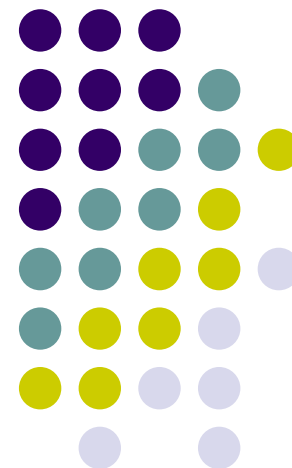


Evolution of Public investment in transition economies: Belarus country case study

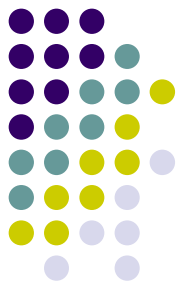


Junghun Cho
World Bank
Seoul, Korea
November, 2008

Common institutional weaknesses of PFM system in transition economy

	Organizational Structure	Incentives
Legislative budget formulation	Structure of legislative not conducive for budget formulation No independent analytical capacity	Political incentive to increase expenditure
Executive budget formulation	Fragmented control over budget formulation process Weak budget formulation and analysis capacity, often based on inertia of historical norms Lack of necessary budget-related data	Conflicting incentives cause poor coordination between central budget authority and spending units
Budget execution	Absence of effective financial management information system Lack of effective control at the commitment stage	Spending units seek and find avenues to allocate additional resources in excess of budget plan
Budget performance	Absence of effective external controls and performance measures	Spending units benefit from limited transparency and lack of accountability

Source: budgeting and fiscal management in transition economies, Martinez-Vazquez, Boex

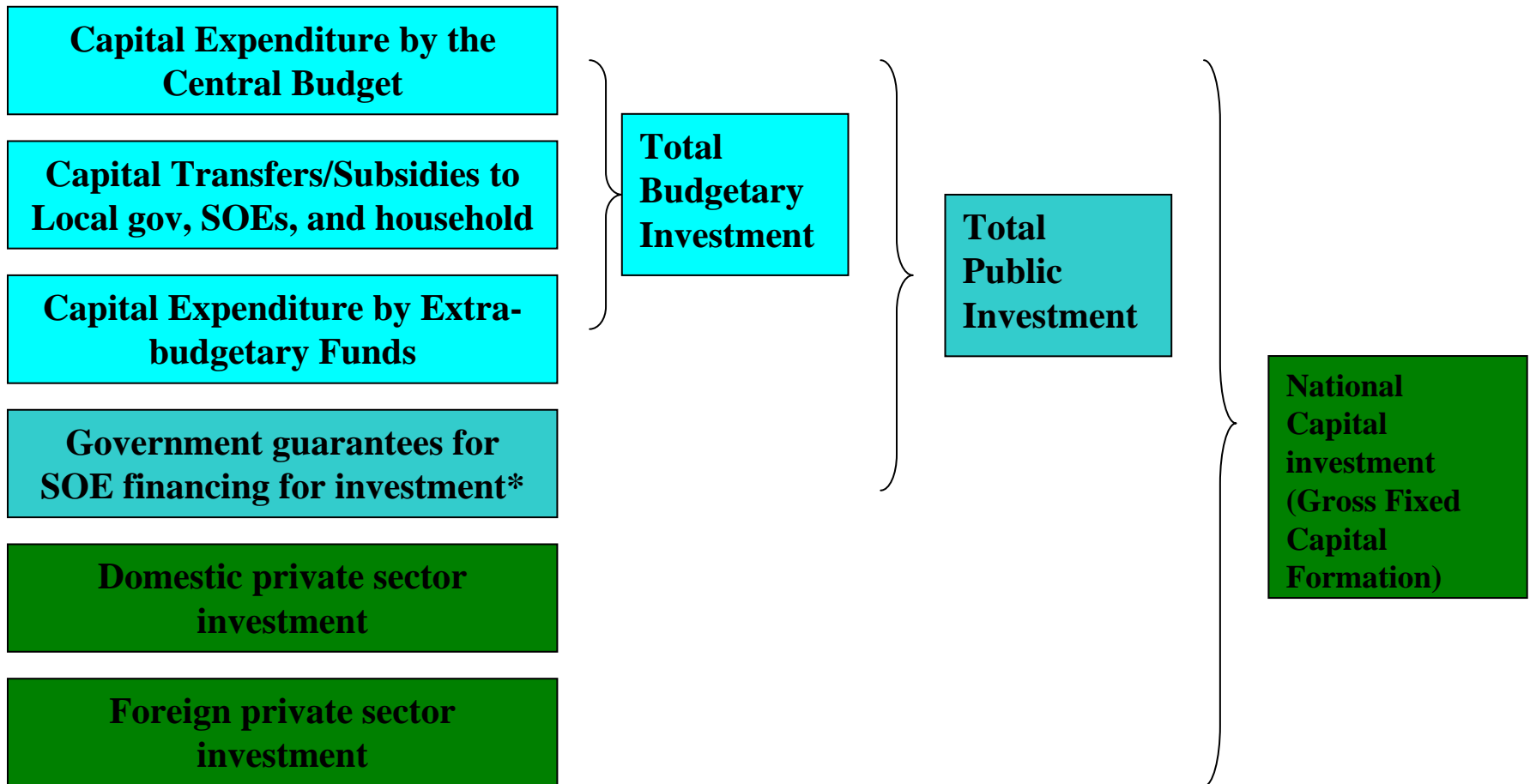


1. What is Public Investment?

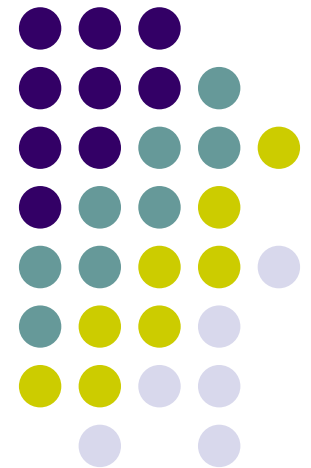
1. Un-bundling Public Investment: National capital investment?



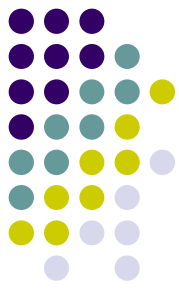
public investment ? or budgetary investment ?



The Case of Belarus



Public Investment in Belarus: “A Solid Foundation...but with Weighty Challenges”



- Public investment in Belarus has been integral to the national economic development
- A number of good practices in project preparation and execution— A solid budgetary basics in place
- Need to develop a comprehensive public investment strategy with a medium perspective
- Need to integrate currently separate procedures for public investment
- Require a strong commitment from the top-leadership and realistic and sequenced implementation plan.

Snapshot of Belarus Capital Expenditure

	2004	2005	2006
		<i>in % of GDP</i>	
Consolidated budget	4.2	6.0	6.4
Extra budgetary funds	1.4	0.0	0.1
Total budgetary investment	5.6	6.0	6.5
SOE Guaranteed External Financing	2.9	3.2	4.1
Total public capital investment	8.5	9.2	10.6
Enterprises and organizations	9.9	10.7	10.6
Households	1.8	1.8	1.8
Total Domestic Capital Investment	20.2	21.7	23.0
Foreign investment (incl. foreign bank loans)	0.8	0.6	0.5
Other sources	0.6	0.8	0.8
Total Capital Investment	21.6	23.1	24.3

How much and how effectively resources were spent on building capital stocks?





Total Amount of Public Spending on capital stock building:

“Stands highest among neighboring countries”

Figure 1a: Capital expenditures in Belarus (in % GDP)

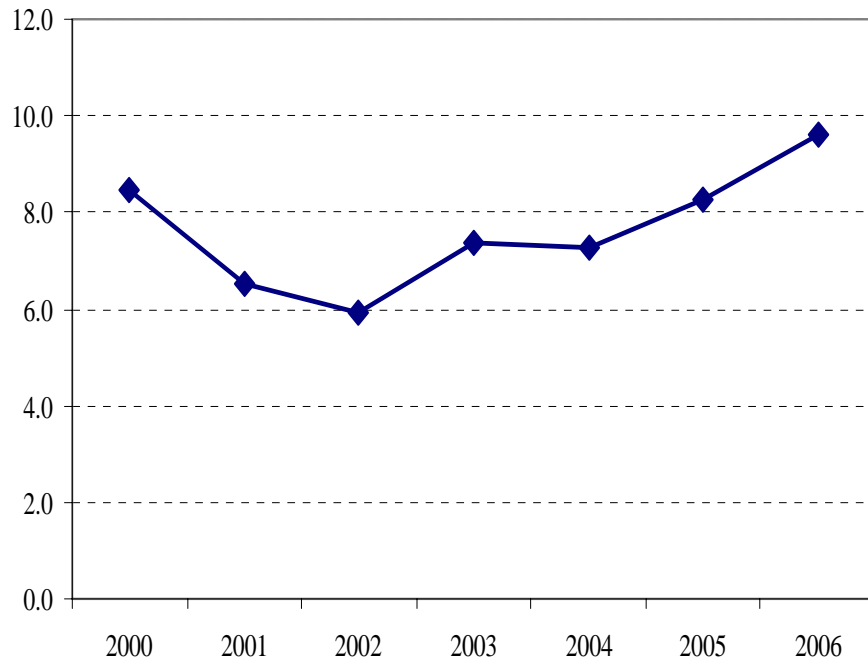
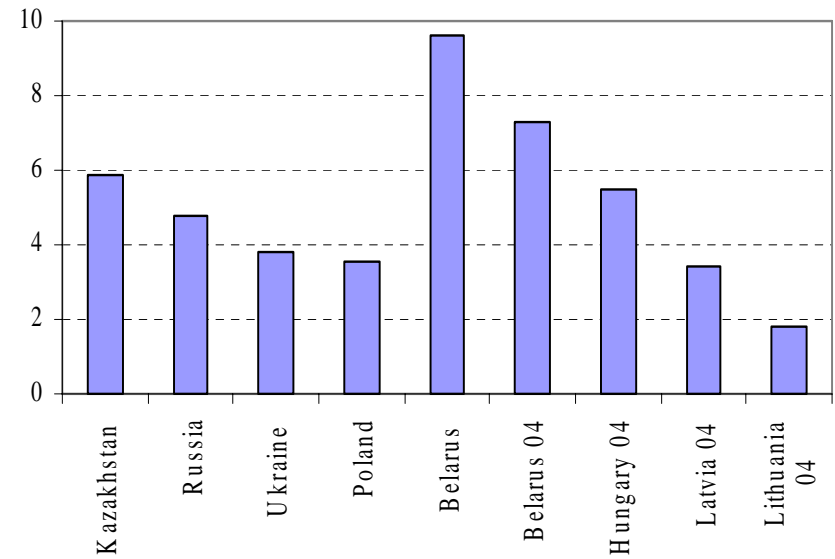
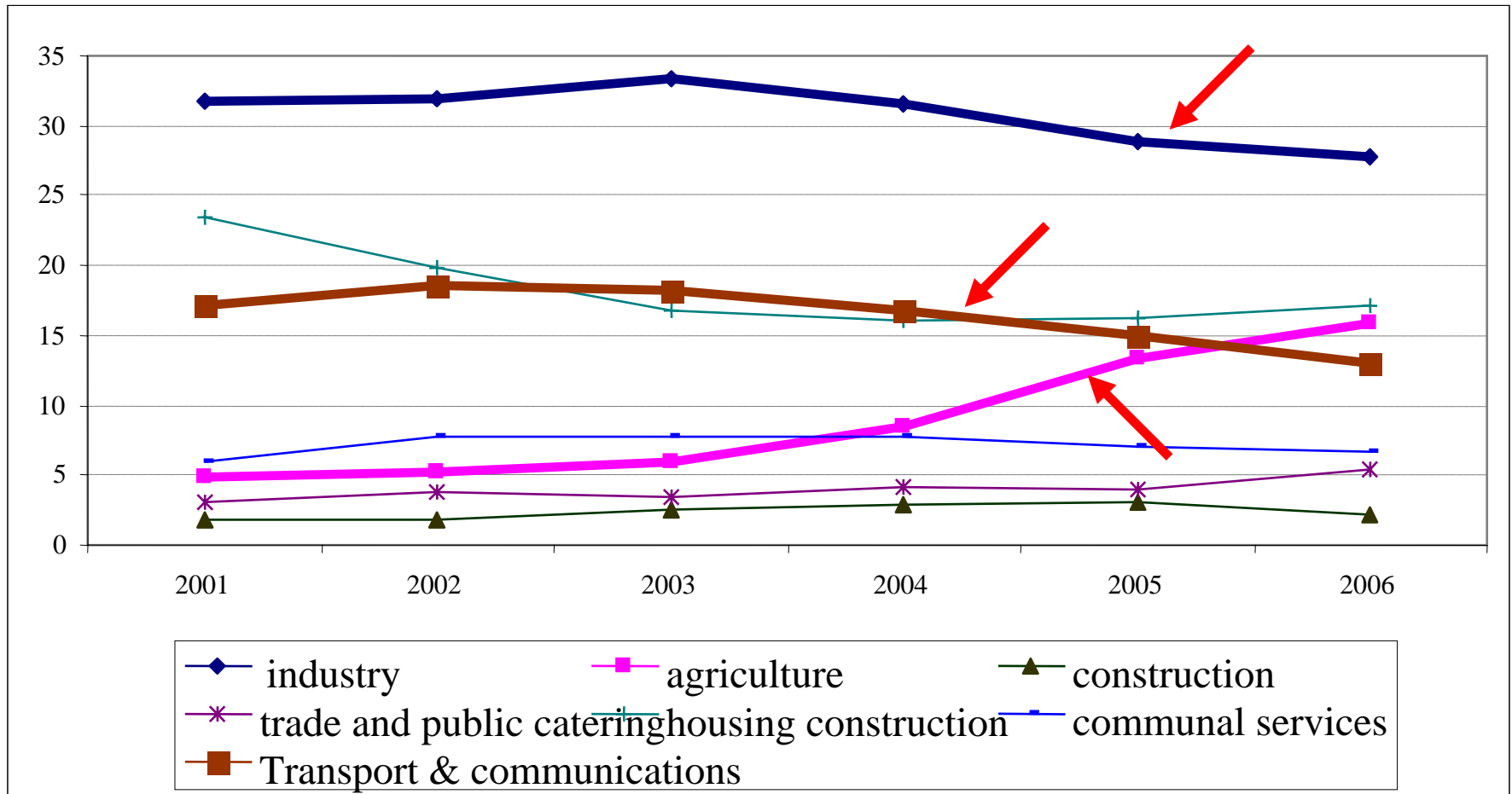
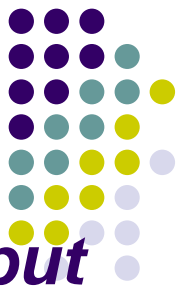


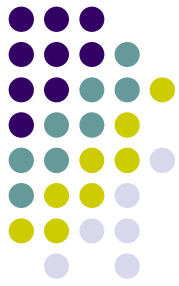
Figure 1b: Capital Expenditures in Belarus and Selected Countries (in % GDP, in 2005 unless otherwise is stated)



A Noticeable Sectoral Trend in Total National Investment :

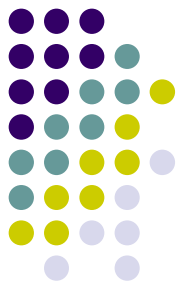
“Broadly consistent with national priority shift but debatable priorities for economic development”





The Issues of Capital Expenditure:

Structure of Capital Expenditure



- Relatively large share of capital transfers to various entities

	Belarus	Russia	Lithuania	Ukraine
Net acquisition of non-capital assets	86.4%	99.8%	94.9%	61.3%
Capital transfer to other levels of governments	0.0%	0.0%	0.0%	6.6%
Other Capital transfers to state enterprises and organizations, financial institutions, individual citizens, and other transfers within the country	13.5%	1.2%	5.1%	32.1%
Total Capital Expenditure	100.0%	100.0%	100.0%	100.0%



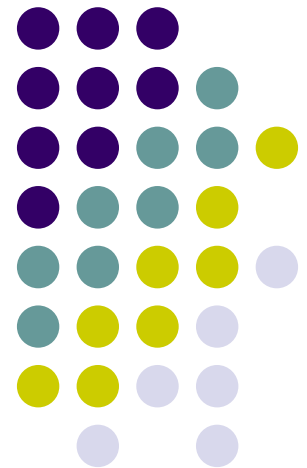
Proliferation of Earmarked Funds (EMFs)

- About 40% of capital expenditure earmarked
- Severely undermines budgeting principle of competition and strategic allocation
- Innovation Fund(s) (2% of GDP): debatable rationale and management

Total number of EMFs	9
As % of total expenditure (FY 2006)	17.2%
As % of total public capital expenditure	42.3%
Average age of EMFs	10.2 years

Institutional Arrangement to Support effective public investment :

***Sound Mechanism for
Operational Efficiency but
Insufficient Strategic
Orientation***



Capital Programming Cycle

Planning

- Strategic & Program Performance Linkage
- Baseline Assessment
- Functional Requirements
- Alternatives to Capital Assets
- Choosing the Best Capital Asset
- The Agency Capital Plan

Management In Use

- Operational Analysis
- Execution of Operation and Maintenance Plan
- Post-Implementation Evaluation
- Execution of Asset Disposal Plan

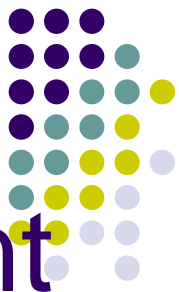
Procurement

- Validate Planning Decision
- Manage the Procurement Risk
- Consider Tools
- Select Pricing Mechanism
- Issue the Solicitation
- Proposal Evaluation & Negotiation
- Contract Award
- Contract Management
- Acquisition Analysis
- Acceptance

Budgeting

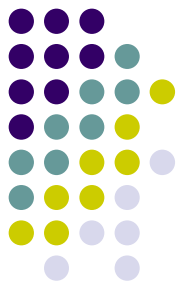
- Agency Submission
- Passback
- Agency Revision
- Approved for President's Budget
- Congressional Approval and OMB Apportionment

Source: US Office of Management and Budget



Q1: Is Public Investment
Prepared through a
Comprehensive and Strategic
Approach?

Existing plans lack comprehensiveness and medium term perspective



- Strong political directive for sectoral budgetary decision, particularly, public investment decision
- Program for Economic and Social Development, but only at aggregate level without sectoral discussion
- Separate investment plan for social and real sector; the State Investment Plan (SIP) and a so-called Priority Project List
- Line ministries' sectoral capital investment plans exist, but actual capital spending has often deviated from the plan
- A large share of earmarked revenue for special purposes, which undermines strategic orientation and responsiveness
- Own-source funded capital projects are included neither in the SIP nor in the consolidated budget



**Q 2: Is Public Investment
Planning and Preparation
Consistent and Efficient?**

Budgetary basics in place for further improvement



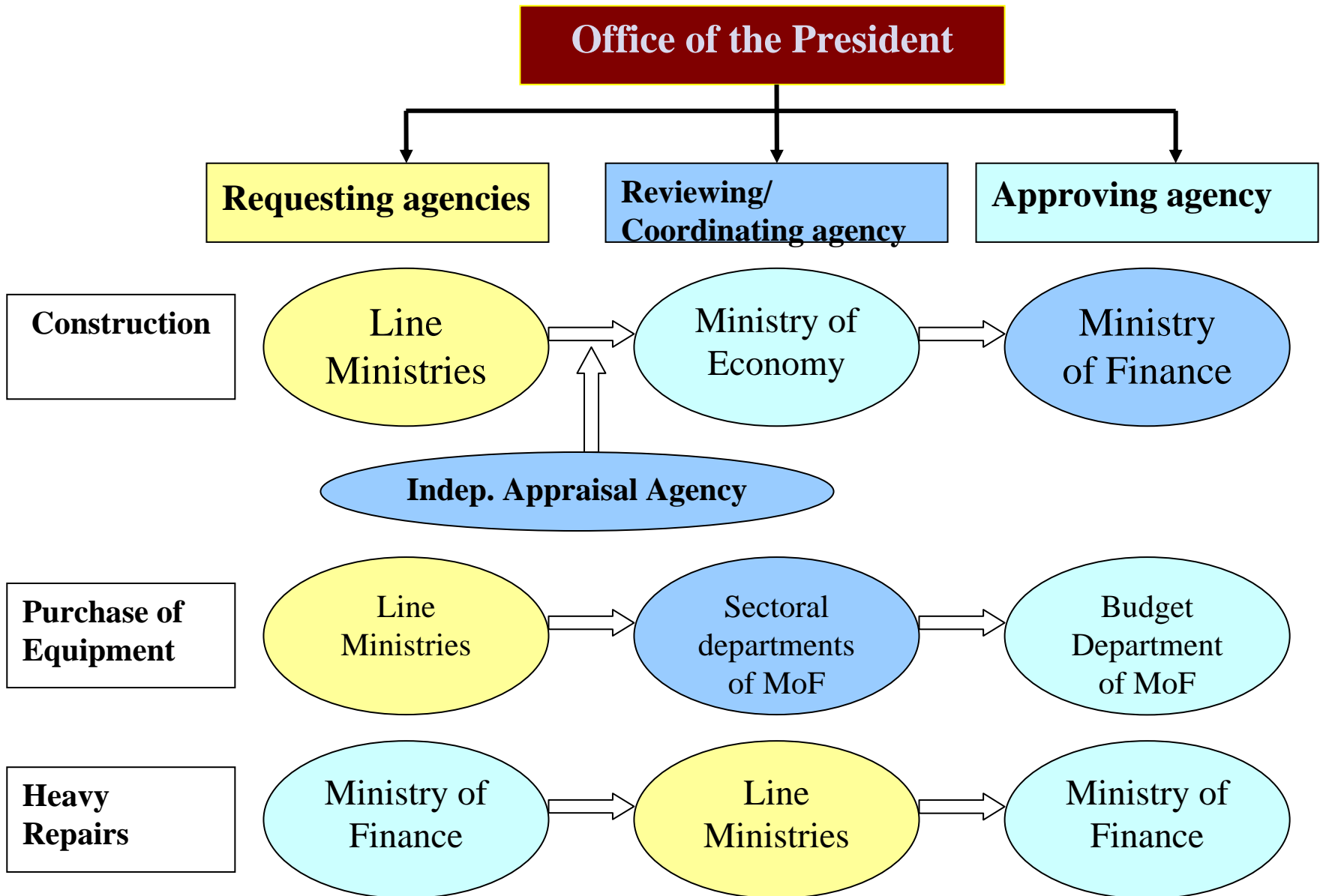
- **High level of operational efficiency**

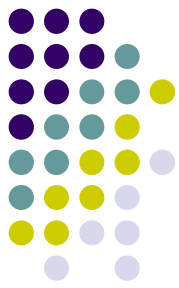
from rigorous technical and financial project for construction projects (e.g., Independent Appraisal Agency)

- **Low level of allocative effectiveness & medium-term perspective**

from different procedures and institutional arrangement for different items (e.g., purchase, construction, and heavy maintenance) and earmarking practices

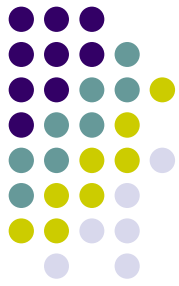
Stylized Processes for Public Investment Preparation





Q 3: Is the Current Public
Investment Portfolio
Rationalized?

Number and Size of Project Allocations in State Investment Program



“Too large number of small projects at the bottom”

	Unit	2006 Budget	2007 Budget
Number of Projects	No	495	598
Average Size of Project Allocation			
	Mean (BYR)	million	1881.6
	Median	million	428.3
Share of total capital budget			
	100 largest projects	%	71.4%
	200 smallest projects	%	2.0%

Potential Steps to rationalize public investment projects



- Identifying and reclassifying maintenance spending that is currently shown in the Budget as capital investment
- Consolidating the large number of small investment allocations within fewer and larger projects.
- Reviewing the investment portfolio to identify those projects that are either not consistent with the sectoral strategic priorities or no longer to be technically or economically viable
- Make recommendations for the redesign or discontinuation of specific investment projects



**Q4: Is Project Implementation
Efficient and Monitoring and
Evaluation System Strong?**

Highly efficient execution system but with little information regarding performance



- Close to full execution of capital expenditure:
A strong indicator for operational efficiency
- Well established accounting and reporting for financial information

	2005	2006
Belarus	97.7%	127.3%
Ukraine	84%	80%
Latvia	87%	88%
Poland	98%	94%

- Little collection and use of performance-related information in resource allocation : a potential obstacle for the proposed program budgeting

Areas	Recommended Activities
Comprehensive and Strategic Approach to Public Investment Management	Develop a comprehensive multi-year national investment strategy that could guide the proposed medium-term expenditure framework
	Bring all remaining off budget funds into budget
	Set up a timetable to fully incorporate the earmarked funds into the budget based on their rationale and age profile
Project Preparation, Appraisal, and Selection	Streamline project preparation processes for different types of capital investment
	Review and revise the roles of the Ministry of Economy and the Ministry of Finance
Project Implementation and Monitoring	Review and rationalize existing capital project portfolio
	Begin monitoring basic performance information of major projects and gradually roll out into other projects that as a part of the proposed program-based budgeting efforts
Other issues	Review and Streamline a regulatory framework for public investment, which deems overly complex
	Reclassify budget classification and chart of accounts according the international standard

Thank you

