencies, or other such efforts that do not address the fundamental problem that the political incentives of client governments may be misaligned with those of the World Bank in particular situations.
1.4 This review, therefore, focuses on the specific forms of PEA that examine the determinants and effects of these underlying incentives, namely:

(i) The opportunities, incentives, and behaviors of relevant public officials responsible for the design, implementation, and enforcement of economic policies;

(ii) The ability of individuals or groups to mobilize collectively in support of or opposition to specific economic policies or policy reforms; and

(iii) The effect of the interactions between these two groups on the risks, obstacles, and constraints to the successful completion of World Bank-supported policies, projects, and/or reforms.

1.5 This review seeks to evaluate two related issues with respect to PEA: (i) whether PEA has changed how the World Bank thinks about development problems and solutions, and; (ii) whether it has changed the way in which the World Bank operates in its client countries.

1.6 First, in what way has political-economic analysis changed how the World Bank conceptualizes the central problems of poverty and economic development? In particular, what is the relevance of the current political-economic guidance? Do the features of existing PEA reflect current thinking in the political economy of development? Are they aimed at identifying the key impediments countries face in developing and implementing effective GAC programs, policies, and/or projects? To what extent does this guidance differ from that offered prior to the implementation of the GAC Strategy?

1.7 Second, how has political-economic analysis influenced World Bank operations in borrower countries? How has PEA guidance been applied to country operations? Have the basic principles of the PEA guidance been mainstreamed into World Bank ESW and into other analytical work? To what extent have innovative solutions been proposed that address these underlying constraints identified by PEA in countries? Given the Bank’s particular mandate, what opportunities exist to form partnerships with other international organizations and players to devise innovative solutions? Finally, what are the implications for Bank-client relationships? In what ways can the World Bank utilize the information and analyses contained in PEA to engage with clients in a constructive manner?

1.8 This review used a variety of evaluative techniques as the basis for its findings and recommendations. A list of key evaluative material is provided in the references. This review also considered evaluation results from outside the World Bank, discussions with staff, and analysis of data from inside and outside the institution.
2. POLITICAL-ECONOMIC ANALYSIS IN THE CONTEXT OF GOVERNANCE

2.1 Despite the prohibition on political activity in Article IV, Section 10 of the Articles of Agreement of the International Bank for Reconstruction and Development (IBRD) (and similar articles for the International Development Association [IDA], International Finance Corporation [IFC], and the Multilateral Investment Guarantee Agency [MIGA]), PEA has a long history within the World Bank. It has been shaped by both intellectual trends in political science and development economics, as well as by substantive challenges facing borrowers. Significant PEA was contained in the World Bank’s first report on a developing country. In May 1949, the economist Lauchlin Currie was asked by IBRD Vice President Robert L. Garner to lead the World Bank’s first general survey mission to a developing country, Colombia. Among the recommendations in The Basis of a Development Program for Colombia (the Currie Report) are the following (IBRD 1950):

(i) The establishment of an independent Public Railways Corporation to administer the Colombian National Railways, in order to limit interference by ministries;

(ii) The establishment of “autonomous, semi-judicial” commissions to regulate utility and transportation rates, in order to eliminate rate-setting based on regional favoritism;

(iii) The purchase of a freighter by the state-owned shipping company in order to maintain “adequate coastwise shipping,” which the report noted was “justified for social and political reasons” despite its expected unprofitability;

(iv) An increase in salaries of government employees in order to improve the quality of the civil service; and

(v) The allocation of highway funds according to traffic surveys, rather than administrative discretion, in order to reduce the influence of “economic pressure groups and vested interests which are likely to carry undue weight.”

2.2 The PEA behind these (and other) recommendations in the Currie Report was largely informal, based on several months of meetings and discussions with government officials, political party members, and the private sector. The Currie Report, however, examined political and institutional constraints to development in considerable depth—including the lack of autonomous administrative units, the effects of factionalism on

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1 IBRD Articles of Agreement, Article IV, Section 10: “The Bank and its officers shall not interfere in the political affairs of any member; nor shall they be influenced in their decisions by the political character of the member or members concerned. Only economic considerations shall be relevant to their decisions, and these considerations shall be weighed impartially in order to achieve the purposes stated in Article I.” See also IDA Articles of Agreement, Article V, Section 6; IFC Articles of Agreement, Article III, Section 9; MIGA Convention, Chapter V, Article 34.
regulation, the incentives of stakeholders, political leaders, and bureaucrats, and the absence of technocratic knowledge in economic policy making—and deliberately incorporated these concerns into its recommendations for Colombian economic policy and institutional reforms. More importantly, the Currie Report served as something of a model for PEA to inform program and project design in subsequent surveys of developing country economies, coming at a time when the IBRD’s commitments to post-war European reconstruction were coming to an end (Alacevich 2005).

Political-Economic Analysis Prior to the World Bank’s GAC Strategy

2.3 Generally speaking, it is possible to divide World Bank PEA over the past three decades into three overlapping eras. The “structural adjustment” period, which begins with the Debt Crisis in the early 1980s and lasts until the early-to-mid 1990s; the “transition” period beginning with the reform of formerly centrally-planned economies primarily in the Europe and Central Asia (ECA) Region, but also in Mongolia, Vietnam, and (continuing) in China, lasting until the mid 2000s; and the “Monterrey” period beginning with the run-up to the 2002 United Nations International Conference on Financing for Development held in Monterrey, Mexico. It is in this last period that the World Bank’s present GAC Strategy was elaborated.

Three Decades of Political Analysis: A Brief Historical Assessment

2.4 The Structural-Adjustment Era. During the structural-adjustment period, pressures for monetary and fiscal austerity among the World Bank’s borrower countries generated PEA consistent with this imperative. One common external criticism of World Bank analytical work in general from this period is that it largely ignored questions of governance and institutions (de Haan and Everest-Phillips 2007; and Bayliss and Fine 1998). A large body of World Bank PEA focused primarily on the political constraints to scaling back the state’s developmental and redistributive commitments. World Development Reports (WDRs) from the late 1980s—on trade liberalization (World Bank 1987), on public finance (World Bank 1988), and on financial liberalization (World Bank 1989)—each examine the capacity of organized interests to obstruct necessary reforms. Reports and policy papers on public enterprise reform (Shirley and Nellis 1991) and privatization (Kikeri, Nellis, and Shirley 1992) similarly emphasize the political feasibility of reforms. Others examine the role of international constraints, domestic distributive conflicts, electoral pressures, and state capacity to implement and sustain policy adjustment.

2.5 The Transition Era. The end of state-socialism in Eastern Europe and in the Commonwealth of Independent States (CIS) (but also, to a certain extent in Mongolia, Vietnam, and the continuation of market-oriented reforms in China) informed World Bank PEA in a number of ways.

2.6 First, World Bank PEA explicitly examined the effects of political institutions—legislatures, courts, sub-national governments, bureaucracies—on development outcomes. The WDR on the post-socialist transition (World Bank 1996), for example,
examined the influence of the “level of trust” in the state and of government credibility on reform progress. Second, a sharper focus on the micro-institutional foundations of economic performance—banks and corporations, as well as capital markets, regulatory regimes, accounting standards, contract enforcement and property rights—prompted analyses of the political constraints, potential winners and losers, attached to the establishment or reform of institutions (Pleskovic 1994; Gray 1996; Claessens 1996; Brunetti, Kisunko, and Weder 1997; Campos 2000). Although much of this agenda was facilitated by the post-socialist transition, similar emphases appeared in analytical work for all regions. Third, “governance” emerged as a core component of development assistance, and the World Bank became directly involved in fighting corruption (rather than simply assisting countries in adopting reforms that would limit corruption). In the *Assessing Aid* report, in addition to “sound policies,” secure private property rights, the absence of corruption, and respect for the rule of law are identified as key determinants of aid effectiveness (World Bank 1998). A voluminous amount of explicitly political diagnoses of corruption and of related concerns such as political financing, “capture” by elites, and the effects of corruption on political stability characterize this period.

### 2.7 The Monterrey Era

Pressures for debt relief, combined with criticisms of aid effectiveness produced several efforts among aid donors and recipients to address problems of traditional aid practices. These efforts emphasized the need for effective political management of the economy and recipient-government “ownership.” Commitments for increased aid, moreover, were being made in the face of doubts about the “absorptive capacity” for aid among the poorest aid recipients. The partnership enshrined in the 2002 Monterrey agreement established a formal basis for donors to address the politics of development:

> Good governance is essential for sustainable development. Sound economic policies, solid democratic institutions responsive to the needs of the people and improved infrastructure are the basis for sustained economic growth, poverty eradication and employment creation. Freedom, peace and security, domestic stability, respect for human rights, including the right to development, and the rule of law, gender equality, market-oriented policies, and an overall commitment to just and democratic societies are also essential and mutually reinforcing (United Nations 2003, p. 7).

### 2.8 Consequently

Consequently, the period since the Monterrey meetings have seen the World Bank, along with other major donors, adopt various approaches to identifying and addressing the political nature of the governance constraints to aid effectiveness, and incorporate analyses of domestic political dynamics in operations. Poverty Reduction Strategy Papers (PRSPs), as well as budget-support and sector-wide assistance all incorporated PEA of constituencies, institutional constraints, and political commitment as part of their implementation. The PRSP approach has been based partly on the principle of country ownership (and donor partnership) through broad, nationwide participation and, given the general lack of political agency (access, representation) among the poor, a greater focus on the inclusion of the poor in policy-making processes. Formally, the
PRSP Sourcebook argues that “strong country demand at all levels” is a precondition for developing national monitoring and evaluation systems, and looks for the creation of such demand in a participatory PRSP design process (Klugman 2002). Meanwhile, sector-wide and budget-support programs, arising primarily out of perceived failures of commitments to improved governance and conditionality (in addition to complaints about a lack of donor coordination) focused on supporting changes in public expenditure frameworks and budget management, as well as in creating a more “pro-poor” policy environment.

2.9 More notably, during this period, the concept of “governance” expanded from one relatively narrowly focused on “corruption” to cover a wider range of issues, including the institutions of a country’s polity (its political executive, its legislatures, its courts) in addition to its public sector and civil service. In addition, this period experienced a shift from a growth-diagnostics approach in analytical work which identified and sought to alleviate actual “constraints” to growth toward an approach which primarily aimed at identifying the political obstacles that blocked policies needed to alleviate growth constraints.

Table 2.1: Three Eras, Three Governance Perspectives

<table>
<thead>
<tr>
<th></th>
<th>Structural Adjustment Era</th>
<th>Transition Era</th>
<th>Post-Monterrey Era</th>
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</thead>
<tbody>
<tr>
<td>Orienting event(s) affecting client countries</td>
<td>Debt crisis, “lost decade” of economic stagnation, economic reforms in China</td>
<td>Break-up of the Union of Soviet Socialist Republics (USSR), post-socialist transition, global financial turmoil (Mexico, East Asia, Russia, Turkey, Argentina, Brazil)</td>
<td>Debt relief and United Nations Millennium Declaration</td>
</tr>
<tr>
<td>Economic policy currents</td>
<td>Orthodox (monetarist) versus heterodox stabilization programs, capital and current account liberalization</td>
<td>Privatization, capital market development, property rights enforcement, post-crisis financial sector reform</td>
<td>“Pro-poor” growth, development partnerships, community-based development</td>
</tr>
<tr>
<td>Political economy currents</td>
<td>State building, new industrialism, redistributive politics</td>
<td>Democratization and growth, political economy of institutions, social capital</td>
<td>Origins of political-economic institutions, aid effectiveness, state fragility</td>
</tr>
<tr>
<td>Governance focus</td>
<td>Governance as public sector management</td>
<td>Governance as barrier to economic development (administrative corruption, “state capture”)</td>
<td>Governance as political “pathology” (patronage, clientelism)</td>
</tr>
<tr>
<td>Governance reforms</td>
<td>Civil service, public financial systems, public enterprise</td>
<td>Regulatory reforms, checks and balances, political finance reforms</td>
<td>“Good-enough” governance reforms</td>
</tr>
</tbody>
</table>

*Source:* Author’s assessments.

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2 For an early assessment of the PRSP process, see Booth and Lucas (2001).
Governance, Public Sector Management, and the PRSP Process

2.10 Whereas during the structural-adjustment era, “governance” referred broadly to the processes of public sector management and financing, the World Bank’s emphasis on “good governance” beginning in the mid-1990s shifted to a greater focus on the economic cost of poor governance, and in particular, toward the need for effective state institutions in which policy making would be “predictable, open, and enlightened” (World Bank 1994). In addition to a meritocratic, professional civil service, an accountable executive, and transparency and inclusiveness in relationships between government and civil society were the basic components of this approach, which was justified on the basis that “a capable and accountable state creates opportunities for poor people, provides better services, and improves development outcomes” (World Bank 2007c). The recognition that the World Bank, in previous efforts to improve public management systems, had relied on overly technocratic approaches, inflexible lending instruments, and had tried to build capacity without improving underlying governance structures had, in part, motivated changes to the ways in which the Bank engaged in institutional reform in client countries (Girishankar 2001). At the end of the 1990s, a consensus had emerged among the international development community that stressed more effective measurement and benchmarking of “institutional” performance, the use of more flexible financing instruments, and the proper sequencing of reform efforts.

2.11 The 2000 Governance Strategy, for example, acknowledged that the World Bank had, in previous efforts, limited its concerns to the internal rules, mechanisms, and restraints of the governmental bodies in borrowing countries—for example, internal accounting and auditing systems, independence of the judiciary and the central bank, civil service and budgeting rules, and rules governing ombudsmen and other internal watchdog bodies, and so on (World Bank 2000a). In contrast to earlier public-sector management approaches, the new governance strategy emphasized that reforming the public sector and improving governance would be, above all, politically-driven phenomena that would succeed or fail based on the ability of individual reformers within governments to mobilize supporters, restrain or co-opt opponents, and establish incentives for bureaucrats and other public officials to follow through on the reforms. The 2000 Strategy, in addition, urged greater selectivity in supporting public sector reforms, that is, to recognize where such reforms would succeed, and where they would fail (where opposing forces might be too powerful, where stroke-of-the-pen reforms might not be implemented). The Strategy also advocated allocating resources accordingly, considering “second-best” options (where improvements that would be politically feasible might not be technically the most desirable), and devising ways in which the demand for good governance might be strengthened (World Bank 2000a, pp. 27–28; World Bank 2000b, pp. 73–76).

2.12 Finally, the Governance Strategy also advocated that explicitly “political” analyses be conducted as a routine part of the World Bank’s operations, focusing on matters such as political support for reform, analyses of the political power of
stakeholders, whether “windows” of opportunity were in place, and so on. Whereas in previous analytical work that emphasized the underpinnings of governance reform tended to focus on the capacity of organizations to absorb skills and finances, and on internal incentive frameworks within government—the formal rules, codes, procedures, as well as the norms, customs, and informal rules in place—the 2000 Strategy noted that governance reforms often required a transfer of power to reform-oriented leaders to “unlock” dysfunctional equilibria, and that these and other potential catalysts should be investigated (World Bank 2000a, pp. 34–36). The medium-term approach was to solidify the political-economic and institutional focus of both the Institutional and Governance Reviews (IGRs) and the Public Expenditure Reviews (PERs), with the latter being concerned more centrally with public expenditure issues and the former with other core functions of government and their connections with the quality of public service delivery. Finally, the 2000 Strategy also called for more flexible lending instruments to support institutional reforms.

2.13 The need for local “ownership” of governance reforms—mentioned in the 2000 Governance Strategy as well as elsewhere—was at the heart of the PRSP process. The PRSP era moved World Bank–supported governance reforms and PEA toward a more country-driven focus through, for example, country-led governance plans in PRSPs, the relative shift toward budget support, the enhanced scale of community-driven development (CDD) operations, and greater alignment with and support for country programming systems. The PRSP Sourcebook recommended the active involvement of all stakeholders—donors, civil society, and the state—as well as a better understanding of the interactions between them (based on interests, alliances, relationships of power or authority, conflicts, and so on). The PRSP Sourcebook defines governance more broadly:

[T]he exercise of power through a country’s economic, social, and political institutions in which institutions represent the organizational rules and routines, formal laws, and informal norms that together shape the incentives of public policymakers, overseers, and providers of public services… Three key dimensions are (a) the process by which governments are selected, held accountable, monitored, and replaced; (b) the capacity of governments to manage resources efficiently and to formulate, implement, and enforce sound policies and regulations; and (c) respect for institutions that govern economic and social interactions (Girishankar et al. 2002, p. 271).

2.14 One of the main innovations of the PRSP Initiative was in the linking of civil society to policy making and monitoring as a way of increasing the political “weight” (access, representation) of poor and marginalized groups in decision making in order to strengthen the legitimacy of economic policy reforms. Additionally, a principal rationale is that incorporating the poor in a national dialogue improves the quality of policy making, governance, and service delivery, and can serve as a check on the excesses of elites, as long as the participatory machinery of government functions properly (Girishankar et al. 2002, pp. 276–277).
Toward “New Generation” Political-Economic Analysis

2.15 In the past few years, the international development community had reached a broad agreement that (i) governance mattered for economic prosperity; (ii) the underlying problems in achieving good governance were more political than technocratic, and (iii) PEA plays a crucial role in enhancing the effectiveness of development. This section first examines some general points of guidance that characterize these forms of PEA—most of which have revised earlier ideas and analytical tools. Some central themes that distinguish the new political-economic guidance from previous analytical work will also be highlighted.

Figure 2.1: Governance and Political Economy in World Bank Public Documents, 1982–2010

Source: Author’s calculations based on World Bank documents and projects database, queried as of October 26, 2010. Note: Line graphs are generated from a simple exact-phrase keyword search for “governance” and “political economy” in all document types in the World Bank’s database annually from January 1, 1982, to October 25, 2010. The histogram shows the total number of documents generated by leaving all fields blank (2010 total is an annualized estimate).

2.16 An imperfect but useful proxy of the salience of political-economic and governance concerns in World Bank analytical and operational work is depicted in figure
2.1, which shows the fraction of total (publicly disclosed) documents available through the World Bank’s online Documents and Projects database that are found using “governance” or “political economy” as keywords. As the graph in figure 2.1 shows, this measure of governance and political-economy “salience” increases dramatically between 1986 and 2000 and then declines. Indeed, World Bank President James D. Wolfensohn’s “cancer of corruption” speech was delivered during the middle of this trend. Although the number of public documents available increases from 800 in 1982 to approximately 7,500 since 2007, the fraction of these documents with keyword references to “governance” peaks between 2000 and 2003 when over one-third of these documents are governance related. By contrast, the GAC Strategy appears to have come at a time when the salience of governance and political economy is on the decline in World Bank public documents. At last count, the fraction of governance-relevant documents has fallen to less than one-fifth—levels last seen during the late 1980s. Similar patterns are seen with respect to “political economy” references, which rise from about 5 percent to 16 percent in 2000, falling thereafter to 7 percent.

General Outlines

2.17 The intellectual watershed in terms of political-economic work generally follows figure 2.1, in that many of the prevailing frameworks for PEA in the post-GAC era were developed during the early to mid-2000s. Several features of this body of work included a clearer focus on the problems of political incentives, distribution of political power, credibility, institutional fragility, as well as the recognition of significant regional and sub-regional variation in the political-economic landscape.

2.18 Political incentives. Above all, the recognition that there are powerful incentives for governments to deviate from behavior expected from a welfare-maximizing social planner is at the core of the newer guidance. Governments, and in particular, the elected or unelected officials who lead the various branches of governments, wish to be re-elected or otherwise remain in power. In other words, the explicitly political incentives of World Bank borrowers are potentially misaligned with the objectives of growth, equity, or poverty reduction—a situation often characterized as a “lack of political will.” Politically-driven policies, as is well-known, can involve transfers to groups or individuals whose characteristics may have little to do with their level of poverty or other economic characteristics (Grindle 1997; Tendler 1997; Robinson 2003; Diaz-Cayeros and Magaloni 2003; Keefer and Khemani 2005; and Levi 2006). Moreover, the actual mechanisms used to redistribute are often inefficient but politically valuable, designed to be narrowly (and often regressively) targeted to key constituencies rather than according to need (Acemoglu and Robinson 2001; Bueno de Mesquita et al. 2003). In the past, several WDRs recognized this explicitly. A central argument in the 2004 WDR, for example, is that the poor lack access to high-quality services not because of the capacity constraints of service providers, but because political incentives are in place that do not reward pro-poor delivery (World Bank 2003c). The 2005 WDR demonstrates that politically-influential firms, which tend to be subsidized, protected from competition, and granted a host of other privileges through economic policy tend to be less dynamic and innovative than non-influential firms (World Bank 2004). The 2006 WDR makes a
similar point suggesting that the incentives of elites often involve maintaining stark economic inequities (World Bank 2005a).

2.19 The key challenge for operational work, with respect to political incentives, is how to overcome the realities that many of the clients with whom the World Bank works are driven by political survival. The 1997 WDR appeared to rely on enlightened leadership: “reform-oriented political leaders and elites,” or “farsighted political leaders” (World Bank 1997, p. 14). Analyses of policy reforms also identify “policy champions,” or “agents of change” who can play crucial roles. This approach has been criticized for excessive reliance on individual personalities, while ignoring the more necessary role of institutional design that could balance the aspirations of political leaders with the aims of achieving good policy outcomes (Shepsle 1999). Subsequent guidance has emphasized the enfranchisement and mobilization of the poor (World Bank 2003b; Narayan 2009) as a way of pushing politician’s incentives in the “right” direction—that is, in favor of pro-poor policy making. Putting aside whether such mobilization is possible, there is little evidence or consensus that greater participation by the poor actually enhances the quality of governance or policy outcomes (Mansuri and Rao 2001). Other findings have emphasized the importance of “reform windows of opportunity,” or occasions during which opportunities arise to re-balance the incentives of politicians such that welfare-maximizing policies are more likely to be adopted (World Bank 2008e, pp. 13–14).

2.20 Findings for policy or program design highlight the importance of understanding the incentives that drive political incumbents, and in thinking creatively of ways to influence agenda-setting in borrowing countries. Reforms can be triggered in a number of ways—changes in government, crises, following the conclusion of new international agreements, and so on. The timing of these changes can affect the various “entry points” for programs, and requires that those pushing governments to reform be aware of, and time programs to coincide with, these potential catalysts. An analysis of investment climate reforms notes that increase in global competition and technological change, for example, created new constituencies in export-oriented industries, and shifted the incentives of incumbents once opposed to trade (Kikeri, Kenyon, and Palmade 2006, p. 23).

2.21 Political incentives that push countries to diverge from World Bank goals can also stem from the control of rent streams. To the extent that reforms—in policies, or at the sectoral level—threaten access to rents that might otherwise be shared with key constituencies, the political incentives of government leaders may oppose these efforts. A perspective from institutional economics considers rent-seeking to be “directly unproductive” (since the existence of rents not only leads to deadweight losses, but can divert productive resources towards rent-seeking activities) and thus something to be minimized, above all (Krueger 1974; Shleifer and Vishny 1994). A separate, political perspective suggests the existence of some rents can be a “second-best” solution, for example, under conditions of political instability (Haber 2006; Khan and Jomo 2000), or where private sector institutions are weak (Kang 2002).
2.22 Stakeholders and the distribution of political power. A long tradition in comparative political economy places distributional conflicts at the center of analyses of the scope and depth of governance reform. Elite “capture,” for example, was widely cited as one of the main threats to governance and anti-corruption efforts. In response, policy actors and analysts have sought to overcome the problems of capture through two main routes. The first has been to improve project design so as to insulate projects from elite domination—for example, through the use of independent agencies and implementing units outlined above. The second has been to focus on “empowerment” of marginalized groups as a means to develop their capacities vis-à-vis the elite.

2.23 It should be noted that political incentives of public officials can also be shaped by the degree of access to and representation in decision-making that individuals or interest groups have, the resources they hold, and their level of mobilization. Although analyses of the distribution of political power across key players—“stakeholder analysis”—has long been a cornerstone of World Bank social analysis, particularly in “social assessments” and in projects that involve a participatory framework, the underlying rationale has been to grant the poor more political power” (McPhail and Jacobs 1995; World Bank 1995). More recent assessments have questioned the efficacy of mobilizing the poor, particularly in communities where the poor are typically mobilized by vote buying, patronage, or other methods that may undermine the public spiritedness of democratic participation. Others have suggested that increasing the political power of the poor does not guarantee improved governance (and can in fact worsen outcomes).

2.24 One of the explanations of bad policies, including bad governance, is that those who benefit from improvements face steep collective action costs relative to those who favor the status quo. Consequently, stakeholder analysis is now a key component of PEA in general, and with respect to governance issues in particular. Moreover, the use of stakeholder analysis has expanded from one focused primarily on key individuals in government to one that has embraced the concept of the “interest group” and its organizational capacity (Bianchi and Kossoudji 2001).

2.25 Stakeholder analysis goes further by aiming to predict how World Bank-financed programs will perform in the face of potentially opposing interest groups:

Stakeholder analysis assesses: (i) the extent to which reform may provoke political or social action; (ii) the level of ownership among different groups; (iii) differences in perception of the reform among different ethnic, religious or linguistic groups. Stakeholder analysis can be expanded into fuller political economy analysis that identifies affected groups and looks at: (i) their position vis-à-vis policy; (ii) their influence on government; (iii) the likelihood of their participation in coalitions to support change; (iv) strategies for overcoming opposition such as compensating losers or delaying implementation (World Bank 2003b, p. 49).
2.26 What differentiates more recent stakeholder assessments from some previous ones is that recent analyses implicitly aim to “co-opt” or compensate reform opponents. This is developed further in the Sourcebook for Poverty and Social Impact Analysis (PSIA), which considers “options to limit negative impacts through the design of appropriate compensation mechanisms” (World Bank 2007d, p. 16). It is also addressed specifically in the “manual” for reforming the investment climate, which urges reformers to consider both direct compensation (cash transfers, new benefits) or indirect compensation (additional reform measures, expanded social protection) to appease labor unions, bureaucrats, and other potential opponents (Kikeri, Kenyon, and Palmade 2006, p. 40). Regarding governance reforms and anti-corruption measures, stakeholder analysis can indicate who the beneficiaries will be, and thus highlight the need to incorporate and “empower” these constituencies in order to increase local demands for better governance (World Bank 2007a).

2.27 Government credibility. In understanding the effects of governance constraints on growth and poverty, a central insight from three decades of research on the political economy of growth is that economies prosper when transactions can take place at low cost (Bethell 1986; North 1990; North 1993; North and Weingast 1989; Keefer and Knack 1997; Clague 1999; and Henisz 2000). But in this there is a fundamental dilemma: a state that is strong enough to delineate and secure property rights and enforce contract laws (and thereby lower transaction costs) can also confiscate the assets of its citizens (Weingast 1995). Markets, therefore, require mechanisms that limit the ability of the state to arbitrarily expropriate wealth. The 1997 WDR had already noted that private arrangements cannot always supplement state enforcement, and that states that cannot resolve an inherent time-consistency problem will drive out investment and entrepreneurship (World Bank 1997, pp. 33–34). The 2002 and 2005 WDRs, similarly, identified the “unpredictability” and “uncertainty” of government actions (in addition to static, inefficient policies) as detriments to investment (World Bank 2001, 2004). Guidance on overcoming credibility problems and in building consistency on government policies typically involved the fashioning of effective “commitment” mechanisms in countries.

2.28 For several years, in the World Bank’s lending programs, this involved delegating specific responsibilities (and discretion) to autonomous agencies that would be responsible for specific actions (for example, regulating monopolies, contracting with private investors, privatizing state industries, issuing business licenses or permits, managing public lands, or managing assets in a particular sector such as electricity, telecoms, transport, and so on, and, in many cases, extending to managing relationships with donors). Project implementation units (PIUs) may have once been viewed as a commitment device, although World Bank-financed operations now focus on a greater use of, and support for, country systems and institutions.3

3 PIUs were developed as organizational structures for project management that would be “responsible and accountable for implementation of the project and for timely progress and expenditure reporting that adheres to Bank policies and guidelines.” Evaluations of PIUs, however, revealed that they were more likely to undermine long-term institutional development in countries’ line ministries, sustainability, and ownership. In addition, they have often created tensions with sector ministries. Although PIUs may have
2.29 These concerns are repeated in GAC and related documents. The 2007 Implementation Plan identifies the need to strengthen “core” public-management systems (financial and budgeting management, procurement, public administration) combined with independent oversight institutions (World Bank 2007b). Among the indicators used in the Public Expenditure and Financial Accountability (PEFA) multi-donor partnership are those that emphasize budgetary credibility, “predictability,” and “control.” (World Bank 2007c). Similarly, the Extractive Industries Transparency Initiative (EITI), recognizing the need for improved management of revenues from natural resources (as well as the economic rents that may be diverted), emphasizes budgetary transparency as well as the need for “impartial and independent” administration of revenue streams (DfID 2005, p. 23).

2.30 There is also broader recognition of the potential role of constitutional checks and balances in countries, and other accountability mechanisms, as a mechanism for fostering credible commitments:

[O]ver the longer run, well-functioning checks-and-balances institutions are key to sustainability. They help keep the executive arm of government focused on the public purpose. They are vital for fighting corruption, for ensuring that state actors at all levels use public resources efficiently and effectively, and for helping to ensure that citizens perceive state institutions to be legitimate (Levy 2007, p. 57).

2.31 It is accepted that, under most circumstances, the various institutions that involve oversight, external review, separation of powers, and reduced overall executive discretion can stabilize policy making and form the basis for effective commitment mechanisms. A survey of accountability institutions in GAC is part of the present IEG evaluation, and thus an assessment of the relationship between these institutions and GAC strategies is beyond the immediate scope of this background paper. Accountability institutions—courts, parliaments, sub-national governments, and civil society at the country level, direct oversight and monitoring at the sector and project-level—are considered key components of the overall political-economic challenge of improving governance. Finally, the second GAC progress report notes that bolstering the “demand” for governance can be accomplished by enhancing “public scrutiny” of governmental actions and behaviors to achieve better GAC outcomes (World Bank 2009g, p. 60).

2.32 Institutional capacity and fragility. A fourth area of focus for PEA is state capacity, with some special attention to the problems of conflict-affected and post-conflict states. One of the central messages of the 1997 WDR was the key role of the state—the formal-legal entity which administered a territory through the compliance (forced or voluntary) of its citizens—in building prosperous economies. In highlighting the place of political development in market formation, the 1997 WDR (and subsequent

contributed to government credibility vis-à-vis investors, their adverse effects on capacity development have led to Bank-financed operations toward organizational structures that rely on greater use of and support for country systems and institutions (see World Bank 2005d).
WDRs) made explicit the problem of state capacity and weak states in development. Moreover, it acknowledged that much of the World Bank’s work in poor nations (for example, civil service reform, public sector capacity building, social protection, and so on) was closely tied to state building.

2.33 One of the posited effects of elite capture is that those in possession of agenda-setting authority will design institutional structures that essentially guarantee a stream of rents to these elites. Thus, it can be the case that state institutions with low capacity are deliberately designed as such, and are not a result of limited resources or human expertise. The 2006 WDR, for example, argues that capture has a direct effect on the quality of governance, and that institutional quality suffers when political power is concentrated in the hands of a narrow elite (World Bank 2005a, p. 107). Public agencies and governing bodies that rely on the discretion of those who run them, of course, can be used to shelter supporters, harm opponents, transfer benefits to favored groups, and overall, can be far more valuable politically than equivalent rule-bound institutions.

2.34 The World Bank’s GAC Strategy has recognized that state weakness is at the heart of the matter, and that the purpose of GAC work should be “to help develop capable and accountable states and institutions that can devise and implement sound policies, provide public services, set the rules governing markets, and combat corruption…” (World Bank 2007c, p. 2).

2.35 In extreme cases, conflicts, protracted factionalism, and polarization can weaken states to the point that they fail to deliver basic public goods, and in particular, fail to maintain order across a given territory. In recognition of the close relationship between “conflict traps” and “poverty traps,” the World Bank has assisted fragile and conflict-affected countries since 1997 through the Post-Conflict Fund (PCF), and since 2004 through the Low-Income Countries under Stress (LICUS) Trust Fund. In 2007, both the PCF and LICUS-TF were replaced by the State- and Peace-Building Fund (SPF). By placing the interlinked processes of “state-building” and “peace-building” at the core of the new trust fund, the aim of the SPF was to align the World Bank’s work in conflict-affected states with that of other inter-governmental actors such as the United Nations Peace-Building Commission, the OECD-DAC, and other regional and multilateral development banks. Among the over-arching goals of the SPF is to “strengthen, build, or rebuild institutions of governance that are capable of providing the population with transparent and accountable management of public finances and state assets, investment in human capital and social development, the rule of law, basic services and infrastructure . . .”, recognizing that, by strengthening and building institutional capacity to discharge those functions, state-building contributes to increasing the state’s effectiveness (World Bank 2008b, p. 7; World Bank 2008a).

Regional Themes

2.36 This section highlights some of the region-specific PEA guidance as it relates to issues of governance. It should be noted that the components of PEA mentioned in the preceding section are intended to be cross-regionally valid. Therefore, identifying
region-specific topics risks ignoring the wealth of approaches and agendas across widely-differing countries within each region. The purpose here, however, is to identify those particular PEA issues that are related to the regional GAC and governance-reform agendas.

2.37 **Latin America and the Caribbean.** Persistent inequality remains among the overarching concerns in Latin America and the Caribbean (LAC), with this region being characterized as one with the greatest economic inequality in the world. The political effects of inequality and the implications for GAC strategies in the region have been explicitly considered in a number of analyses. One report notes that the “incompleteness of inclusion of subordinate groups in overall social and political arrangements in society” have produced a number of adverse effects, including minimal protection for vulnerable groups, regressive expenditure patterns, political manipulation of traditional antipoverty programs, and heightened macro-economic volatility due to distributional conflicts and the prevalence of cronyism (De Ferranti et al. 2004). If patterns of asset and income inequality have been replicated in inequality in access, voice, representation, then one solution involved helping enfranchise marginalized groups, including the poor and the indigenous communities in LAC. Indeed, there is evidence that this approach has taken hold in governance-reform strategies in the region—with the emphasis on “inclusive governance” in the regional framework for engaging with civil society being an example. Perhaps the signature achievement in poverty reduction in the region, the conditional cash transfer, has not only targeted cash to vulnerable populations, but has also served as a potential platform to increase the engagement of these populations in public affairs (de la Brière and Rawlings 2006). Governance surveys recognize that, in most countries in the region, citizens express growing disillusionment with their governments, complaining about a lack of responsiveness and accountability on the part of public officials. This is depicted in stark terms:

The relationship between citizens and their governments is characterized by a lack of legitimacy or a governance crisis. The effectiveness of both vertical and horizontal accountability mechanisms has proved limited. In this context, social accountability mechanisms allow citizens to access, use and analyze public information, voice their needs and opinions, and demand accountability beyond elections (World Bank 2005b, p. 17).

2.38 **East Asia and Pacific.** Prior to the elaboration of the current GAC Strategy, PEA of governance constraints and challenges in East Asia and Pacific (EAP) economies was influenced partly by the aftermath of the Asian Crisis, as well as by the specific problems of poverty and reform in large, diverse countries such as China, Indonesia, and the like. Reports have noted that government effectiveness improved through core public management reforms, including a higher profile given to anti-corruption efforts, along with support from the Association of Southeast Asian Nations (ASEAN). However, recent PEA for the region notes that there remain serious shortcomings—particularly in terms of the continuing disenfranchise of vulnerable groups, and limited accountability in some countries which constrains progress in governance reform. There
is also some suggestion that EAP governments are facing political pressures to reverse recent progress in economic policy reforms.

2.39 **Europe and Central Asia.** By the end of the “first decade” of the post-socialist transition, corruption had come to be recognized as a central challenge to progress in Europe and Central Asia (ECA). Corruption and governance were at the forefront in the discussions surrounding European Union (EU) enlargement, and have figured prominently in political campaigns in Eastern and Central Europe. Further, they have been a key concern of citizens, businesses, and international organizations. Three reports gauging progress in controlling corruption have been published since 2000, as well as significant additional work on various political aspects of private sector development, fiscal reform, administrative reform, and social protection. Much of this implicitly recognizes a major difference in progress in improving governance between the countries of Central Europe, the Baltic countries, and Southeastern Europe (with the possible exception of the former Yugoslavia) on the one hand, and the countries of the Commonwealth of Independent States (CIS) on the other. While the former have been prodded to improve governance as a consequence of the EU accession process, the latter have confronted challenges of protracted political stalemates and conflicts (Ukraine, Georgia), reform-unfriendly governments (Belarus, Moldova, Armenia), and the “natural resource curse” (Russia, Kazakhstan, Turkmenistan). The multi-pronged strategy for governance improvements in ECA countries developed in 2003 has remained in place and encompasses: building political and public accountability, strengthening competitiveness in the private sector, building capacity and institutions for public sector management, enhancing civil society participation, and fostering institutional restraints.

2.40 **South Asia.** A major theme of PEA of governance issues in South Asia pertains to the problems of public administration and the effects of politicization, distorted incentives, and limited accountability of governance. Unenforceable property rights and contracts, deteriorating law and order, and the widespread absenteeism of officials responsible for delivering services (teachers, doctors, and so on) are emphasized, as is the disproportionate burden of weak public administration on the poor. Meanwhile, a widening gap between the rich and the poor threatens stability and social cohesion in some countries in the region. Consequently, a major operational emphasis has been on both improving service delivery and on designing alternatives to public service delivery, particularly at the sub-national and local levels through decentralization, community-based service provision, e-governance initiatives, and so on.

2.41 **Middle East and North Africa.** Political analyses of governance constraints for the Middle East and North Africa (MENA) emphasize pressures from population growth, urbanization, and in particular, demographic shifts (including the “youth bulge”) that are straining governance effectiveness and institutional capacity. Moreover, although gender is typically highlighted as the main problem of “exclusion” in the region, other groups suffer as well, in particular, youth populations. PEA also recognize that some groups—for example, rural dwellers—have been systematically denied public services, creating some of the highest levels of illiteracy among middle-income countries. Problems of non-competitive elections, nepotism, tribal affinity, and patronage are also identified. The
effects of these governance weaknesses are several, but two deserve mention. First, weak governance has historically undermined confidence in the MENA business environment, limiting investment (outside of the oil and gas sector) and job creation. Second, weak governance has been linked to an exclusionary, inefficient social contract whereby a minority of workers obtain security of (usually public-sector) employment, but at the expense of declining wages and standards of living. Operational implications for governance reforms in the region, therefore, focus on particular groups, such as youth and women, as well as on reforms in the civil service to, for example, increasing wage dispersion and decentralization.

2.42 **Sub-Saharan Africa.** Political analysis of governance in Sub-Saharan African countries highlights the inter-related themes of natural resources, state fragility, and conflict management. Moreover, failures of previous efforts at improving state capacity in Sub-Saharan Africa have been recognized, and decades of capacity building have produced poor results (Levy and Kpundeh 2004). Efforts at indigenizing the inherited, colonial, extractive, and elitist state were often swamped by patronage and clientelism and unsustainable expansions in the scope of government (World Bank 2005a, p. 22). Ethnolinguistic fragmentation also produces political markets characterized by a lack of credibility of political promises, combined with clientelistic politics, resulting in dysfunctional bureaucracies and underperforming bureaucrats who are either direct recipients of patronage jobs or who are tools to deliver patronage benefits for politicians, and for unproductive enterprises. In addition, it has been suggested that, more than in other regions, Sub-Saharan African countries suffer from “quiet corruption,” that is, weak effort or commitment by frontline service providers that do not necessarily involve graft or bribery. This approach recognizes that increased government spending on social services alone may not improve the quality of public services (World Bank and United Nations Development Programme 2010). In treating capacity-building as a principal problem of governance, regional guidance urges operational work to focus on developing partnerships (with regional organizations and civil society) to bolster “demand-side” efforts to improve governance, on developing the capacity of non-state actors, and on improving the predictability of resource flows, given the adverse effects that volatility have on governments in the region.

*Other Donor Activities*

2.43 **United Kingdom Department for International Development (DfID): Drivers of Change.** Drivers of Change (DoC) is an approach developed by DfID to address the lack of linkages between a country’s political framework and development agency operations, focusing primarily on the interplay of economic, social and political factors that support or impede poverty reduction (DfID 2004). DoC focuses on power relationships and the institutional and structural factors affecting the lack of political will, based around a three-part approach that identifies “structures,” “individual agents,” and “mediating institutions,” and coupled with an emphasis on how to effect change. One of the aims behind this approach is to capture the importance of informal institutions and relationships:
Usually, we have a good idea about what needs to be done to achieve poverty reduction, but are much less clear about why it’s not happening. All too often, we attribute slow or no progress to lack of political will … It’s this black box of lack of political will that DOC analysis unpacks. This should result in this phrase disappearing from the risk column of a Country Assistance Plan or Regional Assistance Plan.4

2.44 Swedish International Development Agency (SIDA): Power Analysis. The “power analysis” approach has been developed by SIDA. It is based on the understanding that issues of power asymmetries, access to resources and influence over politics must be addressed if poverty is to be reduced. Power analysis seeks to map the informal political landscape, including its rules and structures. It seeks to understand how development cooperation and donor activities are influenced by this landscape, and how the landscape of power shapes their activities. The Power Analysis approach is informed by a commitment to working toward “justice, equity, and organized redistribution of access to the welfare among the world’s people” (SIDA 2005, p. 30).

2.45 German Society for Technical Cooperation (GTZ): The Governance Questionnaire. The Governance Questionnaire was designed by the GTZ as a tool to analyze the political and institutional frameworks, actors and relationships in a country. The aim is to help development practitioners to produce better informed and more effective strategies for policy reform. As with DfID and SIDA, the GTZ approach takes the view that political reform processes are strongly influenced by informal values, norms, customs and processes, rather than by following formal rules. This is thought to apply particularly to new democracies or weakly-institutionalized political systems. It also explicitly sets out to employ a multi-disciplinary approach, combining political science, law, economics, legal anthropology, and empirical social research. The Governance Questionnaire does not aim to provide a comprehensive assessment, but rather to highlight important issues, facilitate debate, and stimulate further enquiry to inform decisions about how to support reform (Faust and Gutiérrez 2004).

2.46 United States Agency for International Development (USAID): Democracy and Governance Assessment. One of the earliest donor-based political assessments is the Democracy and Governance Assessment designed by USAID for assessing the state of democracy and governance in a country, and the prospects for their improvement. The framework “guides a political analysis of the country, leads program choices, and incorporates what researchers and practitioners have learned from comparative experience” (USAID 2000, p.1). It also aims to identify certain comparable elements of countries’ political economy and institutions and use those to inform a strategic analysis of how best to promote democracy. The assessment focuses primarily on developing the elements of liberal democratic government, that is, on “liberty, open competition, the rule of law, and respect for pluralism and minority rights” (USAID 2000). This approach is designed to provide an entry point analytical overview for those considering actions to promote democracy in a given country.

4 Suma Chakrabati, DfID Permanent Secretary, quoted in Thornton and Cox (2005).
3. THE NEW ENVIRONMENT FOR POLITICAL-ECONOMIC ANALYSIS

3.1 The 2007 GAC framework and strategy, while remaining within the World Bank’s Articles of Agreement’s limitations on World Bank interference in politics, highlighted a need to better understand political-economic interactions that drive governance reforms. The GAC Strategy paper cites international evidence supporting the conclusion that:

When implemented, reforms have been particularly effective in combating certain types of administrative corruption, such as petty bribes to utility officials, tax collectors, licensing officials, and inspectors. In many states, however, forms of corruption with deep political roots—such as state capture and procurement corruption—have been more difficult to address. Political and business interests, including multinational corporations from developed countries, often collude to obstruct progress in combating corruption; unraveling these networks is extremely difficult. Thus, it is clear that effective leadership from both arenas is essential to tackling the problem. (World Bank 2007c, p. 40).

3.2 The GAC Strategy paper also recognizes the critical role of politics in ―governance systems,‖ that is, that public-sector governance is a result of the behaviors of different branches of government, multiple levels of nation-states (national and sub-national), as well as bureaucracies and the private sector, each of which can function as its own “interest group.” But at the apex of each of these groups sit politically salient actors with varying degrees of influence over economic policy making. They ultimately shape the political incentives those individuals within these institutions face, as well as their willingness to support or obstruct reforms to these relationships.

3.3 Implicitly, this acknowledges a stylized fact regarding chronic economic underdevelopment long recognized in the relevant literature, namely, that state weakness and fragility can be “built into” institutional design, precisely because it implies a greater tolerance for patronage-based decision-making or unrestricted access to public assets. If so, it is not easily amenable to strengthening via the provision of financial resources and human expertise. In the context of the post-socialist transition in ECA, for example, “state capture” was found to be prevalent in several countries where powerful private actors managed to control law-making processes and judicial enforcement, thus guaranteeing themselves a stream of rents (Hellman, Jones, and Kaufmann 2003). In Russia, regional governors were found to be complicit in designing highly discretionary subsidies and other transfers to the private sector because they shared in the rent stream (Desai and Goldberg 2001; Yakovlev and Zhuravskaya 2003). Whether during the Asian financial crisis or in Latin America, favored groups have institutionally granted privileges of economic value—directed credit, monopoly rights, protectionism, non-competitive procurement contracts, and the like—so that the government itself may share in the rents generated by asset holders in ways that are institutionalized (Haber 2006).
3.4 For several years “governance” has been a useful, value-neutral term donors can use to refer to politics. But the “traditions and institutions by which authority in a country is exercised for the common good” (a definition used by the World Bank⁵) is, above all, about political power and authority, and governance reform is inevitably a political act, contingent on the political process with implications for the dynamics of power and influence across individuals, groups, and institutions. The GAC Strategy recognizes the mutually reinforcing nature of poor governance with political “pathologies” by which elites benefit from corruption and graft, weak enforcement of existing laws, policy making based on special interests rather than the public welfare, or the private diversion of public assets.

**New Political-Economic Diagnostics**

“Problem-Driven” Governance and Reform Diagnostics

3.5 The elaboration of the GAC Strategy presented a new opportunity to recognize the inter-relationship between governance and political-economic conditions, as well as a need to have this relationship reflected in analysis and operations. Frameworks for using PEA to enhance World Bank-supported strategies and operations have been developed, in particular, by two primary reports: *The Political Economy of Policy Reform* (PEPR) published by the Social Development Department in 2008 and *Problem-Driven Governance and Political Economy Analysis* (PDG) published by the PREM network in 2009. Although the former is primarily focused on the operational implications of PEA for sectoral reforms (with agriculture and water given prime importance), the latter identifies principles for conducting and incorporating “Governance and Political-Economy” analyses in World Bank programmatic activities. Although they differ in terms of emphases, the points of convergence between them are the common themes for a new (more pragmatic) type of PEA.

3.6 The importance of political diagnostics. Both reports emphasize the importance of conducting credible, empirical PEA that goes beyond technical assessments combined with broad statements about governance problems. The PDG report notes that evidence-rich PEA can require: de facto as well as de jure mappings of institutional arrangements; interviews with local stakeholder representatives; focus groups; surveys of public opinion; sector-specific data, among other sources. The PEPR report also stresses the importance of an empirically-driven PEA that contains insight into, for example, distributional struggles and institutional arrangements that may bear on sector-specific reforms. Thus, both reports advocate going beyond limited analyses of formal institutions to better understand the wide divergence between formal and informal rules that may be present in societies characterized by high levels of clientelism and “patrimonialism” (that is, where public finances are managed and dispersed through personal ties to an individual leader, and where the dividing lines between public assets and the assets of those who occupy governmental offices is thin). Both reports also emphasize the need to link systematic

⁵ For example, see [http://go.worldbank.org/EBMU3VA0Z0](http://go.worldbank.org/EBMU3VA0Z0).
analysis with effective communication strategies to reduce the risk of ideological capture or resistance to policy reforms.

3.7 **Follow the rents.** A critical component of both “problem-driven” PEA and PEA used to gauge reform opportunities lies in an understanding of the political economy of rent seeking. Economic rents stem from a variety of sources and shape the incentives of relevant actors in significant ways. Rents from inefficient regulation or from natural resource monopolies have major economic costs, and can lead to widespread discontent with incumbent political authorities. The PDG report also emphasizes two types of rents: those emerging from the control of resources, and those from government regulation. It notes that external attempts to curtail or redistribute rents can result in political instability, and to a worsening of governance. Thus a realistic assessment of the nature and dynamics of rents, as well as their effects on key players, is critical for designing country and sectoral strategies. This guidance also notes that rents can be harmful, but under some circumstances beneficial. In this regard, rent-seeking can potentially enhance government credibility where the distribution of rents remains an important source of political stability:

External attempts to curtail or redistribute rents, or internal contest over the distribution of rents can result in political instability, and in the worst case, can lead to violent conflict. By implication, attempts to change rents should be approached with caution especially in potentially or actually fragile states. (Fritz, Kaiser, and Levy 2009, p. 49).

3.8 **Feasible approaches.** Both reports acknowledge that politically unfeasible solutions may be worse than the status quo. Privatization that, due to the configuration of institutions and powerful stakeholders, is accomplished through non-competitive bidding, and that produces a “private” entity with monopoly rights, privileged access to credit, and a system of corporate governance that does not protect investors, for example, is worse than maintaining a state enterprise under government ownership. Therefore, it is incumbent upon designers of programs and projects—especially those involving governance reforms—to identify the political feasibility of these efforts, and if they are not feasible, to find alternatives that, although second best in a technical sense, can produce measurable (if limited) change.

3.9 **Creating, rather than waiting for, windows of opportunity.** Although previous guidance on the political economy of reform emphasized the need to “seize” on or “assess the likelihood of” windows for reform, both reports push for a more active role in the reform process. In particular, the PDG report suggests that sharing and disseminating outputs widely (depending on country contexts) can—albeit rarely—help domestic reformers build support and mobilize constituencies. The report warns that it is may be difficult to pin-point stakeholders based on single issues—and indeed may be misleading to do so—since some individuals may have distinct policy preferences along multiple dimensions. The PEPR report notes that informed dialogue and public debate can build coalitions for change—and that PEA can serve as a starting point for public debate and can initiate the participation of reform-supporting stakeholders in the decision-making
process. Moreover, the PEPR report stresses the importance of “promoting transformative processes of institutional change,” that may come about when previously excluded groups are enfranchised.

The Evolution in Political-Economic Approaches

3.10 Much of the intellectual basis for the GAC Strategy recognition that governance and politics are intertwined was laid starting in the mid-1990s. Consequently, political analysis following the implementation of the GAC Strategy, to a certain extent, represents not so much the initiation of a new analytical exercise as much as the cumulative effect of a decade-long evolution in frameworks and perspectives on the constraining effect of political processes, actors, and institutions in development.

3.11 The challenge for newer PEA and political-economic frameworks, however, remains operational. In this regard, the newer guidance represents something of a departure from the ways in which World Bank operations have historically been conducted. In previous eras, a premium was placed on identifying the efficiency and/or optimality of programs that were part of lending operations, for example, in correcting price distortions, trade barriers, inefficiencies in public investment, poorly-designed tariff schedules or fees for public services, and so on, that were often the target of adjustment programs. In a subsequent step, the World Bank was expected to “ensure that the process of policy reform [was] ‘internalized’ in the country as quickly as possible” (World Bank 1986, p. iv). Borrower “ownership” emerged as an important consideration by the early 1990s mainly in evaluations of adjustment lending. A typical evaluation, for example, examines a range of political correlates of effective country ownership, and finds that politically stable countries and countries in which critical interest groups are arrayed in support of lending programs were most likely to have shown greater “ownership” of World Bank programs (Johnson and Wasty 1993).

3.12 The current political-economic guidance, with its emphasis on goodness of fit and “feasibility” signifies a different approach, namely, that it is important to determine the level of prospective country ownership prior to the initiation of lending operations (including, but not limited to, political incentives to reform, configuration of stakeholders, capacity of state institutions, and so on). Moreover, this assessment of country ownership should, in part, drive the design and implementation of lending operations. If so, this represents a reversal of the traditional political-economic approach taken by World Bank operations. Whereas the limits to the earlier method were that optimal programs were rendered ineffective due to the political environment, the current “inductive” method also has its disadvantages in, for example, limiting program results ex-ante, or in creating incentives for borrowers to signal a political “inability to implement” if it leads to less onerous lending operations. This review returns to these issues in subsequent sections.
New Financing, New Frameworks

The Governance Partnership Facility

3.13 Concomitant with the emphasis on PEA in the GAC Strategy, increased financing has been made available to diagnose the underlying political constraints that client countries face in order to identify appropriate entry points and develop innovative instruments that can ameliorate these constraints, thereby mitigating the governance risks that World Bank-supported programs and projects face. To foster learning with regard to good GAC practice at the country level, and to push the “new frontiers” of governance work—including political economy—the World Bank in partnership with the United Kingdom, the Netherlands, and Norway, established the multi-donor Governance Partnership Facility (GPF) in 2008. The GPF was created to support joint GAC strategies in selected countries as well as to generate GAC “public goods.” A proposal note from the UK’s Department for International Development states that the GPF should, among other goals:

[Encourage] the Bank to view governance from a broader perspective, going beyond its traditional areas of interest in public financial management and civil service reform, and grounding all its work in a better understanding of the political economy of countries and the political and economic governance obstacles to poverty reduction . . . The Bank sees in DfID a partner with a strong in-country presence in the governance area including a large number of governance advisors and an ability to address a number of issues such as political party reform, election finance, the media and criminal justice that fall outside the Bank’s mandate or expertise (DfID 2007, p. 3).

3.14 The GPF provided up to US$2 million for the implementation of country-GAC (CGAC) pilot programs in Afghanistan, Albania, Burkina Faso, Cambodia, the Democratic Republic of Congo, Haiti, Liberia, Mongolia, Nepal, the Philippines, and Zambia. The GAC implementation report notes that competition for GPF resources has been intense. The “new frontier” activities in CGAC pilots were to include political-economic analyses, strengthening of the demand side of governance and accountability institutions at national and sector levels, and implementing global governance initiatives and generating public goods at the country level.

The Operational Risk Assessment Framework

3.15 The vital role of operationally-relevant, applied political-economic analyses in GAC is further evident in the new initiative to institute “risk-based” lending in all World Bank projects. The ORAF, in place since July 2010, attempts to better manage corruption and fiduciary risks and to ensure that development funds are used for intended purposes.

3.16 The ORAF encourages attention to the various risk factors stemming from the broad political economy of the nation, from bad practices in a particular sector to project-
specific risks, in order to devise appropriate risk mitigation efforts. In contrast to the previous, more fragmented system of “flagging” risks during project implementation, the ORAF forces project planners to assess 10 risks across four different categories based on both likelihood and potential impact: (i) stakeholders (the risk that opposition groups will derail implementation); (ii) the operating environment (country-wide political risks); (iii) the implementing agency (focusing on fraud, corruption, political interference), and; (iv) the project (capture, adverse local effects, problems of monitoring and enforcement). As such, ORAF effectively builds political economy concerns into the heart of every project. A review by external GAC advisers notes, however, that “[ORAF] cannot hide one of the most profound issues in Bank operations: how to work effectively in nations with corrupt governments or sectors and limited, if any, institutional legitimacy and regulatory capacity?” (World Bank 2009f, p. 2).

The Political Economy Community of Practice

3.17 Accompanying the more favorable environment, the Political Economy Community of Practice (PECoP), has emerged as a focal point for supplying applied political-economic analyses to support operations. The principles of the PECoP, as announced during its launch are to: lead World Bank applied PEA, disseminate this knowledge, and to stimulate demand for applied PEA through efforts to demonstrate its value-added to country teams, and develop specific product lines to serve that purpose (World Bank 2010b). Currently, the PECoP relies on a core group of 25–30 World Bank staff members, plus approximately another 250 staff who have informally expressed an interested in joining the community. The PECoP is also building a roster of potential consultants with regional, country, and sectoral expertise who can conduct applied PEA in response to demand. According to the PECoP, since 2006, 71 applied PEA have been completed as independent assessments or as inputs to World Bank operations or reports—the bulk of these since 2008 (see below).6

3.18 To systematize its potential operational support, the PECoP has recently designed three sets of applied PEA for country teams, sectoral units, and project-specific teams: (i) support for Country Assistance Strategies (CAS); (ii) sector-specific analytics; and (iii) what is termed “process support.” The first and second are designed to assist country teams and sectoral units with the preparation of CAS or risk-management strategies (via the ORAF) though short notes, longer baseline country/sector political-economic reviews, or in-depth assessments. By contrast, “process support” is aimed at providing country teams with crucial political intelligence to facilitate program design and implementation in, for example, “fast-changing” environments, or through advisory services throughout the project cycle.

3.19 The product list of the PECoP notes: “Ultimately, if the political economy work is to be successful, the engagement and leadership of relevant country/sector team members throughout the process is essential.” (World Bank 2010a, p. 4).

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6 This is the result of stock-taking attempts by PECoP staff to determine how many PEA have been completed since 2006, and thus does not necessarily represent the total number of World Bank reports with political-economic content.
4. APPLIED POLITICAL-ECONOMIC ASSESSMENTS: A REVIEW

A Review of Political-Economic Analytical Inputs

4.1 The PECoP lists 71 applied PEA reports completed since 2006 in 39 countries (another four are cross-national within regions; two are multi-regional/global). Of the 71 reports, 59—over 80 percent—of these were started after FY2008. Forty-one are country-level (or multi-country) analyses, another 38 are primarily sectoral-based PEA, and only two are project-specific risk assessments. The Africa and Latin America-Caribbean regions account for over 50 percent of completed PEA, and the rest are spread across four other regions. From these 71 reports, fifteen were selected for in-depth review, based on regional representation (the sample covers all six World Bank regions), timing, and country/sector balance (a full list of reviewed work can be found in the references section).

4.2 The problems diagnosed by these reports are extremely varied—from managing natural resource wealth, to identifying the most corrupt institutions based on surveys, to assessing the impact of recent elections on reform programs, to understanding the political biases of those who allocate public investments, manage electricity cooperatives, operate buses, or regulate hospitals, and so on. Six of the 15 are inputs to CASs or Country Economic Memoranda (CEMs). Another six are (mainly) sectoral analyses. The remaining three are country case studies of larger reports.

Three Themes from Political Diagnostics

4.3 The balance of power among stakeholders matters. The majority of the analyses surveyed recognize that the various outcomes supported by the World Bank in each case—a more efficient public sector, more progressive service-delivery, broad-based economic growth, and so on—involve costs that are borne up front by certain groups, in addition to the benefits that may accrue over longer periods to the winners. In this context, there are two problems. First, potential losers who have access and representation in the political system have the means to oppose any program or project that imposes these costs. Second, the costs are typically well-known and understood to those who will pay them; by contrast, the benefits may be uncertain or simply unknown. For example, a CGAC input to the CEM from 2009 for Cambodia notes that smallholding rice farmers—overwhelmingly poor and vulnerable to demand shocks—are unaware of benefits they would obtain under rice-exports promotion or rice competition-supporting efforts, and are thus generally under-mobilized politically. By contrast, large millers are well aware of the losses in monopoly rents they would suffer from these rice development initiatives, and oppose them staunchly.

4.4 Other reports note a similar disparity in the balance of power between stakeholders—a disparity due to both collective-action constraints as well as information:  

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7 Of these 15, two are considered highly sensitive, and thus will not be directly cited here.
between individuals from different electricity catchment regions in the Philippines, between urban and rural users of public-investment projects in Mongolia, between commuters and bus companies in Bangladesh, between water service providers and consumers in urban Yemen, between large conglomerates and smaller firms in Ukraine, and so on. In each case, the power gap has obstructed or delayed implementation of previously-agreed reforms. Indeed the reports detail the numerous ways in which governments have in maintaining the status quo when pressured to do so by status quo beneficiaries despite World Bank pressure: foot-dragging, non-compliance with their own laws, and loan renegotiations.

4.5 Consequently, World Bank operations that support these reform programs are left with having to accept government intransigence—as is noted in several reports—or of finding ways to shift or rebalance the disparity between stakeholders. Note that “empowering winners” through, for example, consultative mechanisms or information-sharing stakeholders has been part of the World Bank’s implementation for several years. Most of the pre-GAC reports reviewed, in fact, advocate some form of support to prospective constituencies that would favor World Bank programs—for example, poor and vulnerable households, small and medium enterprises, smallholders, and so on. Pre-CAS governance notes for Ukraine (2007) and for Bosnia-Herzegovina (2007), for example, argue in favor of supporting civil society groups that represent these interests, such as entrepreneur associations and community organizations, and for creating “demonstration” pilots in order to raise demand for similar programs elsewhere.

4.6 Some recent reports, however, go further than simply supporting the weak and disenfranchised directly (via information) and indirectly (via support to civil society organizations that might mobilize these groups) to limiting the influence of status quo supporters. One of the reports, for example, notes that a necessary long-term strategy for the World Bank and other donors is to find ways to limit the influence of actors that benefit from current rent flows. An analysis of Mongolia’s public investment management systems (2010) recommends that a continuation of limited rent streams may buy-off opponents of reform. An assessment of Filipino electricity cooperatives (2009) warns against corporatizing cooperatives (as previous advisory work had recommended) as this would simply increase the weight of cooperative managers in the political system.

4.7 The pathologies of bad governance are difficult to address. By far the most common theme among the reviewed reports is that bad governance is a function of economic efficiency being undermined by political-distributorial concerns. In a nutshell, bad policies occur when they are designed and implemented in ways that benefit politically influential groups. This idea—found in the political-economic literature for many years—was also prominently highlighted in the 2004 WDR, which attributed poor service delivery to decisions made on behalf of the rich rather than the poor (Robinson 1998). Thirteen of the 15 reviewed reports identify some form of “clientelism” (policies that narrowly benefit particular interest groups rather than the general public), “patronage” (the distribution of public goods on the basis of favoritism, loyalty, and so on, rather than efficiency), or “patrimonialism” or “neo-patrimonialism” (governing according to cults of personality or individual discretion rather than laws or rules).
Poorly-institutionalized state structures, patron-client networks, and other elements of poor governance, in these views, are not simply a matter of bad design or insufficient resources. Rather they are considered elements of a governing “pathology” that often has deep-seated, structural or historical causes. It should be noted that none of this necessarily involves actual corruption, bribery, graft, or malfeasance. Bad governance can be perfectly legal.

4.8 In Ghana, for example, the inability of politicians to make credible promises to voters means that they can only appeal to narrow groups on the basis of ethnic solidarity, tribal kinship, and so on. Ghanaian electoral debates therefore hinge on matters of the personality of leaders and of local public works rather than broader reform efforts that affect the entire nation. In Zambia, successive governments have been unable to adopt international “best practice” in electricity, telecommunications, and water regulation, mainly because reforming these sectors would disrupt the flows of cash to or the allocation of public-sector jobs by governmental agencies. In Nepal, health ministry and hospital staffing is a major source of patronage. In Bangladesh, bus permits and licenses generate large funds to agencies that are controlled by political parties. In Ecuador, oil contracts are distributed not to the highest bidders, but often to pre-determined parties that are in the good graces of the government. In each case, the money, employment, or procurement contracts are doled out to political favorites.

4.9 Again, these are not new or unprecedented diagnoses of government problems. And, as with those done in past years, some of the main reforms—for example, building more “programmatic” political parties, encouraging credible political challenges to the authority of incumbents, nation and identity-building efforts—are out of reach for the World Bank (although these reform measures are mentioned in several reports). Other long-term recommendations involve, as they have done previously, improving basic education and literacy, or ensuring equity in access to public services across ethno-linguistic or regional groups.

4.10 A few of the surveyed reports advocate “feasible,” second-best options where best-practice efforts have previously failed. The review of Mongolian private investment suggests that some politically-driven, pet projects may be allowable if the bulk of public-investment funds are allocated to national priorities. The Zambian infrastructure assessment argues that the basic reforms advocated—an independent regulator, de-monopolization, and unbundling of power generation from distribution—have failed to take place due to an explicit political calculus that these reforms would deny access to rents. The alternative should be to secure a series of partial commitments from governmental authorities, for example, to allow limited private participation, potentially creating an alternative source of rents, and potentially breaking the governmental attachment to the public monopoly.

4.11 Discretionary authority allows bad governance to persist. High levels of executive discretion over policy implementation are a third prominent theme in the reviewed PEA. Discretion means that politicians and public officials do not have to negotiate with other branches of government, that their decisions do not have to be
formula- or rule-based, and that existing rules can be selectively enforced or interpreted. Moreover, discretionary authority makes the allocation of public goods or services according to patron-client determinations all the more easier. The Zambian infrastructure report states that service receipts from electricity and telecommunications utilities, combined with lax controls on public financial management, allow that cash to be used to finance political parties, shelter friends, withhold from enemies, and so on. Similarly, water subsidies in Yemen are allocated on a highly discretionary basis. So too are national revenues that are shared with Peruvian regions, oil contracts in Ecuador, pharmaceutical permits in Nepal, and all other goods that are the currency of patron-clientelism.

4.12 The standard solution to problems of extreme executive discretion is to enhance the system of checks and balances between branches and levels of government. Some of the surveyed reports hint that “stalemates” or “gridlock” have had adverse effects on economic governance; most, however, advocate support for counter-weights to the political executive. One solution is support for parliamentarians, as well as for judicial reform, although only one of the reports argues for this approach. Others rely on strengthened sub-national governments, independent regulatory bodies, sub-agencies of the government, nongovernmental organizations (NGOs) and other “watchdogs,” to enforce accountability on the executive. 8 A Nepal health sector assessment supports the decentralization of health services to individual service providers. A Yemen urban-water survey argues for continuing efforts to decentralize the governance of the water utilities to the regions. An analysis of decentralization in Peru notes that regional presidents can counter-balance the national government. In Bosnia, a report suggests that supporting independent think-tanks that can act as watchdog groups. The Philippines electricity report argues for making the existing electricity regulatory agency independent of the government, and so on.

4.13 In addition to creating constraints on executive power, outside monitoring or audit functions are also supported by several of the reports reviewed. The Mongolia public investment analysis argues for a shift in operation focus from upstream preparation of investment projects to better ex-post oversight. The Bangladesh bus sector report notes that the regulatory agencies themselves need more effective accountability mechanisms. A regional report on natural resource management in Latin America, based on a review of the evidence, indicates that “commitment mechanisms” (greater accountability, democratic institutions) are needed to prevent governments from exploiting price cycles.

Some Operational Implications Summarized

4.14 **Information access should be a priority.** Improved information access through consultative fora, mandatory disclosure rules, third-party monitoring and audit, public debate, dialogue with affected parties, and so on, can have several ameliorative effects on poor governance, including mobilizing potential supporters, limiting room for clientelism, and supporting constraints on administrative discretion. But openness alone

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8 A separate background note on accountability institutions is being prepared as part of this overall GAC evaluation effort.
may be insufficient to incentivize key decision makers to improve the quality of their
decisions, and governments retain ways of bypassing transparency requirements.

4.15 **It is sometimes necessary to intervene in political markets.** In the political
marketplace, groups vie for the attention of policymakers and battle to have their
preferences expressed in national policy. World Bank-supported programs that favor or
oppose a subset of those policies will, with few exceptions, be subject to the same types
of pressures. One implication of this is that, without constituencies that favor these
programs, they cannot achieve the degree of legitimacy or acceptance needed to achieve
their developmental objectives. Thus, it is sometimes important to find ways to mobilize,
support, and/or empower these allies. Other donors have explicitly incorporated these
considerations into program design and implementation strategies—for example, DfID’s
Drivers of Change approach, SIDA’s Power Analysis, and the like.

4.16 **Consider implications of programs for factionalism.** “Factionalism” here does
not refer to the competition between groups over policy preferences, but rather the
presence of long-standing ethnic, linguistic, religious, regional, or other cleavages. This is
especially true in conflict-affected states, where program designers must consider what
effect their efforts will have on sectarian tensions and consider ways to manage or resolve
conflicts.

4.17 **Don’t worry about elections.** In some parts of the donor community, changed
in government are often dreaded for the turmoil that leadership turnover can cause in
their programs, given that donors must now attempt to continue efforts with the
cooperation of new leaders whose political preferences may be different. The analyses
reviewed above, however, are far more sanguine about constitutional changes—that can
force accountability on governments, and that can restrain policy making based on
narrow interests—and more focused on problems of broader political and policy making
uncertainty. Arbitrary enforcement or interpretation of rules, contracts, or unpredictable
changes in the quality of public goods, and so on, are more harmful to long-term
development objectives than electoral turnovers. In the extreme, political violence and
conflict are far more worrisome.

4.18 **Stalemate may benefit governance reform.** There is, here and there, still a wish
for “reform champions” as well as enlightened political leadership to advocate on behalf
of donor-funded programs and to break through the gridlock or partisanship that may
have hamstrung reform efforts. However, most reports recognize that stalemates may be
signs of equity in the political power of different stakeholders, or of checks on executive
power having effect.

4.19 **Rely on other donors.** Several of the surveyed reports note the need for World
Bank partnerships with other donors—particularly in areas where the World Bank cannot
intervene—and thus reflect the spirit of the GPF that donor partnerships can support
needed political reforms that are outside of the World Bank’s mandate.
Political-Economic Content in Economic and Sector Work

4.20 In addition to separate PEA, this paper also reviewed several written outputs of the World Bank’s ESW to identify the relevance and quality of political-economic content, and to examine the extent to which attempts to mitigate political risks or address political-economic constraints were present in operational recommendations.

4.21 A review sample was selected as follows. Based on the countries selected for Level-2 analysis in accordance with the approach paper for the larger GAC evaluation, all ESW for these countries from 2004 onwards was compiled. The final list consisted of 877 ESW reports covering thirty-five countries. This population of reports was then stratified according to pre-GAC or post-GAC timing (2004–2007 versus 2008–2010), region (across the six World Bank regions), and report type (core diagnostics consisting of CEMs, PERs, Development Policy Reviews (DPRs), and Poverty Assessments versus other diagnostics and advisory reports). Taking into account these strata, a sample of 17 documents was randomly selected constituting some US$4 million in total cost, about ten percent of which were financed by trust funds. The resulting sample is balanced across region, between pre- and post-GAC periods, and between core and non-core reports. For each of five different dimensions of political analysis, each report was scored from zero to 4 based on the extent to which the relevant dimension was integrated into the report. (These ratings rank the degree of political analysis; accordingly, zero to 1 rates the amount of political analysis as Negligible, that is, ignored or left unanalyzed, 2 is Modest, or minimally analyzed, 3 is Substantial, and 4 High). Table 4.1 lists all scores and group averages.

Five Dimensions of Political Analysis

4.22 Political incentives. One of the tests of the extent to which political analysis has been integrated into ESW is whether specific country- or sector-level political sources of incentive distortions are examined. The pursuit of power, wealth, and incumbency can be shaped by political processes, institutional arrangements, or informal relationships in which key players participate and which influence their behavior. This requires an understanding of the extent to which the political motives of key players (who may receive rents, status, or privilege from the status quo) are responsible for the current conditions, including conditions of poor governance, failed attempts at previous reforms, a poor record of project implementation, or other adverse program outcomes. Conversely, the extent to which past reform successes occurred alongside changes in these incentives also merits investigation.

4.23 On this critical issue, very few of the reviewed ESW reports engage in much discussion of potential, underlying incentive incompatibilities with World Bank-supported programs. Indeed, only four reports do so in any extended fashion. The Haiti CEM from 2006 explains that deficiencies in security, in the investment climate, and in the quality of service delivery, are directly traceable to behaviors prompted by the precariousness of governmental tenure, the widespread de-institutionalization of governmental agencies, and the individual control politicians often have over public
finances. The 2005 Pakistan Country Financial Accountability Assessment (CFAA) notes the lack of incentives within the executive branch to make timely spending decisions as well as to deliver quality services. The 2008 Nicaragua Institutional and Governance Review (IGR) indicates that the absence of credible challenges to a political “duopoly” of two parties has left few reasons to deviate from the status quo. The 2010 Indonesia DPR notes that changes in political incentives as a result of democratization processes combined with decentralization have improved accountability at the central level, but may have increased room for local-level governance problems.

Table 4.1: ESW Scoring

<table>
<thead>
<tr>
<th>Country</th>
<th>Report</th>
<th>FY</th>
<th>Incentives</th>
<th>Stakeholders</th>
<th>Credibility</th>
<th>Institutions</th>
<th>Mitigation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mali</td>
<td>Transport Sector Report</td>
<td>2004</td>
<td>0</td>
<td>2</td>
<td>1</td>
<td>1</td>
<td>0</td>
</tr>
<tr>
<td>Sri Lanka</td>
<td>Development Policy Review</td>
<td>2004</td>
<td>2</td>
<td>3</td>
<td>1</td>
<td>2</td>
<td>0</td>
</tr>
<tr>
<td>Uzbekistan</td>
<td>Public Expenditure Review</td>
<td>2004</td>
<td>2</td>
<td>3</td>
<td>2</td>
<td>2</td>
<td>1</td>
</tr>
<tr>
<td>Pakistan</td>
<td>Country Financial Accountability Assessment</td>
<td>2005</td>
<td>1</td>
<td>1</td>
<td>1</td>
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<td>Public Expenditure Review</td>
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<td>Morocco</td>
<td>Public Financial Management Report</td>
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<td>Mozambique</td>
<td>Food Prices Report</td>
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<td>Post-GAC Average</td>
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<td>1.9</td>
<td>1.4</td>
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<td>Averages (total)</td>
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<td></td>
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<td>2.1</td>
<td>1.5</td>
<td>1.7</td>
<td>0.8</td>
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</table>

Source: Author’s assessment of ESW cited.
Note: ESW are scored based on extent of integration of these political-economic dimensions: 0 = not mentioned; 1 = mentioned but not analyzed; 2 = minimal analysis of implications; 3 = analysis of concepts and implications; 4 = extensive analysis and use in identifying recommendations and feasibility of programming.
4.24 Some other reports do note the pernicious effects of incentive distortions that are mainly political, but do not elaborate, nor do they link these incentives to potential incompatibilities with country, sector, or project objectives. The 2010 Azerbaijan CEM describes the potential for rents from oil and cement production, as well as the destabilizing effects of non-equitable rent distribution on governmental behavior, but does not assess the implications of these incentives for deregulating both sectors (a main recommendation of the report). In a concluding note, the 2004 Sri Lanka DPR suggests that a fragile balance of power between rival groups combined with short election cycles creates an environment where short-term thinking is rewarded, but does not consider the impact of these short time horizons on the management of public finances, on passing policies that boost exports, or on reviving non-plantation agriculture, the main topics of the review.

4.25 More commonly, policy areas where political incentives have shaped past trajectories, and therefore are likely to continue to do so, are simply ignored. For example, two poverty assessments reviewed—for Cambodia (2006) and Bangladesh (2008)—identify severe disparities in the delivery of basic services, access to common property, and allocation of public investment between regions. But neither report examines whether these allocative decisions are shaped by inter-regional distributional conflicts which may, in turn, influence the incentives of key policymakers as well as the prospects for greater equity. The same is the case for the two PERs reviewed—for Uzbekistan (2005) and Liberia (2009)—both of which mention that these governments have failed to implement public financial management procedures in accordance with their own laws. However, they do not explain whether incentive distortions may be at the heart of these failures. The record is even spottier when the sector-specific ESW is examined: reports on youth employment (Kosovo), land use (Paraguay), transport (Mali), and so on, do not contain any discussion of sector-specific political incentives that may have contributed to governance failures.

4.26 Stakeholders. Some indication of “stakeholders” seems to be obligatory in ESW outputs—indeed, the term is mentioned 64 times in the seventeen reviewed reports. However, an integrated political assessment of country, sector, or project-specific governance obstacles and risks (as now required by, for example, the ORAF) hinges on not only whether stakeholders can be identified along with their preferences, but whether their capacity for collective action can be estimated and their relationships with key decision-makers can be mapped. A small number of reports—the Haiti CEM and the Nicaragua IGR, mentioned above—do this well. However, by these standards, most of the ESW reviewed here do poorly. In most cases, the term is simply mentioned as part of a recommended consultation process or policy dialogue, that is, a report merely mentions that a “full range of stakeholders” must be involved in a project cycle. But there is little analysis of the actual distribution of stakeholders in the sectors under investigation, or of their status quo/reform preferences, their degree of mobilization, the rents to which they have access, or their ability to veto reforms.

4.27 Most reports reviewed here, to be sure, identify key players. Several go further in implying that the political strength of these groups may be responsible for previous
reform failures. However, they do not usually consider the extent to which the agenda-setting power of these groups may obstruct proposed reforms. The 2004 Mali transport sector report identifies three potential groups that oppose certain reforms: the state-owned airports authority, employees and managers of the now-defunct national airline, and a state-owned river transport company, all of which benefit from an inefficient system of subsidies and transfers. The report does not examine the obstacles these groups present for one of the pillars of the reform agenda, that is, the establishment of “market-based” transport services.

4.28 One of the more contentious issues in economic policy—land use—is the focus of the 2007 Paraguay report on real property taxes, and much of this report examines potential divisions between rural and urban, landholding and landless, rich and poor, and so on, in creating an environment of heightened social tensions over land issues. But the disparity in organizational and resource strength, or political influence of these groups (and therefore their unequal weight in formulating existing land tax and administration regimes) is not explored. Similarly, a 2008 Mozambique survey of food and fuel prices identifies cleavages between producers and consumers of food (overlapping the divisions between urban and rural residents), but does not examine the effects of difference in political influence between the two in setting food pricing policy (for example, the familiar “urban bias”), nor the implications of price hikes on relationships between these groups and policymakers.

4.29 More commonly, extended analysis of inter-group tensions and their effects on reform agendas (sectoral or country-wide) and project design are simply ignored. A representative example is the 2008 Kosovo youth employment report which, although mentioning that low-quality jobs cluster in construction and agriculture where workers are paid without contracts, benefits, social security, and so on, does not examine the extent to which employers in these sectors have or have not resisted labor-benefiting reforms. Similarly, the 2009 Morocco Public Expenditure and Financial Accountability Assessment (PEFA) identifies several budgetary weaknesses—procurement, audit, and proper budget classification—without examining the extent to which these non-transparent aspects of public financial management benefit particular groups, sectors, regions, and the like.

4.30 Credibility and time consistency. A third component of political analysis that is well integrated into ESW is some assessment of the risks of deviation from country, sector, or project GAC priorities due to changes in governments, changes in relative strengths of coalitions or constituencies that favor sectoral or project priorities, changes in agreements regarding sectoral or project-level rent extraction and distribution, and so on—in sum the ability of governments to send credible signals of reform commitment. In addition, some analysis of potential commitment mechanisms that limit the ability of political leaders, public officials to divert assets, impede reforms or project implementation, or otherwise ensure sectoral or project-level credibility, is warranted. On this measure, the ESW reviewed exhibit considerable variation.
4.31 Most of the reviewed reports identify problems of governmental credibility and commitment, albeit indirectly. Reports most closely linked to issues of time consistency in government decision-making, namely, the public-finance/expenditure reviews, usually consider these conditions directly. The 2005 Pakistan CFAA, the 2004 Liberia PER, the 2009 Uzbekistan PER, and the 2009 Morocco PEFA, in particular, all address the impact of budgetary and fiscal rules on government credibility. The Uzbekistan PER, for example, notes that the time-consistency of governmental behavior may be seriously compromised by large amounts of contingent liabilities, made possible by the proliferation of off-budget items. Also noted is the instability of tax rates due to the large discretion given the cabinet, as well as the need for greater checks and balances on the authority of the executive branch.

4.32 Some of the reviewed reports, while cognizant of credibility problems, appear to be restricted in terms of the types of credibility-boosting measures that they can propose. The 2005 Syria investment climate assessment (ICA), for example, identifies “regulatory unpredictability” as a major constraint to doing business. However, it does not examine the role of commitment mechanisms as a means of reducing uncertainty, nor the constraints to adopting such an approach given the particular country context. Rather, it argues for formula-based customs and tax procedures as preferable approaches. More bluntly, the Nicaragua IGR recognizes the futility of proposing strengthened commitment mechanisms on a government that has easily evaded formal accountability by, for example, weakening the audit office, or by resisting a diminution of its prerogatives in regulatory matters. Similarly, the Indonesia DPR urges accountability reforms for local governments, which appear to have increased their levels of time-inconsistency even as the central government has resolved some credibility problems.

4.33 Again, several reports simply ignore the issue. The sectoral reports—transport in Mali, food prices in Mozambique, land use in Paraguay—all diagnose governance problems that seem partly a function of poor governmental credibility (an inability to secure private investment in transport, the lack of a supply response in agriculture to policies that should smooth out price shocks, and the failure of land tax reforms to improve land utilization, respectively). None of these reports, however, elaborate on the implications of these credibility problems for their recommendations, nor do they examine possible commitment mechanisms.

4.34 Institutional design and weaknesses. After the mention of stakeholders, problems of state capacity/weakness are among the most-commonly mentioned governance deficiencies in reviewed ESW. The key for quality of applied political analysis—as suggested by the general guidelines discussed previously—lies in assessing the extent to which these institutional fragilities are due to deliberately-designed limits on administrative or regulatory capacity and internal conflicts, relative to a lack of financial resources and human expertise. Without exception, all reviewed ESW mention problems of institutional capacity affecting relevant government agencies, public-sector bodies, and policy regimes. Several recommend the need to insulate regulatory or implementing units from discretionary intervention. Very few explore whether these capacity constraints are politically-driven, and fewer still examine issues of institutional or
regulatory capture, or whether and/or how particular groups or individuals benefit from these problems of institutional design.

4.35 Some reports are better at unearthing political determinants of capacity weaknesses. The Nicaragua IGR notes that water and sanitation regulation will not benefit from the usual technical assistance to improve their regulatory decisions, mainly because those reforms would eliminate an instrument political party-machines use to reward supporters. Similarly, the Haiti CEM recognizes the potential futility of capacity-building in the civil service due to its valuable role as a source of patronage. The Paraguay land use report notes that existing laws guarantee a permanent under-valuation of land as a means of providing de factor tax breaks to large landholders.

4.36 Most of the reviewed reports, however, do not undertake this kind of assessment. In some cases—particularly when dealing with matters of public expenditure—this leaves a gaping analytical hole, and a significant governance problem unresolved where capacity-building is recommended without recognizing how weak capacity can be part of institutional design. The Uzbekistan PER (2005), for example, emphasizes the widespread presence of extra-budgetary accounts. Additionally, the report notes that excise taxes, privatization proceeds, and other revenues are “earmarked” for certain industrial-financial conglomerates and that security service personnel wages are paid outside the formal wage bill, among other problems. In response, the PER recommends capacity-building support and technical assistance to the public financial institutions of the central government. But the report does not analyze the extent to which this fragmentary fiscal regime has been intentionally put in place over time by political leaders in concert with key players (industrialists, security police, and so on). It is maintained precisely because it allows discretionary access to the public purse. Similarly, the more recent Liberia PER (2009) notes that most ministries lack functioning internal audit units, and those that exist tend to combine controller and policing functions. The report recommends that capacity-building support be offered in order to help develop the internal audit functions, which should be separated. But there is no assessment of the degree to which this institutional status quo benefits key players or whether it is, for example, a post-conflict compromise.

4.37 Mitigating political factors. The final dimension on which the quality of political analysis in ESW should be evaluated is whether the proposed reforms, projects, or programs are designed with components that address the political challenges of governance in the countries in question. To do this, identified priorities should examine whether the effects of incentive distortions might be somehow minimized, as could be the intransigence of opponents, and problems of credibility and institutional weakness. Proposals could, for example, be structured in ways that potentially raise both the political benefits of reform and the political costs of undermining reform, while minimizing potential tensions and social polarization. At a minimum, the possibility of these factors impinging on program objectives should be explored.

4.38 There is considerable variability in the extent to which reviewed ESW address these issues. The reports in which political analysis is most thoroughly integrated not
only identify how political risks can be mitigated, they also adjust reform proposals based on the governance track-record to avoid repeating past mistakes, attempt to determine the presence of reform windows of opportunity, find ways of rallying reform-supporting constituencies, and reach out to other donors and potential international partners who are not restricted from pushing for political reform. The Haiti CEM cautions that reforms that aim to change the rules by which public agencies operate, and to augment their financial resources will prove ineffective unless there are incentives of political leaders to work through the existing institutions of the state, rather than relying on personal connections and informal relationships. The report advocates targeting improvements to public security, courts, the national police in particular areas rather than country-wide, while at same time enhancing the political power of local authorities and citizens through community development and support to grassroots organizations. Ultimately, this requires the kind of state-building that can only be accomplished through a broad-based multi-donor effort together with the continued assistance of United Nations forces in the country.

4.39 Although they may not find ways to mitigate actively the various binding political constraints, some reports do adjust reform proposals to deal with political realities. The Indonesia DPR, noting the political constraints to broad-based governance reform, outlines an experimental approach that focuses on seeking reform-ready policy areas that could subsequently be scaled up or replicated. In Indonesia, these efforts focus on select anti-corruption institutions and budget reforms within a small group of ministries. Similarly, the Paraguay report on land use strongly urges self-assessment of land values as a feasible procedure given capacity constraints facing municipalities. It warns that greater municipal discretion to set tax rates (recommended by international experience) may make matters worse due to the institutional weaknesses of municipal governments. In Nicaragua, the IGR notes that the “ideal” independent-regulator approach to public utilities will not be politically feasible because of the close connections that political parties prefer to have with regulatory bodies. Instead, the report advocates a push for passage of a regulatory reform law—which contains prudent principles of utility regulation—along with the active participation of those who could demand further reforms (consumer advocates, regulated companies, and so on).

4.40 By contrast, several reports simply note that “political commitment” or “will” is necessary for the successful implementation of reforms, or rely on enlightened political leaders to shepherd reforms through political waters. The Cambodia poverty assessment (2006), for example, emphasizes the need for “far-sighted” leaders to manage public assets more effectively, provide law and order, secure property rights, and do several other things that are needed to narrow the urban-rural income gap. This report does, however, advocate strengthening communal councils as a way of increasing the political power of rural residents. By contrast, the Sri Lanka DPR notes that the commitment of leaders will be needed to address bureaucratic constraints to public service delivery—overstaffing, salary compression, fragmentation, duplication, and wastage—but does not identify how that commitment can be built, nor what options remain in the absence of that commitment.
4.41 Most of the reviewed reports, however, do not even conduct this minimal level of analysis. They do not explicitly identify any means of mitigating political obstacles, nor do they estimate whether status-quo stakeholders are powerful enough to block reforms, or whether their resistance can be mitigated/bypassed. They do not identify any explicit “political” benefits to reform advocates within and outside of government. The Liberia PER, for example, compliments the post-war government for passing laws and enacting reforms that have improved financial-management functions. However, it does not examine the mechanisms/strategies/methods by which these reforms were designed and implemented, or their likely sustainability.

4.42 Most reports do not explore ways in which status-quo biases of certain stakeholders can be mitigated, and do not address country-wide or sectoral fiscal reform risks or the likelihood that reforms may be undermined. The Uzbekistan PER, for example, notes that transparency and accountability mechanisms for the executive branch of government are necessary, but it does not propose any short-term or medium-term means to accomplish this.

Some Remaining Challenges

4.43 What does this review—however limited—reveal about progress in integrating political-economic concerns regarding governance problems and risks to reform in World Bank analytical work? Some tentative and preliminary themes are highlighted below.

4.44 A considerable amount of political analysis was conducted prior to the GAC Strategy. This review does not show the integration of PEA to be increasing following FY2007. One of the reviewed reports that comes the farthest along in incorporating political analysis along the five dimensions is the Haiti CEM, written in 2006. The pre-GAC Pakistan, Paraguay, and Cambodia reports also contain limited political analysis. Two post-GAC reports that deserve above-average grades are the Nicaragua IGR (2008) and the Indonesia DPR (2010). However, the other post-GAC reports (on Bangladesh, Kosovo, Azerbaijan, Liberia, Morocco, and Mozambique) show little signs of a trend towards the “new-generation” of PEA in this regard.

4.45 The extent and quality of political analysis is uneven. The ESW review shows a large degree of variability in the extent to which PEA is integrated in analytical reports, both before and after the rollout of the GAC Strategy. It is not the case, moreover, that the type or quality of explicitly “political” or “semi-political” issues embedded in ESW has changed before and after the GAC Strategy in terms of level of sophistication or in coverage of pertinent issues, although there is more explicit recognition of what is “political” in post-GAC reports. A representative pre-GAC report (the Sri Lanka DPR), for example, notes that the report must remain silent on “political” matters, but then proceeds to recommend that the government slash spending, fire civil servants, cut public wages, raise income taxes, expand the value-added tax and excise tax, and privatize public enterprises. That these reforms—which, in any country, would ignite bitterly-contested distributional conflicts—are not somehow “political” begs credulity, and most recent ESW recognizes this.
4.46 The “solution gap” is widening. It is likely that the implementation of the next phases of the GAC Strategy combined with the imperatives contained in the ORAF will further deepen and mainstream political analysis and diagnosis. But despite this expanded knowledge base, the operational implications of greater PEA may remain constrained by the World Bank’s mandate. In some areas, recent analytical work (both PEA inputs and ESW reviewed) reflects adjusted recommendations based on assessments of political feasibility, for example, in tolerating rents that may be politically valuable to keep key constituencies happy or to co-opt opponents, or to avoid the “independent-agency” approach to policy making where institutional weaknesses are rife, and so on. Yet many of the solutions proposed are similar to those suggested in the World Bank’s 2000 Governance Strategy, and in the PRSP Sourcebook: consultative policy making, checks and balances to central authority, and a premium on information sharing and access. If correct, then the gap between political-economic diagnosis and operational solutions will continue to widen. New rationales will mean better-informed PEA in all aspects of World Bank analytical work and in operations, but it will also require highly innovative solutions to operational problems given these political constraints—solutions which, thus far, have not been widely forthcoming.

4.47 The gap between the incentives of experts and operations staff within the World Bank is also wide. Thus far, the main approach of the Political Economy Community of Practice has been to build up a roster of in-house experts and to maintain a similar roster of consultants with the requisite skills and knowledge of the politics of countries and sectors, as well as those with more general skills, as well as to advertise its product lines to country teams. This has contributed to a wider awareness of the importance of the political constraints to the World Bank’s activities in client countries. But the PECoP can serve as more than a mere clearinghouse. Rather, the PECoP can function as a source of continuous guidance and training for country teams and task leaders themselves, and thereby help in mainstreaming and integrating PEA within project design to ensure that operational staff are conversant with the main dimensions of political analysis, and that political aspects of operational risk are adequately highlighted and addressed.

4.48 Political analysis can be more explicit about the politics of lending and of the political role of the World Bank itself. It is notable that none of the ESW reviewed (or for that matter the political diagnostics reviewed above) examine or recommend reductions in the exposure of the World Bank to the countries analyzed. Granted, this latter recommendation would be an extreme response to problems of operational risk and/or moral hazard in borrower countries. Yet it is noteworthy that none of the reviewed items discuss—even minimally—the tolerability of risk in countries given political circumstances or equilibria, or the inclusion of a reduction in lending operations as a possible instrument available to the World Bank, or the need to restructure the types of lending instruments used. This is not to suggest that all ESW or PEA should, by default, examine the implications of reducing exposures in borrower countries. However, analytical work that recommends solutions to problems of poor governance should, at a minimum, be cognizant of the implications of this last resort for government incentives.
and behavior. Similarly, reviewed analytical work largely ignores the “politics of aid” in aid recipients, in particular, how donor aid and lending decisions, aid dependency or volatility may have influenced past policy decisions, reforms, or other actions.

4.49 Some operational implications of political analysis carry their own risks. In recent years, a number of governance reforms that have been devised while taking account of political constraints have been enthusiastically embraced by the World Bank—as well as the donor community. The potential for unintended consequences of these reforms is potentially large, and is often left under-investigated. Three such reforms are mentioned here as examples: decentralization, pro-poor empowerment, and tolerance of limited rent-seeking.

4.50 Delegating authority to sub-national governments is often seen as both a “participatory” approach to policy making and as a form of check on centralized executive power. The assumption is that better information is available at the regional or local level than at the center, and that local institutions being closer to program beneficiaries, are more accountable to citizens. But elite control over local projects is often pervasive and the informational advantage of decentralized programs can be compromised by its diversion to benefit local elites (Bardhan and Mookherjee 2006). Depending on the peculiar lineages of sub-national power relations, local governments may be more prone to capture (and consequently, less accountable than the central government). Under these conditions, decentralization may simply shelter local elites, who use their position to over-provide services or public goods to themselves or their families.

4.51 In some respects the World Bank has, in fact, attempted to re-shape the political equilibrium in countries in which it works. The “pro-poor” focus in service delivery, expenditure reform, CDD initiatives, participatory approaches to development, local-level accountability, governance “score-cards,” and so on, all essentially work to shift political power from the rich to the poor. The governing assumption—supported by the political science and political-economic literature—is that many of the exclusions faced by the poor (in access to services, in allocations of public goods, several of which are documented in the reviewed ESW) are due primarily to the lack of political agency among the poor. Consequently, increasing the weight of the poor in policy making processes, on these grounds, makes sense. But there is little reason to believe that replacing pro-rich patron-clientelism with pro-poor patron-clientelism will reduce poverty. In fact, much available evidence suggests that the poor are more, not less, likely than the rich to favor narrowly-targeted gifts, favors, public jobs, or other transfers rather than public goods provision that reduce their poverty or cushion their households against shocks (Robinson and Verdier 2002; Chandra 2004).

4.52 It is common for members of the donor community to state that governance outcomes (transparency, accountability, separation of private interest from public office, and so on) are not ends in themselves, but rather the means to achieving positive development outcomes. Thus while they may be the ideal, there now seems to be greater tolerance for governance reforms that are more country-specific and that take account of
the unique circumstances and conditions different countries face—a move away from a “best-practice” to a “good-enough” perspective on governance (Grindle 2004; Carothers 2002). The timelines of these types of efforts may be too short for thorough evaluation. However, some adverse implications of, for example, tolerating rents, allowing low-level corruption to persist, or permitting the limited distribution of public goods, offices, works projects, or tax breaks in return for loyalty within the context of World Bank-supported programs should assessed.
5. INTEGRATING POLITICAL ECONOMY IN BANK OPERATIONS

5.1 This section examines the extent to which political analysis has been mainstreamed into World Bank operations. It focuses on two questions: (i) the extent to which World Bank projects demonstrate greater use of political analysis in either the project preparation or implementation phase (and, more importantly, how this usage has changed since 2007); and (ii) how World Bank operational staff perceive the relevance of political economic analysis in their work. Two surveys implemented for the GAC evaluation are used here: an intensive review of World Bank project documents, and a survey of operational staff.

Political and Institutional Analysis: Evidence from a Review of Projects

5.2 A review of 200 World Bank projects approved between June 2004 and October 2010 was conducted based on the methodology detailed in the approach paper of the IEG GAC Evaluation.

5.3 The use of formal and informal political-institutional analysis in projects is high, and has not changed significantly between pre-GAC and post-GAC periods. Table 5.1 shows the percentages of project documents that use formal or informal PEA. The majority of projects (greater than 90 percent) reviewed are based on analysis of formal factors (organizational structures, decision-making rules, staff skills and capacity of implementation arrangements, accountability and disclosure mechanisms) or informal factors (history, culture, informal or social relationships, election processes, rent seeking, and so on). By far the most common analytical tool is of formal institutions, with 80–90 percent of projects incorporating this tool, while the rarest is some analysis of electoral cycles. Meanwhile, more than 85 percent of governance and political-economic analyses in projects are based on some form of ESW.
Table 5.1: Use of Political Analysis in Projects (Pre- and Post-GAC Averages)

<table>
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<tr>
<th>Institutional Analysis (formal or informal)</th>
<th>Pre-GAC</th>
<th>Post-GAC</th>
<th>p &lt; χ²</th>
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<tr>
<td>Formal institutions</td>
<td>82.5</td>
<td>90.0</td>
<td>(0.140)</td>
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<tr>
<td>Relevant historical legacies</td>
<td>49.2</td>
<td>62.5</td>
<td>(0.064)</td>
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<td>Cultural practices, norms, or other traditions</td>
<td>35.8</td>
<td>27.5</td>
<td>(0.218)</td>
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<td>Informal relations among different levels of government</td>
<td>36.0</td>
<td>36.3</td>
<td>(0.355)</td>
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<tr>
<td>Social, regional, ethnic, religious, or linguistic relations</td>
<td>40.8</td>
<td>38.8</td>
<td>(0.768)</td>
</tr>
<tr>
<td>Electioneering and/or electoral cycles</td>
<td>14.2</td>
<td>13.8</td>
<td>(0.934)</td>
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<tr>
<td>Rent-seeking</td>
<td>25.8</td>
<td>36.3</td>
<td>(0.115)</td>
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<td>Other</td>
<td>15.0</td>
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<tr>
<td>Any institutional analysis</td>
<td>92.5</td>
<td>93.8</td>
<td>(0.734)</td>
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<td>31.3</td>
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<td>Poverty and Social Impact Assessment</td>
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<td>Country Economic Memorandum</td>
<td>15.8</td>
<td>18.8</td>
<td>(0.591)</td>
</tr>
<tr>
<td>Institutional Governance Review</td>
<td>9.2</td>
<td>7.5</td>
<td>(0.679)</td>
</tr>
<tr>
<td>Technical Assistance</td>
<td>50.0</td>
<td>48.8</td>
<td>(0.862)</td>
</tr>
<tr>
<td>Political Economy Assessment (PEA)</td>
<td>0.8</td>
<td>1.3</td>
<td>(0.772)</td>
</tr>
<tr>
<td>Other</td>
<td>63.3</td>
<td>68.8</td>
<td>(0.430)</td>
</tr>
<tr>
<td>Any ESW</td>
<td>85.0</td>
<td>88.8</td>
<td>(0.447)</td>
</tr>
</tbody>
</table>

Note: Pre-GAC and Post-GAC columns show percentages of projects that utilize specific types of analysis. p values are from Chi-squared tests of independence.

5.4 As table 5.1 shows, however, there is little significant change before and after the implementation of the GAC Strategy; only the use of historical analysis and Poverty and Social Impact Assessments (PSIA) has increased significantly between the pre-GAC and post-GAC periods.

Figure 5.1: Distributions of Analytical Tools Usage for Projects

Sources: Project Review, IEG-GAC evaluation.
5.5 The total usage of analytical tools by project, similarly, shows little pre- vs. post-GAC period difference. Figure 5.1 shows the distribution of formal and informal institutional analyses in projects, and the use of ESW, according to pre- and post-GAC periods (the horizontal axes are simply a cumulative score of the number of analytical tools or ESW used in projects based on the table above; both range from zero to eight). As the graph shows, the averages of the distributions change little before and after the GAC Strategy implementation. The average number of political-institutional analytical tools incorporated in projects before and after shifts slightly from 2.9 to 3.2. The average number of ESW increases from 2.2 to 2.5.

5.6 It is important to note that the purpose of incorporating political-analytical tools in projects is to improve design of programs—“smarter” design, whereby project implementing arrangements are robust to political-economic realities (World Bank 2009a). Project reviews examined the extent to which project design responded to GAC constraints depending upon, among other things, whether projects were adjusted to take into account “informal/actual reality.” Reviews classified program response depending on whether the response was “to a great extent,” “somewhat,” or “not at all.” Based on these responses, it is possible to categorize projects in terms of their design responsiveness to political realities, and to measure the relationship between this responsiveness and the usage of analytical tools. Figures 5.2 and 5.3 depict these relationships graphically.

**Figure 5.2: Distributions of Analytical Tools Usage by GAC Responsiveness**

5.7 Projects that were judged to be highly responsive to political realities utilized political-economic analytical tools to a greater extent than those projects that were considered either moderately responsive or non-responsive. Figure 5.2 shows significant differences between responsive and non-responsive projects in terms of their usage of analytical tools. For example, more than 50 percent of moderately responsive and approximately 80 percent of highly responsive projects used three or more political-institutional analytical tools. By contrast, less than 6 percent of non-responsive projects used more than three tools. Similarly, 60 percent of moderately responsive projects and
80 percent of highly responsive projects used two or more ESW to inform governance and political-economic analyses, and less than 6 percent of non-responsive projects did.

5.8 However, this relationship between the usage of analytical tools in political economy and the governance responsiveness of project design is not new. Indeed, the project reviews show only slight differences between pre- and post-GAC periods. Figure 5.3 examines distribution of analytical tools for only those projects deemed to be highly GAC responsive. There is a slight right-ward shift for ESW reliance post-GAC, suggesting that highly GAC-responsive projects were more likely to use a greater number of ESW after the GAC Strategy than before, but the difference in means is not statistically significant.

**Figure 5.3: Pre-GAC versus Post-GAC Distributions for Highly GAC-Responsive Projects**

Sources: Project Review, IEG-GAC evaluation.

5.9 In sum, project reviews indicate that GAC responsiveness in projects is positively influenced by the extent to which political-economic analytical tools—either in the form of institutional analyses or ESW—are drawn upon in project design. But the GAC “design-responsiveness” effect does not show any significant change before and after 2007.

**Evidence from a Staff Survey**

5.10 To assess perceptions among World Bank operational staff, a staff survey was conducted electronically among approximately 700 staff in regional units, and following the sampling methodology described in the GAC Evaluation Report.

5.11 The first relevant question concerns staff self-assessments of competence in and the quality of PEA both relative to the pre-GAC period, and relative to other donors. World Bank operational staff members rate both highly, with majorities reporting that their “country team” has improved political-economy assessments relative to pre-2007,
and that their team does a better job in political-economy and governance assessment than other donors. Table 5.2 shows summary results.

**Table 5.2: Self-Assessments of Political-Economy Competence (percent of responses)**

<table>
<thead>
<tr>
<th>Assessment</th>
<th>Better</th>
<th>Same</th>
<th>Worse</th>
<th>DK</th>
</tr>
</thead>
<tbody>
<tr>
<td>Assessing governance and/or political economy constraints now relative to pre-2007</td>
<td>57.7</td>
<td>29.3</td>
<td>2.6</td>
<td>10.4</td>
</tr>
<tr>
<td>Assessing political-economic constraints relative to other donors</td>
<td>63.3</td>
<td>22.8</td>
<td>3.6</td>
<td>10.4</td>
</tr>
<tr>
<td>Assessing and managing risk relative to other donors</td>
<td>71.9</td>
<td>16.0</td>
<td>3.1</td>
<td>9.0</td>
</tr>
</tbody>
</table>

*Sources: Staff survey, IEG-GAC evaluation.*

5.12 The next question is whether this competence has contributed to improved results. Staff were asked to rate whether the Bank’s country program had achieved results in the following areas: improving service delivery, improving the investment climate, strengthening domestic accountability, and increasing “candor and transparency in the Bank’s engagement with the client.”

5.13 Table 5.3 lists response percentages disaggregated into whether the respondent considered their team’s competence in governance political-economy assessments to have improved or not improved (including worsened) since 2007. As the table shows, staff holding a favorable opinion of their team’s basic political-economy competence were also more likely to believe that their programs had achieved results. In the case of service delivery, almost three times as many respondents who thought their political-economy abilities had improved through their program had achieved results relative to those who saw no improvement in their competence. Results are similar when broken down against those who consider their political-economy competence to be better than that of other donors.
Table 5.3: Program Results by Political-Economy Competence in Country Teams

<table>
<thead>
<tr>
<th></th>
<th>Improved</th>
<th>Same/Worse</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Service Delivery:</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Achieved results</td>
<td>70.4</td>
<td>26.8</td>
</tr>
<tr>
<td>Did not achieve results</td>
<td>25.7</td>
<td>65.5</td>
</tr>
<tr>
<td><strong>Investment Climate:</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Achieved results</td>
<td>54.8</td>
<td>27.9</td>
</tr>
<tr>
<td>Did not achieve results</td>
<td>36.3</td>
<td>63.2</td>
</tr>
<tr>
<td><strong>Domestic Accountability:</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Achieved results</td>
<td>51.4</td>
<td>43.6</td>
</tr>
<tr>
<td>Did not achieve results</td>
<td>43.6</td>
<td>70.3</td>
</tr>
<tr>
<td><strong>Transparency:</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Achieved results</td>
<td>67.8</td>
<td>36.8</td>
</tr>
<tr>
<td>Did not achieve results</td>
<td>29.2</td>
<td>59.7</td>
</tr>
</tbody>
</table>

*Sources: Staff survey, IEG-GAC evaluation.*

5.14 The breakdown of political-economy competence by regional unit (figure 5.4) shows some interesting patterns. In the Middle East and North Africa and in the South Asia units, the percentages who consider their teams’ competence in governance and political-economy analysis to have improved are considerably lower than in Latin America, Europe/Central Asia, East Asia, and Sub-Saharan Africa. By contrast, large majorities across regions consider their political-economy skills to be superior to that of other donors.

Figure 5.4: Staff Self-Assessments of Political-Economy Competence by Region

*Sources: Staff survey, IEG-GAC evaluation.*

5.15 Moreover, the staff survey shows that operational staff are relatively self-reliant in conducting political-economy assessments—generally using guidance materials, toolkits, sourcebooks, and other informational resources only on a limited basis compared to other GAC-related resources. Although 30 percent of operational staff considered various political-economy sourcebooks to be highly or moderately “directly relevant” to their
operational GAC work, only slightly more than 20 percent of respondents had actually used these sources of guidance—the lowest percent among five categories of source material (including GAC-in-country guidance, GAC-in-sector guidance, GAC-in-project guidance, and demand-for-good-governance guidance). Additionally, almost 60 percent are unfamiliar with, or report no intention to use PECoP products.
6. CONCLUSIONS

Consistency, Coverage, and Relevance

6.1 Political analysis was and is thinly and inconsistently applied. This review found a large variability in the use of PEA both before and after the elaboration of the GAC Strategy. A review of projects showed little change in the use of formal or informal institutional or political analysis to inform governance strategies or approaches. Moreover, specialized or “stand-alone” PEAs were the least-likely analytical product to be used to inform GAC issues, with approximately 1 percent of projects utilizing political economy assessments. Finally, political-economy guidance was the least likely to be used by operational staff relative to other source material.

6.2 High standards of quality and methodological rigor yield more useful political diagnoses. In addition to consistency, the rigor and quality of political analysis was also uneven, partly as a result of the lack of a common definition of what constituted “political economy.” Although some diversity of approaches may be desirable to inform a broad set of relevant issues, this has also inevitably led to outputs of variable quality. In integrating multiple perspectives and methodologies, the various toolkits, training, and assessments lacked consistency and were of limited use in country operations. Approaches to political economy ranged from general mappings of stakeholders, to assessments of formal and informal institutions, to analyses of “politics” writ large. Outputs that provided the greatest operational relevance, by contrast, were typically more rigorous in terms of methodology, for example, formal analyses of institutional reforms, simulations of the incentives of bureaucrats and politicians involved in Bank operations, or careful assessments of program impact using relevant data such as focused public-opinion surveys.

6.3 Better operational, sector- and project-level political-economy guidelines are needed. Although opinion was divided, over 30 percent of country staff surveyed did not find political and PEA to be operational relevant. More sophistication is needed in the design of instruments and tools used in World Bank-supported programs, taking into account both the political constraints in countries, sectors, and projects, as well as the possible unintended consequences. It is likely that the implementation of the next phases of the GAC Strategy combined with the imperatives contained in the ORAF will further deepen and mainstream political analysis and diagnosis. In some areas, recent analytical work (both PEA inputs and ESW reviewed) has adjusted recommendations based on assessments of political feasibility, for example, in tolerating rents that may be politically valuable to keep key constituencies happy or to co-opt opponents, or to avoid the “independent-agency” approach to policy making where institutional weaknesses are rife, and so on. Yet many of the solutions proposed are similar to those suggested in the World Bank’s 2000 Governance Strategy, and in the PRSP Sourcebook: consultative policy making, checks and balances to central authority, and a premium on information sharing and access. If correct, then the gap between political-economic diagnosis and operational solutions will continue to widen. New rationales will mean better-informed political analysis in all aspects of World Bank analytical work and in operations, but it
will also require highly innovative solutions to operational problems given these political constraints—solutions which, thus far, have not been widely forthcoming.

Mainstreaming

6.4 **The utilization of free-standing, political-economy assessments by country teams is likely to be slow.** Many of the types of stand-alone political-economy outputs that would eventually constitute, for example, the PECoP menu of products have been financed through incremental funding, buttressed by increased Bank and donor spending on governance work, a trend that preceded the launch of the 2007 GAC Strategy. This review concludes that, while these specialized political analyses may be necessary to country teams in some cases, the development of a separate analytical product line (analogous to IGRs or CEMs) purely devoted to political-economy analyses is unlikely to lead to significant “mainstreaming” of political analysis in Bank operations. This is evidence that the PECoP has faced some difficulties in generating demand for these products, even after receiving seed money. Even with significant improvements in the quality, rigor, and operational relevance of these products, the tight-budget concerns that characterize the current Bank environment combined with the lack of awareness of these tools suggests that demand will increase slowly. After GAC financing ends, the current political-economic assessment effort may face challenges in stimulating demand.

6.5 **Far more promising is the practice of providing political-economy “inputs” to ESW (or CAS).** This review concludes that, while there has been no significant improvement in the quality and coverage of political-economic issues in ESW since 2004, high-quality “embedded” forms of political analysis often carried a great deal of weight, impact, and value-added in Bank operations. In some cases, (for example, Haiti) they opened dialogues between the Bank and the borrower on relevant GAC reforms. In other cases, where they may not have shaped reforms, they highlighted underlying political drivers of GAC problems (for example, in Nicaragua and Indonesia). Alternative approaches to mainstreaming political economy could include a more systematic peer review of standard economic and sector work for political-economic analytical content, along with the development of project-level political-economic decision tools.

6.6 **However, the gap between the perspectives of political-economy experts and of operational staff remains wide.** Thus far, the main approach of the PECoP has been to build up a roster of in-house experts and to maintain a similar roster of consultants with the requisite skills and knowledge of the politics of countries and sectors, as well as those with more general skills, as well as to advertise its product lines to country teams. This has contributed to a wider awareness of the importance of the political constraints to the World Bank’s activities in client countries. The staff survey, however, showed that most respondents did not believe that political-economic guidance and support had been provided in a user-friendly way. The PECoP can serve as more than a mere clearinghouse, providing World Bank country teams with guidance on how to involve country partners in the initiation, preparation, and dissemination of political-economy assessments. Moreover, the PECoP can function as a source of continuous guidance and training for country teams and task leaders themselves, and thereby help in
mainstreaming and integrating PEA within project design, to ensure that operational staff are conversant with the main dimensions of political analysis, and that political aspects of operational risk are adequately highlighted and addressed. Mainstreaming political analysis into World Bank analytical work and operations can be more systematically undertaken, involving the PECoP, but also creating incentives for operational staff to more fully integrate political-economic assessments into their work.

**The Uses of Political Economic Analysis**

6.7 **Recommendations of political analyses tend to be highly conventional.** Although political-economic analyses (both as specialized political assessments and in ESW) expanded the Bank’s knowledge of political and institutional constraints to project outcomes, most analyses proposed solutions closely related to those elaborated in the 2000 governance strategy, or in the *PRSP Sourcebook*, focusing on inclusive policy making, the need for checks and balances on executive authority, and transparent decision making. Moreover, in recent years, a number of governance reforms that have been devised while taking account of political constraints and “goodness of fit” have been enthusiastically embraced by the World Bank—as well as the donor community. The possibilities for unintended consequences of these reforms, however, are potentially large, and are often left under-investigated, for example, in the case of decentralization, pro-poor empowerment, or tolerance of limited rent-seeking, each of which can worsen problems of governance. What appeared to be “good fit” ex ante might not be considered to be ex-post if it failed to produce desired results.

6.8 This review also found that political analyses ignored the role of donors. In particular, political analyses were rarely explicit about the political economy of aid in borrower countries, and in particular, in aid-dependent countries. Analytical work that recommended solutions to problems of poor governance ignored the implications of changes in donor exposure in these countries, of restructuring lending instruments used, as well as of the tolerance for risk in countries given political circumstances or equilibria. Analytical work also failed to recognize the “politics of aid” in aid recipients, in particular, how the World Bank’s own lending decisions may have influenced past policy decisions, reforms, or other actions. Unlike that of other donors (such as SIDA and GTZ), World Bank political analysis did not explicitly address its own role or that of other donors in shaping incentives in sectors and countries.

6.9 **There is little downstream political-economy support.** Currently, most political-economic analytical work is focused primarily on upstream project design. World Bank operations would benefit, as a result, from political-economic assessments informing evaluations of program effectiveness, particularly as they relate to institution-strengthening and sustainability given political conditions. Additionally, impact evaluation initiatives could consider political-economic outcomes as worthy of evaluation. For programs that incorporate political-economic elements in their design, such as participation (especially in CDD programs), accountability, social capital-building, and so on, such political-economic evaluations could explicitly examine the impact of interventions on these behaviors.
REFERENCES


