drawn up action plans to strengthen budget systems. These action plans are being implemented in the context of the countries' World Bank- and IMF-supported programs. Despite recent progress, PEM systems remain deficient in many of these countries, and rigorous implementation of these action plans will be essential for achieving sustainable development.

Increasing the transparency of government operations will be essential to ensure that governments are accountable for their use of public funds. In this regard, transparency can be enhanced if governments adhere to the IMF's Code of Good Practices on Fiscal Transparency. The participation of governments in reports on the observance of standards and codes (ROSCs)—which assess a government's practices on transparency against this benchmark—can provide a useful step in this regard. Thus far, 36 developed and developing countries have participated in fiscal ROSCs, with another 15–20 per year expected in the near future.

Moving Forward

There are many economic, social, and environmental challenges along the path to sustainable development, and there is no panacea to address them all. Rather, accelerated development will require progress in multiple policy areas, with the right policy mix and focus varying from country to country. Countries may also need to make difficult choices regarding trade-offs between competing policy objectives. Achieving more sustainable development will thus require a concerted effort from developing countries, the international community, and the international financial institutions.

Developing Countries

Sound fiscal and macroeconomic policies are essential. Sustainable growth and poverty reduction are possible only with prudent macroeconomic and, in particular, fiscal policies.

Tax and expenditure policies should also be designed to minimize adverse incentive effects, which can hinder economic growth. Tax policies should seek to raise revenue in a way that least distorts labor supply, consumption, saving, and other decisions. Expenditure policies should not deter the active participation of the poor in the labor market and the process of economic development.

Higher spending on poverty reduction is not sufficient to achieve better social outcomes. Increased spending must be accompanied by steps to strengthen the efficiency and targeting of these outlays. There is significant scope to make existing spending more effective in fostering development by reallocating it to inputs that are most needed, such as textbooks and medicines. There is also scope to increase the share of outlays that most directly benefit the poor, such as those for primary education and preventive health care. To ensure that economic reforms do not hurt the poor, countries will need to integrate PSIA into their policymaking processes with a view to both modifying the design of their economic policies and implementing well-targeted social safety nets.

Fiscal policies must also provide appropriate incentives for the efficient and sustainable use of natural resources. Harmful subsidies and inappropriate tax policies that lead to the excessive exploitation of natural resources should be phased out. The prices of energy products should reflect their social costs, and subsidies for pesticide and fertilizer use—which contribute to overfarming of land—should be eliminated and replaced with government expenditure programs that more directly benefit small farmers. At the same time, industrial countries should implement similar policies to ensure that the world's environmental resources are not overexploited.

A strengthening of governance and public expenditure management systems is also needed. Countries need to move ahead to address their most serious deficiencies in public expenditure management; HIPCs, in particular, must work together with the international community to help implement their action plans to improve their capacity to track poverty-reducing spending. For many countries, a useful step toward strengthening transparency would be to adopt the IMF's Code of Good Practices on Fiscal Transparency.

It will also be necessary for countries to monitor the actual delivery and impact of poverty-reducing programs on human and natural resource development. Within the context of the PRSP process or other country-owned poverty strategies, countries should continue to monitor the impact of poverty-reducing spending on social indicators that measure human development. Improved and more detailed data on social indicators, combined with more disaggregated data on poverty-reducing spending by program, will facilitate a more solid understanding of the relationship between government spending and social outcomes. In this regard, improvements in

PEM systems—and the concomitant ability to track poverty-reducing spending—will also improve understanding of the complex link between government spending and sustainable development. There are welcome signs that PRSPs are increasingly reflecting recognition of the role that proper use of natural resources can play in reducing poverty.

International Community

Freer access to industrial country markets and greater and more predictable aid are needed to support sustainable development (included under Goal 8 of the MDGs). Countries in the developed world need to support more robust world economic growth by opening their markets to exports from the developing world. As IMF Managing Director Horst Köhler has stated, "we need to work first and foremost on trade . . . this requires greater ambition to open markets and phase out trade-distorting subsidies in the industrial countries, beginning with agriculture, textiles, and labor-intensive manufactures."[54] Higher aid flows will also facilitate growth, since it is unlikely that many poor countries, particularly in Africa, can mobilize enough of their own resources to meet all of their human development needs. Moreover, aid flows could be made more continuous and predictable, in order to facilitate budget planning in developing countries. The need for more trade and more aid is echoed in the New Partnership for Africa's Development (NEPAD), which calls on the international community "to reverse the decline in ODA [official development assistance] flows to Africa and . . . . admit goods into markets of developed countries. . . ."[55]

International Financial Institutions

The international financial institutions (IFIs) need to continue to provide financial support to countries pursuing sustainable growth and poverty-reduction strategies. In this regard, IFIs need to ensure that such support is used to promote strategies that are country-owned and developed with input from PSIA. In countries where the institutional capacity to develop and implement such strategies is weak, it is essential for IFIs to provide technical assistance, including in public expenditure management,

[54]Köhler (2002).
[55]NEPAD (2001).

as well as assistance in improving the understanding of links between government policies, poverty, and sustainable use of the environment. In addition to supporting capacity building, the IFIs and their development partners should continue analytical work on the links between economic policy and sustainable development, since many facets of development are still not fully understood. Finally, international financial institutions should foster more extensive dialogue with member country governments and civil society to improve communication and better explain the rationale for their policies.

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