Public Spending, Governance, and Development: A Review of the Literature

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1. Introduction

As the deadline for the Millennium Development Goals approaches, international organizations and donors have shown increasing interest in how institutional changes can improve the efficiency of pro-poor spending and lead to better development outcomes in areas such as education and health. A large empirical literature exists documenting the inefficiency of public spending in producing improvements in development indicators, and economists have developed a number of theoretical models explaining this ineffectiveness. Many of these models have focused on governance quality as an important determinant of government expenditure effectiveness, and further attention has been paid to particular aspects of governance, including accountability and transparency, that can affect human development. Despite increased interest in the relationship between transparency, accountability, and human development, the economic literature on this relationship is still relatively limited. The following sections review the current literature on governance, public spending, and development, focusing on where transparency and accountability enter the literature.

The remainder of the literature review is organized as follows. Section 2 discusses empirical studies relating public spending and development outcomes, particularly in the areas of education and health. Section 3 focuses on the theoretical and conceptual literature on governance and public spending efficiency. This section includes both theoretical models that incorporate transparency and accountability and papers that discuss current global trends in these two aspects of governance. In section 4, empirical studies on the relationship between accountability, transparency, spending, and development outcomes are discussed. Section 5 reviews studies that investigate the effects of governance and corruption on public spending and

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human development. Section 6 discusses conceptual papers on participatory budgeting, and section 7 summarizes the entire literature.

2. Does public spending affect human development?

Many models have been developed to examine the link between government expenditures on public goods and the social development outcomes of this spending. This area of research has been especially important as developing countries and international donors alike work towards achieving the Millennium Development Goals by 2015. The majority of studies linking public spending and development outcomes attempt to show that government expenditures are not having the desired effect on health and education outcomes. Although a wide array of development indicators have been used in this literature, the empirical evidence on the relationship between public spending and development outcomes has largely confirmed the hypothesis that a greater allocation of public funds towards education and health does not have a significant impact on indicators such as educational attainment and infant mortality.

One recent study that does find a positive relationship between spending and improvements in development is Gupta, Verhoeven, and Tiongson (2002). In a recent study of fifty developing and transition countries, the authors find that both educational outcomes (primary and secondary school enrollment ratios, persistence through Grade 4, and primary school drop-out rate) and health outcomes (infant and child mortality rates) are correlated with overall sector spending and the intrasectoral allocation of public funds. The study uses two-stage least squares methods to find strong evidence of causality in the education models, though the health models present only weak evidence of this causal link.

However, the majority of the literature on public spending and outcomes finds a small if not insignificant relationship between expenditures and development measures. Focusing on the primary health care sector, Filmer and Pritchett (1999) hypothesize that country demographic variables play a larger role in determining health outcomes than government expenditures on primary healthcare. The authors find evidence to support this hypothesis, showing that the share of government expenditure on health care has a statistically insignificant effect on both child and infant mortality in a cross-section of developing countries. While socio-economic factors (income per capita, income inequality, female education, predominant religion, and ethnic fragmentation) play a major role in determining health outcomes, the authors find that health spending only explains one-seventh of 1% of cross-country variation in infant and child mortality rates. Castro-Leal et al. (2000) and Canagarajah and Ye (2001) find similar results using a benefit incidence analysis of public health spending in Africa.

Although there are a few exceptions, the majority of the literature linking public spending and development outcomes confirm the hypothesis that spending plays a minor if not insignificant role in explaining variation in development outcomes such as test scores and immunization rates. Authors in this literature utilize many different methods to test this link; however, these studies in general provide only limited explanations for the insignificant effect of development expenditures on development outcomes. One exception to this trend is Deolalikar, Jamison, and Laxminarayan (2006). By focusing on differences in public health spending within India rather than across countries, the authors are able to identify great heterogeneity in the impact of public spending on health outcomes rather than losing this variation across Indian states by aggregating. The authors observe that public spending efficiency is likely to be affected by such factors as administrative capacity and governance and that quality of spending must be analyzed in addition to quantity in order to determine whether additional spending will have a significant impact on health outcomes.

Some discussion exists in the conceptual literature of capture of funds at the local level which could lead to increases in public spending not having the desired effect on development. Because the majority of empirical studies on government spending utilize national level in cross-country analyses, these studies cannot measure the actual level of government expenditure that is received by schools and health clinics. One paper that investigates the idea of leakage of public funds is discussed in section 4 below. Overall, although the papers linking development outcomes and public spending provide significant evidence that the effect of spending is weak, more work is needed to investigate why a stronger link does not appear to exist.

3. Theoretical models relating governance and the effectiveness of public spending

As the empirical evidence of the weak link between public spending and outcomes continues to grow, economists have sought to explain this phenomenon theoretically. The result has been two distinctive schools of thought as to why government spending is not having the intended effect on development outcomes. The first group of theoretical models explains that government spending crowds out private investment in social institutions such as healthcare facilities and schools. The second set of theories focuses on actual inefficiency of government spending. The majority of studies focusing on developing and transition countries start from the latter theoretical framework. These studies present a wide array of reasons for the inefficiencies of government spending, including but not limited to corruption of government officials.

Focusing on the inefficiency of government expenditures and investments, Pritchett (1996) discusses situations in which governments fail to act as profit-maximizers and, as a result, the value of public investment is higher than the value of public capital produced. The author presents several explanations for why governments may not act in a cost efficient manner, including government corruption and patronage. Filmer et al. (2000) argue that the inefficiency of public spending (specifically health sector spending) is a result of market failures and insufficient institutional capacity. The authors discuss the aspects of public spending that are susceptible to these market failures, including inefficient composition of public expenditures.

As the theoretical literature on inefficiencies in government spending has continued to grow in recent years, researchers have increasingly focused attention on international trends in governance and public administration. Armstrong (2005) discusses good governance programs supported by the UN that have resulted in increased accountability and transparency in local and national public administration practices. She argues that these aspects of good governance have generally increased worldwide in recent decades and stresses the important role that transparency and accountability play in reaching development objectives including the Millennium Development Goals.

Florini (1999) looks more objectively at both the benefits and costs of increased transparency in an era of globalization. Like Armstrong, Florini acknowledges that increases in global transparency have the potential to improve both economic and political outcomes. However, the author also recognizes that transparency can be costly to attain and that exerting the effort to gain transparency is only beneficial if government officials have the incentive to comply and the public is willing to act upon information they receive about the government.

In their study of budget reforms, Campos and Pradhan (1996) find that lack of transparency and accountability is one of two major factors that have contributed to weak spending efficiency in Ghana, Malawi, and Uganda. Specifically, the authors argue that, without transparency and accountability, countries are unable to enforce existing laws regarding budget priorities and choices. In contrast, Thailand and Indonesia were found to have relative efficient budgetary procedures, although the authors found that Thailand could better use information from local governments to make better spending decisions. Although they explicitly discuss the role of transparency and accountability in spending efficiency, the authors spend little time covering specific development outcomes.

In contrast to these conceptual papers, Kaufmann et al. (2005) take a more quantitative approach to measuring trends in governance and find no evidence of an overall global trend in governance quality in the past decade. The study employs the Kaufmann-Kraay aggregate governance indicators (Kaufmann et al., 1999) based on measures of accountability, instability, government effectiveness, regulatory quality, rule of law, and corruption to analyze global trends in governance quality in 209 countries from 1996 to 2004. The authors find significant improvements and losses in governance measures within countries over time; however, their results do not support Armstrong's claims of an overall increase in governance quality.

As outlined above, research on the relationship between public spending and development outcomes is extensive and well-established. However, the literature linking governance (specifically accountability and transparency) and development outcomes is still relatively sparse. A small number of theoretical models have been developed to explain this relationship. Keefer and Khemani (2005) discuss ways in which budget allocations can fail to benefit the poor due to political market imperfections. The paper focuses on a lack of transparency (specifically imperfect information available to voters and lack of credibility of politicians) as one of the key market imperfections that can lead to public expenditures that do not benefit poor people. The authors claim that the education and health sectors are especially susceptible to these market failures.

In their study of public spending efficiency, Rajkumar and Swaroop (2002) create a model with development outcomes as a function of a country's gross domestic product, spending on development programs, and country-specific parameters. The model allows for some leakage of public funds, where the fraction of public program funds reaching the program is a function of the quality of governance of the country.

In testing the effects of public access to information and political accountability on government spending decisions, Besley and Burgess (2002) develop a principal-agent model that allows political transparency and accountability to impact pro-poor government spending decisions. The authors use the theoretical model to show that politicians will employ more effort in poorer areas if media access is high and if there is a higher voter turnout for elections.

Despite differences in specific parameters, theoretical models of the relationship between transparency and development outcomes focus on how political transparency affects the incentives of politicians to implement policies that meet the demands of civil society. The majority of these models are extensions of the basic principal-agent model and start from the idea that the agent (government) will exert more effort when it believes that the principal (civil society) can better monitor its effort. Although these models cannot completely explain the weak link between public spending and development outcomes discussed in section 2, these theories introduce the idea that government officials can affect human development through actions outside expenditure decisions. In addition, the theoretical studies outlined above present the government as an agent with its own interests that not only affects civil society but also has the potential to be affected by civil society.

4. Empirical studies on transparency, accountability, public spending, and development

In the field of transparency and accountability, only a small number of studies have been conducted to bridge the gap between the theoretical discussion of how these concepts should effect human development and the empirical evidence that this link does exist. Without exception, these studies work from the hypothesis that increasing the public knowledge of government processes and implementing ways in which civil society can hold government accountable for its actions will increase administrators' incentives to allocate money and effort towards social development programs. The methods that researchers have used to test this hypothesis, however, fall into two distinct categories, micro-level studies in individual countries and cross-country studies. The former largely centers on the role of the media in improving access to information, using media variables to proxy for transparency and measuring the effect on public spending rather than outcomes. The latter set of studies uses aggregated transparency indices to explain cross-country variation in human development indicators.

One of the first studies to use media access as a measure of transparency is Besley and Burgess (2002). The authors develop a model of political transparency to test the hypothesis that government officials will put more effort into pro-poor spending if the public has greater access to newspapers (transparency) and if voters are more responsive during elections (accountability). The study exploits exogenous shocks (natural disasters such as drought, flooding, and food shortages) to test whether Indian states with greater newspaper circulation and more political competition receive more public funds for food distribution and disaster relief services from 1958 to 1992. Using a fixed effects model, Besley and Burgess show that a one percent increase in newspaper circulation is associated with a 2.4 percent increase in public food distribution and a 5.5 percent increase in calamity relief spending, controlling for the need for state intervention.

Strömberg (2004) also employs media access variables to measure the relationship between political transparency and government expenditures. The author presents a model that explicitly defines the relationship between transparency, accountability, and public spending, hypothesizing that areas with greater media access will have a higher voter turnout and areas with higher voter turnout will receive more government funding. Focusing on Federal Emergency Relief Act (FERA) spending in the United States during the New Deal-era, the author finds that a one percentage point increase in the share of radio listeners in a county resulted in a 0.59 percent increase in FERA funding for the county, controlling for county income level.

The previous two studies use public accounts information to measure the level of public spending promised by government officials. However, if funds are subject to capture by local officials, these public accounts may not accurately reflect the actual level of spending received by civil society. Reinikka and Svensson (2004) circumvent this issue by using data from individual schools in Uganda regarding the amount of money they received from a school grant program in the late 1990s. The authors exploit a newspaper campaign which allowed citizens to monitor the implementation of this grant program in order to test the hypothesis that districts with more access to the media have less corruption in the form of capture of public funds. Using reduced-form empirical analysis, the authors find that the public's and schools' access to information regarding education spending significantly reduces to the capture of public school funds by local officials and politicians from 80 percent in 1995 to less than 20 percent in 2001.

The proximity to a newspaper outlet is used as an instrument to correct for the endogeneity of head teacher's knowledge of the grant.

In one of the few country-level studies that does not use media access as a measure of transparency, Deininger and Mpuga (2005) use household-level data from the Ugandan Nationa Integrity Survey to test how transparency and accountability affect both corruption in service provision and quality of service delivery. The accountability and transparency variable used is the share of households that know the institutionalized procedure for reporting incidences of corruption. The authors find that knowledge of corruption reporting procedures significantly lowers incidences of corruption (households asked to pay bribes to service providers) and improves the quality of service delivery according to survey participants. While the transparency variable introduced by Deininger and Mpuga is a more direct measure of transparency than media access, it has the disadvantage of being a far more subjective measure.

Qualitative studies on the relationship between transparency, accountability, and development outcomes have the advantage of not needing to define a proxy for borad concepts such as transparency and accountability. Although these studies provide minimal empirical evidence of the relationship of interest, a few country case studies are worth highlighting in this literature review. In a largely qualitative study of transparency and accountability, Foster and Zormelo (2002) discuss the current prioritization of poverty reduction in Ghana's budgetary process, presenting the efficiency of public expenditures in key areas and the possible reasons for the relative failure of pro-poor spending in the country. The paper presents an extensive discussion of development outcomes in the areas of education, health, water and sanitation, roads, and agriculture, highlighting the overall failure of the Ghanaian government to ensure consistent improvements in these areas. The authors conclude by discussing why the government has failed in making poverty reduction a priority. This discussion centers on the overall lack of government integrity in the forms of budget discipline, accountability to the public, and transparency.

Ablo and Reinikka (1998) take a similar approach to health and education spending in Uganda. The authors consider the efficiency of public spending in developing countries and argue that budget allocations to public sectors institutions such as schools and health facilities do not have the intended effects on development outcomes because the promised funds do not reach intended facilities. Analyzing descriptive statistics from a Ugandan field survey, the authors find evidence that the effectiveness of public spending suffers from a lack of accountability in the transfer of funds from governments to education and health facilities.

The alternative approach that some authors have taken in investigating the relationship between transparency, accountability, and development is to model the cross-country variations in development indicators as a function of transparency. One of the few studies to explicitly investigate the link between transparency and development outcomes falls into this category of cross-country studies. Bellver and Kaufmann (2005) construct a transparency index for 194 countries, using information from twenty sources (including the International Budget Project). The overall index has two distinct components (economic/institutional and political). The economic and institutional transparency index incorporates country data on economic transparency, the integration of technology into governance, access to information laws, budgetary transparency, policy transparency, and transparency of the public sector. The authors find that higher income countries in general are also more transparent economically and politically.

While the link between development and transparency is not the primary focus of the authors, Bellver and Kaufmann do perform one set of empirical tests relating the transparency indices to human development outcomes. The authors regress three world development indicators (life expectancy, female literacy rate, and child immunization levels) on per capita GNI and the transparency index. The results confirm that transparency is highly significant in explaining variation in human development measures across countries; however, the authors caution against drawing conclusions of causation.

While research on transparency and human development is largely limited to the studies discussed above, a growing number of cross-country studies investigate the relationship between transparency, accountability, and the quality of governance. The results from this field of research largely confirm that increases in transparency and accountability improve the quality of governance and lower corruption. Although these studies do not extend their empirical analyses to development outcomes, much of this research is motivated by the assumption that good governance leads to advances in human development.

In a study of cross-country governance trends, Islam (2003) asks whether countries with better information availability also have better governments and hypothesizes that greater public knowledge about economic performance should be associated with improved political and economic outcomes. The author develops a transparency index to measure information flows using freedom of information laws and the frequency with which economic data is published, while she uses the Kaufmann-Kraay indicator (Kaufmann et al., 1999) and the International Country Risk Guide indices as measures of governance quality. The study finds that transparency is positively and significantly correlated with many aspects of governance, including effectiveness, control of corruption, accountability, rule of law, and bureaucratic efficiency. However, the addition of variables measuring media ownership weakens the results, suggesting increased transparency is only associated with higher quality governance if public information is presented by unbiased independent sources. Further, the author is unable to determine the direction of causation based on her empirical analysis.

In a study of fiscal transparency, Hameed (2005) creates a fiscal transparency index and four sub-indices (data assurances, medium-term budgeting framework, budget execution reporting, and fiscal risks) which he uses to compare transparency levels across countries. The author hypothesizes that increased fiscal transparency should be associated with a lower level of corruption and tests this hypothesis using simple regression methods. Hameed finds that fiscal transparency is negatively and significantly correlated with corruption; these results are robust to different measures of corruption including the Kaufmann-Kraay control of corruption indicator (Kaufmann et al., 1999) and the Transparency International corruption perception index. Although the author believes that transparency lowers corruption by making governments more accountable to the public, he is unable to determine causation and thus cannot provide direct evidence for this mechanism.

Although these empirical studies all find that good governance and low corruption are strongly correlated with greater transparency, Mehmet (2001) develops a theoretical model in which increases in transparency has two opposing effects on corruption. The author expresses that transparency does lower incentives for policymakers to engage in corrupt activities for fear of detection by the public. However, the model also presents a "connections" effect through which increased public awareness of corrupt officials allows members of the public to make connections with those people involved in illegal activities. The author does not specify which effect is likely to dominate, and he does not present any empirical evidence of increased transparency associated with increased corruption.

The current literature relating transparency, accountability, public expenditures, and human development present a solid foundation of evidence that increased transparency and accountability can lead to improvements in development measures. However, neither the cross-country studies nor the micro-level country studies are without large gaps in the literature. One of the major issues with both sets of studies is the large variation in definitions of transparency. Each paper outlined above uses a different definition of transparency, making comparisons across the literature more difficult. The cross-country studies generally employ an aggregate transparency index which allows for the incorporation of a number of transparency measures into one study. However, even authors of these studies recognize the inability of country-wide transparency indices to capture the many dimensions of transparency measures and reforms in a country (see Bellver and Kaufmann, 2005). Studies of individual countries allow researchers to focus on one specific and narrow definition of transparency; however, due to these narrow measures of transparency, the results from these studies are often difficult to extend to other countries.

Perhaps the greatest gap in the literature at this point is the absence of cross-country studies measuring a causal relationship between transparency and development outcomes. While the cross-country transparency literature has provided strong evidence of a correlation between governance and development measures and transparency, the cross-country have been unable to provide any evidence as to the direction of causation in this relationship. Authors of these studies have recognized this shortcoming and cite data restrictions as the primary reason for this gap in the literature.

5. <u>Empirical studies on governance, corruption, public spending, and development</u>

In contrast to the limited number of studies relating transparency and accountability to human development outcomes, there is an extensive literature linking governance and corruption with economic growth, development programs, and human development indicators. The majority of this literature focuses on the relationship between government institutions and economic prosperity. These studies test the hypothesis that aspects of governance rather than geographic characteristics explain the large variation in productivity and income across countries. The individual contributions of these papers are largely the introduction of new instruments for governance and institutions and the testing of different aspects of governance, including rule of law and corruption. A smaller subset of this field is motivated by the hypothesis that better governance and lower corruption can result in improvements in human development. Unlike studies in the transparency field, many of these studies are able to successfully determine causation in the relationship between governance and development.

The governance and growth literature has focused largely on the importance of institutions and rule of law in explaining income differences across countries. One of the first papers to empirically investigate this relationship is Hall and Jones (1999). The authors argue that differences in productivity rather than educational attainment or capital intensity explain vast differences in output per worker that is seen across countries. After providing evidence supporting this belief, the authors hypothesize that differences in social infrastructure (defined by the authors as institutions and governance) explain much of the international variation in productivity and thus worker output. The authors construct a social infrastructure variable using two indices – the International Country Risk Guide indices and the Sachs-Warner index measuring openness to trade. The paper employs a number of instruments to control for endogeneity, including two measures for the shares of country populations speaking Western European languages and English as first languages. The social infrastructure variable is highly significant in each of the specifications, supporting the hypothesis that governance and institutions have a large effect on economic performance.

Acemoglu, Johnson, and Robinson (2001) expand upon the work of Hall and Jones (1999) by explicitly considering the role of geography in determining per capita income. The authors repudiate the common belief that geography plays a role in determining the economic prosperity of a country, explicitly hypothesizing that institutions have a much greater effect on economic growth than does geography. Using a two-stage least squares approach, the authors find that geographical variables (including distance from the equator and an Africa dummy variable) are statistically insignificant when institutional quality is controlled for. In the specifications of the model, institutional quality is measured as the risk of expropriation index of the International Country Risk Guide indices. The major contribution of this paper is the introduction of settler mortality rates in former European colonies as an instrument for institutional quality; the justification for this instrument is that more extractive institutions were set up in colonies with higher potential settler mortality rates and that these institutions carry through to modern times.

Rodrik, Subramanian, and Trebbi (2004) introduce a third separate component, trade openness, into the debate over determinants of economic growth. The paper starts with the hypothesis that institutional quality (rule of law in particular) explains the majority of income variation between countries while geography and trade play minor roles in determining economic growth. The authors run a series of regressions of country per capita income on measures of geography, trade, and institutions, using instruments for the latter two in order to determine the direction of causation. Using property rights and rule of law as indicators of institutions, the results of the model show that institution variables are consistently significant with the expected sign, whereas trade variables are insignificant and geography variables are, at best, small and weakly significant. In fact, the authors find that the measure for trade openness is negatively correlated with per capita income in many specifications. Like Acemoglu et al. (2002) and Hall and Jones (1999), the authors instrument for institutional quality with variables for settler mortality and English and Western European language as first language.

Although many studies consider the relationship between economic growth and quality of governance, Kaufmann and Kraay (2002) is one of the first studies to explicitly separate out the direction of causality and to provide evidence against the common belief that improved economic performance leads to improvements in governance quality. The authors use the Kaufmann-Kraay governance indicators (Kaufmann et al., 1999) and per capita income levels as measures of governance quality and economic performance, respectively. In order to determine the effect of economic improvements on governance quality, the authors use non-sample information, isolating the variance of measurement errors in the governance and income variables and the correlation of error terms in the simultaneous governance and income equations. The results indicate that per capita income in fact has a weak negative impact on governance quality, rejecting the idea that “virtuous circles” exist in countries and governance and income improvements reinforce each other.

While these studies present solid evidence that governance quality is a major determinant of economic growth, the papers outlined above do not provide any information about the effect of governance on inequality. Although economic growth is certainly important in developing countries, a rise in per capita income does not necessarily imply an improvement in human development, particularly among poor and rural parts of the population. A growing number of studies have adopted some of the methods and governance indicators from the governance and growth literature and have applied them to investigations of public spending and development outcomes. While researchers in this field adopt a wide range of dependent variables, these papers all attempt to demonstrate that improvements in governance and control of corruption lead to an improvement in various measures and indicators of human development.

Although much of the governance and corruption literature in this area has focused on economic growth as a dependent variable, a growing number of studies attempt to measure the effects of corruption and governance on public spending. Mauro (1997) tests the hypothesis that decreases in corruption levels lead to a reallocation of public expenditures towards social development programs. In a cross-country study, the author employs both the International Country Risk Guide index and the Business International corruption index as measures of corruption and finds a significant negative correlation between both corruption variables and government expenditure on education as a percentage of GDP. Although he tests causality in this study, Mauro finds mixed evidence that corruption causes lower education spending.

In the governance literature, Kaufmann et al. (1999) take a similar approach to Mauro (1997), focusing on development outcomes rather than composition of public spending. The authors hypothesize that better governance leads to improvements in human development measures such as literacy and infant mortality. One of the major contributions of this paper is the creation of governance indicators (now widely used in this field of research) that incorporate measures of accountability, government instability, effectiveness, regulatory burden, rule of law, and graft. In one of the few studies in this field to isolate the direction of causation, the authors use instruments created by Hall and Jones (1999) to find evidence that good governance has a significant positive effect on per capita income and literacy rates and a negative effect on infant mortality.

Although they start with the same hypothesis as Kaufmann et al. (1999), Rajkumar and Swaroop (2002) employ a variable that interacts government quality and sectoral public spending to test the relationship between governance quality and effectiveness of government spending. This method allows the authors to test the effect of governance quality on not only development outcomes but also the effectiveness of spending in improving development outcomes. Using data from ninety countries in 1990 and 1997, the authors find that countries with low levels of corruption and high bureaucracy quality (measured using the International Country Risk Guide indices) experience improvements in child and infant mortality rates and primary school attainment when they increase the share of public spending on health and education, respectively. For countries that are highly corrupt or have poor governance quality, the authors show that increasing spending on health and education has no significant effect on these development outcomes.

Although the majority of studies in this field use a cross-country anaylsis, a more recent study by Azfar and Gurgur (2005) considers variations in corruption levels across communities within the Philippines. Because much corruption occurs at the local rather than national level, this study provides useful information about how variations in corruption across communities can impact development. The authors hypothesize that communities with higher levels of perceived corruption will have worse health and education measures. Although the authors use a subjective measure of corruption (corruption level perceived by residents, officials, and administrators), they are able to show that communities with high levels of perceived corruption also rank poorly in a wide range of health and education measures, including immunization rates, average age of immunization, access to public health clinics, satisfaction with public health services, school rankings, test scores, and parent satisfaction with schools. While this study presents an interesting alternative to the cross-country studies outlined above, it is difficult to extend the implications of these results to other countries.

In one of the few studies to link governance to intra-sectoral allocation of public spending, Stasavage (2005) exploits the recent democratization of many African countries to test the effect of political accountability on composition of education spending. The author starts with the hypothesis that the need for an electoral majority has led African politicians to reallocate education spending towards primary schools as opposed to universities. Using longitudinal data from forty-four African countries during the period 1980-1996, the study presents evidence that multiparty competition is associated with increased primary school spending; however, the change in governance was not found to be correlated with a change in university-level expenditures.

Similar to the transparency and accountability literature, the literature relating governance and development outcomes suffers from the lack of a common definition for governance quality. While many of the studies outlined above adopt the same governance indicators, the authors have focused on different components of these indices. The Kaufmann-Kraay governance indices, for example, have six separate components, and different studies focus on different aspects of governance. As a result, the studies above reach no consensus about the relative merits of different aspects of governance in improving human development. Unlike the transparency literature, studies of governance, expenditure, and human development present solid evidence of not only the significant correlation between development measures and governance but also the causal effect of governance and corruption on social development.

6. <u>Participatory budgeting</u>

The idea of participatory budgeting has gained prominence in recent years as a means for citizens to become more involved in government expenditure decisions and for governments to be more accountable to the people who are benefiting or suffering from budget decisions. The majority of studies on the relative success of participatory budgeting have been based on case studies. The overwhelming conclusion that researchers have drawn from these case studies is that participatory budgeting can be successful at implementing pro-poor policies and spending, but effort needs to be exerted to ensure that citizens and government officials are involved in the process.

Bräutigam (2004) reviews examples of participatory budgeting in Ireland, Chile, Costa Rica, Mauritius, and Brazil and finds that these programs have had mixed results in terms of improving policies directed towards the poor. Based on the results from these five cases, the author concludes that three issues play an important role in determining the success of participatory budgeting – who participates, the institutions necessary for pro-poor participation, and the revenue side of budgeting. The case studies indicate that both civil society and government officials need to have a pro-poor leaning in order to ensure money is allocated to poverty reduction programs. The study also indicates that transparency and accountability must be institutionalized in order for participatory budgeting to be successful. Finally, the author expresses that the revenue side of budgeting is often ignored by the public in participatory budgeting; however, these programs are not sustainable unless citizens consider both the expenditure and the revenue side of budgeting.

Heimans (2002) reaches a similar conclusion but focuses more on the agents involved in participatory budgeting (civil society, government, and legislatures). The author's major finding is that all agents must be actively involved in the budgeting process in order for it to be successful. The paper is largely directed towards international donors, concluding with policy recommendations for donors interested in improving participatory budgeting in developing countries.

Much of the literature on public participation in budgeting and policymaking considers how civil society organizations (CSOs) can have a greater impact on incorporating the public's interests into policymaking. Pollard and Court (2005) present an excellent review of the literature on civil society organizations and analyze the strategies that CSOs use to influence the policymaking process. The authors identify seven goals that organizations should have in order to maximize the influence that they have on government officials – legitimacy of organizations, effectiveness, integration of stakeholders, translation of technical evidence, access to the policymaking process, credibility, and communication (both vertical and horizontal).

Robinson (2006) develops a more targeted study of six civil society organizations in Uganda, South Africa, Croatia, Brazil, India, and Mexico and analyzes the impact that these CSOs have on the transparency of the budget process and on pro-poor spending decisions. Although the author presents a thorough discussion of the successes of these organizations, he spends little time on changes that could be made to increase the effectiveness of budget-focused organizations. In contrast, Ghaus-Pasha (2005) highlights specific ways in which CSOs can impact investment, social services, poverty alleviation, and relief work. Although she does not isolate her discussion to budget-focused organizations, the author does investigate ways in which organizations can improve the overall quality of governance, particularly by increasing the voice and awareness of citizens. The author concludes with a discussion of the role of civil society organizations in reaching the Millennium Development Goals.

In one of the few studies to analyze country-wide citizen involvement in budgeting, Devas and Grant (2003) discuss examples of "good practices" in Uganda and Kenya while discussing areas in which more work is needed. The authors look at the role of vertical downward accountability (accountability of the local government to civil society) and the potential of the media to increase the public's knowledge of local budgeting practices. Although they discuss the role of transparency and accountability at length, the authors do not directly tie these concepts to service delivery, health, or education outcomes, nor do they present solid evidence for the effects of transparency and accountability on spending. Instead, the paper focuses primarily on examples of transparency and accountability in specific budgetary practices in Uganda and Kenya.

Although these conceptual discussions of participatory budgeting are valuable in documenting the trend towards civil society involvement in expenditure management, the literature on this subject suffers from a lack of quantitative papers measuring the true impact of participatory budgeting programs on spending allocations and human development outcomes. This gap in the literature is probably largely due to the relatively recent rise in popularity of these programs; the original participatory budgeting program was introduced in Porto Alegre (Brazil) in the mid-eighties, and subsequent programs were in their infancy in the mid-nineties. A quantitative analysis of these programs has the potential to contribute to evidence of the impact of transparency and accountability on social development. Further, econometric studies of participatory budgeting could provide an explanation for why public spending does not have a strong effect on human development. At this point, however, the participatory budgeting literature remains highly qualitative and case study-based.

7. Conclusion

The sub-set of literature on transparency and human development has a strong foundation in the larger area of the efficiency of public spending. A long and extensive literature has focused on measuring the effect of government expenditures and allocation of public resources on measures of human development such as educational attainment and infant mortality rates. The broad consensus reached by these studies is that government expenditures have a small or insignificant effect on development indicators, which leads to the question of why public spending does not have the desired effect. Although a number of theoretical models have been proposed to answer this question, many of these models center on the assumption that government does not act efficiently with regards to public expenditures. These models largely propose that government efficiency can be increased by making government policies more transparent and by increasing the accountability of public administrators to civil society.

The empirical tests of these theoretical models of transparency and accountability have been small in number and have only partially bridged the gap in the literature between conceptual discussion and quantitative evidence of the link between transparency and human development. Studies within countries have provided evidence that public access to information and political competition has led to increases in pro-poor spending and satisfaction with service delivery in developing countries. The narrow definitions of transparency and accountability and country-specific programs highlighted in these models, however, make it difficult to extend the results of these studies to other countries. A limited number of cross-country studies have employed aggregate transparency indices to test the extent to which transparency explains variation in development outcomes across countries. These studies, in particular Bellver and Kaufmann (2005), provide significant evidence that economic and political transparency is positively correlated with measures of human development such as literacy rates. However, these studies all suffer from the inability to assign causation in the relationship between development and transparency.

Although the interest in relating transparency and development continues to grow, a more extensive related literature explores the relationship between governance quality, corruption, and human development indicators. Overall, these studies find significant evidence that higher quality of governance and lower levels of corruption lead to increases in economic growth and improvements in development. While these studies do not focus on transparency, they represent an important contribution to the transparency literature for two reasons. First, many of the econometric methods and models developed in the governance literature could be extended to transparency indices in cross-country studies. Second, many studies in the transparency literature present evidence of a significant negative relationship between level of corruption and degree of transparency, in which case declines in corruption can be seen as one avenue by which transparency can impact development outcomes.

The literature on transparency and development has major implications for developing country policies, including participatory budgeting. Advocates of participatory budgeting programs argue that transparency and accountability are two of the key features that determine the success of these programs in improving pro-poor spending and policies. However, quantitative studies of the effects of public expenditure management reforms are needed in order to determine whether these policies that improve transparency can result in reallocation of public funds and overall improvements in human development.

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