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How to Gain the Most from Structural Conditionality of IMF-Supported Programs

by Jochen Andritzky, Zsuzsa Munkacsi, and Ke Wang

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How to Gain the Most from Structural Conditionality of IMF-Supported Programs

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Abstract

Structural conditionality of IMF-supported programs is designed to support structural reforms by countries borrowing from the IMF. Taking stock of program conditions and their implementation, this paper finds that conditionality focuses on fiscal, monetary and financial issues—areas where IMF expertise is strong—and shies away from structural areas such as labor or product market reforms. Hence, tackling deep-rooted structural issues during IMF-supported programs often remained elusive. To ensure countries gain most from IMF conditionality, the paper outlines an evaluation matrix for prioritizing and designing structural reforms, and applies it to case studies.

JEL Classification Numbers: E02, E61, H12

Keywords: IMF-supported programs, conditionality, structural reforms, energy reform, financial sector reform, governance reform, labor market reform, pension reform, product market reform, SOE reform

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I. Introduction

Conditionality is a key element of IMF-supported programs to help members strengthen their economic and financial policies. Under the IMF's Guidelines on Conditionality (IMF, 2002), structural conditions must be critical to either the achievement of program goals, monitoring program implementation, or implementation of specific provisions under the Articles of Agreement. Only if the program's conditions are carried out, the Fund will make disbursements under a program. Conditionality is a long-standing feature of Fund lending after it was introduced in the 1950s.

Until the 1980s conditionality typically centered on monetary, fiscal and exchange policies. Since, conditionality has also started to target structural weaknesses outside monetary and fiscal domains. This shift reflects members' desire to tackle macro-structural weaknesses in a world of intensifying economic integration, although there have been periods during which the emphasis on structural reforms have been more pronounced. Most lately, structural reforms featured heavily during IMF-supported programs in the European monetary union, given the common currency puts a premium on structural reforms to achieve economic adjustment. The possible economic transformation that could follow today's Covid-19 pandemic may well trigger another period of heightened structural reform needs.

Notwithstanding the importance of structural reforms, the Fund's 2018 Review of Program Design and Conditionality ("2018 RoC"; IMF, 2019a) finds that IMF-supported programs were largely found ineffective in tackling deep-seated structural weaknesses. In the first part of this paper, we determine the reasons for this. Analyzing program conditionality from 2011 to 2017—the period after the Global Financial Crisis—we find that the number of structural benchmarks (the main instrument for anchoring critical macro-structural reforms in IMF-supported programs) has remain broadly unchanged vis-à-vis earlier periods. Also, measures such as the depth of structural conditions, a proxy for the extent of structural transformation to be expected from the reform, or implementation rates have not changed notably. However, we find a notable discrepancy between structural reform needs identified in previous IMF surveillance and the structural conditionality agreed in subsequent programs: Conditionality appears heavily biased toward areas of the Fund's core expertise, such as fiscal, monetary and financial areas. In contrast, other macro-structural areas, such as labor or product market reforms, are rarely addressed in IMF-supported programs notwithstanding reform needs identified by Fund surveillance. While this finding can also reflect that crises shift reform needs and that Fund policies set a higher bar for conditions outside its core expertise, it should not be surprising that deep-seated structural reform needs persist after the completion of IMF-supported programs.

To achieve a well-balanced prioritization of critical structural reforms in IMF-supported programs, we propose an evaluation tool. The tool brings together different economic and political aspects of structural reforms to help Fund staff and policymakers identify the reforms most critical to reach the objectives of IMF-supported programs, such as reducing vulnerabilities and enhancing growth. The tool reflects on issues such as macroeconomic impact, reform design, and implementation risks to arrive at a holistic view to maximize the chances of program success.

We illustrate the use of the evaluation tool in seven case studies. A key takeaway is that Fund-supported programs could draw more on macro-structural gaps identified in prior surveillance, while keeping conditionality design as parsimonious as possible. To prioritize reform needs, program objectives should be formulated in sufficiently specific terms. To achieve reform objectives, Fund-supported programs need to pay attention to appropriate sequencing and packaging of reforms and consider implementation risks, such as political risks or capacity constraints. For instance, some structural reforms can have short-term contractionary effects, and reform payoffs can only be expected once the economy recovers. Fiscal or monetary policy could buffer short-term contractionary effects but only if sufficient policy space for offsetting measures is available.

The case studies furthermore shed light on common pitfalls and provide lessons for good practice in reform design and implementation. A common theme is that structural reforms tend to take a long time and require sustained and outcome-oriented action as well as strong ownership to reap benefits. Conditionality design can help by breaking down reforms into smaller steps, keeping conditions parsimonious and focusing on concrete actions. However, these steps need to end with final reform implementation, rather than with interim outcomes such as plans, strategies, or roadmaps. Policymakers need to pay careful attention to the sequencing of reforms and to policies that can alleviate negative side effects. Overall strong macroeconomic policies and wide consultation can bolster ownership of reforms, alongside openness to consider second-best reform designs.

The remainder of this paper is structured as follows. Section II presents an analysis of structural conditions in IMF-supported programs focusing on the period from 2011 to 2017. Based on this diagnosis, Section III introduces an evaluation tool, and Section IV applies it to seven case studies. Section V concludes.

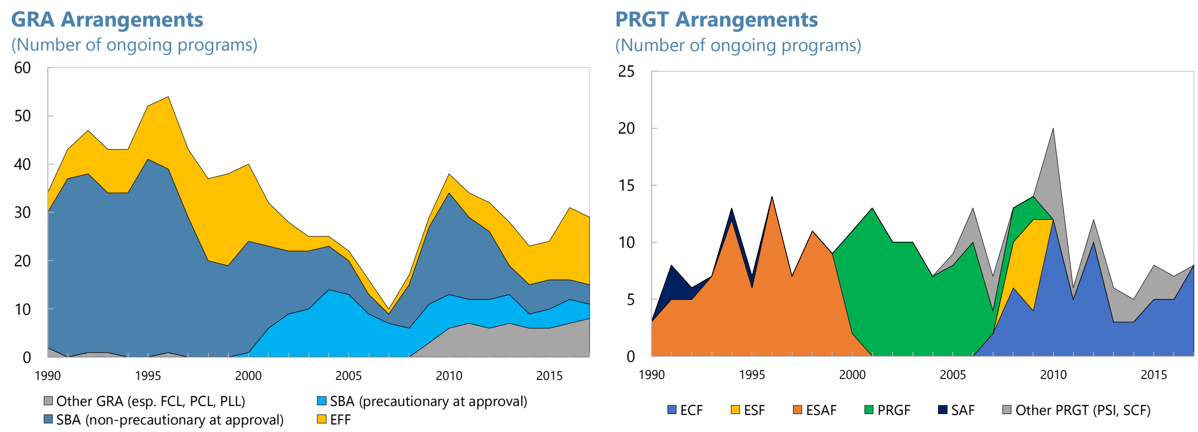
II. Structural Conditionality in Recent IMF-Supported Programs

IMF members can request Fund financing under a wide range of circumstances to give them breathing room to implement adjustment policies in an orderly manner. All IMF members are eligible to access the Fund's resources in the General Resources Account (GRA) on non-concessional terms. Low-income countries can access financial support at concessional terms through the Poverty Reduction and Growth Trust (PRGT; Figure 1, right panel).

The IMF's various lending instruments are tailored to the specific circumstances, in particular the type of adjustment required and the expected duration of financial support needed. Stand-By Arrangements (SBAs) typically cover a shorter period of 12-24 months and are frequently used during acute crisis episodes such as the Global Financial Crisis

(Figure 1, left panel).[2] Arrangements under the Extended Fund Facility (EFF) provide support for comprehensive programs including the policies needed to correct structural imbalances over an extended period and features a duration of up to four years and a longer repayment period.[3] Among concessional lending operations, arrangements under the Extended Credit Facility (ECF) serve a similar purpose (Figure 1, right panel).[4] These instruments, designed for addressing structural impediments or slow growth, have become the most commonly used instruments in recent years.

Figure 1. Fund Arrangements by Facility



Sources: MONA and authors' calculations.

How are structural reform efforts reflected in IMF conditionality? IMF-supported programs set their objectives and policies based on a common understanding between a country's authorities and the IMF on how to address Balance of Payments (BoP) difficulties and achieve medium-term external viability. Program objectives and policies are described in a "Letter of Intent", which often has a "Memorandum of Economic and Financial Policies" attached.[5] Most IMF financing is provided in installments following program reviews, in which the IMF's Executive Board assesses whether policy commitments have been met and whether the program targets and access to the Fund financing need to be adjusted to any new developments.

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[2] See IMF factsheet on SBA.

[3] See IMF factsheet on EFF.

[4] See IMF factsheet on ECF.

[5] See IMF factsheet on conditionality.

Policy measures that constitute structural reforms in IMF-supported programs are typically defined as structural conditions. They describe required actions that often are non-quantifiable, but critical for achieving program goals, monitoring program implementation, or implementing specific provisions under the IMF's Articles of Agreement.[6] Structural conditions typically take the form of structural benchmarks, which are markers to assess implementation during regular program reviews upon which scheduled access to the Fund resources are released. In some cases, measures can be specified as prior actions—measures critical for program success that a country agrees to implement before the IMF Executive Board approves financing or before it completes a review.

In the following, we are analyzing structural conditions in recent IMF-supported programs. This analysis was partly carried out for the 2018 RoC (IMF, 2019a), a review conducted about every seven years. The analysis covers all structural benchmarks (as well as previously used structural performance criteria) and prior actions as recorded in the Monitoring of Fund Arrangements (MONA) database. To discern trends, we contrast two samples: A more recent sample of 133 programs initiated between September 2011 and December 2017 ("2018 RoC sample"), and a sample used in the 2011 Review of Conditionality of 159 programs initiated between January 2002 and September 2011 ("2011 RoC sample").

A. Number, Depth, Implementation and Flexibility of Structural Conditions

The following analyzes the number of structural conditions along several dimensions.

Number

Despite the shift toward programs that are more focused on structural reforms in the aftermath of the Global Financial Crisis (GFC), the average number of structural conditions per year under IMF-supported programs did not increase notably over time period 2002-17 (Figure 2, left panel). This finding could be interpreted in different ways. On one hand, this could reflect that program design preserved the principle of parsimony in conditionality. On the other hand, this could reflect an insufficient focus on critical reform needs, documenting an inconsistency between program objectives and program design.

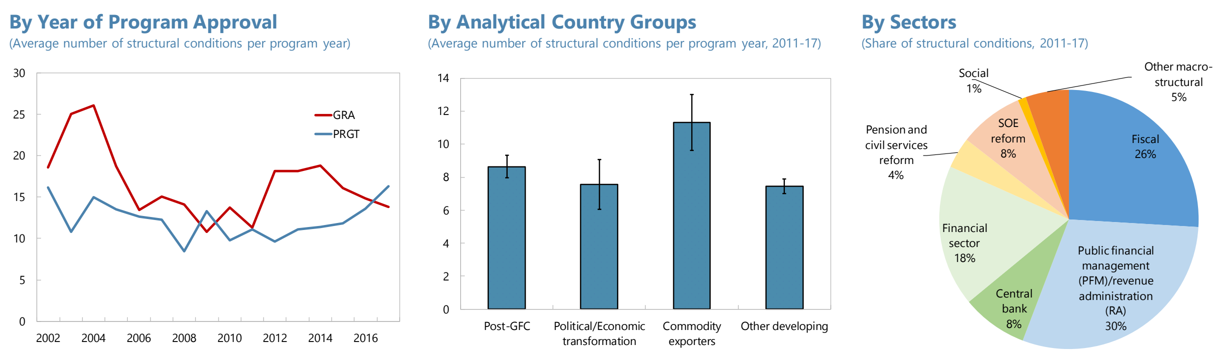
Across different country groups, the average number of structural conditions per program year was broadly similar, with commodity exporters featuring a somewhat higher number of

[6] A judgement that a condition is of critical importance means that if it was not implemented, it is expected that the goals would not be achieved or that program monitoring would not be possible. All critical measures generally must have conditionality associated with them because the Fund needs to be able to interrupt purchase or disbursements if the program is off track. While the criticality criterion applies to all measures, whether in the Fund's core area of responsibility or not, conditions in non-core areas require more detailed explanation of their criticality along with a strong justification.

conditions (Figure 2, middle panel).[7] While commodity exporters experienced a major and persistent terms-of-trade shock following the sharp decline in commodity prices from late-2014, it is not obvious the higher number of structural conditions reflects a stronger focus on structural transformation than in other countries. Notably, other developing countries—mostly low-income countries typically with weaker policymaking capacity—feature a number of conditions similar to those seen in post-GFC countries typically with higher capacity.

Structural conditions mostly relate to the fiscal, monetary, and financial sector areas (Figure 2, right panel). An increasing number of financial sector conditions can be related to reforms in the aftermath of the GFC (IMF, 2019a). However, there were on average just three conditions per year dedicated to structural reforms in other structural areas, such as pension and civil service reforms, state-owned enterprise (SOE) reforms, the social sector, or other macro-structural reforms including product and labor market reforms.[8]

Figure 2. Number of Structural Conditions



Sources: MONA and authors' calculations.

Depth

The number of structural conditions may not be representative of the structural change they bring about. To explore this further, we distinguish the extent of implied change or durability of reforms if a structural condition is fully implemented.[9] We distinguish among three

[7] Post-GFC countries include those directly affected by the GFC, particularly in the euro area. Political/economic transformation countries include countries faced with major political transitions (e.g., Arab Countries in transition), or economic transformation from public to private sector-led growth. Commodity exporters include mainly PRGT-eligible member countries. Other developing countries are mainly remaining PRGT-eligible members. See Annex II for the classification of individual countries in the sample.

[8] The sector of "other macro-structural reforms" further includes: international trade policy (excluding customs), statistics, governance (including corruption), natural resource and agricultural policies (excl. public enterprises and pricing). See Annex III.

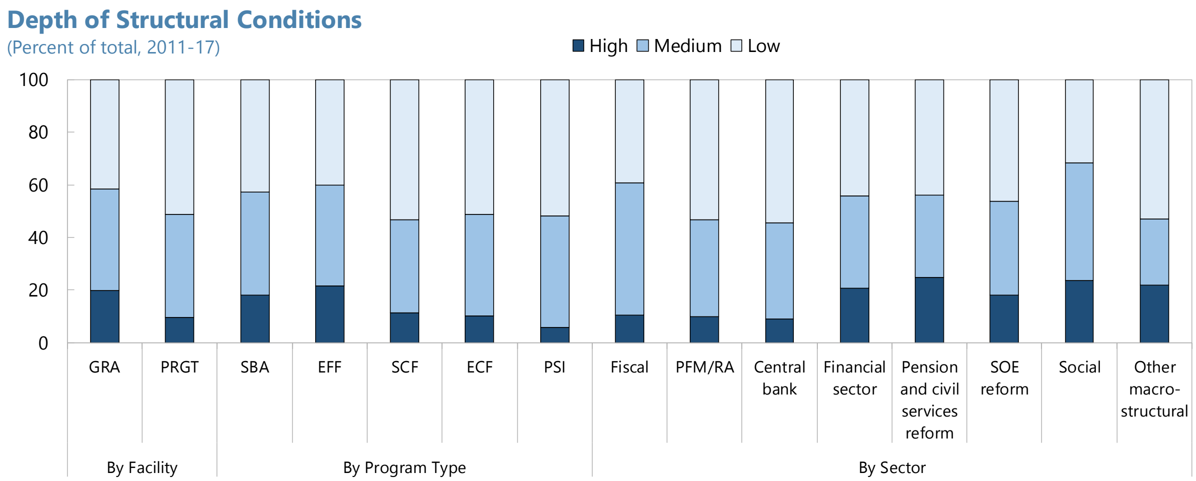
[9] This classification builds on IEO (2008) and IMF (2019a).

categories: High-depth reforms refer to permanent institutional changes, such as reforms that involve legislative changes (parliamentary approval), or conditions with long-lasting impact (e.g., civil service reforms, SOE reforms, privatization). Medium-depth reforms refer to measures that imply an immediate and possibly significant change, but are one-off in nature (e.g., budget approval, one-time change in tariff rates as compared to a permanent change of institutionalizing an automatic tariff adjustment mechanism). Low-depth reforms refer to reforms that in themselves do not bring about significant structural change, but that are steps toward a change.

The classification exercise shows that depth depends mainly on country circumstances and differs greatly across programs. Structural conditions in GRA programs displayed higher depth (Figure 3, first set of columns). This difference could reflect higher implementation capacity, as a larger number of measures in PRGT programs are used as intermediate steps to more significant reforms. However, despite their focus on structural change, structural conditions in EFF and ECF arrangements do not display a significantly higher depth than structural conditions in SBAs and SCFs (Figure 3, second set of columns). Surprisingly, structural reforms in the category of other structural reforms (including labor and product market reforms) were not associated with measures of significantly higher average depth (Figure 3, third set of columns). While social sector reforms as well as pension and civil service reforms exhibited the highest depth, structural conditions for other macro-structural reforms—which are perceived to be more difficult to achieve—are of lower depth than average. Overall, this suggests that structural conditions aimed at non-core structural reforms are generally not of higher depth, which could have provided an explanation for the smaller number of structural conditions in non-core structural reform areas.[10] The finding could reflect that structural conditionality is often occupied with low-depth preparatory steps like developing reform strategies or roadmaps, while not following through with high-depth implementation measures. On one hand, this results from reforms often taking longer than typical Fund programs. On the other hand, it may reflect that reform ambitions wane once countries leave crises behind.

[10] IEO (2008) classifies reform areas in (i) core areas of Fund expertise, (ii) areas of expertise shared with other institutions such as the World Bank, and (iii) non-core areas. This classification was also used in IMF (2019a).

Figure 3. Depth of Structural Conditions



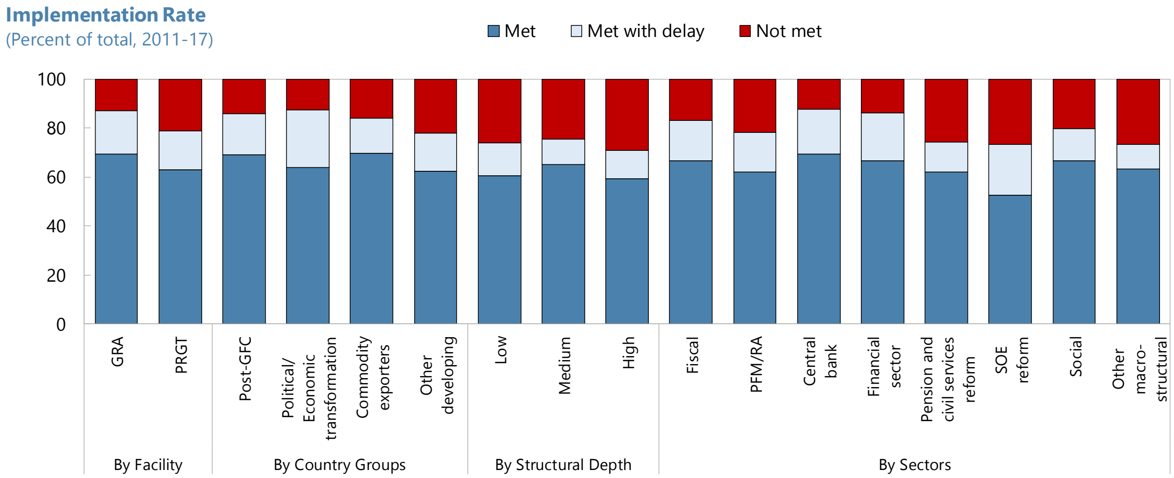
Sources: MONA and authors' calculations.

Implementation and Flexibility

Once countries commit to measures, implementation of structural conditions, as assessed in program reviews, is generally strong. We measure implementation by their assessment in staff reports where they are classified as "met" per the agreed test date, "met with delay" after the agreed test date but before the program's last completed review, or "not met" otherwise.[11] The share of implemented conditions exceeds 80 percent in programs between 2011 and 2017, with implementation somewhat higher for GRA than for PRGT programs (Figure 4, first set of columns). Among country groups, countries under political or economic transformation and other developing countries—mostly low-income countries—feature somewhat lower implementation rates (Figure 4, second set of columns). As expected, given likely difficulties in meeting them, the share of unmet conditions is somewhat higher for high-depth structural conditions (Figure 4, third set of columns). Implementation rates of other macro-structural reforms (which mostly reflect non-core areas like labor and product market reforms), SOE reforms, pension and civil service reforms, and to some extent public financial management and revenue administration (PFM/RA) reforms are notably lower (Figure 4, last set of columns). Separately, regression analysis suggests that countries' track record proxied by lagged implementation rates significantly matters for performance against structural benchmarks (IMF 2019a).

[11] Thereby, conditions that were not met include structural conditions that were (i) outstanding, in other words not implemented before the last completed review, (ii) assessed to be partially implemented, or (iii) waived, in other words dropped from the program.

Figure 4. Implementation of Structural Conditions



Sources: MONA and authors' calculations.

Besides implementation, we also analyze modifications of structural conditions during program reviews.[12] Modifications of structural conditions reflect the Fund staff's flexibility in assessing the implementation of structural conditionality at Board-approved program reviews. Most modifications consist of delaying a measure by changing its test date only, with the overall share of modified conditions being roughly similar in GRA and PRGT programs (Figure 5, first columns). In a few cases, measures are further amended, including making it a prior action for completing a program review. Modification rates are higher in the group of other developing countries, possibly related to lower capacity, and in countries undergoing economic/political transformation (Figure 5, second set of columns). Moreover, modification rates are somewhat higher in non-core areas of IMF expertise. This is mirrored in the sectoral breakdown where modification rates are higher than average for pension and civil services reform, other macro-structural reforms, financial sector reforms and social reforms (Figure 5, third set of columns). Higher modification rates in non-core areas could reflect that lower expertise in designing conditionality requires more frequent adjustments, or that the Fund assigns lower relevance to these areas. It could also reflect that these areas cover reforms that are more difficult to implement given political or capacity constraints. In Serbia (2015 SBA), for example, both staff and authorities realized that more small steps were needed toward SOE reform, owing to technical capacity constraints and pushback from

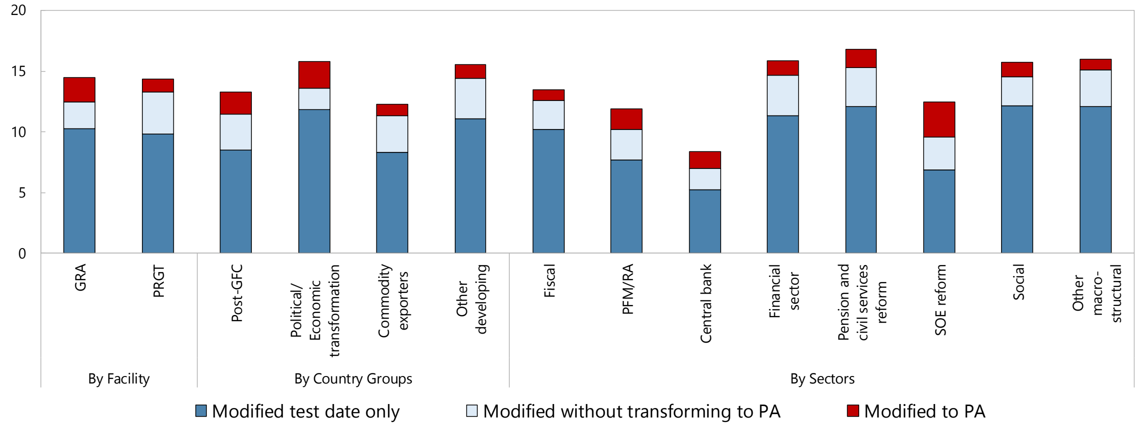
[12] Note that there is no exclusive relationship between implementation and modification. In other words, it is not only structural conditions that were not fully implemented that are modified. Conditions that are not yet due can also be modified during program reviews, for instance to reflect changes in circumstances.

vested interests, and modified SOE reforms to a sequence of medium- and low-depth structural conditions.

Figure 5. Modified Structural Conditions

Modification Rate

(Percent of total structural conditions, 2011-17)



Sources: MONA and authors' calculations.

Taken together, our analysis of structural conditions in programs suggests that—despite the renewed focus on structural weaknesses and the increased use of EFF-supported programs—Fund conditionality in structural areas has not increased. Although conditions associated with structural reforms are not of higher depth—possibly reflecting a lack of reform ambition in itself—our analysis shows that implementation is weaker in reform areas that most likely facilitate structural transformation.

B. Did Conditionality Tackle Key Macro-Structural Gaps Identified in Surveillance?

In this section, we analyze how well structural conditionality follows the principle of criticality in practice. *First*, we ask how the structural conditions in IMF programs are related to stated program objectives. In other words, were program objectives underpinned by policy actions as set out in structural conditions, and—vice versa—are structural conditions related to program objectives? *Second*, we relate findings from Fund surveillance with conditionality from IMF-supported program. In other words, were the structural weaknesses identified prior to the program addressed through structural conditions during the program?

Answers to these questions are derived from a text analysis for a subset of 12 programs from the 2018 RoC sample ("subsample").[13] We extract program objectives and structural

[13] The subsample includes 12 randomly chosen programs of the 2018 ROC sample: Armenia's 2014 EFF, Benin's 2010 ECF, Greece's 2010 SBA, Côte d'Ivoire's 2011 ECF, Honduras's 2010 SBA-SCF, Iraq's 2016 SBA, Ireland's 2010 EFF, the Kyrgyz Republic's 2011 ECF, Mauritania's 2010 ECF, Mozambique's 2013 PSI,

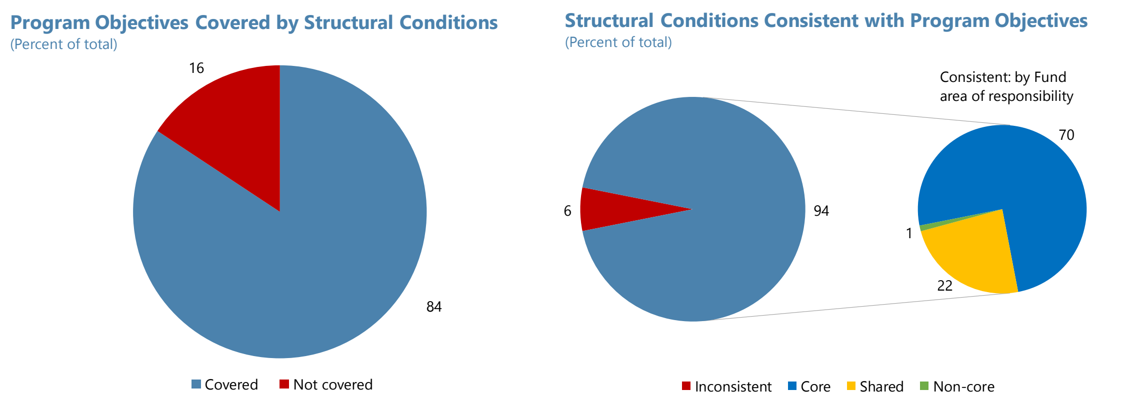
(continued…)

conditions from initial program request documents. To identify macro-structural weaknesses, we analyze the most recent Article IV surveillance reports preceding the program to identify staff's surveillance findings of reform needs ("surveillance gaps").

Objectives and Structural Conditions

We find that 85 percent of program objectives were covered by structural conditions (Figure 6, left panel). This suggests that conditionality was generally well-aligned with program objectives. Conversely, almost 95 percent of structural conditions were consistent with program objectives (Figure 6, right panel).

Figure 6. Program Objectives and Structural Conditions



Sources: MONA and authors' calculations.

However, there are important caveats to this apparent consistency between program objectives and conditionality. First, program objectives often remained ambiguous. For instance, a program document may refer to different, not fully consistent sets of objectives in different parts of the same document. Second, program objectives were typically stated in very broad terms. For example, program objectives were often formulated as "enhancing economic growth" or "achieving macroeconomic stability." In contrast, structural conditions were typically focused on rather narrow issues, such as transferring the control over education payroll to the Ministry of Finance (Honduras) or increasing electricity tariffs by CFAF10 per kilowatt hour on average (Benin).[14]

São Tomé and Príncipe's 2015 ECF, and Sri Lanka's 2009 SBA. The subsample represents the 2018 ROC sample in a well-balanced manner along several dimensions, including analytical group, arrangement/instrument type and region (Annex II).

[14] However, there are examples of programs narrowly targeted on certain objectives, such as Ireland (2010 EFF) on financial stability or Benin (2010 ECF) on revenue administration. In most programs, however, program objectives were broader, including enhancing growth and reducing poverty.

Ambiguous or excessively general objectives make prioritizing of conditionality difficult. While almost all program initiation documents provided some rationale for chosen conditions, they rarely discussed how the set of reforms help achieve objectives, or what alternative conditions were considered.

Surveillance Gaps and Structural Conditions

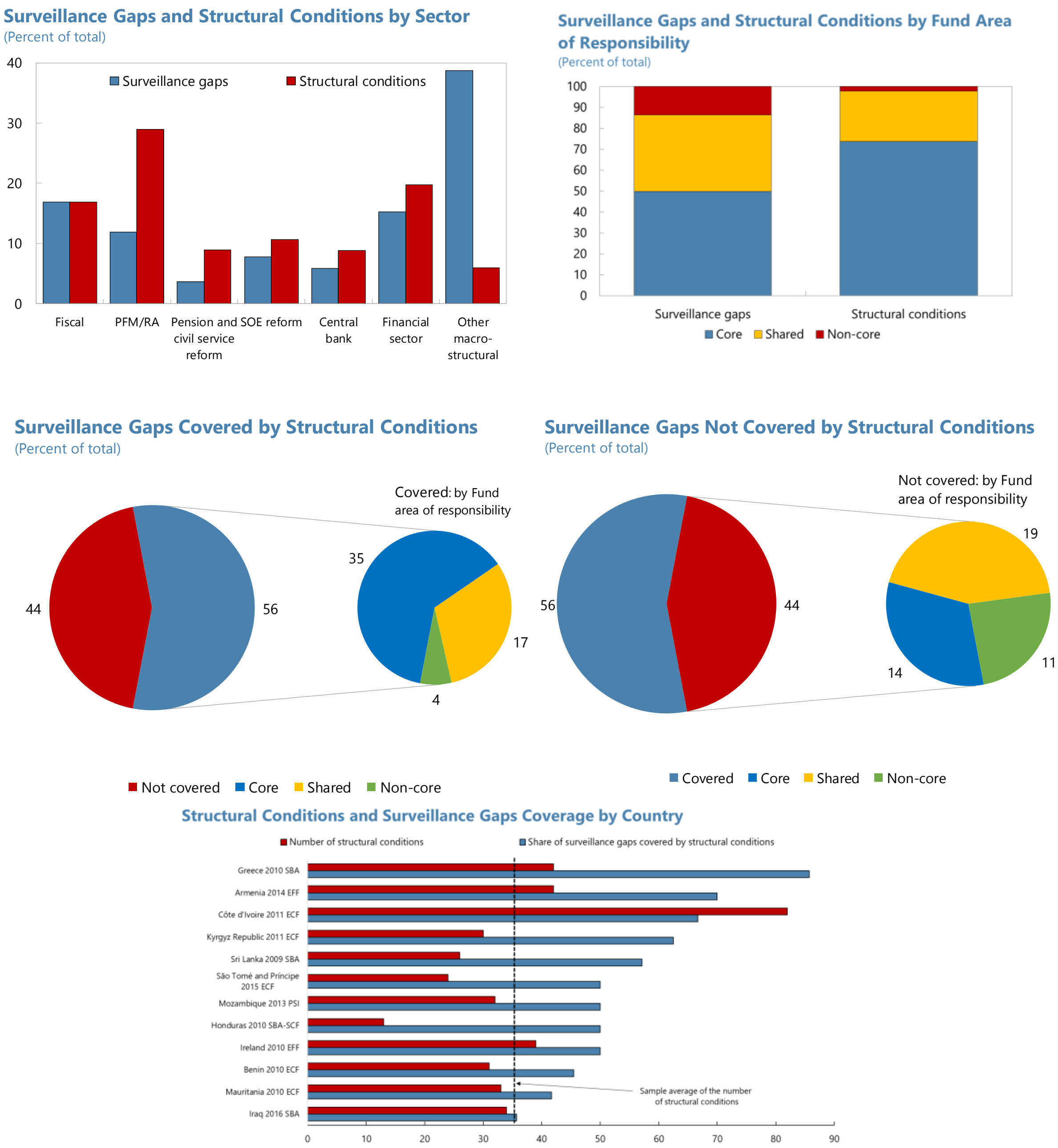
Comparing the composition of surveillance gaps and structural conditions, we find a notable discrepancy between macro-structural weaknesses and structural conditionality.

The distribution in the number of identified surveillance gaps and the number of structural conditions across main reform areas is very different: About 40 percent of the identified structural weaknesses are found in other macro-structural areas, such as labor and product markets, whereas 30 percent of structural conditions are concentrated in the area of public financial management and revenue administration (Figure 7, top left panel).

The IEO (2008) classifies Fund expertise into core and non-core areas of expertise, as well as areas of shared expertise with other institutions (such as the World Bank). Using this classification, the identified discrepancy between surveillance gaps and structural conditions seems to be related to available in-house expertise. While about half the surveillance gaps are in non-core and shared areas, less than 30 percent of structural conditions fall into these areas (Figure 7, top right panel). Only 2 percent of structural conditions are found in the non-core area in the subsample.

The relationship between the discrepancy between Fund diagnosis and treatment on the one hand, and the bias of treatment toward core areas of expertise on the other, is most obvious from a breakdown of surveillance gaps: Of those gaps covered by structural conditions, about two thirds fell into core areas, while most gaps not covered by structural conditions tended to be in shared or non-core areas (Figure 7, middle panels).

Figure 7. Structural Conditions and Surveillance Gaps



Sources: MONA and authors' calculations. Notes: PFM stands for public financial management, RA for revenue administration, and SOE for state-owned enterprise. "Other macro-structural" includes (i) social, gender, inequality and poverty, (ii) labor market reforms, (iii) governance, including corruption, (iv) product market reforms and competition, and (v) other, e.g. trade or national accounts statistics.

The aggregate result hides significant country variations (Figure 7, bottom panel). For example, Mauritania's 2010 ECF contained conditionality on less than half of the previously identified surveillance gaps. Many of Mauritania's structural reform needs not addressed by conditionality pertained labor market reforms and reforms to the business environment—mostly areas where the Fund relies on sharing expertise with other institutions. At the other end of the spectrum, Greece's 2010 SBA covered most surveillance gaps: The 2009 Greece Article IV surveillance report listed eight major reform needs, and the 2010 program request included conditionality on all except one of them.

Better coverage of surveillance gaps does not necessarily result in a larger number of structural conditions, thereby sacrificing the parsimony of program conditionality. While Greece's program indeed had a larger number of structural conditions, which reflects factors specific to this program, the overall correlation between the number of structural conditions and the share of surveillance gaps covered is only 0.4.

Certainly, the identified discrepancy between macro-structural weaknesses and structural conditionality can be interpreted in different ways. On one hand, it could reflect country circumstances, such as technical capacity constraints and more pressing adjustment needs in other areas following the onset of a crisis. On the other hand, it could reflect Fund policies and practices, such as the higher bar for criticality of program measures outside the Fund's core expertise,[15] the drive for parsimony, or the fact that demand management policies can deliver program objectives much more easily—albeit possibly less sustainably. However, the heavy use of facilities such as the EFF or ECF geared toward addressing structural weaknesses seems out of line with programs that do not address weaknesses in macro-structural areas.

III. EVALUATING STRUCTURAL REFORM OPTIONS: A TOOL

The diagnosis of the previous section suggests structural conditionality in IMF-supported programs could be geared better toward tackling structural weaknesses. The analysis also suggests this could be related to the lack of internal expertise in some reform areas. However, several more explanations are possible. For example, some reforms have short-term economic costs or pay off only in the long run, which could be incompatible with a program horizon of four or five years maximum under a Fund arrangement. Alternatively, some reforms may be deemed politically too uncertain to achieve, or too complicated for countries with limited technical capacity.

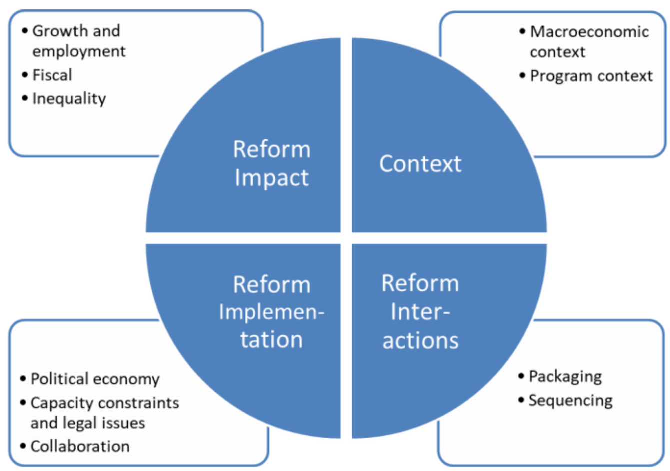
Most program documents provide some rationale for the choice of structural conditions. However, they rarely discuss the wider set of potential reforms, or how chosen reforms are most conducive to achieve program objectives. Given the observed discrepancy between structural weaknesses and structural conditions, it appears member countries could gain more

[15] Note that criticality is defined differently in Fund surveillance and programs. In *surveillance*, policies are examined to the extent that they significantly influence present or prospective balance of payments or domestic stability ("macro-criticality"). In contrast, in *programs*, conditions need to be of critical importance for achieving the program objectives ("criticality with regard to program objectives"). However, program objectives in turn aim to resolve a balance of payments problem and to achieve medium-term external viability.

from IMF-supported programs if conditionality were better geared toward macro-structural reform needs. Accordingly, the 2018 Review of Conditionality (IMF, 2019a) recommends improving the identification, prioritization and sequencing of reforms based on criticality.

To gain a holistic view on reform options, their benefits and potential pitfalls as well as trade-offs, we develop a set of evaluation criteria (Figure 8). These criteria are based on existing guidance, e.g. IMF (2016a), and related academic literature. These criteria could be evaluated for different reform options within a reform area. The criteria are necessarily interrelated—for instance, a different sequencing of reforms will lead to a different growth impact—and should be interpreted in a holistic way. In particular, the political economy of some reforms may require a reform design that is second-best from an economic point of view. Explicitly laying out these criteria for different reform options could enable country authorities and Fund staff to arrive at a better-informed judgement on critical program conditionality and to better justify the choices made.

Figure 8. Evaluation Matrix: Criteria



Source: authors' illustration.

In the following, we motivate and explain the criteria in turn.

A. Context

During IMF-supported programs, structural reforms are embedded in a particular context, typically a post-crisis situation which also encompasses measures for crisis management. Hence, the macroeconomic and program context is an essential aspect in prioritizing and designing structural conditionality. Macroeconomic considerations include:

- **Cyclical condition.** For the economy-wide impact of structural reforms—in particular for labor and product market reforms—business cycle conditions matter: the sign and size of reform impacts vary depending on the extent of economic slack (Duval and Furceri, 2018). The larger a country's output gap, the more it could prioritize structural reforms that will support growth in the short term, also considering the possibly larger fiscal multipliers in times of economic slack, or design structural reforms in ways to minimize possible short-term output costs (Duval and others, 2020a).

- **Fiscal and monetary policy space.** Where budget constraints or public debt are binding constraints, those reforms could be prioritized that are budget-neutral (e.g., an increase in infrastructure spending financed by a reduction in energy subsidies) or have positive demand effects (e.g., reducing product market entry barriers). Buffering of negative short-run effects of reforms will require sufficient space for expansionary fiscal offsets or loser monetary policy.

- **Income level or reform priorities.** The state of economic development matters—less developed countries typically have different needs or reform priorities than more advanced economies. For example, for emerging market economies, the largest productivity payoffs are associated with reforms that improve market functioning, while for advanced economies, reforms that facilitate technological progress may be more relevant. Reform priorities could also be benchmarked against other countries of comparable economic development, using the IMF's Structural Reform Database (IMF, 2019b; Ciminelli and others, 2019).

In addition, structural reforms need to be consistent with the overall program design. As discussed in the previous section, reforms should address major macro-structural weaknesses as identified in IMF surveillance or other analyses such as World Bank or OECD reports. The design of structural conditions needs to be parsimonious yet effective for achieving program objectives. Program length and access, the amount of financing being made available under the program, also determines conditionality: longer programs could tackle deeper reforms or phase reform implementation over a longer period, while access determines the resource envelope for the program. In addition, overall program risks should be factored in, such as reform fatigue or other elements of the program that could cause it to go off track.

B. Reform Interactions

Appropriate packaging and sequencing can mitigate short-term costs and facilitate the implementation of reforms. Packaging refers to the combination of reforms with other reforms or policies which have enabling or complementary character. To this end, it is useful to identify binding constraints which need to be removed to facilitate structural reform or to enhance reform payoffs.[16] Sequencing refers to the chronological order and speed of executing the reform package which is often found key to successful implementation (Edwards, 1989; Murphy and others, 1992; Dewatripont and Roland, 1995; Hausmann and others, 2005).

The literature on the economic and political impact of reforms offers useful insights that can inform reform packaging and sequencing. On the interaction of labor and product market

[16] Chapter 3 of IMF (2019b) identifies weak governance or high corruption as well as insufficient access to credit as the two key binding constraints in emerging market and developing economies.

reforms, the literature provides a variety of insights. Kugler and Pica (2004) find that product market rigidities can mitigate the impact of labor market deregulation. In contrast, Blanchard and Giavazzi (2003) argue to initiate product before labor market reforms, as the former can increase real wages, while the latter can drive them down. While Munkacsi and Saxegaard (2017) find that sequencing labor before product market reforms facilitates an earlier new equilibrium, Benlamine and others (2019) conclude that reforms should proceed in lockstep. Bouis and others (2020) find that while gains from non-manufacturing industry deregulation in advanced economies take time to fully materialize, they were statistically and economically significant already after two years, while no evidence of any short-term costs were found. Therefore, the authors advocate prioritizing product market reforms over labor market reforms in crisis times.

The aspect of packaging and sequencing is often related to the political economy. Funke (1993) cautions against gradualism as this is administratively more challenging and allows time for interest groups to form lobbying power. Rodrik (1994) and Dewatripont and Roland (1995) note that reform bundling can help, as voters may be willing to swallow less popular reforms if packaged with other more popular reforms. Yet, winners of early reforms have an incentive to derail later reforms from which they lose (Martinelli and Tommasi, 1993).

C. Reform Implementation

Implementation risks to reforms are a key concern which in the past did not receive sufficient attention. Given the importance of ownership to program success, the choice and design of structural conditionality to achieve a certain structural reform needs to carefully consider the country-specific political context. Generally, reforms are easier accomplished if the political window of opportunity is right, for instance when government credibility and reform ownership is high (Funke, 1993; Agarwal and others, 1992) and no election is looming (Ciminelli and others, 2019). There can be a tension between economic and political economy considerations—while the short-term economic payoff from certain reforms (notably labor market reforms) is weaker in crisis times, crises may offer a window of opportunity of reform. For instance, Duval and others (2020b) find that weak macroeconomic conditions are the most robust correlate of labor market reforms. If reforms have a strong distributional effect, finding consensus may take long, in particular in more polarized societies (Alesina and Drazen, 1991; Alesina, 1994).[17] Another implementation risk stems from country-specific legal issues, such as constitutionality or legal challenges in presence of constrained capacity of courts.

Especially in less developed countries, informality and governance weaknesses can hinder reform implementation, and administrative and capacity constraints may be binding. In this case, reforms may need to be broken down into smaller steps and closely aligned with

[17] Wei (1997) finds that a package of reforms that would have been rejected by majority voting may gain approval if submitted piecemeal because of a growing constituency in favor of reforms.

technical assistance. Likewise, if Fund expertise is insufficient—which may have contributed to the observed bias in Fund conditionality—evaluating reform options needs to consider opportunities for collaboration with institutions such as the World Bank or the OECD.[18]

D. Reform Impact

A reform's economic impact is typically a key consideration in evaluating its criticality. Quantitative estimates can draw on the extensive literature in this area.[19] In the context of IMF-supported programs, the challenge is to estimate reform pay-offs amid uncertainty about post-crisis economic developments and within the fairly short time horizon of program engagement. The 2018 Review of Conditionality (IMF, 2019a) finds that the growth payoff from structural reforms is often overestimated in programs, as some structural reforms have short-term growth costs while benefits may take longer to materialize.

Besides their effect on growth and employment, structural reforms can have fiscal implications (Banerji and others, 2017). Also, analyses of the distributional impact of structural reforms—such as through growth incidence assessments (Kireyev and Chen, 2017—can help gauge political support and anticipate vested interests (Ciminelli and others, 2019). If fiscal offsets are considered, such as social assistance to compensate short-term negative employment effects of labor market reforms, realistic assumptions need to be made about their phase-out. However, direct compensation of losing groups may not work to underpin support for the reforms if their temporary nature is anticipated (Fernandez and Rodrik, 1991).

IV. Case Studies

This section applies the evaluation criteria to seven case studies and derives lessons. While the evaluation applies an ex-ante view—putting us into the shoes of the IMF mission chief at that time—, the lessons we draw benefit from hindsight.

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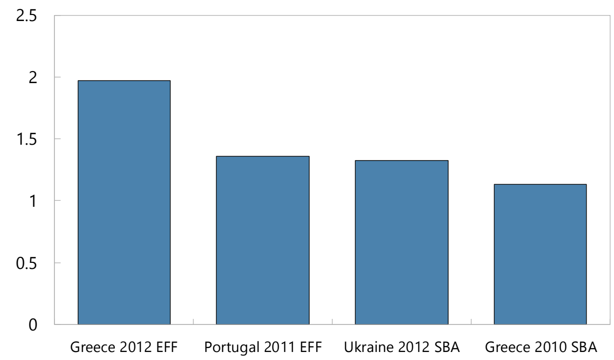
[18] See IEO (2020). These and other measures to enhance capacity could be elaborated on in the country's capacity development strategy document.

[19] For analyses in a closed-economy setup, see Berger and Danninger (2005), Boken and Hallett (2008), and Fernandez-Villaverde and others (2014). For analyses taking international spillovers into account, see Lusinyan and Muir (2013), Andres and others (2014), Eggertson and others (2014), and Vogel (2014). For analyses focusing on specific characteristics, like the existence of a large informal sector, see Farrell (2004), Bailey and others (2005), La Porta and Shleifer (2008), Charlot and others (2015), Anand and Khera (2016), and Munkacsi and Saxegaard (2017). For labor and product market reforms, see Cacciatore and Fiori (2016) and IMF (2016b).

A. Labor Market Reforms: The Case of Latvia

Despite labor market inefficiencies often identified in surveillance, very few Fund-supported programs attempt comprehensive labor market reforms. Some programs include measures in related reform areas—such as (disability) pension reform, education reforms, or reforms to enhance gender equality and childcare—which also contribute to labor force participation and employment. However, between 2011 and 2017, significant labor market reforms are found in only four programs, mainly in the euro area (Figure 9).

Figure 9. Top 4 Programs with Labor Market Reforms
(Average number of structural conditions per program year)



Sources: MONA and authors' calculations.

Latvia's 2008 SBA presents a successful example of how labor market reforms supported the country's adjustment amid strong ownership. Key objectives of Latvia's 27-month SBA included fiscal tightening and improving competitiveness which required a substantial internal devaluation given Latvia's membership in the European Exchange Rate Mechanism (ERM II). To preserve social and capital spending, fiscal adjustment imposed significant cuts on public sector wages. Wage cuts in the central government were expected to lead to nominal wage reductions in other parts of the government and the private sector. Achieving this adjustment turned out to be more difficult than anticipated, partly because external conditions deteriorated further. Hence, policies under the program needed to be adjusted further, and several labor market-related conditions were introduced over the course of the program.

What was the scope of the problems?

Box 1 illustrates an evaluation of labor market reforms for Latvia's SBA. The arrangement was approved in 2008 after years of unsustainably high growth, including excessive wage increases, and large current account deficits which had coalesced into a balance of payments, financial and fiscal crisis. Between August 2007 and December 2008, private sector deposits

Box 1. Evaluation Matrix: Labor Market Reforms During Latvia's 2008 27-Months SBA

Criterium		Evaluation
Context	Macroeconomic context	**Macroeconomic situation:** • Unsustainably high growth and large current account deficits over several years preceding the program. • Private sector deposits fell by 10 percent and official reserves fell by almost 20 percent during the months prior to the program. **Fiscal policy space:** Fiscal consolidation necessary. However, 20 million lats are reallocated from the European Social Fund for active labor market policies and temporary public employment programs. **Monetary policy space:** Latvia's currency is pegged to the euro. **Income level or reform priorities:** Latvia is an emerging market economy with strong reform drive in anticipation of membership in the European Economic and Monetary Union.
	Program context	**Surveillance gaps:** The 2006 Article IV surveillance report noted the need for increasing labor force participation, partly by making the public sector more efficient. **Program objectives:** • The immediate objective is to stabilize the financial sector, restore depositor confidence, and avoid the disorderly adjustment that would follow if the exchange rate peg were abandoned. • For the medium-term, the program seeks to facilitate economic adjustment and to strengthen the peg. **Program risk:** Considerable risks, in particular given the difficulty to correct currency misalignment without nominal depreciation.
Reform interactions	Packaging	**Enabling reforms:** Active Labor Market Policies to enhance the dialogue between public and private sectors. **Complementary reforms:** Promoting wage restraint to support fiscal adjustment.
	Sequencing	Labor market reforms to be introduced over the course of the program.
Reform implementation	Political economy	High ownership of Latvian authorities to safeguard Latvia's future membership in the euro area.
	Capacity constraints and legal issues	Need for substantial technical assistance to relieve institutional constraints, although not necessarily in the area of labor market reforms.
	Collaboration	Close cooperation with the EU, the ECB, the World Bank, the EBRD, and some Nordic country authorities, including participation in Fund missions.
Reform impact		• Reforms will support relative price adjustment, including in the labor market where wages experienced some nominal decline. • However, mismatches in the labor market usually take time to unwind, so the level of structural unemployment may remain high. • Inequality may increase, linking to the discussion on the guaranteed minimum income scheme.

fell by 10 percent, and the second largest bank in Latvia suffered a deposit run. Official reserves dropped by almost 20 percent as the central bank sold foreign currency to defend the peg to the euro. This situation necessitated to arrest the immediate liquidity crisis, followed by measures to ensure long-term external stability, including through labor market reforms.

How were the problems addressed?

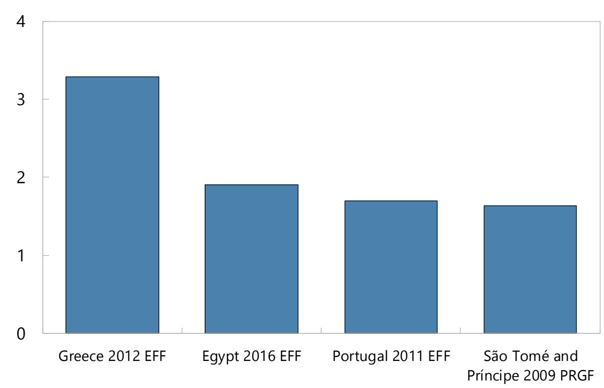
Internal devaluation was complicated by a worsening external environment following the Global Financial Crisis, dampening external demand and causing exchange rates of Latvia's main trading partners to depreciate sharply. To support internal devaluation through lower wages and support fiscal adjustment, four structural benchmarks on labor market reforms were introduced during the program period (see Annex IV.A). These included measures to promote wage restraint and to prepare an active labor market policy strategy, drawing on previous surveillance findings.

What are the lessons?

Latvia's program proved to be a success. The IMF's Ex Post Evaluation (IMF, 2013) notes internal devaluation policies helped support relative price adjustment including in the labor market where wages experienced some nominal decline. However, these outcomes were achieved under very specific circumstances which may not be easily replicable in other countries. In particular, strong ownership to safeguard Latvia's accession prospects to the euro enabled support for deep policy adjustments. The Ex Post Evaluation also notes that flexibility in program design, which had to be adapted given the deteriorating external environment, helped the program to achieve its objectives. However, the adjustment proved to be more lengthy than anticipated, and structural unemployment remained elevated over a longer period of time.

B. Product Market Reforms: The Case of Portugal

Figure 10. Top 4 Programs with Product Market Reforms
(Average number of structural conditions per program year)



Sources: MONA and authors' calculations.

Product market reforms have been more common than labor market reforms in IMF-supported programs, with a number of countries conducting reforms in the aftermath of the Global Financial Crisis (Figure 10). The design and implementation of product market reforms can be challenging. Generally, product market reforms are easier to design and to implement when addressing general frameworks such as investment codes or competition laws, or when targeting strategic sectors such as the mining sector of a commodity exporter. However, the chosen approach needs to consider the country-specific circumstances.[20] In addition, economic payoffs from product market reforms may take time.

Portugal's 2011 EFF presents an example of a program with an extensive structural reform agenda, including on product market reforms, to close its competitiveness gap. While significant efforts were undertaken, reforms took time, often remained incomplete, and did not generate large immediate benefits.

What was the scope of the problems?

Since entering the euro area, economic imbalances in Portugal have significantly increased. When the crisis in the euro area unfolded, the country was among the most vulnerable, featuring wide current account and fiscal deficits, and high financial and corporate sector debt. Lack of competitiveness has been identified as key issue for long, with the 2009 Article IV surveillance report noting the decline in price- and cost-based measures of competitiveness, low and declining productivity, and the weak export base focused on low-skill products.

How were the problems addressed?

Enhancing competitiveness and growth was a key objective of the program (Box 2). Within an extensive structural reform agenda, product market reforms aimed at fostering competition to exert downward pressure on non-tradable relative prices and enhancing productivity. To this end, the program request document contained a structural condition to revise the Competition Law, among other program commitments to enhance competitiveness (Annex IV.B). At the outset there was broad political consensus. Later, though, several challenges arose, such as reform fatigue and vested interests, especially in the energy sector.

What are the lessons?

With hindsight, a key lesson is to taper expectations of rapid competitiveness gains despite a turnaround of the current account. The Ex Post Evaluation (IMF, 2016c) notes that despite wide-ranging structural reforms, growth remained tepid and unemployment high. It also cautions that, while costing of reforms was attempted, it proved difficult to establish a link between competitiveness reforms and their effects on prices. Hence, IMF-supported programs should be built on conservative assumptions for the payoff from product market reforms, with most benefits often materializing far after the end of the program.

Portugal is a good example for buffering the impact of structural reforms on the most vulnerable through recalibration of social protection. Among other measures, means-testing

[20] For instance, in Greece, initial structural conditions on economy-wide legislation encountered severe legal hurdles and required numerous sector-by-sector conditions which proved difficult to implement.

Box 2. Evaluation Matrix: Portugal's 2011 3-Year EFF

Criterium		Evaluation
Context	Macroeconomic context	**Macroeconomic situation:** Large economic imbalances including significant REER overvaluation, large current account and fiscal deficits, and high financial and corporate indebtedness. Deep-rooted structural deficiencies, such as impediments to competition and a weak court system. **Fiscal and monetary policy space:** Very limited. Portugal is one of the most indebted euro area members with a fiscal deficit of 9.1 percent of GDP and a public debt ratio of 93 percent. Monetary policy is governed by the ECB. **Income level or reform priorities:** Portugal is an advanced economy with significant structural weaknesses despite some significant reforms in recent years.
	Program context	**Surveillance gaps:** The 2009 Article IV surveillance report notes low competitiveness given overvaluation, and low and declining productivity. Exports consist mainly of low-skilled products. The non-tradeable sector suffers from a lack of competition. **Program objectives:** • Enhancing competitiveness and growth • Instilling confidence and ensuring fiscal sustainability • Safeguarding financial stability and avoiding excessively fast deleveraging **Program risk:** Several risks to program success, including elections in June 2011.
Reform interactions	Packaging	Enabling and complementary structural reforms include: • Labor market reforms to create jobs, increase productivity and promote competitiveness-enhancing wage adjustments; • Reduction in labor costs via fiscal devaluation; • Market liberalization in the energy and telecommunication sectors, reducing state involvement including through privatizations in the transport, energy, communications, and insurance sectors; • Improving the efficiency of judicial system by reducing backlog and enhancing transparency.
	Sequencing	Front-loading of fiscal and labor market reforms to achieve internal devaluation.
Reform implementation	Political economy	Broad political consensus may erode over time, and vested interests, especially in the energy sector, may prevail. (In 2012 and 2013, Labor Code revisions were reversed, and deeper labor market reforms faced political resistance.)
	Capacity constraints and legal issues	Adequate capacity.
	Collaboration	The program is closely coordinated with the European partners.
Reform impact		**Short-term:** Negative growth impact, also given necessary front-loaded fiscal adjustment. **Long-term:** Positive growth impact. Improved competition in domestic markets will increase, promoting price competitiveness. However, declining wages may curtail domestic demand, while payoffs from product market reforms may take much longer than the EFF arrangement. **Inequality:** Reforms may have a detrimental impact on equality. Measures to provide targeted support include: • Enhancing means-testing by applying unified and consistent selection criteria throughout the transfers system; • Exemption threshold to protect the more vulnerable from the proposed "moderating fee" increases in the health sector.

of transfer system was enhanced by applying unified and consistent selection criteria, and an exemption to "moderating fees" in the health sector was introduced.

Even though the program was largely successful, the Ex Post Evaluation (IMF, 2016c) noted that inappropriate sequencing may have reduced the effectiveness of reforms: if product market liberalizations had been undertaken before labor market reforms, the latter could have been more effective.

Furthermore, the case of Portugal illustrates the difficulty to maintain parsimony of program conditionality. Gershenson and others (2016) estimate more than 150 measures in the areas of product markets were implemented, within Portugal's structural reform program containing close to 500 actions. Given some of the measures faced stiff opposition from vested interests, the reform program put a large burden on the administration. While Portugal was able to successfully handle the reform burden, other countries with lower capacity may not.

C. Governance Reforms: The Case of Madagascar

Reforms to address governance and corruption vulnerabilities can be part of conditionality in Fund-supported programs when these vulnerabilities are assessed as severe and addressing them is of critical importance for achieving the program's objectives (IMF, 2018).

Critical economic governance issues include improving the management of public resources through reforms of public institutions and administrative procedures; and supporting the development and maintenance of a transparent and stable economic and regulatory environment conducive to efficient private sector activities, including fighting corruption. This could translate into conditionality on institutional reforms of the treasury, budget preparation and approval procedures, tax administration, accounting, and audit mechanisms, central bank operations, regulatory framework of taxation and banking, and market mechanisms on the exchange, trade, price, or the financial system. Measures to fight corruption could include regulatory reforms to reduce the scope for bribes, stronger anti-money laundering measures, and more effective anti-corruption legal frameworks. While the Fund has increasingly built up expertise in some areas of governance reforms (supported by recently reviewed guidance), collaboration with other relevant institutions such as the World Bank or assessor bodies such as Financial Action Task Force (FATF) remains important. The Madagascar (2016 ECF) program demonstrates a good example for governance reforms, resulting in solid progress toward better governance and reduced corruption.

What was the scope of the problems?

Following the re-establishment of constitutional democracy in 2014, Madagascar entered a difficult path to recover from a long political crisis and international isolation. On this path, one of the main challenges was Madagascar's deep-rooted structural weakness. In 2015, the economic recovery failed to gain momentum due to falling commodity prices and weather-related shocks while poverty was widespread. Governance remained weak, and corruption was widespread.

How were the problems addressed?

On the heels of financial assistance under the Rapid Credit Facility (RCF) and a broadly successful Staff Monitored Program (SMP), Madagascar requested a 40-month ECF arrangement in 2016. The purpose of the ECF arrangement was to help reinforce macroeconomic stability and boost sustainable and inclusive growth. Reform objectives closely matched the gaps identified in the previous Article IV surveillance report, including enhancing economic governance and reducing corruption. Box 3 illustrates an evaluation matrix for reforms in this area.

Governance-related conditionality included a comprehensive set of measures to strengthen public financial management (PFM), fight corruption, and reform the legal system (see Annex IV.C). Program approval was subject to a prior action to submit legislation for establishing special anti-corruption centers, strengthening asset declarations, as well as expanding the definition of corruption offenses. Other conditionality was strongly biased toward the governance area and included structural benchmarks to improve PFM and legislative amendments to regulate assets management and public establishments.

The performance of the ECF program has remained generally strong with solid growth and robust external position. Implementation of the structural agenda has been quite good, although capacity constraints posed difficult challenges. On the economic governance side, implementation of PFM reform plans has been broadly satisfactory, including the adoption of the new strategic plan in 2018. Noteworthy progress has been made in recent years in strengthening the anti-corruption framework. Several laws adopted since 2016 helped bring Madagascar's legal framework toward international standards: an anti-corruption law, a law on anti-corruption courts, a law on international cooperation, and a law on Anti-Money-Laundering/Countering Financing of Terrorism (AML/CFT) were adopted by end-2018.[21] Legislative actions were followed by implementation measures, including the opening of the first anti-corruption court in June 2018 and increased budget allocation to the anti-corruption agency.

What are the lessons?

Madagascar's ECF showcases the use of Fund conditionality to achieve progress in a difficult but critical reform area. The ambitious structural reform agenda focused on improving economic governance including reforms on public financial management and AML/CFT. Applying structural conditions on concrete measures ensured Madagascar could achieve solid progress in enhancing governance and fighting corruption. However, successful

[21] However, one important anti-corruption law on asset recovery was not passed.

Box 3. Evaluation Matrix: Madagascar's 2016 40-Month ECF

Criterium		Evaluation
Context	**Macroeconomic context**	**Macroeconomic situation:** Madagascar is a fragile country striving to recover from an extended political crisis and international isolation between 2009 and 2013. At program request, Madagascar has a negative output gap. **Fiscal and monetary policy space:** Limited. **Income level or reform priorities:** Madagascar is a low-income country with weak economic climate in need of quick wins to help build public support for continued reforms.
	Program context	**Surveillance gaps:** The 2014 Article IV surveillance report notes that weak institutions and weak governance eroded the foundation for solid economic growth, with short-term rent-seeking having taken precedence over longer-term nation building. It highlights the need to strengthen the economic climate, including through improving governance. **Program objectives:** One of the main structural reform objectives is enhancing economic governance and fighting corruption. **Program risk:** Significant risks to program success, including political uncertainty and lack of progress to tackle corruption.
Reform interactions	**Packaging**	**Enabling reforms:** The three main areas of PFM reforms, anti-corruption reforms, and AML/CFT reinforce each other in improving economic governance. **Complementary reforms:** Among other, tax and customs administration reform to improve administration and fight corruption; business environment reform to reduce excessive bureaucratic procedures; and public investment and debt management, especially for publicly guaranteed loans and PPP projects.
	Sequencing	**PFM reforms:** (i) reduce administrative discretion; (ii) develop a medium-term PFM strategy and action plan; (iii) reinforce external audits; (iv) strengthen expenditure management on procurement procedures for public entities and SOEs. **Anti-corruption reforms:** (i) drafting and approving new, stronger anti-corruption legislation; (ii) restructuring the public anti-corruption agency; (iii) establishing anti-corruption units at all ministries; (iv) developing an information system that tracks all legal anti-corruption cases; (v) establishing a commission to improve the integrity of the judicial system; (vi) launching of a system for the coordination, monitoring, and evaluation of anti-corruption measures; and (vii) making the Council of Budget and Financial Discipline (CDBF) fully operational. **AML/CFT:** (i) conducting a national risk assessment; (ii) developing an action plan; and (iii) joining the regional Anti-Money Laundering Group.
Reform implementation	**Political economy**	Authorities show high buy-in as they recognize that action is necessary to reverse harmful trends. However, political and institutional constraints limit the scale and pace of some measures.
	Capacity constraints and legal issues	There are significant administrative and institutional capacity constraints, as also indicated by low revenue collection and substantial low-priority spending. Lack of judicial independence allows frequent political interference in the judiciary affairs. Long time lags for enacting legal changes.
	Collaboration	TA provided by World Bank, EU, and AfDB. Close collaboration with the World Bank on improving social sector and PFM efficiency as well as AML/CFT. AfDB provides support on various areas including governance.
Reform impact		**Short-term:** Positive impact on confidence from strengthened governance. **Long-term:** Better economic governance is expected to improve growth and stability, including by attracting private investment. **Inequality:** Mitigating inequality (staff analysis in Selected Issues Paper).

implementation of governance reforms requires the authorities to be fully committed and to cooperate closely with the Fund. Madagascar's case shows that significant achievements can be made—outside the Fund's traditional core area of expertise—even under a difficult political situation, including a political transition and elections.

D. SOE Reforms: The Case of Serbia

State-owned enterprises (SOEs) have a strong presence in many advanced and developing economies, often playing a significant role in addressing market failures and promoting public policies. At the same time, SOEs are often lossmaking and weigh on public finances. For the period 2002 to 2017, Baum and others (2019) find that close to 90 percent of IMF-supported programs included structural conditionality on SOEs. Their empirical analysis shows that governance reforms of SOEs improved the performance and productivity of non-financial SOEs. Serbia's 2015 SBA showcases how comprehensive SOE reforms, focused on reducing state aid to SOEs and resolve loss-making SOEs, contributed to fiscal consolidation and enhancing growth.

What was the scope of the problems?

When the 3-year precautionary SBA was approved in 2015, Serbia's economy faced large fiscal imbalances and protracted structural challenges. One of the main fiscal concern was the rapidly expanding state aid to SOEs. Direct fiscal costs included subsidies, net lending and payments of called guarantees, which amounted to more than 2 percent of GDP in 2014. Losses were concentrated in seven companies, largely in the transportation and energy sectors. Some SOEs caused indirect fiscal costs, including from implicit subsidies on borrowing costs via state guarantees, and arrears to other public enterprises. Some SOEs also ran tax and social contribution arrears.

How were the problems addressed?

Serbia's program focused on strong fiscal consolidation supported by deep reforms of the SOE sector to foster medium-term growth potential and reduce fiscal risks, including through resolving loss-making SOEs (Box 4). The program objectives aligned closely with the reform needs identified in the Article IV surveillance report. Conditionality on SOE reform was comprehensive (Annex IV.D). Over the course of the program, there were six prior actions and fourteen structural benchmarks related to SOE reforms which included the elimination of state aid, strengthening the energy arrears framework, financial restructuring plans, and redundancies.

The program was successfully completed and succeeded in addressing macroeconomic imbalances and restoring fiscal sustainability and growth. Under the program, Serbia made significant progress in implementing SOE reforms to improve their operational viability and contain fiscal risks, while substantially reducing the provision of state aid to those enterprises. Comprehensive financial and corporate restructuring, appropriate regulatory price adjustments, and enhanced revenue collection improved the financial position of critical public network utilities, including Serbia Gas, the electricity generation company EPS, and Railways of Serbia. Also, their operational efficiency improved, and the number of employees was reduced.

However, SOE reforms took time. At the end of the program, many reforms were pending, including in the energy and mining sectors as well as on SOE governance, management and investment. Many SOEs still needed further work until successful resolution or free market viability, especially in the mining and petrochemical sectors. Also, reform implementation was slower than originally envisaged for some SOEs. During the program, some structural benchmarks were met with delays or not met. Therefore, Serbia decided to continue its engagement with the IMF through the Fund's Policy Coordination Instrument (PCI) to support implementation of the remaining reform agenda.

What are the lessons?

Key to success was Serbia's strong ownership, which was pivotal to the implementation of durable fiscal adjustment and the progress on a focused set of structural reforms. This was facilitated by the authorities' strong reform orientation, with important structural reforms in other areas already taken care of before the program approval. Yet, timely implementation of the comprehensive and ambitious SOE reform agenda was a challenge. Serbia needed to build on the achievements of the program, and continue to pursue structural and institutional reforms, including improving SOE governance. Its experience shows the importance of setting realistic targets and timelines and of allowing for some flexibility when implementing an ambitious reform agenda.

Serbia's experience also shows the importance of an enabling environment for deep structural reforms. Complementary measures such as public financial management enhancements, labor market reforms and improving the business environment helped the overall implementation of the SOE reforms, which were further enhanced by close collaboration with the World Bank. Also, maintaining strong macroeconomic policies was a prerequisite to allow these reforms to bear fruit. Relaxation of macroeconomic policies after the successful completion of the adjustment program may have slowed down the reforms and fostered the re-emergence of imbalances.

Box 4. Evaluation Matrix: Serbia 2015 36-Month SBA

Criterium		Evaluation
Context	Macroeconomic context	**Macroeconomic situation:** In addition to protracted structural challenges, the economy was hit by exogenous shocks in 2012 and in 2014. At program request, GDP is still below pre-crisis levels and the output gap is negative. **Fiscal and monetary policy space:** Rising deficits and debt as well as sharply increased gross financing needs require fiscal adjustment, including through SOE reforms. Controlling inflation remains a challenge for Serbia's inflation targeting regime, with tight monetary policy partly offsetting overly loose fiscal policy. Fiscal consolidation with the help of SOE reforms may create room for gradually easing monetary policy. **Income level or reform priorities:** Serbia is an upper-middle income country facing an unfinished reform agenda.
	Program context	**Surveillance gaps:** The 2013 Article IV surveillance report notes the need to reduce excessive state-directed intervention in public enterprises, which strains public finances and crowds out private sector activity. **Program objectives:** Among other, the program aims to reduce fiscal cost of SOEs, improve competitiveness and enhance growth. **Program risk:** Substantial risks to program success, in particular from resistance to deep structural reforms and fiscal cutbacks, delays in SOE resolution, and the negative growth impact of fiscal consolidation.
Reform interactions	Packaging	**Enabling reforms:** (i) Curtailing direct and indirect subsidies, (ii) limiting issuance of new guarantees, and (iii) enhancing accountability, transparency, and monitoring of these enterprises. **Complementary reforms:** The reform agenda contains other measures aimed at sustaining job creation and improving the overall business environment which complement SOE reforms.
	Sequencing	The program will address two groups of SOEs sequentially: • The first group includes over 500 companies in the portfolio of the Privatization Agency, including companies in need of immediate bankruptcy, privatization, and other types of resolution in 2014 and 2015. • The second group comprises large SOEs including the electricity, gas, railways and road companies, where corporate and financial restructuring plans need to be developed over the course of 2015 and implemented in the coming years. This will include legal framework changes, improving collections, increasing efficiency and cost savings, and tariff increases in the period of 2014-17.
Reform implementation	Political economy	The new government is highly committed to implementing deep reforms. However, SOE reforms may be subject to a myriad of political pressures.
	Capacity constraints and legal issues	Some capacity constraints in the PFM area. TA missions were carried out in the areas of PFM, tax administration, and real sector statistics. Legal issues regarding the control of the public sector wage bill including SOE employees need to be resolved, which requires adapting the framework to ensure coverage of all public sector employees and amending the Budget System Law.
	Collaboration	The World Bank is involved in preparing a comprehensive plan to privatize and corporatize SOEs and improve their transparency. The World Bank, EBRD, and EU, are involved in restructuring large public utilities companies.
Reform impact		**Short-term:** Positive. Lower SOE subsidies could alleviate fiscal pressures. **Long-term:** Positive. SOE restructuring will improve fiscal balances and enhance economic efficiency. **Inequality:** Unclear, with elevated inequality and poverty a key concern.

E. Pension Reform: The Case of Georgia

Population aging is a key challenge faced by more and more countries, often putting pressure on pension schemes and public finances. Pension reforms can help to improve the sustainability of the pension system and can also contribute to capital market development, promoting longer working lives, and adjusting social assistance.

Despite aging societies, very few past IMF-supported programs have taken on pension reforms. Out of the 133 IMF-supported programs between 2011 and 2017, just 16 programs included structural conditions on pension reforms. Of those structural conditions, equal shares aimed at reforming the pension system or modifying some parameters of it, with a small portion aiming at both. Georgia's 2017 EFF is among the programs with the highest number of structural conditions, in line with the program's objective of significantly reforming its retirement system.

What was the scope of the problems?

Georgia's 3-year EFF was initiated amid an economic recovery but vulnerabilities from elevated external imbalances and low reserves remained. The 2016 parliamentary elections gave the ruling party a constitutional majority, and the new government united around a policy agenda centered on bolstering growth. As part of its structural reform agenda, the authorities aimed at enhancing the sustainability of the pension system in light of an aging population and shrinking labor force. Together with capital market development, the reforms were also expected to mobilize domestic savings and support private sector investment through creating a contributory pension system (Box 5). These reform objectives were broadly in line with findings of the 2013 Article IV surveillance report.

How were the problems addressed?

In a first step, the authorities committed to submit a pension law establishing the second pillar pension system and to introduce indexation of public pensions by end-2017 (Annex IV.E). To this end, the authorities received technical assistance from the World Bank in June 2017. In subsequent steps during the following reviews, additional structural conditions were set including for establishing an independent pension agency, following the reform sequence established at program initiation. In December 2019, the newly established second pillar of the pension system started collecting contributions. However, there were delays in making Pension Agency fully operational and introducing the indexation of basic pensions. The EFF was extended by one year in December 2019.

What are the lessons?

While the program is ongoing, significant reform delays exemplify the need for realistic timelines and flexibility in program design. While the authorities remained committed to the objectives of the program, momentum slowed. Reform fatigue was already mentioned as one of the program risks at the outset, also given the reform agenda and its timeline was very ambitious.

Box 5. Evaluation Matrix: Georgia's 2017 3-Year EFF

<table>
<tr><th colspan="2">Criterium</th><th>Evaluation</th></tr>
<tr><td rowspan="2">Context</td><td>Macroeconomic context</td><td>Macroeconomic situation: Growth is subdued, partly due to adverse external circumstances.
Fiscal and monetary policy space: There is no fiscal space to support structural reforms, with fiscal consolidation a key objective of the program. Monetary policy has already been loosened, yet inflation is low.
Income level or reform priorities: Georgia is an emerging economy with policy agenda to bolster continued growth.</td></tr>
<tr><td>Program context</td><td>Surveillance gaps: The 2013 Article IV surveillance report notes a need for reforming the social system (universal health care, pension, targeted social assistance and education). It also discusses higher private savings through developing local capital markets and creating a contributory pension system.
Program objectives:
• Fiscal consolidation over the medium term
• Structural reforms aimed at promoting savings, private sector investment, and improved competitiveness
Program risk: Sustained weak domestic demand, in the context of fiscal consolidation and subdued global growth, could weaken the growth outlook. In such an environment, reform fatigue could set in and support for the program could decline.</td></tr>
<tr><td rowspan="2">Reform interactions</td><td>Packaging</td><td>The pension reform is accompanied by a capital market reform.</td></tr>
<tr><td>Sequencing</td><td>In a first step, a law establishing the second pillar pension system will be submitted. In a second step, an independent pension fund agency will be established.</td></tr>
<tr><td rowspan="3">Reform implementation</td><td>Political economy</td><td>High ownership at the outset. Recent parliamentary elections gave the ruling party a constitutional majority, and the new government is united around a policy agenda, including pension reforms.</td></tr>
<tr><td>Capacity constraints and legal issues</td><td>Adequate capacity.</td></tr>
<tr><td>Collaboration</td><td>Technical assistance is provided by the World Bank.</td></tr>
<tr><td colspan="2">Reform impact</td><td>Short-term: None.
Long-term: Positive growth impact. The pension reform is expected to mobilize domestic savings and private investment and deepen domestic capital markets. In addition, the pension reform could improve fiscal sustainability while rule-based indexation for basic pensions can reduce uncertainty.
Inequality: Unclear.</td></tr>
</table>

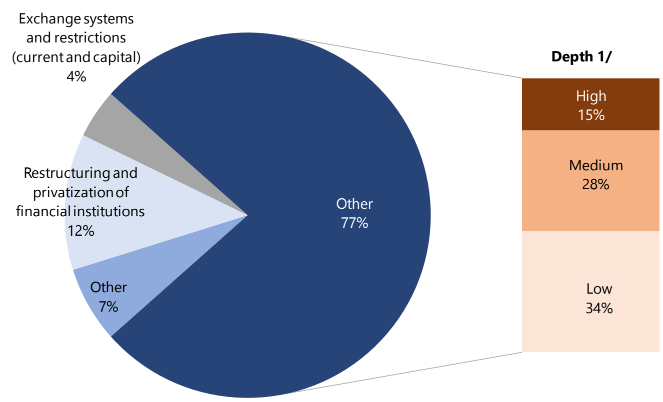
F. Financial Sector Reforms: The Case of Ireland

Structural reforms in the financial sector address impediments to financial intermediation which can result in low investment, misallocation of capital, and vulnerabilities to financial crises. In IMF-supported programs, about one in five structural benchmarks pertain to financial sector issues, with a somewhat lower share in low-income countries. In many cases, financial sector measures are taken in the context of banking crises. This does not mean that structural benchmarks are dominated by bank restructuring measures, given three-quarters of structural benchmarks referred to legal reforms, regulation, and supervision (Figure 11). Most of these reforms are low or medium depth and therefore imply limited lasting effect. There are, however, examples of reforms that result in permanent institutional improvement, such as Ireland's reform of its personal insolvency framework.

What was the scope of the problems?

In the years preceding the outbreak of the Global Financial Crisis, Ireland experienced a booming property market, fueled by a massive credit expansion funded from abroad. When Lehman Brothers fell in September 2008, the repercussions for Irish banks were severe. In addition to liquidity problems, banks suffered from solvency problems in light of the plummeting domestic property market.

Figure 11. Financial Sector Conditions by Type
(Number of structural benchmarks, 2011-17)



1/ High depth indicates permanent institutional change or reforms with long-lasting impact.
Sources: MONA and authors' calculations.

The Irish authorities undertook several bold actions to restore financial stability, including a blanket guarantee scheme, interventions in major banks, and establishment of a state-owned restructuring agency. However, these measures proved insufficient, and Ireland decided to request support from the Fund and Ireland's European partners, with the objective to restore the banking system to health and secure fiscal sustainability.

How were the problems addressed?

To resolve the large number of defaulted mortgages, the program request noted the necessity of substantial reforms of the personal insolvency regime. To this end, the authorities' strategy was to make bankruptcy a more viable option for households with unsustainable debt, yet to rely primarily on less costly out-of-court alternatives (Box 6). This approach could facilitate debt settlements without forced house sales which have negative externalities.

While the need for reform was obvious at the outset, it was decided not to address personal insolvency reform upfront. Due to the weak economy as well as administrative and political constraints, the authorities preferred to push ahead their agenda on mortgage arrear workout in a second phase of the program.

Accordingly, no conditionality was proposed initially, also reflecting the authorities' own efforts in laying out a path toward reform. Conditionality was introduced only in 2011, one year into the program, including developing a reform strategy (Annex IV.F). Subsequently, the personal insolvency bill was developed and passed in 2012. In parallel, preparations started to establish the Insolvency Service which became operational in 2013. These steps were closely aligned with measures to accelerate residential mortgage arrear workout which required increased supervisory pressure.

Only in the last year of the program—once the banking system stabilized, the real estate market bottomed out, and the broader economy started to recover—the authorities decisively pushed toward resolving distressed assets, supported by conditions on supervisory targets for loan resolution and updating impairment guidelines.

What are the lessons?

Several lessons emerge from Ireland's experience. First, design and implementation of deep structural reforms require time and sustained effort. In Ireland's case, finalization of the legal reforms required a public consultation process and lengthy legal refinements. Throughout the program, the supervisor encouraged banks to address the loan workout proactively, yet progress was initially slow. Additional conditionality including on removing procedural impediments to repossession and setting supervisory resolution targets helped crystalize progress. Yet, despite the program's relatively strong commitment to non-performing loan (NPL) reduction, only 17 percent of mortgage NPLs were restructured by the end of the program.

Second, given the sustained effort needed, ownership is of utmost importance to enable strong implementation. In Ireland, historical and political constraints made some options for NPL workout seemingly not viable, including repossessions of a significant number of owner-occupied residences, threatening ownership of these reforms. The Ex Post Evaluation (IMF, 2015) notes that progress was in the end much delayed, although the time was used to build a broader consensus on a restructuring reform strategy.

Third, achieving deep structural reforms can involve trade-offs with other objectives of the program. Ireland's program strategy included giving time to develop a reform strategy which balances the chances of successful implementation with the cost of possibly elevated strategic defaults. Although some delay and temporary forbearance can be justified to reduce household financial distress in the short run, arrears that had built for years without consequence made it later difficult for banks to work out these loans (Andritzky, 2014). However, at the end of the program, an innovative personal insolvency framework had been put in place. This serves the country well in tackling the unfinished mortgage resolution work, notwithstanding that case numbers remain low and legal proceedings continue to be long.

Box 6. Evaluation Matrix: Ireland's 2010 3-Year EFF

Criterium		Evaluation
Context	Macroeconomic context	**Macroeconomic situation:** Large output gap (-6.3 percent) and high and rising unemployment (13.5 percent). **Fiscal and monetary policy space:** Costs of the banking crisis caused a deficit of 32.0 percent (2010f). While the Irish authorities already implemented sizeable fiscal consolidation over 2008–10, further deep fiscal consolidation is considered critical, providing little room for fiscal measures to offset negative impacts from personal insolvency reform. Monetary policy is governed by the ECB. **Income level or reform priorities:** Ireland is an advanced economy with a dynamic economy, efficient institutions, and generally limited reform needs.
	Program context	**Surveillance gaps:** The 2010 Article IV surveillance report focused on banking sector reforms and fiscal consolidation. It noted fears that homeowner distress may be the biggest legacy of the crisis. **Program objectives:** • Restoring the banking system to health • Underpinning fiscal sustainability • Securing sustainable economic growth through structural reforms **Conditionality:** Conditionality focused on shoring up confidence in the short run and strengthening the policy framework in the medium term. **Program risk:** Substantial execution risks given the extreme technical delicacy of the many tasks.
Reform interactions	Packaging	**Enabling reforms:** Personal insolvency reform is facilitated by: • Reforms to enable banks' NPL workouts by ensuring appropriately prudent provisioning treatment of loan modifications; • Supervisory pressure to ensure timely workout via mortgage workout schemes; • Reforms to facilitate court-based repossession procedures; and • Reforms to adjust excessively strong protections for debtors. **Complementary reforms:** To soften undue hardship of debtors, the mortgage subsidy scheme is extended, and the new Mortgage Advisory Service offers debtors a free consultation.
	Sequencing	Personal insolvency reform is a second step after stabilizing the banking system. As part of bank restructuring, measures to improve transparency of asset quality help to estimate the possible impact of the reform, and bank recapitalization provides the buffers for banks to offer loan workouts. Implementing personal insolvency reform requires first the completion of the Enactment of Personal Insolvency Bill, including an extensive public consultation process. Subsequently, the new framework is operationalized, including licensing Personal Insolvency Practitioners and establishing the Insolvency Service.

Box 6. Evaluation Matrix: Ireland's 2010 3-year EFF (concluded)

Reform implementation	**Political economy**	Traditionally strong social partnership is being tested by deep fiscal consolidation and already high public costs of bank restructuring. While there is strong ownership across the political spectrum, there is a likely change in government following elections in the program's first year. The difficult political economy of mortgage debt workout, given (i) the primacy of private property rooted in Ireland's history, creating hostility against workouts involving repossession, and (ii) a very negative popular sentiment toward banks, which were seen as culprits for Ireland's crisis, may require time to improve sentiment and build broader social consensus on private insolvency reform.
	Capacity constraints and legal issues	Administrative capacity limits given the program's already heavy legislative burden. Court capacity to handle repossessions is overstretched. Legal issues from debtor protections being strongly defended by courts.
	Collaboration	Close collaboration with the authorities and others in identifying solutions jointly as there is limited international best practice to household insolvency.
Reform impact		**Short-term:** Overall neutral on growth. The reform strives to protect creditors' rights as well as debt-servicing discipline while safeguarding reasonable standards of living for the debtors. **Long-term:** Positive for the recovery by restoring prospects for credit growth. **Inequality:** Neutral. The reform affects a limited number of households with debt servicing problems while safeguarding reasonable standards of living. However, the reform may be perceived as hurting those with debt servicing problems, in particular the unemployed.

G. Energy Reforms: The Case of Jordan

Energy reforms can be critical for program success, as energy subsidies can weigh on fiscal balances and public debt, discourage investment in the energy sector, and diminish the competitiveness of the private sector (Clements and others, 2013). Programs that aim at energy reforms often start out with developing a comprehensive energy sector strategy, involving extensive consultation with stakeholders, and include well-targeted measures to protect the poor and vulnerable when scaling back subsidies or adjusting prices. Institutional reforms, such as the introduction of automatic pricing mechanisms, can help to depoliticize energy pricing. Conditionality in this area can not only include structural conditions but also quantitative conditionality, depending on the circumstances. Jordan presents an interesting example of long-standing attempts at energy reform, in particular during Jordan's 2016 EFF arrangement.

What was the scope of the problems?

Jordan achieved substantial progress in strengthening its fiscal and external positions after completing a three-year SBA initiated in 2012. During this program, large fiscal adjustment was facilitated through the implementation of ambitious fuel subsidy and electricity sector reforms which phased out electricity and natural gas subsidies. Suffering another external shock from declining external demand and the influx of refugees in 2016, the authorities requested a three-year EFF to reduce balance of payments vulnerabilities, strengthen international reserves, and further the implementation of Georgia's structural reform agenda.

One of its main challenges was to continue the energy reform in the electricity and water sectors, as sizeable cross-subsidies from large industrial consumers to households remained. In addition, central government transfers to the electricity and water companies remained very large, reaching 6.2 and 0.8 percent of GDP in 2014, respectively.

How were the problems addressed?

One of the key objectives of the program was gradual fiscal consolidation to bring public debt down while protecting the poor. Reforms of the energy sector were a key contributor to this end (Box 7). To move the electricity company to operational cost recovery, measures were taken to diversify the energy mix further toward cheaper sources and explore options for reducing cross-subsidization. Phasing in an automatic tariff adjustment mechanism required measures to protect poor households from higher electricity tariffs. In the water sector, it was essential to reduce water sector losses and consolidate the finances of the water company.

To achieve this ambitious reform agenda, energy reform was underpinned by extensive program conditionality (Annex IV.F). The program request included two prior actions and three structural benchmarks on energy reforms, and two indicative targets on arrears to utilities companies. The second review added two additional conditions on energy companies to improve PFM and transparency.

Overall program implementation was mixed. Energy reforms made progress mainly at the start of the program, with overperforming electricity and water utilities in the first review. While energy reform indicative targets were met, slippages in the implementation of critical reforms appeared. Misses of fiscal and reserves targets in 2018 delayed the completion of the second review amid deteriorating external conditions that included regional conflicts, refugee immigration, disruption of critical export markets, and rising borrowing costs. Subsequently, no reviews were completed. Jordan requested a new four-year EFF in 2020. In the area of energy reform, the 2020 EFF largely reinstated previous reform intentions, including reduced electricity prices for businesses to improve competitiveness, together with development of a plan to reduce production costs and direct households' subsidies only to those who need it.

What are the lessons?

Difficult energy reforms require strong commitment and persistent effort. After a long period of failed reform attempts in the early 2000s, Jordan made steady progress in energy reforms during the last decade. This included efforts to eliminate fuel subsidies in 2012, adopting a monthly fuel price adjustment system in 2013, diversifying energy sources for electricity in 2015, and furthering cost recovery reforms for electricity and water sectors.

Yet, persistent reform effort is harder to sustain if the economic and political environment is uncertain. In Jordan, widespread protests over rising fuel and electricity prices and the submission of the income-tax law resulted in resignation of the Prime Minister in 2018. In response, the electricity tariff increase was put on hold resulting in operational losses of the electricity company. This experience reiterates the importance of a gradual approach based on a clear strategy that includes prior introduction of well-targeted mitigating measures for adversely affected groups (Clements and others, 2013).

Box 7. Evaluation Matrix: Jordan's 2016 3-Year EFF

Criterium		Evaluation
Context	Macroeconomic context	**Macroeconomic situation:** While the economic situation stabilized, Jordan's economy faces considerable challenges including from hosting refugees, low growth, and high unemployment, with a negative output gap. **Fiscal and monetary policy space:** Further consolidation needed to contain public debt and financing needs against the backdrop of higher-than-expected fiscal deficits, also reflecting the performance of SOEs in the water and electricity sectors. However, there is a need to allocate budgetary resources to help finance the water company's capital expenditures (about 1 percent of GDP per year). The monetary policy stance is already accommodative amid low inflation. **Income level or reform priorities:** Jordan is a middle-income country with vulnerabilities highlighting the need to further structural reforms.
	Program context	**Surveillance gaps:** Continued implementation of energy reforms (electricity and water sectors) was identified as necessary to return the utilities to cost recovery (2014 Article IV surveillance report). Strengthening the finances of public utilities requires increases in tariffs and efficiency, diversification in energy sources, and developing strategies. **Program objectives:** Among other, ensuring sustainability of the electricity and water sectors and improving fiscal sustainability. **Program risk:** Significant risks to structural reforms, including from difficult socio-economic conditions, technical capacity limits, shortfalls in financing, and unfavorable external developments.
Reform interactions	Packaging	Complementary structural reforms include measures to increase labor force participation, protect social spending, and enhance governance.
	Sequencing	**Electricity sector:** In parallel to implementing the strategy to diversify the energy mix further toward cheaper sources, the reform sequence includes: • Carry out a study on cross-subsidization; • Announce and implement an automatic tariff adjustment mechanism; • Prepare a financial plan to reduce the electricity company's debt; • Prepare a comprehensive study to improve the overall tariff structure; • Pass a comprehensive energy-reform plan for medium-term sustainability. **Water sector:** • Recalibrate the water company's debt strategy and investment plan in response to risks, including higher energy prices and refugee migration, and allocate budgetary resources to the water company accordingly; • Adopt and publish an updated action plan to reduce water sector losses; • Implement the cost-reducing and revenue-enhancing measures.

Box 7. Evaluation Matrix: Jordan's 2016 3-Year EFF (concluded)

Reform implementation	**Political economy**	The transition government is committed to implementing policies and reforms. (However, a new government was formed following widespread protests over rising fuel and electricity prices and the delayed income-tax law in 2018. Complex socio-political challenges including corruption added to public discontent and eroded support for politically difficult reforms.)
	Capacity constraints and legal issues	The authorities need to enhance capacity of debt and public financial management of the central government and its agencies, including the National Electric Power Company and the Water Authority of Jordan. Technical assistance to be delivered by the IMF, the World Bank, and the U.S. Treasury.
	Collaboration	The World Bank provided support on energy reform and policy advice on social measures to alleviate the impact of this reform on the most vulnerable. The implementation of the tariff adjustment mechanism is monitored by the World Bank and Japan's International Cooperation Agency.
Reform impact		**Short-term:** Mixed impact. While the energy reform can facilitate fiscal consolidation, social resistance could endanger macroeconomic stability. **Long-term:** Positive growth impact from improved energy and fiscal sustainability. **Inequality:** Possible large impact depending on offsetting measures.

V. Conclusions

In recent years, IMF-supported programs increasingly faced situations dominated by structural challenges. While this paper finds an increased focus on structural policies in Fund arrangements, efforts toward transformational reforms as part of IMF-supported programs often remains unsuccessful. Improving conditionality design could help to achieve more impactful reforms.

Complementing the recommendations of the 2018 Review of Conditionality (IMF 2019a), this paper identifies ways that could improve the chances of successful structural reform during IMF-supported programs. *First*, parsimony in conditionality design commands program objectives to be more specific which helps to identify the most critical reforms to achieve them. *Second*, Fund expertise could be expanded and Fund policies and practices could be adjusted to ensure structural conditionality focuses on key macro-structural weaknesses, particularly in areas such as labor and product markets, which could make countries more resilient against future shocks. *Third*, a systematic evaluation of reform options in IMF-supported programs could improve reform prioritization and increase reform success. While Fund staff implicitly takes some of these aspects into account, a more systematic evaluation of reform designs and options would improve staff's ability to rigorously identify, package and sequence structural reforms and ensure that chosen measures have tangible impact. Laying out these considerations in Fund staff reports as well as in Ex-Post Evaluations would also improve transparency and accountability.

This paper therefore proposes a new tool for evaluating structural reform options. The evaluation matrix provides a short summary of the most pertinent considerations in reform design, including the macroeconomic and program context, packaging and sequencing of reforms, implementation hurdles including political aspects and capacity constraints, and the reforms' macroeconomic impact. Applied to seven case studies, the evaluation matrix reveals pressure points that often emerge in reform implementation: the difficulty of implementing reforms when there is no space for offsetting macro policies, the extensive time needed to properly sequence reforms and accommodate reform delays, including due to capacity constraints, and the reforms' limited macroeconomic impact during the program horizon. Taking time to evaluate reform options and laying out the considerations can help in building consensus, thereby boosting ownership, and arrive at realistic reform designs addressing key structural weaknesses.

ANNEX I. GLOSSARY

Article IV: Country surveillance is a process that culminates in regular (usually annual) consultations with individual member countries. The consultations are known as "Article IV consultations" given their legal foundations in Article IV of the IMF's Articles of Agreement. During an Article IV consultation, an IMF team of economists assesses the country's economic and financial developments and discusses economic and financial policies with government and central bank officials as well as parliamentarians, the private sector, and representatives of labor unions and civil society.

Core areas of responsibility: The 2002 "Guidelines on Conditionality and associated Operational Guidance to Staff" defines the Fund's core areas of responsibility as "macroeconomic stabilization; monetary, fiscal, and exchange rate policies, including the underlying institutional arrangements and closely related structural measures; and financial system issues related to the functioning of both domestic and international financial markets" (IMF, 2002).

Criticality: Conditions are established only on the basis of those variables or measures that are reasonably within the member's direct or indirect control and that are, generally, either (i) of critical importance for achieving the goals of the member's program or for monitoring the implementation of the program, or (ii) necessary for the implementation of specific provisions of the IMF's Articles of Agreement or policies adopted under them.

Extended Credit Facility (ECF): The Extended Credit Facility provides financial assistance to countries with protracted balance of payments problems. The ECF was created under the Poverty Reduction and Growth Trust (PRGT) as part of a broader reform to make the Fund's financial support more flexible and better tailored to the diverse needs of low-income countries (LICs), including in times of crisis. The ECF is the Fund's main tool for providing medium-term support to LICs.

Extended Fund Facility (EFF): When a country faces serious medium-term balance of payments problems because of structural weaknesses that require time to address, the IMF can assist with the adjustment process under an Extended Fund Facility. Compared to assistance provided under the Stand-by Arrangement, assistance under an extended arrangement features longer program engagement—to help countries implement medium-term structural reforms—and a longer repayment period.

General Resources Account (GRA) arrangement: General Resources Account arrangements comprise a variety of lending programs with different disbursement schedules and maturities depending on the balance of payment needs of the member. All IMF members can draw under GRA facilities.

IMF-supported program: Countries facing difficult economic conditions may request financial support and policy advice from the IMF. The financial support provided by the IMF helps the country with its most immediate macroeconomic problems, and the government's economic policy program aims to restore financial stability while laying the foundations for strong economic growth. While the effects of an economic or financial crisis are felt immediately and can last many months, the results of remedial actions may take longer to materialize.

Monitoring of Fund Arrangements (MONA): The Monitoring of Fund Arrangements database contains comparable information on the economic objectives and outcomes in Fund-supported arrangements. It tracks the performance of countries in terms of scheduled purchases and reviews, quantitative and structural conditionality, and macroeconomic indicators. Data are available for most arrangements since 2002 and are collected at the time of arrangement approval and following each review.

Parsimony: Parsimony means that program-related conditions should be limited to the minimum necessary to achieve the goals of the Fund-supported program or to monitor its implementation and that the choice of conditions should be clearly focused on those goals.

Poverty Reduction Growth Trust (PRGT) arrangement: Poverty Reduction Growth Trust arrangements represent lending programs providing concessional financing support to low-income countries.

Prior action: Prior actions are measures that a country agrees to take before the IMF’s Executive Board approves financing or completes a review. They ensure that the program has the necessary foundation to succeed or is put back on track following deviations from agreed policies. Examples include the elimination of price controls or formal approval of a budget consistent with the program’s fiscal framework.

Review of Conditionality: Conditionality is reviewed regularly by the Fund as part of its effort to assess its policies and adapt them to a changing environment. The latest review commenced in 2018 and was concluded in 2019 (IMF, 2019a).

Standby Credit Facility (SCF): Arrangements under the Standby Credit Facility provides financial assistance to low-income countries (LICs) with short-term balance of payments needs. The SCF was created under the PRGT as part of a broader reform to make the Fund’s financial support more flexible and better tailored to the diverse needs of LICs, including in times of shocks or crisis.

Stand-By-Arrangement (SBA): In an economic crisis, countries often need financing to help them overcome their balance of payments problems. Since its creation in June 1952, the IMF’s Stand-By Arrangement has been used time and again by member countries, and it is the IMF’s workhorse lending instrument for emerging and advanced market countries. The SBA was upgraded in 2009 along with the Fund’s broader toolkit to be more flexible and responsive to member countries’ needs. Conditions were streamlined and simplified, and more funds were made available up front, as borrowing limits were doubled in response to the Global Financial Crisis. These limits were increased further in 2016. The new framework also enables broader high-access borrowing on a precautionary basis.

Structural conditionality: When a country borrows from the IMF, its government agrees to adjust its economic policies to overcome the problems that led it to seek financial aid from the international community. These loan conditions also serve to ensure that the country will be able to repay the Fund so that the resources can be made available to other members in need. Lending reforms approved in 2009 streamlined IMF conditionality in order to promote national ownership of strong and effective policies.

Structural benchmarks: Structural benchmarks are (often non-quantifiable) reform measures that are critical to achieve program goals and are intended as markers to assess program implementation during a review. They vary across programs: examples are measures to improve financial sector operations, build social safety nets, or strengthen public financial management.

Surveillance: A core responsibility of the IMF is to oversee the international monetary system and monitor the economic and financial policies of its 189 member countries, an activity known as surveillance. As part of this process, which takes place at the global, regional, and country levels, the IMF identifies potential risks to stability and recommends appropriate policy adjustments needed to sustain economic growth and promote financial and economic stability.

ANNEX II. SAMPLE CHARACTERISTICS

Table 1. 2018 RoC Sample

Post-GFC (39 programs)		
Country and arrangement type and approval date		
Albania	EFF	2014
Antigua and Barbuda	SBA	2010
Armenia	ECF-EFF	2010
Armenia	EFF	2014
Bosnia and Herzegovina	SBA	2009
Bosnia and Herzegovina	SBA	2012
Bosnia and Herzegovina	EFF	2016
Cyprus	EFF	2013
Dominican Republic	SBA	2009
El Salvador	SBA	2010
Georgia	SBA-SCF	2012
Georgia	SBA	2014
Georgia	EFF	2017
Greece	SBA	2010
Greece	EFF	2012
Ireland	EFF	2010
Jamaica	SBA	2010
Jamaica	EFF	2013
Jamaica	SBA	2016
Kosovo, Rep. of	SBA	2010
Kosovo, Rep. of	SBA	2012
Kosovo, Rep. of	SBA	2015
Latvia	SBA	2008
Macedonia, FYR	PCL	2011
Maldives	SBA	2009
MOLDOVA	ECF-EFF	2010
MOLDOVA	ECF-EFF	2016
Pakistan	EFF	2013
Portugal	EFF	2011
Romania	SBA	2011
Romania	SBA	2013
Serbia, Rep. of	SBA	2011
Serbia, Rep. of	SBA	2015
Seychelles	EFF	2009
Seychelles	EFF	2014
Seychelles	PCI	2017
Sri Lanka	SBA	2009
Sri Lanka	EFF	2016
St. Kitts and Nevis	SBA	2011

Political transformation (14 programs)		
Country and arrangement type and approval date		
Central African Rep.	ECF	2016
Cote d'Ivoire	ECF	2011
Egypt	EFF	2016
Jordan	SBA	2012
Jordan	EFF	2016
Morocco	PLL	2012
Morocco	PLL	2014
Morocco	PLL	2016
Tunisia	SBA	2013
Tunisia	EFF	2016
Ukraine	SBA	2010
Ukraine	SBA	2014
Ukraine	EFF	2015
Yemen, Rep. of	ECF	2014

Commodity exporters (19 programs)		
Country and arrangement type and approv		
Angola	SBA	2009
Burkina Faso	ECF	2010
Burkina Faso	ECF	2013
Chad	ECF	2014
Chad	ECF	2017
Congo, Dem. Rep. of	PRGF	2009
Gabon	EFF	2017
Guinea	ECF	2012
Guinea	ECF	2017
Guinea-Bissau	ECF	2010
Guinea-Bissau	ECF	2015
Iraq	SBA	2010
Iraq	SBA	2016
Mali	ECF	2013
Mauritania	ECF	2017
Mongolia	EFF	2017
Sierra Leone	ECF	2013
Sierra Leone	ECF	2017
Suriname	SBA	2016

Other developing (61 programs)		
Country and arrangement type and approval date		
Afghanistan, Islamic Rep. of	ECF	2011
Afghanistan, Islamic Rep. of	ECF	2016
Bangladesh	ECF	2012
Benin	ECF	2010
Benin	ECF	2017
Burundi	PRGF	2008
Burundi	ECF	2012
Cameroon	ECF	2017
Cape Verde	PSI	2010
Central African Rep.	ECF	2012
Comoros	PRGF	2009
Cote d'Ivoire	ECF-EFF	2016
Djibouti	PRGF	2008
Gambia, The	ECF	2012
Ghana	PRGF	2009
Ghana	ECF	2015
Grenada	ECF	2010
Grenada	ECF	2014
Haiti	ECF	2010
Haiti	ECF	2015
Honduras	SBA-SCF	2010
Honduras	SBA-SCF	2014
Kenya	ECF	2011
Kenya	SBA-SCF	2015
Kenya	SBA-SCF	2016
Kyrgyz Rep.	ECF	2011
Kyrgyz Rep.	ECF	2015
Lesotho	ECF	2010
Liberia	PRGF-EFF	2008
Liberia	ECF	2012
Madagascar	ECF	2016
Malawi	ECF	2010
Malawi	ECF	2012
Mali	PRGF	2008
Mali	ECF	2011
Mauritania	ECF	2010
Mozambique	PSI	2010
Mozambique	PSI	2013
Mozambique	SCF	2015
Niger	ECF	2012
Niger	ECF	2017
Rwanda	PSI	2010
Rwanda	PSI	2013
Rwanda	SCF	2016
Sao Tome and Principe	PRGF	2009
Sao Tome and Principe	ECF	2012
Sao Tome and Principe	ECF	2015
Senegal	PSI	2010
Senegal	PSI	2015
Sierra Leone	ECF	2010
Solomon Islands	SCF	2010
Solomon Islands	SCF	2011
Solomon Islands	ECF	2012
Tajikistan	PRGF	2009
Tanzania	PSI	2010
Tanzania	SCF	2012
Tanzania	PSI	2014
Togo	ECF	2017
Uganda	PSI	2010
Uganda	PSI	2013
Yemen, Rep. of	ECF	2010

Table 2. 2018 RoC Sample and Subsample Composition

		2018 RoC sample (Percent of total)	Subsample (Percent of total)
By analytical group	Post-GFC	29.3	30.8
	Political/economic transformation	10.5	7.7
	Commodity exporters	14.3	7.7
	Other developing	45.9	53.8
By arrangement/ instrument	Extended Credit Facility	35.3	46.2
	Extended Credit Facility/Extended Fund Facility blend	3.0	0.0
	Extended Fund Facility	14.3	15.4
	Policy Coordination Instrument	0.8	0.0
	Precautionary Credit Line	0.8	0.0
	Precautionary and Liquidity Line	2.3	0.0
	Poverty Reduction and Growth Facility	6.0	0.0
	Poverty Reduction and Growth Facility/Extended Fund Facility blend	0.8	0.0
	Policy Support Instrument	8.3	7.7
	Stand-By Arrangement	20.3	23.1
	Stand-By Arrangement/Exogenous Shocks Facility blend	0.8	0.0
	Stand-By Arrangement/Standby Credit Facility blend	3.8	7.7
	Standby Credit Facility	3.8	0.0
By region	Africa	47.4	46.2
	Asia and Pacific	6.8	7.7
	Europe	18.8	15.4
	Middle East and Central Asia	16.5	23.1
	Western Hemisphere	10.5	7.7

Source: Authors' calculations.

ANNEX III. CLASSIFICATION OF STRUCTURAL CONDITIONS

structural conditions are classified by category and area of Fund responsibility (Table 4). The categories are mapped into areas of Fund responsibility, distinguishing areas of the Fund's core (or traditional) responsibility, areas where responsibility is shared with other institutions, and non-core areas.

Table 3. Classification of Structural Conditions by Area

Category	Description
Fiscal	Revenue administration (incl. customs) Expenditure measures (incl. arrears clearance) Debt management
PFM/RA	Revenue measures Budget preparations Expenditure auditing Fiscal transparency Inter-governmental relations
Central bank	Central bank operations, auditing, transparency, and financial controls Exchange systems and restrictions
Financial sector	Financial sector legal reforms, regulation, and supervision Restructuring and privatization of financial institutions
Pension & civil service reform	Pension reform Health and education sector reforms Civil service and public employment reforms, including wages PRSP development and implementation
SOE reform	Public enterprise reform (excl. financial sector) Public enterprise pricing and subsidies Privatization
Social	Other social sector reforms
Other macro-structural	Labor Market Reforms (excl. public sector) Product Market Reforms (excl. financial sector) International trade policy (excl. customs) Statistics Governance, incl. corruption Natural resource and agricultural policies (excl. public enterprises and pricing)

Sources: Authors.
Note: Font color indicates area of expertise: core, shared, non-core.

ANNEX IV. STRUCTURAL BENCHMARKS OF CASE STUDIES

A. Latvia: Labor Market Reforms

Initial program period: 23 December 2008 to 22 March 2011.

Timeline	***Condition***	***Initial test date***
Program request	Establishment of a committee to promote wage restraint.	Jan 2009
1st review	Reform of the Committee to Promote Wage Restraint by involving the social partners and outside labor market experts.	Aug 2009
2nd review	Prepare a comprehensive report on proposed revisions to the public-sector wage grid and the relative wage adjustment across public institutions since end-December.	Oct 2009
4th review	Preparation of an active labor market policy strategy to replace Latvia's Public Works Program.	Nov 2011

Source: MONA.

B. Portugal: Product Market Reforms

Initial program period: 20 May 2011 to 19 May 2014.

Timeline	***Condition***	***Initial test date***
Program request	Amend the Insolvency Law to better facilitate effective rescue of viable firms and support rehabilitation of financially responsible individuals.	Dec 2011
	Review the Code of Civil Procedure and prepare a proposal addressing the key areas for refinement.	Dec 2011
	Submit to Parliament legislation revising the Competition Law, making it as autonomous as possible from the Administrative Law and the Penal Procedural Law and more harmonized with the European Union competition legal framework.	Jan 2012
3rd review	Make effective the amendments to the Corporate Insolvency Law to better support rescue of viable firms (after completing all necessary legislative and publication requirements).	Jun 2012
	Prepare a proposal to implement identified best international practices in order to reinforce the independence of the main sectoral regulators.	Sep 2012
	Submit to Parliament amendments to the Code of Civil Procedure to streamline and speed up the court procedures.	Nov 2012

Source: MONA.

C. Madagascar: Governance Reforms

Initial program period: 27 Jul 2016 to 26 Nov 2019.

Timeline	*Condition*	*Initial test date*
Program request	Submission to Parliament of draft laws (i) establishing special anti-corruption centers that ensures the operational independence of each center and establishes an independent committee at each center that is responsible for staff recruitment and management, supervision, monitoring, and evaluation of the center activities; and (ii) strengthening asset declarations and their use, as well as expanding the definition of corruption offenses.	Prior action
	The terms and conditions of all PPP contracts will be published within one month of the date of signature on ARMP's web site.	continuous
	Prior notification of World Bank and IMF staff of any exceptions (such as emergencies) allowing for single source procurement contracts for JIRAMA's purchases of electricity and purchases and rentals of generators.	continuous
	Make the Council of Budget and Financial Discipline (CDBF) operational by issuing a decree, appointing its staff, and publishing its disciplinary decisions.	Sep 2016
	Submission to Parliament of the law regulating the collection, administration, and management of assets that have been seized because of investigations related to corruption, embezzlement, money laundering, financing of terrorism, or organized international criminal activities, in line with the relevant FATF recommendations.	Oct 2016
	Publication and submission of the 2015 financial statements of ten large SOEs to the Court of Auditors: Air Madagascar, FANALAMANGA, CEM, ARO, ADEMA, SOAVOANIO, SPAT, SMMC, SONAPAR, and SEIMAD.	Dec 2016
1st review	Submit draft law on asset recovery, that is consistent with all FATF recommendations, to parliament.	Prior action
	Extend performance contracts to the anti-fraud service (in charge of ex post inspections) at customs.	Sep 2017
	Revise and submit to Parliament the law governing the National Public Establishments (Etablissements Publics Nationaux, EPN).	Jun 2018
2nd review	Start the process of publishing, including providing searchable internet access (using the criteria of topics and presiding judges), of all final court decisions by the anticorruption centers.	Sep 2018
4th review	Establish a public registry of companies that have violated the procurement regulations and are prohibited from participating in future bids.	Aug 2019

Source: MONA.

In addition, there are seven structural benchmarks related to economic governance including improving transparency of contracts and financial statements, budget and financial discipline, law of regulating assets management, law of governing the public establishments, registry of companies which violated the procurement regulations. There are two continuous benchmarks to publish terms and conditions of PPP contracts and notification regarding certain single source procurement contracts.

D. Serbia: SOE Reforms

Initial program period: 23 Feb 2015 to 22 Feb 2018.

Type	*Condition*	*Initial test date*
Program request	Elimination of state aid—including budget subsidies, government guarantees, lending from the budget, or any other forms of public support—to steel producer Zelezara Smederovo and preventing accumulation of arrears by this company.	Prior action
	Adoption by the Government of a financial restructuring plan for EPS (Serbia Electricity).	Mar 2015
	Adoption by the Government of a corporate and financial restructuring plan for Railways of Serbia, to be prepared by an independent consultant.	Sep 2015
	Adoption by the Government of a financial restructuring plan for Srbijagas, to be prepared by an independent consultant.	Oct 2015
1st review	Submission to the Energy Agency of the Republic of Serbia a request to increase the regulated electricity tariff by 4.5 percent, to be effective from August 1.	Prior action
	Adoption of the EPS financial restructuring plan by the Government.	Prior action
2nd review	Amendment to the EPS collective agreement to allow for the implementation of the rightsizing identified in the restructuring plans.	Dec 2015
	Resolution through either privatization or bankruptcy of at least 7 of the 17 strategically important companies that received protection from debt enforcement until May 2016.	May 2016
3rd review	Finalize the terms of reference for hiring an independent audit firm to establish a credible baseline for the financial position of Srbijagas.	Prior action
	Adoption by the Government Steering Committee of a decision on net employment reduction in 2016 of at least 2700 employees in Railways of Srbija.	Mar 2016
	Resolution through either privatization of or initiation of bankruptcy procedures for the remainder of 17 strategically important companies that received protection from debt enforcement until May 2016.	May 2016
4th/5th review	Adoption by the EPS supervisory board, in consultation with World Bank, of a credible 2016-19 optimization plan with no less than 1,000 net staff position reduction in 2016.	Prior action
	Adopt, in consultation with World Bank, debt restructuring plan for Srbijagas.	Oct 2016
	Complete special diagnostic review of Dunav Osiguranje.	Nov 2016
8th review	Launch of privatization tender for MSK privatization.	Prior action

Source: MONA.

In addition, there were related prior actions and structural benchmarks including on amendments of the corporate insolvency law, full registry of public employees, law on transactions between public entities, resolution through privatization or bankruptcy procedures, and employment reduction.

E. Georgia: Pension Reform

Initial program period: 12 April 2017 to 11 April 2020.

Timeline	***Condition***	***Initial test date***
Program request	Submission of a pension law establishing a 2nd pillar pension system and introducing indexation of public pensions.	Dec 2017
1st review	Establishing an independent pension agency.	Jul 2018
2nd review	In consultation with the IMF, we will submit to Parliament legislation proposing a rule-based mechanism to index basic pensions.	Dec 2019

Source: MONA.

F. Ireland: Financial Sector Reforms

Initial program period: 16 December 2010 to 15 December 2013.

Timeline	***Condition***	***Initial test date***
3rd review	Finalize a strategy to guide the development of broader legal reforms around personal insolvency, including significant amendments to the Bankruptcy Act 1998 and the creation of a new structured non-judicial debt settlement and enforcement system.	Dec 2011

Source: MONA.

G. Jordan: Energy Reforms

Initial program period: 24 August 2016 to 23 August 2019.

Timeline	***Condition***	***Initial test date***
Program request	Indicative targets on domestic payment arrears of National Electric Power Company (NEPCO) and Water Authority of Jordan (WAJ).	continuous
	Prepare detailed quarterly financing plan for next 12 months in coordination with NEPCO and WAJ.	Prior action
	Announce the government’s commitment to maintain NEPCO at operational balance during the program period and over the medium term and to adopt by mid-December 2016, and start implementing on January 1, 2017, an automatic electricity tariff adjustment mechanism.	Prior action
	Publish studies on cross-subsidization and options for price adjustments in response to oil price changes.	Sep 2016
	Adopt an automatic electricity tariff adjustment mechanism, with effective implementation on January 1, 2017.	Dec 2016
	Submission to Cabinet and publication of an updated action plan on how to reduce the water sector’s losses over the medium term.	Dec 2016
2nd review	Approval by cabinet of a comprehensive energy-reform plan that ensures NEPCO’s medium-term sustainability and gradually phases out cross-subsidies; with initial implementation to include upfront revenue and cost-savings measures that prevent further losses in 2019.	Prior action
	Transfer the Water Authority of Jordan to the 2020 general budget law.	Nov 2019

Source: MONA.

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