



QUALITY OF GOVERNMENT SPENDING: EFFICIENCY AND EFFECTIVENESS

OECD perspectives

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Roadmap of presentation

Assessing government operations: spending,
production costs and value added

How much?, On what?, For whom?

Gauging the quality of spending: Efficiency and effectiveness

Metrics, impacts, tools

Agenda for future work

Methodological, conceptual, policy tools



Motivation

- Fragile public finances in most OECD countries; high debt and need for retrenchment over the medium term
- Steady growth in government spending and already high (average and marginal) tax rates in many countries
- Perception of inefficiency/ineffectiveness in government operations; lack of trust in institutions and government, especially since the crisis
- Disenchantment among public administration specialists with different public management strategies

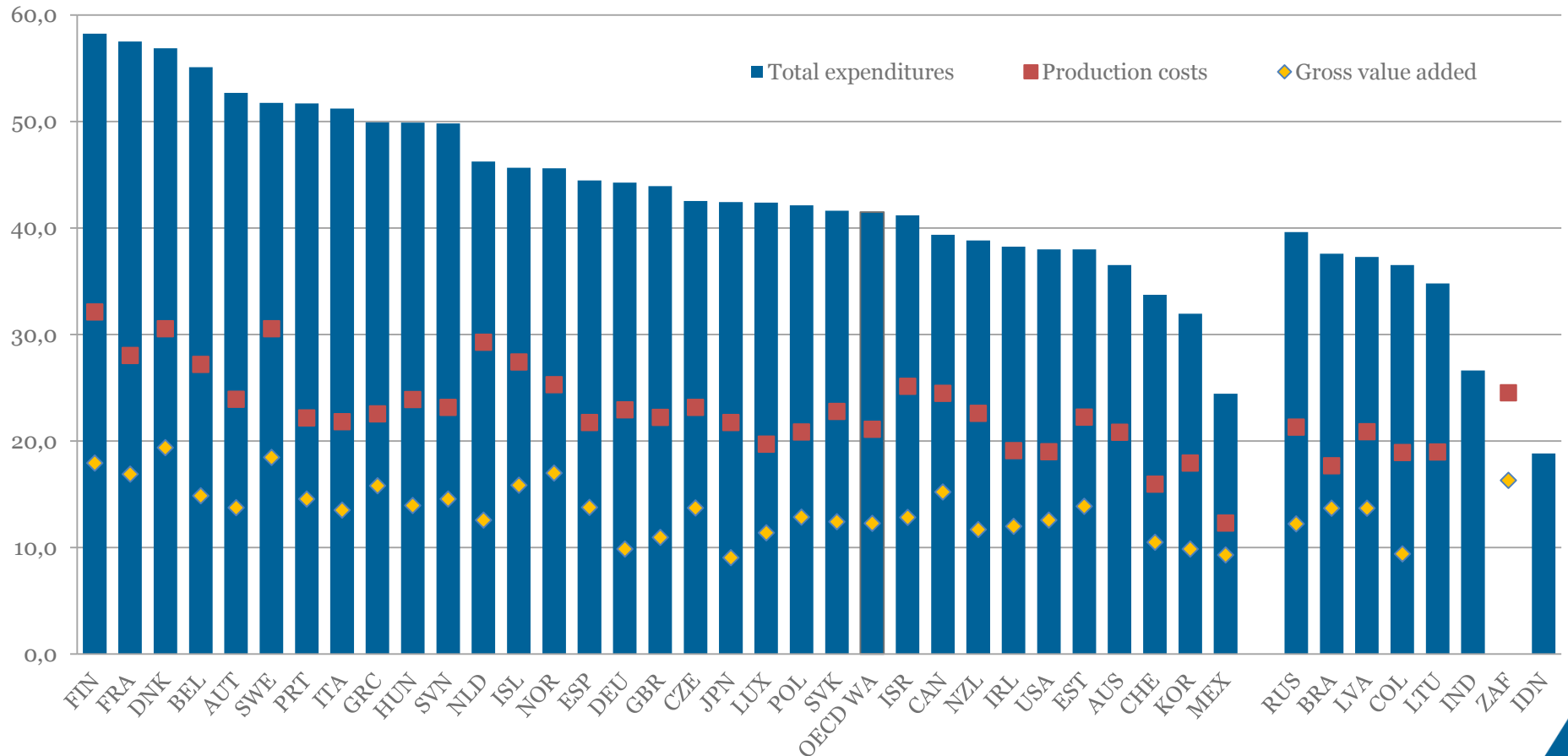


Government spending: How much?

- Expenditure is a conventional measure, but it is a misleading proxy of the “value added” of government operations
 - Because it includes intermediate consumption, compensation of employees, subsidies, property income, social benefits, other current and capital outlays
- A finer analysis consists of looking at production costs and *gross value added* using the national accounts
 - Production costs include compensation of employees and the goods and services used and financed by government (e.g. outsourcing), and other costs (mainly consumption of fixed capital)
 - Gross value added includes compensation of employees, consumption of fixed capital, taxes less subsidies on production and net operating surplus
 - (Net value added is gross value added minus consumption of fixed capital)



Government is much smaller when measured in terms of production costs and gross value added (% of GDP, 2014)



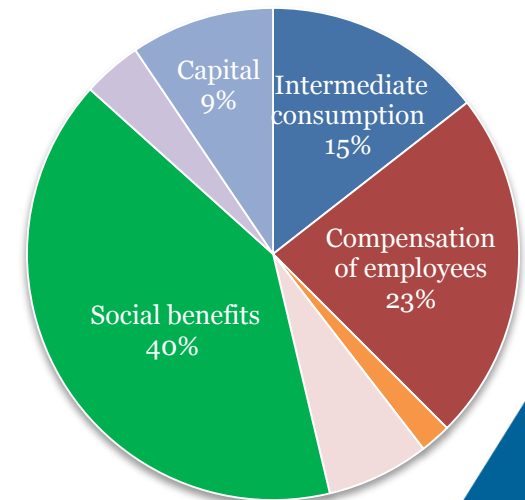
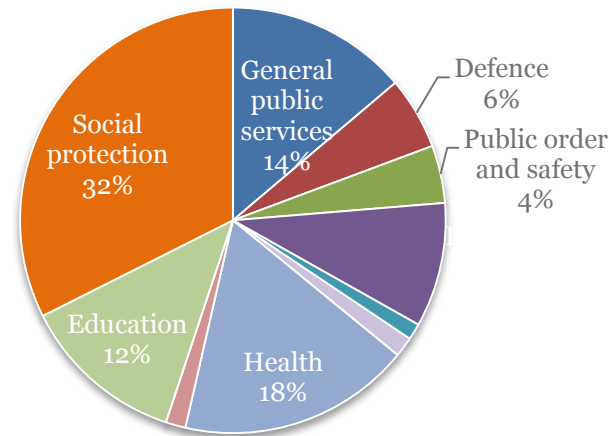
Source: OECD National Accounts and Government at a Glance databases. Data for Brazil (total expenditures), India and Indonesia are from the *IMF Economic Outlook* (October 2015). Data for 2014 for total expenditures for Australia, Japan and New Zealand are estimated. Data for Mexico, Colombia and Russia refer to 2013. Data for production costs for Australia, Japan, New Zealand refer to 2013. Data for New Zealand for gross value added refer to 2013.



Government spending: On what? For whom?

- Conventionally, government spending is classified along functional and economic lines
 - According to the functional classification, the bulk of spending among OECD governments is on social protection, education and health care...
 - ... and in economic terms, social benefits, compensation and intermediate consumption
- But this split says nothing about how much the government spends on service delivery and its own operations to delivery those services, which is essential for gauging efficiency and effectiveness

Functional and economic classification of government spending (OECD average, %)



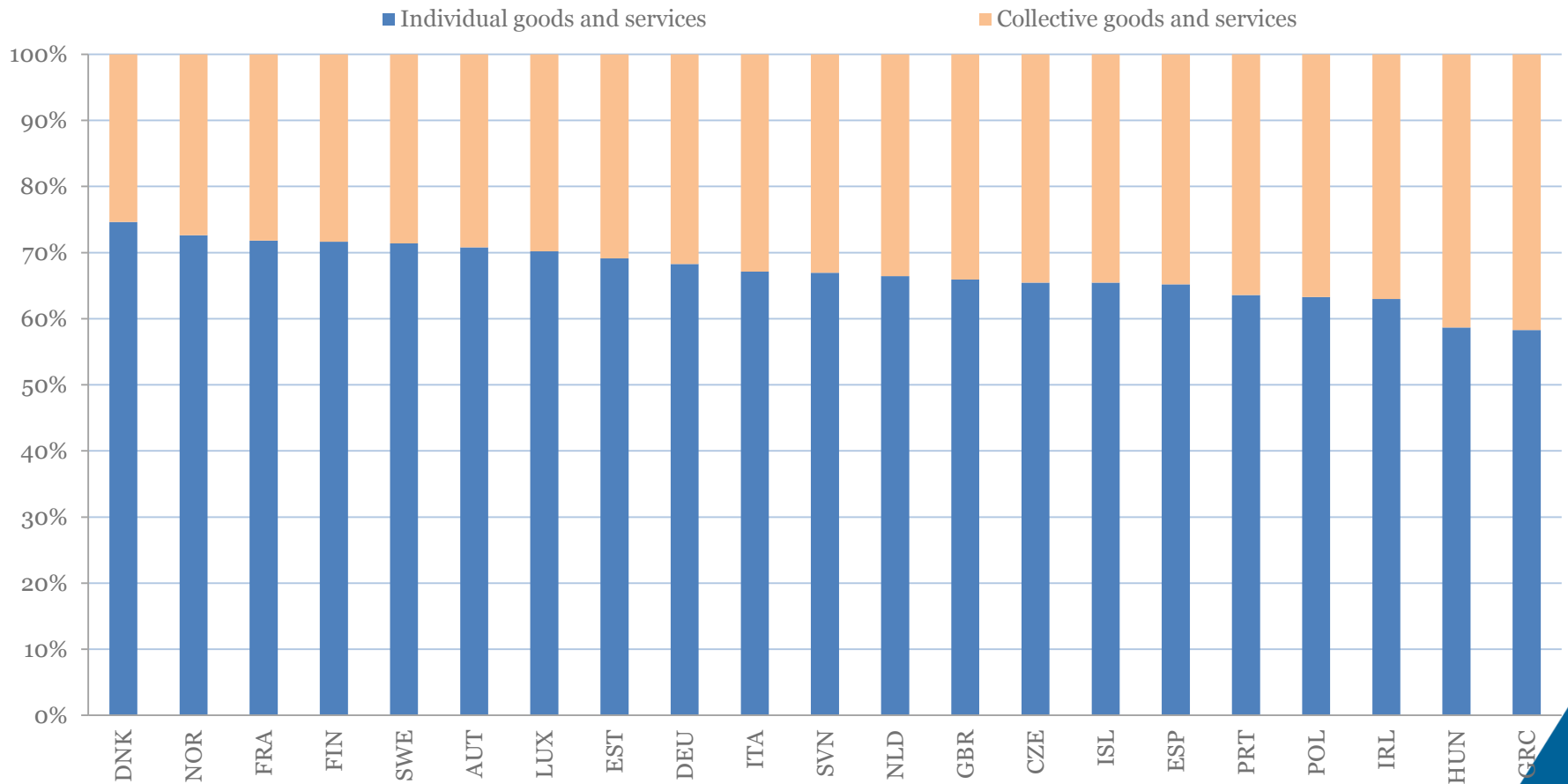
Source: OECD Government at a Glance database.



- A finer split between *frontline* and *back-office/transactional* services would be particularly useful
- Frontline services can be considered as those that are delivered directly to *individuals/households*, whereas back-office and transactional services are of a *collective* nature
 - For example, in education, individual services would include all expenditures minus subsidies which are provided to individuals/households, whereas collective services are related to the formulation and administration of government policy; setting and enforcement of standards; regulation, licensing and supervision, etc.
 - More generally, spending on defense, public order and safety, etc., could be considered as collective in nature.
- The advantage of the split between frontline/individual and collective/back-office/transactional services is that it also allows for some analysis of distributional impacts
 - This complements the conventional incidence analysis of spending and tax across income groups



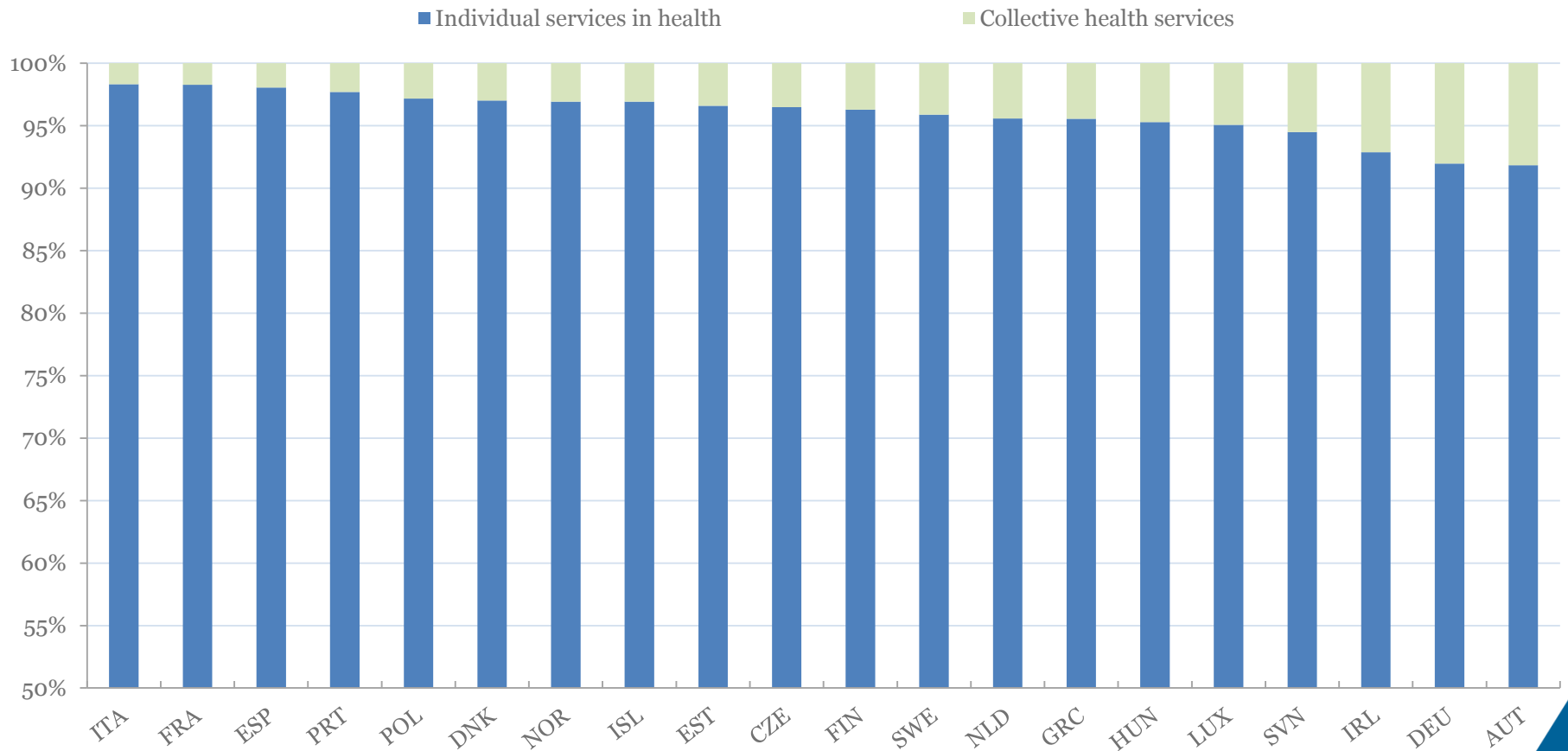
Composition of government spending (%), 2011



Source: OECD National Accounts database,
Data refer to 2010 for Spain and 2009 for UK.



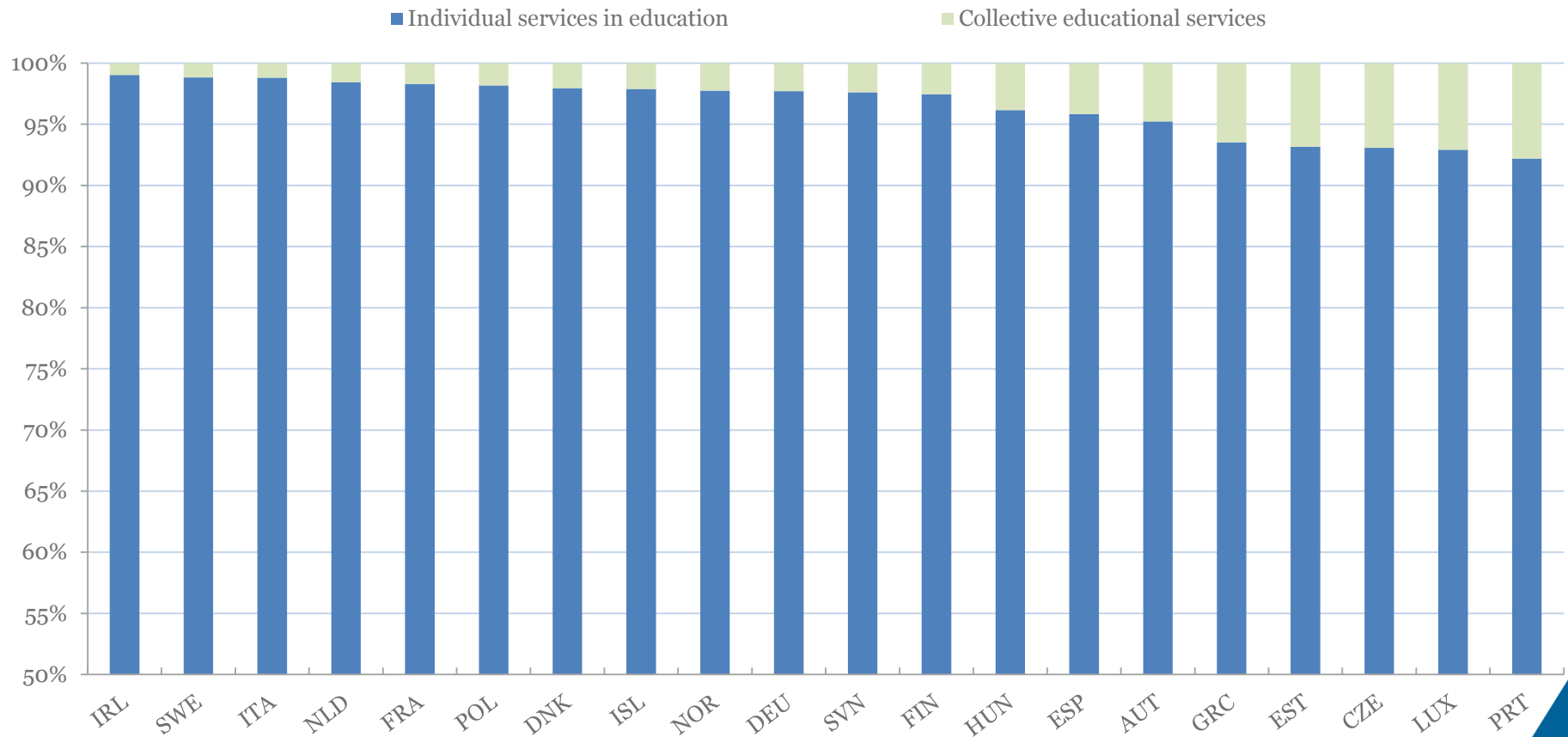
Composition of government spending on health care (%), 2011



OECD National accounts statistics (database). Data for Spain refer to 2010.



Composition of government spending on education (%), 2011



OECD National accounts statistics (database). Data for Spain refer to 2010.



Quality of spending: Metrics and Impact

- A basic difficulty to gauge the efficiency/effectiveness of government operations is the measurement of inputs and outputs
 - Inputs: it makes a difference if frontline or back-office/transactional activities are the object of analysis; there is limited information on the unit costs of services (eg Australia), as well as on prices/deflators
 - Outputs: governments engage primarily in non-market activities, and by convention SNA uses costs as proxy for non-market output; quality adjustments are difficult (eg, UK)
 - For discussion: eg, Atkinson (2005), Stiglitz et al (2010), OECD (2011, 2014), Bean (2015)



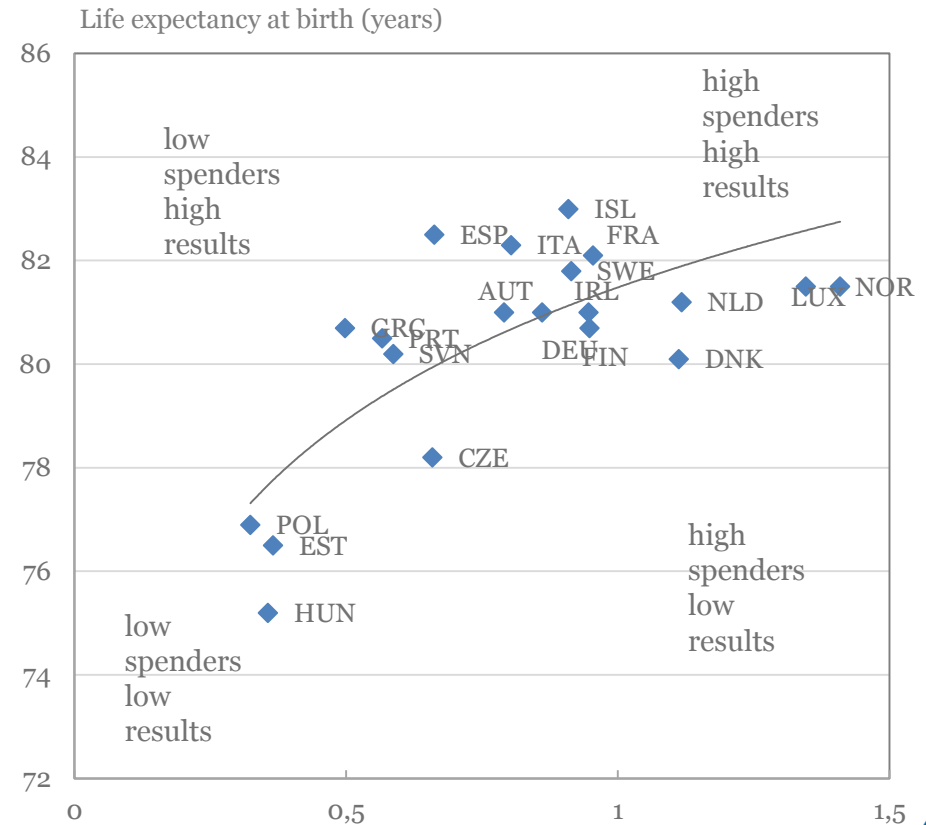
- Another difficulty is the distinction between outputs and outcomes
 - Wellbeing indicators are good metrics for outcomes and recognise multidimensional nature of impacts, which implies trade-offs, synergies and unintended consequences (OECD, 2011)
 - There are interesting experiences at the national (eg, NZ) and subnational levels (eg, Southern Denmark, Morelos (MEX), etc.) (OECD, 2014)
- Impact is not observable directly and needs to be inferred econometrically: production function/stochastic frontier approaches
 - Parametric and non-parametric (eg, FDH, DEA) techniques, latent variable models, efficiency/performance scores;
 - Cross-country and country-specific analyses; all suffer from measurement problems



Takeaways from empirical literature

- Sectoral focus: education and health care, sometimes investment
- Income swamps government spending in cross-country analysis, but composition matters; some cross-sectoral effects (eg, de Mello et al, 2003)
- Some evidence on institutional context in country-specific work (eg, Boueri et al, 2015)
- Scant evidence on governance effects, except for decentralisation

An illustration: spending on health care (individual services) and life expectancy



Source: OECD Government at a Glance database.



Quality of spending: Tools

- Governments have sectoral and systemic tools to foster efficiency/effectiveness; of course, tools are context-specific and depend on institutions and traditions
- Budget instruments are particularly important; in particular:
 - Conventional tools include MTEFs, performance budgeting, spending reviews, impact assessments, ex ante evaluations and CBA; use of different tools varies significantly across OECD countries
 - These tools depend on a solid information basis, capacity to project spending and benchmark provision; despite lack of data on unit costs, etc.
 - Ex post evaluations are important but they are carried out infrequently; they inform discussions about reallocation of resources to most efficient/effective uses, despite institutional constraints (eg, earmarking) and rigidity of entitlements (eg, pensions, health care, social protection)



- But there is also a “performance continuum” that goes beyond budgeting and includes other public administration aspects; in particular:
 - Links to HRM (evolving skills and competencies of the civil service; productivity targets, outsourcing); management and organisation; procurement (strategic and secondary objectives); digital government (access to info but value creation as well)
 - Integrity, control and accountability: output/outcome-focused external control is an important driver of reform (OECD, 2015); open government programmes also help
 - Coordination, alignment of objectives and multilevel governance: the centre of government has an important role to play in this area, as do institutional arrangements for intergovernmental policy coordination (Ter-Minassian and de Mello, 2016)
 - New areas of interest include greater stakeholder engagement, which is evolving from traditional consultation towards co-creation and co-production, especially in service provision, but also crowdsourcing for legislative action



The case of MTEF: LAC experience

	Existence and legal basis of MTEF	Length of ceilings (including upcoming fiscal year)	Target(s) of expenditure ceilings		
			Total expenditures	Programme or sector expenditures	Organisational expenditures
Argentina	⊖	x	x	x	x
Barbados	○	3 years	✓		
Brazil	⊖	x	x	x	x
Chile	○	3 years	✓		
Colombia	●	4 years		✓	
Costa Rica	⊖	x	x	x	x
Dominican Republic	⊖	x	x	x	x
Ecuador	⊖	x	x	x	x
El Salvador	⊖	x	x	x	x
Guatemala	●	3 years			✓
Haiti	○	3 years	✓		
Honduras	⊖	x	x	x	x
Jamaica	○	5 years	✓		
Mexico	●	5 years	✓		
Panama	⊖	x	x	x	x
Paraguay	○	2 years			✓
Peru	⊖	x	x	x	x
Total			5	1	2
● Yes in a law which stipulates both the existence of a MTEF and budget ceilings	2				
● Yes in a law stipulating the creation of a MTEF which should be based on budget ceilings	1				
○ Yes in a law stipulating that spending thresholds should not exceed medium term estimates	0				
○ Yes in a strategy/policy stipulating the MTEF and/or budget ceilings	5				
○ No	9				
x Not applicable (e.g. No MTEF in place)					

Source: OECD Government at a Glance, Latin America, 2015.



Performance budgeting: LAC experience

	Existence of standardised performance budgeting framework for central government	Use of performance information in negotiations with CBA						Consequences for poor performance			
		Financial data	Operational data and performance reports	Performance evaluations	Spending reviews	Independent performance information	Statistical information	No consequences	Organisational or programme's poor performance made public	More intense monitoring of organisation and/or programme	Budget decreases
Argentina	Yes	●	⊙	○	x	○	○	○	●	○	⊙
Barbados	Yes	●	⊙	⊙	●	○	●	○	○	●	⊙
Brazil	Yes	●	●	●	●	⊙	●	●	○	○	○
Chile	Yes	●	⊙	●	x	⊙	⊙	⊙	●	⊙	⊙
Colombia	No, Line Ministries/Agencies have their own	⊙	x	⊙	●	⊙	○	⊙	○	⊙	⊙
Costa Rica	Yes	●	⊙	○	⊙	⊙	⊙	●	●	●	⊙
Dominican Republic	No, Line Ministries/Agencies have their own	●	●	⊙	●	⊙	●	..	..	..	..
Ecuador	Yes	●	●	●	●	⊙	●	⊙	○	●	⊙
El Salvador	No, Line Ministries/Agencies have their own	●	●	●	●	○	●	..	..	..	..
Guatemala	Yes	●	⊙	●	⊙	●	●	●	⊙	●	⊙
Honduras	No, Line Ministries/Agencies have their own	⊙	○	⊙	⊙	⊙	⊙	●	⊙	●	○
Mexico	Yes	●	●	●	●	⊙	●	○	●	●	○
Panama	Yes	●	⊙	⊙	●	⊙	●	●	⊙	○	⊙
Paraguay	Yes	●	●	⊙	⊙	⊙	⊙	⊙	⊙	⊙	○
Peru	Yes	●	●	○	⊙	⊙	⊙	⊙	○	●	○
Total											
● Always		11	3	2	5	1	4	3	3	2	0
● Usually		2	4	4	3	0	4	2	1	5	0
⊙ Occasionally		2	5	3	1	5	4	1	2	2	3
○ Rarely		0	1	3	0	3	2	3	5	3	5
⊙ Never		0	1	3	4	6	1	4	2	1	5
x Not applicable (information not produced or negotiations do not take place)		0	1	0	2	0	0	2	2	2	2
.. Not available		0	0	0	0	0	0	2	2	2	2

Source: OECD Government at a Glance, Latin America, 2015.



Budget flexibility: LAC experience

	Percentage of total expenditure that is pre-assigned	Legal basis of budget earmark and corresponding sector						Transfers to sub-national governments
		Health	Education	Defence	Security	Justice		
Argentina	41-60%	●	●	x	x	●	x	
Brazil	81-100%	●	●	x	●	x	●	
Colombia	61-80%	x	x	x	x	x	●	
Costa Rica	81-100%	●	●●	x	●	●●	x	
Chile	0-20%	x	x	●	x	x	●	
Ecuador	0-20%	●●	●●	x	x	x	●●	
El Salvador	0-20%	x	x	x	x	●	●	
Guatemala	41-60%	●●	●●	●●⊙	●●	●●	●●	
Honduras	0-20%	x	●	x	x	●	●	
Jamaica	..	..	..	..	..	..	..
Mexico	41-60%	x	x	x	x	x	●	
Panama	..	..	..	..	..	..	..
Paraguay	21-40%	x	●●	x	x	●	x	
Peru	x	x	x	x	x	x	x	
Total								
● Constitution		3	6	1	1	3	5	
● Primary legislation		4	5	2	3	5	5	
⊙ Secondary legislation		0	0	1	0	0	0	
○ Other legal basis		0	0	0	0	0	0	
x Not applicable/no budget earmark		7	5	10	9	6	4	
.. Not available		2	2	2	2	2	2	

Source: OECD Government at a Glance, Latin America, 2015.

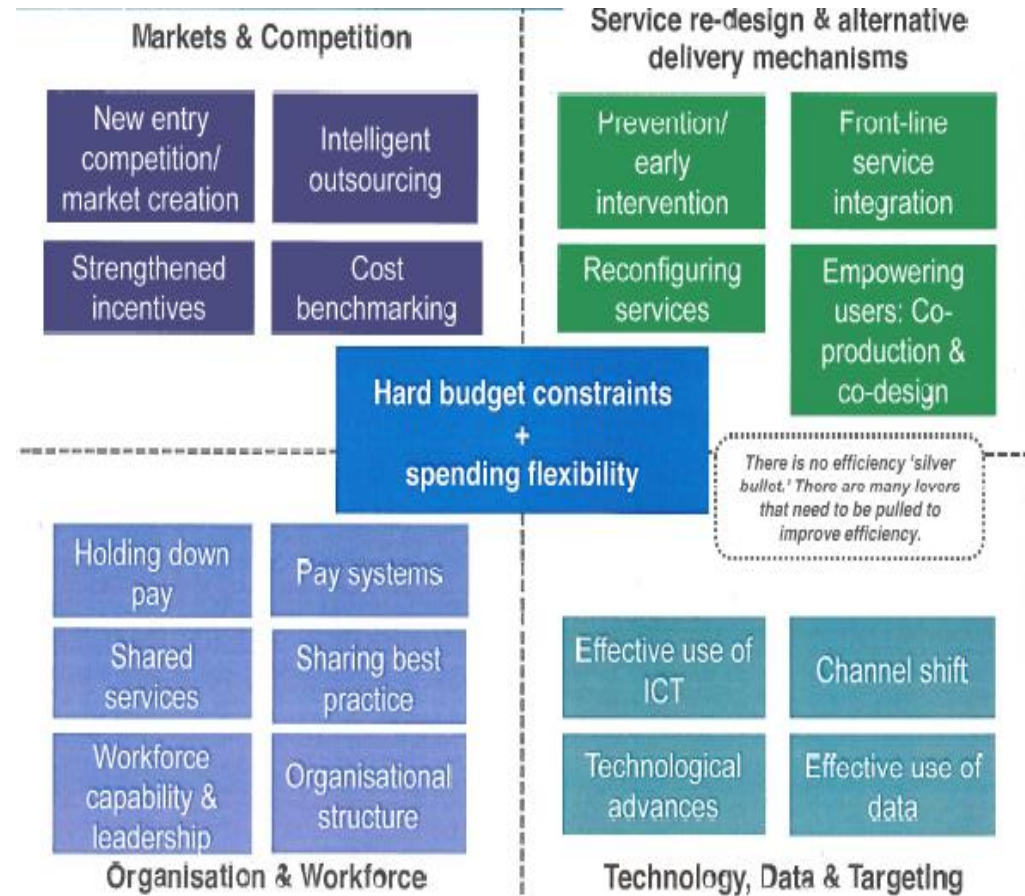


A few operational mechanisms

- Systemic approaches require operational mechanisms; in particular:

- Performance indicators: building the information base with KNIs; could the SDG indicators help in this area?
- Organisational tools: “Value maps” (eg, UK), scoreboards (eg, NZ) and “checklists” (eg, Scotland)
- Alignment and coordination instruments: interagency and intergovernmental performance contracts (eg, France, Chile)

UK approach: Public Sector Efficiency Group



Source: Government Strategic Services, UK.



Agenda for future work

- Closing measurement gaps, ... much to be done...
 - abandoning the “input=cost=output” convention in the national accounts, comparable unit costs, price and quality adjustments, etc.
- Conceptual discussion, ... beyond blue sky thinking...
 - how much emphasis on outcomes (eg, growth, wellbeing) vs outputs in performance assessment? Distributional considerations?
- Policy tools, ... easier said than done...
 - identifying toolkits and testing different instruments; international benchmarking and “best practices”; governance and practices; evaluation culture



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