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The IMF and the Poor

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Prepared by

Sanjeev Gupta
Benedict Clements
Calvin McDonald
Christian Schiller

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The following symbols have been used throughout this paper:

. . . to indicate that data are not available;

— to indicate that the figure is zero or less than half the final digit shown, or that the item does not exist;

– between years or months (e.g., 1994–95 or January–June) to indicate the years or months covered, including the beginning and ending years or months;

/ between years (e.g., 1994/95) to indicate a crop or fiscal (financial) year.

"Billion" means a thousand million.

Minor discrepancies between constituent figures and totals are due to rounding.

The term "country," as used in this paper, does not in all cases refer to a territorial entity that is a state as understood by international law and practice; the term also covers some territorial entities that are not states, but for which statistical data are maintained and provided internationally on a separate and independent basis.

Preface

This pamphlet is a revised version of a paper prepared for the Development Assistance Committee's Forum on Key Elements for Poverty Reduction Strategies, held in Paris on December 4–5, 1997. The authors would like to thank Peter S. Heller and Louis Dicks-Mireaux for their very helpful comments on an earlier draft. Elisa Diehl of the IMF's External Relations Department edited the pamphlet and coordinated its production.

The IMF and the Poor

The Poor and the IMF's Mandate

The mandate of the IMF, as laid out in its Articles of Agreement, is to promote international monetary cooperation, balanced growth of international trade, and a stable system of exchange rates.[1] Since the late 1970s, some elements of the IMF's operational policy advice have evolved significantly.

In earlier periods, the IMF's policy advice emphasized the management of aggregate demand with the aim of creating conditions for macroeconomic stability. In recent years, the focus and the scope of the IMF's work have broadened, and the structural and social aspects of fiscal policy have become increasingly important, both in programs that the IMF supports in members undertaking reforms (IMF-supported programs) and in its general policy advice (Tanzi, 1997). A major element of this advice now is how to facilitate "high-quality growth" (International Monetary Fund, 1995). High-quality growth can be defined as growth that (1) can be sustained and does not collapse in the face of the slightest external shock; (2) is accompanied by appropriate domestic and external balances as well as by adequate investment, including in human capital, so as to lay the foundation for future growth; (3) is accompanied by policies that protect the environment; and (4) is accompanied by policies that attempt to reduce poverty and improve the equality of opportunity (Camdessus, 1990). This paper focuses on the last component of high-quality growth—reducing poverty and improving equity—and describes how the IMF works to achieve these objectives in its three core activities of surveillance over member countries' economic policies, financial support for adjustment programs, and technical assistance.

[1]The purposes of the IMF, as laid out in its Articles of Agreement, are "(i) to promote international monetary cooperation . . . ; (ii) to facilitate the expansion and balanced growth of international trade, and to contribute thereby to the promotion and maintenance of high levels of employment and real income . . . ; (iii) to promote exchange stability, to maintain orderly exchange arrangements among members . . . ; (iv) to assist in the establishment of a multilateral system of payments . . . ; and (v) to give confidence to members by providing temporary financial resources to help them correct balance of payments disequilibria."

IMF Policy Advice and the Poor

IMF policy advice can benefit the poor by influencing a country's macroeconomic policies, design of social safety nets, and public expenditures.

Sound Macroeconomic Policies

Through its policy advice, the IMF seeks to promote sound monetary, fiscal, and exchange rate policies to help countries achieve macroeconomic stability. Even in the short term, such macroeconomic stability directly benefits the poor because it implies low inflation and realistic exchange rates. More important, a sustainable macroeconomic framework is critical for achieving broad-based growth over the long term, which is necessary for alleviating poverty (Squire, 1993; Ravallion and Chen, 1996).

A country that fails to correct serious macroeconomic imbalances often suffers serious social costs. When inflation is high and variable, the poor and those in middle-income groups are affected the most because they usually have limited access to mechanisms that can protect consumption levels, such as interest-bearing checking accounts or other deposit accounts in stable foreign currencies, and a limited ability to purchase goods on credit. High inflation can also erode the tax base—and consequently affect the government's ability to maintain social expenditures—and has an adverse impact on investment decisions. Increasing evidence shows that countries with high inflation rates have lower investment ratios and slower economic growth. Even intermediate levels of inflation (10–40 percent) have been shown to hamper growth (International Monetary Fund, 1997a).

The source of inflation in many countries is excessive borrowing from banks by government to finance its spending. An important element of IMF policy advice, particularly in the context of IMF-supported programs, is therefore to limit the government's access to bank credit while ensuring that the private sector receives an adequate share of total credit. The quality of fiscal adjustment is also critical: changes in government spending or tax policy should be sustainable and have a lasting impact on the fiscal balance over the medium term.

Exchange rate policy is an important element of the policy mix designed to achieve macroeconomic stability. An overvalued exchange rate is likely to negatively affect the incomes of the rural poor, whose liveli-

hood is often dependent on agricultural exports. Correcting exchange rate overvaluation should eventually lead to an increase in output and employment in the export sector. However, the reallocation of resources induced by changes in the prices of goods and services that are internationally traded relative to those that are not takes time and is often accompanied by employment and welfare losses in sectors that the government had previously protected.

Sound macroeconomic policies and a stable macroeconomic framework alone will not create the conditions necessary for economic growth. Usually, structural reforms—designed to ensure continued growth by promoting efficient resource use and providing incentives for competition and private initiative—are also needed. These reforms include eliminating distortions in tax and expenditure policies and their management; liberalizing prices and interest rates; restructuring public enterprises to foster conditions for sustainable growth and job creation in the medium term; reforming financial institutions to make it easier for people in rural areas to obtain credit; changing labor market policies to enhance competitiveness and increase employment; limiting administrative intervention in the economy; and reducing opportunities for corruption (International Monetary Fund, 1997b).

Social Safety Nets to Protect the Poor in the Short Term

Some reforms that are designed to achieve macroeconomic stability and remove impediments to long-term sustainable growth may hurt some of the poor in the short term. Examples are the removal of generalized price subsidies on basic products; an exchange rate devaluation, which typically hurts urban consumers of imported goods; the reduction of budgetary subsidies to state enterprises; civil service reform; and the lowering of protection associated with trade liberalization. These reforms can cause a decline in the real incomes of the poor and losses in employment. To mitigate these adverse short-term effects on the poor and other vulnerable groups, many IMF-supported programs incorporate budgetary outlays on temporary social safety nets to transfer income or protect consumption (Chu and Gupta, 1998).

Safety nets can enhance the political support for reforms. In helping governments design safety nets, the IMF considers their cost-effectiveness and financial viability. Safety nets may include subsidies directed at particular groups or cash compensation in lieu of subsidies; an improved distribution

of essential commodities, such as medicine; temporary price controls on some essential commodities; severance pay and retraining for public sector employees who have lost their jobs; and employment through public works programs. Many of these elements can be found in the recent reform programs in Asia (see, for example, Gupta, McDonald, Schiller, Verhoeven, Bogetić, and Schwartz, 1998). When possible, existing social security arrangements, such as unemployment insurance and pensions, are modified to protect vulnerable groups from the adverse effects of economic reform. This was the case in countries making the transition from a centrally planned to a market economy (see, for example, Chu and Gupta, 1998).

Improved Composition of Public Expenditures

A reallocation of public expenditures can benefit the poor in the long term by shifting resources to (1) activities that promote growth (for example, productive investment spending) from expenditures that do not contribute to the goals of government policy (for example, untargeted, generalized subsidies and excessive military outlays); (2) basic education and health care, which build human capital and thus enhance growth and equity; and, of course, (3) targeted poverty alleviation programs.

A key step in reallocating expenditures toward growth-enhancing outlays is to reduce "unproductive" public expenditures—those that can be reduced without affecting the achievement of government's outputs or objectives, such as the provision of law and order or basic education and health care. Often, when the government pursues multiple objectives in its public expenditure programs—such as using the public sector as the employer of last resort—and when weak institutions or corruption exists, unproductive expenditures result (Chu and others, 1995).

In reorienting budgetary expenditures toward capital outlays, IMF-supported programs are intended to reflect realistic expectations of a country's ability to implement capital projects and the availability, on appropriate terms, of external financing during the program period. The objective is to ensure that capital projects add to the productive capacity of the economy and that adequate resources are allocated to operations and maintenance. Given that capital spending can also be affected by revenue shortfalls, IMF-supported programs recognize the importance of protecting critical public investment programs from budget cuts.

A shift in public expenditures to education and health care can increase growth, improve equity, and reduce poverty over the long run through the

beneficial effects of these outlays on the accumulation of human capital (Harberger, 1998). Because the productivity and benefit incidence of these expenditures are highly dependent on their intrasectoral distribution, IMF policy advice increasingly emphasizes shifting the pattern of expenditures to accommodate higher spending on basic education and primary health care. In its work in these areas, IMF staff relies heavily on the expertise of other institutions. These include the World Bank, regional development banks, the United Nations Development Program, the International Labor Office, and other UN agencies.

IMF-Supported Programs and the Poor: The Experiences of Low-Income Countries

In 1987, the IMF established the Enhanced Structural Adjustment Facility (ESAF) to provide resources to low-income countries for longer periods on concessional terms (see Box). Like its precursor, the Structural Adjustment Facility (SAF), the ESAF was created in response to a need to better address the macroeconomic and structural problems of low-income countries. In a review of 36 countries (International Monetary Fund, 1997a; see Table 1) that have implemented structural adjustment policies under SAF/ESAF-supported programs during 1986–95, the IMF found that these countries have made substantial progress in creating the conditions for a stable macroeconomic environment and sustainable growth and in improving the composition of their public expenditures. An even more recent analysis of data for 66 countries (Gupta, Clements, Verhoeven, and Tiongson, 1998; see Table 2), of which 32 had SAF/ESAF programs, shows an increase in social spending since the mid-1980s.[2] What has been the impact of such IMF-supported programs on the poor? The following section reviews the experiences of these countries and changes in key variables that affect the poor—inflation, growth, and the composition of public expenditure.

Inflation

Overall, IMF-supported programs have been most successful in ending episodes of high inflation—when the rate is over 40 percent—which

[2]The findings in the sample of 66 countries largely confirm an earlier analysis of developments in social spending in 23 countries supported by SAF or ESAF programs (see Abed and others, 1998).

Box. SAF/ESAF: A Concessional Facility to Assist Poorer Countries

The IMF's Executive Board established the Enhanced Structural Adjustment Facility (ESAF) in 1987 to better address the macroeconomic and structural problems faced by low-income countries. It offers loans with lower interest rates and for longer terms than the typical IMF market-related arrangements. The principal objectives are to promote balance of payments viability and foster sustainable long-term growth. Although the objectives and features of the ESAF are similar to those of its predecessor, the Structural Adjustment Facility (SAF), set up in 1986, the ESAF was expected to be more ambitious with regard to macroeconomic policy and structural reform measures. The IMF no longer makes disbursements under the SAF.

ESAF loans are disbursed semiannually (as against quarterly for regular IMF stand-by arrangements), initially upon approval of an annual arrangement and subsequently on the observance of performance criteria and after completion of a mid-term review. ESAF loans are repaid in 10 equal semiannual installments, beginning 5!/2 years and ending 10 years after the date of each disbursement. The interest on ESAF loans is 0.5 percent a year. By contrast, charges for stand-by arrangements are linked to the IMF's SDR market-determined interest rate, and repayments are made within 3!/4 to 5 years of each drawing. A three-year access under the ESAF is up to 190 percent of a member's quota. The access limits of stand-by arrangements are 100 percent of quota annually and 300 percent cumulatively.

An eligible member seeking to use ESAF resources develops, with the assistance of the IMF and the World Bank, a policy framework paper (PFP) for a three-year adjustment program. The PFP, updated annually, sets out the authorities' macroeconomic and structural policy objectives and the measures that they intend to adopt during the three years. The PFP also lays out the associated external financing needs of the program, a process that is meant to catalyze and help coordinate financial and technical assistance from donors

strongly correlates with slow growth. However, countries have been less successful in achieving low (single-digit) inflation (International Monetary Fund, 1997a). The countries with high initial inflation rates experienced a sharp reduction in inflation, and the vast majority of them managed to exit these high-inflation situations. Countries with intermediate inflation (the largest group) showed a mixed record. Many countries saw some disinflation, although in some cases it amounted to a reversal of

TABLE 1. SAMPLE OF 36 SAF/ESAF COUNTRIES

Albania	Guyana	Nepal
Bangladesh	Honduras	Nicaragua
Benin	Kenya	Niger
Bolivia	Kyrgyz Republic	Pakistan
Burkina Faso	Lao People's Dem. Rep.	Senegal
Burundi	Lesotho	Sierra Leone
Cambodia	Madagascar	Sri Lanka
Côte d'Ivoire	Malawi	Tanzania
Equatorial Guinea	Mali	Togo
Gambia, The	Mauritania	Uganda
Ghana	Mongolia	Vietnam
Guinea	Mozambique	Zimbabwe

a run-up of inflation before the program began. By the third year of the program, only about one-fourth of the countries with intermediate initial inflation had managed to reduce it to low rates. In one-third of the countries with low initial inflation rates, inflation rose to the intermediate level of about 16 percent. However, the rest of the group, on average, experienced slightly reduced inflation.

Growth

During the early 1980s, developing countries, on average, experienced virtual stagnation in per capita real GDP. In the 36 program countries reviewed, the picture was even bleaker, as real GDP declined by 1.4 percent a year on average in the first half of the 1980s. In the 10 years thereafter (1986–95), growth picked up in the developing countries as a group, but was faster in the sample of program countries, leading to the elimination by 1995 of the gap between their growth rates and the average of other developing countries. However, this improvement varied among regions. Western Hemisphere countries experienced the sharpest turnaround in growth rates, whereas those of African countries with a SAF or an ESAF in place turned negative in the early 1990s, so that per capita GDP growth rates, on average, remained close to zero.

A comparison of growth in the three years after the start of such programs, relative to their growth in the three years preceding the programs, shows the following picture: all 36 program countries reviewed, on average, were able to increase real per capita GDP growth. The turnaround

TABLE 2. SAMPLE OF 66 COUNTRIES WITH IMF-SUPPORTED PROGRAMS

Albania*	El Salvador	Niger*
Argentina	Ethiopia*	Nigeria
Bangladesh*	Georgia*	Panama
Barbados	Guatemala	Papua New Guinea
Belarus	Guinea-Bissau*	Peru
Benin*	Honduras*	Philippines
Bolivia*	India	Romania
Brazil	Jordan	Russia
Bulgaria	Kazakhstan	Rwanda*
Burkina Faso*	Kenya*	São Tomé and Príncipe*
Burundi*	Korea	Sierra Leone*
Cambodia*	Kyrgyz Republic*	Sri Lanka*
Chile	Lesotho*	Tajikistan
China	Madagascar*	Tanzania*
Comoros*	Mali*	Thailand
Congo, Republic of*	Mexico	Turkey
Costa Rica	Moldova	Ukraine
Côte d'Ivoire*	Mongolia*	Uruguay
Croatia	Morocco	Uzbekistan
Czech Republic	Mozambique*	Venezuela
Dominica*	Nepal*	Zambia*
Egypt	Nicaragua*	Zimbabwe*

*Countries with SAF/ESAF-supported programs.

was most dramatic in African countries outside the CFA franc zone[3] and in countries in the Western Hemisphere.

The results of a standard empirical model (International Monetary Fund, 1997a) used to examine the determinants of economic growth suggest that part of the marked narrowing of the growth gap between developing countries with programs and those without is attributable to stronger macroeconomic policies. These policies were designed to reduce both inflation and budget deficits and were reinforced by structural reforms in key areas. Other factors were more benign exogenous influences, particularly trends in the terms of trade and the weather. However, policies fell short in several areas—most notably by not opening up to international trade and not reducing the size of government.

[3]The 14 countries that make up the CFA franc zone are Benin, Burkina Faso, Cameroon, Central African Republic, Chad, Republic of Congo, Côte d'Ivoire, Equatorial Guinea, Gabon, Guinea-Bissau, Mali, Niger, Senegal, and Togo.

Composition of Expenditures

Social expenditures

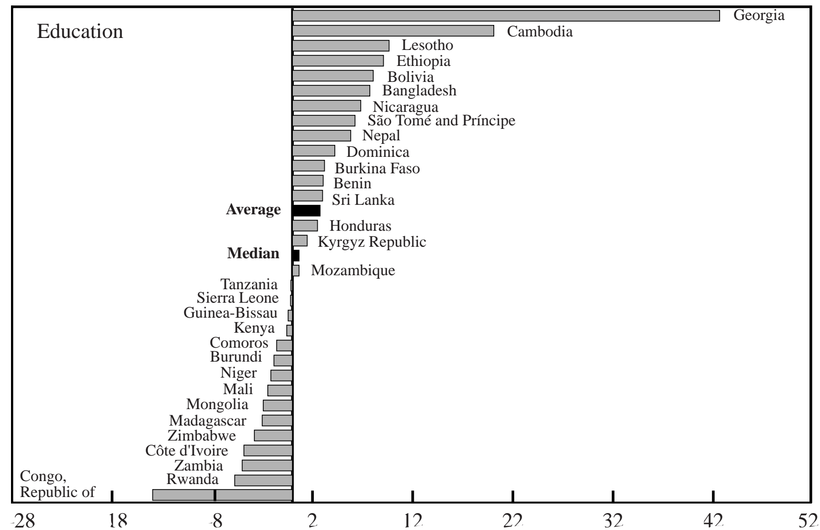
On the basis of evidence for the 66 countries with IMF-supported programs for which data are available during 1986–96, spending on education and health, on average, fared reasonably well. Changes in such spending were larger in the 32 countries supported by a SAF or an ESAF program. While changes in social indicators varied among countries, the indicators did, in general, improve. The data reported here do not include education and health spending by the private sector, which can be sizable.[4]

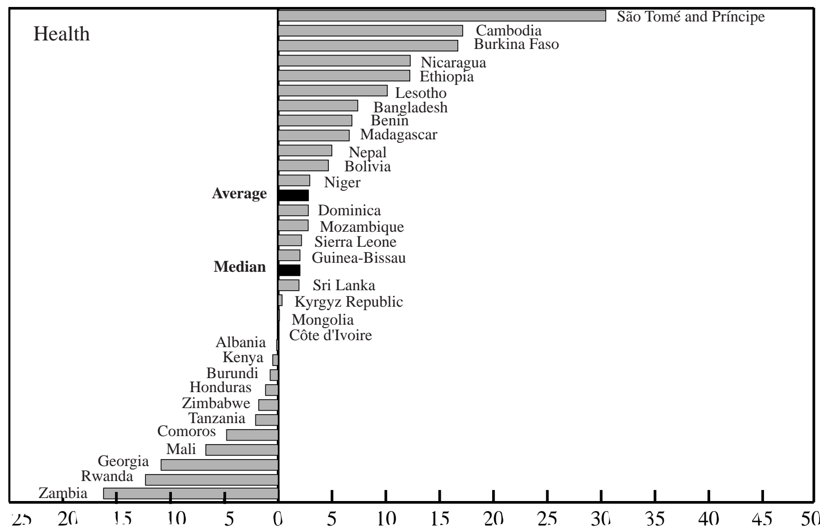
Many countries included in the sample sought real increases in education and health expenditures as well as improvements in expenditure efficiency. A comparison of the last year for which data are available and the preprogram year (defined as the year preceding the first IMF-supported program for each country) shows that real public spending on education increased by 44 percent (43 percent in SAF/ESAF countries). Real per capita spending increased on average by 0.9 percent a year in the 66 countries and 2.8 percent a year in countries with a SAF/ESAF program (Figures 1 and 2). However, this increase in education spending varied substantially across regions. African countries increased spending by less than the others in the sample: education spending rose only 2 percent in real terms a year, compared with 11 percent a year in other SAF/ESAF countries. Because of the small increase in such spending and the high population growth in Africa, per capita education spending actually declined by 0.7 percent a year, on average, compared with a rise of 9 percent a year in the other SAF/ESAF countries.[5] In the 66 countries, real public health expenditures increased by 61 percent (79 percent in SAF/ESAF countries). Health expenditures increased in real terms in all but eight countries with a SAF or an ESAF program, with per capita spending increasing, on average, by 2.8 percent a year (Figures 1 and 2). As with education expenditures, African countries with SAF or ESAF programs in-

[4]In 1990, for example, the private sector accounted on average for 45 percent of health outlays in Africa and for 60 percent of such outlays in Asia (see Psacharapoulos and Nguyen, 1997).

[5]The performance in Africa was influenced by the drop in spending in CFA franc zone countries in the aftermath of the 1994 currency devaluation and by the repatriation of expatriate teachers. In some African countries, such as Burkina Faso, Ghana, and Lesotho, real per capita education expenditures increased significantly.

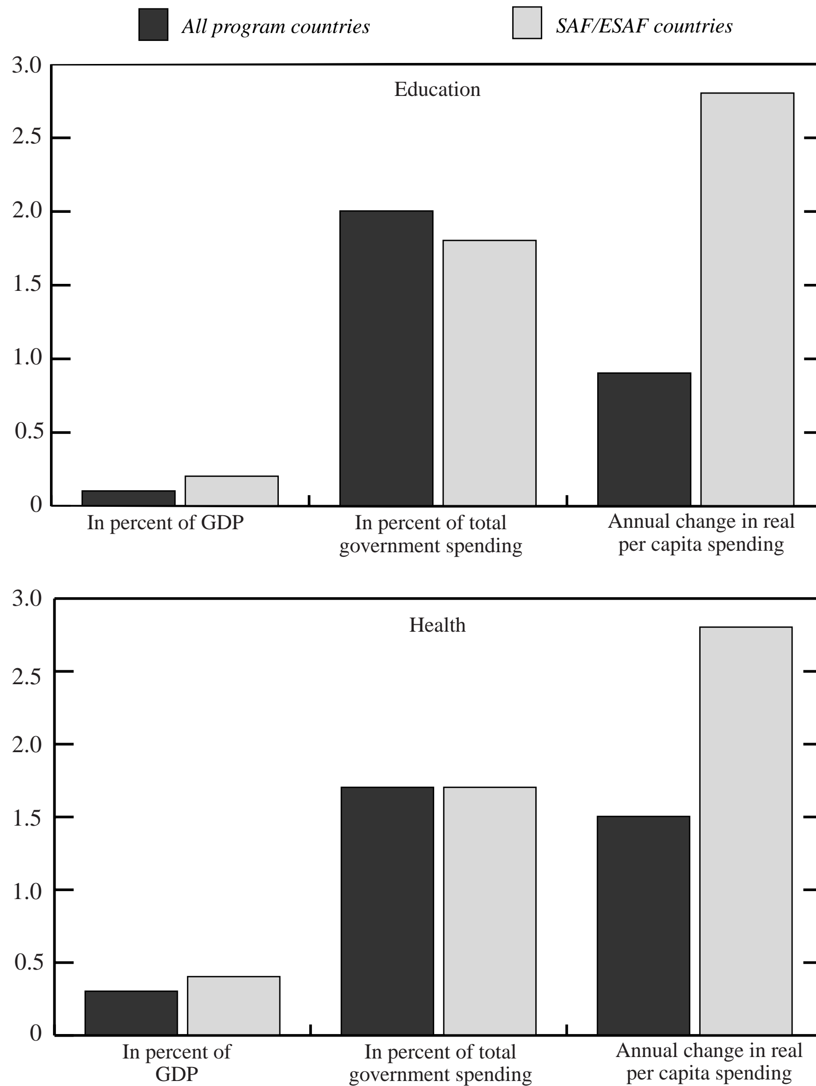
FIGURE 1. AVERAGE ANNUAL CHANGE IN REAL PER CAPITA EDUCATION AND HEALTH SPENDING UNDER SAF/ESAF-SUPPORTED PROGRAMS
(Percent)





Sources: Country authorities; and IMF staff estimates.

FIGURE 2. GOVERNMENT SOCIAL SPENDING UNDER IMF-SUPPORTED PROGRAMS, 1986–96
(Mean changes)



Sources: Country authorities; and IMF staff estimates.
Note: The mean changes are between the preprogram year and the latest year for which data are available.

creased their spending by less, with their real per capita outlays on health increasing by only 2.5 percent a year, compared with 3.3 percent elsewhere in the sample of SAF/ESAF countries. For both education and health, their shares in total expenditures increased, indicating that these sectors became higher priorities under IMF-supported programs.

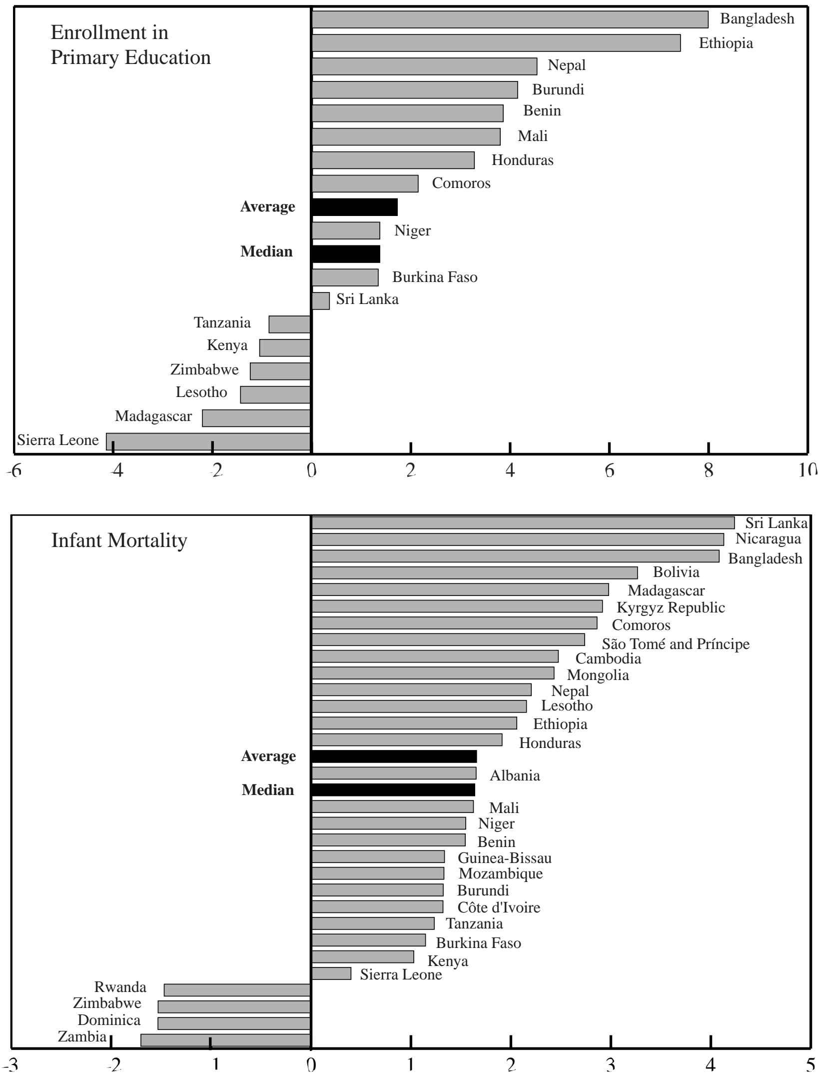
While many factors can potentially affect the link between government expenditures and social indicators, the increased spending on education and health care coincided with improvements in both education and health indicators. The illiteracy rate has declined by 2.4 percent a year since the start of the first IMF-supported program, with comparable improvement in SAF/ESAF countries. Gross primary and secondary enrollment rates rose more sharply in SAF/ESAF countries (about 12 percent on average between the last year for which data are available and the preprogram year) compared with the overall sample of 66 countries (about 6–9 percent on average for the same period). Again, gains in literacy were comparatively lower in the African SAF/ESAF countries, with the increase in gross primary enrollment rates being typically lower than in other countries (Figure 3).

In the health sector, access to health care increased on average to 79 percent of the population from 69 percent, with a sharper rise (60–74 percent) in SAF/ESAF countries. Immunization rates and access to safe water and sanitation also increased, with some SAF/ESAF countries experiencing greater improvements. At the same time, life expectancy increased by 0.3 percent a year (0.2 percent in SAF/ESAF countries), and infant mortality fell by 1.8 percent a year (1.7 percent in SAF/ESAF countries). Improvements in health in the African countries were smaller than in other countries in the sample.

As mentioned above, the poverty-reducing impact of social expenditures depends largely on the intrasectoral allocation of these outlays. In the earlier review of SAF/ESAF countries for 1986–95, Abed and others (1998) showed that the distribution of benefits from social spending disproportionately favored higher-income groups. The ability of upper-income groups to capture a disproportionate share of the benefits of this spending may have reflected an urban bias in the provision of social services.[6] In the education sector, the poorest 20 percent of the population in a group of eight countries received 13 percent of the benefits on average, compared

[6]See Schwartz and Ter-Minassian (1995) for a recent review of the literature on the distributive incidence of public expenditures.

FIGURE 3. AVERAGE ANNUAL CHANGE IN PRIMARY EDUCATION ENROLLMENT AND INFANT MORTALITY RATES UNDER SAF/ESAF-SUPPORTED PROGRAMS



Sources: World Bank, World Development Indicators database; and *UNESCO Statistical Yearbook*, various issues.

Note: An improvement in infant mortality rates is indicated by an increase.

with 32 percent for the richest 20 percent. To improve the benefit incidence, government should spend more on primary education and impose user charges for tertiary education, in combination with a system of financial aid for poorer students. For the five SAF/ESAF countries for which health data are available, the poorest 20 percent received an average of just 12 percent of the benefits of total health care spending, compared with 30 percent for the richest 20 percent (see Abed and others, 1998). Again, countries could improve the benefit incidence by emphasizing primary and preventive health care services and focusing less on curative and hospital care. The findings of Abed and others (1998) are supported by a more recent analysis by Gupta, Clements, and Tiongson (forthcoming). In a sample of 46 countries, the average share of education spending allocated to tertiary education was found to be 21 percent, with Asian countries allocating the lowest share. While it is difficult to determine the appropriate sectoral shares of education expenditures, it is noteworthy that Asian countries with IMF-supported programs have experienced the sharpest improvements in education indicators. This same study found that, in a sample of 33 countries, 60 percent of health spending is absorbed by high-cost curative care, with sub-Saharan African countries allocating the largest share. This finding may partly explain why improvements in overall health indicators among program countries have been more modest in African countries.

The Managing Director of the IMF has recently called on IMF staff to improve the collection of data on health and education expenditure and to monitor developments in basic social indicators in developing and transition economies. The Executive Board has requested that the staff pay particular attention to social spending and social indicators in the most heavily indebted poor countries (see International Monetary Fund, 1997c), which are receiving assistance under an initiative instituted by the IMF and the World Bank.

Military expenditures

Excessive military spending can crowd out private investment or more productive public expenditures, with a potentially adverse effect on growth (Knight, Loayza, and Villanueva, 1996). Recent research also confirms that in countries where large increases in military expenditures have occurred, the budget deficit has increased and public investment has declined (Gupta, Schiff, and Clements, 1996). The IMF therefore often advises countries to review military expenditures to identify potential fiscal savings.

Progress has been encouraging in recent years (Gupta, Clements, and Ruggiero, 1997; Gupta, McDonald, and Ruggiero, 1998). In developing countries with IMF-supported programs, the declines in worldwide military outlays have been even more rapid, although one should be cautious in attributing these declines purely to the programs. In these countries, military expenditures fell, on average, by 2.5 percentage points of GDP between 1990 and 1997, compared with 1.3 percentage points in developing countries without an IMF-supported program. This larger decline in program countries is due mainly to the relatively more rapid reduction in military expenditures in the transition economies (former centrally planned countries making the transition to market economies). The decline in military expenditures has allowed social expenditures to expand. For the 52 countries for which consistent data are available for 1990–96, military spending fell by an average of 3.1 percentage points of total expenditures, while social expenditures increased, on average, by 1.2 percentage points.

Other aspects of expenditure composition

The review of the 36 countries' performance during 1986–95 showed that SAF/ESAF-supported programs aimed, on average, to roughly maintain the level of total expenditures as a share of GDP (see Table 3 and Figure 4) while shifting expenditures from current to capital. Relative to the three-year preprogram average, an increase in capital expenditures and net lending of about 1.4 percentage points of GDP was targeted. This increase in capital expenditures was to be facilitated by an average reduction in current spending of 2.2 percentage points, with budgetary savings anticipated to come from reductions in excessive public sector employment and in inefficient subsidies and transfers. In practice, these countries did make significant progress in changing the composition of expenditures in favor of capital outlays, although by less than programmed. Compared with the three-year preprogram average and the last year for which data are available, the share of outlays devoted to capital and net lending rose by about 2.6 percentage points, whereas the portion of expenditures absorbed by wages and salaries as well as by subsidies and transfers declined (Table 3 and Figure 4).

Social safety nets

Although data problems make it difficult to distinguish subsidies designed to help the poor from those designed for other policy purposes, sev-

TABLE 3. SUMMARY OF EXPENDITURES BY ECONOMIC CLASSIFICATION IN SAF/ESAF COUNTRIES

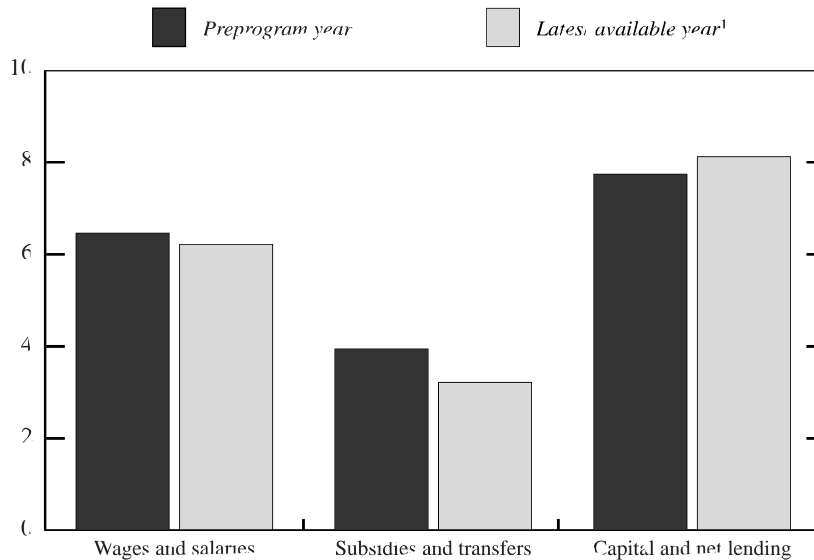
	Three-Year Preprogram Average	Preprogram Year	Average Program Target	Last Year (1994 or 1995)	Last Year Minus Three-Year Preprogram Average	Last Year Minus Preprogram Year	Sample Size[1]
	(Percent of GDP)[2]						
Total expenditures and net lending	29.0	27.6	28.2	26.2	–2.8	–1.4	36
Current expenditures	20.9	19.7	18.7	17.9	–3.0	–1.8	36
Goods and services	13.6	12.6	11.9	11.1	–2.5	–1.5	28
Wages and salaries	7.1	6.5	6.1	6.2	–0.9	–0.3	33
Other	6.3	5.8	6.0	4.9	–1.4	–0.9	28
Interest	4.0	3.9	4.0	3.6	–0.4	–0.3	35
Subsidies and transfers	4.4	3.9	3.2	3.2	–1.2	–0.7	29
Other	3.9	3.9	5.1	3.6	0.3	–0.3	21
Capital expenditures and net lending	7.9	7.7	9.3	8.1	0.2	0.4	36
	(Percent of total expenditures and net lending)						
Total expenditures and net lending							
Current expenditures	70.5	69.6	65.4	67.8	–2.7	–1.8	36
Goods and services	44.4	43.4	40.5	40.9	–3.5	–2.5	28
Wages and salaries	24.9	23.7	22.4	23.5	–1.4	–0.2	33
Other	19.7	19.9	19.5	18.0	–1.7	–1.9	29
Interest	12.3	12.5	13.5	13.5	1.2	1.0	35
Subsidies and transfers	12.4	12.6	9.6	11.4	–1.0	–1.2	31
Other	16.1	15.9	17.9	15.3	–0.8	–0.6	20
Capital expenditures and net lending	28.9	29.7	34.0	31.5	2.6	1.8	36

Sources: Country authorities; and IMF staff estimates.

[1]Number of countries for which data are available for a given expenditure category. If the sample size varies for different columns, then the maximum figure is given.

[2]The sum of the expenditure components may differ from the totals because of differences in sample size.

FIGURE 4. GOVERNMENT SPENDING UNDER SAF/ESAF-SUPPORTED PROGRAMS
(Percent of GDP)



Source: Table 3.
[1]Either 1994, 1995, or 1996.

eral countries improved the efficiency of outlays on subsidies and transfers by reducing generalized subsidies and increasing spending on targeted social safety nets during 1986–95. Partly as a result of such reductions (particularly in transition economies), spending on subsidies and transfers by the group of 36 SAF/ESAF countries declined by about 1 percent of total expenditures between the last year for which data were available and the three-year preprogram average. Some countries temporarily froze prices on key staples after major exchange rate devaluations, whereas others instituted programs to transfer income to the poor during the reform period.

When civil service reform involved cutting staff, most countries included severance packages for the newly unemployed and made it

easier for small enterprises to obtain credit, often with the support of donor financing. Public works or “food-for-work” programs were also implemented to provide income support to the unemployed, those adversely affected by reduced employment opportunities, and soldiers rendered unemployed by military demobilization programs. In some other countries, a part of the privatization proceeds was used to compensate workers who were made redundant in privatized enterprises.

Countries that have attempted to reform existing social assistance programs and implement new social safety nets have faced several difficulties, and the results have often been uneven. First, weak administrative structures and the lack of appropriate social policy instruments have constrained the implementation of cost-effective social safety nets, especially when the poor are located in geographically isolated areas. Furthermore, because of a lack of data, it has sometimes been difficult to assess a social safety net’s effectiveness in reaching its intended beneficiaries. In some countries, political support for establishing and reforming social safety nets has at times been insufficient, so that social safety nets continue to have unintended beneficiaries. Finally, the weakening of the revenue base has dried up sources of financing for social benefits in some transition countries (Chu and Gupta, 1996).

Changes in Poverty and Income Inequality Under IMF-Supported Programs

Have countries with IMF-supported programs reduced poverty and income inequality? This question is important not only in itself, but also because recent research suggests that inequality can hinder growth.

In 1986, the IMF’s Fiscal Affairs Department studied how adjustment programs affected the distribution of income in 94 countries (International Monetary Fund, 1986). The study concluded that, although there was no evidence that IMF-supported programs worsened income inequality, different policy measures had different effects on different income groups. Measures that made the distribution of income more equal included devaluation of the exchange rate in countries where small farmers depended on agricultural exports, elimination of exchange controls, expansion of access to credit markets, expansion of the tax base for property and income taxes, and reallocation of expenditures toward basic ed-

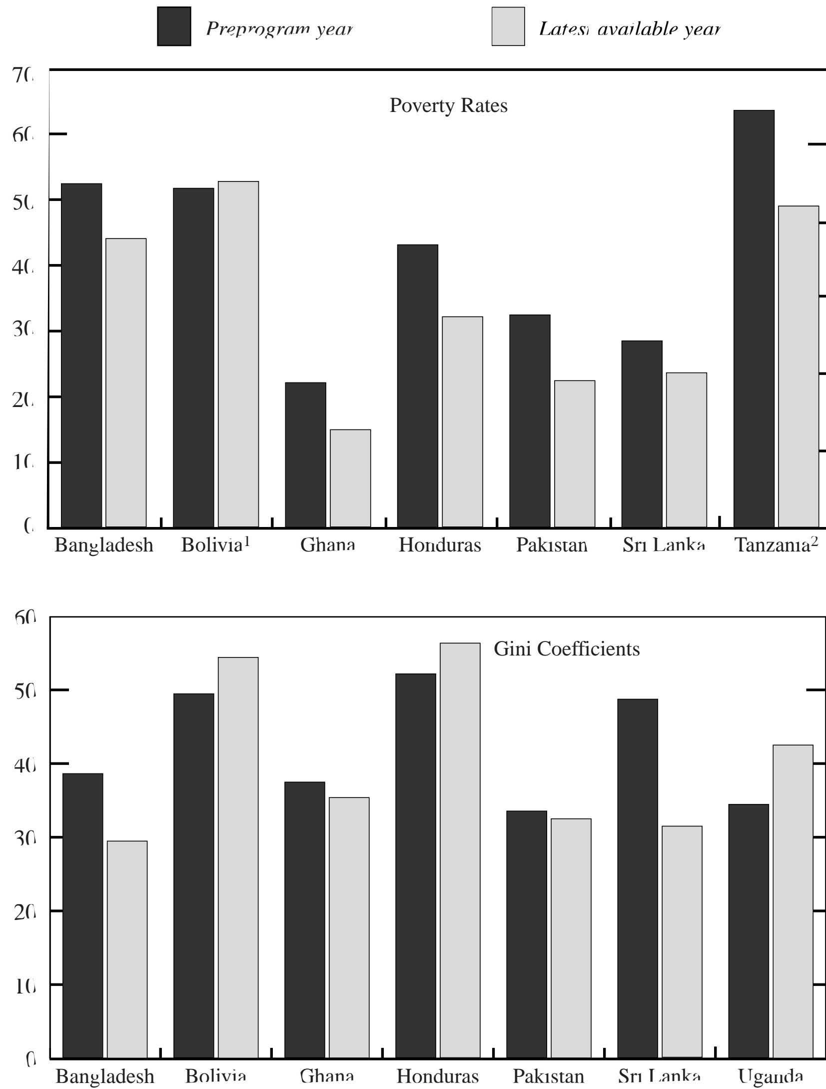
ucation and health care. Measures with adverse distributional effects included increases in indirect taxes (for example, customs duties and the value-added tax). A follow-up study (Heller and others, 1988) that focused on seven countries concluded that the distributive effect of IMF-supported programs depended on the policy mix used to achieve fiscal adjustment.

In seven SAF/ESAF countries for which data are available, poverty rates declined by an average of 20 percent under IMF-supported adjustment programs, implying an average annual reduction of 5.3 percent (Figure 5). The reduction for the two SAF/ESAF countries in Africa (Ghana and Tanzania) was somewhat stronger, at 6.3 percent each year. Poverty rates declined significantly in Asia (Bangladesh, Pakistan, and Sri Lanka); in Latin America, urban poverty increased in Bolivia—mainly because of the migration of rural poor to urban areas—while poverty declined at the national level in Honduras.

For income inequality, the data indicate that, on average, the distribution of income improved in countries with SAF/ESAF-supported programs (Figure 5). The decline in the average Gini coefficient—a measure of the inequality of income distribution—was nearly 1 percent each year, from 0.41 to 0.39. For the two SAF/ESAF countries in Africa for which data are available (Ghana and Uganda), income inequality increased in Uganda and fell in Ghana. For the three Asian countries, poverty reduction was, on average, accompanied by a more equal distribution of income, with especially sharp declines in the Gini coefficient in Bangladesh and Sri Lanka. In contrast, for the two Latin American countries—Bolivia and Honduras—income inequality increased. Similar trends can be observed for the evolution of the income share of the richest 20 percent of the population relative to that of the poorest 20 percent. However, given the small sample, it is difficult to generalize these results for other SAF/ESAF countries with IMF-supported adjustment programs during that period.

The IMF's deepening interest in income distribution issues reflects the belief that, as a matter of social justice, all members of society should share in the benefits of economic growth. Adjustment programs that are equitable and growth that is equitable are more likely to be sustainable (Camdessus, 1998; Fischer, 1998; International Monetary Fund, 1998). As a result of these considerations, the IMF hosted a major conference on income distribution and sustainable development in 1995 and a conference

Figure 5. Poverty Rates and Gini Coefficients Under SAF/ESAF Supported Programs



Sources: Deininger and Squire (1996); Jayarajah, Branson, and Binayak (1996); and World Bank (1996a and 1996b).

[1]Figures for urban areas only.

[2]Figures for rural areas.

on economic policy and equity in June 1998. The 1998 conference focused on operational aspects in addressing equity.[7]

Addressing Poverty Concerns in Other Core IMF Activities

The increased focus on high-quality growth has been incorporated not only in program design but also in the other core activities of surveillance and technical assistance. With respect to surveillance, the IMF's policy advice has focused on a wide range of current economic policies, including structural policies and the reforms needed to improve the quality of growth and economic performance. For example, policy advice to some European countries has stressed the importance of labor market reforms to reduce unemployment. To address the social effects of these labor market reforms, policy advice has focused on appropriate adjustments in tax and expenditure policies.

In many industrial countries, demographic trends indicate that the rapid aging of the population may raise expenditures on health and social security to unsustainable levels (Chand and Jaeger, 1996; and Heller, 1997). In these countries, IMF advice on reforms has focused on the long-term viability of health and social security spending.

The IMF's technical assistance has included advice on efficient and equitable tax and expenditure policies, which is a necessary adjunct to program design if the objectives for growth and poverty reduction are to be achieved. Some of the areas in which such assistance has been provided are public expenditure management, tax policy, tax administration, public expenditure policy, and social safety nets. Since 1991, the IMF has fielded about thirty technical assistance missions to help member countries design cost-effective and financially sustainable social safety nets.

[7]The IMF's interest in this area is also reflected in studies that have recently been undertaken (see, for example, Clements, 1997; and Tanzi and Chu, 1998). Clements's recent study on Brazil found ample evidence in the literature that income inequality is largely explained by the extreme disparity in educational attainment levels. Since the Real Plan of July 1994, inequality in Brazil has been lessened, although the distribution of income in that country remains one of the most unequal in the world.

Summary and Conclusions

The focus of the IMF's policy advice is to help member countries achieve a sustainable macroeconomic framework that creates the conditions for growth and the reduction of poverty. The aim is to devise macroeconomic polices that foster sustainable growth while reforming expenditures and tax policies to reinforce this process, thus ultimately improving income distribution and reducing poverty. Through this process, the IMF's approach to fiscal policy, particularly its social aspects, has evolved so that it is no longer viewed solely as a macroeconomic tool. The IMF is paying more attention to the distributional implications of fiscal policy and its role in fostering long-term growth, particularly during adjustment. Nevertheless, further research is needed on the linkages between social expenditures and social output indicators, with a view to providing guidance for better targeting of social expenditures.

Through the programs it supports, the IMF is continuing its efforts to better protect the poor. Guidelines have recently been issued to IMF staff for improving the monitoring of social expenditures and social output indicators as a further step in this process. IMF-supported programs can be made more effective, in general, if the analysis of the distributive effects of policy measures and economic developments is improved. They can also be strengthened through a more systematic evaluation of the effectiveness of social safety nets and of the composition of expenditures. With the increased emphasis on second-generation reforms to foster high-quality growth—such as the reform of the labor market—there is likely to be an even greater impact on the poor than in the past, which underscores the need for more work in this area. The IMF Board has recently received an assessment by external evaluators of the social aspects of adjustment programs in low-income countries. This will further guide the IMF's policy advice and cooperation with the World Bank on poverty reduction.

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