INTERNATIONAL MONETARY FUND

October 2, 2018

2018 REVIEW OF THE FUND'S CAPACITY DEVELOPMENT STRATEGY—EXTERNAL COMMENTARY AND BACKGROUND STUDIES

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[1] These papers represent the views of the authors and do not necessarily represent IMF views or IMF policy. The views expressed herein should be attributed to the authors and not to the IMF, its Executive Board, nor its management.

BOX

ANNEX

Acronyms

AFR	African Department
APD	Asia & Pacific Department
BTOs	Back-to-Office Reports
CAP	Capability Assessment Program
CCB	Committee on Capacity Building
CD	Capacity Development
CSN	Country Strategy Notes
DAC	Development Assistance Committee
EUR	European Department
FAD	Fiscal Affairs Department
FARI	Fiscal Analysis of Resource Industries
FSAP	Financial Sector Assessment Program
FSSR	Financial Sector Stability Review
FTEs	Fiscal Transparency Evaluations
IEO	Independent Evaluation Office
LEG	Legal Department
MCD	Middle East & Central Asia Department
MCM	Monetary and Capital Markets Department
MOOCs	Massive Open Online Courses
PDIA	Problem-Driven Iterative Adaptation
PEFA	Public Expenditure and Financial Accountability
P-FRAM	Public-Private Partnership Fiscal Risk Assessment Model
PIMA	Public Investment Management Assessment
RA-FIT	Revenue Administration Fiscal Information Tool
RA-GAP	Revenue Administration Gap Analysis Program
RAP	Resource Allocation Plan
RBM	Results-Based Management
RSN	Regional Strategy Notes
RTAC	Regional Technical Assistance Center
RTC	Regional Training Center
STA	Statistics Department
TA	Technical Assistance
TADAT	Tax Administration Diagnostic Tool
WHD	Western Hemisphere Department

EXTERNAL COMMENTARY[1]

A. Institutions Matter

1. Policies matter but institutions probably matter more. There is a vast economic literature that shows that institutions are critical determinants of whether countries are rich or poor, stable or instable, good at improving the welfare of their citizens or not.[2] Of course, better institutions make better policies, but that is the point—weak institutions can adopt good policies (including under an IMF program), but strong institutions can sustain good policies over the long term. That is what makes the IMF's work on capacity building such a vital part of its mission.

2. Sadly, there is no recipe book for building strong institutions. Research by political scientists and economists like Putnam, Acemoglu, and Robinson tend to point to historical evolution and sometime flukes, and they conclude that it takes decades for institutions to evolve and grow.[3] But it is also possible to point to important reforms—like meritocratic hiring, investments in training, clear targets and accountability, adequate budgets, and well-defined processes for formulating and adapting policies that have shaped good institutions. The IMF's work in capacity building has historically focused on training and policy advice, paying less attention to whether institutions have adequate resources or processes for making decisions, a theme to which I will return.

3. The IMF's work on capacity development (CD) is at a critical juncture. It has grown to be about one-third of the IMF's work and it seems unlikely that it will grow further as a share of total activity. The quality of the work has always been excellent and is valued by countries as such. The Fund has now built a global network of training and technical assistance (TA) centers that reaches every corner of the world. CD at the Fund historically had two distinct streams—training and TA—but since the 2013 strategy there has been an attempt to integrate them further.[4] There have been reforms to improve prioritization and introduce results-based management (RBM). The main areas for improvement are that it is hard to measure progress and ensure the thousands of TA reports and hundreds of thousands of training hours are having a sustained impact on building better economic institutions in member countries. That, I think, is the critical question for the future and will be the focus of this "think piece."

4. Let me start by acknowledging the many areas that are going well. These include the improvements in capacity achieved thus far, the creation of a global network, the strategic

[1] Prepared by Minouche Shafik, Director, London School of Economics.

[2] D. North, *Institutions, Institutional Change and Economics Performance* (Cambridge University Press), 1990. For cross-country econometric evidence showing that nations with high quality institutions outperform those without them, see R. Levine and D. Renelt, "A Sensitivity Analysis of Cross-Country Growth Regressions," *American Economic Review*, Vol. 84, No. 4 pp. 942–963, 1992.

[3] R. Putnam, *Making Democracy Work: Civic Traditions in Modern Italy* (Princeton: Princeton University Press), 1992. Daron Acemoglu and James A. Robinson, *Why Nations Fail: The Origins of Power, Prosperity and Poverty*, (Crown Publishers), 2012.

[4] I should declare an interest since I oversaw this strategy in my role as Deputy Managing Director at the time.

partnerships with donors, and prioritization. There is another set of issues where progress has been made, but more is needed—such as integrating TA and training, embracing digital opportunities and RBM. In the final section, I will try to identify some newer, longer-term issues that might shape the Fund's work in future.

B. What is Going Well?

The Bar is Higher

5. **Perhaps the most striking change in my personal experience of working with government ministries, central banks, and agencies over 30 years has been the massive increase in expertise across most low- and middle-income countries.** Today most countries have staff that are trained in good universities and access to information and comparative practices around the world that once used to be the sole purview of the international agencies. They have multiple sources of advice and training—through regional organizations, private consultants, universities, and international agencies. The Fund can take some credit for this progress, but it also means that for most countries the bar on the quality of CD work has also gone up and the support needs to be more targeted and specific.

A Global Network

6. **The Fund has also successfully created a global network of 16 regional CD centers that can reach every member country in the world.** Staff are close to government officials and can respond quickly to requests for advice. Training is now conducted in five languages. That extensive infrastructure has been a huge investment and by and large feedback from member countries has been overwhelmingly positive. I suspect the returns to further expanding this network are low and the overheads and organizational complexity make it not worthwhile. The only exception might be where there is an opportunity to consolidate and build more integrated CD centers that deliver TA and training under one roof.

Prioritization

7. **Prioritization and resource allocation are perennial problems given that the IMF rarely charges for CD (the arguments have been well rehearsed and I won't repeat them here).** For prioritization between countries, the lessons of experience are clear—governments that are keen to reform are more likely to use advice and training effectively. It is not surprising that reviews of capacity building usually find that countries with an IMF program use CD well because there is a strong imperative to implement successful reforms when there is a political window of opportunity. For prioritization within countries, area departments are key and the Fund has developed improved mechanisms for them to influence the topics and institutions of focus. There will always be tension between who controls budgets and who picks what topics are addressed in a particular country, but much of this is healthy debate and by and large I think recent reforms have improved priority setting considerably.

CD and Surveillance

8. IMF surveillance often does a good job of identifying where capacity falls short, but could go one step further in putting it in the context of the institutional realities of the country. Integrating CD into the surveillance process is often challenging, partly because there is not the sense of urgency that exists in program countries. Some have argued that CD priorities and issues should be mandatory in Article IV consultations to insure they are adequately addressed. I would be wary of this since it risks becoming a "tick box" exercise. Instead, I would encourage greater use of country CD strategies jointly developed between the Fund and the authorities where it is likely to matter most—particularly in fragile states, low-income countries, and countries undergoing major structural transformations.

C. Areas Where There is Progress, But More is Needed

TA and Training

9. Integrating TA and training is absolutely key for institution building and while some important progress has been made, I think more needs to be done. There is now considerable evidence that policy advice absent the skilled individuals to implement it is ineffective. Similarly, training individuals and putting them back in institutions that have dysfunctional policies is a recipe for frustration.

10. Governments want to build capacity to do things—collect taxes, manage their debt, promote financial integrity, implement monetary policy—and they often want their staff trained in the areas where they have received policy advice but lack the capability to implement it. From the recipient's perspective, it is all part of the same objective of being able to do something that is important—not two distinct product offerings by the IMF. The Fund has achieved the most progress in delivering what countries need in integrated regional CD centers, and there has been welcome integration and diversification of the IMF's offer including modular and customized training and more "hands on" support to implementation. These developments should be encouraged going forward.

11. The challenge of integrating TA and training is most acute in states where capacity is weak, everything appears to be a priority and more direct support is needed for implementation. The Fund did try a different approach in Libya and Tunisia where they conducted extensive institutional diagnostics shortly after the regime change, followed by a comprehensive reform program for the central bank and finance ministries in those countries. The lessons from that experience point to it having been costly, perhaps too comprehensive to be implementable by the authorities and difficult given the huge political upheavals occurring in both countries. I think investing in better country CD strategies could be a better approach in future, perhaps focusing initially on countries in more stable situations to learn lessons before tackling more challenging cases.

Digital Opportunities

12. Another area of progress has been the response to the digital revolution. The Fund was an early adopter of online learning, being the first international organization to offer massive online courses through the EdX platform and using blended learning for core offerings. This has doubled the reach of IMF training from about 8,000 individuals in 2013 to 16,000 in 2017. There is great potential to expand this even further—by using digital means to expand access to training, explore policy issues, create communities of practice, and provide "real time" TA. Partnering with other providers to share IMF content and case studies also seems a good opportunity to expand impact even further given how many other organizations are investing in digital learning.

Donor Partnerships

13. The relationship with donors has also evolved positively. The development of strategic partnerships with some large donors, alongside more specific collaborations with smaller donors has been a good approach that results in a more efficient use of resources and provides greater stability of funding for CD. These partnerships also enable the Fund to do more for member countries, foster knowledge sharing, and the development of peer networks—all of which contribute to stronger institutions over time. Donors should increasingly focus less on extensive reporting to them and ask for more evidence on implementation and impact. They should also be encouraging publication of findings from CD as an important public good that could benefit all countries.

Results-Based Management

14. Finally, the Fund is making an important investment in RBM which it should continue. It is important to be realistic about what can be measured and continue to work on improved methods of measurement. Eventually RBM can become a tool to help with prioritization as it becomes possible to assess which types of interventions are the most effective. At a minimum, it will help considerably with donor accountability and assessing the efficiency of the IMF's own delivery. Ideally it will be able to answer questions about whether investments in CD are delivering better institutions. But, as in many domains in life, the most important things are very hard to measure and a mechanistic approach should be avoided.

D. What Could be Different in Future?

More Attention to the Nuts and Bolts of Staffing and Decision-Making Processes

15. Most who have worked in public service know that the quality of decision making depends mostly on the caliber of staff and the decision-making processes, including data collection, analytical capacity, mechanisms for accountability and challenge, and the ability to adapt and adjust policies to changing circumstances. The Fund pays less attention to these kinds of issues in its CD work, although seasoned bureaucrats will tell you they matter more than training and external advice.

16. I recall when I was at the Bank of England and macroprudential policy was in its infancy, we had many officials come to ask questions about how we operated our relatively new Financial Policy Committee. Their questions were often very practical. How did we choose and prioritize topics for our agenda? Who prepared the papers? How were external members briefed and supported? How were decisions implemented? These are the nuts and bolts of policy making, and the Fund could do a great service to countries by synthesizing these experiences and sharing that knowledge.

17. Fund staff do venture into this terrain in areas like tax administration, but I think the need is far greater and there is huge value in (at a minimum) sharing cross-country experience. It would be useful to have cross-country data on qualifications of staff in economic ministries, numbers of staff in tax administrations or statistical authorities, mechanisms for evaluating policy effectiveness, procedures for review and challenge in policy deliberations. Over time, the Fund will build its own expertise of what practices work best in which contexts, thereby being able to give not just "best practice" advice but also "best fit" advice. Donors should be encouraged to support such work given its wider value.

Fragile States

18. Countries coming out of conflict or plagued by fragility present the greatest challenge for CD because institutional development has stagnated or in some cases regressed. While many of the IMF's clients for CD have seen substantial improvements, those in fragile states require a fundamentally different approach. The imperative is to build institutional capacity and legitimacy, even if the policies are not ideal. The recent Commission on State Fragility, Poverty, and Development recommends that the focus should be on helping governments implement their own programs subject only to a minimum standard of economic governance such as honesty, realism, and inclusion.[5] Engagement on the basics of institution building (hiring practices, resources allocation, consultation mechanisms) would be consistent with such an approach.

19. Given that the bulk of the world's poor will increasingly live in fragile states, there will be considerable expectations for the Fund to have an effective approach. I would argue that CD work in those countries needs to be based on in-country or regional training blended with TA focused on putting in place basic processes that support government policy making and support for implementation. This would imply a strong focus on areas such as public financial management and adequate resourcing of government institutions and supporting decision-making process and implementation. Time frames should be realistic, and there should be less focus on writing reports and accountability to donors and more on supporting weak governments to achieve institutional milestones and results.

[5] The Commission on State Fragility, Growth and Development (March 2018) was chaired by David Cameron and supported by the London School of Economics and Oxford University. It drew on extensive academic research as well as public evidence sessions to identify successes and failures in fragile states and to make recommendations on how their challenges could be better addressed in future.

Transparency

20. The IMF has already made progress in making its training materials a public good through the use of Massive Open Online Courses (MOOCs). The lessons of IMF TA are also a public good and yet fewer than 5 percent are ever published because few recipient governments authorize publication. That is clearly too low. Publishing more of the IMF's TA reports and providing regular studies that synthesize experience across countries would also be helpful in expanding the impact of the Fund's work making the lessons of advisory work more widely available.

21. Clearly it is important to maintain the trust and confidence of authorities, especially when reforms are politically sensitive. Countries can currently redact from TA reports information that is market sensitive or policy intentions that have not yet been announced. This must be done in a way that does not undermine the integrity and independence of staff advice. One option would be to move to an "opt out" system whereby the presumption would be that all reports would be published unless authorities request otherwise. Another possibility is to publish all reports after a certain amount of time has passed, say 3–5 years, when the findings may be less sensitive.

Topics of Focus

22. Countries' demands for IMF capacity building are also changing in terms of the topics that are priorities. The joke that IMF stands for "It's Mostly Fiscal" certainly applies to capacity building. Fiscal policy advice, especially around taxation, continues to be the largest share of TA. But the growing demand for advice on monetary policy and the financial sector is welcome, especially after the financial crisis, when demand for assistance on financial stability issues rightly grew. The Fund has also innovated and offered advice in new areas such as energy subsidies, inequality, gender, and climate with a focus on macro-criticality. It seems appropriate for the Fund to continue to respond in this demand-driven way in future since responding to country priorities is the best insurance that advice will be used effectively.

23. What other issues might be on the horizon? I suspect some issues that have fallen off the agenda—like trade and debt management—may become important again given rising protectionism and debt levels. I also think that new issues like how to apply machine learning and artificial intelligence to areas like tax policy, big data and statistics, and how to regulate digitally driven parts of the economy will also move up on the agenda. As in the past, the Fund will need to respond to countries' needs and perhaps initially draw on outside expertise until internal capacity to respond is developed. A good example of this is the recent efforts by the Statistics Department (STA) to develop new partnerships to help countries use innovative data tools to improve policy making.

Peer Learning

24. Given improvements in capacity in many countries and the possibilities enabled by the digital revolution, the Fund could create even more opportunities for peer learning and good practice sharing among policy makers. This already happens to some extent during the Annual and Spring Meetings for the most senior officials. But there are few opportunities for middle and junior level officials to learn what others are doing in areas like banking supervision or tax administration. The Regional Technical Assistance Centers (RTACs) do some of this, but it needs to be a more explicit part of the offer and should include greater engagement from headquarters to provide a global perspective.

25. The Fund also has a unique role to play in establishing norms and standards of good practice in many areas of economic policy making, as it has done with statistics and on anti-money laundering. This is another area where peer learning would be very valuable in building international consensus on emerging areas of policy making. For example, the Bank for International Settlements has done a very good job of creating opportunities for peer learning among central bankers, even though TA and training are not a major part of their work. By creating opportunities for interaction and comparing notes around substantive issues among policy makers at various levels, they have managed to "improve everyone's game." I suspect there is a market for such a forum among officials in finance ministries who could benefit from comparing notes on emerging issues—like taxation in the digital economy or lessons on managing capital flows.

26. There may also be an appetite for peer reviews of entire institutions, such as those facilitated by the OECD for development agencies. The Development Assistance Committee (DAC) of the OECD facilitates intensive reviews of development agencies by two of their peers in other countries supported by OECD staff. This process provides important learning across development agencies, both for the countries involved and for DAC members collectively who benefit from the reports. It has been key for building support for international policies like aid harmonization and coordination and the importance of building and using country systems.

I. A REVIEW OF THE IMF'S EFFORTS TO STRENGTHEN INDIVIDUAL AND INSTITUTIONAL CAPACITY[1]

Summary

1. **Building institutions and strengthening capacity are among the most difficult challenges in the long process of development.** These processes take many years, the path to success is often unclear, and it is difficult to measure progress. Nevertheless, there has been progress in many developing countries in building capacity, especially in central banks and other areas in which the IMF works. The Fund can take some credit for this success, but there is still far to go. Although the Fund's CD efforts have improved, there is scope for further strengthening in the future.

2. **Committed and effective leadership within target organizations is perhaps the most important ingredient for strengthening institutions and capacity.** Where that leadership exists, progress can be achieved; where it is absent, progress is much less likely. In turn, the Fund should focus more of its CD activities in countries and organizations with committed leadership that can own and embrace these efforts, and less in situations where committed leadership is absent.

3. **Closely related to leadership is importance of country ownership:** CD efforts must be owned, embraced, understood, and guided by the leadership of the organization (or sub-unit of the organization). Although the Fund has shifted towards more country ownership, there is still a tendency in some cases for Fund staff implicitly to take the lead in some CD efforts.

4. **The Fund (and other partners) should encourage leaders of target organizations (and sub-units of organizations) to develop a concise and targeted CD strategy.** These strategies should be country-owned, short, succinct, focused, and set a small number of priorities (and thus differ from many strategies that are not fully owned), are too comprehensive, and not prioritized. The Fund's role should be to encourage the leadership to develop a concise strategy, to provide support as appropriate, be willing to compromise on the objectives and strategy, and assist in implementing the strategy alongside other partners. This does not mean that the Fund must always follow whatever the local authorities say they want to do. If the strategy does not make any sense, the Fund and other partners can decide not to support it.

5. **The Fund can strengthen its CD efforts by organizing training and TA for each country as an integrated series of modules and interlocking pieces that reinforce each other and that are designed to foster ongoing and regular engagement with local authorities.** The Fund's CD efforts are still too fragmented, and therefore miss opportunities for mutual reinforcement. In turn, better integration will require enhanced internal coordination within the Fund so that the CD-delivering departments work more closely together to meet the needs of the target organization. The area departments should play a central role in improving internal coordination in CD efforts.

[1] Prepared by Steven Radelet, Georgetown University.

6. The Fund should explore the possibility of introducing (or supporting) training and other advice focused on building leadership, management, strategy development, and related skills. These skills are central to the effectiveness of long-term CD efforts, and therefore to the Fund achieving its core goals. If the Fund cannot take on these training roles directly, it should work with other groups with management and leadership expertise (e.g., business or public policy schools), or with other donors that can support these efforts. What the Fund should not continue to do is to simply ignore these critical skills and assume that somehow they will take care of themselves.

7. One of the IMF's most important successes has been in creating global norms of practice and standards of behavior among central bank governors, ministers of finance, and other senior finance officials. The Fund should more intentionally aim to create and strengthen these norms at deeper levels within organizations, and recognize that doing so is a core CD activity. It can do so by purposefully bringing together the same group of people over time for workshops, on-line forums, aimed at fostering a community of people across countries that share experiences, develop standards of behavior, and create some healthy competition for countries to move forward in their CD efforts. The Fund should continue to emphasize and develop peer-to-peer CD efforts, which can be particularly powerful and effective means of transmitting ideas, lessons, and experiences.

8. There is broad endorsement for the Fund's introduction of a more structured approach for RBM. Nevertheless, CD efforts pose particular challenges for RBM, since CD is inherently difficult to define and measure, takes a long time to achieve, and usually does not unfold in a neat, linear process. As a result, achieving intermediate benchmarks may not necessarily lead to improved long-term functional performance. In addition, if local authorities are not fully involved, they may begin to feel that RBM is a form of "stealth conditionality." The Fund can reduce these risks by ensuring that the RBM system is flexible enough to allow for some degree of experimentation, iteration, and adaptation. It should regularly assess targets to ensure that they are moving towards desired long-term outcomes. Local authorities must be involved in establishing metrics and goals, and must understand and internalize these goals. The Fund should work with the donors funding the system to allow for longer-term time horizon in CD efforts, avoid focusing too narrowly on easily achievable targets, and investing in new data as needed to improve metrics.

9. The Fund's CD activities face particular challenges in fragile states, where there tends to be more political and institutional instability, frequent reversals of direction, greater vulnerability to shocks, lower initial capacity, and weaker governance. As a result, progress is likely to take even longer, the costs are higher, and the path forward is less clear. The key question in fragile states, as with any country, is whether there are local leaders that are committed to taking the hard steps necessary to build capacity over time. The Fund should devote greater resources to CD efforts in fragile states with weak capacity but committed leadership; it should invest less so in countries without that committed leadership. The initial focus should be on basic building blocks that are relatively simple and require less implementation, such as exchange rate management, payments systems, budget frameworks, and collecting customs duties. It will be particularly important to engage fragile states with interlocking modules of CD activities, even if these are of smaller scale, and reinforce these activities over time. Achieving sustained progress is likely to require a stronger presence on the ground with additional resident advisers and additional training and TA.

10. In countries where individual capacity is particularly weak, in some circumstances the Fund should consider utilizing a time-limited "capacity supplementation" approach, in which it could work with other donors to hire experts to work in target organizations to carry out key functions (i.e., not just as advisors). This approach should be time-limited and be combined with efforts to identify, train, and place a national expert in the position as quickly as possible, ideally to work directly with the expert during a transition period.

11. The most difficult situations are fragile states in which there are no local leaders that are champions for reform, and the authorities show no interest in capacity building or reform. In these situations, the Fund should scale back its efforts, and focus on strengthening relationships, possibly with some limited CD efforts, and building the case for reform with the hope that the situation may change in the future and these efforts may eventually bear fruit. In effect, the Fund should play a much more patient, longer game. It should devote much less time and other resources to fragile states that show little interest in CD.

A. Introduction

12. Building institutions and strengthening capacity are among the most difficult challenges in the long process of development.[2] These processes take a long time—many years, or even decades. There are no shortcuts, and success cannot be achieved during the three-year project cycle in which most donors operate. Moreover, the path to success is often unclear: there is no well-defined course of action that works across organizations and countries, or that can be copied from one case to the next. Institution building is highly context-specific, so it requires creativity, experimentation, determination, the willingness to take risks, and the flexibility to change course as needed. It is also hard to measure progress, in part because of the uncertainty of the path to success, but also because key aspects of "capacity" are difficult to conceptualize, define, observe and quantify.

13. Despite these challenges, there is general agreement that many developing countries—indeed most—have made important progress in strengthening institutions and building capacity over the last three decades, especially in the areas where the IMF works most closely.[3] Central banks in particular have much more capability both at the individual level, with more trained and experienced experts, and at the organizational level, with greater independence, and more ability to undertake and perform their key tasks well: manage exchange rates, control inflation, monitor banks, and ensure overall macroeconomic stability.[4]

[2] Daron Acemoglu and James Robinson, *Why Nations Fail: The Origins of Power, Prosperity, and Poverty* (New York: Crown Publishing), 2012.

[3] Steven Radelet, *The Great Surge: The Ascent of the Developing World* (New York: Simon & Schuster), 2015.

[4] While there is general agreement on this point (at least for financial institutions), it is very difficult to prove or disprove the point, largely because of weaknesses in the data on institutions and governance. Some of the key indicators (like the World Bank's Worldwide Governance Indicators) are constructed to measure each country's performance relative to the global median in a given year. While an individual country can show progress over time relative to other countries (or to the median), large groups of countries (and especially all countries as a whole) cannot show progress by these measures because they are measured relative to the median.

14. The IMF can (and should) claim some success in supporting this progress. The Fund has helped provide advice, TA, training, and funding to help countries improve policies, strengthen implementation, and improve organizational effectiveness. Importantly, it has also helped build and strengthen institutional and individual norms of behavior and performance, such as around the importance of central bank independence, control of inflation, and personal probity among financial leaders. But while there is agreement that central banks and ministries of finance are stronger and more effective than they were in the past, there is equally strong agreement that in many countries there is still far to go, especially deeper in organizational hierarchies where there are fewer highly skilled personnel and more complex tasks are undertaken.

15. This short paper examines some of the IMF's efforts in capacity building in terms of both individual capacity and institutional capability. It draws on interviews with IMF staff in area departments, CD-providing departments, and in the field, alongside outside experts (from governments, donor agencies, and academia) and relevant literature. The paper explores how the Fund can target its efforts for greater and more sustained impact over time. It examines a range of actions the Fund could take to make its work in capacity building more effective and concludes with several specific recommendations.

B. Starting Points and Context

16. Several major points emerged in nearly all of the interviews conducted for this report that are worth emphasizing at the outset.

- First, there is widespread agreement that one of the most important ingredients for building successful institutions and strengthening capacity over time—perhaps the single most important ingredient—is effective leadership within the country and within the particular organization that is the focus of attention. There is no substitute for a leader (and even better, a leadership team) that is committed to improving an organization's performance and achieving its core objectives over time. In the absence of such leadership, there is far less that the IMF can do (or any other outside group), and far less progress that can be achieved. Closely related to leadership is the importance of country ownership in capacity building efforts. It almost sounds cliché to emphasize the value of country ownership, but it is critical that long-term capacity building efforts be fully owned, internalized, understood, and led by the right local reformers.

- Second, long-term capacity building requires efforts aimed at *both* individuals and institutions. The question is not either/or, but quite the opposite. Attention to each aspect is necessary, and in fact they tend to reinforce each other: strengthening individual capacity can make institutions more effective, while building institutions can make individuals more productive. Both parts are necessary in strengthening capacity and building institutions over time. Having said that, many of the people interviewed for this report believe that the Fund should focus more attention on strengthening institutions, and that it can improve its effectiveness in this area by adjusting how it organizes and carries out its CD efforts. This view does not mean that there should be less attention given to individual capacity, but rather that the Fund's resources and efforts can be better utilized to have a greater impact on building capacity at the institutional and organizational level.

- Third, it is important for the Fund staff, its senior leadership, its Board members, and its partner donor organizations to recognize how difficult it is to build capacity, how long it takes, and how challenging it is to measure progress. Capacity building is *really* hard. But at the same time, it is important to recognize how central these efforts are to sustainable progress in developing countries.

- Fourth, by almost all accounts, the Fund's efforts in these areas have begun to improve in recent years. CD efforts are gradually becoming better integrated than they once were, there is improved communication across departments, a greater focus on involving country authorities in setting priorities, more effort on continued engagement and follow up on CD activities (e.g., not just writing reports and leaving), and more regional and customized training sessions. At the same time, almost everyone interviewed for this project said that much more can be done. Continued progress will require thinking in longer time horizons, a willingness to adapt and try new approaches. Several people noted that while the Fund has shifted towards more country ownership, this change has not gone far enough, and there is still a tendency in some cases for Fund staff to implicitly take the lead in setting the priorities and deciding the course of action in CD efforts, which ultimately can weaken local commitment and long-term sustainability. Moreover, many noted that while there has been progress, CD activities still are not always well integrated, and that there is a need for stronger internal coordination so that CD efforts better reinforce and complement each other to more effectively achieve long-term goals.

With that background, we now turn to some of the main ideas that emerged from this review.

C. Supporting Country-Led Strategies for Building Capacity

17. Building more effective institutions and organizations requires an understanding of both where the organization is starting from and where it is aiming to go, and then charting a course to get there. The starting point should be for the leadership of the organization (or the relevant sub-unit of the organization) to oversee development of a concise strategy that articulates its highest priority medium-term functional goals and objectives, appraises its current capacity to achieve these goals, and outlines a basic course of action to build its capacity to better carry out its core functions (Box 1). To be effective, these CD strategies should be short and succinct, should avoid trying to do too much and overburdening the organization, and should set a small number of clear top-line priorities. Above all, the leadership of the organization must see the strategy as their own. These CD strategies can be designed for a ministry or central bank, but can be effective by having a narrower focus targeting a specific division, department, or office. These characteristics—country-led, concise, prioritized, and narrowly focused—would make these CD strategies different from many other strategies which often are not successful precisely because they are not fully owned and are too broad, too comprehensive, and not well prioritized.

Box 1. Country-Led Strategies

The first step in strengthening an organization's capacity is for its leadership to articulate its most important objectives and goals over a three- to five-year time horizon (or longer if possible), identify the highest priorities among these goals, and appraise its current capacity to achieve these goals. A second step is to develop a strategy to get there, including (for example) obtaining the necessary legal authorities for action, developing and implementing the appropriate top-line policies and processes, attracting and developing staff with the right skills, and utilizing the most appropriate TA to achieve its goals.

The process of formulating an organizational strategy should start with, and be led by, the head of the target organization, whether that be the minister of finance, the director of the property tax division, the head of the bank supervision department, or the director of the customs administration. It need not be a strategy for the government as a whole, nor should it necessarily be for the entire central bank or ministry of finance (although that may be appropriate in some cases). As much as possible the process should involve the entity's core leadership team, alongside key people from supporting organizations (e.g., the IMF, World Bank, major donors), and perhaps someone from a local think tank, university, civil society, or consulting firm as appropriate. The organization's leadership should articulate the organization's most important objectives over the medium term aimed at achieving its core functions, a set of intermediate goals (1–2 years), an outline of an implementation strategy, and an agreement on who will play what roles.

An effective strategy will include a small number of clear top-line goals. Adding too many goals makes it hard to focus on the ones that really matter, weakens the implementation efforts that follow, and adds to the difficulty of measuring progress towards results. In establishing these goals, it is worth bearing in mind the widely cited business management adage (attributed to Jim Collins) that "if you have more than three priorities, you don't have any."[1] An effective strategy also should give appropriate attention to implementation. Too often strategies focus at length on diagnosis and policy responses but not enough on the hard work of how to implement these policies successfully over time. A key part of the exercise will be to focus realistically on what is possible and what can be achieved, given the financial and personnel resources available.

The strategy need not be long or detailed, and the group formulating the strategy should avoid the common mistake of trying to do too much. "Comprehensive" assessments sound good, but often are not helpful and can be counter-productive, as they can take a long time to develop, often obscure the most important objectives, and ask an organization to try to do too much at once.[2] The group should meet regularly to review progress, which will bring more attention to implementation and follow-up, and—importantly—will allow for iteration and revision of the strategy to change the approach over time as necessary. Since the best approaches to long-term capacity building are often unclear and context-specific, the strategy should be flexible and allow for learning by doing, or what Matt Andrews, Lant Pritchett, and Michael Woolcock call Problem-Driven Iterative Adaption (PDIA).[3] PDIA focuses on solving locally defined problems, encouraging experimentation (instead of rigid pre-defined approaches), incorporating feedback loops, and engaging a broad set of actors in reform efforts.

[1] Jim Collins and Jerry Porras, *Built to Last: Successful Habits of Visionary Companies* (New York: HarperCollins), 1994.
[2] Matt Andrews, Lant Pritchett, and Michael Woolcock refer to the tendency to ask an organization to do too much too soon as "premature load bearing," which they argue causes stresses that lead to a weakening (rather than strengthening) of capacity. See Matt Andrews, Lant Pritchett, and Michael Woolcock, *Building State Capability: Evidence, Analysis, Action* (Oxford: Oxford University Press), chapter three, 2017.
[3] Andrews and others, *op. cit.*, chapters 6–10.

18. **The Fund's role in developing these concise CD strategies should not be to lead the process but rather to encourage the leadership of the organization** (or sub-unit of the organization) to undertake this exercise, and then to fully participate in it, provide support as

appropriate, be willing to compromise on the objectives and strategy under the organization's leadership, and play its role in implementing the strategy in partnership with others.

- The IMF resident representative, where they are present, should be involved from the outset to represent the Fund, provide ideas and support, and to help determine the ways in which the Fund can best be supportive.

- Many countries will not be able to fully develop the strategy on their own and will require support from the Fund and other partners. The leadership may ask the Fund (or other partners) to undertake assessments and diagnostics, to assist with drafting of parts of the strategy, or help with developing time-bound action plans. The Fund (and others) can also help provide guidance (or a workshop; see next section) on the core elements and processes of how to develop an effective strategy. Playing these and other supportive roles is fully appropriate, so long as they are carried out under the clear leadership of the local authorities, and the authorities feel that the strategy and the key decisions are their own.

- The Fund (and other partners) should take great care to avoid asserting its own priorities and strategies and should be willing to follow the course set by reasonably capable leaders.

- In parallel, the Fund will have to organize its own internal plan for how it will support a country's capacity building efforts, and how it will bring together the appropriate diagnostic tools, TA, training, financing, and other means of support. The Fund's own internal strategy to support a country's CD efforts should not be confused with the country's own CD strategy. These internal CD strategies should be complementary to (and perhaps components of) the Fund's country strategy notes and regional strategy notes.

19. The key points are the importance of the local authorities owning the process and encouraging them to develop a concise, focused, and achievable CD strategy. As mentioned previously, the Fund has moved towards more country-led approaches in recent years, but most of those interviewed for this project thought that this change has not gone far enough. Shifting more towards this approach will require time, patience, and flexibility, and the recognition that developing these strategies—even concise ones—will often take longer than if Fund staff just did it themselves. This approach does not put the Fund in the lead, but neither does it suggest that the Fund should stand back and simply be reactive. There is an art to getting the balance right between being proactive and supportive while not taking over the process and asserting priorities.

20. There is likely to be some pushback to this idea (as there was when the shift to country-led approaches began) with a view that most low-income countries, or most organizations within low-income countries, do not have either the capacity or the interest to lead this kind of process. In some countries, that view is accurate (see below). But in many other countries, including some very low-income and fragile states, there are local leaders and reform champions that have the interest and ability to formulate a concise strategy, so long as they are given the patient support and encouragement necessary to do so. This process will be hard work, and sometimes it will fail. But the alternative of the Fund (or other partners) continuing to develop strategies and establish priorities without the organization's leadership understanding and owning the process will continue to weaken long-term progress and sustainability in building capacity.

21. Of course, designing a country-led strategy does not mean that the Fund (and other actors) must always follow whatever the local authorities say they want to do. If the strategy does not make any sense, or is just a wish list, or full of empty promises, the Fund and other partners can decide not to support it.

22. Similarly, in some countries (or in some organizations within countries) the authorities will show no inclination for, or interest in, developing or implementing a basic CD strategy. In these situations, the expectations for progress must be lowered considerably, and the Fund's level of effort should also be reduced. The Fund can remain engaged, and can focus on building relationships, creating trust, and encouraging the case for reform to begin to create a partial foundation for when the conditions for progress have improved. Some limited CD may still be appropriate, but the Fund should devote a larger share of its time, effort, and funding to the countries that show an interest and commitment to capacity reform.

23. Although this approach has some similarities with the Capability Assessment Program (CAP) that the Fund implemented in Tunisia and Libya, it differs in several ways.

- First, in the CAP the IMF drove the process, conducted the assessments, and issued reports to the authorities with recommended priorities and steps for action. Staff in reviewing the program concluded that there needed to be more country ownership, and that the authorities should draft their own road map for reforms.

- Second, the IMF's assessments appear to have been too detailed and comprehensive to be fully useful. Staff reviewing the exercise concluded that the reports were comprehensive but could have given a better sense of priorities and focused on the key areas for reform.

- Third, the CAP assessed the central banks (Libya and Tunisia) and ministry of finance (Libya) as a whole. Sometimes this kind of an organization-wide approach is useful and appropriate, but often the assessments can be more beneficial if they are targeted at a sub-group within the organization, such as the debt management office or the bank supervision department.

- Fourth, the two countries of focus in the CAP pilot phase were both in the midst of major transitions (the choice of countries in transition was more by circumstance than design). While countries in transition are an important set of members for the Fund, they present much greater risks and uncertainty in leadership and capacity. The experiences and characteristics of countries in transition differ in important ways from the situations in the larger number of countries that have more stable governments in which CD efforts are more likely to achieve greater progress (see the penultimate section for more on working in fragile states).

D. Strengthening Capacity Development Efforts

24. With this kind of strategy in hand, the Fund can then work to strengthen and better integrate its CD efforts in support of the organization's key goals. By all accounts the Fund has made important progress in better integrating TA and training activities, but there remains significant scope for further improvement. Most of those interviewed for this project felt that CD activities are still too fragmented, and as a result they miss opportunities for mutual reinforcement and sustained effort that could achieve greater long-term impact.

25. The Fund can strengthen its CD efforts by organizing training and TA for each country as an integrated series of modules and interlocking pieces that reinforce each other and fit together, and that are designed to foster ongoing and regular engagement over time with local authorities. The Fund has a wide range of options for assisting countries in building capacity—the key is to ensure that these efforts are well integrated and sequenced to help achieve the same goals, that they reinforce each other, and that they foster regular engagement over time. Stand-alone TA reports or trainings without follow-up are far less effective than activities that are based on continued, purposeful, and coordinated engagement that recognize the long-term time frame required for effective CD. These integrated modules and engagement can take the form of a combination of online training, regional workshops, face-to-face training, TA in country, phone or video calls between Fund staff and local counterparts for follow-up, and other measures designed to help achieve the local organization's main goals. These efforts can be complemented with more customized trainings (one-on-one, small group, or in-country workshops) and can focus on the same key people in the organization.

26. In some cases, the Fund can shift to this approach by reorganizing existing activities and levels of effort; while in others it will require devoting more time, effort, and resources to particular projects. As a result, this shift may require prioritizing among projects, and allocating more sustained resources over time to a more limited number of projects, which in turn should improve their chances of ultimate success.

27. In turn, better integration will require enhanced internal coordination within the Fund so that the CD-delivering departments work more closely together to meet the needs of the target organization. By all accounts, while coordination has improved, there is significant room for improvement so that CD efforts are working together more closely to achieve the same goals and can better reinforce and strengthen each other over time. Greater coordination will be essential in making long-term multi-faceted engagement successful. The area departments, in particular, should play a central role in improving internal coordination in CD efforts, since they engage most closely with countries and are involved in all areas of Fund engagement. Improving internal coordination around more flexible delivery of CD activities will be a difficult challenge but will make these efforts more effective over time.

28. The Fund should explore the possibility of introducing training focused on building leadership, management, strategy development, and related skills. This report, along with many others, has highlighted the importance of local leadership and management in building capacity over time, and therefore in advancing the Fund's core work in macroeconomic and financial stability. However, the Fund (and others) make little effort to develop these skills and treat them as static: the authorities either have them, or they do not. But leadership and management are skills that can be taught, learned, and developed just like economics and statistics skills. Providing this kind of support would help improve the effectiveness of the Fund's core technical work—and therefore help the Fund achieve its core goals—since those efforts are often hampered by weak management and leadership. The Fund can help countries develop these skills through workshops, mentoring, and other forms of CD, with these activities integrated into the other modules described above. Some will argue that these kinds of activities are outside of the Fund's mandate, but that is less clear when leadership and management are seen as core skills that are critical to advancing the Fund's major objectives. If the Fund cannot take on these roles directly, it should work with other groups with management and leadership expertise (e.g., business or public policy schools), or with other donors that can support these efforts. What the Fund should not continue to do is to simply ignore these critical skills and assume they will somehow take care of themselves.

E. Creating Global Professional Norms and Communities of Practice

29. One of the IMF's most important successes over the last few decades—often overlooked—has been in creating global norms of professional practice among central bank governors, ministers of finance, and other senior finance officials. In part, this progress has been achieved through regular face-to-face meetings and other contacts among global finance leaders, most clearly through the Spring and Annual Meetings, but other meetings as well. Through these regular contacts, governors and finance ministers have come to see themselves as part of an elite international group of global leaders. Membership provides them with high-level status and access, but also demands that they adhere to standards of behavior and action in terms of both technical capability and probity for themselves and the institutions they lead. By creating these professional associations and networks and helping to establish standards of behavior, the Fund has powerfully helped strengthen institutional norms and build capacity in its partner countries (Box 2).

30. The IMF should more intentionally aim to create and strengthen these norms, networks, and communities of practice at deeper levels within organizations. It should recognize and articulate that doing so is a core CD activity that is complementary to and integrated with its other core services of TA and training. In the best of circumstances, all three—training, TA, and building professional norms—work together to strengthen both individual capability and institutional capacity to improve organizational performance. These norms and networks can help create and strengthen incentives for improved performance at an international level, which CD can help achieve; in turn, TA and training can help reinforce these norms and networks.

Box 2. The Benefits of Building Professional Norms and Communities of Practice

Building professional norms and communities of practice helps strengthen institutions in three somewhat different but overlapping ways:

- First, it creates opportunities for communication of ideas and peer-to-peer learning on policies and implementation strategies. Officials can learn from each other's experiences in managing exchange rates, conducting monetary policy, introducing tax reforms, or changing procurement systems (for more on this point see the next section).
- Second, it helps build norms of professional standards of best practice on policies and behaviors. Participants quickly learn the international norms for central bank independence, exchange rate management, budget policy, or debt management. The desire to be seen as a member in good standing of the "club" of top-flight global financiers, and to be held in esteem by your colleagues, increases the attractiveness of adopting these practices, and can be an important counterweight to domestic opposition to certain reforms. At the same time, participants also learn the norms for personal and institutional behavior, for example around fighting corruption or enhancing transparency. The desire to adhere to these standards can be powerful: nobody wants to be known as the governor that allowed hyperinflation, or the one that everyone is whispering rumors about embezzlement or corruption.
- Third, it creates healthy competition across countries and stronger incentives towards improved institutional performance. As ministers come to realize that their country is trailing their neighbors in tax collection or debt management and see that the information on their relative standing is publicly available to their peers, they have an extra incentive to try to catch up with their peers.

31. The IMF has been most successful at creating these norms and communities of practice at the highest levels of central banks and ministries of finance, and with the major policies conducted at that level (e.g., monetary policy, exchange rate policy, and aggregate budget management). It has been less successful in doing so at deeper levels within organizations with mid-level officials responsible for policies and processes that are harder to implement, such as property tax reform, banking supervision, or detailed budget execution. Part of the reason for the slower progress is that the work processes that are carried out at deeper levels within organizations are inherently more difficult, involving more people with weaker backgrounds that are trying to carry out complex tasks. But part of the reason may also be that at this level, the Fund tends to focus on providing TA and training and gives comparatively less attention to *intentionally* creating these international norms and communities of practice.

32. There are some noteworthy examples where Fund staff are already involved in efforts to build these norms and communities of practice at deeper levels, with promising results. For example, some of the regional centers have had some success in supporting groups like regional tax associations or the East African Community, and there have been efforts to bring together groups to work on macro frameworks, fiscal policy, customs reform, and other issues. There also has been some success in supporting statistical agencies in this way.

33. The Fund should build on these efforts and more intentionally focus on creating international communities of practice at deeper levels within organizations. It should purposefully integrate these efforts with TA and training, as part of the more structured ongoing engagement discussed in the last section. For example, building on some of the efforts already underway, regional workshops and trainings on customs administration can be structured purposefully to involve a group of (say) 4–5 people from each of the participating countries, and that same group of people should be expected to return for a series of workshops and meetings over several years. These trainings can be complemented with online discussion forums or other mechanisms involving the same people to create additional opportunities for participants to share experiences and ideas. Of course, there will always be normal staff turnover, so the exact same people may not be there over time, but the selection of participants should be made with the expectation that they (or their replacements) will be regular participants. The Fund should be more purposeful and strategic in who is invited to participate in regional or Washington-based training to ensure that they are critical to the organization's strategy, and that their regular participation will help build norms and standards of practice.

34. Ideally, these workshops should be complemented by TA at the country level working with the same people, with each building on and reinforcing the other. As these groups meet on a regular basis, they will learn from each other's experiences in implementing difficult policies, experimenting with different approaches, and other issues. They will begin to identify with an international community of best practices and begin to form and adopt standards for policies and practice. These meetings will also create some healthy competition across countries; since participants will be meeting on a regular basis, each will expect the others to be making progress over time towards their stated goals.

35. These norms and networks can be built and strengthened in other ways. For example, the Fund can help create new, or strengthen existing, professional associations and regional groupings. Or it can hold regional conferences on a regular basis that invite many of the same group of core people over time. Some of these organizations already exist, such as regional tax associations, or intergovernmental organizations such as the East African Community. The Fund itself need not build these—in fact, in some cases, having the Fund too closely identified with the organization may not help—but it can help encourage and facilitate them, and use them as vehicles to help strengthen institutional norms and build capacity.

36. The point is not to build these international associations for their own sake, or to hold needless meetings or conferences. Rather it is for the Fund to look intentionally for opportunities to build communities of practice that can exchange ideas and build international professional norms and use these communities to reinforce and strengthen TA and training aimed at building individual capacity and institutional capability. Doing so should be recognized as an important service which the Fund can (and already does) deliver on an ongoing basis.

F. Emphasizing Peer-to-Peer Capacity Development

37. A recurring theme in the background interviews for this report was the importance of peer-to-peer CD. (This point overlaps with, but is slightly different from, the previous point on building norms and communities of practice.) The Fund already utilizes peer-to-peer approaches in many CD activities, especially at the regional level, but many of those interviewed for this project felt these efforts could and should be expanded. Technocrats in developing countries are particularly interested in, and receptive to learning from the experiences of countries that they perceive to be their closest peers, which they see of great relevance to their own situations. They point out that they learn most powerfully when they hear directly from the people in their peer countries that were most directly involved in the process.

38. There are several ways in which the Fund can take further advantage of the power of these peer-to-peer experiences.

- First, staff providing CD should continue to increase the emphasis on using examples and lessons from closest peers. Authorities will pay closer attention to the examples (good and bad) of countries they see as similar to their own, and particularly those they see as slightly more advanced. They want to learn from those countries that they perceive to have recently been in a similar situation as theirs, and what steps they took to move forward. The more distant the example from their reality, the less effective it will be.

- Second, training sessions (both courses and workshops) should more purposefully select participants in ways that bring together people from similar countries. Ideally, workshops and other training groups would bring small groups of staff from one country together with groups from peer countries. In these settings, participants can learn significantly from their peers who are facing similar issues, constraints, and challenges. (This point echoes and reinforces the suggestion made earlier to bring together groups in training to build norms and communities of practice.) Hearing an idea from a peer can be far more powerful than hearing the same idea from Fund staff.

- Third, in as much as is possible, the Fund can do more to utilize experts from peer countries to deliver CD, since they will have a better sense of the problems and constraints in the target country (of course the Fund already does this to some extent; the point is that it can do more). A workshop session led by someone from a peer country can be much more effective than one run by someone from North America or Europe, or a distant continent, since those experts will be more familiar with the institutional, financial, and political constraints faced by the authorities. The same is true about TA, including long-term resident TA. A highly skilled expert from an advanced country may know the best technical answer but have little understanding of actual implementation difficulties, or when to consider second-best alternatives.

- Fourth, the Fund can expand its efforts in helping to send local staff from one country to be “attached” to a peer organization in another country to learn from their example and experiences. Managers and staff from the target country can learn significantly by spending time imbedded in more highly functioning organizations in other countries that have dealt with similar issues, and then bringing those lessons home. Several of the Regional Training Centers (RTCs) already support attachments, with examples including the attachment of Ethiopian officials to Tanzania to learn from Tanzania’s experiences with internal audit, officials from Nepal spending time in India as they proceed with decentralization and design the architecture of their intergovernmental fiscal relations, and staff from Suriname visiting The Bahamas to learn from the latter’s experience in introducing its VAT. Typically the Fund assists in arranging the attachment and pays for travel costs, while the two countries continue to pay salaries and facilitate the time needed for the assignment.

G. Results-Based Management and Capacity Building

39. There is broad endorsement for the Fund's recent introduction of a more structured approach for RBM. Almost everyone interviewed as background for this report voiced agreement with the movement towards specifying clearer goals and targets and initiating a process to monitor progress towards those goals over time. Specifying intermediate milestones is an essential part of developing the strategies for capacity building discussed earlier in this report, for taking stock of progress along the way, and to understand whether to continue in the same direction or change course along the way.

40. While recognizing the importance of RBM, there are three concerns relating to capacity building efforts that should be taken into account when designing the system.

- First, compared to other processes, CD is inherently difficult to define and measure, takes a long time to achieve, and usually does not unfold in a neat, linear process. It is hard to identify the right milestones and intermediate benchmarks. This challenge creates a risk of using metrics that are available and easy to measure, but ultimately might not be leading to the actual long-term goal. It creates the incentive to "do what can be measured"—identify easily measurable targets, define success as achieving those targets (as distinct from actual long-term functional performance) and then shift resources towards meeting them. However, if these measures are mis-specified, or incomplete, or insufficiently flexible to allow for iteration and experimentation, an organization risks achieving all of the benchmarks but failing to achieve the true goals. Passing the right laws, introducing the appropriate policy, or adopting a new budget framework may be the right first step towards the long-term goal, but in and of themselves they are not success, and may or may not lead to improved functional performance of the organization. The key is to continually assess whether the benchmarks are leading to improved functional performance. The pressure to achieve results (and to do so quickly) can lead to targets being watered down, or to focus only on the easiest targets, or on focusing on inputs and outputs rather than long-term outcomes and improved functionality. One person aptly described this problem as "hitting the targets but missing the point;" another described it as "measuring the wrong things well."

- Second, if the system is too rigid, it can undermine the incentives for experimentation, iteration, and adaptation. Implementers do not want to be seen as failures (and risk losing funding), and so they tend to stick to more traditional approaches, even when the latter are not always working well. For them the safest bet is to do what others have done, set easy-to-achieve targets, and avoid being too bold. The effect can be to slow or stall progress, rather than accelerate it. The rationale is clear: if you want to be seen as successful by your funders, don't take risks, and focus on the targets that are the easiest to achieve.

- Third, if the local authorities are not deeply involved in establishing the intermediate metrics and the long-term goals, they may come to see the RBM system as a form of "stealth conditionality" imposed by the Fund. Fund staff will naturally push local authorities to meet RBM targets, but if the authorities do not understand or own the targets, they may quickly come to resent the system, which could sow the seeds for its ultimate failure.

41. As stated earlier, an effective RBM system is essential for designing and implementing a good strategy for building capacity in the long run. What can be done to minimize the risks noted here and to help achieve long-term progress?

- First, Fund staff must simply be aware of these risks and establish metrics with care and caution. Good metrics are designed with an eye towards value creation and improving the long-term functionality of the organization.

- Second, local authorities must be deeply involved and invested in selecting and implementing the RBM targets. They must understand why the targets have been set, and why achieving them is in the interest of the organizations they head. The more they see RBM targets as their own, established to help them achieve their own goals, the higher the likelihood of success, and the lower the likelihood of resentment and discord.

- Third, targets should be established taking into account the country's and the organization's initial capacity. Countries and organizations with lower capacity (even those with committed leadership) can be expected to make progress on a slower timeline that those with stronger capacity.

- Third, Fund staff must regularly assess, and re-assess, input and output metrics to ensure that they are actually moving toward the desired long-term outcomes. The RBM is based on a standardized catalog with a menu or results, but these metrics should be reviewed periodically to ensure that they continue to be appropriate and effective in moving organizations towards improving their ability to carry out core functions. The system must be flexible enough to allow for experimentation and trying new methods, for iteration and adaption, and for changing course as necessary.[5]

- Fourth, the Fund should work with the donors funding the system to allow for longer-term time horizons, and to avoid focusing too narrowly on the most immediate and easily achievable targets.

- Fifth, in some cases where metrics and data are inadequate, the Fund, donors, and local authorities may want to invest in developing the data needed for better metrics.

All of these steps call for broader and ongoing discussions with the authorities and the donors on designing a framework that adds value and focuses on the right long-term functional objectives while recognizing the need to demonstrate results in the short term.

[5] Andrews and others, *op. cit.*, chapters 6–10.

H. Capacity Building in Fragile States

42. The Fund's CD activities face particular challenges in fragile states, where progress is likely to take even longer, the obstacles are larger, the costs are higher, and the path forward is less clear. CD efforts in fragile states are more complex because of higher levels of political and institutional instability, reversals of direction, greater vulnerability to shocks, lower initial capacity, and weaker governance structures.

43. The Fund should devote greater resources to CD efforts in fragile states with weak capacity but committed leadership; it should invest less so in countries without that committed leadership. The key question in fragile states, as with any country, is whether there are local leaders that are interested in and committed to taking the hard steps necessary to build capacity over time. In some fragile states there are such leaders, and in these countries, progress can be achieved; where there is less effective leadership, expectations need to be lowered considerably.

44. In many ways, the key steps in fragile states are broadly similar to other countries. The starting point is to try to identify leaders that can be champions for reform, and to work closely with them. They can put together (with Fund and other partner assistance as appropriate) a concise and focused strategy that establishes their key (realistic) objectives, charts out a course to begin to get there, and delineates who will do what to get the process started. In fragile states it will be important to identify tasks that are easier to accomplish, where the objectives are clear and the path forward is well defined so that there can be some quick wins and the leadership begins to establish confidence and a record of progress.

45. The initial focus in fragile states with committed leadership should be on basic building blocks that are relatively simple and do not require as much implementation capacity as more complex tasks, such as exchange rate management, payments systems, cash management, budget frameworks, and collecting customs duties and excise taxes. The strategy can build from there, but always bearing in mind what is realistic, and avoiding the temptation to try to do too much (it is particularly easy to overburden systems in weak and fragile states). Fund staff should work hard at building strong relationships of trust, which will typically be very important at this stage. It will be particularly important to engage fragile states with a set of interlocking modules of CD activities, even if these are of smaller scale, to reinforce CD activities with regular engagement over time. Working in fragile states with committed leadership is likely to require a stronger presence on the ground with additional resident advisers and additional training and TA, as has been pointed out in previous reviews of Fund efforts in fragile states. And while coordination with donors is always important, it is particularly crucial in fragile states where resources are scarce and the margins for error are narrow. The African Department (AFR), for example, has introduced "Capacity Building Frameworks" for five fragile states on a pilot basis with many of these characteristics, which may prove a useful model for expanding CD efforts in an expanded set of fragile states.

46. In countries where leadership is committed but individual capacity is particularly weak, in some circumstances the Fund should consider utilizing a time-limited "capacity supplementation" approach. In this arrangement (sometimes also called capacity augmentation), the Fund could work with other donors to hire experts to work in target organizations to carry out key functions (i.e., not just as advisors). The basic idea of this approach is that in situations where the leadership is committed to change but capacity is so weak that there are simply not enough skilled people available to carry out critical functions (e.g., in immediate post-conflict situations), temporarily placing an outside expert to play this role under local leadership may be an appropriate step. This approach should be time-limited and be combined with efforts to identify, train, and place a national expert in the position as quickly as possible, ideally to work directly with the expert during a transition period. For example, the outside expert could be hired for a two-year period, with a commitment by the host country to identify the successor so that the expert and the successor can work side-by-side during the second year in preparation for a hand-over. This approach could also be used in very small countries or island states in which the pool of skilled workers is small, and the availability of people with specialized skills is limited. Bilateral and multilateral donors finance capacity supplementation efforts regularly. This approach can be used in parallel with some of the approaches the Fund currently uses, such as more traditional long-term TA advisors (that could also build in training successors by working together for extended periods), and placing TA advisors at RTACs so they can visit countries regularly to support TA implementation, transfer knowledge, and minimize the risk of dependence.

47. The most difficult situations are fragile states in which there are no local leaders that are champions for reform, and the authorities show no interest in capacity building or reform. In these situations, the Fund should scale back its efforts, and focus on strengthening relationships, possibly with some limited CD efforts, and building the case for reform with the hope that the situation may change in the future and these efforts may eventually bear fruit. In effect, the Fund should play a much more patient, longer game. It should devote much less time and other resources to fragile states that show little interest in CD.

I. Summary of Main Conclusions and Recommendations

48. The main conclusions and recommendations of this report are as follows:

- First, the Fund should focus its CD efforts on countries and organizations with effective leaders that are committed to building capacity and strengthening its institutions. CD efforts can be successful and sustained only where those efforts ae fully owned, internalized, understood, and led by the right local reformers.

- Second, Fund staff should encourage and support the leaders of government agencies (or sub-units of agencies) in developing a concise and focused CD strategy that articulates the organization's most important CD objectives, appraises its current capacity, and formulates a plan to achieve those objectives. The process of developing the strategy should be led by the head of the organization, with coordinated support by the IMF and other donors as appropriate. These CD strategies should be country led, concise, prioritized, and narrowly focused. The Fund's role should not be to lead this process, but rather to encourage the authorities to undertake this exercise, provide ideas and input, and offer assistance in designing and implementing the strategy as appropriate, all under the authority's leadership. The IMF resident representative, where in place, should be involved throughout this process to represent the Fund.

- Third, the Fund can strengthen its CD activities by organizing them as an integrated series of modules and interlocking pieces that reinforce each other and fit together, and that are designed to foster ongoing and regular engagement over time with local authorities. Successfully integrating these modules and sustaining them over time will require enhanced internal coordination within the Fund (with the area departments playing a key role) so that the CD-delivering departments work more closely together to meet the needs of target organizations.

- Fourth, the Fund should explore the possibility of introducing training, mentoring, and advising focused on leadership, management, strategy development, and related skills. Leadership and management are critical to the success of CD efforts and to long-term development. Helping to strengthen these skills will help improve the effectiveness of all of the Fund's core technical work. If the Fund cannot take on these roles directly, it can work with other groups with management and leadership expertise (e.g., business or public policy schools), or with other donors that can support these efforts. But it should not ignore the importance of purposefully building leadership and management skills.

- Fifth, the IMF should more intentionally aim to create and strengthen professional norms and communities of practice across countries at deeper levels within organizations. The regional centers are well placed to help build norms of behavior and support communities of practice among mid-level officials through regional workshops, training, conferences, and other activities that bring together the same group of people over time. Doing so will help strengthen professional standards of best practice on policies and behaviors for both institutions and individuals, and will create opportunities for both learning and healthy competition across countries.

- Sixth, the Fund should continue to emphasize and develop peer-to-peer CD efforts by purposefully bringing together participants in training sessions from peer countries, using more examples and cases from peer countries, utilizing experts from peer countries in CD activities, and increasing support for "attaching" staff from an organization in one country to the peer organization in another country to learn from their approaches and experiences.

- Seventh, with respect to RBM, the Fund should ensure that local authorities are deeply involved and invested in selecting and implementing targets and benchmarks. Local authorities must own and understand these targets if RBM is to be successful. RBM targets should be designed so they take into account the organization's initial capacity. Countries and organizations with lower capacity (even those with committed leadership) can be expected to make progress on a slower timeline that those with stronger capacity, and RBM targets should reflect that reality.

- Eighth, Fund staff must regularly assess and re-assess RBM targets to gauge whether intermediate milestones are actually helping the organization improve its long-term core functional purposes. The system must be flexible enough to allow for experimentation and trying new methods, for iteration and adaption, and for changing course as necessary. The Fund should work with the donors funding the system to allow for longer-term time horizons, and to avoid focusing too narrowly on the most immediate and easily achievable targets. In addition, where available metrics are inadequate, the Fund, donors, and local authorities may want to invest in developing the data needed for better metrics.

- Ninth, in fragile states, the Fund should try to identify leaders that can be champions for reform, and assist them in developing a basic CD strategy. The Fund should focus its efforts in fragile states with at least some committed leaders and champions for reform. In fragile states with such leaders, progress is achievable; in countries without that leadership, much less can be expected. The initial focus should be on basic building blocks that are relatively simple and do not require as much implementation capacity as more complex tasks, and should avoid trying to address too many challenges at one time. Fund staff should work hard at building strong relationships of trust, which will be even more important at this stage. It will be particularly important to engage fragile states with a set of interlocking modules of activities over time (even if these are of smaller scale), reinforce CD activities with regular engagement over time, and have a strong presence on the ground.

- Tenth, in countries where individual capacity is particularly weak, the Fund should consider utilizing a time-limited "capacity supplementation" approach in which it could work with other donors to hire experts to work in target organizations to carry out key functions (i.e., not just as advisors). This approach can be effective in certain circumstances, but should be time-limited and be combined with efforts to identify, train, and place a national expert in the position as quickly as possible.

- Finally, in countries where the authorities show no inclination for, or interest in, a basic CD strategy, the expectations for progress must be lowered considerably, and the Fund's level of effort should also be reduced. The Fund can remain engaged and can focus on building relationships, creating trust, and encouraging the case for reform to begin to create a partial foundation for when the conditions for progress have improved. Some limited CD activities may still be appropriate, but the Fund should devote a larger share of its time, effort, and funding to the countries with more engaged leaders (including fragile states with committed leaders) that show an interest and commitment to building capacity and strengthening institutions.

II. IS IMF WORK ON CAPACITY DEVELOPMENT SUFFICIENTLY DEMAND-DRIVEN?[1]

Summary

1. **Background.** Demand from country authorities should be the key driver of the IMF's work on CD because it strengthens the likelihood that IMF advice will be absorbed and implemented. Due to excess demand for CD work and the need to set institutional priorities, however, it is appropriate that the framework to allocate CD takes into account both the demand from countries and the IMF's strategic objectives. Checks and balances in the system to prioritize CD delivery have improved the reconciliation of institutional priorities with country priorities. But this does not mean that poorly justified CD, driven more by supply than demand considerations, does not exist.

2. **Focus of paper.** The paper argues that the dichotomy between demand versus supply-driven CD is exaggerated. This puts the focuses on the following questions: as the IMF seeks the equilibrium between demand-side and supply-side criteria in prioritizing and allocating CD, is there sufficient attention on demand considerations? In particular, is there sufficient attention to country views, ownership, and absorption capacity in the allocation and design of CD to ensure traction? To shed light on these questions, the paper discusses the interplay between the prioritization of CD and country ownership by examining a variety of issues that could influence decisions about CD priorities and buy-in from country authorities. These issues relate to the IMF staff's engagement with country authorities in deciding CD priorities and modalities, which is central to gauging country ownership and fostering demand-driven CD.

3. **Steps to put greater emphasis on country ownership in CD decisions.** As country commitment is essential to limit unwarranted supply-driven CD and maintain attention on demand factors, the paper recommends steps to make country ownership more central in CD prioritization and delivery decisions. These include:

- Further strengthening the regional allocation plan (RAP) process to (i) better integrate CD and area department country work; (ii) promote better information exchange between departments and utilization of this information; and (iii) ensure that the RAP process is not just an internal prioritization process with limited country engagement.

- Increasing the role of the Committee on Capacity Building (CCB) to foster budget reallocations that might be needed to meet shifts in country demand.

- Focusing more on assessments of country ownership in regional and country strategy notes.

- Using the diagnostic work conducted by CD departments to assess and promote country ownership.

[1] Prepared by Ajai Chopra, Independent Consultant and former Deputy Director, IMF.

- Making country engagement more integral to the RBM process.
- Further mitigating risks to the prioritization of CD related to external funding.
- Leveraging on-the-ground presence (resident representatives, regional centers, long-term experts based in the field) to enrich country engagement.
- Putting greater emphasis on pairing technical assistance and training to enhance country ownership.

4. Country responsibilities. The onus is not just on IMF staff. To have ownership, it is also vital that country authorities have their own set of priorities and a strategy to help target CD at their most important needs.

A. Introduction

5. Demand from country authorities should be the key driver of the IMF's work on CD. Greater emphasis on demand considerations in the allocation and delivery of CD, taking country interests and circumstances into account, strengthens the likelihood that the advice will be absorbed and implemented. This principle has prompted several reforms to put more weight on demand considerations to promote better prioritization of CD delivery. Yet, some observers, including country authorities, complain that on occasion CD is improperly driven by supply considerations not aligned to a country's own priorities.

6. In practice, because of excess demand for CD and the need to set institutional priorities, the framework to allocate CD relies on a "two-level prioritization system." This system, described in greater detail in the 2014 report on IMF Policies and Practices on Capacity Development, takes into account both the demand from member countries and the IMF's strategic objectives. The aim is to "ensure that CD is targeted at the most important needs of countries as defined by both the country authorities and the Fund" (2018 Quinquennial Review of the Fund's Capacity Development Strategy: Concept Note, March 2017, page 6).

7. Overall, the checks and balances in the two-level prioritization system have improved the reconciliation of institutional priorities with country priorities. This reconciliation process has helped curtail unwarranted supply-driven CD. As the IMF's Independent Evaluation Office (IEO) concluded in 2014, "after 2005, the Fund moved towards giving more weight to demand considerations" in the prioritization and allocation of TA (IMF Technical Assistance: Revisiting the 2005 IEO Evaluation, 2014, page 16).

8. But this does not mean that poorly justified CD, driven more by supply than demand considerations, does not exist. In the same 2014 IEO report, the evaluators correctly cautioned that "vigilance is needed going forward to ensure that the new system does not revive perceptions of IMF TA being excessively driven by institutional priorities" (page v). Although such CD may only be a small fraction of the total, it is enough to amplify perceptions of disproportionate supply-driven

CD. Separating perception from reality would require a forensic examination of a sizable sample of CD projects to determine the actual extent of unwarranted supply-driven CD. Such an examination, however, is beyond the scope of this paper.

9. **As demand for IMF TA and training—which together constitute CD—exceeds what can be supplied, the IMF needs to prioritize various demands.** The focus therefore shifts to two related questions. First, how well does the IMF target CD to ensure that it is allocated to the most important priorities of countries as identified by both country authorities and the IMF? And second, is there sufficient attention to country views, ownership, and absorption capacity in the allocation and design of CD to ensure traction? These questions relate to the fundamental premise that CD delivery that arises from a genuine process of interaction between the IMF and the country is more likely to be "owned" by the recipient country, which in turn improves the likelihood that the outcomes that the IMF and country hope to achieve will be realized as a result of the intervention. Furthermore, although ownership (namely, willingness and commitment) by the authorities is a necessary condition for the traction and impact of CD, it is not sufficient. Absorption capacity is also required: the authorities need to have the resources, training, and technical skills to be able to implement CD recommendations.

10. **To shed light on these questions, this paper draws on interviews and the findings of the survey of CD stakeholders.** The interviews were conducted with representatives of IMF area and CD departments, the Office of Budget and Planning, and some IMF Executive Directors representing CD-receiving countries and external funders. As such, the findings and conclusions are more impressionistic than definitive. Nevertheless, they still point to broad areas where the IMF could devote more attention to promoting better allocation of TA to priorities identified by both country authorities and the IMF and to foster greater attention to country ownership.

11. **The paper focuses primarily on the TA component of CD activities, with the training component discussed only from the perspective of promoting TA that has stronger country ownership and traction.** This is not because issues related to demand versus supply considerations in the allocation of training are less relevant or important. Rather, the purpose is to keep the paper more focused by concentrating on the largest component (82 percent in terms of spending) of the IMF's CD work. But that said, training is an integral part of the IMF's CD mandate and sharp distinctions between "TA" and "training" are not meaningful. Appropriately, the IMF has focused on "capacity development"—that is, to help countries strengthen institutional capability through better organizational and legal structures as well as human capacity, often through a combination of technical advice, hands-on engagement in implementation, training, and peer-to-peer learning.

12. **The remainder of this paper is organized as follows:** Section B discusses the conceptual issues that arise when considering whether TA is demand or supply-driven and argues that this dichotomy is often exaggerated. The focus therefore should be on the following question: as the IMF seeks the equilibrium between demand-side and supply-side criteria in prioritizing and allocating TA, is there sufficient attention on demand considerations and hence country ownership? Accordingly, Section C discusses the interplay between the prioritization of TA and country ownership by examining a variety of issues that could influence decisions about TA priorities and

buy-in from country authorities. Finally, based on the discussion in the previous sections, Section D summarizes steps that could be considered to enhance country ownership of TA.

B. The Inexact Dichotomy Between Demand Versus Supply-Driven Technical Assistance

13. What does supply-driven TA mean in the context of excess demand for TA and the need to set institutional priorities? After all, without a price system to allocate TA when there is excess demand, the supplier chooses what will be delivered.

14. Inevitably, therefore, considerations for allocating CD involve both demand-side and supply-side criteria. The demand-side elements include country needs, requests, and ownership. The supply-side factors include the IMF's institutional priorities, availability of expertise, availability of internal and external financing, and the priorities of donors as TA providers and financiers.

15. The CCB reviews institutional medium-term priorities for CD work annually. These priorities are drawn from the Managing Director's Global Policy Agenda, the Regional Strategy Notes (RSNs) prepared by area departments, and commitments made by the IMF to the international community. The priorities proposed by the CCB are reviewed and endorsed by IMF management and then communicated to the Executive Board in the context of the Office of Budget and Planning's paper on the annual budget outturn. The FY2019–2021 priorities are:

- Financing for development:
  - Fragile states;
  - Revenue mobilization and sound public financial management; and
  - Financial market deepening for low-income countries.
- Aligning CD, surveillance, and lending:
  - Addressing needs of highly vulnerable and IMF program countries;
  - Financial supervision and regulation, including developments in fintech, particularly supervisory approaches to managing cyber risks, and monetary policy frameworks;
  - Closing data gaps, improving data quality, and broadening data dissemination; and
  - Financial integrity (anti-money laundering and combatting the financing of terrorism).

16. In applying these priorities, IMF CD covers areas that are critical to build strong institutions and boost skills to implement policies that promote macroeconomic and financial stability. Focusing on the TA component of CD, the core areas of IMF TA are summarized in Box 1. These core areas specify a supply-side menu of TA provided by the IMF. Supply then needs to be matched to actual country demands. This supply-side menu, however, is not static because it evolves to meet emerging demands (for example, mounting issues related to fintech).

Box 1. Core Areas of IMF Technical Assistance

Fiscal Policy and Management
- Tax policy
- Tax and customs administration
- Expenditure policy
- Public financial management
- Fiscal policy and institutional framework
- Fiscal federalism

Monetary Policy and Financial Systems
- Central bank operations
- Monetary policy
- Foreign exchange operations
- Financial supervision and regulation
- Macroprudential policies
- Systemic risk analysis
- Financial crisis prevention and management
- Capital market development
- Debt management

Macroeconomic & Financial Statistics
- Multisector statistical issues
- Balance of payments and other external sector statistics (for example, external debt, foreign direct investment, international investment position)
- Government finance statistics
- Monetary and financial statistics
- Financial soundness indicators
- National accounts and price statistics
- Data dissemination standards

Legislative Frameworks
- Laws and regulations, mainly on central banking, financial institutions, tax and public financial management, foreign exchange, insolvency, and creditor rights
- Anti-money laundering/combatting the financing of terrorism

17. IMF advocacy is natural and appropriate as the IMF undertakes this matching process. In particular, it is important for the IMF to provide guidance on TA that could be appropriate when revealed demand from a country is absent. But there is a fine line between advocacy and imposing TA on a country that has poor ownership. Vigilance is essential to avoid crossing this boundary as area and CD departments play this advocacy role.

18. In the case of area departments, IMF surveillance and lending may point to a need for TA that was not initially requested or identified by country authorities. Such advocacy depends on country teams, as mission chiefs identify potential areas of CD need based on policy discussions during surveillance and program missions, focusing on a country's capacity to implement recommended policies. If this revealed need persuades the country, it generates demand for the TA in question and may lead to a concrete TA request from the country.

19. Similarly, in the case of CD departments, the application of diagnostic and assessment tools can lead to the identification of potential TA needs. In addition, when CD departments meet with country authorities, the authorities may not have articulated a specific need or request, in part because of insufficient knowledge of what is available. The CD department can then inform the country of specific areas where it could provide TA and training that is suitable for the country's needs, again generating demand if the country is convinced.

20. As the IMF plays its advocacy role, it should be recognized that there are certain cases where the balance might appropriately be tilted more toward supply-driven factors. For example, in highly vulnerable countries where economic and financial repair takes place under a program or more intense IMF surveillance, a greater weight of supply-driven factors may be acceptable because it derives from the IMF's surveillance and lending mandate, including limiting the negative external spillover effects of domestic policies. But in the large majority of other cases, the balance in TA delivery and execution must be tilted more toward demand factors.

21. Overall, however, it is essential that IMF advocacy does not result in the imposition of TA on a country. Country ownership and commitment are crucial because without it TA is unlikely to deliver results and resources will be wasted.

22. There are also cases where countries may "demand" TA, but a need is questionable. For example, a country may request TA on the implementation of advanced approaches for capital adequacy calculation or bank stress testing, but such TA is not suitable for the country or is of low priority given other more basic needs. Another example would be situations where the IMF's view on risks differs from that of the country. Or, on occasion, country priorities may not match IMF priorities or expertise. For example, a country may ask for TA on micro-level social indicator statistics, but the IMF views other statistical areas to be of higher immediate priority. In addition, TA on such statistics is not one of the IMF's core areas and the request would be directed to institutions with the relevant expertise. In such situations some TA demands could be legitimately rejected because providing the demanded TA would be a misallocation of resources. In all these situations it is important to give country authorities a clear explanation of the reasons for declining their request for TA.

23. It is also difficult to distinguish between countries' genuine complaints of supply-driven TA from complaints of TA that had a prominent demand component but did not meet the country's needs. That is, even if there is agreement on the TA requested and provided, there are situations where what is delivered is ineffective or not what the country wanted. This could happen because (i) recommendations are not suitable for local conditions (for example, they are too ambitious or not consistent with implementation capacity); (ii) the scope of engagement is too narrow (for example, recommendations focus excessively on "what to do" when the country is also seeking advice on "how to do"); or (iii) there is disagreement about recommendations.

24. Another factor that creates the perception of supply-driven TA is that excess demand and hence rationing is greater in some areas than others. To take a hypothetical example, there may be substantial excess demand for TA on tax policies or central bank operations in contrast to other areas such as public financial management or debt management. This can result in considerable rationing of TA that can be provided in the first set of areas while availability appears ample for the second. This is less of a problem if it is temporary, but if it persists—for example, because of inertia in budget allocations or a mismatch between available staff resources and TA that is in demand—it forces difficult prioritization choices year after year. Avoiding such problems requires enhanced flexibility in budget resource allocations and also more nimble processes to deal with staffing rigidities.

25. Although the dichotomy between demand-driven versus supply-driven TA is often exaggerated, unjustified supply-driven TA can still occur. This typically has three sources despite the receipt of a formal request from country authorities:

- First, when the IMF devotes resources to a country on a topic even though country ownership is absent or insufficient. This could include situations where the need for the requested TA is dubious and situations when IMF advocacy has crossed the line and resulted in the imposition of TA.
- Second, even if the country has a need and ownership, when the IMF devotes excessive resources to the case—that is, it oversupplies TA relative to demand and absorption capacity.
- And third, although external donor funding allows the IMF to undertake CD activities that it would not be able to finance otherwise, donors often prefer to fund specific TA topics and recipient countries that are dear to them, often driven by the agenda of their domestic patrons. This can result in the relative richness of funding for certain topics or countries to the disadvantage of other IMF and country priorities. Donor-funding can therefore tip the decision-making scale and lead to TA being provided for countries or topics where the results are poor or ownership is weak.

The goal should be to limit such occurrences to a negligible level.

C. Prioritization of Capacity Development and Country Ownership

26. The prioritization and allocation of CD is inherently complex. It requires multidimensional decision-making—across regions, across countries in regions, across the IMF's CD departments, and across topics—taking into account both demand from country authorities and established IMF priorities for CD. The setting of IMF institutional priorities assists in this task, but still provides considerable leeway because these priorities are not ranked at an institutional level, are broadly defined, and priority groups overlap.

27. Allocation across the multiple dimensions is achieved through the RAP process for delivery of CD. The RAP process can be distilled into three fundamental steps:

- Area departments prioritize demands by country and topic, building on their dialogue with country authorities and input from CD departments about potential projects based on their discussions with authorities.
- CD departments state what they can supply given resource constraints and existing commitments.
- Agreement is reached on CD projects, both one-off and multi-year, following further dialogue between area and CD departments.

28. The RAP process has been recently reformed (effective September 2017). The primary innovations include establishing a three-year CD delivery plan for projects at an aggregated level (as opposed to the previous focus on planned missions for the coming year); increasing the transparency and efficiency of the process by promoting better exchange of information between departments, thus enhancing the dialogue between area departments and CD departments as they negotiate CD delivery plans and try to reconcile the demand and supply constraints; management's approval of the RAP aggregates showing the use of resources in both U.S. dollars and full-time equivalents; preparation of country strategy notes (CSNs) for heavy users of CD; and sharing of RSNs and CSNs with management for information. The reforms also introduced the requirement that area department mission chiefs review all briefing papers and terms of reference for planned CD missions and indicate their agreement on the timing and scope of missions. The objective is to strengthen demand-side accountability and better integrate CD activities with surveillance and lending.

29. It is not the purpose here to do a deep examination of the RAP process, not least because additional experience is needed to judge the effectiveness of recent reforms. Rather, the focus is on the following question: As the IMF seeks the equilibrium between demand-side and supply-side criteria in the allocation of CD, is there sufficient attention on demand considerations and hence country ownership? In other words, the issue is not just the need to match supply priorities to actual country demands, but also to ensure that there is sufficient country commitment and ownership.

30. An unequivocal answer to this question remains elusive, but a number of issues that influence the response come into play and are the focus of this section. These issues relate primarily to the nature and extent of IMF staff's engagement with country authorities in deciding CD priorities and modalities, which is central to gauging country ownership and fostering demand-driven CD. Such engagement is crucial for the RAP process because in its absence it becomes an internal prioritization exercise that simply maps what the IMF believes should be the country's priorities. But it is important to emphasize that the onus is not just on IMF staff—to have ownership, it is also vital that country authorities have their own set of priorities and a strategy to help target CD at their most important needs.

31. The rest of this section reviews the relevant findings of the survey of stakeholders, followed by a discussion of factors that might influence CD prioritization and country ownership.

Survey Findings

32. The survey of stakeholders to inform the 2018 review of the IMF's CD strategy touched on several issues concerning the prioritization of TA and country ownership. These findings are summarized below.[2]

[2] For details about the survey results, see the accompanying paper on "Survey of Stakeholders" prepared for the 2018 Review of the Fund's Capacity Development Strategy.

- On the question of the criteria that the IMF should apply to determine the allocation of TA because demand exceeds supply, the first choice answer for most respondent groups was that "TA should go to governments that are prepared to implement the advice."

- On the question of who initiated the original idea for the TA, respondents reported that the TA they observed was largely initiated or co-initiated by the recipient government.

- On the question of the factors that best explain why the government accepted TA, the top choice for country recipient respondents and IMF staff respondents was that "the government agreed the TA was important."

- On the question of the degree of engagement between the recipient government and the IMF to establish objectives prior to the delivery of TA, survey respondents generally reported a high degree of engagement but with variation across groups of respondents. Notably, recipient governments had the most favorable view of the degree of engagement, with the majority in this group reporting a high degree of engagement. By contrast, a minority in other respondent groups viewed the degree of engagement as being high, with a sizable proportion viewing the degree of engagement as either moderate or low.

- On the question of the areas that are most important for the IMF to focus on to improve the impact of TA on policy, which allowed for multiple possible responses, the most selected responses were to "ensure government buy-in before undertaking TA" and "better integrate TA with priorities identified in IMF surveillance," followed by improving analysis to identify the key problems or issues.

33. The survey findings do not lend themselves to definitive conclusions about whether IMF work on TA is sufficiently demand-driven. But neither do they point to deep concerns about poor prioritization of TA with unwarranted emphasis on supply-side factors. The findings do confirm, however, the importance of ensuring government buy-in before undertaking TA. In this connection, the observation that a sizable proportion of survey respondents viewed the degree of engagement between the recipient government and the IMF prior to the delivery of TA to be moderate or low suggests that this is an area where more effort will be needed in the future.

Surveillance and Program Needs as a Driver of TA

34. Integrating TA with IMF lending, surveillance, and policy advice is an institutional priority. But as this integration proceeds, is the resulting TA still sufficiently demand-driven with strong country ownership?

35. Based on interviews with IMF staff and some country authorities, the answer depends on various idiosyncrasies:

- In program countries, area departments' engagement with country authorities on integrating TA with program implementation needs is typically good. Persuading country authorities on the desirability of TA to implement policies needed to meet program goals is not difficult when program conditionality is involved. Ownership in these circumstances will be closely linked to overall program ownership.

- By contrast, in surveillance cases, area departments' engagement on TA priorities tends to be spottier.

  - Some mission chiefs and country teams identify potential TA topics based on policy priorities detected in surveillance missions, focusing on the capacity to implement the policies that the mission recommends. This translates to an area department-determined wish list of possible TA projects that the authorities should consider requesting. Sometimes this leads to concrete TA requests and delivery. But sometimes no request is received and the TA is not pursued because it can only be provided upon request by the authorities.

  - Some mission chiefs, however, tend not to engage much with country authorities on TA needs, playing less of an advocacy role. This may occur in part because they see TA-related discussions as an extra burden in view of the breadth of issues that typically need to be covered in surveillance discussions. But this is a lost opportunity to increase traction in surveillance. Identifying TA needs and priorities in the context of the vulnerabilities and policy requirements discussed during missions should be an integral part of surveillance work rather than being a burden on area departments.

  - But even in cases where there is good engagement, it tends to be segmented rather than universal. That is, possible TA projects are often discussed separately with central banks and ministries of finance. This can make it difficult to judge relative priorities across different streams of TA from a country's perspective. For example, does the country see a greater need for TA on tax administration versus monetary policy frameworks? Such segmentation, however, is often due to underlying organizational issues in TA-recipient countries that lead to poor internal coordination, adding to the tasks for area department staff as they seek to gauge TA priorities.

  - Area departments may also hesitate to propose TA in the context of a surveillance mission because they cannot ensure timely delivery due to CD department constraints, or because they do not feel empowered to lead a discussion on TA priorities without the CD department's prior vetting and formal clearance. This can lead to a two-step process of country engagement, with cursory initial discussions with country authorities on their TA needs, followed by more serious engagement only after the CSN or RAP is approved.

- CD departments typically have dedicated engagement with country authorities, especially during Spring and Annual Meetings. At these meetings, country officials express a need for TA on specific topics, which provide an indication of demand.

  - The country officials at these meetings with CD departments—for example, the chief of tax administration—are often different from the officials that meet with area departments. There is, however, a mix of practices about whether area department country teams participate in the meetings organized by CD departments.

- CD departments also have ongoing relationships with specialized country officials, which can help distill country needs. Such relationships provide an important input on specific needs that can then be used to create a prioritized TA delivery plan, as long as the danger of inertia in the selection of projects is avoided.

- Further, as discussed below, CD departments typically do their own diagnostic assessment of needs.

- Overall, as CD departments have a more limited mandate than area departments, it facilitates deeper engagement with country authorities on TA needs, which can help their ability to gauge demand and the degree of country ownership.

- Setting institutional priorities based on the type of country—fragile states, low-income countries, systemic or vulnerable emerging market countries—helps stimulate more focused country engagement by both area and CD departments. In turn, such engagement can promote stronger country ownership and help ensure that resulting TA is sufficiently demand-driven. But although prioritizing TA by type of country is appropriate, care needs to be exercised when engaging with these countries on TA needs because complaints about supply-driven TA often come from fragile states and low-income countries that feel less able to push back on TA offered by the IMF.

36. Overall, although the integration of TA with program and surveillance work has idiosyncrasies, this process does not appear to result in an intrinsic undesirable component of supply-driven TA.

Emphasis on Country Ownership in Regional and Country Strategy Notes

37. Area departments prepare medium-term RSNs at the start of the annual CD prioritization and RAP cycle. These RSNs aim to provide strategic perspective on CD priorities for each region based on countries' surveillance and program needs. The emphasis in RSNs on country ownership and country-specific engagement strategies to promote demand-driven CD varies among area departments. The Annex provides a snapshot of the treatment of country ownership and engagement in RSNs produced in 2017, although it needs to be recognized that this snapshot does not necessarily provide a full measure of the importance that departments put on this matter.

38. Since 2016, AFR has prepared detailed CSNs for most countries in the department. By end-2018, they plan to prepare one for each CD recipient in the department, with the exception of some difficult cases such as conflict-affected countries if available information is not sufficient. These CSNs cover context (relationship with surveillance or IMF program priorities); an assessment of past CD support; forward-looking CD priorities by topic; an assessment of implementation and absorption capacity; and risks and their mitigation. The notes are discussed with CD departments (and are prepared in consultation with them), RTACs, and countries. Importantly, the notes also have a section on "Authorities' Views" and play a vital role in engagement with country authorities, including by sharing summaries of the CSNs with the authorities.

39. The Asia Pacific Department (APD) produces a "TA-Surveillance Integration Matrix" for each potential recipient country in lieu of individual CSNs. With only a few program countries and historic stigma about IMF involvement in the region, APD sees CD as a promising way to engage country authorities. The matrix lists all possible areas of TA activity, and then specifies macro criticality (high to low); traction with authorities; and whether TA is ongoing or a new area. This matrix approach helps APD prioritize TA needs for an individual country and across countries. However, there is little engagement with country authorities in the preparation of these matrices, and they serve primarily as an internal disciplining device for country teams and APD's senior management.

40. With the recent RAP reforms, area departments are responsible for defining "heavy users of CD" and prepare an AFR-style CSN for these countries. It remains to be seen how well such a voluntary self-regulatory mechanism will work. A more mandatory approach that requires CSNs for objectively defined "heavy users," with due emphasis on the authorities' views, would be preferable.

41. The terms of reference (or briefing papers) prepared in advance of individual TA projects do not systematically assess country ownership or report on authorities' views. However, as such terms of reference are typically produced following a request for TA from country authorities, either in the form of a formal letter or verbal requests by country delegations during the Annual or Spring Meetings, it suggests that countries do have some ownership and support the TA in question. Back-to-office reports (BTOs) following the conclusion of TA missions, by contrast, tend to be a more likely place to report on issues related to country ownership, the possible divergence of views with the authorities, and potential risks.

TA Diagnostics and Design to Promote Better Engagement

42. Strong TA diagnostics and design are essential to foster country ownership and respond effectively to country needs. Indeed, country involvement in diagnostics, as well as TA design and objective setting, should be standard practice. Often the modality of TA and the selection of experts and what they deliver influence how recipient countries view the quality of TA and the traction that it generates. In addition to standard missions prior to TA delivery to discuss the design and objectives of planned assistance, CD departments have a variety of diagnostic and assessment tools at their disposal to undertake this work.

43. The Monetary and Capital Markets (MCM) department's tools are the Financial Sector Assessment Program (FSAP); the Financial Sector Stability Review (FSSR);[3] and multi-topic

[3] The FSSR is a new tool. To date, three have been completed (Honduras in 2016, Costa Rica and Paraguay in 2017) and two are underway (Uganda and Fiji).

scoping missions. These programs are closely linked to the IMF's standard surveillance work. The goal of FSSRs, which are intended to be both a diagnostic and planning instrument, is to help countries define a programmatic, medium-term, sequenced TA roadmap to help countries build capacity and strengthen financial sector resilience. The scope of the diagnostic is established in agreement with the authorities and the technical recommendations are tailored to individual country circumstances. If capacity constraints are identified, they are duly noted in the reports (for example, to increase personnel resources, to provide additional training, to increase capacity to recruit and retain specialized staff).

44. Recommendations made in FSAPs are integrated into Article IV staff reports. This can lead to the identification of a TA need and possible interest from the country authorities. TA needs identified in an FSSR are discussed with the area department (and also the World Bank when they are involved) and with country authorities. If country authorities agree on the need for TA, a diagnostic mission is mounted to develop a programmatic TA roadmap. There are, however, also cases where a TA need might be identified in an FSAP or FSSR, but the country does not want the TA. In such cases, if the country were not persuaded to accept the recommended TA, neither the area department nor MCM should impose the proposed TA.

45. The Fiscal Affairs Department (FAD) has a range of diagnostic and assessment tools that are less closely linked to standard surveillance work than in the case of MCM. These tools are (i) the Revenue Administration Fiscal Information Tool (RA-FIT); (ii) Revenue Administration Gap Analysis Program (RA-GAP); (iii) Tax Administration Diagnostic Tool (TADAT); (iv) Fiscal Transparency Evaluations (FTEs); (v) Public-Private Partnership Fiscal Risk Assessment Model (P-FRAM); (vi) Fiscal Analysis of Resource Industries (FARI); and (vii) Public Investment Management Assessment (PIMA). In addition, the IMF is a partner in Public Expenditure and Financial Accountability (PEFA) assessments. There is considerable engagement with country authorities both in advance of and during missions to apply these tools. Application of these tools helps IMF staff better understand a country's needs and absorptive capacity, and may or may not lead to the identification of specific TA needs. Some tools facilitate peer-to-peer learning (for example, TADAT) or allow countries to benchmark themselves against other countries at a similar level of development (for example the FTE, which distinguishes between basic, good, and advanced practices in its assessment of various transparency principles). Some also facilitate IMF learning from countries (for example, P-FRAM), which can help enhance future TA delivery by FAD to other countries in that field.

46. FAD sees undertaking a thorough diagnostic in advance of TA delivery in a specific area to be crucial, especially in surveillance cases. Diagnostic work is therefore carried out systematically for most countries as a precursor to actual TA activities. This also helps ensure that what is included in the RAP is appropriate. TA activities can then be designed to implement recommendations of diagnostics or address capacity deficiencies identified in the diagnostic reports. Diagnostic missions also help produce a roadmap for longer-term engagement if required by circumstances.

47. STA maintains a "score card" of outstanding statistical issues in a range of countries, which it aims to align with the information annex on statistical issues in Article IV staff

reports. Countries' compliance with the IMF's data standards initiatives and countries' reporting to both STA and area departments can also point to statistical gaps that could be addressed by providing TA. If a TA need is identified and agreed with the area department, the next task is to design the modalities of how best to deliver the TA, which depends on country circumstances. In a multi-country context, STA organizes a workshop in the region to show how STA can help on a topic. Workshops also facilitate peer learning. Based on the workshop, STA can then design a work program based on individual country circumstances and make decisions about the mode of delivery (including, for example, headquarters or RTAC delivery) and source of funding. In a single country context, STA fields a diagnostic mission in agreement with the area department to assess the situation and determine what it would take to achieve the agreed objective. Modalities, approaches, and choice of experts are also discussed.

48. The Legal Department's (LEG) preparation for TA typically starts with a diagnostic step. For financial integrity TA, the diagnostic would be followed by a full proposal for programmatic TA for the country to consider. For financial and fiscal law TA, a shorter "remedial stage" TA will seek to address the gaps through law reform missions. The diagnostic review of the existing legal framework is typically done at headquarters, and sometimes followed by a specific diagnostic mission. If not, remedial missions would start with confirming the diagnostic analysis prepared at headquarters. Long distance lawyer-to-lawyer communications are also helpful in this regard.

49. The diagnostic practices described above are sound, as is the attention to the appropriate design and modalities of proposed TA activities based on these diagnostics. Systematic diagnostic work, with strong engagement of country authorities and an eye to the country's absorption capacity when designing subsequent TA activities, is important to promote country ownership. A systematic assessment of issues related to country ownership, including whether institutions have the organizational capacity to accomplish TA objectives and how best to gain traction at all policy levels—from technical staff, department directors, and high-level policy makers—would be a useful addition to such diagnostic work.

RBM and Promoting Country Ownership

50. A formal system to carry out RBM for CD has been embedded in a new comprehensive project management framework and supporting information technology systems. The RBM system's purpose is to specify the objectives of CD interventions and monitor the actual outcomes that the IMF hopes the country will achieve as a result of the intervention. RBM employs a standard logical framework, or "log frame," to summarize how outcomes will be achieved as a result of a CD intervention. This includes establishing milestones to provide checkpoints to assess whether results are on track for projects that take several years to complete. Importantly, the system requires an explicit evaluation of project implementation risks including political buy-in, institutional capacity, and idiosyncratic risks.

51. Taking an example from FAD, the log frames for externally financed projects have been produced as part of the project proposal document. The objectives, outputs, outcomes, and verifiable indicators are drawn from the RBM catalogue, which FAD notes relies on international best practice to define standards for capacity improvements. The priorities and areas of focus, however, are typically the result of discussions with donors and authorities, plus an examination of diagnostic material.

52. The RBM system could potentially help get better agreement with country authorities on the objectives and outcome of TA and the milestones to gauge whether the project is on track. At present, however, it appears that country engagement is not sufficiently systematic in terms of whether the authorities have been fully involved in the design of the priorities, log frames, and milestones, except perhaps in the larger cases. Going forward it will be important to develop a process to make country engagement more integral to the RBM process and ensure that the outcomes embedded in the system rely not only on what the IMF hopes member countries will achieve but also on the desires of member countries.

Do Divergent Departmental Agendas Affect TA Prioritization?

53. The interaction between area departments and CD departments is cordial and cooperative but divergent perspectives and agendas do arise. However, these divergences matter only if they result in poor prioritization and allocation of TA, especially TA that has an undue supply component and insufficient country ownership. An attempt to assess these divergences and the potential impact on TA allocation is provided below.

54. A common observation by area departments is that because CD departments manage the budget for TA, they have significant power over TA allocation and tend to promote their own priorities. They note that this can create incentives for CD departments to protect their turf and budgets. But in assessing this concern, it is important to keep in mind that CD delivery is “free,” not just for recipient countries but also for area departments, which can affect their behavior and incentives. Indeed, there is little clamor from area departments to transfer budget control to them, and in any case this solution would come with its own set of potential harmful consequences.

55. Rather, the RAP process is designed to mitigate potential problems arising from budget control. As part of this process, area departments need to use their prerogative in approving all TA, including any changes in programmed TA during the course of the year, to prevent potential improper budget use by CD departments. Deficiencies in the availability of real time information, however, can hinder area departments from exercising this prerogative and more generally can hamper the good cooperation and communication needed for the RAP process to work well. This puts a premium on completing ongoing work to improve knowledge management and broader information sharing for CD under various capital projects.

56. Area departments also note that CD departments may correctly identify needs but may miss relative priorities, or that on occasion they may misidentify needs. To take a somewhat extreme example to illustrate the point, if CD departments have substantial resources (including under-employed experts) available for TA in a certain area (say, public financial management or central bank operations), they tend to be more aggressive in promoting TA in that area, both with area departments and directly with country authorities. Many countries have a need to improve capacity in these areas, but this does not mean that these are the areas where the need for TA is greatest. Area departments thus believe that they are in a better position to help countries identify TA needs and priorities, both within a country and across countries in a region.

57. CD departments' counterpoint is that it is a flawed assumption that area departments have superior knowledge about the needs of a country. They note that area departments often suffer from the problem of "unknown knowns" because they tend to think in terms of generalities, while meeting country needs requires deep and specialized knowledge. Often conversations about specific TA requirements need to take place expert-to-expert, and area departments are poorly equipped to contribute to these conversations. CD departments acknowledge that area departments might be in a better position to identify within-country or across-country priorities, but they point out that the issue is more complicated because it is not just what TA should be prioritized and provided but also how the TA should be provided and how much TA is needed to address a particular issue, which the area department is rarely well placed to determine.

58. CD departments also stress that they are willing to reject some projects proposed by area departments if a country's capacity and willingness to implement recommendations is insufficient. Furthermore, CD departments assert that they typically take a more medium- to long-term view of a country's TA needs, while area departments tend to focus on near-term needs. In addition, they point out that more frequent turnover of area department mission chiefs compared to their CD counterparts can lead to gaps in the transfer of information to new area department mission chiefs about past TA requests made by area departments that are still reflected in CD departments' medium-term plans. (Following the recent RAP reforms, CD departments now provide this information to area departments to fill such gaps.)

59. The application of assessment and diagnostic tools by CD departments may also lead to the identification of TA needs in a country that was not initially identified by the area department. It is natural that CD departments may have a greater interest in providing TA that is generated through such diagnostic work. Nevertheless, if a TA need is identified based on assessment and diagnostic tools but the country does not want the TA or the area department is not supportive, CD departments state that they do not push to impose such TA.

60. Area departments would also prefer to be in a stronger position to say that a country needs more TA on, for example, tax administration from FAD rather than bank supervision from MCM. They note, however, that budget rigidities do not allow such shifts quickly enough. They also comment that there is insufficient fungibility between topics covered by the same CD department. CD departments acknowledge these problems but point out that their budget allocations and staffing levels, including short- and long-term experts, reflects country demand and institutional priorities, which is hard to adjust to changing conditions without a lag because of the nature of employment contracts and non-fungible specialized staff in these departments. They note that even when their staff and experts are on limited-term contracts, changes take time because of time left on contracts and recruitment delays. These are legitimate issues but it also appears that inertia plays a significant role in delaying the reallocation of IMF funds across departments and within departments.

61. Although area and CD departments' perspectives may differ, it is important to reiterate that overall there is healthy cooperation and constructive engagement between the two. In addition, there is no compelling reason to believe that possible divergences in their agendas results in endemic flaws in the selection and prioritization of TA that results in an undue supply component of TA that is delivered. Ultimately, the area departments need to be on board with CD department proposals and a concrete request from the country is also needed, otherwise the TA does not proceed.

62. Further improving the dialogue between departments would benefit all concerned parties. Rather than divergent agendas, each type of department brings its own comparative advantage to TA prioritization and these advantages can best be leveraged through dialogue and cooperation. For example, to the extent that CD departments may have superior knowledge about country requirements, it should be incumbent upon them to convey this knowledge to the country team in a timely and accessible manner. Similarly, although area department mission chiefs may not know the specific details of TA requirements, CD departments also have experts that may not understand the macroeconomic concerns of mission chiefs. Participation of area department staff in TA missions and conversely participation of TA staff in area department missions would improve coordination and dialogue and help develop a common understanding of country priorities.

External Funding and the Prioritization of CD

63. External funding covered half of total direct spending on CD activities by the IMF in FY2017 ($134 million out of a total of $267 million), with the other half financed by the IMF's own resources.[4] In view of the sizable stock of unmet TA demands because of limits to the IMF's own resources, the availability of donor funding allows the IMF to undertake additional TA activities in response to demand. Thus, a rising proportion of external funding has facilitated the increase in CD activities in recent years, greatly benefitting member countries.

64. As set out in the funding principles established in the 2013 Review of CD Strategy, donor funding must be linked to IMF institutional priorities for CD. Nevertheless, even when external funding is related to IMF priorities, issues that affect the prioritization and allocation of TA might still arise. For example:

- Donors often have preferences on the TA topics and recipient countries (usually on a regional basis) that they wish to finance. As donors finance four-fifths of field delivery costs of TA (based on data from the Travel Information Management System for financial year 2017), their preferences can have a significant influence on TA priorities and areas where the IMF devotes its attention. Notably, these preferences result in the relative abundance of funding for certain topics or countries to the detriment of other IMF and country priorities. The availability of donor

[4] Data on external funding and total direct spending on CD activities are from the IMF Annual Report 2017, page 70.

financing also creates incentives for IMF teams to push certain types of TA for which funding is plentiful to ensure that available resources for these purposes is fully utilized, resulting in TA sometimes being provided to countries where ownership is weak. These are tangible and significant risks that require attention, but there are also mitigating factors. First, IMF staff seek to mitigate risks by pursuing funding only on topics that are priorities for the institution and through the CCB/RAP process. Second, greater use of multi-donor trust funds has been an important moderating factor as bilateral funds pose the highest risk of donor influence. And third, these dangers are somewhat allayed by the need for the IMF to finance costs that cannot be attributed to a specific project, such as overhead, supervisory staff, and governance, which gives it an institutional stake in the success of the project.

- Donors might have preferences on the choice (especially nationality) of TA experts, but IMF procedures for vetting and approving all TA experts before they are added to the roster of qualified experts alleviates potential pressure from donors.

- In bilateral cases where donor funding is narrowly earmarked, if the risk of insufficient traction in a country materializes and the IMF wishes to withdraw TA from that country, donors could get dismayed because their money is not being used. A mitigating factor, however, is that donors are also interested in value for money.

- The IMF sets its institutional priorities for CD independently, but the weights given to specific priorities within overall priorities can be influenced at the margin by the agenda of some donors.

65. Efforts continue to be made to reduce the risk that the availability of external financing distorts the allocation of TA. For example, the IMF has taken steps to negotiate fewer earmarks on the use of funds (such as accepting earmarks on topics but letting the IMF decide on highest need countries to receive TA in that area) so that donor-funded TA meets all standard criteria for providing TA. Sustained vigilance will be necessary to contain risks related to external financing. Willingness to push back on donor preferences when necessary and continued emphasis on more flexible vehicles and funding arrangements would mitigate the potential for unwarranted supply-driven TA associated with external funding.

On-the-Ground Presence and Country Ownership

66. The IMF has a global network of RTACs and RTCs to help deliver CD services to member countries. These regional CD delivery centers—which are funded by member and host countries, external development partners, and the IMF—together with resident representatives stationed in member countries, provide the IMF with an on-the-ground presence in countries and regions. This local presence can help promote demand-driven TA with stronger country ownership because it enables frequent dialogue with country authorities and better integration of TA and training. Notably, RTACs typically ask country authorities to provide, at least annually, an assessment of their needs when work plans for the next fiscal year are being prepared and country visits by center coordinators also provide an opportunity to update and refine these assessments of demand. Such local presence enhances the ability to respond quickly to emerging demands. Many reforms are opportunistic and being in frequent and close contact with countries facilitates accommodating these opportunistic demands. RTACs and RTCs also foster regional integration and make it easier to tailor knowledge sharing to the needs of the region.

67. But these advantages do not mean that RTAC-based TA is superior to headquarters-based TA. Such a dichotomy between RTACs and headquarters is too simplistic. Furthermore, RTACs operate under the guidance of headquarters and rely heavily on backstopping from Washington. Rather, resident representatives and RTACs can help enhance country engagement to discuss specific TA priorities—within the overall strategic priorities established by headquarters—and determine true demand. In addition, once a decision is made to deliver TA, implementation and delivery by RTAC experts who are typically more familiar with local conditions allows for more hands-on interaction with country authorities and can increase traction.

68. Interviews suggest that the quality of communication and coordination between RTACs and headquarters (both area and CD departments) varies across departments. Stronger coordination to fully exploit all available synergies between headquarters and the IMF's on-the-ground presence would benefit all parties and promote greater emphasis on demand-driven TA and country ownership.

69. Resident long-term experts, another mode of on-the-ground presence, also facilitate country ownership. Long-term experts based in the field work directly with country authorities and can play an instrumental role by providing advice to the authorities on TA that could be requested and assessing demand, reporting to headquarters on the needs identified in the field, and supporting the implementation of TA recommendations. Some resident long-term experts are associated with RTACs while others are not.

Training and Country Ownership

70. The focus so far has been on the TA component of CD, but greater emphasis on pairing TA delivery with training could enhance a country's ownership of TA that it receives. As part of its CD mandate, the IMF "helps train government officials so they improve their ability to analyze economic developments; develop diagnostic, forecasting, and modeling tools; and formulate and implement sound macroeconomic and financial policies" (IMF Annual Report 2017, page 67). Moreover, as noted in paragraph 7, training is an integral part of the IMF's CD mandate and sharp distinctions between "TA" and "training" are not meaningful.

71. TA activities that are complemented with training could strengthen implementation of TA recommendations and help enhance a country's absorption capacity. All modes of traditional training delivery—namely, face-to-face catalogue courses, online courses, and customized training—and others, such as peer-to-peer workshops, should be deployed more strategically to support TA and promote country ownership. As the term implies, much of the customized training currently being delivered is unique, which can make it more difficult to deliver, including because it may be more costly. But customized training need not be difficult to deliver or more costly if there were to be more emphasis on TA experts and RTACs delivering such training as part of TA projects, a mode where some effort is already ongoing. Too often training is mistakenly seen as the job of the Institute for Capacity Development rather than of all CD departments in their areas of expertise. Furthermore, catalogue and online training can be tapped at little extra cost by being more deliberate in the selection of topics, participants, and timing to support TA and surveillance or program priorities.

D. Steps to Put Greater Emphasis on Country Demand and Ownership in TA Decisions

72. As the IMF seeks the intersection of country demand on one side and IMF institutional priorities on the other, strong country ownership and commitment should be a critical factor. Ensuring strong country ownership and commitment, including through substantial country engagement prior to the delivery of TA, is essential to limit unwarranted supply-driven TA and maintain attention to demand factors in TA allocation decisions. Focusing on ownership should be a fundamental element of the process to ensure that scarce resources are appropriately allocated across regions, across countries, across topic areas, and across short- and medium-term needs. Distilling the discussion in previous sections, recommendations to make country ownership more central in TA prioritization, and allocation decisions are outlined below. These recommendations are deliberately general. Converting them to specific steps that can be acted upon is best left to practitioners to design.

a) **Further strengthening the RAP process to better integrate TA and area department country work.** The RAP process is central to promote TA that has strong country commitment and is the first line of defense against unwarranted supply-driven TA. The process needs to ensure that prioritizing and allocating TA is well integrated with IMF surveillance, lending, and policy advice. Thus, the first and perhaps most critical step in the RAP process is that area departments prioritize demands by country and topic drawing on their surveillance and program work to identify risks, vulnerabilities, and policy priorities, together with an appraisal of country ownership. Indeed, in view of their surveillance role, area departments are uniquely placed to provide a cross-sectoral and macroeconomic assessment of relative TA needs in a country. It was appropriate, therefore, that the RAP process reforms that became effective in September 2017 strengthened the ability of area departments to be an effective counterpart to CD departments as they negotiate TA delivery plans and try to match demand and supply. As area departments take on this task, country mission chiefs and teams need to be fully engaged in the TA dimension of their work, better integrating TA into surveillance so that the IMF's technical expertise can be targeted more effectively at key policy priorities. This engagement, however, is idiosyncratic and much depends on the emphasis that mission chiefs put on this aspect of their work. A culture shift, with appropriate incentives for mission chiefs and country teams to fully integrate CD-related work into their country work is paramount. To help prioritize TA demands this country engagement should involve not just advocacy and persuasion but also an assessment of potential country ownership and commitment and capacity to implement the advice being provided. Such a culture shift will not occur unless there is also a change in accountability for department heads and mission chiefs.

b) **Improving the exchange of information between departments and utilizing this information to increase the efficiency and transparency of the RAP process.** Better information exchange and utilization are essential to empower area departments to step up their role in discussions of TA priorities. It will therefore be important to assess whether existing systems to exchange information between departments are achieving the desired result, and more importantly to evaluate whether the information is being utilized to increase the effectiveness of the RAP process. If there are deficiencies, a corporate systems solution to manage CD information—rather than the current compartmentalized department-level information management system—will be required. More generally, the quality of the RAP process depends on the quality of the dialogue between area departments and CD departments, with an emphasis on the joint assessment of country ownership. More frequent embedding of staff from area and CD departments in each other's missions could enhance the quality of the dialogue and help develop a common understanding of country priorities.

c) **Ensuring that the RAP process is not just an internal prioritization exercise with limited country engagement.** Assessing whether there is sufficient country ownership and commitment to implement the policy and reform plans the IMF intends to support with CD interventions will require detailed and sustained dialogue with countries at a leadership and technical level by both area and CD departments. This is a prerequisite for a robust RAP process. Without such prior engagement, the RAP exercise would merely be the IMF's mapping of what it believes countries should do.

d) **Fostering budget reallocations to meet shifts in country demand.** The allocation of funds across CD departments in the IMF's budget process needs to be made more flexible to respond faster to shifting demands. Flexibility will be more important as resources devoted to CD move from the recent phase of rapid growth—which made it possible to allocate more resources to most areas without making difficult choices about areas to cut—to a more stable phase. A greater role for the CCB on CD budget matters would help address the inherent inertia in incremental budgeting and also identify required shifts in staffing and expertise. This stepped-up role for the CCB to promote needed adjustments in resource allocation should include (i) a stronger link between the CD priorities established by the CCB and the budget; and (ii) greater granularity in CCB proposals and their time horizon. For example, the CCB could distinguish between the following three types of resource shifts (in ascending order of rigidity) as input into the budget process:

   - *Shifts in regional or country focus*—CD departments should be able to implement such shifts within their IMF-financed CD envelopes without much difficulty. For example, if the overall IMF budget envisages a shift in area department resources toward a particular department because of heightened vulnerabilities, then IMF-financed CD should be able to follow suit if this region is also identified as a priority by the CCB.

   - *Intra-departmental shifts in topic*—such shifts (for example, from tax policy to expenditure policy or from balance of payments statistics to government finance statistics), should also be achievable within existing departmental CD budget envelopes. But these shifts can take longer to implement because of staffing rigidities.

- *Inter-departmental shifts in topics*—such shifts (for example, from FAD's work on public financial management to MCM's work on bank supervision) are harder to achieve because of rigidities related to staffing and expertise and also because incremental budgeting is prone to inertia as all departments individually believe that they should be the beneficiaries of any shift in resources and are loath to give up resources. A corporate agreement on such shifts, fostered by the CCB, would therefore be required.

By providing an annual breakdown along these lines, consistent with the medium-term priorities for CD, the CCB could provide an important input into the budget process. Both near-term and medium-term implications of CCB proposals for the budget could be reflected taking into account that budget flexibility increases with the time horizon.

e) **Focusing more on assessments of country ownership in key TA documents.** Key TA documents should contain more systematic and rigorous discussions of country ownership and commitment, the track record of implementing advice from previously delivered TA, and the authorities' views. In particular:

- RSNs should be required to outline tangible departmental procedures and practices to promote country-specific engagement strategies in the region to foster country ownership and commitment. The role of country ownership in TA prioritization decisions should also be explicitly addressed.

- CSNs are required only for "heavy users of CD," with the definition of such users left to departments. It remains to be seen how well such a voluntary mechanism will work. It would be preferable to have an obligatory approach that requires the preparation of CSNs, with due emphasis on the authorities' views, for a priority list of objectively defined heavy users. An important advantage of the CSN process is that it forces coordination between all relevant parties—area departments, CD departments, RTACs, donors, and country authorities—and allows a holistic view of a country's TA needs thus reducing the risk of segmentation.

- BTOs following the conclusion of TA missions should be required to assess country ownership of the TA being provided and potential risks. They should also report on areas where the authorities' views differ and the implications for gaining traction at all policy levels. The assessments from BTOs should feed into subsequent RAP rounds with mid-course corrections as needed.

f) **Using diagnostic work to assess and promote country ownership.** Diagnostic work as a precursor to actual TA activities, with strong engagement of country authorities and an eye to the country's absorption capacity when designing plans for TA delivery, is an important tool to promote country ownership. Diagnostics also help ensure that what is included in the RAP is appropriate. The emphasis that CD departments put on diagnostics is therefore welcome. A systematic assessment of issues related to country ownership and how best to gain traction at all policy levels—from technical staff, department directors, and high-level policy makers—would be a useful addition to such diagnostic work. A word of caution, however—mounting comprehensive diagnostic assessments prior to providing TA can be tantamount to supply-driven TA making it important to be judicious in their use, including ensuring agreement with country authorities on the type and depth of assessment that is conducted.

g) **Making country engagement more integral to the RBM process.** The new RBM system can be instrumental in getting better agreement with country authorities on the objectives and outcome of TA, thus enhancing country ownership. It will be important to develop a process to make country engagement more integral to the RBM process, including the full involvement of authorities in the design of priorities, log frames, and milestones. The monitoring and evaluation of TA using the RBM system should also be used to answer three basic questions during the course of a project and appropriate action should be taken based on the answers:

   - Is TA being oversupplied relative to demand and absorption capacity?
   - Should TA be withdrawn because of insufficient traction and country ownership?
   - Is the right kind of TA being supplied or does the TA suffer from some of the problems identified in paragraph 19?

h) **Further mitigating risks to the prioritization of TA related to external funding.** External funding of CD activities has ramped up significantly in recent years greatly benefiting the membership. But external funding also poses risks to the prioritization and allocation of TA. Notably, donors often push for what they want to spend their money on, which results in the relative abundance of funding for certain topics or countries at the expense of country and IMF priorities and sometimes the provision of TA to countries where ownership is lacking. Even though external funding is related to IMF priorities, issues that affect the prioritization and allocation of TA might still arise. Mitigating the potential for unwarranted supply-driven TA associated with external funding will require continued emphasis on more flexible funding vehicles and funding arrangements, together with the courage to push back on donor preferences when necessary. Internally, within IMF staff, guarding against incentives to promote certain types of TA primarily because external funding for it is plentiful will remain important.

i) **Leveraging on-the-ground presence to enrich country engagement.** Opportunities to leverage resident representatives and RTACs to enhance country engagement and identify and promote TA opportunities with a strong country ownership should be exploited. In addition, TA delivery by RTAC experts, who are typically more familiar with local conditions and are also well placed to integrate TA and training, allows for more hands-on interaction with country authorities and can increase traction. As the quality of communication and coordination between RTACs and headquarters varies across departments, stronger protocols to promote better coordination between headquarters and the IMF's on-the-ground presence would benefit all parties. Work underway on a comprehensive project management framework and supporting technology systems should improve information sharing, but this is a complement not a substitute for better underlying communications structures.

j) **Putting greater emphasis on pairing TA and training to enhance country ownership.** Complementing TA activities with training strengthens the implementation of recommendations and helps enhance a country's ownership of TA. Therefore, it would be beneficial to put greater emphasis on paring TA and training, tailoring the modalities of delivering the training to needs and circumstances. This might have resource costs, but the payoff in terms of meeting TA objectives would make it worthwhile. Further, training should be provided by all CD departments in their areas of expertise, and also by RTACs, and become an integral part of their work. This is already the practice to some degree but needs to be stepped up. The notion that "training" is the job of the Institute for Capacity Development, while specialized departments do "TA," is wrong.

73. The recommendations above have concentrated primarily on internal IMF matters, but country authorities also bear some responsibility to improve the prioritization of TA. To have ownership it is essential that country authorities have their own set of priorities, better internal coordination, and a strategy to request TA for their most important needs. This should include expressing their relative priorities across different CD departments (for example, whether there is a greater need for TA on tax administration versus monetary policy frameworks) to permit a more holistic view of TA allocation. Meeting this responsibility is an important defense against supply-driven TA and to ensure that the IMF's CD work is sufficiently demand-driven.

Annex I. Treatment of Country Ownership and Engagement in 2017 Regional Strategy Notes

African Department

1. "Country and regional strategies based on track record, ownership, and prospects are being used as a guide to allocate TA resources both across and within countries" (page 4).

Asia and Pacific Department

2. "APD's near-term focus is to (i) further integrate CD activities with policy advice in country work, (ii) emphasize country ownership and results …" (page 1).

3. "CD delivery also needs to be nimble so that it can seize opportunities of strong ownership" (page 2).

4. "Key criteria for prioritizing TA and training needs to include capacity constraints within countries, macroeconomic vulnerabilities or criticality as informed by surveillance and program work, systemic importance, ownership of reforms, track record on previously delivered TA/training, demand from the authorities and complementarity with other TA providers" (page 2).

5. "While country ownership is instrumental, donor coordination and cooperation can play an important role particularly in countries where donors are numerous but capacity is limited" (page 5).

6. "CD activities with an outreach dimension could also help strengthen ownership and provide an impetus for implementing Fund CD and surveillance recommendations" (page 9).

7. "APD will continue collaboration with ICD to scale-up and enrich engagement with the authorities" (page 9).

European Department

8. "Country authorities generally share European Department (EUR) views on CD priorities and strategy. In program and near-program countries, TA needs are defined through an iterative process between the respective EUR country team and the authorities, and generally consist of TA in areas that are jointly seen as critical for program implementation. In non-program settings, TA priorities are broadly reflective of needs identified in the Article IV surveillance consultation process, and are determined often with the authorities' agreement with the identified need" (page 7).

Middle East and Central Asia Department

9. "Mission chiefs will be key drivers of CD, guided by country-specific engagement strategies, and in close consultation with authorities, functional departments, regional centers, and external partners" (page 1).

10. "While the areas noted above are critical anchors to our program, the prioritization and allocation of TA and training will continue to be guided by country ownership and commitment, including by considering track records in implementing past TA recommendations and absorption capacity" (page 5).

11. "New modalities of CD planning and delivery, underpinned by reforms to better integrate CD into policy work, with mission chiefs as key drivers of CD, in some cases with country-specific engagement strategies to be discussed with authorities, particularly for some heavy CD users (e.g., Afghanistan) and systemically-important countries (Saudi Arabia), and greater analytical collaboration and coordination with CD providing departments and other regional institutions. Work has begun to assess options on how to strengthen the CD engagement with the CCA and other Middle East & Central Asia Department (MCD) countries, including through a regional CD center" (page 4).

12. "CD efforts across the two sub-regions have strengthened engagement and traction, with enhanced understanding of conditions, better analysis and design of policy responses, and improved implementation in some countries" (page 3).

Western Hemisphere Department

13. "Ownership and Track Record—Priority will be given to those countries with strong ownership and a proven track record of leveraging TA/training for positive policy outcomes, or for a demonstrable improvement in institutional capacity, ideally supported by the RBM system. Positive changes to support reforms, impact of factors outside of the control of the authorities, and other developments that might give rise to expectations that the country will take greater ownership of future TA/training delivery shall be considered" (page 1).

14. "Topical Prioritization: With our strong emphasis on country ownership, Western Hemisphere Department (WHD) has, and will continue to follow primarily a demand-based approach to prioritizing topical areas of TA and training provision" (page 2).