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Implementing Results-based budgeting in the Ministry of Defense of Peru

Natalie J. Webb

Abstract

Leaders of the Peruvian Ministry of Defense (MINDEF), at the direction of national lawmakers and the Ministry of Economics and Finance (MEF), have begun a process to implement a results-based budget (RBB). A change in national law prompted the current transition from an input (cash)-based, one-year, non-transparent budgeting system with few links between strategy and execution, to a system linking measurable results to corresponding budgets. Current efforts are underway to structure processes and information systems to assist in linking defense expenditures to goals and desired outcomes.

This paper evaluates the Peruvian MINDEF's efforts to implement RBB. We argue that the current processes of planning and budgeting in the MINDEF and military institutions have significant problems in several areas; if MINDEF leaders are unsuccessful in overcoming these obstacles then the benefits normally attributed to implementing RBB may not occur. We examine strategic guidance from the government and the MEF's implementation of RBB in all government organizations, neither of which focus on defense actions and outcomes. We note that no centrally coordinated effort or "champion" exists within the MINDEF to implement RBB, which leads to significant disparities in comprehension, organization, and implementation among the defense institutions. We also observe no consistent method, data collection and information tracking within the MINDEF, and little communication among officials. With continued pressure on national and especially defense budgets, and pressure on the armed forces to show their value, continuing an unsound implementation could have national and international ramifications given the increase in Latin America's security concerns.

Introduction

Leaders of the Peruvian Ministry of Defense (MINDEF), at the direction of national lawmakers and the Ministry of Economics and Finance (MEF), have begun a process to implement a results-based budget (RBB). The change in national law prompted a discussion of transitioning from the current input (cash)-based, one-year, non-transparent budgeting system, which has few links between strategy and execution, to a system that links measurable results to corresponding budgets. The Peruvian government wants 16 ministries to design and implement planning and budgeting systems that link performance indicators and budgets to desired national outcomes. The drive for implementing a RBB in the MINDEF appears to have begun in 2008; however, the intent to implement results-based budgeting focused on national goals and legal requirements, with less attention to or little understanding of how to link defense capabilities and “results” to defense budgets. Current efforts are underway to structure processes and information systems to link defense expenditures to defense goals and capabilities, and desired outcomes.

This paper evaluates the Peruvian MINDEF’s efforts to implement results-based budgeting. We argue that the current processes of planning and budgeting in the MINDEF and military institutions (what we think of as military services in the United States) appear to have significant problems in several areas; if MINDEF leaders are unsuccessful in overcoming these obstacles then the benefits normally attributed to implementing results-based budgeting may not occur in the Peruvian case. First, we find that strategic guidance from the government focuses on social and national goals rather than on the contributions defense can make towards their achievement. Second, the MEF oversees the implementation of budgeting for results in all government organizations, directing the method, terminology, and processes to use and determining whether budgeting for results is appropriate in various organizations. Third, there does not appear to be a centrally coordinated effort or a “champion” within the MINDEF to implement results-based budgeting; this leads to significant disparities in comprehension, organization, and implementation among the defense institutions. Fourth, we observed a distinct lack of communication among MINDEF officials regarding the necessity of having a method and data collection that flows into an information system, which can support resources management and evaluation of defense actions or “results.”

The remainder of the paper is structured as follows. The next section discusses historical, political, and economic circumstances leading to the current legislation for implementing results-based budgeting in the Peruvian government. We then examine the extant, relevant literature on results- or performance-based management and budgeting. In the fourth section, we describe the state of planning and resourcing in the MINDEF and institutions, and current difficulties in linking resources to defense outputs and outcomes. We then provide recommendations for how to proceed with results-based budgeting from existing planning and budget systems and consider the prospects for an effective implementation of results-based budgeting in the MINDEF.

Section 2: Recent historical, political and economic circumstances leading to results-based budgeting in Peru’s Ministry of Defense

The environment for current government implementation of a results-based budgeting system in which the MINDEF operates is largely based upon the evolution of political-military relationships over the past 40 years. In 1968, under General Juan Velasco Alvarado, the

military, led by President Fernando Belaunde Terry, overthrew the elected government and began to nationalize industries, assert authoritarian rule and mismanage the Peruvian economy. In 1980, a more moderate military leader, General Francisco Morales Bermudez, began to restore the country's economy and presided over the May 1980 elections, ushering in a civilian government. President Belaunde Terry returned to office, elected by a large majority. However, economic problems left over from the military regime, along with natural disasters in the early 1980s, resulted in an economic collapse, lowering the living conditions of Peru's poor. Under these conditions, the Sendero Luminoso (Shining Path) and Movimiento Revolucionario Tupac Amaru (MRTA) emerged as terrorist groups, sometimes financed from narcotraffickers who had "established strongholds in the Peruvian Andes and Amazon basin during this period" (U.S. Department of State, 2012). In 1985, Peru elected Alan Garcia Perez as president, marking the first time the presidency passed between civilians for the first time in 40 years. Garcia's inadequate economic management resulted in hyperinflation in the late 1980s. Concerned about the increasing terrorist threat and poor economic conditions, the populace elected Alberto Fujimori as president in 1990.

President Fujimori implemented severe economic reforms and quickly tackled inflation. Facing continuing opposition to his actions for improving the economy, in 1992, Fujimori dissolved the Congress in a "self-coup." Through intimidation, reorganization, bribes and political power, Fujimori successfully introduced a new constitution, and eventually reached agreement with the president of Ecuador on a long-standing border dispute. Over time, Fujimori presided over legal and economic reforms, privatized many state-owned industries, and improved public finances and investment conditions. At the same time, however, his government, particularly under the direction of his security advisor, Vladimiro Montesinos, gave free rein to military and other government actors to brutally suppress the MRTA and Shining Path; this resulted in countless human rights violations by military and terrorist actors. Fujimori ran for a third term in 2000, but in November 2000, resigned amid allegations of bribery and revelations of human rights violations by military (and terrorist) actors. After Fujimori stepped down, the Peruvian transition government created the Truth Commission, later called the "Truth and Reconciliation Commission," to "clarify the process, the facts and the responsibilities of the terrorist violence and the violation of human rights produced since May 1980 and until November 2000, attributable both to the terrorist organizations and to State..." (Decreto Supremo, 2001) (as quoted in Arce, p. 29.)

The actions of military leadership under Fujimori and Montesinos fueled public distrust of the military. Although Montesinos blackmailed military officials to force their compliance, and the Truth and Reconciliation Committee ultimately found him to be responsible for activities resulting in murder, drug trafficking, trade in illegal weapons, graft and embezzlement, the military's acquiescence set the stage for a poor relationship with future civilian administrations. Further provoking distrust between the military and civilian sectors, Peruvian officials revealed that the CIA, the U.S. international intelligence agency, gave Montesinos approximately \$10 million in cash plus sophisticated equipment for the Fujimori government's anti-terrorist

activities. (Paez, 2001)¹ Unfortunately, U.S. officials continued to turn a blind eye to Montesinos' activities until:

In what is surely among the most embarrassing turn in post-Cold War U.S. foreign policy, Montesinos used his CIA-backed position of influence to get rich and to betray his benefactors. He arranged an arms deal that sent at least 10,000 AK-47 assault rifles from Jordan to Colombia's leftist FARC guerrillas, collectively public enemy number one in the U.S. war on drugs in Latin America and the main target of Washington's \$1.3 billion counternarcotics aid package to Colombia (Paez, 2001).

Subsequent revelations increased mistrust as the Truth and Reconciliation Committee revealed a "Subjugation Act," "signed in 1999 by, virtually, all high commanders of the Armed Forces, in which they supported the so-called self-*coup* of 1992 [that resulted in] counter-subversive policy applied by the Armed Forces" (Arce, 2010, p. 28). Although some military officials managed to be absent on the day of the act's signing, the Truth and Reconciliation Committee revealed that most of the senior military leadership was at least aware of, if not complicit in wrongdoing. After release of the committee findings, transitional government officials required the retirement in 2006 of 50 major generals and brigadiers of the Army, 20 vice-admirals and rear-admirals of the Navy, and 14 generals of the Air Force, all of whom signed the document (Arce, 2010, p. 29).²

It is important to note that Peruvian society, while distrusting the military, also reinforced military applications that continued violent interventions:

[P]articularly during the 1980s, Peruvian society came to view the military's power as excessive and had little or no confidence in it due to military coups and human rights abuses committed in the war against Sendero and the MRTA. Nevertheless, civilian society as well as policymakers advocated a violent solution in dealing with these terrorist movements. In other words, while Peruvians came to distrust the military, they preferred no other alternative (sway negotiation or mediation) to end the internal war (Nieto, 2011, p. 524).

From the military regime of 1968-1980 to the "Catch-22"³ situation of the 1980s to today, military leaders are maintaining a strained relationship with civilian and political societies due to lack of civilian control and "the consequences that the process of political violence living

¹ "Over the years, the United States accumulated plenty of evidence of corruption, human rights abuses and other anti-democratic actions by Montesinos, but it shrugged off the reports because Montesinos -- the unofficial head of the National Intelligence Service -- was a CIA asset deemed key to Washington's drug war in the Andes" (Paez, 2001).

² Afterwards, the commanding officers for the three institutions and the Peruvian National Police "apologized to the Peruvian people for the institutional participation of the Armed Forces in the *coup* of 1992" (Arce, 2010, p. 29).

³ Catch-22 refers to a paradoxical situation in which a person or organization is trapped, no matter what they do.

in Peru between 1980 and 2000 [...] which has certainly not concluded in some regions of the country [...]” (Arce, 2010, p. 28). Although democratization of the Peruvian government and society has resulted in many positive changes, the history of mistrust remains. Today’s struggle continues to reflect the movement towards civilian control over the armed forces: “the ability of a democratically elected civilian government to carry out a political policy without interference by the military, to define the goals and general organization of national defense, to formulate and carry out a defense policy, and to supervise the application of military policies” (Aguero, 1995, p. 47). However, balancing a historically strong military against less-powerful government officials can result in unexpected consequences. Jaskowski notes that in Peru, reducing military privileges “can be like squeezing a balloon: it may trigger military contestation in the political arena, such as rebellion, or it could spur military unresponsiveness when it comes to mission performance” (2012, p. 84). The government and military of Peru continue to shift roles as civilians gain ground in controlling the use of the armed forces. Today, civilian administration and defense leaders work towards effective use of the armed forces through government policies, laws, and actions that deal with issues of human rights and military roles and responsibilities, slowly changing the sentiments of either side. This sets the stage for civilian government intent to require results from the military as a condition of receiving funding.

The Peruvian Armed Forces Today

Today, the armed forces play an important role in the country’s development. The most important goals of President Ollanta Humala Tasso’s current government deal with social conditions. Government leaders set national goals largely derived from their effect on the population through development and increased living standards. Military institutions must try to connect their roles and missions to these higher-level goals, often struggling to find appropriate goals for defense actions. Their “mandates” include things such as improving the ability to govern, contributing to economic success, and providing safety and security. Other organizations, however, participate in the achievement of these goals, making it critical for the government to better define military roles.

President Humala appointed the current minister of defense, Luis Alberto Otárola, in December of 2011. Mr. Otárola leads a General Secretariat, Vice Ministry of Administrative and Economic Matters, Vice Ministry of Logistics and Personnel Matters, National Directorate of Politics and Strategy, Joint Command of the Armed Forces, and the Peruvian Navy, Army and Air Force. According to the MINDEF (Peru Ministry of Defense, 2012), Mr. Otárola’s objectives are to:

- Improve the operational capability of the armed forces to maintain control of airspace, land, sea, river and lake, as well as the ability to perform essential response to any threat
- Dismantle terrorist organizations, drug trafficking and other crimes, and to restore conditions of stability and security in the Apurímac and Ene River’s Valley (VRAE)
- Participate actively in economic and social development and civil defense
- Participate in international peace and security
- Strengthening the System of National Security and Defense
- Optimize institutional management
- Institutional Strengthening of the Armed Forces and staff welfare

These very broad goals and objectives summarize much of the government's perception of MINDEF's responsibilities. Typically, however, military institutions play a role in security, stability, and peace operations including fighting drug trafficking, providing maritime security and enforcing border control. With Peru now ranking as the world's second largest producer of coca leaf (Central Intelligence Agency, 2012), its government receives considerable pressure from both internal and external individuals and organizations to thwart narco-terrorism. The biggest military role is providing responses to the narco-terrorism threat in defense of the Amazon region, which includes portions of eight countries and covers nearly half the territory of Peru (Onnig, 2011, p. 59). Peru's military institutions participate in joint operations to combat illegal drug activities, and are of great importance to Peru's allies in the United States and Europe. "The United Nations Office on Drugs and Crime UNODOC suggests that Colombia, Peru and Bolivia produce practically all the drugs that supply European and U.S. markets" (Onnig, 2011, p. 66).

The successful battle to eradicate MRTA and the current battle to eliminate the Sendero Luminoso define narco-terrorism operations mainly in the Amazon region. Current operations continue in the VRAE area (Apurimac and Ene River's Valley) of the Amazon, but the geography of the region gives the approximately 200⁴ remaining active *senderistas* many places to conceal themselves (Nieto, 2011).⁵ Military institutions continue to provide capabilities to combat terrorism, to control Peru's land, water and air borders, to help maintain security and stability, and to contribute to civil defense and international security operations.

Increasingly Peru's military institutions take on greater, less defined roles and responsibilities. President Humala recently assigned the military greater responsibility for maintaining public order and safety. "They will now also be expected to crack down on illegal mining and to intervene in social protests" (Paez, Global Information Network, 2011).⁶ Given broader responsibilities, MINDEF planners have their work cut out for them in explaining how military institutions contribute – measured as "results" – to national goals and objectives for social development.

Economic situation affecting budget reform and military spending in Peru

In recent times, Peru has seen stable and growing economic conditions. From the 1980s, the growth of violence and insurgency negatively affected the economy, but beginning with the Fujimori administration in 1990, market-oriented economic policies have provided "robust macroeconomic performance" (Central Intelligence Agency, 2012). Peru's main sources of external revenue come from its important mineral and petroleum resources. Its economy reflects its varied geography that includes coastal, mountainous, and tropical regions. GDP has grown at an average rate of 6.4% per year since 2002, and grew at almost 9% in 2010 and 7% in 2011

⁴ Workshop participants from military institutions suggest that this number may be closer to 300.

⁵ Senderos survived the end of the Cold War and the fall of the Soviet Union, and remains today as a narco-terrorist movement (Nieto, 2011, p. 518).

⁶ Chile and Ecuador rejected Peru's November 2005 unilateral legislation to shift the axis of their joint treaty-defined maritime boundaries along the parallels of latitude to equidistance lines which favor Peru; organized illegal narcotics operations in Colombia have penetrated Peru's shared border; Peru rejects Bolivia's claim to restore maritime access through a sovereign corridor through Chile along the Peruvian border

with little fluctuation in the exchange rate and low inflation (Central Intelligence Agency, 2012). Private investment has fueled growth, particularly in extraction industries, but infrastructure development remains poor, hampering the spread of growth to areas away from Peru's coast. The national poverty rate has fallen by 23% since 2002, to just over 31% (Central Intelligence Agency, 2012). Peru's administration continues to pursue free-trade policies, attracting foreign investors and providing for stable government revenues. However, political disputes and social protests may affect the country's ability to grow at a steady rate.

Due to Peru's economic situation, defense funding has remained reasonably stable, and the military has been able to update its military equipment. The MINDEF budget has been below 2% of GDP since 1999, and closer to 1.3% in the last few years (Stockholm International Peace Research Institute, 2012). Equipment procurement funds come mostly from the Defence and National Security Fund, established in 2004 and passed into law in 2005. This fund collects royalties from extraction operations. Under this law, the Camisea gas project (one of the largest energy projects in Peru and of great importance to the Peruvian economy) provides 12.5% of its income to this fund. Additionally, China, Russia and Israel supply much of Peru's military equipment: Peru recently purchased MBT-2000 tanks from China (Jane's Information Group, 2012).

Government leaders show concern with the crowding-out effect military expenditures have on the private sector. Klein (2004) found a negative net effect of defense expenditure on economic growth in Peru; Klein found the direct effect, or externalities of military activities on the civil sector of the economy, to be insignificant at any conventional spending level. However, the indirect or crowding-out effect was "quite substantial" (Klein, 2004, p. 286).

Whether due to crowding out concerns or pursuit of other goals, Peruvian government leaders continue to limit military expenditures. In fact, in recent years, Peruvian military spending has been the lowest of the South American states covered by Jane's Defence Budgets (Argentina, Bolivia, Brazil, Chile, Colombia, Ecuador, Falkland Islands, French Guiana, Guyana, Paraguay, Peru, Suriname, Uruguay and Venezuela). Jane's analysis suggests that this position reflects the Peruvian government's low priority assigned to defense and the existence of competing government social and development priorities. The analysis also projects that defense budgets will rise based only upon economic growth (Jane's Information Group, 2012).

In sum, a history of mistrust, shifting national priorities (with accompanying shifts of resources away from defense), changing roles and responsibilities of the military, and current law set the stage for understanding planning and RBB in the Peruvian Ministry of Defense. We now turn to a discussion of the scholarly literature on RBB.

Section 3: Relevant literature on results-based management and budgeting

Given its efforts to institute processes for tracking results from or the performance of publicly funded projects, Peru's leadership is similar to many other countries. As is the case with most countries, limited resources and public demands for accountability require leaders to tackle efficiency, effectiveness, and transparency. Efforts to build the RBB system stem from at least two initiatives. The first is to control better the allocation of resources from top levels of government through top levels of defense to sub-organizations within defense, and the second is

to improve managerial information to better direct resources and efforts within defense and institutions.

Of critical importance to the success of performance- or results-based budgeting⁷ is how governments manage. Schick (2008, p. 18) notes that governments budget the way they manage, so it is typically necessary to change management practices to reform the budget process. He confirms the relationship of governance, management, and budgeting in the following:

Confirmation of the interdependence of governance, management and budgeting comes from the fact that countries that have made most headway in performance-based budgeting have been among the best managed in the world. They are reputed to have low corruption, efficient public administration, effective accountability arrangements, political and administrative channels for citizens to express preferences and grievances, and procedures for monitoring the quality of public services. An incomplete list of these countries would include New Zealand and Australia in the Pacific region, Sweden and the Netherlands in Europe, Singapore in Asia and Chile in Latin America (Schick A. , 2008, p. 19).

Modern results – or performance-based management and budgeting practices stem from the paradigm of New Public Management (NPM), in which government actors focus on finding ways to get things done more efficiently and effectively.⁸ NPM illustrates a management culture centered on the citizen or customer, and accountability for results. In the 1980s, Latin American countries began reforming, adapting models and concepts from NPM and the experiences of more-developed countries (López, 2011, p. 249). Today, they continue to work towards changing the focus from public administration to public management, striving to integrate governance, management, and budgeting processes within their organizations.

NPM suggests an approach called “managing for results,” (MfR), which “takes on characteristics specific to the state, like the processes for decision-making and accountability in a democratic regime and the public interest as a focus for management” (López, 2011, p. 250). In the Peruvian context, this approach follows Moynihan’s principal of results-based management, using performance information to improve results by setting goals and holding managers accountable for them (2006, p. 78). Countries like Peru use an approach that measures economic and social development or “managing for development results” (MfDR). In these developing countries, government actors concentrate on improving public value or effecting social change through government goals, expenditures, and actions. The results of importance to the administration are general social outcomes rather than products or outputs that contribute to social change. MfDR requires managers and institutions to “assume responsibility for achieving results and not simply for the completion of processes” (López, 2011, p. 251).

Studies of managerialism (see Kioko, for example (2011)) suggest that organizations change to flexible network settings, transforming from traditional, bureaucratic hierarchies; focus on outcomes, rather than structure and process; and use market-based competition, rather than the authority of command and control, to make better decisions in resource allocation. While

⁷ Although not always used interchangeably, “results-based” and “performance-based” are used interchangeably in this article.

⁸ See, for example, Christopher Pollitt and Geert Bouckaert (Pollitt, 2011).

MfDR and managerialism approaches have good intentions, they do not confront some realities of modern public budgeting and management, especially in defense organizations. Military organizations generally require hierarchical organization due to the specific nature of their operations, and authoritative decisions about defense require a hierarchical process to maintain civilian control of military forces. Parts of defense, such as some procurement practices, can be more efficient and effective under market-like conditions; managers certainly concern themselves with outcomes and results, but many managers cannot neatly transition defense decisions and actions into those they base on the market and results. Next, we discuss the challenges to achieving more ideal forms of management practices.

Havens (1983) notes that, in practice, managers who try to integrate information on performance or results into the budget process face at least three difficulties. First those who evaluate performance tend to be in other parts of the organization than those who allocate resources. Second, budget and evaluation processes operate on different time schedules and events (budgeters respond to calendar deadlines, while evaluators often operate relative to events that happen at different times (Havens, 1983). Third, budgeters and evaluators use different analytical frameworks for evaluation (Havens, 1983).

When budgeters and those who plan for and evaluate performance work in different parts of an organization and on different timetables, the linkage between funding and results is broken. Robinson (2007, p. 1) notes that budgeting is the financial component of results-based management, where budgeters and managers design financial processes to strengthen this linkage. Measuring results requires understanding not only the funding of particular expenses, but the links from funding to outcomes:

[Figure 1 here]

Thus, to budget for results with separate groups of individuals responsible for either end of this spectrum requires an information system linking funding to results by tracking inputs, activities, outputs, and the outcomes from which they are generated. Even the most developed of countries has not managed to find a system that can do this without making leaps from outputs to outcomes, and often generalize about the inputs required to produce an output. As Havens (1983) and Heinrich (2004) note, integrating information on results requires linking outputs to the outcomes or the achievement of results. Managers and leaders do not want to be accountable for results because causal relationship between outputs and outcomes can be ambiguous, other things in the environment besides outputs affect outcomes, and there may be a lag between producing an output and experiencing an outcome.

Joyce (2003) suggests the term “performance budgeting” be described as “performance-informed budgeting,” which he says is more practical because the politics of budgeting will not allow a “formulaic” approach to replace discussions and decision making accompanying budget decisions. This argument further supports the notion that RBB cannot be put into practice without adjustments in the way it is used – the “simple” logic of tying budgets to results is fraught with difficulties. For example, Joyce (2011) notes that most RBB systems measure agency or program output or activity, revealing what the organization does rather than what it buys; or if the agency knows what it buys, then it cannot connect expenditures to actual costs (a limitation of many accounting systems) much less results. Further, he notes that systems such as

the proposed RBB for Peru may exhibit a bias towards programs with measurable results rather than programs with results that are more difficult to quantify, and bias towards programs that show short-term results rather than those that take longer to show.

Perhaps the most successful country to date in terms of progress in implementing performance management and budgeting is New Zealand, whose government adopted “output-budgeting.” In the New Zealand case, ministers and “chief executives” enter into contracts based on the production of outputs rather than outcomes because many variables beyond the control of either party affect outcomes. As an example, the police commissioner contracts with the minister of police to provide a certain level of policing services, patrols, community security programs, road safety commercials, etc. The commissioner does not contract to lower the crime rate because many variables beyond the control of the commissioner affect the rate (OECD, p. 139). Conditional on this approach, of course, is the ability to tie funding to outputs. In developing countries, Schick (1998) cites the dangers of replicating the New Zealand approach in countries that still have to build up the basics of a budget system and other essential pre-conditions.

In Peru and other developing countries, classifying expenditures relative to the output or activity for which they were made remains difficult. Before moving to a RBB system, budgeters and evaluators need to classify expenditures in a framework so that they can formulate policy, measure the allocation of resources among organizations, review performance (or at least production of outputs), and provide accountability. Without such a system, managers, leaders and political figures cannot participate in meaningful decision-making processes because goals and results, activities, and expenditures cannot reflect the trade-offs that need to be made at each level of the organization. Further, Lu (1998) notes that one of the key factors in the success of implementing performance budgeting is the quality of measures and acceptance of them by decision makers. Without setting up a system based on classifying expenditures, activities, and outputs, neither budgeters nor evaluators can agree on the allocation of resources and the difficult trade-offs that they must make to meet higher-level goals.

Another issue of importance to the Peruvian case is incentives. Grizzle (1987) suggests that incentives for managers and budgeters must be constructed so that they align well with the use of performance information. As noted above, individuals and institutions do not want to be held accountable for results with elements outside their control. And as Schick (2008, p. 8) notes, the “agency problem is especially acute on matters of performance, because adverse results can prejudice an entity’s budget.” Governments implementing RBB must structure processes and requirements so managers and leaders have motivation to participate fully in implementing the system.

Finally, of consequence to RBB in Peru, Carranza (2011) notes that for a reform to be successful, it must meet five conditions. Of particular importance for RBB in Peru are: (1) to have a leader; (2) have backing from an administration willing to bear the political cost; and (3) have a good technical team to design it, take on legal issues, and avoid issues in operational aspects of implementation. We return to these conditions in the sections that follow.

In the next section, we describe the planning and budgeting systems in place in today’s Peruvian armed forces.

Section 4: Results-based budgeting in Peruvian Defense

As noted in the introduction, leaders of the Peruvian MINDEF are currently responding to the government's directive to implement a RBB. Peruvian MINDEF and armed forces officials seek to design and implement a planning and budgeting system that links budgets to desired results.

In May of 2011, officials from the United States and Peru met to discuss the issues and challenges facing the MINDEF and institutions in creating and integrating a process within which defense organizations can link goals to programs and budgets.⁹ Prior to this meeting, Peru's stated objectives were to improve the quality of defense spending by strengthening the relationship between the budget and outcomes by establishing performance indicators, and monitoring and evaluating the defense sector performance through information generated from performance indicators for more effective and efficient allocation of public resources. A longer-term goal was to design and implement a results-focused management system in defense. Yet to discuss these goals with any clarity, transparency and accountability must be in place; this is of great concern not only to civilian and political societies in Peru, but also of concern to military officials charged with explaining costs and effectiveness of military units, systems and actions.

In the sections that follow, we discuss the state of planning and budgeting in the MINDEF, focusing on four aspects of RBB in Peru: (1) strategic planning and goal setting; (2) budget planning; (3) MINDEF coordination and leadership efforts relative to RBB; and (4) method, data collection and information systems, and the communication relative to these in the MINDEF and institutions. In each case, we present positive steps taken and possible pitfalls in the implementation of RBB in Peruvian defense.

Strategic planning and goal setting

Strategic planning and goal setting in Peruvian defense result from a number of factors: the national government's focus on social goals; the legal and operational framework for implementing RBB through the MEF; the planning roles of the institutions, Joint Command, and civilian leadership in the MINDEF; and planning processes already underway in each institution and the Joint Command.

Figure 2 illustrates the strategic planning process in the MINDEF.

[Figure 2 here]

Through an initiative called the social macroeconomic framework, Peru's government focuses on MfDR goals of improving the social and economic conditions of Peru's citizens by defining sectoral goals. Given the administration's focus, it is not surprising that the strategic guidance to the MINDEF focuses on social and national goals rather than the contributions defense can make towards their achievement. The MEF guides the MINDEF, and MEF managers work with MINDEF budget staff to agree on "products" and "results" the military must achieve to comply with the RBB law. Further, the MEF makes funding contingent on showing results related to the higher-level goals.

⁹ The author has led the effort in four workshops in Lima since May 2011.

MINDEF budgeters find themselves caught in a difficult position between the MEF and military strategic planners. Currently, the budgeters set the “official” defense goals, products, measures of results, and links to the defense budget, while leaders in the Joint Command and each of the military institutions set goals and objectives they believe will contribute appropriately to higher-level social outcomes and to maintaining security and stability in the country. Budgeters have made great efforts to try and link their goals and measures to those of the Joint Command and institutions, but their focus is on providing information to the MEF in a format that the MEF approves. This takes the critical lead in strategic planning away from defense planners and puts it into the hands of budget planners. Rather than measuring what defense *can* do, the process measures abstract concepts of “results” (like “governability”), avoiding the difficult process of linking funding to inputs to activities to outputs and *then* to results, something that we noted (above) that no country in the world has been successful in doing, even if the country had a sophisticated accounting and management system.

Military managers, at least in some parts of defense, work well with MINDEF budgeters in trying to agree on what they can measure and what measures serve as the best proxies for the results that defense achieves. The Chief of the Joint Command reports directly to the Minister, and works with the institutions to determine current and future capability requirements. Similar to processes used in many countries, the Joint Command and at least two of the institutions (the Navy and the Air Force) have begun using a capabilities-based assessment process to define critical capabilities and doctrine, organization, training, materiel, leadership and education, personnel and facilities (DOTMLPF) that they need to achieve military objectives. These assessments provide tasks to be reviewed by institution and Joint Command leaders, a list of capability gaps and suggested solutions for DOTMLPF issues. It appears that MINDEF leaders are beginning to concentrate planning through the Joint Command. However, the institutions receive funding directly from the ministry, and administer at least some military planning and all spending at the institution level. This may result in goals and capabilities planning that conflicts with joint planning goals and capability needs.

Approaches to goal setting in RBB vary in the Joint Command and institutions. For example, Peruvian Navy leaders have made significant progress in detailing the capabilities the Navy needs and where gaps in capabilities lie. These processes work towards connecting desired outcomes with military capabilities needed to provide the outputs (missions, flight hours, steaming hours, etc.) that can result in the desired outcomes. At the institution level, we see good work on attempting to fit defense into national goals and objectives, positive effort in developing indicators with which to measure success, and a growing cohesiveness in terms of willingness to share information on processes, capabilities determination, common goals and objectives, and how to translate national guidance from the MEF to defense action. At this point in the development of their systems, however, institutional managers have come to little agreement on nomenclature and appropriate measures of efficiency and effectiveness. These managers understand, in theory, that goals must connect from the top down through the institutions, and that a process in which goals cascade through a hierarchy-like structure to guide measurable targets at different levels throughout the organization, but there is no common process to tie results to higher-level goals. Furthermore, each institution fails to connect to the MINDEF’s planning, programming and budgeting system, preferring to develop its own (understandable, and related to its budget) RBB system.

In sum, much of the difficulty in moving towards one RBB system in defense stems from the misalignment of strategic planning as suggested in Figure 2. Joint Command and institution leaders cannot help but structure their own strategic plans in the hopes of achieving more reasonable military outcomes. They know that achievement of strategic goals and desired results or outcomes are not directly measurable, thus they measure their “results” by proxy using outputs (e.g., how many flight hours on patrol) or capabilities (mission readiness). Just as in the case of the New Zealand police commissioner, defense leaders feel they can only be responsible for providing outputs or capabilities within their control. Currently MINDEF and MEF managers are negotiating acceptable measures of results with MEF managers focused on outcomes and MINDEF leaders on capabilities and outputs. However, as one workshop participant (in a discussion between U.S. and Peruvian officials in April 2012) noted, the particularly “inconvenient” process in which the budget and finance people generate MINDEF goals and results means the budgeting-for-results focus, and the corresponding results required, are driven by who holds the money (MEF) rather than the desired outcomes and goals of government activity.

The budget takes precedence over planning

As noted above, the MEF oversees the implementation of budgeting for results in all government organizations, directing them on the method, terminology, and processes to use, whether they apply appropriately in various organizations. The case in Peru follows Schick’s (2005) logic that in some countries, the budget takes precedence over the plan (and in others, the plan over the budget). Lopez (2011, p. 256) notes that Latin American governments continue to work to strengthen their planning capacity, but that a lack of coordination and integration between planning and budgeting limits the success of budgeting for results, and is one of the greatest challenges for MfDR. Given the roles of the MEF and MINDEF budgeters on the one side and Joint Command and institutions on the other, it is not surprising that the MINDEF has not established one budgeting system tied to results for all of defense.

During the annual budget process, lack of coordination between the MEF budgets and ministry plans comes to light, sometimes resulting in conflicts between the spending ministries and the MEF (Filc, 2010, p. 69). We observed that Peruvian MINDEF financial officials well understand the logic of Figure 1, and that budget categories must map to plans through “programs” or some sort of products to facilitate tracing budget expenditures to specific defense activities or outputs. These officials use a program structure for resources management purposes. They define a program as “a basic unit of management and control of results or a set of activities needed, providing integrated and articulated products (goods and / or services) designed to achieve a specific result in a target population and that in this way solves the problem that gave rise to the same.”¹⁰ However, the evolving budget program structure follows the MEF logic rather than linking directly to defense capabilities, activities, and outputs. On its current track, the MINDEF budget will not link to defense outputs, and will likely increase conflict between MEF and MINDEF budgeters and Joint Command and institution leaders.

Contributing to the RBB disconnect between planners and budgeters is the fact that Peru does not have a comprehensive and consolidated medium-term budgeting system (Filc, 2010, p.

¹⁰ From presentation Planeamiento y Ppto Publico DIRI PERU, workshop briefing.

67). In 2000, the Fiscal Responsibility and Transparency Law, which Peru enacted to increase transparency and to frame the budget within the economic policy of the government, drove leaders to develop the Medium-Term Macroeconomic Framework (MTMF) that uses a revolving time horizon of three years (Filc, 2010, p. 61). Prepared by a sub-organization within the MEF, the MTMF serves to link expenditures and debt with fiscal rules. This sub-organization uses historical budgeting of total expenditures plus a given additional percentage to plan to project expenditures and debt. This implies that Peru's budget method has incremental characteristics but also provides baseline expenditure numbers for MINDEF planning. While the MEF has technical advantages to forecast and transfer funding, which enables continuity in funding, it also cannot react to unexpected circumstances such as demands on military forces in the case of a large terrorist attack. If MEF officials continue to have disproportionate control of spending decisions from their offices in Lima, they may undermine defense planning and severely limit the MINDEF from responding independently and flexibly rather than in lock-step with national budgeting processes. (For an analysis of a more advanced RBB process in Peru, see Acosta (2011)¹¹.)

Since MINDEF establishes its goals in plans within defense, while the MEF determines the allocation of resources, the likelihood of implementing a successful RBB system is small. Unfortunately, ministries have the incentive to “wait out” the mandate, and the government may experience noncompliance with established goals. The Peruvian government could address such noncompliance if it strengthens the fiscal framework using a multi-year expenditure plan and establishes a better flow of information by linking budgets, expenditures, inputs, activities, and outputs through some sort of planning, programming, and budgeting system.

In summary, the money holder rather than the desired outcomes and goals of government activity and a comprehensive system to measure efficiency and effectiveness, drives the Peruvian government's budgeting for results. The Peruvian MINDEF and institutions have not implemented a resources management system that has the capability to link strategic goals and desired outcomes with budgets, expenditures, or costs, and the current RBB initiative is unlikely to result in such a system without substantial changes in the process.

No centrally coordinated effort or “champion”

There does not appear to be a centrally coordinated effort or a “champion” to implement RBB in Peru and inside the MINDEF; this leads to significant disparities in comprehension, organization, and implementation among both high-level MINDEF personnel and the subordinate commands in the MINDEF. As noted in section 3, there can be little possibility for transformation without leadership backing the change effort. In the Peruvian MINDEF, no leader has emerged to back the process; at both MINDEF and higher levels, it is not yet clear that administrations are willing to bear the political cost of instituting such a system, particularly as it will likely take decades to implement.

¹¹ In 2006, a pilot was begun of RBB in five sectors (among the programs included in this initiative are those focused on nutrition, maternal neonatal health care, and student achievement). These programs, which are considered strategic, are evaluated on a quarterly basis in terms of their achievement of physical goals and results. The nutrition study by Acosta (2011) presents findings supporting performance- or results-informed budgeting.

Lopez (2011, p. 262) notes that “in implementing a RBB, two complementary fronts must be addressed: the political-institutional aspect and the development of technical instruments. These are actually two sides of the same coin.” He states that while change requires political leadership, organizations also need leaders with technical abilities that facilitate the transformation process. (He also notes that technical leadership can be in either budget or planning sections, but that the best reform outcomes occur when both sections participate in concert with one another.) We note that some of the technical expertise to implement RBB exists in the working group we observed; however, as of yet, that group has no clear leader supporting and defending the group in operationalizing a system linking outputs or capabilities to budgets, and then defending a proper method and measures to the MEF and administration.

Lack of communication on method, data collection, and information systems for RBB

In the above sections, we detailed progress and discussed problems in strategic planning, goal setting, budget planning, a lack of connections among the three, and the absence of a defense “champion” in steering the development of the RBB system. Given these issues, we are not surprised to see a distinct deficiency of communication among the MINDEF officials regarding both the necessity of a RBB and especially the process by which it should move forward. Considering that the MINDEF and each institution uses its own method to try linking planning and RBB, and given that each institution has its own framework of rules that they interpret from the law and MEF guidance, we find separate processes for developing identifying indicators, systems, and etymologic terms. Most likely MINDEF leaders neither have a clear understanding of the various methods for planning and budgeting, nor an agreement on the best way to move forward with an RBB implementation method, to include setting up data collection and information systems needed for its support.

Leaders have not yet examined possibilities for feeding information from the institutions’ planning systems into a larger resources management system that the MINDEF budgeters administer. Similarly, they have not reached an agreement on a method for data collection and reporting using processes with standardized terminology, which would connect the resources management information system with the budgets. Leaders have not made this connection because it would require the (at least partial) resolution of the planning conundrum listed above; until the MINDEF can put forward a clear method to show “results,” leaders can make little genuine progress in terms of methodology. Without a method and data collection, reliable information will not be available, and evaluations and results will not be valid. As noted above, one of the key factors for the success RBB implementation is the quality of measures and acceptance of them by decision makers. Without starting at the beginning by setting up a system based on classifying expenditures, activities, and outputs, neither budgeters nor evaluators can agree on the allocation of resources and the difficult trade-offs that must be made to meet higher-level goals.

At the institutional level, managers have data on expenditures, but it is not clear that they have accounting systems in place to match resources to capabilities. Navy programmers are writing software to manage their capabilities-based planning system, and have begun to analyze resources needed by capability. They are writing their own software to connect to the MINDEF budget. Perhaps managers could exploit this methodology and use it to guide a defense-wide resources management system connecting goals to capabilities to funding. Without information

system that connects capabilities or products with resources allocated defense-wide, defense has a low level of transparency with the government and the public, and reduced bargaining power to obtain resources needed to meet defense goals.

We argue that these issues hinder MINDEF's implementation of results-based budgeting and detract from the possible gains associated with better management of resources through a multi-year, programmatic allocation of defense resources.

Section 5: Recommendations and prospects for success for RBB in Peruvian Defense

In this paper, we analyzed the current progress of and barriers to successful implementation of results-based budgeting in the Ministry of Defense of Peru. We next highlight some of the steps MINDEF leaders must take if they are to see positive progress from the current reform.

The most critical step MINDEF leaders must take is to work with the MEF and other government administrators to build trust and to work towards effective and efficient use of the armed forces. MINDEF leaders should initiate a process of open communication among MEF leaders, MINDEF top-level budgeters, Joint Command leaders and heads of the institutions on constructing common and applicable goals for defense.

Before MINDEF can make any progress, its leaders must convince MEF and other administrators to focus on defense goals and the responsibilities defense has in providing services to the national government and population. Rather than continuing to discuss nebulous "results," such as "governance" or other national-social goals, defense leaders must convince the MEF and others that they know best how to measure the "results" of defense roles and missions. As Lopez (2011, p. 257) notes, in RBB "results include not only the final impact of programs but also all contributions made at any point along the chain of public value generation." Thus, MINDEF leaders require guidance on roles and missions that the administration believes are most important and agreement on capabilities needed so they can (1) begin to make contributions to higher-level goals through agreed-upon defense goals, (2) construct appropriate measures for effectiveness, and (3) cost out defense activities. This requires administration, MEF, and MINDEF officials to shift to "results-informed budgeting" (RIB) as the MINDEF does not have the planning or accounting systems needed to track expenditures through to outputs, let alone outcomes or results. The MINDEF has yet to persuade the MEF that capabilities and outputs best measure defense results unless they use forces in battle or in other actual operations; thus it necessitates agreement on the best proxy measures for effectiveness. Finally, it requires the MEF and MINDEF to change their focus from RBB to building up the basics of a budget system and other essential processes and infrastructures to allow budgeters and planners to track useful performance and cost information.

If successful in reorienting goal planning towards appropriate defense activity and RIB, MINDEF leaders should name a top-level executive to run the RIB implementation process. The executive must have the authority to compel budgeters and institution leaders to align strategic goals with those of the Joint Command. The MINDEF should change the flow of information and chain of authority for strategic planning, resourcing, and execution. Specifically, high-level strategic planners (not budget planners) and the Joint Command should be responsible for

planning capabilities needed (within reasonable resource expectations) to address and prioritize MINDEF goals and objectives. The vice minister of resources should then respond to the capability priorities planned and direct the Joint Command to provide the capabilities for those that they can resource. Budget/finance groups must structure the budget in a way that links capabilities-based plans to the budget, using a program or budget structure¹² based on capability provision, not on national goals. The executive must also structure processes and requirements so that managers and leaders are motivated to participate fully in implementing the system. This will be no easy feat, as transparency in the use and cost of military assets will bring the realization that resources may shift among the players.

We suggest pursuing the Navy's lead in developing an information system that links "capabilities" through "programs" (forces, units, systems) to the resources they need – manpower, O&M, procurement, etc. Navy planners focus on results based on capabilities provided. This mirrors many militaries in that readiness measures proxy for results measures. Unless the Navy uses defense assets in combat, it can only measure their effectiveness by their ability ("readiness") to provide desired services. Even when the Navy uses the assets in combat, it can be difficult to generalize their "results" and "costs" to other situations. Thus, RIB would help the MINDEF think differently about "war zone" budgeting and results when in a situation like VRAE, for example, as these situations require different types of planning, operations, and resources allocation.

As much as is feasible, MINDEF budget planners should adopt a medium-term outlook for the MINDEF. The RIB executive should direct the budget division to strengthen the defense fiscal framework by using a multi-year programming and expenditure plan. This should be a relational database that records multi-year programming and "rolls" by year. Such a system would establish a better flow of information by linking proposed budgets and expenditures to inputs, activities, and outputs. If aligned properly with desired capabilities, this system could help the MINDEF make trade-off decisions in the use of resources.

We noted frustration among some workshop participants about the pace of progress in budgeting for results. Once MINDEF and MEF leaders agree on defense goals and results, the MINDEF executive and an advisory team should plan an implementation strategy for RIB. Although moving cautiously, perhaps via instituting a pilot program with the Navy, may provide a more sustainable process, it is important to take advantage of momentum when political and leadership conditions allow for faster progress.

Thus, the next steps for the MINDEF of Peru are first, to commit to adequately integrating plans and budget, even though this might result in a change in power and shifting of resources. Second, top officials must promise sustained political and technical leadership to

¹² While a properly constructed program structure would facilitate moving forward, Lopez suggests that program budgeting is not a prerequisite to proceed with a RBB. He states that it is possible to transition directly from a budget based on expense classification to a RBB, but countries that have program budgeting can change over more quickly (López, 2011, p. 263). Some countries have adopted program budgeting as an intermediate step; this more gradual process may be justified in Peru.

move forward the process of change.¹³ Third, appropriate high-level executives must design rigorous but flexible processes and develop information systems that support decision making. These must include standardized terms, classifications of expenditure data, and appropriate indicators to monitor and evaluate “results.” Finally, leaders must communicate the importance and commitment to the RIB system and provide training on the processes and information systems. These four steps will help ensure some success in RIB by motivating personnel to participate, allowing budgeters and planners to collect high-quality, relevant data and produce useful performance information, and by moving the MINDEF to a new level of planning-to-budgeting.

Summary

In this paper, we discussed the historical, political and economic aspects of Peru leading to current budget reform to budget by results. We found that budgeters in the MINDEF take strategic guidance from the MEF and administration and focus on social and national goals rather than on the contributions defense can make towards their achievement. This has led to implementation of “results” with a method, terminology, and processes not well suited to defense. At present, no leader within the MINDEF is proactive in implementing RBB, which has led to miscommunication and significant inconsistencies in comprehension, organization, and implementation among the defense institutions. With continued pressure on national and especially defense budgets, and pressure on the armed forces to show their value, continuing a flawed implementation could have national and international ramifications given the increase in security concerns in Latin America.

¹³ Ideally, technical leadership will come from both budget and planning areas. The workshop group can provide some of the most skilled individuals in both areas to advise higher-level MINDEF leaders.

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Funds ⇔ Inputs ⇔ Activities ⇔ Outputs ⇔ Outcomes or Results

Figure 1: Linkages from budgets to results

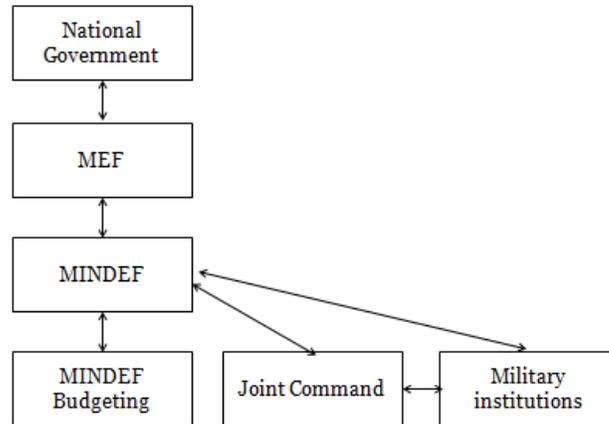


Figure 2: Strategic planning and goal setting in the MINDEF