

# **Public Sector Reform in Developing Countries**

## **Issues, Lessons and Future Directions**

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## A. What is “Public Sector Reform”

Public sector reform (PSR)<sup>1</sup> is about strengthening the way that the public sector is managed. The public sector may be overextended – attempting to do too much with too few resources. It may be poorly organized; its decision-making processes may be irrational; staff may be mismanaged; accountability may be weak; public programs may be poorly designed and public services poorly delivered. PSR is the attempt to *fix* these problems.<sup>2</sup>

## B. What is “Government” and Why Does it Exist?

There are three branches of government: legislative, executive and judicial:

- The *legislature* (often referred to as a “parliament” or “national assembly” or “congress”) has exclusive authority to enact laws.
- The *judiciary* is the system of courts of law.
- The *executive* implements the government’s policies. It normally consists of the political leadership – the president or prime minister and his or her cabinet ministers – and a set of public “departments” or “ministries” or “agencies” whose staff is on the public payroll and which report, ultimately to a cabinet minister.

### “Public Sector”

The “public sector” is broadly synonymous with “government”. In this paper, we focus on the executive branch. From that perspective, the public sector is made up mainly of government departments and agencies that are staffed by public servants.

### Why Do Governments Exist?

There are certain goods and services that all citizens value – defense, diplomacy, law and order, property rights, parks, street lighting, public sanitation, pest control, public health, to name a few – which market forces, on their own, would either under-provide or not provide at all. Economists refer to these as “public goods.” Only governments can be relied upon to provide them in quantities and at a quality demanded by society.

Beyond government’s undisputed role as a provider of public goods, there are controversial questions about the economic and social role of the public sector. Opinions are (and always will be) divided on how active and influential a participant government should be in a country’s economic and social life. How much industrial output should be produced by the public sector? How should the government regulate the private sector? How should it address economic inequality? How should it pursue a range of issues related to social justice, environmental protection, etc? The way that countries deal with these questions has an

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<sup>1</sup> The term “civil service reform” (CSR) is also commonly used. CSR is one element of PSR.

<sup>2</sup> Our discussion of PSR does not cover the military or state-owned enterprises. We also do not address public financial management (PFM), a topic closely linked to PSM and sharing many common issues. A useful overview of PFM in developing countries is found in World Bank (1998) and Schick (1998).

impact on the appropriate size, role, functions and structure of the public sector.

### C. What Does the Public Sector Look Like?

Figure 1 provides a generic model of the public sector (executive branch). The entire public sector reports ultimately to the *head of state*, although its day-to-day operation is normally the responsibility of the *head of government*. In some countries, the heads of state and government are combined in one office (e.g. the President of the United States). In other countries, the two positions are distinct, with the head of state limited to a ceremonial role (e.g. in Canada where the Prime Minister is head of government and the Governor General is the ceremonial head of state). In still other countries – France and its former colonies, for example – both the head of state (President) and head of government (Prime Minister) play substantive political and policy roles.

The head of government governs with the advice of his *cabinet*, which is made up, for the most part, of the political heads (often referred to as “Ministers” or “Secretaries”) of government departments (see below). Cabinet has both a political and a policy/managerial function. Cabinet is the country’s most powerful political institution – a forum where the country’s top political officers address, away from public scrutiny, matters related to advancing the government’s political agenda, managing political opposition, etc. It also serves a more technical, policy/managerial function because cabinet ministers are also the heads of government departments. Cabinet is therefore a forum for addressing major policy issues that arise in particular government portfolios.

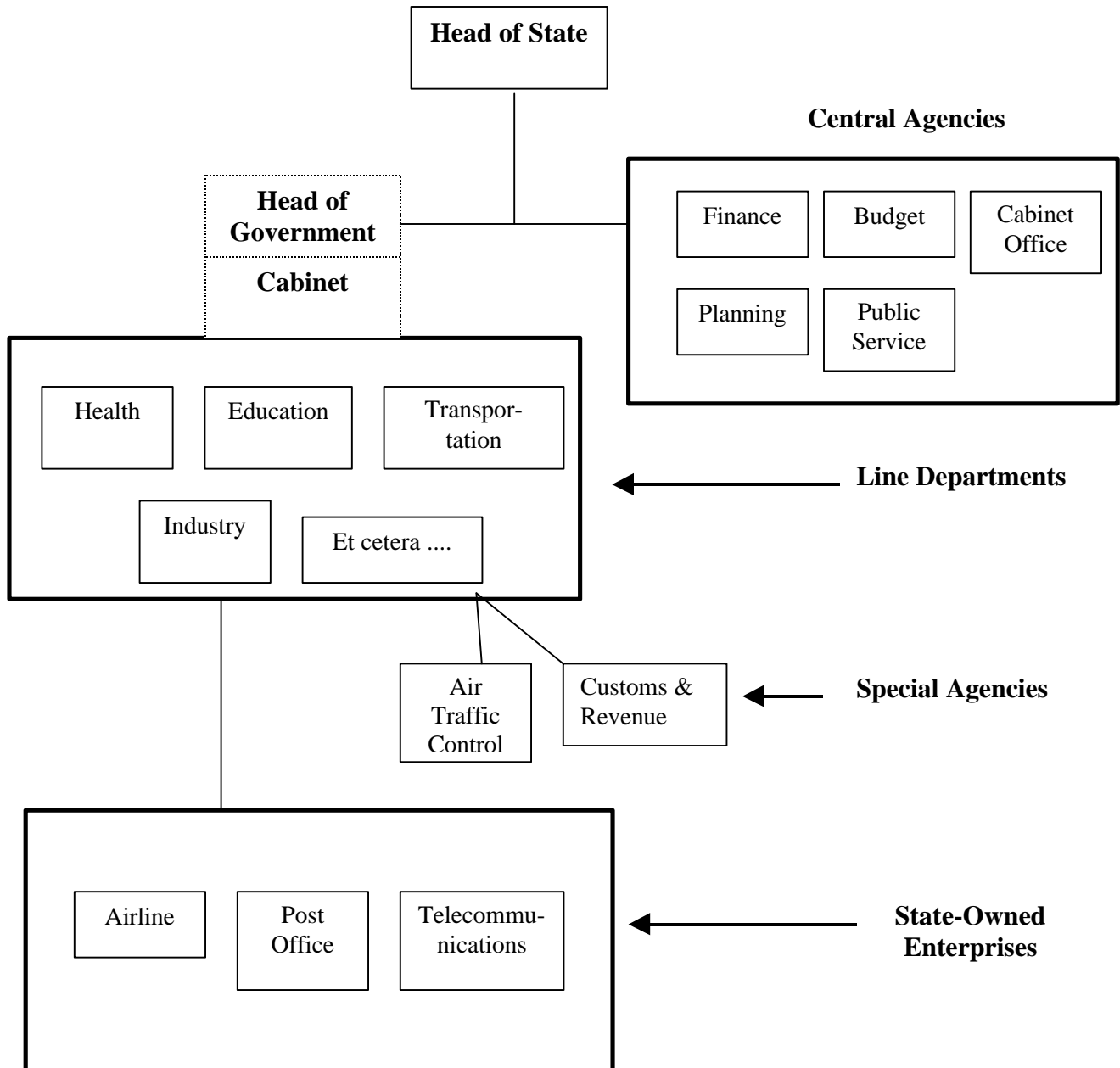
The public sector is divided into organizational units, each with a particular functional specialization and related set of responsibilities and authorities. Broadly, there are two major types of organizational units: central agencies and line departments. There are also various types of specialized agencies, and state-owned enterprises.

*Line departments* are specialized around programs and policies that relate to a particular economic or social sector, e.g. Department of Industry, Department of Health, etc. Each department is headed by a high-ranking political officer – a “Minister” or a “Secretary”

*Central agencies* are specialized around functions that affect the entire government. For example, a budget office manages the annual budget-making process; a cabinet office manages the flow of policy and program proposals from all departments into the cabinet for decision; the Department of Finance sets budget allocation levels that affect resources available for departments; a planning agency (common in developing countries) develops proposals on major investment initiatives that might be implemented by line departments.

In recent years there has been an increasing tendency for governments to take certain well-defined functions out of line departments and place them in *specialized agencies*. Customs and revenue agencies are a good example of this trend in the developing world. Specialized agencies often have greater flexibility to manage their human and financial resources than do line departments. In return, they are normally subject to tighter performance standards. Specialized agencies may report to the departmental bureaucracy or directly to the Minister.

**Figure 1: A Simple Model of the Public Sector**



*State-owned enterprises* (SOEs) are government-owned companies that may undertake commercial, industrial or financial activities.<sup>3</sup>

## **D. What Does the Public Sector Do?**

This paper concentrates on the executive branch (see above). The executive branch designs and implements policies and programs that aim to fulfill the government's broad economic and social objectives. In particular, it:

- ***Makes economic and social policies***
  - ⇒ The public sector makes and enforces policies that cover virtually everything the government does. Policies developed by the public sector serve the government of the day, reflecting its social and economic goals.
- ***Designs and implements public programs***
  - ⇒ Policies are realized through the design and delivery of public programs involving delivery of public services, production of goods, or transfers of resources to individuals, organizations or other levels of government. Governments also use regulation – in areas such as workplace standards, consumer protection, the environment, foreign investment, transportation safety – as a tool for achieving policy goals
- ***Raises revenue***
  - ⇒ The government must raise the funds in order to implement its programs. The public sector collects taxes and user fees that are levied on citizens and companies. Governments also use tax policy as a means to pursue social and economic goals. E.g. governments may pursue social goals by providing tax breaks to certain segments of the population. They may also use tax provisions to encourage certain forms of investment or industrial development.
- ***Manages accountability***
  - ⇒ Citizens demand accountability in return for the powers granted to the executive to raise and spend revenue. The public sector responds by enforcing internal accountability measures, and by reporting to citizens on how money is spent and on the successes (and failures) of public programs. Governments typically create and sustain independent public *institutions of accountability* that are empowered to oversee the government's actions and demand explanations. Key institutions of

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<sup>3</sup> SOE reform is a major topic in development, and is beyond the scope of this paper. SOEs are mentioned here for the sake of completeness.

accountability may include auditors general, public ombudsmen, the judiciary, the legislature, human rights commissions, etc.<sup>4</sup>

## **E. Development Agencies' Perspective on the Role of Government**

Fluctuating views about the role of government have had a profound influence on approaches taken by development assistance agencies to PSR. In the early days of development assistance, donors tended simply to take it for granted that governments should play a major and direct role in economic development. Donors supported state-dominated economic development strategies, while paying little attention to the inner workings of the public sector. PSR was not seen as a major issue.

When developing countries fell into financial crisis in the late 1970s and 1980s, donors began questioning the state-dominated model. Development assistance was made contingent upon curtailing the economic role of the state, reducing the size of the public sector, privatization<sup>5</sup> and cutting public expenditure. The pendulum swung from the public sector being regarded as an engine of development to its being seen as an obstacle to it. But there was still little effort to understand how the public sector really worked.

By the 1990s there was consensus that the pendulum has swung too far in the “anti-public-sector” direction. A renewed appreciation of the public sector’s developmental role began to emerge. The World Bank concluded recently that PSR has “great potential to reduce poverty”<sup>6</sup> and that “good ... government institutions [are] associated with higher income growth, national wealth, and social achievements”<sup>7</sup>. The current consensus is thus that PSR matters a great deal for development, and in at least two ways: (i) first, it will lead to better delivery of the basic public services that affect living standards of the poor;<sup>8</sup> and (ii) second, it will create a climate conducive to private sector development.<sup>9</sup>

These conclusions are based on a growing body of studies showing positive links between public sector performance and economic and social outcomes. One recent study showed significant correlation between government effectiveness and increased per capita income, increased adult literacy and reduced infant mortality<sup>10</sup> (Figures 2-4, p. 15). Other work has shown an inverse relationship between public-sector corruption and private investment.<sup>11</sup>

## **F. What Has Been Tried?**

Much of the PSR activity supported by donors over the past 20 years or so fits into the following areas: (i) administrative capacity building; (ii) strengthening policy capacity; (iii)

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<sup>4</sup> Schacter (2000).

<sup>5</sup> Privatization is the sale of state-owned enterprises to private investors. For a review of recent experience, see World Bank (2000b) and Kikeri (1999).

<sup>6</sup> World Bank (2000), p. 100.

<sup>7</sup> Thomas (2000), p. 136.

<sup>8</sup> World Bank (2000), Ch. 6.

<sup>9</sup> World Bank (1997), p. 103.

<sup>10</sup> Kaufmann, et. al. (1999).

<sup>11</sup> World Bank (1997), p. 103.

institutional reform; and (iv) civil service downsizing. Activities in these areas may be undertaken either as part of a comprehensive program of PSR that covers many or all government departments and agencies, or a narrower program that focuses on only one agency or a few.

***Administrative Capacity Building.*** This is probably the most frequently used form of assistance to public sectors in developing countries. Measures under this heading respond to the perception that many civil services are poorly managed and inefficiently structured. Often seen are training and skills upgrading in line departments operating in areas of particular interest to donors. Activities include:

- organizational restructuring and renewal, including strengthening of capacity to be more responsive to the needs and preferences of citizens;
- strengthening of linkages between government agencies, including strengthening the capacity of line departments to interact with one another and with central agencies;
- improving the quality of human resources through training and recruitment;
- addressing management problems related to employee performance management, wage and non-wage incentives, irrational job classification systems and ineffective payroll and personnel systems.

***Strengthening Policy Capacity.*** These measures aim at building the capacity of the government, either at the central agency level (see above, and Figure 4) or at the level of individual departments, to develop rational and effective public policies. They include:

- rationalizing and standardizing the decision-making process, improving the flow of policy-relevant information, etc.
- strengthening capacity for policy-analysis.

***Institutional Reform.*** These measures aim at making the state more open and accountable. They include support for:

- civil service codes of conduct and strengthened safeguards concerning public procurement;
- strengthening institutions and procedures that act as an accountability check on the executive, such as the judiciary, independent oversight bodies, and rules related to public access to information.

***Civil Service Downsizing.*** The motivation for downsizing has normally been some combination of fiscal discipline – governments trying to reduce the costs of public administration – and a desire to move toward a more market oriented economy. A typical package of interventions involves:



- *workforce size reductions*, implemented through mechanisms such as voluntary early retirement, hiring freezes, natural attrition and strict enforcement of the retirement age;
- *compensation schemes*, including lump-sum severance payments and job re-training, aimed at easing the transition of laid-off workers into the private sector;
- *wage policy reforms* such as wage-bill caps, wage freezes and monetization of non-cash allowances and benefits, all aimed at containing wage expenditures.

## G. What Have We Learned?

The last 20 years of donor assistance for PSR have produced little to cheer about. The most readily available information on the record of donor-assisted efforts comes from the World Bank<sup>12</sup>. A recent evaluation of the Bank's support for PSR since 1980<sup>13</sup> found that only about one-third of the Bank's projects had satisfactory outcomes. And even when satisfactory outcomes were achieved, it appeared unlikely in most cases that they would be sustained.

### Why Have Things Gone Wrong?

A major factor contributing to the failure of most PSR efforts has been the “technocratic” approach taken by donors.<sup>14</sup> For too long, donors treated PSR as an “engineering” problem – a phenomenon to be addressed through “blueprint” or “textbook” solutions. There was an assumption that PSR problems and their solutions could be fully specified in advance, and that projects could be fully defined at the outset and implemented on a predictable timetable, over a fixed period. This accounts for the formulaic and mechanistic approach favored by donors, featuring quantitative targets for payroll and workforce reductions, redrawing of organizational charts, rewriting of job descriptions, training courses for public servants, installation of new systems for human resource and public financial management, etc.

The technocratic approach overlooked the fact that PSR, though it has important technical aspects, is a social and political phenomenon driven by human behavior and local circumstances. It is a long and difficult process that requires public servants to change, fundamentally, the way they regard their jobs, their mission and their interaction with citizens. The technocratic remedies supported by donors underplayed the degree to which progress in PSR depends upon thorough “culture change” in the public service.

A related flaw is the *failure of local ownership* that characterized many donor-supported PSR efforts. A powerful lesson to emerge from 20 years of donor support for PSR is that significant reform will not flourish without local leadership and ownership. The donors' tendency to arrive in a developing country with a pre-fabricated, “blue-print” for PSR meant, not surprisingly, that there was little genuine support from the local bureaucratic and political leadership for the proposed reforms. Donors often based their PSR efforts on the false

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<sup>12</sup> There is no reason to believe, based on a review of the literature, that the record of PSR supported by other donors has in the aggregate differed significantly from that of Bank-supported efforts.

<sup>13</sup> World Bank (1999); see also World Bank (1999a) and Nunberg (1997).

<sup>14</sup> World Bank (2000a); World Bank (1999); Schacter (2000a)

assumption that “outsiders can build state capacity despite the lack of effective internal demand for more capable governments.”<sup>15</sup>

This point about “internal demand” for capable government opens the door to an additional insight about the poor record of PSR. Although one can (and should) find fault with the donors, it is also clear that donors have been stymied by a harsh local environment for PSR in many developing countries. At the heart of it is a failure of accountability between government and citizens.<sup>16</sup> The channels through which governments hold themselves accountable to citizens, and citizens communicate their demands for better government, are often highly dysfunctional in countries that are badly in need of public sector reform. One finds a vicious circle:

- governments do a poor job of delivering public services;
- citizens, accustomed to years of unresponsive performance and attitudes on the part of the government, feel little motivation to make demands for better service;
- the government, sensing little pressure from citizens, feels little accountability to them, and continues to deliver poor public services.

There is thus a failure of demand for PSR both outside and inside the government.

- *External demand* from citizens is muffled by popular cynicism about the public sector and by inadequate channels for communicating demand.
- Strong *internal demand* from public sector leaders does not emerge because they feel too little pressure from citizens for change.

Until this vicious circle is broken, the range of meaningful PSM actions that may be supported by donors is extremely limited.

A second kind of vicious circle also limits what donors can expect to accomplish in PSM. Designing and managing a PSR program requires a high level of administrative capacity. It follows that the countries most in need of PSR are also the ones with the least capacity to manage the process. A commentator<sup>17</sup> writing about PSR in the United Kingdom observed that it risks creating “administrative overload.” The situation is necessarily more fragile in many developing countries, where the management of routine business – let alone of a reform program – may be enough to induce “overload”.

### **What Do We Know About What Works?**

The stark truth about PSM is that we know much more about what hasn’t worked in the past than what is likely to work in the future. There are many examples of obvious failure, but few cases of unequivocal success. However, the mistakes of the past provide indications of

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<sup>15</sup> Brautigam (1996), p. 99.

<sup>16</sup> Boeninger (1991), p. 278; Schacter (2000); Schick (1998), p. 39; World Bank (1983), p. 123.

<sup>17</sup> Cited in Corkery (1997).

promising paths for future efforts. Consensus is building around approaches to PSM that emphasize (or at least take into account) the following elements:

**1. *Local Leadership and Ownership.*** PSR is doomed to fail if the main source of energy and leadership for it comes from outside. Donors cannot play a leading role, and they must not dictate the content, pace and direction of PSR. PSR is, among other things, an intensely political process that will inevitably pose a threat to important local stakeholders. Strong, relentless and well-placed local leadership is essential for overcoming the political and bureaucratic obstacles that confront a reform program.

**2. *Popular Pressure for Reform.*** Although local political and bureaucratic leadership is an essential ingredient for PSR, it is not sufficient. The public administration cannot be relied upon to reform itself. Impetus for reform must come from local stakeholders who are outside as well as inside the public sector. Organized civil society (e.g. civic associations, users' groups, labor unions, NGOs), the private sector, political parties and other influential domestic institutions all have a critically important role to play in pressuring the public sector to do a better job of serving society.

**3. *The Impact of Accountability.*** Failed accountability is at the root of public sector dysfunction. A strong bond of accountability between citizens and the public sector generates demand for PSR. Public sector performance is determined to an important extent by the interplay between the public sector and the country's key institutions of accountability (IAs)<sup>18</sup>. Successful PSR strategies should therefore be adapted to and (where possible) address shortcomings in the accountability environment within which the public sector operates. Reformers must have an appreciation of factors such as IAs' access to information about public programs and public expenditure, their capacity to analyze information about the public sector and place demands on it for better performance, and the degree to which public agencies feel compelled to respond to IAs.

**4. *The Power of Information.*** Wide dissemination of information that allows citizens to monitor public service delivery and public expenditure can have a powerful positive impact on the attitudes and behavior of public officials. Experience in developing countries with "service-delivery surveys" has shown that information flows can set in motion an uncontrollable dynamic promoting a more accountable and better-performing public sector.<sup>19</sup> Donors should use their influence to encourage governments to publish timely, complete and accurate information about government operations.

**5. *The Impact of Organizational Culture.*** Public sector organizations with a culture that is outcomes-oriented and "mission-driven" appear to have higher levels of performance than organizations lacking these features.<sup>20</sup> This underscores the importance to successful PSR of

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<sup>18</sup> The legislature, the judiciary, auditors general, ombudsmen, the news media, and organized civic groups are examples of key institutions of accountability. See Schacter (2000).

<sup>19</sup> World Bank (1999b), Paul (1998)

<sup>20</sup> Grindle & Hilderbrand (1995).

public-sector leadership styles and internal performance management practices that focus on results and service to the public.<sup>21</sup>

**6. *Build Capacity for Policy-making.*** Providing timely and well-argued policy advice to public decision-makers is generally regarded as a core responsibility of the public service. Capacity to fulfill this function is in short supply in many developing countries, a problem that has been under-addressed by donors. Recent experience in this area has yielded lessons for policy capacity building in developing countries.<sup>22</sup>

**7. *Take a More Sophisticated View of Downsizing.*** The first generation of public-sector pay and employment reforms generally failed to achieve its objectives.<sup>23</sup> This does not mean that pay and employment reform should be abandoned. It does however suggest that reformers should take a more sophisticated approach to downsizing, seeing it as a means to the end of a more focused, more effective and more efficient public sector. This means integrating downsizing programs into a larger frame of reference that includes a view on the appropriate role and size of government, an appropriate system for setting performance objectives and measuring progress against them, and a reformed pay structure conducive to attracting, retaining and motivating highly qualified staff.<sup>24</sup>

## H. Concluding Note

Perhaps the most easily overlooked lesson about PSR is that *it takes a long time to achieve fundamental reform of a public sector*. The experience of the developed world illustrates this well. It took centuries for today's industrialized countries to develop reasonably effective public institutions. In Great Britain, for example, it was only in 1854 that a series of reforms was launched aimed at constructing a merit-based public service shaped by rule of law. It took a further 30 years to eliminate patronage as the *modus operandi* of public sector staffing.

Many developing countries are therefore attempting to do in the space of a few decades what took hundreds of years in what is now the developed world. It is not surprising that the record to date has been full of failures and disappointments. Reformers in developing countries and their donor partners require a long-term perspective because fundamental change demands sustained effort, commitment and leadership over many generations. Mistakes and setbacks are a normal and inevitable part of the process. The big challenge is to seize upon mistakes as learning opportunities, rather than use them as excuses for squashing reform.

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<sup>21</sup> Schacter (1999a).

<sup>22</sup> Schacter (1999).

<sup>23</sup> In most countries where they were attempted, pay and employment reforms had little impact on either the cost or the performance of the public sector. World Bank (1999); (1999a).

<sup>24</sup> Nunberg (1997).

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(Internet links are provided for documents known to be available online.)

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## **Internet-based Resources for PSR**

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### **Governance and Public Sector Reform**

<http://www1.worldbank.org/publicsector/>

Operated by the World Bank's Public Sector Group

### **Public Sector Management (World Bank)**

<http://wbIn0018.worldbank.org/research/workpapers.nsf/SearchForm?OpenForm&FON=Public+Sector+Management^FOV=^Op1=^>

Seachable data-base of World Bank research related to the public sector.

### **Public Expenditure On-line**

<http://www1.worldbank.org/publicsector/pe/index.htm>

Operated by the World Bank

### **Governance and Anti-Corruption Resource Center**

<http://www.worldbank.org/wbi/governance/>

Operated by the World Bank Institute.

### **UNDP Management and Governance Network**

<http://magnet.undp.org/>

### **Eldis**

<http://nt1.ids.ac.uk/eldis/>

A searchable data-base covering the full range of development issues, including governance and public sector reform.

### **Public Affairs Centre (Bangalore)**

<http://www.pacindia.org/>

A source of information on citizen surveys of municipal government services.

### **OECD Public Management and Governance (PUMA)**

<http://www.oecd.org/puma/>

Oriented toward the OECD countries, but relevant to matters of broader concern.

**Capacity.org**

[www.capacity.org](http://www.capacity.org)

Focuses on capacity building issues (including issues related to PSM) in developing countries.

**Alliance for Redesigning Government**

<http://www.alliance.napawash.org/alliance/index.html>

Oriented toward U.S. issues in public administration, but relevant to matters of broader concern. Includes a searchable data-base.

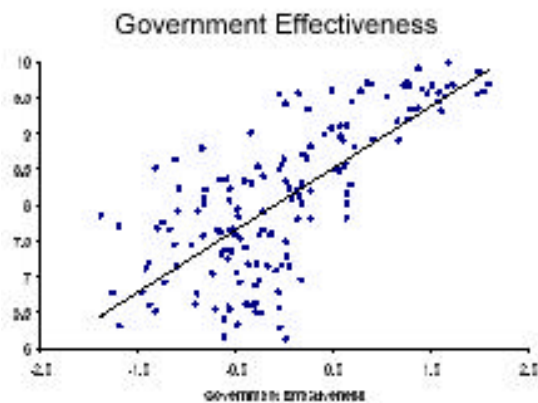
**Results Measurement and Accountability**

[http://www.tbs-sct.gc.ca/rma/rma\\_e.html](http://www.tbs-sct.gc.ca/rma/rma_e.html)

Operated by Canada's Treasury Board Secretariat, with a focus on Canadian issues.

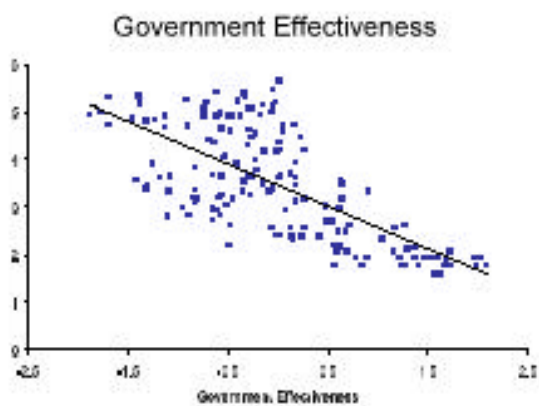


**Figures 2-4: Correlation of “Government Effectiveness” to Economic and Social Outcomes.** From Kaufmann, et. al. (1999)



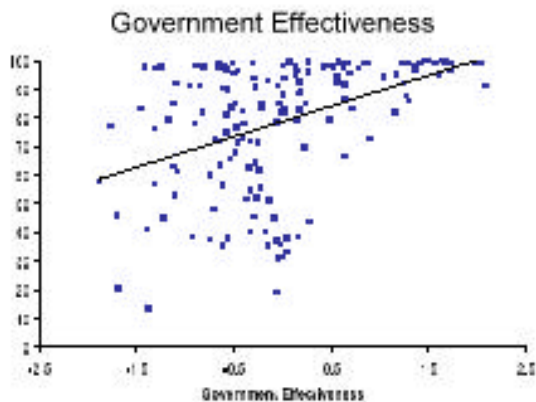
**Government Effectiveness and Per Capita Income**

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**Government Effectiveness and Infant Mortality**

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**Government Effectiveness and Adult Literacy**

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