



# How does the institutionalisation of development policy influence the effectiveness of ESF interventions?

Evidence from the evaluation of human development programmes in Hungary

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*For useful knowledge*

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# Motivation

Evaluations of ESF-financed development programmes regularly concluded that

- there is cherry-picking of clients (or some other distortion) due to the indicator requirements of financing contracts
- there is lack of coordination with sectoral policies, which leads to sustainability problems

We have drawn the following lessons:

- It is not enough for the evaluator to say that such distortions should be corrected.
- Evaluation should make recommendations for changing institutional incentives in order to solve these problems.
- This requires an institutional approach in evaluation.

# Perspective and Questions

- Perspective:
  - Efficiency and effectiveness requires that actors in the implementation process have **incentives** congruent with policy goals.
  - These incentives depend on the way the implementation process is **institutionalised**.
- Questions:
  - What are the **key challenges** to institutionalising the implementation of Operative Programmes?
  - What **institutional solutions** did Hungary adopt in the 2007-2013 period?
  - How did these institutional solutions **affect** the efficiency and effectiveness of OPs?
  - What general **lessons** can be drawn?

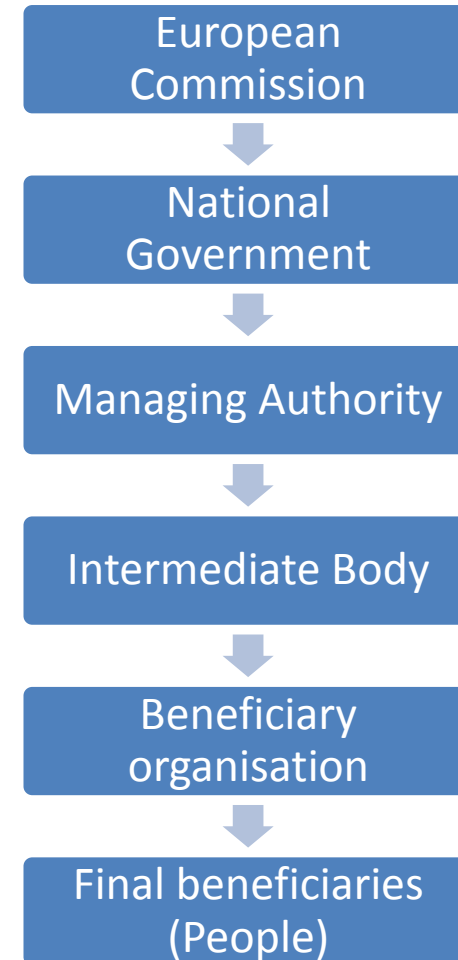
## HETFA Research Institute conducted in 2012-13

- Nine evaluations of human development programme financed by Hungary's Social Renewal OP (ESF) and Social Infrastructure OP (ERDF)
- Sectoral, not territorial programmes
- Mixed methodology
- New institutional economics as theoretical framework to explore institutional solutions in implementation
- Can we generalise?
  - Hungary's specific responses to general dilemmas
  - Large amount of funds – 12% of central budget in 2012

# Key challenges of institutionalising OPs

- Chain of Principal-Agent contracts
  - Divergence of interests and information asymmetry
  - Problems of coordination and moral hazard
  - Selection and motivation by incentives as potential solutions
  - Each P-A relationship is constrained by incentives from 'above' and limited ability to control agents 'down the chain'

## Simplified graph of P-A relationships



# Key challenges of institutionalising OPs

- 2 key challenges:
  - How to respond to the expectations laid down in the contract between EC and national government?
    - National ‘promises’ in terms of absorption, regularity, quantifiable indicators
  - How to involve existing sectoral or territorial organisations of public administration in the implementation?
    - Alternative is to create separate organisations.

# Institutional solutions I – OP Management

- National Government – Managing Authority relationship:
  - Selection: MA separated or subsumed under sectoral ministry

	Separated ( <b>Hungary's choice</b> )	Subsumed
<i>Organisational goals</i>	Few clear OP-specific goals (absorption, no irregularities, ESF indicators)	Multiple sectoral goals; overall performance of sectoral policy
<i>Strength</i>	Strong incentive to fulfil OP specific goals	Strong ability and incentive to coordinate with other sectoral policies
<i>Weakness</i>	Weak ability and incentive to coordinate with other sectoral goals	Weak incentive to fulfil OP specific goals Compromise with other goals

# Institutional solutions II – OP intermediation

- Between the Managing Authority and beneficiaries:
  - Level of involvement of sectoral administration:
    - as Intermediate Body or
    - as beneficiary of a ‘strategic project’
  - Hungary’s choice:
    - centralised, separated IB
    - Tendering systems managed by IB vs ‘strategic projects’ managed by sectoral ministry or agency
- Dilemma of delegation to sectoral administration
  - Under delegation: sectoral internal monitoring and incentives must be trusted
  - Problem of credible threat against a (powerful) ministry



# Institutional solutions II – OP intermediation

- Responses:
  - Delegation only if credible internal control and incentives exist or are easily created (eg scholarship programmes in higher education)
  - Partial delegation – direct performance contracts with lower level agencies within the sector (eg regional public employment centres)
  - ‘Own’ tendering system if lack of trust in sectoral agencies (eg grants to universities, nonprofit organisations in employment policy)

# Effects of institutionalisation

- *Overstretched projectification*: almost exclusively financing through projects
  - Project as one-off, short-term performance contract with quantified indicators
  - Suitable for procuring infrastructure and standardised, easy-to-measure services
  - Ill-suited to human services whose true effects are difficult to measure and often long-term (basic research, primary education, social care, employment support etc.)
  - Behaviour of beneficiaries biased towards short term goals, foregoing beneficiary's investment with long-term effects

# Effects of institutionalisation

- *'Hot Potato' game of risk-shifting*
  - MA and IB minimise risk of producing OP-level indicator values
    - OP-level indicators appear directly in financing contracts
    - Payment is directly tied to fulfilling indicator requirements
  - Risky indicators induce risk-aversion
  - Two strategies:
    - Ex ante: promise very low indicator values
    - Ex post: structure activities to minimise risk of not fulfilling the promise – refrain from real innovation; cherry-pick non-risky clients etc.
  - MA is complacent due to pressure to absorb and supply indicators
- *Role of incentives beyond financing contracts*
  - Success where the existing institutional environment gives incentives
    - E.g. universities embedded in international science or with strong partnerships with labour market actors
    - E.g. nonprofit service providers working closely with churches or municipalities.

# Effects of institutionalisation

- *Problem of sectors receiving large funds (especially under fiscal austerity): Crowding out of regular budgetary resources*
  - Projects are allocated where they can be absorbed, not where project finance suits the activity
  - Ordinary activities labelled as ‘developments’ and projectified
  - Traditional governance structures are weakened:
    - At personal level: low wages and lack of career finance
    - At organisational level: insecurity of long-term finance and weakening of non-project-based management structures

# Lessons learned

- Planning for 2014-2020
  - Increased stress on OP indicators may have unintended negative effects
  - Creating trust in sectoral administration is key to mitigate these effects
    - Presumes making sectoral monitoring and incentives credible
  - Focus should be on easy-to-measure developments
  - For difficult-to-measure developments:
    - Financing should share risks sensibly – contracts should go beyond crude use of indicators
    - Where project finance, i.e. short-term performance contracts, are ill-suited, effectiveness can be ensured by greater reliance on existing governance structures

# Lessons learned

- Evaluation:
  - Need for theory-based evaluation to provide useful recommendations to change equilibria
  - New institutional economics as a theoretical frame to identify problems of information and incentives as well as alternative solutions
  - Recommendations at different levels:
    - European Commission
    - Setting up Mas and IBs
    - Choice of allocation mechanisms
    - Contract details



Thank you for your  
attention.

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