



QUARTERLY PROJECT REPORT [Second Quarter, 2007]

**United Nations Development Programme
Afghanistan
Making Budgets and Aid Work project
01-Apr-2007 – 30-Jun-2007**

Project ID:00056407
Duration: 60 months May 2007 to April 2012
**Component (MYFF): Public Administration Reforms
and Anti Corruption**
Total Budget: USD 7,541,170
Unfunded: 0.00

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I. PROJECT IMPLEMENTATION CHALLENGES

PROJECT RISKS AND ACTIONS:

There are several risks which may jeopardize the overall success of the project in supporting an effective and efficient budget preparation, planning and implementation process in the 1386 Afghan fiscal year. These risks include:

Delay in the preparation of the ANDS

Integration of the ANDS in the budget process is a key for its successful implementation and transformation of the budget into an effective tool for prioritization and realization of the government policy objectives. The Budget Department plans to use ANDS priorities as a basis for setting budget ceilings within the Medium-term Budget Framework. However, in order to be used as a basis for the budget allocation decision-making process for the 1387 budget cycle, ANDS sector strategies must be finalized by end of August. In order to ensure that this deadline is met by the ANDS team, the project has initiated regular meetings with ANDS to track new developments.

Low capacity in the line ministries

A major milestone achieved by the 1385 budget was the improved execution of the development budget process. This has mainly been the result of an active role played by the Budget Department in initiating implementation of the new mechanism. This new mechanism has introduced pipeline projects which can access a common pool of limited resources whenever these pipeline projects are ready to be implemented on first-come basis. This mechanism has increased competition among line ministries and quality of project preparation process. In addition, improved monitoring and coordination with line ministries have significant impact on budget execution.

Still, external impediments during the reporting period continue to hinder the speed of the budget implementation, including lengthy procurement process and unclear procurement regulations, which are significantly slowing down the purchase process in the provinces and ultimately affecting budget execution levels, insufficient projects preparedness and low capacity in some line ministries.

PROJECT ISSUES AND ACTIONS:

Next Phase of the Project:

The finalization of the new phase of the project was achieved during the second quarter. The second stage of the project is financed by DFID, CIDA and GTZ with DFID providing the bulk of financial support to the project. In addition, DFID is expected to fund technical assistance support to the MoF and line ministries through the provision of international advisors and training activities. The project is preparing to institutionalize a new coordination mechanism which is currently being reviewed by the donors. It is expected that the coordination mechanism will, through the introduction of an independent TA Coordinator position in the MoF, ensure that various technical assistance initiatives (supported by donors such as USAID, DFID, ADB and UNDP) work more effectively as a whole without wasted duplication of time and resources.

II. IMPLEMENTATION PROGRESS

The initial phase of the project, entitled Making Budgets Work, was completed at the end of March 2007. The second phase of the project, entitled Making Budgets and Aid Work began in April 2007. The following progress update summarizes key achievements of the project during the second quarter of the year.

Two-thirds of the advisory staff currently working with the Budget Department of the MoF are contracted by the MBAW project. Thus, the project is in a special position to ensure the daily operations of the department and to improve the human capacity, skills and competency level of the civil servants in the Budget Department so that the department is empowered to take ownership of the following results:

COMPONENT 1: THE BUDGET IS COMPREHENSIVE, POLICY BASED, PREPARED IN AN ORDERLY MANNER AND SUPPORTIVE OF THE NATIONAL DEVELOPMENT STRATEGY

OUTPUT 1: STRENGTHENED BUDGET POLICY AND PLANNING PROCESSES

The project is continuing to provide support to the Budget Department to develop and implement the National Budget in line with national strategic objectives and policy priorities, in a timely manner.

1386 Budget Approval

After incorporating changes recommended by parliament, the 1386 budget was re-submitted to Parliament and was adopted on 24 April 2007. The budget preparation process for 1386 proceeded more smoothly than in previous years and adhered to its schedule. This resulted in the adoption of the budget by the Parliament much earlier in the year than in previous years, which should result ultimately in a better actual budget implementation rate for the 1386 budget. To further improve budget execution and implementation of the development budget, a new mechanism which aims to ensure that the national development budget is realistic has been introduced by the Budget Department.

Integration of ANDS into the budget planning process

Integration of the ANDS into the budget process is the key to successful budget implementation with regards to, ensuring that the it serves as a tool which translates the government's priorities and objectives into services that address the needs of citizens. Therefore, the Budget Department has initiated discussions with the ANDS teams on next year's budget formulation. The aim is to provide incentives and support for line ministries to incorporate ANDS priorities into their budget planning process and to have these priorities reflected in the ceilings identified by the MoF and approved by the Cabinet. Hence, the timing of the completion of the ANDS sector strategies (expected in August) will be crucial for the improvement of the budget process in .

OUTPUT 2: STRENGTHENED BUDGET FORMULATION PROCESSES

The MoF has invested a great deal of effort to improve the budget formulation process and introduce more credible and implementable budgets in the last few years. In order to support these efforts, the project continues to provide assistance in the development of and adherence to a more realistic and transparent medium-term and annual budget preparation process.

Preparation of the 1387 Budget

Budget calendar - Work on the preparation of the 1387 budget has already started. The Budget Department prepared a Budget Calendar for 1387, incorporating a medium-term approach to budget

preparation and attempting to make a clear link between ANDS, as a strategic document, and the budget decision-making process and budget allocation. The Budget Department has already shared this timeline with relevant stakeholders including the ANDS secretariat, line ministries and other departments at the Ministry of Finance to obtain their comments and suggestions.

Parliament involvement – The budget calendar has also been submitted to the Parliament for their information. The Budget Department is planning to involve Parliament in the budget preparation process to a much greater extent this year, and in particular, having them present at each major step of the budget formulation process, including medium-term fiscal framework preparation, budget ceilings development, line ministries budget submission preparation and budget hearings. This way the Parliament will develop a greater sense of ownership over the budget, which should result in a more smooth process of budget adoption by the Parliament, as well as a swifter budget implementation period later on in the year. A draft letter to the Parliament introducing this new practice has been prepared and will be issued by Ministry of Finance (Budget Department) in July.

Preparation of the Medium Term Budget Framework

Budget Circular No 1 - The project team has designed a new step within the budget calendar with the aim to facilitate the process of preparation of the Medium Term Budget Framework (MTBF) that has to be approved by March 2008. Namely, the Budget Department is planning to release, early on in the budget process this year, a budget circular (Circular No. 1). This circular would require line ministries to provide information on new spending initiatives planned for the coming three-year period, linking them with the priorities and benchmarks set in the ANDS. Additionally, the line ministries' budget ceilings set in the MTBF would be based on this information. Through the incorporation of this additional step, the Budget Department would achieve two goals: (i) the creation of a clear link between the ANDS (strategic objectives and policy priorities) and MTBF, and (ii) the setting of budget ceilings in a more transparent way. This procedure is in line with global best practices for budget formulation.

Budget Circular No 1 will be issued in early July. Meetings with ministries and donors to discuss Circular No 1 as an initial step in 1387 budget formulation will be held in throughout July and August.

Programme Budgeting Pilot

In developing the 1386 budget, the Ministry of Finance selected three ministries (Ministry of Education, Ministry of Public Health, and Ministry of Rehabilitation and Rural Development) to pilot the integration of the operating and development budget through the introduction of programme budgeting. These ministries were required to present their budget information in a basic programme format, linking their budgets with ANDS policy priorities and objectives. However, it is important to stress that the pilot ministry programme budgets for 1386 were purely indicative, and were presented in the budget for informational purposes and to provide a supplement to the traditional budget format. These pilot programme budgets are not intended to be used as a basis for appropriation.

Several lessons have been learned from the last year's process of implementing the programme budget:

- A key precondition for a high quality and meaningful programme budget is the existence of a sector or line ministry strategy which contains strategic objectives, policy priorities and performance benchmarks;
- Organizational and programme structure should be aligned to enable clear responsibility and accountability of the programme manager;
- In order to plan and monitor full cost of the programme (specific objective) both budgets, operational and development need to be integrated;

- Strong support by the senior management is crucial in order to successfully implement the programme budget.

Based on the findings, a Steering Committee (at the DM level) meeting was held to wrap-up 1386 budget cycle process, discuss lessons learned in the last year, and to plan the way forward.

The review of programme budget implementation in the Ministries of Education, Health, and Rural Development was initiated. First, a performance reporting circular was issued by the Ministry of Finance (Budget Department) to the three pilots recently. A workshop has been conducted to provide guidelines and explain to pilots how to prepare their reports. By the end of July, these three line ministries are required to provide their quarterly budget execution report on a programme basis, as well as their performance results for the first quarter.

This year, an additional four line ministries have been chosen as pilots: the Ministry of Agriculture, the Ministry of Water and Management, the Ministry of Public Works and the Ministry of Finance. Work on the preparation of each ministry's respective programme budget document has already been initiated. Initial meetings with the four pilot ministries were held at the Deputy Minister and senior management team level. A Steering Committee with all seven pilots (DM level) is planned for July 10-15 to formally initiate the 1387 budget cycle and provide pilots with a detailed action plan.

Provincial Budgeting Pilot

A provincial budgeting pilot exercise was introduced for the 1386 budget preparation process with the support of the DFID/Maxwell Stamp project. The MBW national project team has been oriented and involved in this pilot exercise. Three provinces were selected for the pilot project in the last year: Balkh, Panjshir and Kandahar. Three ministries were selected for the pilot project based on their contribution to the economic development process in these provinces: Ministry of Education, Ministry of Agriculture and Ministry of Rehabilitation and Rural Development.

This year seven additional provinces have been added to the exercise. These provinces are Herat, Ghazni, Logar, Badakhshan, Nangahar, Bamyan and Paktia. Provincial budgeting is proceeding through scheduled trips by provincial and programme budget officers in provinces where orientation and consultation meetings with the provincial governor's office, directors of pilot ministries, provincial directors, and other stakeholders such as USAID and PRTs were held. The provinces covered as of the end of the reporting period include Balkh, Herat, Panjshir and Logar. It is expected that future implementation of the exercise will be supported by the new international Provincial Budgeting Advisor who is expected on board in August.

OUTPUT 3: STRENGTHEN BUDGET EXECUTION PROCESSES

The MBW project has continued to play an active role in improving the budget execution by line ministries during the reporting period, in alignment with its budget formulation work.

Improved Budget Execution rate

Close monitoring of the large projects as well as improved coordination with key line ministries by the Budget Department have proven to be effective in improving the budget execution. As a result, the budget execution rate increased to more than 54 percent in 1385, compared with the 44 percent execution rate of the 1384 budget. Translated into nominal values, this means that execution increased from \$459 million in 1384 to \$707 million in 1385. Similarly, the execution rate for the operating budget increased to 98 percent.

In the first quarter of the 1386 budget (second quarter of 2007), development budget execution reached \$101 million, compared to \$28 million by the same date for 1385. This translates to a 6.6 percent execution rate as of the end of the first quarter of the budget year (21 June), compared to 2 percent by the same date for 1385. Similarly, the budget allotment for the development budget reached \$399 million as of 21 June, compared to \$120 million in the same period for 1385. This translates to a 26 percent allotment rate for 1386, compared to 9.5 percent for the same period for 1385.

The Budget Department, through its sector managers and budget officers, played an important role in working with the line ministries to execute their projects. The Budget Department's decision to hire more budget officers to be focal points for all primary budgetary units at line ministries has proved to be a significant factor in this regard.

Workshop on budget execution

A three-day workshop on formulation, execution, budget expenditure forms, programme and provincial budgeting was held in the Ministry of Finance for line ministries on 12-14 June, 2007. During the workshop, the Budget Department provided line ministries with specific instructions and guidelines on 1386 budget implementation. This opportunity was used also to discuss budget execution related issues faced by the line ministries and the Ministry of Finance last year.

Budget software

A four-member delegation went to Canada to meet with a vendor who provided a presentation on potential ways in which budget software might improve the budget formulation process. The Budget Department is planning to visit Synergy International software vendor in the next period, as well as other vendors providing budget FMIS module in the region, in order to select a module that would best address all the needs of the Budget Department for easier data manipulation, better coordination with budgetary units, and better control over the budget, during the budget preparation process and throughout the budget year, and at a same time be compatible with the existing AFMIS system supporting Treasury functions in the Ministry of Finance.

OUTPUT 4: STRENGTHENED AND REFORMED BUDGET MONITORING AND REPORTING

The project has started a couple of initiatives to improve budget reporting which can be made publicly available to donors, government agencies and the public through the MoF website. These initiatives include creating a central database with fiscal and budget data, weekly and monthly fact-sheets and reports, quarterly budget bulletins, and an annual performance report.

Budget execution reporting

Annual performance report - The 1385 Performance Report has been finalized and submitted to the Director General, Budget for a review. The report covers the issues of revenue performance, budget performance, budget executions, fiscal policy, aid coordination, and expenditure trends by I-ANDS sectors. Once approved by the Director General, the 1385 performance report will be printed and circulated to all donors, other international partners and government agencies.

Bi-weekly reports - In order to improve the budget execution process for the development budget, the budget department initiated a mechanism to track the top 50 project expenditures. The goal was to observe what impediments exist in the implementation of projects and to find ways to reduce or remove those obstacles through meetings with line ministries/departments by the Budget Department, Senior Management of the Ministry of Finance and with Cabinet. These reports will be produced on a bi-weekly basis this year.

Budget Department performance reporting

Quarterly bulletin – The Budget Department has initiated preparation of the quarterly budget bulletin. The first quarterly budget bulletin, covering the period 21 March to 25 June, was prepared in June. The bulletin was designed to incorporate most recent fiscal and budgetary developments, including the execution rates and issues related to the budget process and implementation. The bulletin will be posted on the MoF website and circulated to donors and line ministries shortly.

Weekly and monthly reports – At the Minister's request, the budget department has started submitting a brief report on a weekly and monthly basis to the Minister's office. These are internal reports shared within the Ministry of Finance only. The purpose of the reports is to provide an overview to the Minister and other MoF departments on Budget Department work and performance, as well as to improve information flow and increase efficiency in processing documents.

Fiscal database

Fact-sheets, which were started in July 2006, are now being updated on a weekly basis and incorporated in the budget execution reports. It is planned that they will also be distributed to donors through emails and posted on the Budget Department website (<http://aacadad.synisys.com>).

COMPONENT 2: ALIGNMENT OF EXTERNAL ASSISTANCE AND IMPROVED AID EFFECTIVENESS TO SUPPORT AFGHANISTAN DEVELOPMENT GOALS AND STRATEGY

OUTPUT 5: IMPROVED CO-ORDINATION OF EXTERNAL FUNDING IN LINE WITH THE PARIS DECLARATION, AFGHAN COMPACT AND ANDS

Aid effectiveness and managing grants and loans continue to be an important part of the project. The project plays a key role in national aid coordination.

Some of the major achievements of the Budget Department - Aid Coordination Unit (ACU) during the second quarter of 2007 are as follows:

ACU has been working on developing an Aid Policy Paper in collaboration with ANDS. The paper is intended to clearly set out what the Government will do to make aid more effective and to ensure that aid is spent in a manner that has maximum impact on economic development and poverty reduction in Afghanistan.

In order to set the medium-term agenda for the aid effectiveness, ACU has prioritized six benchmarks of Annex II of the Afghanistan Compact on aid effectiveness and has prepared an action plan. The benchmarks were presented in the Afghanistan Development Forum (ADF) 2007 and were approved by the GoA and the international community.

ACU conducted an analysis of the local impact of aid through the Peace Dividend Trust. Its findings were shared with all stakeholders in the ADF 2007. The main goal of this analysis was to encourage donors to increase their local procurement of goods and services in order to help the country achieve sustainable economic growth.

In order to streamline the reporting process, the ACU has developed a Harmonized Reporting Format (HRF) and a timeline for reporting donors' data which coincides with the national budget timetable. This will improve the reporting, monitoring and analyses of external aid significantly and will help the Government plan better for medium and long term.

Aid information management is one of the major responsibilities of the ACU. Focal points are assigned for each donor to track the information and update the Donors' Assistance Database (DAD) on a regular basis. Each year the ACU conducts financial and portfolio review with individual donors to assess donor financial performance. After each review the DAD is updated.

COMPONENT 3: IMPLEMENTATION OF THE EXIT STRATEGY TO BUILD SUSTAINABLE CAPACITY WITHIN THE GOA

As the third component of the project addresses the sustainability of the project and institutional development within the MoF Budget Department, the project will support a "Young Graduate" scheme, in which 15 young graduates will be recruited every year and given hands-on training from the project staff. Civil servants and graduates will be promoted through the PRR process. The project will gradually decrease its own staff complement (currently 76 staff) to zero by the end of the project.

The Budget Department of the Ministry of Finance had several meetings with the leadership of the Faculty of Finance at Kabul University during the year 1385 and sought their cooperation and coordination for persuading their students to join Budget Department of Ministry of Finance. Fortunately, the response was very positive and they expressed appreciation for this initiative of the Budget Department, promising full cooperation in this regard.

The Budget Department organized a presentation session for graduating students of the Faculty of Finance in order to provide an update on the performance and activities of this department and to inform them about the benefits of joining the department in terms of overall career development and acquisition of practical work experience. DG Budget/MBW Project Manager, Mr. Mohammad Mustafa Mastoor led the presentation, with other Budget Department staff assisting. After the presentation and question/answer session, students showed readiness and interest in joining the Budget Department. The DG Budget also provided information about how they could apply to the Young Graduates initiative and asked the Budget Department, Office Management Unit to coordinate with students in this process.

The Office Management Unit received 22 applications from young graduates of the Finance Faculty of Kabul University during the last few months. The project officially started recruiting the 15 first young graduates in the second quarter of 2007. On 17 June 2007, the young graduates were invited for a written test, which was a combination of technical and general questions in both local (Dari/Pushto) and second (English) languages in order to determine their technical and linguistic skills. The overall graduates' performance was very good, with 18 candidates selected for the interview session. The rest of the process will be completed in the third quarter. The project facilitates more recruitment and placement of these graduates for on-the-job training at various positions within the Budget Department. The MoF is also seeking for donors or providers to support formal training and additional exposure on public finance management. With the launching of the next phase of the project, these graduates will receive skills training and a gradual hand-over of responsibilities from national project professionals.

OUTPUT 6: SIGNIFICANT LEVELS OF TECHNICAL CAPACITY BUILT AND RETAINED WITHIN THE PUBLIC FINANCE SECTOR, PARTICULARLY WITHIN THE MINISTRY OF FINANCE AND LINE MINISTRIES

Capacity building and training

During the second quarter, the project conducted several "learning hours", held on a weekly basis on Wednesdays. The project is working with several donors, including the World Bank and DFID, on preparation of the training programme for Budget Sector and line ministries staff in Kabul and regional centers.

In addition to “learning hours” the project staff is also participating in overseas training:

Mr. Bashir Quraishi, Budget Policy Coordination and Reporting Officer, attended a three-week training programme facilitated by IMF Senior Economists on Government Finance Statistics 2001 System at the Singapore Training Institute from 4 to 22 June 2007. The training is conducted twice a year from IMF headquarters in Washington, D.C. in order to train Government officials from different countries on systems, which include classification of account codes, revenue codes and other economic codes etc.

Mr. Naseer Shafaq attended a short course entitled *Islamic Financial Products; Principles and Applications*, organized by the Islamic Development Bank (IDB/IRTI) and University Technology Mara (UiTM) of Malaysia. The course started on 26 June 2007 and ended on 1 July 2007. It provided novel insights into various subjects related to financial management and processes.

Database and DAD issues:

A stand-alone new internet connection to improve the local network, net service and information management facilities was established, with work expected to be completed in the first week of April.

The restructuring of the MoF website was also completed during the first quarter, and is expected to improve navigation, content and usability of web-based information about budget department performance.

The restructuring and upgrading of the Donor Assistance Database continued in the second quarter. Improvements are expected to increase accessibility of information by creating more options for information recording and information management, as has been requested by users. For the first time the database was redesigned to capture the development budget (Core and External) by province, which required an extensive amount of work.

Recruitment of national and international staff

The project, in line with its proposed outputs and activities, advertised 11 national vacant positions (Project Manager, Budget Officer, Budget Policy Coordination and Reporting Manager, Aid Coordination Manager, Budget Policy, Coordination and Reporting Manager, Provincial Budgeting and Reporting Officer, 2 Programme Budgeting and Reporting Officer, two Budget Execution Officers, Budget Execution Manager, and IT Officer) of staff and 2 international advisors (programme and provincial budgeting) during the second quarter. The recruitment process is still in process and expected to be completed by end of July.

III. FINANCIAL STATUS AND UTILISATION

FINANCIAL STATUS

TABLE 1: CONTRIBUTION OVERVIEW [MAY 2007 TO APRIL 2012]1

DONOR NAME	CONTRIBUTIONS		CONTRIBUTION BALANCE
	Committed	Received	
DFID	5,000,000	-	5,000,000
CIDA	2,803,738	467,290	2,336,448
GTZ	606,114	606,114	-
UNDP	50,000	50,000	-
TOTAL	8,459,852	1,123,404	7,336,448

FINANCIAL UTILIZATION

TABLE 2: QUARTERLY EXPENDITURE BY ACTIVITY [01 APRIL-30 JUNE 2007]

Activity	BUDGET 2007	QUARTERLY EXPENDITURE	BALANCE	DELIVERY (%)
Activity 8: ALD Costs for international staff	0	12,438	-12,438	
Activity 9: Provincial Programme Budgeting	575,808	385,643	190,165	
UNDP GMS	30,306	19,904	10,402	
Total	606,114	417,985	188,129	69%

Note: *Based on the agreement, the expenditure for the 2nd Quarter is made against GTZ funds. However, GTZ funds are only earmarked for provincial budget activities, not for activities at the central level. The expenditure for the 2nd Quarter of the project activities at the centre will be retroactively charged against CIDA contributions.

TABLE 3: QUARTERLY EXPENDITURE BY DONOR [1ST APRIL –30 JUNE 2007]

DONORS	ACTIVITY (as per approved budget)	2007 Budget	Q2 EXPENDITURES 01/03/07-30/06/07	BALANCE as of 31/03/07	DELIVERY RATE %
GTZ	Activity 8: ALD Costs for international staff	-	12,438	-12,438	
	Activity 9: Provincial Programme Budgeting	575,808	385,643	190,165	
GMS 5%		30,306	19,904	10,402	
Subtotal GTZ		606,114	417,985	188,129	69%
Total		606,114	417,985	188,129	69%