THE BMZ'S MULTILATERAL ENGAGEMENT

Financing and Interplay

Executive Summary

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EXECUTIVE SUMMARY

The international community needs to work together in order to achieve the Sustainable Development Goals and to protect global public goods. Germany makes important contributions to multilateral organisations through various ministries. The Federal Ministry for Economic Cooperation and Development (BMZ), which holds the largest share of the overall German multilateral portfolio, is especially relevant here. Just under 30% of the BMZ's expenditure is made up of multilateral budget items; if earmarked funds are included, the share is as high as 56%.

Despite the extent of the BMZ's involvement in multilateral development cooperation (DC), there are still evidence gaps. Various actors – including the Bundesrechnungshof (Federal Audit Office) and the Ministry itself – identify the need for evaluation and name multilateral DC as an important subject of evaluation (BMZ, 2021a; BRH, 2023).

Against this background, this evaluation is the first comprehensive analysis by the German Institute for Development Evaluation (DEval) of the BMZ's multilateral engagement. The overarching objectives of the evaluation are to contribute to transparency and accountability and to generate stimuli for learning.

The BMZ's multilateral engagement is part of a complex multilateral development system. Multilateral organisations are independent actors that have enough scope to act and operate in accordance with their respective mandates; at the same time they are often deployed in DC as project-implementing organisations (Klingebiel, 2014). Furthermore, their respective reputation and performance vary; some organisations are heavily criticised, while others enjoy a comparatively good reputation. Bilateral donors such as the BMZ are confronted with the question of how they can reconcile the promotion of the multilateral system as such with their own development interests, and what considerations need to be weighed up (Milner and Tingley, 2013). At present, the decision by the United States government to massively cut DC funding seems to be leading to fundamental changes in the multilateral development system.

The question of the BMZ's use of different financing modalities – core and earmarked funding – becomes increasingly important in view of this complex multilateral development system. The use of different financing modalities reflects decisions as to which multilateral organisations and which topics should be supported. Core funding and earmarked contributions (see Glossary: "Core funding" and "Earmarked contributions") each have strengths and weaknesses with regard to different development objectives. While core funding directly strengthens multilateral organisations but involves less control, earmarking can be used to pursue more specific development objectives and can exercise a greater steering role.

Evaluation subject and questions

The subject of the evaluation is the BMZ's multilateral engagement, which, in this evaluation, includes the multilateral financing modalities of core funding and earmarked contributions. Core funding refers to assessed membership contributions, non-earmarked voluntary contributions, capital increases and replenishments (Dag Hammarskjöld Foundation and MPTFO, 2019; Gulrajani and Lundsgaarde, 2023; OECD, 2011). Earmarked contributions are payments made by a donor country to a multilateral organisation for a specified purpose, which may be defined tightly or softly (see Glossary: "Earmarking"). They are provided on a voluntary basis (Reinsberg et al., 2015a).

The evaluation addresses five evaluation questions and assesses the "relevance", "coherence" and "efficiency" evaluation criteria of the Organisation for Economic Co-operation and Development (OECD). These evaluation questions (EQs) relate to the relevance of the multilateral portfolio (EQ 1), to the interplay between, and thus coherence of, bilateral and multilateral DC (EQ 2), to the factors that influence this interplay (EQ 3), to the efficiency of the financing modalities applied (EQ 4), and to the effectiveness of earmarked and non-earmarked contributions (EQ 5).

The focus of evaluation question 1 is the relevance criterion and the question of how the BMZ's strategic priorities are reflected in its multilateral portfolio. These priorities are derived from the Ministry's strategies on multilateral development policy since 2013 (BMZ, 2013a, 2020a, 2023a).

> **Evaluation question 1:** To what extent is the BMZ's multilateral portfolio aligned with the latter's strategic priorities? (Relevance)

In relation to the coherence criterion, evaluation question 2 focuses on interplay. The issue is primarily internal coherence, i.e. the coherence of bilateral projects and those that are financed via earmarked BMZ funds given to multilateral organisations.

> **Evaluation question 2:** To what extent do bilateral and multilateral DC interlink in a meaningful way? (Coherence)

Building on evaluation question 2, evaluation question 3 analyses factors that facilitate or hinder the interplay between bilateral and multilateral DC. The aim is to identify and systematise these factors. No assessment is made.

> **Evaluation question 3:** What factors facilitate or hinder interplay between bilateral and multilateral DC?

Evaluation question 4 emphasises the efficient use of various financing modalities of multilateral DC. The criterion of "efficiency" is thus addressed based on scientific findings on the various financing modalities.

> **Evaluation question 4:** To what extent are the various financing modalities of multilateral DC used efficiently? (Efficiency)

Evaluation question 5 asks how effective different financing modalities are. As regards effectiveness, the focus is on achieving development targets and on other consequences, for example the structures of the partner countries or how the multilateral development system as such functions. International scientific research is processed for this evaluation question; no assessment is therefore made.

> **Evaluation question 5:** How effective are core funding and earmarked contributions?

Methodology

The evaluation design comprises the complementary components portfolio analysis, literature analysis and case study. On the one hand, it describes current multilateral development practice (portfolio analysis, case study); on the other, it covers the scientific findings on this topic area (literature analysis). The evaluation design combines a broad-based analysis (portfolio analysis) with a selected in-depth analysis (case study). Descriptive statistics and a portfolio similarity analysis are used as evaluation methods in the course of the portfolio analysis, supplemented by a strategy and factor analysis. In addition, a qualitative content analysis of documents and semi-structured interviews, as well as a social network analysis, are carried out as part of the case study. The literature analysis component is implemented via a systematic review.

The portfolio analysis compares the multi- and bilateral distribution of funds; the literature analysis interprets the current state of research; and the case study analyses the interplay between bilateral and multilateral DC. The purpose is to provide the BMZ with strategic and management-relevant findings. The aim of the portfolio analysis is to obtain an overview of the components and characteristics of funds within a fixed framework. By analysing the allocation of funds, statements can be made on distribution trends over different time periods, and conclusions can be drawn on consistencies with strategic priorities. The aim of the literature analysis is to summarise research findings in a structured manner and to identify gaps, while the case study examines the interplay between bilateral and multilateral DC in a specific topic area, and analyses the factors that are conducive or obstructive to this interplay.

Results

Strategic relevance of the multilateral portfolio

With regard to the orientation of the multilateral portfolio towards the BMZ's strategic priorities, the portfolio analysis reveals a mixed picture. The BMZ's earmarked portfolio reflects geographical priorities, particularly with regard to the promotion of African countries and regions. However, the priority promotion of multilateral organisations and topics mentioned in the strategies is not clearly reflected in this portfolio. Similarly, financing modalities in the multilateral BMZ portfolio are only partly aligned with strategic priorities. The proportion of non-earmarked contributions has been falling since 2014. By contrast, the rising core funding for United Nations (UN) organisations is in line with the strategic objectives. Finally, the cross-cutting issues of "gender" and "climate" are embedded to varying degrees in the BMZ's earmarked portfolio. Gender is more strongly represented in the earmarked portfolio than in the bilateral portfolio; the reverse is true for climate.

Coherence of the bilateral and earmarked engagement

The second evaluation question on the interlinking of bilateral and earmarked forms of engagement reveals challenges in the relationship between the portfolios. Although the earmarked portfolio strengthens the bilateral portfolio geographically, at the thematic level the BMZ's earmarked contributions have neither a reinforcing nor a complementary effect, so that there is no clear strategic orientation. While the relationship between the bilateral and earmarked portfolios can be complementary and reinforcing, the BMZ's earmarked contributions should be complementary to the disbursements of the multilateral organisations, so that they are used in accordance with their mandate and the comparative advantages usually associated with it.

With regard to the coherence of bilateral and earmarked DC at the country level, the case study on projects within the core area of "Life without Hunger" in Ethiopia paints a more positive, albeit more selective, picture. It shows that there are several channels of communication and coordination between bilateral and earmarked projects. Information is exchanged both formally and informally, and this is generally rated as useful, although coordination with individual UN organisations and with other stakeholders is criticised as insufficient. Furthermore, bilateral and earmarked projects basically pursue coherent objectives, even if in practice there are overlaps and interferences between projects or with other actors. The projects endeavour to practise a division of labour and to find ways to collaborate. In practice, however, there are few joint activities, and actual synergies are difficult to achieve.

All four factors examined under evaluation question 3 – "governance/institutionalisation", "political support", "cooperation", "administrative processes" – are relevant and, depending on their characteristics, can either promote or hinder the interplay between bilateral and earmarked DC. Additional or already established institutional mechanisms in projects and with other stakeholders facilitate interplay, whereas a lack of institutional incentives for cooperation, staff fluctuation and structural challenges makes it more difficult. Political support from both the BMZ and the political partner is key for interplay and is required by project managers. At the same time, various obstacles make it difficult to use political weight to encourage interplay or, in view of vested interests such as visibility, this is not per se in the interests of all the stakeholders involved. According to the unanimous opinion of the interviewees, a good relationship of trust and personal contact promotes interplay; conversely, competition, a lack of trust in organisations and a lack of incentives in multilateral organisations make cooperation between bilateral and earmarked projects more difficult. According to the interviewees in the case study, the administrative processes factor in particular – for example different project cycles – has proved to be an obstacle to interplay. However, these challenges become less significant when there is, for example, a long history of cooperation and an established knowledge of the processes of multilateral organisations (and vice versa).

Efficiency of the financing modalities

The fourth evaluation question on the efficient use of financing modalities offers a positive picture for fragile contexts; at the same time, the use of flexible financing modalities is limited throughout the multilateral portfolio, and efficiency aspects

are of secondary importance in the design of financing modalities. In highly fragile contexts, a large share of tightly defined earmarking enables a flexible use of financing. The comparative advantages of multilateral organisations, such as local structures and a long-term ability to act, are cited as reasons for using them for implementation. In addition, multilateral organisations that are active in highly fragile contexts are supported with a higher proportion of voluntary core funding than those that do not work in these contexts. At the same time, the share of earmarked contributions in the BMZ's overall portfolio is increasing, while the share of core funding is decreasing. Last but not least, efficiency aspects play a subordinate role in the design of financing modalities. Less consideration is given to whether efficiency losses result, for example, from rising transaction costs and higher management overheads for the BMZ, the participating multilateral organisations or the partner countries, since the focus is primarily on substantive considerations and target achievement.

Scientific evidence on the effectiveness of core funding and earmarked contributions

The systematic review in evaluation question 5 results in a mixed picture regarding the effectiveness of core funding and earmarked funds; research emphasises the role of core funding for the overall functioning of multilateral organisations. The regular payment of core contributions by donors to multilateral organisations ensures their ability to function, as the core funding represents a reliable basis for financing. However, with trust funds, which fall under earmarked funding, multilateral organisations can respond better to emergency situations, especially in fragile contexts. At the same time, earmarked funding can limit the partner countries' autonomy in general. Comparative analyses at the project level, furthermore, show that projects financed by trust funds are less effective than those financed by core contributions.

In addition, the systematic analysis reveals evidence gaps in process effectiveness at the project level, and in cost and outcome effectiveness at the system level. Relevant questions that have not yet been addressed in scientific research relate, among other things, to process effectiveness at the project level. This applies to both core and earmarked financing. Overall, there is also little robust evidence on how effective core funding and earmarked contributions are in the overall multilateral development system and what possible overarching effects they have beyond individual projects. Cost and outcome effectiveness is usually discussed at the project and organisational level. While this is relevant, it does not provide a complete picture of systemic effects.

Conclusions and recommendations

Use of financing modalities and portfolio design

At the portfolio level, it is not sufficiently clear what strategic role the earmarked portfolio should play vis-à-vis the bilateral portfolio. The BMZ promotes a wide range of topics with its earmarked portfolio, but it is difficult to see thematic priorities that are in line with the strategic priorities. This finding of the portfolio analysis on evaluation question 1 is similar to that of the DEval allocation study on bilateral DC (Wencker, 2022), according to which no thematic concentration is recognisable in the bilateral portfolio. Furthermore, the portfolio similarity analysis shows that the earmarked portfolio neither reinforces nor complements the bilateral portfolio in thematic terms. In order for the earmarked portfolio to fulfil its function as part of multilateral engagement, it is important to specify the relationship between the portfolios and to align allocation decisions accordingly.

Recommendation 1: Define the relationship between the earmarked and the bilateral portfolio

The BMZ should define the strategic role of the earmarked portfolio in relation to the bilateral portfolio.

The BMZ's earmarked contributions are predominantly complementary to the disbursements of multilateral organisations, but they should be geared towards strengthening the latter's mandates and ability to act. The results of the portfolio similarity analysis under evaluation question 2 regarding the coherence of the bilateral and multilateral portfolios show that earmarked contributions, especially in the case of UN organisations, are predominantly complementary in orientation, even in the case of broadly defined priorities at the sector level. This finding is surprising – for not only in terms of the efficiency of the financing modalities used but also in order to strengthen multilateral organisations and their ability to act, it would make sense for the earmarked contributions to consolidate the thematic portfolio of multilateral organisations to further support the comparative advantages and strengths of individual organisations. The focus should therefore be on comparatively broad priorities at the sector level, so that the contributions have a reinforcing effect and an organisation's own aims in development policy, as well as its strategic and institutional objectives, can be brought together in practice in view of possible areas of tension between different target requirements.

Recommendation 2: Gear earmarked contributions more to the thematic portfolio of multilateral organisations

The BMZ should work towards gearing earmarked contributions more closely to the thematic portfolio of multilateral organisations in order to promote a more efficient use of funds in addition to core funding, to strengthen the organisations' ability to act, and to achieve the BMZ's own development goals.

In its portfolio, the BMZ uses different financing modalities, including core funding and earmarked contributions, which fulfil different functions. The portfolio analysis shows that the relative share of core funding to multilateral organisations decreased during the period under review, while at the same time the earmarked contributions increased in both absolute and relative terms.

With regard to earmarked contributions, it should be noted that those that are tightly earmarked are considered problematic due to high transaction costs and the fact that they restrict the ability of multilateral organisations to act. The systematic review, for example, shows that earmarked funding undermines the cost-effectiveness of multilateral organisations' projects. Where earmarking is strict, the financing can only be used flexibly to a limited extent and transaction costs can rise. Reducing transaction costs is key to efficient action; tight earmarking should therefore only be applied in well-founded exceptional cases. In order to be consistent, the BMZ should (further) reduce the amount of tight earmarking and earmark the funds softly for a predetermined purpose. This can make the engagement more efficient.

Recommendation 3: (Further) reduce tight earmarking

The BMZ should work towards further reducing tight earmarking in the multilateral portfolio and earmark contributions softly – where possible – to ensure the multilateral organisations' ability to act and to reduce transaction costs.

Adequate core funding is necessary to ensure that multilateral organisations can fulfil their mandates. Accordingly, the relevance of core funding for multilateral organisations is emphasised in BMZ strategies, and the Ministry lays down strategic targets for this. The portfolio analysis comes to the conclusion that core contributions for certain UN organisations named as priorities in the strategies increased, at least in relative terms, in the study period from 2014 to 2022. The results of the systematic review on evaluation question 5 show that core funding is seen by many multilateral organisations as the most suitable financing modality, whereas bilateral donors view this more critically, as they have less direct influence over the use of funds as a result. Similarly, the systematic review shows that earmarked contributions represent additional resources for multilateral organisations and are therefore attractive for them.

Core funding is necessary to ensure a multilateral development system's ability to act in the long term. Continuous and stable funding is important – for multilateral organisations and especially for UN organisations. In line with the UN Funding Compact, at least 30% of contributions should therefore be made as core contributions to give UN organisations planning security and, at the same time, help strengthen the multilateral system as envisaged (UN, no date). The BMZ should contribute to this within the scope of its possibilities. Conversely, the BMZ can call for more accountability and transparency from the UN organisations in line with the UN Funding Compact.

Recommendation 4: Ensure stable core funding, especially for the UN system

In accordance with the UN Funding Compact, the BMZ should work towards stable core funding for UN organisations; this would contribute to their ability to act and strengthen the multilateral development system.

Interplay

Interlinking bilateral and multilateral DC is a continuous, strategic aspiration on the part of the BMZ (BMZ, 2013a, 2020a, 2023a)**, and its implementation is demanding.** The results of the case study on the interlinking of bilateral and earmarked projects in the core topic area of "Life without Hunger" in Ethiopia indicate a potential for more interplay between projects and show that project staff see added value in this. However, several obstacles stand in the way, despite the willingness of the parties involved. These results lead to the conclusion that relevant administrative and strategic barriers to more interplay within the sphere of influence of German DC should be identified and gradually reduced.

Recommendation 5: Identify and reduce barriers to bi-multi interplay

The BMZ and the implementing organisations GIZ and KfW should work together in a structured manner to identify barriers to interplay and gradually dismantle them.