

COUNTRY PROFILES

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BANGLADESH

Political Context

A notable feature of Bangladesh's first ESAF program in 1990 was that it coincided with the end of military rule under President Ershad. A spate of domestic violence and demonstrations against the Ershad government led to the dissolution of Parliament in 1987, and thereafter, to elections in 1991 which brought to power Prime Minister Begum Khaleda Zia, leader of the Bangladesh National Party and widow of General Ershad's predecessor, General Zia-ur-Rahman. Given the extreme polarization that has characterized politics in Bangladesh, the process of liberalization meant that from the beginning, the government's commitment to the ESAF program would almost certainly be made subject to the demands of political expediency. Even so, the Zia government affirmed its commitment to the program signed in 1990 by the previous government. But this commitment to the program was soon put to the test as political tensions failed to subside. Violent demonstrations led by the opposition Awami League resulted in fresh elections in 1996 which brought into power a government of the Awami League, under the leadership of Sheikh Hasina.

Thus, the performance of the ESAF in Bangladesh must be evaluated against the background of a political environment dominated by extreme polarization and a continuing quest for a balance between the need for economic liberalization and the challenges of democratic governance. Indeed, even under the Ershad government, there had been periodic political protest which, in some instances, had led to policy reversals.³² The Zia government had endeavored, against difficult odds, to maintain the momentum of the ESAF program by, for instance, rejecting recommendations of a Wage and Productivity Commission to raise wages by a magnitude which it considered incompatible with proper fiscal management. It is interesting to contrast this posture with the stance of the present government in relation to similar pressures for wage increases.³³

³² A Fund mission reported in 1987 that "under sustained pressure from the opposition, including a series of demonstrations and strikes, the government felt compelled in July to withdraw some of the revenue measures introduced in the 1987/88 budget."

³³ On October 6, 1997, the Cabinet approved the national pay scale increases recommended by the secretary committee, formed to review the recommendations of the 5th National Pay Commission. The scale, containing 20 grades, will be implemented in the next three years; what is significant about this measure is that the government has chosen to fix the lowest pay at 86.48 percent of the recommended amount (the highest-ever increase) compared to 75 percent of the amount recommended by the 4th Pay Commission, and 75.75 percent of the pay recommended by the 3rd Pay Commission in 1984. (*The Daily Star*, Dhaka, October 7, 1997, pp. 1, 12) This announcement about pay increases coincided with the Bank's release of its October 1997 draft report on

Consensus-Building

Given Bangladesh's long tradition of political polarization and a fairly active culture of civic protest, the process of consensus-building is naturally a difficult one. What this means is that support for a program under the ESAF, with its obvious distributional implications and difficult political choices, can at best be somewhat tentative. In these circumstances, the personality of key figures in the reform process, particularly the Minister of Finance, has tended to be an important factor in the success or failure of the program and not unnaturally, the former Minister of Finance, Saifur Rahman, who held the position for a relatively protracted period, came to be perceived as the very embodiment of the program. To be sure, this is not a particularly Bangladeshi phenomenon. Ministers of Finance everywhere are always the object of public ire. But in Bangladesh, with its high incidence of poverty, population pressure, and frequent natural disasters whose devastating effects are sometimes intertwined with the effects of policy reform in the public imagination, the personalization of the reform program around the Minister of Finance can be extreme. This in turn complicates the process of consensus-building as, in the words of one interviewee, the program becomes increasingly viewed "as a private transaction between the Minister of Finance and donors".

When ownership of the program is viewed by key figures in government, including Cabinet ministers, as residing almost exclusively in the Minister of Finance, this also bedevils the process of consensus-building and the mobilization of resources for the program as other Cabinet ministers retreat from public support of the program at the slightest hint of opposition.³⁴ This clearly was the experience of Bangladesh's leading reformer, Saifur Rahman.

The new Minister of Finance is so deterred by the political costs of a new ESAF that he sees very little space for the mobilization of political support.³⁵

public expenditure in Bangladesh, criticising the increases in defence expenditure (now 17-18 percent of current spending), growing subsidies, interest payments on domestic debt, and salaries and wages arising out of the issue of absorption of personnel from the completed public projects under the recurrent budget. (*Op.cit.*, p. 6).

³⁴ The former Minister of Finance shared an incident of how he failed to win consensus in Parliament and his reform effort in this regard was subsequently marginalized. The issue was the establishment of a toll system for the Dhaka-Chittagong Expressway and the "cleaning up" of illegal habitation along the sides of the expressway. The Minister of Transport agreed to propose a bill in Parliament to this effect but in the face of strong opposition, retreated and accused the Minister of Finance as the instigator of that untenable proposal. (Interviews, Bangladesh, October 1997).

³⁵ In 1996, representatives of the newly-elected government were said to be concerned about their political image that they reportedly told the Fund that advanced publicity about the negotiation of a possible ESAF arrangement would be politically damaging.

The support of labor in Bangladesh is also difficult to mobilize as it is subject to the same polarization that characterizes the political situation: the unions are apparently under the control of the two main political parties so that strikes are often politically induced and are often drawn on party lines. Finally, the role of Parliament itself in Bangladesh has tended to be often a disruptive one instead of a unifying one. Instead of being a forum for dialogue and consensus-building, Parliament is deprived of its proper role as opposition parties boycott it when they have political grievances to settle.

On the positive side, the private sector is generally supportive of the program. It is particularly supportive of the privatization program and is keen to see it speeded up, and therefore views, with some disquiet, a disruption of the program by the alternation of power between the two main political parties with their different attitudes to the policy. For this reason, the Dhaka Chamber of Commerce and Industry and pro-reform economists whom we interviewed, expressed the rather unusual wish that the ESAF should come with a stipulation that requires, among other things, a mandatory consensus among political parties as a condition for financial support.

One important potential player in consensus-building and a source of support for the program is the NGO community in Bangladesh. Thanks in part, perhaps, to the generally good relationship that this community enjoys with the Bank and the Fund, and the large resources that come to them through Bank and donor-funded safety net programs, it is favorably disposed to economic reform.

Agenda Setting and Authorship of Program Documents

The distinct impression one gets from reading Fund documents and also talking to government officials in the field is that the policy agenda has tended to be set more by the Fund than by the government. This is true perhaps a little less in the macroeconomic area than in the area of structural reforms. But even in the macroeconomic, especially in the fiscal area, there are many references in the documentation, confirmed by the protests of leading officials, that tax policy was mostly dictated by the Fund or was the product of compromises that government felt constrained to accept.

Following the fall of President Ershad in 1991, the successor government claimed greater autonomy and leadership in setting the policy agenda. In August 1991, for instance, it increased the national pay levels for civil servants in a decision that clearly reflected more its priorities than

the Fund's.³⁶ There are two particular areas though in which the government's role in initiating policy was more pronounced, namely the poverty alleviation program and the area of environmental policy. Given the strong NGO role in Bangladesh, it is understandable that the poverty alleviation policy would have been a preoccupation of the government itself. The government's role in putting the issues of environmental policy on the agenda is also not surprising, given Bangladesh's history of floods and natural disasters although, again, donors and NGOs appear at least to have jointly sponsored this push which resulted in the creation of a special Ministry of Environment.

As for the design of policy documents, including the PFP, government officials interviewed in the field readily acknowledged that most documents were prepared by the Fund and thereafter, in the manner of the usual practice, given to the government for discussion and comment.

In the area of tax policy reform, the World Bank's role in preparing appropriate policy proposals, was particularly pronounced.³⁷ However, the role of the Bank and the Fund in authoring these basic policy documents did not seem of any particular concern to either the technicians, the bureaucrats, or even the political leadership of the ministries, indicating both an acknowledgment of weaknesses in the government's own administrative and technical capability in particular areas, a weakness aggravated a great deal by what would seem to be a high incidence of discontinuity and staff rotation in key government agencies, and the government's view that the authorship of policy documents as such, was not a particularly important criterion of ownership.

Initiatives to Promote Ownership

In the late 1980s, in the face of stiffening opposition to the program, the government began to devote greater attention to building national consensus and support for structural reform through public education, with particular focus on the bureaucracy. But these initiatives appear to have been largely ineffectual as they were vitiated by the climate of recrimination and civil unrest which marked the politics of the period.

The Fund, for its part, began to take the business of consensus-building seriously, as domestic opposition to the program escalated and the pace of domestic reform began to slow down noticeably at the beginning of the 1990s.

³⁶ The decision was taken without full consultation with the Fund, although they did not undermine the viability of the macroeconomic program, as they were to be financed by new tax measures as well as reductions in subsidies and non-essential current expenditure.

³⁷ In 1988, for instance, the Bank submitted comprehensive tax reform proposals which were then reviewed by high-level committees who, in turn, reported to government.

A 1993 internal Fund document not only emphasized the need to strengthen the consensus for reform in Bangladesh but it also proposed some rather interesting and commendable initiatives that the Fund might take to help build support for the program. It proposed that the Fund Resident Representative would “play a leading role through the development of a wide range of contacts and by direct participation in the national debate.” It also recommended the publication of Occasional Papers on Bangladesh for discussion in high-level seminars in which the Fund staff would participate, as well as meetings by Fund missions with opponents of reform, both in and outside the government, in a bid to make the case for reform to a wider audience.

In 1994, a Fund mission made a submission in support of accelerated reform to a large group of ministers and senior officials in a roundtable discussion attended also by the Minister of Finance who found the interaction so effective that he asked that it be made a regular feature of subsequent Fund mission work.

The Fund mission leader is also reported to have participated in a seminar on reform, growth and poverty alleviation in May 1994, inaugurated by Prime Minister Khaleda Zia.

Government Commitment to Reform

As we have noted, the level of government commitment and ownership of the program has waned significantly since the beginning of the 1990s, i.e., with the onset of the ESAF program. The present government, while recognizing the need for continuing reform, appears to want to resume an ESAF arrangement with the Fund but is caught in a web of political paralysis, partly of its own creation. In the period between the Khaleda Zia government’s tenure and when it took power, it had waged a campaign of violent opposition and vilification of the reform program and now finds itself unable to create space for a resumption of the reforms. This mood was captured sharply by a senior official of the Ministry of Finance who acknowledged, as if in despair, “my administration is weak; even if I am in agreement with IMF, I won’t be able to produce changes.” The incumbent Minister of Finance himself echoed this same sentiment with a touch of political apprehension, that if the policies insisted on by the Fund were to be followed, “the ESAF will be implemented by another government!”³⁸

³⁸ Interview with Minister Kibria, Hong Kong, September 24, 1997. His predecessor, who had the most outstanding record of program implementation through the 1980s and early 1990s, also noted how difficult a job it is to carry out reform in the extremely polarized, pluralistic and democratic framework that Bangladesh has, and referred to a standing joke which finance ministers in reforming countries in Africa share with their Bangladeshi counterparts in meetings: “These IMF boys will not let one stay long as minister!” (Interview, Bangladesh, October 7, 1997).

Conclusion

In our view, it would take a major consensus-building effort in the form of an all-inclusive national conference (such as Uganda's in December 1989) with the sort of active participation of the Fund, recommended in a 1994 internal Fund document, to break the political stalemate which now hovers over the country, and create conditions for a realization of the country's tremendous potential for higher growth. On the part of the Fund, there would need to be greater recognition of the political constraints that inhibit the consensus-building process and a willingness to allow the government itself to set the time-table for reform.

BOLIVIA

The Ownership Issues

Bolivia has been a long user of Fund resources and has gone through the usual progression from stand-by arrangements starting from the mid-1980s to SAFs, and then to ESAFs. The political situation in the country has, in recent times, been characterized by an alternation between the two major political groupings, with a large number of smaller parties between them. The present government of President Banzer was elected in 1996, and is based on a coalition of several parties. In general, perhaps because of the fragility of the political consensus and the peculiar problems that attend government succession in the country, the role of technical staff affiliated to the economic ministries, especially the Finance Ministry which has the largest concentration of them, has tended to be more pronounced than in other countries. These technocrats have, in general, shown consistently strong support for reform programs. While this has in general been positive, it has tended to often put the Ministry of Finance ahead of the Ministry of Planning and the rest of the government as agreements are sometimes reached with the Fund before the government's internal policy discussions have settled on clear choices and decisions.³⁹

Given the prominent role of technical personnel in the structure of government, these positions have become highly politicized and the composition of negotiating teams has tended to change with every change of government.⁴⁰

Program Support and Government Commitment

The workings of the government machinery in Bolivia appear to be characterized by a number of factors that have an obvious bearing on the scope of support for, and government commitment to, reform programs. In addition to the discontinuities in technical positions in the ministries⁴¹ and the composition of negotiating teams already noted, the transition between incoming and outgoing administrations is often strained.⁴²

³⁹ There are several references in internal Fund documents pointing to this. For instance, a 1992 internal Fund document complains, "in part because of a lack of coordination between the Ministry of Finance and the Ministry of Planning, public sector investment was not limited as envisaged in the program."

⁴⁰ Interviews, Bolivia, October 1997.

⁴¹ Many interviewees emphasized this discontinuity in the policy making machinery, stressing that to a large extent, the short-term focus of successive governments is attributable to interruptions in the institutional memory.

⁴² In the most recent change of government, the incoming government reportedly were handed documents relating to the program that had been negotiated by the outgoing government only ten days before it formally assumed power in a transition period that lasted a whole two months (Interviews, Bolivia, October 1997).

There appear to be different circles of policy making within government, the most prominent among them being a so-called “macro group” that meets weekly and consists of the Minister of Finance, the Vice-President, and the President of the Central Bank, to which the Resident Representative is often invited. Instead of aiding the process of policy coordination and consensus-building, these circles tend in practice to complicate the process through undue overlap and rivalry.

The role of the legislature is especially critical to the fulfillment of government commitments. This point was underscored in interviews with ministers⁴³ and are confirmed by numerous references in internal Fund documents.⁴⁴ Although many political parties seem to support the general direction of the reform program, many of them are critical of what they see as undue secrecy surrounding the Fund’s relations with Bolivia, as evidenced by the lack of access of most congressmen, outside select committees, to basic program documents, including the PFP.⁴⁵

The private sector, including the banking and financial sector on the other hand, has a generally more positive and supportive attitude to the reform programs, an attitude partly reflecting the fact that, in contrast with other stakeholders, they have tended to enjoy much greater access to government. They also have had a great deal of leverage over policy making which they have used, on occasion, to advantage.⁴⁶

Unlike the business community, other NGOs, in particular those representing the indigenous groups and labor unions, have been highly critical of the reforms on account of what they perceive as their weak poverty alleviation impact. The indigenous groups see their main concerns – decentralization, municipal governance and environmental issues – as largely marginal to the Fund. To a very large extent, these groups have tremendous ideological affinity with the labor unions. The unions, for their part, have not only been critical of the reforms, they

⁴³ Ministry of Finance officials complained, for instance, that the Fund does not sufficiently appreciate the complexities of the legislative process in Bolivia, especially the time it takes to obtain congressional approval of major legislation (Interview with Minister Millares and others, Hong Kong, September 24, 1997).

⁴⁴ For example, in 1993, the government’s inability to meet structural benchmarks relating to banking sector reforms was said to be attributable to delays in obtaining congressional approval. There are many other references suggesting that governments had considerable difficulty in securing congressional support.

⁴⁵ Interview with *Partido Demócrata Cristiano* (PDC), Bolivia, October 1997. The mystification of Bolivia’s relations with the Fund reflects not only these widespread perceptions of secrecy but the sensationalism with which these relations are portrayed in the Bolivian mass media. In general, Fund missions have tended to receive a great deal of largely negative publicity in the media, with little attention being devoted to substantive issues of economic policy which the missions are meant to address.

⁴⁶ Thus, in December 1994, for instance, the government scaled back tax rebates to exporters in fulfillment of one of the prior actions required for the presentation of the ESAF program to the Fund Board. However, this measure was subsequently modified in contravention of the commitments made to the Fund, in response to protests lodged by the business community.

have been highly confrontational and ideological in their relations with government. In this respect, they differ a little from labor unions in Africa generally which, by and large, now accept the need for policy reform, focusing their concerns mainly on the issues of governance and adequate safety nets.

Government reaction to labor protests in Bolivia has perhaps, for reasons of their confrontational and ideological nature, tended to be inordinately heavy-handed, thereby leaving precious little room for dialogue and consensus-building. Asked during interviews to provide more specific details of the ways in which the programs affect them detrimentally, and also of how they are consciously marginalized in the government's decision-making processes, they plainly confessed that they were unable to do so, in large measure because of the government's refusal to give them access to statistical and other relevant information. It would seem therefore much of the antagonism the unions feel can be relieved by more conscious efforts at dialogue and education.⁴⁷

Authorship of Program Documents and Policy Initiatives

In the area of agenda setting and the design of policy reforms, the evidence suggests that throughout the program period, but especially in its later years, contrary to the near-unanimous impression of all interviewees, the role of government at the technical level has been quite prominent.⁴⁸

Government Commitment and Program Performance

The Bolivian program has achieved significant progress in both the macroeconomic and structural spheres although program implementation has sometimes been hampered by political strains. This in turn can be attributed to a number of factors, the most important being frequent friction and a lack of coordination between the executive and legislative branches of government.

⁴⁷ According to the union representatives interviewed, for instance, the union protests against the government's privatization plans which precipitated the declaration of a nationwide state of emergency in April 1995, were called only after attempts to engage the government in discussion had failed. (Interviews, Bolivia, October 1997).

⁴⁸ In interviews with officials, the fiscal programming unit of the Ministry of Finance, officials presented the PFP process as one of intensive discussion and interaction between government and Fund staff. They firmly rejected the view that the policy agenda was set by the Fund merely because initial drafts of the PFP came from the Fund. They saw the matter more in terms of "co-authorship" than unilateral decision by the Fund.

To be sure, this friction characterizes not only the conduct of the government's relations with the Fund and the Bank, but other social and economic policies as well, and to some extent is not unique to Bolivia. However, in the area of Fund-government relations in particular, the problem is aggravated in part by a perception on the part of some congressional leaders that the economic reform agenda has somehow become the preserve of the executive branch – Fund missions' meetings are conducted almost exclusively with the executive branch - although the issues involved are national in character. This appears to be a bit of a paradox for as many staff documents point out, Fund missions do meet congressional leaders from time to time. That this feeling of inadequate participation persists in the Congress can perhaps be explained by the fact that the interaction of Fund missions with congressional leaders is neither systematic nor truly consultative.

Other factors include the failure of program implementation schedules to sufficiently factor in realistic time-tables for obtaining congressional approval; discontinuities in the technical leadership of key economic ministries which in turn undermine the efficiency of public administration, with consequent delays in the decision-making process and, finally, a tradition of non-cooperation between outgoing and succeeding administrations, leading often to a withholding of critical policy documents and data from incoming governments for protracted periods.

Initiatives to Promote Ownership

There are indications that governments have, from time to time, sought to explain policy measures to specific interest groups. The present government has begun just such an initiative called rather explicitly "national dialogue", under which regular roundtable discussions are conducted, which bring together representatives of the private sector and NGOs, including the churches, in an attempt to build a national consensus on several policy issues.

On the part of the Fund, staff reports point to Fund meetings with a wide cross-section of stakeholders beyond the normal circle of government officials. There have been meetings of parastatal organizations and importantly, occasionally with members of Congress. It would appear from the hugely negative image of the Fund in the public mind, and the unanimous condemnation of the "secrecy" surrounding its operations in Bolivia, that these meetings have been viewed as largely sporadic and routine, and not as part of a systematic operational style.

It is interesting to observe though, in this connection, that in contrast with the Fund's generally negative public image, the image of the Managing Director of the Fund appears to be fairly

positive.⁴⁹ Indeed, this is a phenomenon we found in other countries we visited, and which attests as much to the significance that the public often attaches to visits by the Managing Director, as to the effectiveness of the Managing Director's communication skills.

The Resident Representative

There has been a resident representative in La Paz since the beginning of the program period. The current resident representative appears to enjoy a particularly good relationship with, and access to, government at the highest political levels. He is clearly very effective and is widely viewed in political circles especially as a friend of Bolivia although, by reason of his professed personal style,⁵⁰ his role is not very well known to the general public (especially the press and NGO community), as a number of interviewees noted.

One other important observation that deserves to be made about the role of the resident representative in Bolivia, and one which a number of interviewees made, is that most resident representatives have always enjoyed good relations with government.⁵¹ The technical staff of the ministries quite understandably view the resident representative's office as a particularly good source of policy advice.

Conclusion:

In spite of the difficult political environment in which reforms have been undertaken in Bolivia, successive governments have shown continuing commitment to the basic principles of the reform process, and a great deal has been achieved in the framework of the 1994-97 ESAF, especially in the area of privatization. Program implementation will probably be later helped if greater attention were paid to the time and politics it takes for government to obtain congressional approval for agreed actions.

⁴⁹ Interview with *Accion Democratica Nacionalista*, Bolivia, October 1997.

⁵⁰ The resident representative said, in an interview, that he preferred to keep a very low profile, and for this reason, he generally does not talk to the press, as other representatives do. He felt he was very much an insider within government, and normally does not even participate in diplomatic activities. (Interview with the resident representative, Bolivia, October 1997).

⁵¹ A number of people interviewed seemed to prefer resident representatives of Latin American origin as the latter seem to relate better to the political and cultural situation in Bolivia.

Côte d'Ivoire

Introduction

Following independence, Côte d'Ivoire had a prolonged period of growth led by agricultural exports. By the 1980s, export crops accounted for half of agricultural output. This period of growth came to an end at the beginning of the 1980s and the economy then went into rapid decline. The decline was triggered by the ending of the coffee and cocoa booms of 1976-79, the aftermath of which produced a fiscal crisis. During the first half of the 1980s there was a reform program, leading to a brief resumption in growth by 1985. However, decline resumed in the late 1980s due to a conjunction of a further deterioration in the terms of trade of 40 percent, and lax public spending: between 1980 and 1990 the civil service increased by 57 percent.⁵² By 1989, the government deficit had risen to almost 18 percent of GDP, external debt was \$15 billion, and per capita GDP was falling rapidly at around 5 percent per year.

This conjunction of fiscal crisis and economic decline induced the government to embark upon an adjustment program, initially supported by an 18-month stand-by arrangement from November 1989, followed by a 12-month arrangement in September 1991.

The Stand-By Arrangements and their Sequel, 1989-93

Adjustment to the negative external shock was complicated by two features of the Côte d'Ivoire policy regime. First, there was a commitment to stabilize producer prices for cocoa and coffee. Whereas this stabilization policy had generated large revenues, by the late 1980s it involved a price subsidy. The implication of this was that a negative shock would be borne by the public sector rather than being automatically transferred to producers. Secondly, membership of the Franc Zone at a fixed exchange rate kept the price level essentially constant. This had the implication that the real incomes of wage earners could only be reduced through nominal wage reductions. The negative external shock reduced the equilibrium real wage in the economy. In a flexible exchange rate regime the real wage would have fallen as a by-product of an increase in the price level. The exchange rate regime thus had important implications for the political economy of wage adjustment. Whereas inflation would have reduced real wages in a coordinated fashion and without any overt action on the part of employers, in the context of price stability reductions required individual employers to change wage contracts. The government as an employer faced precisely this problem. It indeed attempted to reduce nominal wages as part of

⁵² Ministère de l'Emploi, "Situation de l'Emploi en 1995", 1996, Table 12.

the stand-by program. However, this triggered such strong and violent opposition that the policy was reversed. In the context of declining per capita GDP this real wage rigidity implied that the incomes of civil servants were rising relative to mean incomes in the society. This was particularly problematic because even prior to the negative shock Ivorian civil servants had been unusually well paid relative to average incomes.⁵³

As part of the stand-by arrangement, producer prices for cocoa and coffee were halved. Given the concern with the fiscal position this decision was understandable since world prices were falling. However, this was very much a second-best response reflecting the constraint imposed by the fixed exchange rate. Once the exchange rate was adjusted, in January 1994, the domestic currency price of tradables doubled. Hence, the chosen adjustment sequence involved a temporary halving of export crop prices. This first gave farmers an incentive to reduce their production of export crops and then to increase production. The initial reduction, while necessary on fiscal grounds (given the exchange rate constraint), imposed resource misallocation costs on the economy. These costs could have been avoided if the devaluation had taken place earlier. Additionally, as we discuss below, export taxation is highly regressive, so that the chosen adjustment sequence imposed an avoidable regressive redistribution.

Following the initial stand-by arrangement, there were six World Bank Structural Adjustment Loans (SAL) covering the period 1989-93. Various structural reforms were attempted in these years. There was a start to privatization, and financial reform following a major banking crisis. There were substantial reductions in current expenditure (30 percent) and capital expenditure (15 percent), and tax measures aimed at broadening the tax base. The previous expansion in the civil service was reversed with an 11 percent contraction in numbers between 1990 and 1992. Between 1989 and 1991, primary expenditure was reduced by 28 percent.

However, the extent of net fiscal adjustment was constrained. First, there was continued contraction in per capita GDP of around 15 percent between 1989 and 1993. A major reason for the continued deterioration in the economy was that the exchange rate had become substantially misaligned. In addition to the direct resource misallocations implied by this over-valuation, there was increasing financial speculation that the exchange rate would be devalued. Secondly, there was continued deterioration in the terms of trade. Both of these reduced revenues. Because of the inability to adjust the real wage bill in the face of these declines in revenue, its share of revenue rose very rapidly: from 56 percent in 1989 to 75 percent in 1993. Although the program

⁵³ This is indeed a general problem for the Franc Zone. On average in the zone civil servants were paid, prior to the devaluation, eleven times per capita GDP. See L. M. Goreux, "La Devaluation du Franc CFA, un premier bilan, en Decembre 1995", mimeo, World Bank.

initially succeeded in reducing the primary budget deficit by over 6 percentage points of GDP, the overall budget balance remained in heavy deficit. As a result there was continued borrowing. In the first two years of the program (end-1989 to end-1991) external debt rose by a further \$3.7 billion. The fiscal deficit, which had peaked at 18 percent in 1989, was still 13 percent of GDP in 1993.

The ESAF Program, 1994-97

The continuing fiscal and current account deficits proved unsustainable. There were various attempts to reach agreement among Zone members on devaluation but this involved considerable delay. The region finally agreed on a 50 percent devaluation in January 1994. The following March Côte d'Ivoire embarked upon its first ESAF. The objectives of the program were to generate a primary budget surplus of 3 percent of GDP by 1996 (in order to finance debt service), to achieve GDP growth of 5 percent by 1995, and to protect the most vulnerable population groups during the adjustment period. The fiscal objective was to be reached through a combination of a revenue recovery and expenditure reduction. Revenue was expected to recover as a result of the devaluation by around 4 percentage points of GDP in 1994, and thereafter was planned to remain constant at around 21.6 percent of GDP. Primary expenditure was to fall from 21.1 percent in 1994 to 17.8 percent in 1996. The planned structural reforms included liberalization of the labor market, price decontrol, trade reform, including reductions in import taxes, civil service reduction, and accelerated privatization. Of these, there were substantial delays in civil service reduction, privatization, and the deregulation of export crop marketing.

It was recognized at the time that the urban poor might be adversely affected by the reforms, including the devaluation. To mitigate these effects the program planned targeted assistance to urban areas through three channels: emergency assistance targeted particularly to women and children; improvements in social infrastructure including health and education facilities; and labor-intensive public works. It was envisaged that the program would lead to a substantial rise in rural incomes. The government's social strategy also involved reform of the health and education sectors. This involved raising enrollment rates in primary education. The educational system was recognized as having low enrollment and high drop-out rates.

Fortuitously, the devaluation was very soon followed by a doubling in the world price of coffee. While not Côte d'Ivoire's major export, this nevertheless constituted a substantial temporary windfall. Thus, if the 50 percent devaluation was sufficient to restore equilibrium at the terms of trade prevailing at the time of the devaluation, the economy switched from having an over-valued exchange rate during a negative shock to an under-valued exchange rate during a positive shock. Had the exchange rate been flexible, it would have appreciated in response to the terms

of trade improvement. With a fixed exchange rate the external shock was inflationary.⁵⁴ Thus, during 1994 the economy was hit by two inflationary shocks, the devaluation and the terms of trade improvement. During the year the price level rose by 32 percent.

Associated with the devaluation and the terms of trade boom was a large fiscal adjustment. Between 1993 and 1995 revenue recovered, rising as a share of GDP from 17.6 percent to 21.7 percent, while expenditure declined from 30.0 percent to 26.5 percent. As part of the program, the public sector wage bill was frozen, leaving the government the choice between salary levels and employment levels. The government chose to reduce salaries in real terms by only limited compensation for the post-devaluation inflation, and by reducing the nominal wage for new recruits while requiring older civil servants to retire. The number of employees in the civil service actually started to increase again, although only modestly.⁵⁵

The devaluation was successful in changing relative prices. By May 1995, the price of tradables relative to non-tradables had risen by 15 percent and real wages had fallen substantially.⁵⁶ It also succeeded in reversing the decline in GDP: in 1995, 1996 and 1997 GDP grew by 7 percent per annum. Industrial production recovered immediately, increasing by 14 percent between 1993 and 1995: unlike Zimbabwe and Zambia, Côte d'Ivoire did not have the features of a transition economy. Both the devaluation and the temporary favorable shock would have been expected to reduce consumption relative to savings.⁵⁷ This indeed occurred: between 1993 and 1994 consumption fell by 14 percentage points of GDP, with investment increasing by 6 percentage points, and the current account improving by 8 percentage points.⁵⁸

The planned social safety net measures were only partially implemented. The impact of the devaluation on consumer prices was phased in gradually through the use of subsidies and taxation. However, price increases were phased in more rapidly than had been envisaged and the CFAF 10 billion allocated to temporary subsidies was underspent. The plans for labor-intensive public works were not implemented in the first year of the program. The Fund urged the government to accelerate implementation of these public works.

⁵⁴ This is because a favourable external shock raises the relative price of non-tradables. Since the price of tradables is given in nominal terms by the fixed exchange rate, the required relative price change can be achieved only through an increase in the nominal price of non-tradables.

⁵⁵ Ministère de l'Emploi, *op. cit.*.

⁵⁶ Goreux, *op. cit.*, p. 23.

⁵⁷ A devaluation reduces real cash balances, and a temporary positive income shock raises transient relative to permanent income.

⁵⁸ Goreux, *op. cit.*, Table 26.

Distributional Effects, 1989-97

The programs had social consequences partly through changing incomes and partly through changing social expenditures. We first consider the effects on incomes.

Prior to the ESAF there had been a long period of worsening poverty. Between 1979 and 1993, per capita consumption fell by 34 percent (Table 1) and the economy informalized. Whereas in 1980 the modern sector and the urban informal sector had each accounted for 14 percent of employment, by 1992 the modern sector had contracted to 8 percent and the informal sector had expanded to 24 percent.⁵⁹ One reason for this rapid informalization was the constraint imposed by Franc Zone membership, since (as noted above) it was much more difficult for real wages to fall in response to the massive negative shocks of the 1980s.

The link from wage rigidity to informalisation is supported by the results of a computable general equilibrium model. In this model, a real wage cut of 20 percent in the formal sector results in a 16 percent increase in employment in the sector and an overall increase in GDP of 2.5 percent. The wage cut reduces the size of the informal sector and raises overall incomes in the economy.⁶⁰

The adjustment programs affected income distribution through many channels. Here we discuss the three most important channels, the devaluation, changes in crop taxation, and the change in the public sector wage bill.

By design, in improving the balance of payments the devaluation initially reduced mean consumption. However, in addition to this general decline there would be distributional changes: net sellers of tradables would be favored relative to net purchasers of tradables. In general, farm households producing export crops were likely to be net sellers of tradables whereas urban households were likely to be net purchasers. The consequences of this redistribution depended upon the initial incidence of poverty among the various socio-economic groups. Prior to the devaluation, the incidence of poverty was much higher in rural than in urban areas. Within rural areas it was disproportionately high among households growing export crops and female-headed households. Within urban areas, it was disproportionately high among households dependent upon the informal sector.⁶¹ This would suggest that the devaluation would be distributionally

⁵⁹ V. Bodart and J. Le Dem, "Labor Market Representation in Quantitative Macroeconomic Models for Developing Countries: an Application to Côte d'Ivoire" IMF Working Paper 95/87, Table 1.

⁶⁰ Bodart and Le Dem, *op. cit.*

⁶¹ Grootaert shows in a probit analysis of poverty that controlling for education and various endowments these groups are significantly more likely to be poor. See C. Grootaert, "The Determinants of Poverty in Côte d'Ivoire in the 1980s", *Journal of African Economies*, Vol. 6, 1997, pp. 169-196.

progressive although adversely affecting some components of the initially poor, notably those in the urban informal sector and food producers.

Recall that during the stand-by arrangements the prices of export crops were halved. During the ESAF export taxation of cocoa and coffee were reintroduced in 1994.

The distributional incidence of export taxation is regressive. It has been quantified for the case of cocoa, using a computable general equilibrium model.⁶² These simulations suggest that removing the current export tax on cocoa (which effectively amounts to almost 30 percent), would lead to a powerful redistribution from urban to rural groups. However, in the case of cocoa, there is a rationale for the export tax since Côte d'Ivoire has considerable power in the world cocoa market. Although in aggregate the nation therefore gains from the export tax, rural groups lose, while urban groups capture not only the entire terms of trade improvement but also benefit from a transfer from rural groups. These effects are substantial: rural groups would gain about 10 percent from an abolition of cocoa taxation. Since rural groups are poorer than urban groups this gives rise to a trade-off between efficiency and equity. An implication is that because urban groups are gaining from the tax at the expense of rural groups, public expenditure would need to be heavily biased towards rural areas in order to compensate. With respect to coffee taxation, there is no such trade-off because there is no market power. The removal of the coffee export tax would therefore have both a positive distributional effect and improved allocative efficiency.

The reduction in the public sector wage bill had its social consequences. Throughout the Franc Zone, civil servants have traditionally been paid at very high rates. Prior to the devaluation, they received on average over 11 times mean national income.⁶³ Further, in Côte d'Ivoire, the composition of public sector employment is very different from that of the workforce as a whole. First, it is disproportionately male. Whereas women are a majority in agriculture and the informal sector, they constitute only a third of public sector workers. Second, it is disproportionately Ivorien. Whereas immigrants make up almost a third of the labor force, they constitute only 11 percent of the public sector.⁶⁴ Hence, to an extent, the reduction in the public sector wage bill could be regarded as affecting adversely a relatively elite social group.

The net effect of reform programs has been the subject of a number of surveys. These provide snapshots of poverty in 1988 and 1993, thus spanning the pre-ESAF adjustment period. During this period, both the incidence and the intensity of poverty doubled (Table 1). There was little

⁶² J. McIntire, "Welfare Effects of Ivorien Cocoa Export Tax and Marketing Policy", mimeo, World Bank, 1997.

⁶³ Goreux, *op. cit.*, p. xiii.

⁶⁴ Ministère de l'Emploi, *op cit.*, Annex Tables 1 and 5.

change in the distribution of income and the deterioration in poverty reflected the decline in mean incomes.

For the ESAF period, survey data are available only up to early 1995. This truncation is important because in the first year after the devaluation the decline in per capita GDP continued, whereas it was strongly reversed during the following three years. Hence, the comparison of household surveys for 1993 and 1995 does not pick up this recovery but only the impact during the first year and a half. During this initial phase of the ESAF there was a continued increase in poverty, both the incidence and severity of which worsened. This was due, as in the pre-ESAF reform phase, to a decline in mean income rather than to a change in the distribution of income (Table 1). As anticipated in the program, urban poverty had increased dramatically as a result of the devaluation: in Abidjan, the headcount measure rose from 5 percent to 20 percent between 1993 and 1995, and the rate of unemployment rose to 15 percent.⁶⁵ Hence, the safety net programs failed to prevent a substantial deterioration.

Overall, between 1989 and 1995 per capita GDP fell by 12 percent and poverty more than doubled. At the end of this period three socio-economic groups accounted for 80 percent of the poor: farm households producing exports, food crop producing households, and households dependent upon the urban informal sector. The incidence of poverty in these three groups was 43 percent, 58 percent, and 31 percent, respectively. Poverty had become diffused across the major socio-economic groups whereas it had initially been much more concentrated.

We now turn to the effect of the programs on social expenditures and the consequences for health and educational outcomes. A major part of the adjustment program was the correction of the fiscal deficit. Part of this adjustment was borne by reductions in expenditure. Between 1989 and 1995, government primary expenditure as a share of GDP declined from 29.0 percent to 19.5 percent. The social sectors were relatively protected in that the shares of both health and education spending in primary expenditure increased. The protection was more pronounced for the health sector, the share of which in primary expenditure rose from 4.1 percent to 6.4 percent. The share of education increased only marginally, from 23.9 percent to 24.6 percent. However, these budgetary reallocations in favor of the social sectors were insufficient to protect their spending levels in real terms per capita. To do so would have required health expenditure to have risen to 6.9 percent and education expenditure to have risen to 40.3 percent of primary expenditure.

⁶⁵ The poverty incidence in Abidjan is taken from World Bank, *op. cit.*, p. 12 and the unemployment rate from Ministère de l'Emploi, *op. cit.*, p. 32.

Table 1: Poverty 1979-95

	1979	1985	1988	1993	1995
private consumption per capita (in thousands of CFAF, 1987 prices)	225	189	187	148	129
incidence of poverty (%)	-	11.1	17.8	32.3	36.8
intensity of poverty	-	2.9	4.5	9.0	10.4
Gini coefficient	.61	.39	.35	.37	.37

Source: World Bank, *Poverty in Côte d'Ivoire: a Framework for Action*, Report 15640-IVC, 1997.

Note: The incidence of poverty is the percentage of people living below the poverty line of CFAF 6350 per month. The intensity of poverty measures the shortfall from the poverty line: here we use the 'P₁' measure.

Health

During the adjustment program real per capita public expenditure on health declined (Table 2).⁶⁶ Additionally, there was a substantial shift from recurrent to capital expenditure, so that the latter rose strongly in real terms. The growth in the capital budget was disproportionately directed towards primary health care. By contrast, the composition of recurrent expenditure was virtually unchanged. This suggests that the composition of the recurrent budget was failing to take into account the changes in the capital program which would be presumed to have recurrent cost implications.

There is some evidence that prior to the adjustment program the incidence of health spending was highly regressive. One available measure is the share of total consultations in public health centers for each income quintile. In 1988, the richest quintile had double the share of the poorest quintile. By 1995, the difference had narrowed: the richest had 1.6 more consultations than the poorest. However, even by 1995, public spending remained highly regressive. Spending on health care per capita was three times greater for the highest income quintile than for the lowest.⁶⁷

As part of the policy reforms, user charges were introduced into the public health care system in 1991. Despite these charges, usage by the two poorest quintiles increased, while usage of the

⁶⁶ On the data presented by Demery *et al.* the implied fall is somewhat larger, at 16 percent. See L. Demery, J. Dayton and K. Mehra, "The Incidence of Social Spending in Côte d'Ivoire, 1986-95", mimeo, World Bank, 1997.

⁶⁷ Demery *et al.*, *op. cit.*, Figure 2. The data are for 1995.

private formal health care system fell sharply. There is also evidence, however, of a shift into usage of traditional medicine.⁶⁸

There is evidence that during the pre-adjustment crisis of the 1980s there was a deterioration in the quality of health care: for example, the rate of maternal mortality in hospitals tripled between 1978 and 1990. During the adjustment period itself quality improved. A vaccination campaign, launched in 1987, has made substantial progress although failing to reach its original targets: between 1987 and 1991 survey results show significant improvement. During the 1990s, neonatal tetanus has been eradicated from Abidjan, the blood transfusion service has been made safe from HIV, and an increased proportion of pregnant women receive professional health care. Despite these improvements, the state of health remains a major problem. The incidence of stunting increased from 20 percent in 1988 to 35 percent in 1995 (Table 2) and a survey which asked people to identify their problems found that among women health was ranked first.⁶⁹

Education

During the adjustment program real per capita public expenditure on education declined by over 35 percent (Table 2). Within this decreasing total there were compositional changes in recurrent expenditure. Between 1990 and 1995, the share of primary education increased from 46 percent to 49 percent, that of secondary education fell from 40 percent to 34 percent, and that of tertiary education increased from 14 percent to 18 percent.

Within primary education the number of teachers increased slightly: the required reduction in the wage bill was achieved by a reduction in the real salary of teachers. Measured as a ratio of mean per capita GDP, the mean salary of teachers fell from 12.6 to 8.7 between 1992 and 1995. The sharp reduction in the wage bill permitted a massive increase in non-salary expenditures on primary education: from 2 percent of the salary bill to 11 percent. The number of pupils per teacher increased by 10 percent. There were therefore three developments which may have affected the quality of education: the lower wages which demotivated teachers, the higher expenditures on teaching materials, and the increase in the pupil-teacher ratio. The net effect of these changes on the quality of education is ambiguous. Abstracting from a possible change in quality, the policy change achieved both an increase in educational output and a reduction in educational expenditure through reducing the unit cost of primary education. There remained, however, scope for further improvements in educational efficiency. Whereas in principle it should take six years to complete primary education, on average pupils were taking almost nine years.

⁶⁸ See CIRES, "Les strategies d'adaptation sociale des populations vulnérables d'Abidjan face à la dévaluation et ses effets", Abidjan, 1995.

⁶⁹ Côte d'Ivoire and UNICEF, *op. cit.*, Table 37.

These changes were even more dramatic at the secondary and tertiary levels. The unit costs of secondary education fell relative to those of primary education from 4.9 in 1988 to 2.1 in 1996. Similarly, in university education relative unit costs fell from 15.5 to 11.1.⁷⁰ By 1997 this had provoked major political opposition including prolonged strikes.

The incidence of educational expenditure differed enormously as between primary and the higher levels. Comparing the richest and the poorest quintiles, public expenditure per capita on primary education was substantially higher for the poor. By contrast, spending for secondary and tertiary education was around seven times higher for the rich. This swamped the progressivity of primary spending, so that overall public spending on education was around two-and-a-half times greater for the rich than for the poor.⁷¹

Gross enrollment in primary education increased substantially between 1986 and 1995 (Table 2). The increase was relatively larger for the poorer household groups: enrollment for the poorest quintile of households increased from 39 percent to 56 percent, and within this group enrollment of girls increased more than that of boys. Despite this improvement, educational indicators were very poor: by 1995, only 45 percent of girls from the poorest quintile of households were receiving primary education. This improvement in primary education was not matched at the secondary level. The gross enrollment rate declined from 34 percent to 31 percent between 1986 and 1995.

Thus, the two reform programs certainly involved massive reductions in government expenditures and these inevitably substantially reduced social expenditures. The smaller component of these expenditures, health, was, however, almost fully protected by large reallocations of the budget in its favor. With respect to education this was not feasible, and educational expenditures declined almost in line with overall expenditure reductions. However, the effect of the reduction in educational expenditures was borne largely by teachers. This tended to lower the quality of education, partly by demotivating teachers and partly by shifting the composition of the profession towards the less-qualified. A two-tier system of wages was introduced for existing employees versus new entrants and the former were encouraged to leave. However, the reduction in teacher salaries was sufficiently large to leave room for increased non-wage expenditures in primary education. It is, therefore, possible that the deterioration in teacher quality was offset by improved provision of material inputs.

⁷⁰ World Bank, "Secteur Education", Abidjan, mimeo, 1997, Table 3.

⁷¹ Demery *et al.*, *op. cit.*, Figure 4.

Table 2: Health and Education Expenditures and Outcomes

<i>Health</i>	1986	1988	1990	1992	1993	1994	1995
spending per capita			4.6	3.8	3.6	3.9	4.2
infant mortality rate					90		
life expectancy					56		
stunting	20					35	
vaccinations by one year							
BCG						73	
DTC3						45	
polio3						45	
<i>Education</i>							
spending per capita			20.0	17.9	14.2	12.6	12.7
gross primary enrollment	63				71		75
adult literacy		54				49	

Sources: infant mortality, life expectancy, stunting, enrollment and literacy: World Bank, *op. cit.*, p.6; enrollment rate for 1986 from Demery *et al.*, *op. cit.*, Table 8; spending per capita (in thousands of CFAF, 1985 prices) from UNICEF, "Financement des Secteurs Sociaux de Base: Suivi de l'Initiative 20-20 en Côte d'Ivoire", mimeo, August 1997, p.47 and p.56; vaccinations from Republic de Côte d'Ivoire and UNICEF, "Analyse de la Situation des Femmes et des Enfants de Côte d'Ivoire", 1996, p. 80.

Conclusion

The experience of Côte d'Ivoire is distinctive in our sample because of its membership of the Franc Zone. First, the inability to adjust the exchange rate in response to external shocks contributed to the prolonged decline of the economy during the 1980s and the build-up of severe disequilibria in the labor market, the balance of payments and the budget. Second, during the phase of policy reform after 1989, the delay in exchange rate adjustment restricted policy options to actions which were subsequently reversed once devaluation was achieved.

Franc Zone membership also limited the options for fiscal adjustment, forcing the burden of adjustment to be borne by expenditure reduction. The implied real wage rigidity contributed to the informalisation of the economy. This in turn eroded the tax base. As of 1989, the government faced a huge fiscal deficit which could not be eliminated by increased taxation due to the rapid

contraction of the private formal sector. The Fund attempted to increase fiscal revenues through measures which were clearly detrimental to income growth. Privatization receipts were increased by conferring monopoly rights on the businesses to be privatized, and the Fund argued for a high external tariff for UEMOA.

The required reductions in public expenditures were imposed on a system which was already failing to meet basic social needs. First, the composition of social expenditures had been geared to meeting the demands of the urban elite. Second, during the crisis of the 1980s service provision had already massively deteriorated.⁷² As a result, by 1989, Côte d'Ivoire had very poor social indicators for its level of income. However, the government chose to place most of the burden of adjustment on its own employees. This was distributionally progressive because the civil service was initially unusually privileged. As a result, the provision of social services was very largely protected despite massive expenditure reductions.

Turning from social service provision to the generation of income, the social costs of adjustment in Côte d'Ivoire were not high. The major groups which were initially poor, rural households, were mostly net beneficiaries of the relative price changes. Nor did the economy face problems of transition: within four years of the devaluation the economy had grown by more than 20 percent and industrial output had increased substantially. Among the initially poor, the major group of losers were those in the urban informal sector. For this group there was an acute increase in poverty. The government both planned and executed safety net programs for this group, but its interventions could have been larger and faster.

THE OWNERSHIP ISSUES: THE POLITICAL CONTEXT

The nineties marked the beginning of major structural reforms in the economy. So also did they usher in a process of political liberalization with the first multi-party elections in 1990. The death of President Houphouët-Boigny in December 1993 set off a period of political turbulence which subsided only with the endorsement of Mr. Henri Konan Bedie as President by the ruling party in 1995, and the presidential and Parliamentary elections that followed in that same year. The instability generated by this transition was to have significant implications for the implementation of the ESAF.

⁷² See J.C. Berthelemy and F. Bourguignon, *Growth and Crisis in Côte d'Ivoire*, Washington, D.C.: World Bank, 1996.

Interviews conducted with government officials, representatives of the ruling as well as opposition parties, and other stakeholders shed a great deal of light on the issues of governance, program ownership, the depth of social and political support for economic reform, as well as popular perceptions about the Fund's operational methods.

In general, the evidence will seem to suggest that the ESAF program, much unlike the preceding standby arrangements, benefited from a reasonable measure of national ownership, especially judged from the apparent commitment of the top levels of political leadership, and from the degree of government involvement in the preparation of policy documents, particularly the Policy Framework Paper (PFP). Indeed, government officials generally acknowledged, in interviews, that the ESAF program, and in particular the PFP, provided the occasion and opportunity for much broader consultation and consensus-building **within government** than the preceding arrangements. Whereas the standby arrangements were typically negotiated by a small technical group within the Ministry of Finance and cleared with the President, sometimes without even full-fledged Cabinet discussion, the ESAF, through the mechanism of the PFP, involved technical teams (and some ministerial oversight) from other ministries at the stage of program preparation.

Political Commitment

For purposes of a general assessment of national ownership, however, three periods can usefully be distinguished: the first period, starting with the beginning of reform efforts in the eighties and ending with the death of President Houphouët-Boigny in December 1993; the second, roughly covering the period of transition from December 1993 through the end of 1995, with the formal assumption of power by Konan Bedie as President; and the third, starting from 1996 through 1997.

The first period was predictably characterized by strong high-level political commitment stemming mainly from the decisive and highly centralized authority of President Houphouët-Boigny. Given this degree of centralization and the absence of real democratic participation, the reform efforts initially depended very little on wider societal support. Even so, it is worth noting that by the closing years of the Houphouët-Boigny era, as political liberalization dawned, deep fissures had opened in the crust of the body politic and strong popular opposition, especially to reforms in the public sector and in education, had begun. Indeed, a Stand-by arrangement approved by the Board in September 1991 ran into difficulty over disagreements about the public sector wage bill, with the Prime Minister complaining that Côte d'Ivoire had, in his view, "reached the technical and social limits of the domestic adjustment strategy".

However, it was in the second period, the period of political transition, that the sustainability of this high-level political commitment was put to the severest test. The strains of the transition

period found their most vivid expression in the implementation of the privatization program. However, the program soon became a pawn in the contest for this succession when Mr. Bedie, then as president of the National Assembly, introduced in 1993, debate in the Assembly and obtained an overwhelming vote suspending the program until a clear regulatory framework had been established. Although, on this occasion, President Houphouet-Boigny used the tremendous weight of his authority to resolve the impasse by directives to the Central Committee of the ruling party, the program remained mired in controversy after his death, in spite of a general enabling law passed in June 1994 by the National Assembly.

While the continuing slippage in the time-table of envisaged actions was in part attributable to administrative and technical problems resulting from the absence of reliable financial reports and data, it was, in large measure, the product of political factors. It was not until 1995, when the new presidency had been consolidated, that the program regained its momentum with a set of new initiatives that came to be referred to as “Bedie’s style” privatization.

Once the tensions of the transition period and the political maneuvering associated with elections subsided, the political leadership became more cohesive and its commitment to the program more resolute. Starting from the second year of the program, therefore, agreed structural reforms were carried out with greater resolve and with much less slippage. In March, a Fund mission found the results of the program “broadly satisfactory” and reported that with regard to structural reforms, the government had achieved “significant progress”.

Thus, it is fair to say that throughout much of the program period, except for the period of political transition which really began with political liberalization in the closing years of the Houphouet-Boigny era, and ended with the consolidation of power by the new presidency, the commitment of the political leadership to the reform process remained quite high. Indeed, even in the transition period, no fundamental shift in policy as such occurred.

This high level of political commitment and the relatively smooth record of program implementation was, and this is important, in part attributable to the fact that some of the most politically difficult reform issues, notably those of civil service and labor market reforms, had been largely exhausted by the time the ESAF program begun.

Scope of Support: The Depth of the Social Consensus

As noted, earlier, the pre-ESAF reforms had been undertaken under a restrictive political environment which depended mostly on the centralized authority of Houphouët-Boigny for its legitimacy. During this period, relatively little was done to inform and court the support of stakeholders outside the small circle of political actors around the President. This long tradition of non-consultation began to change only slowly with the onset of multi-party politics which paved the way for a deepening of the consultative process within the ruling party itself, and a reaching out to other political constituencies. Within the leadership of the ruling party, support for the reform program was initially restrained, in part because it threatened vested interests and also in part because there was a widespread feeling that the policy changes, in particular the structural reforms, were an imposition from the Fund.

Interviews conducted with the leadership suggest that there is now a larger body of support for the reforms. Objectively, this is no doubt because a recovery is underway. In the view of the leadership, however, this is due partly to a recognition that developments in the globalization of the economy made the changes inevitable and partly also, that the ESAF framework provided a longer-term policy framework which enabled the social impact of adjustment to be better addressed. By contrast, consensus-building with the opposition parties and with the unions and student groups appears to be inadequate, at least in the eyes of the leadership of these bodies; at any rate, dialogue with these constituencies is a rather recent development.

While there is recognition of a welcome change in the political culture towards greater inclusivity, the predominant sentiment in these constituencies is that consensus-building must be closely linked with good governance in order to be credible. In this connection, there is general agreement that a democratization of the electoral code, among other things, to rid it of provisions that are *ad hominem*, at least by implication, and the adoption, by government, of measures to arrest a return to extravagance and conspicuous consumption among the ruling political elite, would be important signals. The unions, for their part, acknowledged in interviews, that in contrast with what had prevailed in the pre-ESAF reform period when policy changes were, in their words, simply “handed down”, there is now the beginning of a tradition of consultation although this is still more formal than substantive. For instance, the new labor code, according to them, was formulated without prior consultation with them and when labor’s views were sought, the code was promulgated before their comments were submitted. There is continuing concern among labor, especially about the impact of privatization on employment.

A number of important observations need to be made on the general outlook of the political constituencies outside the ruling party. One is that in spite of lingering concerns about the social impact of the adjustment process and also about the pace and speed of change, there is general acceptance and understanding of the need for change, and the recognition that this is in the

objective interest of the country, given the general direction of global developments. Second, there was, in our view, a general conviction also in these constituencies, that greater access to information on the context and reasons for reforms would greatly facilitate the process of consensus-building and prevent disruptions in implementation caused by social protest. . These views were also broadly shared by the business community. Asked specifically during interviews, what assurances they could provide to government that if confidential documents were made available to them, they would not be exploited for political advantage, the leaders of these constituencies stressed that their commitment to the national interest and the requirement of stability for national development would rule out any betrayal of confidence for short-term political gain. They further stressed that at any rate, such short-term political gain could become a deterrent to responsible policy making and dialogue with political opponents if they (the opposition) should find themselves in power.

Authorship of Program Documents and Policy Initiatives

Most interviewees did not really see authorship of policy documents and initiatives as the critical determinant of national ownership as such. Nevertheless, they complained that Fund staff tended to stifle local initiatives in preparing drafts, preferring always to work with their own drafts. For the PFP process in particular, staff documents themselves suggest that the custom is for the first drafts to be written by Fund staff, on the basis of consultations with the World Bank. Government officials interviewed and some patchy references in staff documents suggest that there were obvious exceptions to this practice and that occasionally, government participation in the preparation of early drafts was more than token. However, the overwhelming view in government circles was that these were largely grudging deviations from well-established custom.

Technical staff in the government also stressed the need for more effective technical assistance to improve the government's capacity to prepare policy documents and strengthen the government's role in negotiations with the Fund. They acknowledged, in particular, that the secondment of Fund-based staff of national origin was a useful device and that in the case of Côte d'Ivoire, this, along with technical assistance programs with the Fund, World Bank and France had gone a long way in improving national capacity although problems remained, especially in the area of data preparation and analysis. Over the longer term, one problem that would persist in the absence of incentives comparable to those available in the private sector is the constant loss of trained personnel to the private sector.

The Fund's Operational Methods

The Role of the Resident Representative

The Fund has had a resident mission since about October 1984. Our impression is that the incumbent resident representative is rather atypical in that he has fairly extensive contacts and excellent relations, not only with the technical ministries but also with political leaders, both within and outside the ruling party. His contacts with the business community and the unions appear to be equally cordial.

The Range of Contacts

In general, the staff contacts with the country have focused on the top political leadership and the key economic ministries. Fund missions have usually had access to the Prime Minister and the Ministers for Finance, Economy, Planning, and Agriculture, as well as the National Director of the Central Bank of West African States (the BCEAO). In the course of the first mid-term review of the ESAF program, for instance, the Fund mission met with a broad range of government officials, including the Minister of Industry and Commerce, and the Minister of Agriculture and Animal Resources. One notable feature of the Fund's contacts in Côte d'Ivoire is that missions often met the President and the Prime Minister.

There are also references in the staff reports which were confirmed by interviewees in the field, to contacts between Fund staff and officials of public enterprises, as well as representatives of political parties and other interest groups, including representatives of the private sector and the bankers' association.

Interestingly, however, our impression is that this apparent broadening of Fund contacts with stakeholders in the country, outside of the traditional Fund contacts, has done little to encourage a real sense of participation among these constituencies in the process of policy formulation and generally, in the conduct of the country's relations with the Fund. This is a sentiment that was echoed in just about every country we visited, about which we will have more to say in our general observations section.

Cooperation with Donors and the World Bank

The Fund documents portray the usual picture of close cooperation with the Bank and the full participation of the Bank, both at headquarters and at the Bank's resident missions in the work of Fund missions in the country. There are also many references to the participation of Bank

staff in the preparation of early drafts of the PFP. On closer examination, however, there are indications that these relations were not always so well coordinated. This is particularly true in the area of financial sector reforms where there were apparent disagreements between the Fund and the Bank over the appropriate level of cash payments to the domestic banks from the government over the period 1991-95 in the context of domestic debt restructuring.

Government Initiatives to Promote Ownership

In the area of ownership, the government's sensitivity to the need for consensus-building among a broad range of social forces coincided with the onset of political liberalization and the surge of popular protest against measures introduced in the stabilization period to reduce the public sector wage bill and liberalize the labor market. There is every indication that the process of consensus-building is deepening with the beginnings of more effective dialogue with the opposition parties and other stakeholders although suspicions remain about the depth of the government's commitment to genuine dialogue.

MALAWI

Introduction

In Malawi the precursor to ESAF was a sustained break in the growth rate: after two decades of rapid growth, per capita GDP declined by around one percent per annum during 1979-87. This decline had three causes.

First, the growth strategy was arguably unsustainable. It depended upon high implicit taxation of the smallholder sector with the surplus used for investment in parastatals. While this caused the smallholder sector to stagnate, the parastatals became the engine of growth. Although many African countries followed this strategy, Malawi was the only one to make it work. This was at least in part because President Banda imposed hard budget constraints upon the parastatals.⁷³ By the 1980s these broke down, the parastatals sank into heavy losses, and the investment rate collapsed.

Second, the economy was hit by unusually severe external shocks. By 1987, the cumulative loss from the terms of trade decline was 65 percent of 1979 GDP.⁷⁴ Even with ideal policy responses this would have reduced investment and growth through the decade. In addition to the decline in the terms of trade, war in Mozambique broke the transport connection to the ports. By 1984 shipment costs were 2.5 times as high as in 1980 and it is estimated that this reduced the growth rate in the following five years by 1.4 percentage points per annum.⁷⁵ The war also caused an influx of almost a million refugees.

Between them these two problems were both reducing growth and affecting the budget. Revenue as a percentage of GDP declined because of the contraction in imports. Expenditure as a percentage of GDP increased because of the need for a military response to RENAMO, the refugee problem, and the accumulation of a strategic grain reserve.

Third, the initial policy response to the shocks was sub-optimal. Although there was some exchange rate adjustment, trade restrictions were increased and foreign exchange rationed, so

⁷³ See F.L. Pryor, *The Political Economy of Poverty, Equity and Growth: Malawi and Madagascar*, Oxford, Oxford University Press, 1990.

⁷⁴ Calculated from Table 2.2 of World Bank, "Accelerating Malawi's Growth: Long-Term Prospects and Transitional Problems", 1997.

⁷⁵ See Y. Van Frausum and D.E. Sahn, "Perpetuating Poverty for Malawi's Smallholders: External Shocks and Policy Distortions", in D.E. Sahn (ed.), *Economic Reform and the Poor in Africa*, Oxford, Clarendon Press, 1996.

that the currency became over-valued. It has been estimated that this over-valuation was around 40 percent and that it reduced GDP during the 1980s by 15 percent.⁷⁶

Cumulatively, these three elements severely reduced living standards. Between 1979 and 1987 both mean per capita private consumption and mean smallholder value-added fell by around a quarter (see Table 1). Since even before this decline the incidence of poverty in Malawi was among the highest in the world, by 1987 there was an acute poverty problem.

Table 1: Private Consumption and Smallholder Income, 1979-96
(K at 1978 prices)

	p r i v a t e consumption per capita	index	smallholder value added per capita	index
1979	82.1	100	252.8	100
1983	73.4	89.4	223.8	79.1
1987	62.3	75.9	242.4	75.6
1991	74.2	90.3	269.0	74.7
1993	83.2	101.3	311.1	81.4
1996	68.6	83.6	387.4	92.7

Source: *National Accounts*.

Note: The 1991 population is estimated as 9.1 million; we have assumed a population growth rate of 3.0 percent.

⁷⁶ Van Frausum and Sahn, *op. cit.*, Table 11.3.

Even by 1983 these problems were sufficiently serious to require Fund involvement, although the program was in effect aborted in 1986. At the time the program collapsed in 1986/87, the Central Bank was not able to meet external payments obligations and the budget deficit was 12.5 percent of GDP. In 1987, the government adopted a shadow program and in 1988 Malawi became the first recipient of ESAF.

The First ESAF: Program Design

The focus of the program was partly fiscal and partly structural. The fiscal objective was to reduce government expenditure from 33 percent of GDP in 1986 to 24 percent by 1991, partially offset by a planned reduction in revenue from 20 percent to 18 percent over the period. Within revenue, there was to be a switch from taxes on production to taxes on consumption. The structural objectives were liberalization of foreign exchange, productivity gains in smallholder agriculture, reform of agricultural marketing and financial liberalization. The growth objective was modest: it was anticipated that the decline in per capita GDP would be converted into a small increase.⁷⁷ Since the expectation was for little growth, the reduction in the expenditure share implied a reduction in per capita government expenditure of one quarter over five years.

The social impact of the program was explicitly considered. The government intended to increase the share of social expenditure. Since the initial share of social expenditure in total expenditure was 20.5 percent, to be fully protected from the planned reduction in total expenditure, had the planned growth of GDP been achieved, the share of social expenditure would have needed to rise to 27 percent. Plans were broadly consistent with such protection. For example, the 1988/89 budget planned to increase the share of social services to 22.6 percent. Although outturns tended to fall short of these plans, by 1992/93 the share had risen to 24.8 percent.

The structural reforms focused on trade liberalization and the smallholder sector. With respect to the latter, there was attention to raising producer prices, increasing fertilizer use, accumulating a strategic grain reserve and lifting restrictions on entry into cash crops. The likely social impact of the pricing reforms was largely positive. Overwhelmingly, poverty was rural and the reforms were aimed at raising rural incomes. However, the situation was complicated since the poorest 40 percent of smallholders were substantial net purchasers of maize, meeting only about two thirds of their requirements from their own production and so would face higher net costs from increases in maize prices. By contrast, the better off 60 percent of smallholders produced twice as much as they consumed.⁷⁸ A 1990 internal Fund document noted this problem. Since the poorer smallholders were net sellers of labor and disproportionately located in the Southern

⁷⁷ A second scenario conditional upon additional donor funding anticipated per capita growth accelerating to 2 percent.

⁷⁸ World Bank, "Malawi Human Resources and Poverty", November 1995, Table 3.22.

Region, this could have been tackled either through raising minimum wages on the estates, or through a program of targeted labor-intensive rural public works.⁷⁹ The former was indeed adopted: minimum wages were doubled in 1989.⁸⁰ The strategic grain reserve was deployed in 1990 to offset the effects of drought.

⁷⁹ Malawian smallholders are atypically integrated into labour markets. A measure of this is that out of about one million smallholder households, over 300,000 members were away working or looking for work for more than three months during 1992/93 (*National Sample Survey of Agriculture* (NSSA), 1992/93, Vol. 4, Table A6.0).

⁸⁰ Fund staff produced a study in which the impact of changes in consumer prices, producer prices and wages on the real income of various social groups was calculated. See R. Hicks and O.P. Brekk, "Assessing the Impact of Structural Adjustment on the Poor: the Case of Malawi", IMF Working Paper 91/112.

The First ESAF: Outcomes

Fiscal adjustment was gradual but effective: by 1991 the fiscal deficit (including grants) fell to 3 percent of GDP.⁸¹ By contrast, structural adjustment was limited. Agricultural marketing remained heavily controlled, and the exchange rate remained over-valued. The net effect on growth during 1987-91 was that per capita GDP continued its decline but at the more moderate rate of 1 percent per annum. Van Frausum and Sahn estimate a 'pure' effect of the ESAF foreign exchange inflow in the absence of policy changes and this seems the most pertinent characterisation of the impact of the first ESAF. They estimate that the inflow increased GDP substantially, by around 4 percent relative to the counterfactual.

From 1992 the fiscal position rapidly collapsed. There were three further shocks in 1992: the most severe drought of the century during which maize output fell by 60 percent; a cut-back in aid of nearly 4 percent of GDP as donors pressed for political liberalization; and a 68 percent wage increase in the public sector in response to labor unrest. This was followed by a period of contested elections, a change of government, and a further drought, culminating in a deficit (including grants) of 15 percent of GDP in 1994/95. One of the last acts of the old government was to float the exchange rate, the rate against the dollar falling from 4.4 to 15.3. The combined effect of the shocks and the fiscal collapse was that per capita GDP declined by 8 percent between 1992 and 1994.

The Second ESAF

In 1995 the new government adopted a new ESAF Program. This envisaged rapid fiscal adjustment, reducing the fiscal deficit to 4 percent by 1995/96. Government expenditure was planned to fall from 42 percent of GDP in 1994/95 to 28 percent in 1998/99. The structural reforms included privatization of public enterprises, civil service reform, the elimination of the restrictions on smallholder access to land and cash crops, and the liberalization of agricultural marketing. The net effect of the reforms was expected to raise the growth of GDP per capita to 1.5 percent per annum.

There is evidence that the agricultural reforms would indeed be addressing the constraints faced by the rural poor. As of 1990 among the poorest smallholders nearly a fifth considered government regulations or transporting and marketing as the most important constraint on new

⁸¹ This is inclusive of interest payments on domestic debt of 2 percent of GDP. Nearly all of this was in fact debt reduction since real interest rates were much lower than nominal interest rates.

enterprise. However, a further tenth identified lack of technical information as the most important constraint, while enhancing the extension service was not a focus of program design.⁸²

The envisaged reduction in the government expenditure share and GDP growth implied a fall in per capita real public expenditure of 34 percent between 1994/95 and 1998/99. Despite this, social expenditures (on health and education) were planned to increase, not just absolutely, but as a share of GDP, from 4.5 percent to 6.4 percent. As part of this, primary school fees were abolished, leading to a 50 percent increase in enrollment. Although this was fiscally demanding, it should be noted that expenditure in 1994/95 was highly atypical, so that much of the adjustment could be achieved simply by reverting to the pre-crisis budget.

The program was explicitly designed to be pro-poor. It was again explicitly recognized that the poorest were net purchasers of maize. In order to mitigate the negative effect of envisaged food price increases on this group the program included public works, targeted input programs, and supplemental food programs. An innovative feature was the Malawi Social Action Fund in which rural communities themselves identified and part-financed projects. The program faced some difficulties because of the absence of democratic institutions of government at the local level.

To date, the program has been highly successful. Fiscal stabilization was achieved very rapidly with the fiscal deficit falling to 3.8 percent by 1996/97. Combined with favorable weather, the growth effect was dramatic: per capita GDP may have grown by 5.6 percent per annum during, 1994-1997.⁸³ The effect of the agricultural pricing reforms alone has been estimated to increase GDP by around 3 percent.⁸⁴ The effect of the exchange rate adjustment implemented just before the change of government was probably much larger. Recall that the effect of a full exchange rate liberalization (40 percent real devaluation) was estimated to raise GDP by around 16 percent. Although the actual devaluation was initially even larger than this, it was rapidly eroded to about 20 percent by 1996. Its effect on growth was nevertheless probably larger than that of the agricultural reforms. During the financial liberalization, real interest rates were initially heavily negative, but by 1997 had risen to around 16 percent. The banking sector remained uncompetitive: liberalization had focused more on interest rates than on market structure.

⁸² HESSEA Survey of 1990/91. We report the responses of the poorest 40 percent of smallholders in the Southern Region, the poorest of the three regions, Table 29, p. 330.

⁸³ This estimate is based on provisional National Accounts data at 1994 prices.

⁸⁴ Van Frausum and Sahn, *op. cit.*, Table 11.3.

Distributional Effects of the ESAFs

The First ESAF

There are two routes by which the ESAF might have had a social impact, through changes in household incomes and through changes in social expenditures. We consider these in turn.

During the first ESAF there was little structural change. Further, although the decline in the economy was halted, there was no growth in per capita terms in GDP. Hence, one would expect that the impact on incomes would be rather limited. A more sophisticated basis for expectations of the impact on incomes comes from a simulation model.

The main effects of the program were to augment foreign exchange inflows and to contain public expenditure. The distributional effects of the 'pure' foreign exchange inflow has been simulated by Van Frausum and Sahn. Their results suggest that the benefits from a pure foreign exchange inflow would accrue disproportionately to urban social groups: urban wage earners, particularly those in the government sector, and the corporate sector. Conversely, the shares of income accruing to smallholders and estate labor would be reduced. In absolute terms they estimate that for smallholders the adverse distributional effects outweigh the positive overall effect of ESAF on GDP of 4 percent. Smallholder incomes fall by 2 percent as a result of a 'pure' ESAF program without policy change.

The limited evidence on incomes broadly bears out the predictions of the simulation model. Between 1987 and 1991 according to the national accounts per capita smallholder real income was virtually constant. This is supported by a comparison of household surveys for 1984/85 and 1990/91 (see Table 2). Both surveys showed the Southern Region to be much the poorest. Real wages in manufacturing rose by 3 percent. The main deviation from what one would expect on the basis of the model simulations is that the real wages of estate workers rose by 15 percent. However, this reflects that the model does not take into account the social targeting through the increase in the minimum wage on the estates.

Table 2: Survey Evidence on Real Incomes of Smallholders during the First ESAF

(K in 1990 prices)

	Southern	Central	Northern	All
1984/85	695	1305	1301	990
1990/91	568	1300	1411	909
1992/93				452

Source: for 1984/85 from Pryor, *op. cit.*, Table 16-3; for 1991/92 from HESSEA, Tables 15 and 38; for 1992/93 from NSSA, as reported in Table 3.1 of World Bank, *Malawi: Human Resources and Poverty, op. cit.*, converted to household income by assuming a rural household size of 4.4, as cited in Table 2.1. For 1984/85 and 1990/91 the figure is mean income, for 1992/93 the figure is for median income which will be somewhat below mean income. Deflators are from *Malawi Statistical Yearbook, 1995*, rural CPI, and from SM/93/7, Table 10.

We now turn to the impact via social expenditure. Table 3 brings together the input measures of budgetary expenditures on health and education with various output measures.

As discussed in the Zimbabwe section, there are two possible concepts of real government spending. In one case, a value concept is derived by deflating nominal figures by the aggregate GDP deflator. In the other case, a volume concept is derived by deflating nominal figures by an index of costs which in the case of health and education will be dominated by wages. These two approaches may lead to very different results, as indeed was the case in Zimbabwe where wages declined sharply in terms of the GDP deflator. For Malawi, using the first approach, the government maintained total health and education expenditure constant, although this implied a fall in per capita terms (see Table 3). Although there are no official sector-specific deflators for the health and education sectors, we can construct one by using data on the earnings of government workers in community, social and personal services which correspond closely to health and education. The results indicate that wages fell substantially (by 20 percent) relative to the aggregate GDP deflator. As a result, whereas the value concept shows a deterioration, the volume concept implies an improvement. The volume concept implicitly assumes that quality is constant. To the extent that the decline in real wages led to a deterioration in staff performance, the volume measure over-estimates the real delivery of social services. Hence, both the value and volume measures are biased, but in opposite directions. Since the former suggests a deterioration by around 10 percent and the latter suggests an improvement by about 10 percent, the most reasonable inference is that there was little change in real social service delivery per capita during the first ESAF.

Whereas per capita real inputs into health and education appear to have stayed broadly constant, there were significant improvements in the outcome measures shown in Table 3. In health,

ante-natal attendance and immunizations both increased and infant and child mortality both fell. In education, primary school enrollment increased very substantially. However, we should note that the absolute levels of the various indicators are poor even by the standards of low-income countries. Hence, there is some evidence that the productivity of social services increased during the period and that this led to improved outcomes.

Table 3: Health and Education Indicators during the first ESAF
(index per capita, 1987 = 100, unless specified)

Indicator	1987 (or nearest)	1991 (or nearest)
<i>Health</i>		
health expenditure (value)	100	90
health expenditure (volume)	100	113
Ante-natal attendance	100	121
Infant mortality (per 1000)	138 (1985)	134 (1990)
Child mortality (per 1000)	125 (1985)	115 (1990)
Immunizations: BCG	100	99
DPT	100	113
Polio	100	106
Measles	100	131
<i>Education</i>		
education expenditure (value)	100	88
education expenditure (volume)	100	110
Primary school enrollment	100	139

Sources: ante-natal attendances: *Statistical Yearbook, 1995*, Table 3.13; infant and child mortality: *Malawi Social Indicators Survey, 1995*; immunizations: *Statistical Yearbook, 1995*, Table 3.16; health and education expenditure from SM/93/7, Table 14, deflated by the GDP deflator for the value series from Table 1. Deflated by government wages in community, social and personal services from *Statistical Yearbook, 1995*, Table 6.4 for the volume series. The wage data are for 1987-90, rather than for 1991. To the extent that wages declined between 1990 and 1991 this is an underestimate; enrollments from *Statistical Yearbook, 1995*, Table 4.7.

In summary, during the first ESAF period the incomes of the poor were broadly constant, while social expenditure was protected and indeed social indicators showed some improvement.

The Phase of Program Collapse

Between the two ESAF programs, Malawi experienced a series of shocks as discussed above. For smallholders, the most important one was the 1992 drought. This is reflected in the fall in smallholder incomes shown in Table 2. The halving of income shown in that table overstates the decline because the figure for 1992/93 is for the median rather than the mean. However, there is no doubt that smallholder incomes fell substantially: the maize crop fell by 60 percent in the drought year. Also in the 1992/93 NSSA survey a large number of smallholders reported that their income had fallen even in nominal terms from the preceding year, at a time when inflation was around 20 percent. Wage earners, both rural and urban, also lost heavily. Real earnings declined by around 30 percent between 1990 and 1994. Thus, during the period of program collapse all major social groups lost heavily.

The Second ESAF

During the second ESAF, there has been both substantial structural reform and substantial fiscal adjustment. The structural reforms would be expected to have substantial distributional effects.

The Van Frausum and Sahn simulations can again be used to estimate the distributional effects of the agricultural price and exchange rate reforms. Recall that an important distinction among smallholders in Malawi is that the poorer half are net buyers of maize whereas the better off are net sellers. We are able to approximate this effect by distinguishing between smallholders below and above holdings of 1.5 hectare. According to the simulations, the incomes of the poorer smallholders rose by 13 percent as a result of the pricing reforms and by 3 percent as a result of the devaluation. The incomes of the better off smallholders are affected more substantially by agricultural liberalization, with incomes increasing by 33 percent, and also by devaluation, with incomes rising by 5 percent.

Compared with the economy as a whole, smallholders thus gained much more from the agricultural liberalization and much less from the exchange rate liberalization. The relatively weak effect of the exchange rate reflects the fact that smallholders are net purchasers of foreign exchange, buying imported fertilizer, but that they produce a non-tradable good, namely maize. In this distribution respect Malawi is rather distinctive. Usually, smallholders are regarded as disproportionate beneficiaries of exchange rate depreciation because they are sellers of tradable crops while purchasing few imports. Malawi is distinctive partly because its very high transport costs make maize non-tradable over a wide price range, and partly because at the start of the reforms the group of smallholders growing tradable crops such as tobacco was so small.

Whereas smallholders are predicted to have gained quite substantially from the combination of agricultural and exchange rate liberalization, the model predicts that estate workers would face a serious decline in their income of 25 percent. This reflects increasing food prices in the face of nominal wage rigidities.

There are as yet no data at the household level with which to check these predictions. National accounts data suggest, however, that distributional changes have indeed been large. First we consider smallholders. To abstract from the effects of the 1994 drought, we compare data for 1996 with those for 1993. This comparison suggests that per capita smallholder real income went up by 14 percent (Table 1).⁸⁵ This reflects the previously untapped potential for raising incomes by diversification. In 1992/93 incomes of households whose main occupation was tobacco growing was 2.3 times as high as that of households whose main occupation was maize growing. Three quarters of smallholder households had their main occupation as maize growing, whereas only 6 percent were growing tobacco.⁸⁶ Between 1993 and 1997 the number of smallholders engaged in tobacco approximately doubled.

For the whole economy, per capita real income declined over the same period by 3 percent, so that smallholders appear to have gained relative to the economy as a whole. This is consistent with the model predictions for a large agricultural reform and a modest exchange rate liberalization, such as has characterised the ESAF to date.

By contrast, formal sector wage earners lost, at least in the short term. In the urban economy, real wages fell by 38 percent between 1994 and December 1995. This was subsequently offset by wage increases following strikes in 1996. In this case the losers, urban wage earners, were initially considerably better off than the gainers, smallholders. In this sense, therefore, there was not a case for a safety net targeted at this category of losers. In addition, an important policy change has been the deregulation of trading and petty manufacturing activities in urban areas. This has created opportunities for income generation in urban households and has therefore provided a self-selecting safety net for the urban poor.

However, this does not apply to a second category of losers, namely estate workers. Comparison of living standards between estate workers and smallholders is difficult but a survey conducted in 1994 concluded that the welfare of women and children on the estates was broadly comparable with that among the poorer smallholders.⁸⁷ As predicted by the model, estate workers lost heavily. Between 1994 and December 1995, an estate worker receiving a wage entirely in cash would have seen its real value halved.⁸⁸ In practice, to varying degrees, estate workers received

⁸⁵ The National Accounts on which we base these calculations are in 1978 prices. A new series based on 1994 prices is under preparation and may qualify these results.

⁸⁶ *National Sample Survey of Agriculture, 1992/93*, Volume 4, Tables A3.0 and A5.0.

⁸⁷ W.C. Dede Kamkondo and K. Wellard, "Women and Children in the Smallholder and Estate Sub-Sectors in Malawi", Rural Development, Bunda College of Agriculture, Lilongwe, 1994.

⁸⁸ This and the urban real wage change have been calculated from *Monthly Statistical Bulletin*, May 1997, Tables 4.1, 11.5 and 11.6, and *Statistical Yearbook, 1995*, Table 6.3. Agricultural and non-agricultural wages were deflated by the rural and urban CPI, respectively.

part of their income in kind in the form of maize. However, even allowing for this, there was a severe decline in real incomes which would have warranted targeted safety net intervention. During the first ESAF, the government had indeed achieved this through an increase in the minimum wage. Since the inflation during this period was much more rapid than during the equivalent phase in the first stabilization program, there was a much stronger case for intervention.

The second ESAF envisaged a rapid growth in social expenditures driven by a reallocation of the budget. This has been reinforced by the rapid GDP growth between 1994 and 1997. Hence, the expectation is that real value of social service delivery will have increased. This is likely to have been augmented by a fall in the unit cost of social service delivery as over most of the period real wages in the government sector have been lower than in 1994. The most striking evidence of improvement in service delivery is that enrollment in primary education increased by over 60 percent in 1994/95, after school fees were abolished. The change was strongly pro-poor: enrollment rates had been considerably lower for the children of poor households and these differences were reduced.⁸⁹

Against this major improvement in education, there is some evidence of a decline in the coverage of EPI immunizations due to a cut in outreach activities as a result of reductions in the health budget: between 1992 and 1995, the proportion of children fully immunized fell from 82 percent to 75 percent. Over the same period, there was an increase in the incidence of severe wasting from 5.4 percent to 7 percent.⁹⁰ However, both of these deteriorations might have taken place during the 1992-94 period of program collapse. There is also evidence of a reduction in the availability of drugs, possibly due to excessive expenditures on the capital program in the health budget. These problems are compounded by the growing prevalence of AIDS. It is estimated that deaths from AIDS will more than quadruple between 1995 and 2000 by which time AIDS cases will be absorbing half the health budget.⁹¹ As yet it is not possible to verify other aspects of social impact against evidence from performance indicators.

In summary, while during the first ESAF the social impact was modest, that of the second ESAF was substantial. The most important effect was the increase in smallholder income. The groups which lost in this period included urban workers who were not initially among the core poor, and the estate workers who were. This latter group was not sufficiently protected in contrast to

⁸⁹ F. Castro-Leal, *Who Benefits from Public Education Spending in Malawi?*, World Bank Discussion Paper, No. 350.

⁹⁰ *Malawi Social Indicators Survey, 1995*, Fig. 6.2.

⁹¹ B. Lodh, "Economic Impact of AIDS", mimeo, UNICEF, Lilongwe, no date.

interventions during the first ESAF. Social services delivery provides a mixed picture. There was a massive improvement in access to primary education, while some of the health indicators deteriorated.

Conclusion

The first ESAF was characterized by temporarily successful fiscal adjustment, but without substantial structural adjustment. Any social impact of this program was modest. The incomes of the poor were broadly unaltered as were social expenditures, while social indicators improved somewhat. The second ESAF was also fiscally successful, indeed making a much larger correction over a much shorter period. However, in contrast to the first ESAF, it was also a process of structural adjustment. Both the foreign exchange and agricultural markets were substantially liberalized. The structural adjustment produced powerful distributional effects with smallholders gaining and urban wage earners losing. This redistribution was progressive.

However, during the period, estate workers, who were already among the core poor, lost substantially. This cannot be attributed to the ESAF but rather to the inflation which was inherited from the period of program collapse. In the absence of ESAF, this group might well have lost more as inflation would have been even higher. It is to be noted that wage earners are likely to suffer substantial short-term income losses during bouts of unexpected rapid inflation. It is relatively straightforward to protect formal sector wage earners from these effects, as indeed the Malawian government did during the earlier ESAF. However, in Africa most formal sector urban wage earners are not among the core poor, so that intervention on the basis of a safety net argument cannot readily be justified. The estate workers in Malawi constitute a group for which intervention is justifiable on a safety net argument, and for whom targeting is straightforward.

While the second ESAF can be considered as successful, the economy is still far from reaching its growth potential. The transformation of smallholder agriculture has only just begun and is still suffering from weak marketing and transport infrastructure. Investment in the formal sector has yet to become substantial. The large number of Malawian entrepreneurs living abroad constitutes a resource of considerable potential for the economy (as in Uganda), but there not as yet been much return migration.

OWNERSHIP ISSUES

The Political Context

After 30 years of repressive and autocratic rule under President Banda, Malawi succumbed to pressure from the international donor community and domestic democratic forces and finally, in 1992, began a process of political liberalization which culminated in elections that brought to power a new government in 1994. The first ESAF arrangement and its precursor programs were thus managed under a highly-centralized decision-making system with very little consultation outside the Ministry of Finance and the Reserve Bank of Malawi although a loose coordinating body, including senior ministers, heads of the security agencies, and representatives of the ruling party, provided some sort of general oversight through periodical meetings.⁹²

The ESAF arrangement spanning the period 1988-94 had mixed results; the fiscal adjustment it entailed was reasonably successful while the structural benchmarks suffered significant delays in implementation.⁹³ But the restrictive political system under which these reforms had been carried out, had begun to crumble already in the closing years of the Banda regime, as political liberalization began with the repeal or modification of repressive laws in August 1992, and the rise of opposition parties following the referendum in June 1993, which ended one-party rule. Already in September 1993, there were strikes by the civil service demanding increases in salaries and wage compensation, and calling on the government to resign.

The new government took over in a situation of profound fiscal crisis caused by large and unplanned civil service wage increases, and expenditure overruns mainly associated with the elections. These problems had been further compounded by rising food prices, followed by a major drought during the 1994 crop season, and consequent acceleration in inflation.

Ownership of Policy Reforms

Against the background of this crisis, caused by two major droughts (1991-92, 1994), the suspension of donor aid, and the fiscal deterioration noted above, the new government sought

⁹² Interviews, August 1997.

⁹³ The agricultural sector reforms included the lifting of restrictions on smallholder production and private sector participation in marketing and distribution of agricultural products, and in the parastatal sector, included a restructuring of a number of state monopolies, mainly the Agricultural Development and Marketing Corporation (ADMARK) and the Press Corporation.

Fund assistance and an eight-month standby arrangement was granted in November 1994 to help stabilize the economy, and create conditions for the adoption of an ESAF arrangement.

This stand-by arrangement was prepared in rather difficult circumstances. The government was not only new; it had inherited an enormous crisis and was confronted with a restive civil service whose loyalty could not be taken for granted. In the event, the Fund's intervention coincided with large Bank and donor missions, all of them thoroughly well-intentioned but perhaps not mindful enough of the capacity constraints that the new government faced. Indeed, the government recognized these constraints when, in January 1995, it worked out a national capacity-building program for financial management, jointly with representatives from the Fund, the UNDP, the Bank, the EU, and bilateral donors, outlining its technical assistance needs and possible funding sources. In the very nature of the situation, even this capacity-building program was not exactly the government's product, as it required government "endorsement" in August 1994.

Apart from these capacity constraints, the new government also had to contend with other political problems. The labor situation was tense, as was the political temperature, following the arrest of the former President on murder charges.

The Fund staff clearly appreciated these constraints in a remarkable assessment of the overall situation in an internal Fund document but saw them, not so much in terms of their effect on national ownership and the implications therefrom for the longer term sustainability of the program, but as short-term "risks" that could be "minimized to the extent there is sufficient coordination in the reform process to ensure that potential bottlenecks are arrested in a timely manner." Key policy makers, it continued, "*would also need to be focused and made aware of the broad objectives of the program.*" In this regard, it would be useful to engage a broader section of the government in the preparation of the PFP."

The government was required to take a number of prior actions⁹⁴ before the standby arrangement followed in November 1994.

Not surprisingly, the government ran into considerable difficulty in implementing the agreed reforms. To begin with, the drought in 1994 turned out to be even more devastating than was originally envisaged, and GDP declined by 12.4 percent instead of a programmed 9.3 percent decline. Widespread food shortages caused by the drought, a sharp depreciation of the currency,

⁹⁴ The prior actions included substantial increases in petroleum product prices (131 percent for kerosene, 85.3 percent for diesel, and 27.5 percent for petrol) and other revenue measures, a revised cash budgeting system, and an increase in the rediscount rate, among other things.

and the effects of the increases in the prices of petroleum products, among other things, led to an acceleration of inflation which shot up to 66 percent by the end of 1994, against a target rate of 37 percent.

A sense of hopelessness and a feeling of imposition quickly took hold in the top levels of government as they struggled with the political fallout from these hardships. Indeed, this feeling of imposition still pervades the upper echelons of government and the ruling party, and is also very evident in the outlook of key ministers, including the Minister of Finance, with significant implications for the sustainability of the ESAF program in Malawi.⁹⁵ In the business community, no less, the feeling is even more intense. Our meeting with the business community in Blantyre was perhaps the most hostile of all the meetings we had during our country visits. Malawi was also where we found the Fund's image to be the most negative, generally.⁹⁶

The Scope of Support for the Program

Initially, commitment to the program at the top levels of government, including especially the Ministry of Finance, was most determined.⁹⁷ The situation was critical, resources were required, and therefore the government made the policy compromises required to obtain access to external funds. But the base of political commitment in government generally was, from the very beginning, rather narrow. The program was largely borne on the shoulders of the Minister of Finance at the time – a highly capable and dedicated patriot who acted from a genuine conviction that the path chosen was the right one, even if less traveled by. But the result was the increasing isolation of the Minister of Finance as other ministers, and organized groups, including the business community, remained unconvinced and alienated. For the business community, the alienation was deepened by the imposition of an export tax which had evidently been

⁹⁵ A number of donors interviewed in Lilongwe also expressed concern that the program had been imposed upon an inexperienced and ill-prepared government, without due regard for the critical economic and political conditions it faced. (Interviews, Malawi, August 25, 1997).

⁹⁶ Some in the business community blamed the Fund, even for the sins of others. For example, one of the most bitter complaints was the passing of a new industrial relations act which, in their view, contained unreasonably permissive provisions on strikes and which they blamed the Fund for. When we pointed out that this legislation had nothing to do with the Fund and had in fact, been proposed by the International Labor Organization (ILO), we were met with a retort that the ILO must have been directed to do so by the Fund! The Fund, it would seem, is often perceived as having a pre-eminent position among international organizations but this obviously comes with great costs!

⁹⁷ The stabilization measures were greeted with widespread strikes all over the country which the government resisted firmly. It faced off a strike by civil servants in August 1995, arguing that no accommodation could be provided before the following fiscal year. And further, that any further salary increases could only be granted in the context of a general rationalization and reduction in the size of the civil service.

implemented as a once-and-for-all revenue measure but which they, and other donors regarded, quite correctly, as thoroughly irrational.⁹⁸

The bureaucracy, for its part, remained half-hearted at best and mostly cynical about the reforms, and about the role of the rising numbers of well-paid external technical advisors. In these circumstances, the Minister of Finance, as head of the economic management team, had little choice but to put together and work with a small core team, leaving the rest of the ministry and the officials of the Ministry of Planning marginalized and resentful. As the policy agenda got larger with time, and with little relief from uncoordinated technical assistance from different agencies, which the Minister of Finance gratefully acknowledged but sought in vain to better target, the core team quickly became overstretched.

For the majority of the rural poor, including smallholders from around the capital, Lilongwe, frustration over the removal of fertilizer subsidies was very intense. They bitterly complained that these subsidies had been removed without much explanation, and what was more, without any steps being taken to give them access to any form of credit, given that the existing rural credit scheme had all but collapsed under the weight of a high incidence of non-recovery.⁹⁹

Among donors, there was a feeling that policies were not being thought through enough, except where the Fund had a direct interest such as, for instance, the Value-Added Tax (VAT) although even here, they thought the timing was wrong. There was a sense that too many initiatives were being undertaken by different donors, that nobody seemed to be in charge. The Bank, it was felt, had become overpowering and much too obtrusive in its work in Malawi, often to the great irritation of political leaders; there was some expectation that in such circumstances, the Bank would have been “called to order” by the Fund. The general impression was that the absence of a Fund resident representative was not helping matters in this regard.

Authorship of the Policy Agenda

In the final analysis, authorship of the policy agenda and policy documentation is a function of technical capacity which, as we have noted in Malawi’s case, was severely constrained. The ruling party has had a pro-reform posture from the very beginning. Indeed, the party had declared itself in favor of liberalization and privatization in its election manifesto. However, political opposition and weaknesses in the administrative and technical capacity of the civil

⁹⁸ Interviews, August 1997.

⁹⁹ When asked what they would do if some benefactor handed them US\$1,000 each, peasant farmers (mostly women) interviewed around Lilongwe, each replied without any hesitation and in a remarkable attestation to their determination to break out of the stranglehold of poverty, that they would buy fertilizer, and more fertilizer. (Interviews, August 1997).

service had imposed real constraints on the government's space for maneuver. Moreover, donors also often push agendas of their own.¹⁰⁰ Given the government's limited technical capacity and the pressures on such capacity as there is, the PFP process and the entire policy agenda setting has tended to be dominated unduly by the Fund.¹⁰¹

Ownership Promotion

While there are no references to any particular initiatives for the Fund to deepen the ownership of the program, there are references to internal Fund documents that suggest, and again this was confirmed by interviewees in the field, that Fund missions have in the past held meetings with the Economic Committee of the Cabinet "to convey the message that remedial actions are immediately required."

As for the range of Fund contacts, staff reports suggest, and again this is corroborated in the field, that missions have interacted mostly with the usual core team, mainly the Ministry of Finance, Ministry of Planning and Reserve Bank officials. They also have had regular meetings with the donor community, and occasional ones with private sector representatives.

Cooperation with the Bank

Staff documents contain the usual references to full and close cooperation with the Bank, with the participation of Bank staff in meetings of Fund missions, especially joint discussion of the PFP. While there is no reason to doubt that the cooperation is as described in these documents, it is worth noting that the perception of some donors in the country was that the Bank takes initiatives without due consultation with the donor community or with the Fund in areas of common interest.¹⁰²

¹⁰⁰ An anti-corruption bill passed in the context of the civil service reform program was probably done under pressure from the Overseas Development Association (ODA) of the UK, after the ODA Minister reportedly threatened to cut aid to any country that failed to exercise accountability and transparency. (*New African*, May 1994: 43).

¹⁰¹ Interviews, Ministry of Finance, Malawi, August 1997.

¹⁰² The donors made particular reference to an instance when just weeks after the May 1997 consultative group meeting on Malawi, the Bank sent a letter to the Minister of Finance, which it apparently also sent to the President, protesting an increase in the number of ministries contrary to commitments made by the government. This letter evidently caused great disquiet among the Cabinet, and also among donors who felt that the Bank's intransigence over the matter (the Bank had sent two missions to protest the issue even after the government had explained the situation) created unnecessary awkwardness in relations between the government and the donor community, including the Bank and the Fund.