

Evaluation Report

# Evaluation of the IMF's Role in Poverty Reduction Strategy Papers and the Poverty Reduction and Growth Facility



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Evaluation Report

# Evaluation of the IMF's Role in Poverty Reduction Strategy Papers and the Poverty Reduction and Growth Facility



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The following symbols have been used throughout this report:

– between years or months (e.g. 2003–04 or January–June) to indicate the years or months covered, including the beginning and ending years or months;

/ between years (e.g. 2003/04) to indicate a fiscal (financial) year.

“Billion” means a thousand million.

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

Some of the documents cited and referenced in this report were not available to the public at the time of publication of this report. Under the current policy on public access to the IMF’s archives, some of these documents will become available five years after their issuance. They may be referenced as EBS/YY/NN and SM/YY/NN, where EBS and SM indicate the series and YY indicates the year of issue. Certain other documents are to become available ten or twenty years after their issuance depending on the series.

# Foreword

The role of the IMF in supporting economic reform in low-income member countries has been the subject of considerable scrutiny and criticism over the years. At the end of 1999, the IMF and World Bank adopted a new framework for their support to low-income countries. This framework comprised two key elements: first, country-authored Poverty Reduction Strategy Papers (PRSPs), expected to draw on broad-based consultations with key stakeholder groups; and, second, a vehicle for the provision of IMF concessional lending, the Poverty Reduction and Growth Facility (PRGF), which replaced the Enhanced Structural Adjustment Facility (ESAF). Programs supported by the PRGF were to be derived from a country's PRSP to ensure that reforms supported by the IMF were country owned and clearly oriented to achieving the joint objectives of poverty reduction and economic growth.

Although it is still too early to assess the success of the new framework in achieving these objectives, it is time to take stock of progress to date and identify shortcomings that may require course corrections in the design and implementation of the initiative. This is the purpose of this new IEO evaluation, which seeks to strike a balance between measuring progress against initial expectations and against final objectives. In this endeavor, we met two difficulties. First, it appeared that initial expectations about what could be delivered in the short term—by the IMF and by low-income countries alike—were extremely ambitious. Second, yardsticks and benchmarks to assess intermediate progress toward the final objectives appeared to be insufficient, especially with regard to what was expected in terms of country-specific changes in policy processes.

This evaluation adds to an already extensive body of reviews of the PRSP initiative undertaken internally by IMF and World Bank staff, as well as by donor agencies and nongovernmental organizations, by drawing on the comparative advantage of the IEO, which combines an independent perspective with full access to internal IMF documents, staff, and key decision makers. The evaluation, undertaken in parallel with a similar exercise by the Operations Evaluation Department (OED) of the World Bank ([www.worldbank.org/oed/prsp](http://www.worldbank.org/oed/prsp)) is based on extensive cross-section analysis of data for countries that had completed full PRSPs as of the end of 2002 and is further informed by a series of in-depth country case studies and surveys of stakeholders in low-income countries.

Following standard practice, this volume includes, alongside the evaluation report itself, the response of IMF management and staff to the evaluation, as well as the Summing Up of the Executive Board discussion of this report. Executive summaries of the case studies undertaken as background to this evaluation will be published in a separate volume and the full case study reports can be found on our website at [www.imf.org/ieo](http://www.imf.org/ieo).

David Goldsbrough  
*Acting Director*  
*Independent Evaluation Office*



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## **Evaluation of the IMF's Role in Poverty Reduction Strategy Papers and the Poverty Reduction and Growth Facility**

This report was prepared by a team headed by David Goldsbrough and includes Jeffrey Allen Chelsky, Martin Kaufman, Steve Kayizzi-Mugerwa, Isabelle Mateos y Lago, Alex Segura-Ubiergo, Daouda Sembene, and Tsidi Tsikata. Research assistance was provided by Patricia Yang-Yang Chen and Mowafa Taib, and administrative support by Annette Canizares, Arun Bhatnagar, and Maria S. Gutierrez. Important contributions were also received from Professor Arne Bigsten, Soren Jensen, David Peretz, and Kerfalla Yansane. The report was approved by Montek S. Ahluwalia, then Director of the Independent Evaluation Office (IEO). The evaluation team also benefited considerably from its collaboration with the World Bank's Operations Evaluation Department team, led by William Battaile, which conducted a parallel evaluation of the World Bank's role in the Poverty Reduction Strategy Paper process. Final judgments expressed in this report are the responsibility of the IEO alone.

The assistance of the Economic Commission for Africa in hosting a workshop for stakeholders in January 2004 in Addis Ababa to discuss the preliminary results emerging from the evaluation, and the financial support of the Commonwealth Secretariat, which allowed a number of the participants to attend that workshop, are gratefully acknowledged.

# Abbreviations and Acronyms

AFR	African Department (IMF)
APR	Annual performance report
AsDB	Asian Development Bank
BWI	Bretton Woods institution
CAS	Country Assistance Strategy (World Bank)
CDF	Comprehensive Development Framework (World Bank)
CG	Consultative Group
CGE	Computable General Equilibrium
CPIA	Country Policy and Institutional Assessment (World Bank)
CSO	Civil society organization
DAC	Development Assistance Committee (OECD)
DFID	Department for International Development (U.K.)
EC	European Commission
ESAF	Enhanced Structural Adjustment Facility (IMF)
FAD	Fiscal Affairs Department (IMF)
FAO	Food and Agriculture Organization (UN)
GDP	Gross domestic product
HIPC	Heavily Indebted Poor Country
IDA	International Development Association
IEO	Independent Evaluation Office (IMF)
IFI	International financial institution
IMF	International Monetary Fund
IMG	Independent Monitoring Group
I-NGO	International nongovernmental organization
I-PRSP	Interim Poverty Reduction Strategy Paper
JPR	Joint Partner Review
JSA	Joint Staff Assessment
LIC	Low-income country
LOI	Letter of Intent (IMF)
MCD	Middle East and Central Asia Department (IMF)
MDGs	Millennium Development Goals
MEFP	Memorandum of Economic and Financial Policy (IMF)
MFD	Monetary and Financial Systems Department (IMF)
MONA	Monitoring of Arrangements (IMF)
MTEF	Medium-term expenditure framework
NEPAD	New Partnership for Africa's Development
NGO	Nongovernmental organization
ODA	Official development assistance
OED	Operations Evaluation Department (World Bank)
PAF	Performance Assessment Framework
PDR	Policy Development and Review Department (IMF)
PEM	Public expenditure management
PER	Public Expenditure Review (World Bank)
PFP	Policy Framework Paper
PRE	Poverty-reducing expenditure

## ABBREVIATIONS AND ACRONYMS

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PRGF	Poverty Reduction and Growth Facility (IMF)
PRS	Poverty Reduction Strategy
PRSC	Poverty Reduction Support Credit (IDA)
PRSP	Poverty Reduction Strategy Paper
PRSP-PR	PRSP Progress Report
PSIA	Poverty and Social Impact Analysis
RES	Research Department (IMF)
ROSC	Report on Standards and Codes
SOE	State-owned enterprise
TA	Technical assistance
TOR	Terms of reference
UN	United Nations
UNDP	United Nations Development Program
VAT	Value-added tax
WEO	World Economic Outlook (IMF)
WHD	Western Hemisphere Department (IMF)

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**Evaluation of the IMF's Role in  
Poverty Reduction Strategy Papers and the  
Poverty Reduction and Growth Facility**

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# Summary of Major Findings, Lessons, and Recommendations

**T**he Poverty Reduction Strategy (PRS) approach consists of a series of process innovations designed to encourage broader-based participation in the development of a country-owned, long-term strategy for growth and poverty reduction that could also be a framework for coordinating donor support. It was accompanied by a transformation of the IMF's concessional lending facility into the Poverty Reduction and Growth Facility (PRGF). It is too early to evaluate the success of the new approach in achieving its longer-term objectives, especially the extent of reduction of poverty; progress in this dimension will become evident only over a longer period of time. The evaluation has, therefore, focused on intermediate stage outcomes, that is, the quality of the broader-based policy formulation process, the nature of the strategy and policy framework that has evolved, the interaction between this framework and the PRGF, and the effectiveness of the IMF's role. We summarize here our major findings as well as the lessons to be drawn from them and make a number of recommendations for the future. The final section reflects on some implications of the evaluation for the longer-term role of the IMF in low-income countries.

## Summary of Major Findings

*The broad picture that emerges from our study is that the PRS approach has the potential to encourage the development of a country-owned and credible long-term strategy for growth and poverty reduction, which could provide an effective framework for coordinating the efforts of donors and international financial institutions (IFIs), including the IMF. However, actual achievements thus far fall considerably short of potential. This is partly because it is unrealistic to expect quick gains given the initial conditions from which the process started in most low-income countries. But there were also shortcomings in the design of the initiative that have reduced its effectiveness, including a lack of clarity about the role that the IMF should play.*

*Participation in the formulation of Poverty Reduction Strategy Papers (PRSPs) was generally*

*more broadly based than in previous approaches, and most stakeholders involved in the process viewed this as a significant improvement. However, the participatory processes were typically not designed to strengthen existing domestic institutional processes for policy formulation and accountability (e.g., through parliament). In a few cases, institutional arrangements to sustain the process are beginning to develop around the budgetary cycle.*

*The PRS process has had limited impact in generating meaningful discussions, outside the narrow official circle, of alternative policy options with respect to the macroeconomic framework and macro-relevant structural reforms. This reflects in part the absence of any mechanism to ensure that key issues were aired and the broader debate well-informed. Lack of clarity about the role of the IMF in this area contributed to this outcome. In the relatively few cases where a broader debate did occur, there was a positive impact on policy outcomes.*

*Results in terms of ownership are mixed. The approach has often generated relatively strong ownership in a narrow circle of official stakeholders responsible for driving the process, but much less among other domestic stakeholders. The perception that the approach is overly influenced by procedural requirements of the Bretton Woods institutions (BWIs) is widespread.*

*In terms of diagnostics, the approach has generally contributed to a significant improvement in understanding the multidimensional nature of poverty, which has implications for designing poverty reduction strategies. However, the approach has been much less effective in identifying constraints to accelerating growth and making it more pro-poor. The approach has so far not contributed significantly to understanding the linkages between growth, poverty incidence, and macroeconomic policies at the individual country level. These issues present analytical challenges that are not necessarily resolved through participation alone.*

*Strategies outlined in PRSPs generally constitute an improvement over previous development strategies, in the sense of providing greater poverty focus, a longer-term perspective, and some results orienta-*

tion. However, most PRSPs fall short of providing a strategic road map for policymaking, especially in the area of macroeconomic and related structural policies. The focus of most PRSPs is on the composition of public expenditures, especially social sector spending, with much less emphasis on other aspects of a broader strategy to encourage poverty-reducing growth. Even in the area of public expenditure, the operational value of PRSPs is often limited, because of the still rudimentary nature of most costing and prioritization. In many cases, PRSPs also avoid addressing key strategic choices involving “controversial” structural reforms. These weaknesses imply that in most cases PRSPs do not yet provide a policy framework in which PRGF-supported programs can be anchored.

*Except in a few countries where the process is beginning to be embedded in domestic institutions, there is limited feedback from initial implementation to policy design.* This is particularly problematic in the area of macroeconomic policy where the original PRSP was often overtaken by events or proved unrealistic, and there was little in the PRSP to guide choices on key strategic trade-offs involved in recalibrating macroeconomic targets.

*Capacity constraints have been a severe impediment to progress* in the implementation of the PRS approach. There has been insufficient attention to developing a systematic plan of action to strengthen capacity, including in the IMF’s areas of primary competence. Budgetary processes are weak, and the linkages between the PRSP, medium-term expenditure frameworks, and budgets are generally poor. In particular, public expenditure management (PEM) systems are generally too weak to allow the PRSP to play a central role in implementing expenditure priorities or modifying them on the basis of feedback on actual costs and outcomes. Strengthening PEM has been recognized as central to the success of the initiative and is one area where systematic monitoring by the BWIs on the basis of commonly agreed benchmarks is being undertaken (at least for the Heavily Indebted Poor Countries (HIPC)). The results suggest moderate progress. In other areas, however, capacity limitations, which constrain policy design and implementation, have largely not been addressed systematically, including through BWI contributions.

*On balance, joint staff assessments (JSAs) do not perform adequately the many tasks expected of them.* The clarity, candor, and comprehensiveness of the assessment are uneven, with scope for improvement even in “good practice” cases. This partly reflects a built-in bias to reach a “yes or no” signal—which is always “yes” in practice, encapsulated in standardized language. Other factors limiting the usefulness of JSAs include the lack of explicit benchmarks in

most areas on which to base the assessment. Their main contribution has been in giving feedback to the authorities on weaknesses in the PRSP, but JSAs are virtually unknown outside the narrow official circle and consequently have no impact on the broader policy debate. They do not incorporate systematic inputs from development partners and, in practice, have played a limited role in informing lending decisions, including those of the BWIs.

*The effectiveness of the IMF’s contribution has varied considerably across different components of the initiative and across countries—with marked differences between “good” and “average” practice. Its overall contribution has fallen well short of the (admittedly very ambitious) goals it set for itself in the original policy documents:*

- IMF staff typically did not participate actively to inform the policy debate among domestic stakeholders during the PRS formulation process and to ensure that key macro-relevant issues were aired. This is because IMF staff generally interpreted the emphasis on country ownership as implying that involvement on its part should be limited.
- IMF contributions to developing a better understanding of country-specific micro-macro linkages have also been fairly limited. The process has led to much greater awareness within the IMF of the need for ex ante poverty and social impact analysis (PSIA), and this is evident in internal IMF processes, but it has not yet translated into a mainstreaming of such analysis in program design.
- On the positive side, there are signs that the “policy space” in the macroeconomic area has widened—in the sense of greater openness on the part of the IMF to considering alternative country-driven policies—at least in countries where macroeconomic stabilization is no longer a pressing issue.

*Success in embedding the PRGF in the overall strategy for growth and poverty reduction has been limited in most cases—partly reflecting shortcomings in the strategies themselves.* Nevertheless, program design under the PRGF has incorporated greater fiscal flexibility to accommodate aid flows, and there is no evidence of generalized “aid pessimism” or a systematic “disinflation” bias. Expenditures designated as poverty reducing have increased markedly since 1999, although there are questions about how “pro-poor” some of this spending is. IMF structural conditionality has been streamlined, but we have not been able to reach a definitive conclusion on what has happened to aggregate IMF–World Bank conditionality, which is not monitored by the two institutions. There

were only minor improvements in program implementation under the PRGF.

*In terms of outcomes, only tentative messages emerge at this stage.*

- BWI measures of the quality of policies and institutions suggest that PRS countries generally started out in a better position than non-PRS low-income countries, but did not improve at a faster pace.
- Short-term growth for PRS/PRGF countries is only marginally higher than in the earlier period. However, these countries seem to have weathered the worsening of the external environment in 2000–02 better than other low-income countries, which experienced a decline in growth.
- Evidence on poverty-related outcomes, drawn from the parallel evaluation by the World Bank’s Operations Evaluation Department (OED), is still too limited to draw definitive conclusions. The most notable improvements concern various input- and output-related measures (e.g., number of teachers, school enrollment, vaccination rates), but outcomes such as maternal and infant mortality rates have generally not improved.

To summarize, in cases where the PRS approach has been integrated into domestic institutional structures, there have been important improvements in domestic policy processes. In most cases, however, while the PRS approach has generally helped make progress in the right direction, achievements are more tentative. Where the PRS approach has been implemented as an externally imposed, ad hoc exercise, it has acted more as a distraction from strengthening the domestic policy framework.

## Lessons

These broad findings suggest two sets of lessons that illustrate where the approach, and the IMF’s role therein, need strengthening. The first set of lessons relates to the structure of incentives that has been generated by the PRS approach, which are not well aligned with the intermediate objectives of the approach. The second set of lessons relates to the IMF’s role.

### Aligning the structure of incentives with intermediate objectives

A focus on improving fundamental domestic policy processes in countries is more likely to yield longer-term gains, in terms of an improved policy environment for effective use of development aid,

than would a traditional focus on particular policy measures. Whether this refocusing is achieved in practice depends in large part on the underlying incentives faced by countries under the initiative. Unfortunately, actual incentives under the PRS approach do not focus sufficiently on improvements in domestic policy processes and institutions. There are four specific aspects to this problem.

### Too much focus on documents and on BWI-driven procedures

The delicacy of attempting, from outside, to encourage political systems to move in the direction of greater openness, accountability, and participatory policymaking has led to too much emphasis on procedural components. In practice, therefore, what countries perceive as necessary to receive concessional financing and debt relief is to produce specific documents following various procedures, including for participation. At its best, the approach can still lead to important gains in domestic policy processes, and it has done so in some cases. At its worst, however, it risks being a distraction from the task of making improvements in existing domestic procedures for policy formulation and implementation.

### Insufficient scope for treating different countries differently

The philosophy underlying the original initiative was to allow for considerable country variation in approach. As implemented, however, there has been insufficient scope for treating countries differently. The value added of each of the principles underlying the PRS approach varies across countries depending upon circumstances. Some countries had no experience of strategic planning in the area of development and stood to benefit enormously from the exercise of putting together an integrated poverty reduction and growth strategy that is results oriented and provides a long-term perspective. Others had a strong planning tradition but limited experience with broad-based participatory policy formulation; in these cases introducing a participatory element was potentially beneficial. Some countries had both elements, but donors (including the BWIs) were not always willing to treat the country’s own strategy and domestic processes as a basis for their partnership with the authorities. These differences in starting conditions illustrate the need for the PRS approach to be implemented in a manner that capitalizes on existing strengths and focuses efforts on “the missing ingredients” rather than starting anew in all areas. Otherwise, not only can ongoing efforts to improve existing domestic processes be disrupted, but weak domestic capacities may be used inefficiently.



***Insufficient benchmarks to monitor progress toward the intermediate objectives of improved domestic policy processes, and consequent lack of clarity about the criteria for assessments and financing decisions***

The PRS approach was largely defined in terms of broad principles related to processes and inputs. More specific milestones to monitor progress vis-à-vis intermediate objectives, including for strengthening domestic processes according to the broad PRS principles, were expected to be developed at the country level. This has not happened and benchmarks for measuring substantive improvements in policy processes are lacking, both at the country level and initiative-wide. Moreover, these improvements are largely not assessed in JSAs, which generally focus on the more procedural aspects of the participatory process as well as on the specific policy content of the PRSP. Ambiguities about intermediate objectives have also contributed to diverging expectations of different stakeholders and insufficient accountability.

More fundamentally, the PRS approach as designed and implemented does not sufficiently address how trade-offs between domestic ownership and BWI assessments of policies will be handled. Decisions on such trade-offs are still taken, but in a manner that (i) is not transparent, with countries left to divine what is “acceptable” by looking at various guidelines and through exchanges with BWI staff; (ii) focuses too much on procedural compliance; and (iii) often leaves country authorities and other domestic stakeholders feeling that the BWIs control the process partly through unwritten rules of the game.

***Asymmetry of commitments, with too little on what the BWIs are expected to deliver***

PRSs that substantially meet the goals set out in the original policy papers require considerable technical and analytical capacities, not to mention financial support. However, in the current setting, nothing ensures that the capacity-strengthening priorities of countries will be addressed, and the links with lending decisions can be ambiguous. While both the IMF and the World Bank are broadly committed to “aligning” their assistance programs to the PRSP, it is not clear in practice how much countries have to gain by treating the PRSP as an effective strategic road map, rather than as a procedural formality.

***The role of the IMF***

The bold expectations set out in the initial policy documents require greater changes in the IMF’s way of doing business than have occurred so far and are probably overpromising what the IMF can deliver

with existing resources. There are several reasons why the IMF’s effectiveness under the new approach has not matched the original expectations.

***Lack of clarity about what the IMF should be delivering in some areas***

The original policy papers may have overpromised what the IMF could reasonably be expected to deliver, given prevailing resource constraints and its comparative advantage. One example concerns the determination of a medium-term external resources envelope that strikes the right balance between needs, sustainability, and realism as well as the associated efforts to mobilize the requisite donor support. Clearly, these are vital components of the overall strategy, but it is not clear that the IMF is well suited to deliver them.

There is also ambiguity about what donors require in terms of a “signaling role” from the IMF, especially when macroeconomic stabilization has been achieved. This is at the heart of the issue of long-term program involvement, to which we return in the section “Some Reflections on the IMF’s Longer-Term Role in Low-Income Countries.”

Weaknesses in the PRSPs inevitably impede PRGF-supported programs from adapting fully to their expected role. In some countries, this will be a transitional issue as strategies are strengthened and become better integrated into domestic institutions. However, this will happen slowly in many cases, and how the IMF role should adapt in such “difficult” cases remains unclear.

Moreover, some country authorities are reluctant to accept a more active role for the IMF, especially with regard to the broader policy debate.

***Insufficient recognition of the changes the PRS approach implies for the IMF’s “way of doing business”***

The implications of the PRS approach for the IMF “way of doing business” have not yet been fully acknowledged or acted upon. The approach implies a very different way of organizing IMF inputs based on: a country-driven strategy that sets priorities within a long-term timeframe; emphasizing contributions to informing a broader policy debate rather than traditional program negotiations; and operating within a “partnership framework” that recognizes explicitly that IMF contributions are only one part of a broader picture. All of these factors mean that the IMF program and surveillance roles in PRSP countries will be qualitatively different from those in other countries. But the consequences have largely not been spelled out, resulting in an attempt to address a very different set of

challenges with an essentially unchanged institutional approach.

For example, it is clear from our discussions with staff that many, while recognizing the value of the PRS approach, do not see it as implying fundamental changes in the way the IMF would contribute to a broad-based policy debate on the macroeconomic aspects of countries' strategies. However, the evaluation indicates that, for the PRS approach to have a meaningful impact in the IMF's areas of responsibility, encouraging a well-informed debate is critical.

Moreover, the BWIs have not used the PRS approach sufficiently as a mechanism for identifying priorities on what they should deliver and for coordinating key inputs from other partners, drawing on the countries' own priorities. For the IMF, this has meant that scheduling and integrating inputs from the World Bank into program design remains difficult.

## Recommendations

Based on these lessons, we make six broad recommendations. The first three concern the design and implementation of the PRS/PRGF approach. The other three are directed at clarifying expectations about the IMF's role and improving its effectiveness. Each recommendation outlines a broad direction of change rather than specifying a detailed blueprint. This approach seems preferable since there are a number of ways the recommended changes could be implemented that will involve, *inter alia*, choices on resource allocation that are best left to IMF management and the Executive Board. We give examples of possible steps to illustrate what we have in mind, but other approaches to implementing the recommendations are also possible.

### Aligning incentives and objectives

The rationale underlying the first three recommendations is to bring the incentives built into the design of the initiative more in line with its intermediate objectives. The approach we favor is one built around (i) greater country-driven flexibility (e.g., to allow countries to choose their own path toward improving domestic policy processes); (ii) transparency about those country-specific choices, so as to allow other stakeholders to express their views; (iii) monitoring on the basis of explicit benchmarks and strengthened *ex post* accountability; and (iv) a clearer framework in which donor support is decided, including through candid and graduated BWI assessments of countries' strategies.<sup>1</sup>

<sup>1</sup>An alternative approach to modifying incentives would be to establish challenging universal minimum standards in a number

*Recommendation 1. Introduce greater flexibility in the implementation of the PRS approach to fit better the needs of countries at different stages of the process and with different capacities and political and administrative systems.*

The PRS approach would have greater value added if it was made more flexible in practice to fit different country situations. Countries need to be put even more firmly in the driver's seat by determining themselves:

(1) How the policy formulation, implementation, and monitoring processes will be conducted and built up over time, and with what rules of the game (e.g., for opening up the policy process to previously excluded groups or strengthening budgetary processes). Progress would be monitored against an explicit set of country-determined intermediate benchmarks (see Recommendation 2).<sup>2</sup>

(2) What the output of these processes will be in terms of documents (e.g., PRSP Progress Reports) and on what periodicity they will be prepared, relying as much as possible on domestic institutional arrangements and reporting vehicles. IMF process requirements (e.g., linking reviews under the PRGF to completion of specific PRSP documents) should be minimized and oriented around domestic processes (so that they do not conflict with domestic timetables and/or duplicate domestic instruments).

*Recommendation 2. Shift the emphasis of the initiative from the production of documents to the development of sound domestic policy formulation and implementation processes.*

This broad recommendation would involve the following elements:

(1) *Build in greater results orientation.* Countries should be encouraged to establish—with help from BWIs where needed—substantive criteria for judging

of areas (e.g., for participatory processes or *ex ante* PSIA). See, for example, Oxfam (2004). We do not favor such an approach. Even though driven by the best intentions, it would result in the imposition of even more procedural requirements on PRS countries. Moreover, uniform standards do not allow for the diversity of countries' situations or for necessary priority setting.

<sup>2</sup>To give a concrete example to illustrate what we have in mind, a country might propose to broaden participation and monitoring through strengthening the oversight functions and capacities of parliament and at the local government level, with formulation and implementation of its medium-term strategy built around the domestic budgetary process. In which case, the BWIs should accept such an approach by not pressing for other possible procedural components and by accepting for their own internal purposes PRS-related documents oriented around these domestic processes. The country would establish benchmarks for monitoring progress in reaching the objectives it has set for itself, but the BWIs would provide their own frank assessments of the country's strategy and the policy processes by which it was derived.

progress toward key intermediate objectives such as developing (i) an operational road map that provides strategic guidance for setting priorities and resolving trade-offs; and (ii) effective institutional arrangements for formulating, implementing, monitoring, and updating this road map, with a firm link to budget processes.<sup>3</sup> The choice of the criteria/benchmarks judged to be most important would likely vary by country, but in some areas broad guidance could be developed by BWI staff or others, upon which countries could draw as a starting point.<sup>4</sup>

The existing PEM benchmarking exercise is an example of what we have in mind: it combines country-specific action plans for improving domestic processes; clear benchmarks for measuring progress, established with country consultation; and periodic ex post assessments that provide inputs for country-specific and initiative-wide assessments (see Chapter 4, section on “Strengthening Public Expenditure Management”). Given the central importance of good PEM systems to setting and implementing priorities, this is a tool that all PRSP countries—not just the HIPC—should be encouraged to adopt. However, the types of benchmarks chosen by each country will depend on the improvements that their PRS process identifies as a high priority.

(2) *Shift the emphasis of the incentives structure* faced by countries from procedural aspects and production of documents to achieving substantive changes in domestic processes and policies objectively measured as described in (1) above. The new set of incentives would include:

- (i) *Transparency.* Countries should present their intentions and objectives, along with the benchmarks selected to monitor progress in a manner open to public scrutiny.
- (ii) *Accountability.* IMF (and World Bank) staff would be responsible for providing clear and candid assessments of the progress made by each country in implementing the PRS approach, both in relation to the goals set by the

country itself and against initiative-wide benchmarks (see Recommendation 3).

- (iii) *BWI support.* IMF (and World Bank) staff would help countries identify key constraints in making progress toward PRS objectives and support efforts to ameliorate them. This would include not only domestic capacity constraints but also obstacles stemming from policies in advanced economies and other trading partners.
- (iv) *Selectivity in lending.* Realistically, access to donors’ resources will remain the key incentive for countries under the PRS approach. Ideally, donor decisions on the volume of resources provided should be linked to the progress countries are making under the approach. To facilitate this, IMF assessments in its area of expertise need to provide as clear and candid a signal as possible (see Recommendation 3). The criteria guiding the IMF’s own lending decisions under the PRS approach could also be improved in this regard (see the section “Some Reflections on the IMF’s Longer-Term Role in Low-Income Countries”).

*Recommendation 3. Clarify the purpose of the JSA and redefine the vehicle accordingly.*

An objective assessment of a country’s efforts toward poverty reduction and growth, reflecting the joint perspective of the staff of the IMF and World Bank, can be of value to many audiences: (i) to the authorities, as feedback on how to improve the effectiveness of their efforts; (ii) to BWI Executive Boards, as input into their lending decisions; (iii) to other donors, as a signal of BWI views on the quality of the poverty reduction and growth framework of the country; and (iv) to the public, for purposes of monitoring and accountability. In our view, therefore, the JSA is a useful concept whose potential has not been realized and we recommend making the following changes:

(1) JSAs should focus on the adequacy of domestic policy choices and the quality of domestic processes—including monitoring and implementation arrangements, budget decision making, and public expenditure management systems—as well as actual progress toward intermediate objectives, and less on the quality of the PRSP as a document.

(2) To foster clear and candid assessments, we propose: (i) making explicit the criteria and benchmarks used by staff to form their judgments (see also Recommendation 2); (ii) reporting on the views of third parties (especially local stakeholders and donors) when available, and discussing differences

<sup>3</sup>This recommendation is similar to the call for an operational framework made by staff of the European Commission (EC) and World Bank in their “Joint Note on Supporting the PRSP Process in Africa” (EC and World Bank, 2003).

<sup>4</sup>For example, benchmarks on various issues being developed by the New Partnership for Africa’s Development (NEPAD) might be drawn upon by African countries. In other cases, UN agencies (or even international nongovernmental organizations (I-NGOs)) might make suggestions or countries may choose benchmarks tailor-made to their own priorities and circumstances (e.g., for participatory monitoring of local expenditures). The important point is that the countries themselves should choose what are the priorities for monitoring progress and not be overburdened with a multiplicity of requirements.

of view;<sup>5</sup> and (iii) eliminating the need for JSAs to reach a binary (yes or no) conclusion as to the adequacy of the PRS as a basis for BWI concessional lending. JSAs should aim to provide a *graduated* assessment of the strength of the PRS and related processes as well as of the quality of policies.

(3) The effectiveness of the above recommendations could be enhanced if JSAs were produced on an independent schedule (e.g., once a year), rather than being linked to a specific PRSP document—which inevitably creates a focus on the document rather than the process, and creates another procedural requirement for the country. This would have the added benefit that BWI monitoring of PRS implementation would continue regardless of PRGF-related developments.

(4) The JSAs would be more effective if, in addition to flagging weaknesses in the PRS, they indicated clearly what are the main obstacles to overcome (including those not under the control of country authorities); what the IMF proposes to do to help address them in its areas of responsibility; and what needs remain unaddressed, especially in the area of capacity building.

There are a number of ways these key functions could be carried out and an instrument like the JSA is only one possibility. For example, an alternative would be to rely on other instruments within the IMF (e.g., the surveillance process) and the World Bank (the Country Assistance Strategy (CAS)).<sup>6</sup> However, we see merits in maintaining a joint instrument, since it is more consistent with the partnership dimension of the PRS approach.<sup>7</sup> Indeed, looking forward, the assessment instrument may need to adapt further in this direction. For example, if general budgetary support by bilateral donors to a number of PRSP countries continues to expand, a joint “partner” assessment—built around the common performance assessment frameworks (PAFs) that have been developed for several countries (e.g., Tanzania and Mozambique), but expanded to incorporate explicit IMF inputs—might be a logical development in the future.

### Clarifying the IMF’s role and improving its effectiveness

The practical implications of the adoption of the PRS approach for IMF operations go well beyond

<sup>5</sup>We are not suggesting that the JSA should become a “negotiated” document with all of these stakeholders.

<sup>6</sup>The CAS details the partnership between the Bank and each borrowing country. Usually covering a three-year period, it defines the level and composition of assistance to be provided based on needs, portfolio performance, and overall policy performance.

<sup>7</sup>Moreover, unlike the JSAs, the alternative vehicles are not automatically made public.

the formulation and negotiation of IMF-supported programs and have not been fully recognized. In order to orient our recommendations in this area, we note that two types of decisions need to be taken with respect to the IMF’s role:

- Decisions concerning the “architecture” of the IMF’s role in low-income countries. This involves the nature of the IMF’s signaling function as well as the role of IMF conditionality and financing in the longer-term PRS framework. These decisions go beyond the scope of the present evaluation and we do not make specific recommendations. However, we discuss in the section “Some Reflections on the IMF’s Longer-Term Role in Low-Income Countries” a number of principles that should be taken into account.
- Within the present “architecture,” decisions concerning how much the IMF should be directly involved in helping countries implement the PRS approach and changes in the IMF “way of doing business” that need to be made, irrespective of choices on the scope of the IMF role, to improve the effectiveness of the institution’s contribution. These issues are addressed in Recommendations 4–6.

*Recommendation 4. Clarify what the PRS approach implies for the IMF’s own operations and strengthen the implementation of the agreed role.*

The thrust of this recommendation is to clarify what is expected of the IMF under the PRS approach and to outline changes that would improve its effectiveness in meeting these expectations.

#### (1) IMF engagement in the PRS process

- More emphasis should be given to IMF activities that help to better inform broad-based policy discussions in its areas of competence. Guidelines to staff need to be clarified so as to encourage more active inputs to such discussions, including analyzing alternative policy options and trade-offs. In exchanges with the evaluation team, some IMF staff expressed concern that such activities go beyond the Fund’s mandate and can potentially conflict with domestic ownership. However, domestic ownership should not be interpreted to mean lack of transparency in what the IMF would expect on macroeconomic policy and the reasons why it takes this view. One possible approach might be for the IMF staff to prepare a short note on key macroeconomic issues that need to be addressed in the broader growth and poverty reduction strategy, which the authorities could make public if they wished.



- Rather than establish uniform “standards” for the IMF’s role, expectations should be tailored to country-specific circumstances, including the government’s wishes. These country-specific “rules of the game” should be made public—perhaps in the form of an aide-mémoire attached to the JSA or the Article IV staff report—and could describe how IMF staff are expected to participate in the broader policy debate, including what supporting analytical work they will undertake. This is also likely to require a combination of: (i) more “stand alone” missions, set apart from program negotiations, and (ii) enhancing the role of resident representatives.
- There should be more systematic explorations of country-specific macro-micro linkages—both through the IMF’s own analysis and research activities and by drawing more systematically on the work of others.
- Article IV surveillance reports should be used systematically as a vehicle to convey the IMF’s own thinking and analysis on key issues, and the staff should routinely seek the views of the authorities and others on the types of issues that should be addressed in surveillance.
- Assess systematically, as part of broader IMF surveillance activities, obstacles to the achievement of PRSP objectives originating in trade and subsidy policies of main trading partners (drawing, to the maximum extent possible, on inputs from other agencies). The *Global Monitoring Report* (World Bank and IMF, 2004a) has already made important steps in this direction.

#### (2) PRGF-related activities

- The rationale for IMF policy recommendations and program design should be subjected to broader scrutiny and debate. Possible steps in this direction could include (i) facilitating wider dissemination and discussion of IMF analysis that forms the basis of its policy advice (including, where appropriate, technical assistance reports); and (ii) encouraging greater openness to “independent/external voices” as inputs into program design, when agreeable to the authorities.<sup>8</sup>

<sup>8</sup>The Tanzania case is a good example and illustrates that a change in the “way of doing business” toward strengthening the capacity of countries to engage in discussion on such policy advice requires primarily a change in attitude and organizational approach. We are not suggesting that the IMF has to provide the resources for any additional outside inputs, but bilateral donors may wish to do so. Indeed, in the Tanzania case the additional analysis was financed by a bilateral donor.

- Clarify the approach to be taken by the IMF in those cases where the PRS approach has added some value but has not yet produced an operational road map or the necessary institutional framework for implementation. Even in these cases, there may be significant scope for opening up the policy space and incorporating evidence on macro-micro linkages (including PSIA) more systematically into program design, even though the priorities for such activities will not be driven by a coherent country-driven strategy.
- Clarify what the BWIs are trying to achieve *jointly* through the streamlining of conditionality and how this fits with stronger domestic ownership; establish a system for the monitoring of aggregate Bank-Fund conditionality at the country level.

#### (3) Streamline IMF documentation and Board scrutiny of PRS documents

Exactly how this streamlining should be done will depend on what role the JSA plays (see Recommendation 3), but there seem to be two possible approaches: (i) make the JSA the central assessment instrument, with operational meaning—in which case “comfort” letters and detailed analysis of the PRS strategy in other staff reports (Article IV or PRGF-related) would be unnecessary; or (ii) incorporate the functions of the JSA into surveillance and/or program documents. In any event, IMF Board discussion of the PRSP itself seems unnecessary (although Directors should continue to receive PRSPs for information). At the initiative-wide level, separate annual reports on Progress in Implementing the PRSP Approach and the *Global Monitoring Report* on the Millennium Development Goals (MDGs) appear duplicative and could be merged.

*Recommendation 5. Strengthen prioritization and accountability on what the IMF itself is supposed to deliver within the broader partnership framework, built around the priorities emerging from the PRS process, and ensure that resources match commitments.*

The IMF should tailor its involvement more closely to country needs, taking into account the contributions from other partners. Because these needs vary widely and because resource constraints on the IMF will remain tight, a more systematic approach is needed to (i) setting priorities on what the IMF itself will deliver; and (ii) ensuring appropriate coordination of key inputs from other stakeholders. Prioritization and coordination could be improved as follows:

- (1) Generate, as part of the PRS process, specific priority actions for the IMF to assist the country con-

cerned to reach its objectives, including for analytical inputs and long-term capacity building. If the IMF is not well-suited to produce a particular input (e.g., some PSIA), but this input is judged critical for program design, a clear identification—stemming from the PRS priorities—of who has agreed to do what and by when would strengthen incentives. Such key deliverables would be agreed with the government and made public. These priority actions would then be the basis for evaluations of IMF performance, both at the country level and in aggregate.

(2) The IMF's own budget decisions on allocation of administrative resources should be geared to these priorities. Linking realistic resource allocation decisions to a more explicit set of priorities should help improve decision making and make clearer to all what the IMF has committed to, and what it has not. However, the evaluation suggests that the ambitious original expectations of the IMF's role in the PRS approach would require more resources than have been provided so far.

(3) Experiment with broader “external reviews” of the PRS/PRGF process, monitoring in particular the performance of donors and international financial institutions (IFIs) in providing support, and not just performance of the national authorities. Tanzania's Independent Monitoring Group (IMG) is one possible example of such an approach.<sup>9</sup>

*Recommendation 6. The IMF should encourage a strengthening of the framework for establishing the external resources envelope as part of the PRS approach.*

The present “architecture” of the PRS approach does not provide a clear framework for helping countries and donors decide what is an appropriate medium-term resource envelope in which the macroeconomic strategy should be derived. The evaluation has not produced sufficient evidence for us to recommend a particular “right” approach on this issue. However, we would not favor a greatly expanded role for the IMF that would risk taking it beyond its comparative advantage. Elements of a solution would include:

(1) The country itself, not the IMF or World Bank, should eventually play the central role in elaborating macroeconomic frameworks and catalyzing donor support. The pace at which this transition can be made will depend on specific capacity constraints

<sup>9</sup>The IMG was appointed jointly by the Government of Tanzania and donors in 2002 to examine the factors that undermined the impact of aid and its contribution to supporting Tanzania's PRS. In particular, the IMG would monitor the policy dialogue, financial management and governance issues, predictability of aid flows, and the nature and use of technical assistance.

in each country, but country leadership seems essential to “owning” the process.

(2) The IMF role would be to provide debt and macroeconomic sustainability assessments and judgments on the policy framework, but it would not be responsible for the “normative” judgment on appropriate aid levels over the medium term.

(3) The tension between “ambition” and “realism” in determining the external resource envelope can perhaps be handled by presentation of alternative projections (consistent with assumptions of stronger policy reforms as well as additional external financing). The IMF should provide increased analytical support for such approaches when requested. But the choice to prepare alternative projections should remain with the country and not be a uniform requirement.

(4) Improving aid predictability is a wider problem that the IMF cannot resolve on its own. Consistent with the PRS approach, donors should be making and implementing firmer medium-term commitments, linked where possible to country budget processes with clear triggers for financing decisions. However, this is only feasible if the PRS process generates an effective operational road map. The challenge is how to reconcile PRSP countries' concern for aid predictability with donors' concern for aid effectiveness, which implies some performance-based selectivity. For the IMF, this requires finding a way—perhaps through a strengthened JSA—to provide signals to the donor community on macroeconomic performance that are sufficiently calibrated, and take account of the longer-term framework of donor involvement, to be a useful input into selectivity decisions without providing excessive “on-off” signals for financing. We return to this issue below.

## Some Reflections on the IMF's Longer-Term Role in Low-Income Countries

Many of the issues raised in this evaluation have to be addressed in the context of the larger issue of the IMF's longer-term role in low-income countries. A discussion on this subject has already begun.<sup>10</sup> It

<sup>10</sup>Since the summer of 2003, several discussions were held in the IMF's Executive Board on various aspects of the role of the Fund in low-income countries. This discussion is still ongoing. The staff papers on which the Board discussions were based, along with the preliminary conclusions reached by the Board, are available on the IMF's website ([www.imf.org](http://www.imf.org)). The key papers are as follows (starting with the most recent): “The Fund's Support of Low-Income Member Countries: Considerations on Instruments and Financing” (February 24, 2004); “Fund Assistance for Countries Facing Exogenous Shocks” (August 8, 2003); “Role of the Fund in Low-Income Member Countries Over the Medium-Term—Issues Paper for Discussion” (July 22, 2003).

is beyond the scope of this evaluation to make detailed recommendations on the strategic policy choices involved, but our investigation has highlighted a number of unresolved issues—some of which have not yet been aired sufficiently in the IMF’s own papers on the subject—that will require the Executive Board to take several critical decisions. We summarize here the key decisions that will be needed and suggest a number of principles that should be borne in mind as they are taken.

The key *decisions* are:

(1) *What should be the signaling role of the IMF in the longer term and how should it be provided?*

The revealed preferences of major development partners and of many low-income countries suggest that if substantial donor support is to continue, an IMF signal of the quality of macroeconomic policy will be required. This certainly requires an IMF signal that is credible and clear, but it may or may not require financing and conditionality. Decisions on the signaling role should also distinguish between (i) the need for judgments on the overall macroeconomic framework and strategy (for which a JSA-type vehicle may be needed), and (ii) monitoring of shorter-term performance where needed (a role traditionally performed by IMF conditionality; see (3) below).

(2) *What should be the IMF’s financing role in low-income countries and what should be the criteria for “exit” from such financing?*

The existing criteria for such financing are based on the concept of “protracted balance of payments need,” which is so vague as to be difficult to distinguish from development financing in practice. Assessments of a protracted balance of payments need are expected to consider not just the country’s overall balance of payments position at the time of the request for financing, but also “past, present and prospective external performance [indicators], such as export and import performance, terms of trade development, access to capital markets, cost of debt service, foreign reserves [and] medium term financing gaps that the [country] might experience in its growth oriented adjustment effort.” A *present* balance of payments need is not required. These criteria do not provide effective guidance for when the IMF should shift its support from traditional lending arrangements to other forms of engagement and in practice have justified continued financing.

In contrast, there has not been enough emphasis on the implications of the PRS process itself for an “exit” strategy from IMF lending. Unbundling the various nonlending functions that the IMF is expected to perform under the PRS approach (see Recommendation 4) makes clear that the IMF can remain very substan-

tially involved in the PRS process without providing baseline financing over long periods.<sup>11</sup>

(3) *What will be the nature of IMF conditionality in the longer term as the PRS approach takes root?*

This will require decisions on what is the rationale of IMF conditionality in a longer-term, partnership-oriented framework where everyone recognizes that donors are “in for the long haul” and there is a strong emphasis on country ownership.<sup>12</sup> One possible route would be to restructure IMF conditionality to fit within a broader “partnership” approach to monitoring and assessing progress in implementing the PRS. For example, the IMF could join the collective approaches to monitoring PRS progress that are evolving between those donors (including the World Bank) providing direct budgetary support (e.g., the PAFs for Tanzania and Mozambique). However, even within such a framework, the IMF (and its partners in the PRS approach) might come to the conclusion that there are grounds to maintain a separate quantitative monitoring of the short-term evolution of key macroeconomic policy variables—given that providing short-term feedback on key budget constraints and macroeconomic sustainability is a central IMF contribution. But such monitoring need not necessarily be tied to IMF lending, nor should continuation of other flows be mechanically interrupted on the grounds of nonperformance of short-term conditionality.<sup>13</sup>

(4) *What should be the IMF’s role in strengthening the framework for establishing the external resources envelope that countries may count on?*

<sup>11</sup>Present policies call for access to PRGF resources to decline with successive three-year arrangements. However, policies that contemplate defining the appropriate levels of access for, say, the fourth and fifth rounds of three-year PRGF arrangements (i.e., 12 or 15 years into the initiative) raise very uncomfortable questions. It is hard to see any justification for such protracted, albeit low-level, financial involvement except on the grounds that only traditional programs carry sufficient credibility as signaling devices (either with the country or donors).

<sup>12</sup>The earlier IEO evaluation of the prolonged use of IMF resources suggests that traditional approaches to conditionality may lose their effectiveness in such situations, especially with regard to the types of reforms that take time and cannot easily be broken down into specific short-term conditions. (See IEO, 2002, Chapter 5, especially paras. 35–37).

<sup>13</sup>This concern was raised by a number of I-NGOs in their inputs to this evaluation. The Mozambique case study suggests a possible approach. Delays in completing reviews under the PRGF-supported programs flagged emerging concerns to donors but did not trigger an immediate interruption of financing by those donors providing direct budgetary support. Instead, active participation by IMF staff in a donors’ forum served as a mechanism for signaling what progress was being made in resolving the outstanding issues. An agreement was eventually reached and the program review completed, without any interruption in these broader financing flows.

As noted in Recommendation 6, the evaluation evidence suggests no “right” answer to this question—in part because the IMF has not, until recently, encouraged much experimentation with different approaches. However, elaboration of such a framework is not something the IMF can do on its own; all development partners will need to be involved. Part of the agreed framework should be understandings on the implications of IMF signaling on short-term macroeconomic performance for other financing flows.

We recommend that the following *principles* help guide these decisions:

- *The approach to the IMF’s role in the architecture of the PRS should build upon the specific comparative advantage of the IMF.* These include analysis and policy advice on macroeconomic and related structural policy issues, which are preconditions for sustained pro-poor growth. They should incorporate a focus on management of budget constraints and longer-term sustainability issues; technical assistance and capacity building in these areas; and a relatively short-term financing role to help cushion against adverse shocks that might push the longer-term growth and poverty-reduction strategy off track.
- *The IMF’s contribution in low-income countries will be only one part of a broader, partnership-based framework, and its modalities should be designed with this framework in mind.* In other words, strong coordination elements rather than “stand alone” approaches need to be built in from the outset, whether it be with respect to PSIA, conditionality, or decisions on overall external financing.
- *The choice of appropriate instruments to provide signaling should be based on the needs of low-income countries and their development partners.* However, the credibility of different signaling devices will depend partly upon the “architecture” chosen. At present, programs associated with IMF lending arrangements are so

central to the IMF’s role in low-income countries that nonprogram signaling tends to have less credibility. This could change if a different structure, with new signaling and financing instruments, were adopted.

- *The modalities of the IMF’s role should be mindful of the incentives created and should be designed to encourage countries to press ahead with their policy and process changes under the PRS approach.* To give an example, one possible way of integrating the IMF’s relatively short-term financing into the PRS approach that might be consistent with such a principle would be for the PRGF not to provide financing when there is no immediate balance of payments need (nor to design somewhat arbitrary phaseout schedules), but to incorporate provisions for greater contingent ease of access to financing when needed because of adverse exogenous shocks—provided that the JSA (or its successor) has given a sufficiently positive signal on the country’s progress in implementing the PRS.
- *Decisions on the intensity and length of IMF involvement in PRS countries and the way the IMF organizes its operations and allocate its staff resources to these countries need to be made in an integrated manner, so as to ensure consistency between commitments and available resources.*

To summarize, there can be no doubt on whether the IMF has a longer-term role to play in low-income countries. It clearly does, if only because macroeconomic stability is widely accepted as a precondition for sustainable pro-poor growth. However, it is important that the IMF’s role is kept within the institution’s comparative advantage. The challenge is to translate that basic approach into two sets of choices: first, on how to “embed” the IMF’s contribution most effectively into a broader partnership framework and, second, what should be the intensity and scope of the IMF’s involvement in that broader framework.



# Introduction: Origin and Objectives of the PRSP and the PRGF and Scope of the Evaluation

The IMF and the World Bank introduced the Poverty Reduction Strategy Paper (PRSP) approach in 1999 to strengthen their approach to providing assistance to low-income countries, including both new financial assistance and debt relief under the enhanced Heavily Indebted Poor Country (HIPC) Initiative. The new approach was accompanied by the transformation of the Enhanced Structural Adjustment Facility (ESAF)—the IMF’s concessional lending window—into the Poverty Reduction and Growth Facility (PRGF), with a view to giving a more central role to pro-poor growth considerations in the design of IMF-supported programs in low-income countries.

The purpose of this evaluation is to assess the effectiveness of the Poverty Reduction Strategy (PRS) approach, especially as a framework for the role of the IMF in low-income countries and for the delivery of IMF concessional assistance, the IMF’s own contribution to the approach, and the PRGF.<sup>1</sup> Since actual progress toward the objective of poverty reduction can only be assessed over a longer-term horizon, our evaluation focuses primarily on intermediate outcomes, especially changes in policy processes and policies, not on final outcomes. The evaluation assesses whether the approach is bringing about the fundamental process changes expected of it—both in the countries themselves and in the two Bretton Woods institutions (BWIs) and whether some course corrections might be needed at this stage. A parallel evaluation of the PRS process from the perspective of the World Bank’s role has been undertaken by the Operations Evaluation Department (OED) of the World Bank.<sup>2</sup>

<sup>1</sup>In this report, we will use the acronym PRSP only when referring specifically to the document itself. In all other cases, we will use the term Poverty Reduction Strategy (PRS).

<sup>2</sup>In accord with the terms of reference for the evaluation, we have not attempted to assess a number of important issues concerning the PRS where the primary responsibility lies with the World Bank. The terms of reference for the evaluation are available on the IEO’s website ([www.imf.org/ieo](http://www.imf.org/ieo)). The OED’s Approach Paper is available at [www.worldbank.org/oed](http://www.worldbank.org/oed).

## Origin and Objectives of the PRS Approach and the PRGF

Adoption of the PRS framework and the conversion of the ESAF into the PRGF signaled a shift in approach by the BWIs in their support for low-income countries. The PRS approach drew on key elements identified in earlier work, including the Comprehensive Development Framework (CDF) developed by the World Bank, as well as on the debate that took place on strengthening the link between debt relief and poverty reduction.<sup>3</sup> It was also intended to address concerns identified by internal and external evaluations of the ESAF and the related Policy Framework Papers (PFPs). These reviews concluded that PFPs had largely failed to reach their objectives and highlighted a number of problems with ESAF-supported programs: (i) lack of national ownership; (ii) weaknesses in the analytical and empirical bases of the social policy content of programs; and (iii) insufficient attention to trade-offs involving policy choices that imply significantly different paths for growth and social welfare.<sup>4</sup>

Thus, the new approach was intended to strengthen country ownership, enhance the poverty focus of country programs, and provide for stronger collaboration between the BWIs and more broadly among de-

<sup>3</sup>The framework for the approach was introduced in two background documents for the September 1999 Annual Meetings of the World Bank and IMF (1999a and 1999b). A suggested approach for the development of PRSPs and the role of the IMF and World Bank staffs were discussed in World Bank and IMF (1999c).

<sup>4</sup>For example, the *External Evaluation of the ESAF* (IMF, 1998, p. 36) noted that: “The predominant view—and many ministers and senior officials echoed it with some disappointment—is that although initially the PFP process had held great promise, it has become a rather routine process whereby the Fund brings uniform drafts (with spaces to be filled in) from Washington, in which even matters of language and form are cast in colorless stone. Many senior officials expressed the view that the PFP has become so uniform that it is difficult to distinguish one from the other.”

velopment partners in supporting country efforts. Other intermediate objectives included greater public accountability and an improved setting of priorities and design of public actions.

The new approach focuses on developing a country-driven process with broad-based participation, to evolve a comprehensive strategy for poverty reduction based on a long-term perspective. Five underlying principles were enunciated that would guide the process in each country (Box 1.1). The process leads to the development of a PRSP with three purposes:

- for the country, to lay out realistic but challenging poverty objectives, along with the policies needed to achieve them;
- for the BWIs, to provide a suitable basis for their concessional lending; and
- for other development partners, to offer a key instrument around which to organize their relationship with low-income countries.

Initially, there were no specific standards laid down that PRSPs were expected to meet. The idea was that the more general the approach, the better it could be tailored to different country needs, so that even though low-income countries face tremendously diverse conditions, they would in principle all benefit from the approach. Subsequently, in response to countries' requests for greater clarity, a number of "expectations" were outlined (e.g., in guidelines for JSAs to be prepared by IMF and World Bank staff) regarding the contents of PRSPs, but countries were free to pick and choose, at least in theory (Box 1.2).

To underline the dynamic nature of the PRS process, it was emphasized that the production of a PRSP would not be a one-off exercise, but an iterative one, starting with an interim-PRSP, leading to a full PRSP, followed by annual PRSP progress reports and, after three years, a new PRSP, with results from implementation and monitoring feeding back into formulation of the subsequent strategy papers.

For the IMF, the fact that PRGFs would be anchored in a country-owned policy framework was expected to be a major improvement over the ESAF. Seven key features were identified that would distinguish PRGF-supported programs from those supported by the ESAF. (These are discussed in more detail in Box 4.1.)

The policy papers introducing the new initiatives stressed (i) the need to be realistic about what could be achieved in the near term; (ii) that the degree of progress would depend on initial starting conditions and the nature and content of PRSPs would vary from country to country—as would the participatory process involved in their creation; and (iii) that the process would be a dynamic one—as over time both countries and donor institutions should learn by

### Box 1.1. Underlying Principles of the PRSP Process

1. *Country-driven* involving broad-based participation.
2. *Results-oriented* and focused on outcomes that benefit the poor.
3. *Comprehensive* in recognizing the multidimensional nature of poverty and in the proposed policy response.
4. *Partnership-oriented* involving coordinated participation of development partners.
5. Based on a *long-term perspective* for poverty reduction.

doing. However, there was no doubt that the new approach was intended to mark a significant change in the IMF's role and way of doing business in low-income countries.

### Initial Experience with the New Approach

As of March 2004, 37 countries, almost half of the PRGF-eligible total of 77, had completed a full PRSP (Table 1.1). A third of these had also produced their first PRSP progress reports, and 5 countries had more than one progress report. Of the full sample of PRGF-eligible countries, about two-thirds have so far had arrangements under the PRGF.

The initial experience was reviewed in reports on Progress in Implementation, which were initially prepared on a six-monthly basis, and since September 2002, on an annual basis. Each of these reports provided an opportunity to clarify expectations in some areas—with a strong focus on the contents of the documents to be produced by countries. In addition, a more comprehensive review of the PRS approach, discussed by the Boards of the IMF and World Bank in March 2002, incorporated extensive inputs from external stakeholders.<sup>5</sup> It also led to the identification of a number of "good practices" expected to enhance the effectiveness of the approach, directed not only to countries engaged in the PRS approach but also to the donor community and the BWIs.

All of these reports concluded that progress under the approach was "encouraging" and judged it to be "on track," although the criteria on which these judgments were based were not spelled out and progress was not measured in a systematic way across coun-

<sup>5</sup>See IMF (2002b).

### Box I.2. Defining Characteristics of Poverty Reduction Strategy Papers

The JSA guidelines state an “expectation that, although the specific content of PRSPs will vary widely across countries, a PRSP will include four core elements:”

#### *Core elements*

1. Description of the participatory process.
2. Poverty diagnosis.
3. Targets indicators and monitoring systems.
4. Priority public actions.

In addition, the JSA guidelines indicate a series of topics that PRSPs are expected to consider. The most relevant to the IMF’s areas of responsibility are:<sup>1</sup>

#### *Four pillars (of priority public actions)*

1. Macroeconomic framework.
2. Pro-growth structural and sectoral policies.
3. Policies for social inclusion and equity.
4. Governance and public sector management.

#### *Analytical building blocks*

1. Assessment of the impact of past policies on growth and poverty.
2. Analyses of the key constraints to growth and poverty reduction.
3. Analyses of the sources of growth.
4. Poverty and social impact analysis.

#### *Building blocks of the macroeconomic framework*

1. Macroeconomic program (including growth projections and key fiscal choices).
2. Financing plan.
3. Prioritized action plan.
4. Costing of the action plan.

<sup>1</sup>The guidelines note that “it is not expected that all PRSPs will address thoroughly all of the questions listed.”

**Table I.1. Status of PRSPs and PRGF by Region, March 2004<sup>1</sup>**

	Number of Countries	Interim PRSP	PRSP	First PRSP Progress Report	Second PRSP Progress Report	Third PRSP Progress Report	PRGF <sup>2</sup>
Africa	35 (12)	26 (10)	19 (12)	7 (7)	3 (3)	1 (1)	28 (12)
Asia and Pacific	18 (2)	5 (2)	5 (2)	1 (1)	0	0	7 (2)
Europe	2 (1)	2 (1)	1 (1)	1 (1)	0	0	2 (1)
Middle East and Central Asia	13 (4)	8 (3)	8 (4)	1 (1)	1 (1)	0	9 (4)
Western Hemisphere	9 (4)	4 (3)	4 (4)	2 (2)	1 (1)	0	5 (4)
<b>Total</b>	<b>77 (23)</b>	<b>45 (19)</b>	<b>37 (23)</b>	<b>12 (12)</b>	<b>5 (5)</b>	<b>1 (1)</b>	<b>51 (23)</b>

<sup>1</sup>Includes all (77) PRGF-eligible countries—the total has not changed since the late 1990s. Cases from the sample of 23 countries with full PRSPs as of end-2002 are in parentheses.

<sup>2</sup>Countries with an active PRGF-supported program as of March 2004.

tries, except in the sense of reporting increasing numbers of Interim PRSPs (I-PRSPs), PRSPs, and PRSP Progress Reports (PRSP-PRs) completed. The September 2002 “Progress in Implementation” re-

port also made clear that “substantial challenges” remained in the following areas: building capacity, opening up the policy dialogue, aligning external assistance behind national strategies, integrating the

### Box 1.3. Some Common External Criticisms of the IMF's Role in the PRS<sup>1</sup>

In considering the messages emerging from this evaluation, a review of the main external criticisms of the IMF's role in the PRS/PRGF initiatives can be helpful.

Most external critics generally begin with a recognition that the PRS process represents a significant step forward, notably in opening up new spaces for policy dialogue and giving various groups, including civil society representatives, greater access to policy debates previously closed to them.

Focusing on issues most directly relevant to the IMF, the main criticisms on *process* are:

- There has been too little broadening of the participatory debate on macroeconomic policy, although specific country experience varies. Even within governments, the debate is generally too narrowly based.
- The policy discussions and decision-making processes are often not well-embedded in existing political structures (e.g., role of parliaments is too limited).
- Alternative policy options—especially ones that deviate from the so-called “Washington Consensus”—are rarely explored. Donor (and, in the macroeconomic area, IMF) priorities still drive the process too much.
- PSIA of key macroeconomic policy proposals are rarely undertaken and do not represent a significant ex ante input into policy formulation.
- The linkage to the HIPC was partly responsible for rushed procedures that reduced the value added of the new approach.

<sup>1</sup>See, for example, Buirra (2003); Coyle and Evans (2003a and 2003b); Evrard (2003); Gomes and Lawson (2003); Killick (2002); Richmond and Ladd (2001); Oxfam (2003); and World Development Movement (2001).

On PRS *content* and the design of PRGF-supported programs, the main criticisms are:

- The PRGF still drives the PRSP on the macroeconomic framework and related policy issues.
- Program design is still insufficiently oriented toward poverty reduction. (However, different observers emphasize different priorities; some focus on the need for programs to expand further pro-poor spending on key social sectors (health, education, and so on), while others criticize an insufficient emphasis on strategies to improve incomes of the poor, as part of an alternative growth strategy.)
- Programs target too much reduction in fiscal deficits and inflation, to below thresholds at which there is clear evidence that further macro-stabilization is good for the poor and growth.
- The IMF is still seeking to impose conditionality that is not derived from the country-driven PRS.
- The IMF is guilty of “aid pessimism.” There are usually two distinct strands to this accusation: (i) programs are designed around projected reductions in aid flows, perhaps driven by an overall desire to reduce aid dependency. (ii) Macroeconomic frameworks in the PRSP/PRGF do not (but should) begin from a “needs-based” approach that takes as its starting point what external resources are needed to help countries progress toward achievement of the MDGs. Consequently, the IMF is failing to perform its “catalytic” role of signaling to donors what aid would be required to truly make a difference in reaching the MDGs.

This brief summary suggests that part—but not all—of the criticism of the IMF's role reflects differences of view about the underlying objectives. In particular, it is clear that a number of external observers—including various I-NGOs—have a more radical view of the objectives of broad-based participation, the desirable approach to catalyzing “need-based” aid, and the scope of the IMF's contribution to these activities.

PRS into budgetary priorities, and implementing the strategies outlined in the PRSPs. Throughout these reports, calls were made for flexibility in implementation and realism on near-term expectations of changes.

There have also been numerous external reviews of different aspects of the PRS approach. These external reviews reflect widely divergent expectations about what the new approach is meant to deliver, how quickly, and with what contributions from each group of stakeholders, in particular the BWIs themselves. A number of criticisms directed at the IMF emerged and we discuss them in our evaluation (see Box 1.3).

## The Links Between Policies, Growth, and Poverty Reduction

Since the evaluation is about how the IMF can help countries improve their prospects for growth and poverty reduction, it is worth emphasizing at the outset that knowledge of the links between policies and growth remains limited and understanding of the links between policies and poverty reduction even less so. While we do not propose to present a comprehensive literature review, there appears to be broad—albeit not universal—support for the following messages:

- There appears to be a robust association between reduction in absolute poverty and sustained, strong growth.
- Some policies and factors do seem to be associated with growth and, with somewhat less certainty, also with poverty reduction. These include macroeconomic stability (albeit with differences about when stability is achieved—for example, at what threshold inflation ceases to be a problem); investment in health and education; and openness to international trade.<sup>6</sup> However, it is important to avoid overly simplistic causal interpretations of statistical associations. For example, while there is evidence that successful economies (in terms of both growth and poverty reduction) tend to be more open, this outcome is not necessarily assured simply by pursuing market-oriented trade policies; it may require a combination of circumstances and preconditions in which trade policies are only one and not necessarily even the most important factor.
- Good institutions and a favorable environment for private-sector-led development linked to a proper system of incentives are generally favorable for growth.<sup>7</sup>
- Country-specific analyses and policy choices are essential for two types of reasons. First, optimal growth/distribution strategies aiming at poverty reduction in a given time frame would differ depending on initial conditions (e.g., starting levels of inequality) and on the composition of growth.<sup>8</sup> Second, to understand the linkages between the policies discussed above and growth/poverty reduction requires a good understanding of the macro-micro linkages in a particular country context, including the nature of country-specific institutional characteristics that determine the efficiency of markets.<sup>9</sup>

<sup>6</sup>See, for instance, Berg and Krueger (2003); Cashin and others (2001); Srinivasan (2001); Khan and Senhadji (2000); Winters (2000); and Fischer (1993).

<sup>7</sup>Rodrik and Subramanian (2003); Easterly (2003); IMF (2003d); and Frankel (2002).

<sup>8</sup>See, for example, Bourguignon (2003), who notes that, if the objective is poverty reduction, changing the distribution of income may be of relatively greater significance for middle-income inegalitarian countries than for low-income egalitarian countries.

<sup>9</sup>See, for example, Lucas (2002, p. 72): “Simply advising a society to ‘follow the Korean model’ is a little like advising an aspiring basketball player to ‘follow the Michael Jordan model.’ To make use of someone else’s successful performance at any task, one needs to be able to break this performance down into its component parts so that one can see what each part contributes to the whole, which aspects of this performance are imitable of these, and which are worth imitating.” The importance of country-specific circumstances probably accounts for the limited robustness of many cross-section regression findings on the links between policies and growth.

These considerations suggest that policy design poses complex problems. Homegrown policy debates—and more country-specific analytical work as an input to these debates—have the potential for improving the understanding of policy constraints and macro-micro linkages in particular country circumstances.

## Scope and Methodology of the Evaluation

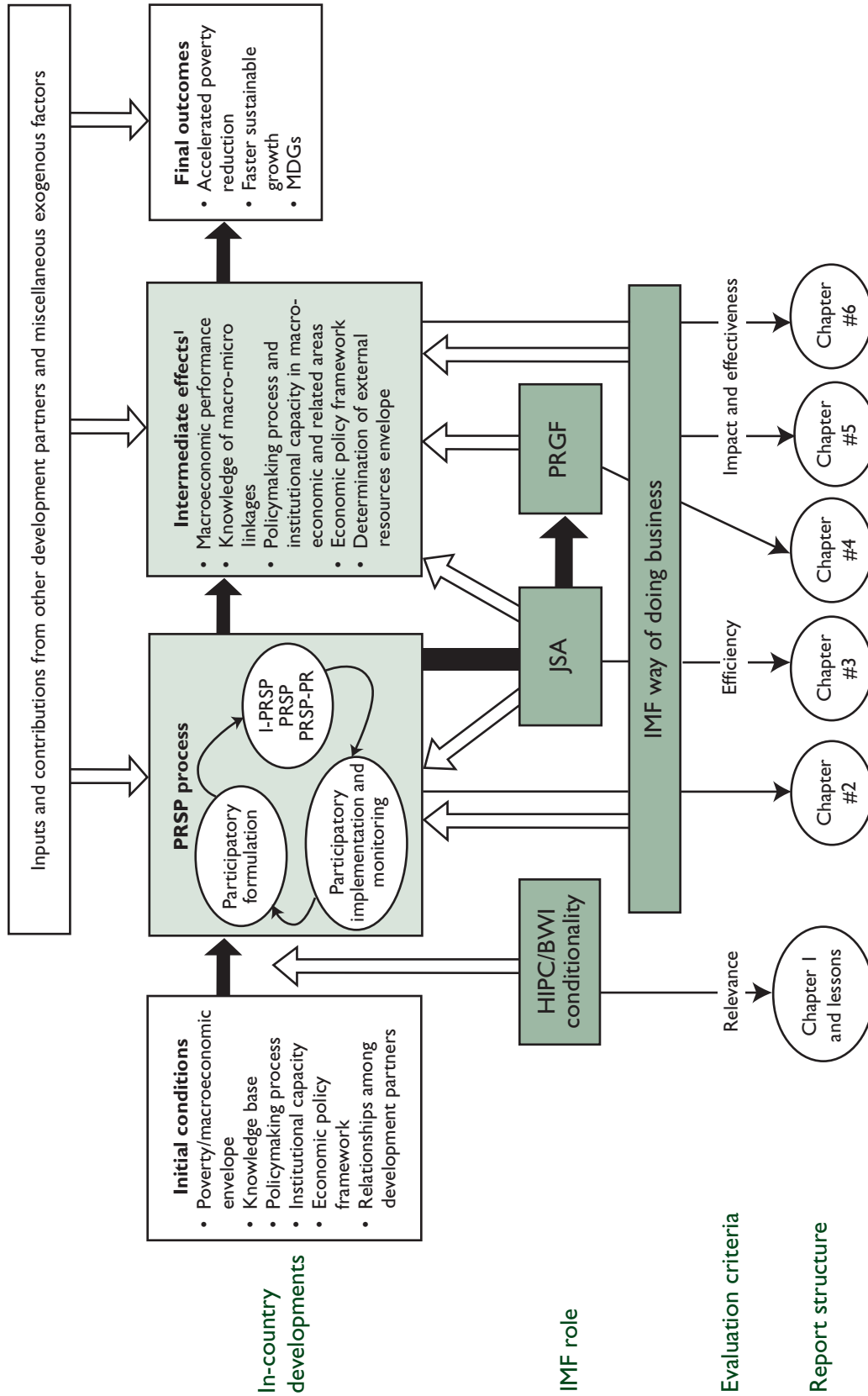
A few important considerations influenced the scope of the evaluation, all dictated by a need to keep it reasonably focused and consistent with the IEO’s comparative advantage:

- The evaluation concentrates on those dimensions of the PRS initiative that are directly relevant to the IMF’s mandate, the role of the IMF in the process, and the PRGF. Clearly though, the ultimate success or failure of the new approach depends on a much broader set of factors, including contributions from many partners in addition to the IMF.
- The evaluation focuses on the experience of countries with full PRSPs, based on the assumption that this experience has the greatest potential for generating lessons of importance for the IMF’s role in the future.
- At this relatively early stage, the evaluation cannot cast much light on long-term outcomes for growth and poverty though some information is available on short-term growth outcomes. The main focus of the evaluation is on inputs (the PRS process and the way in which PRGF-supported programs are formulated), outputs (i.e., PRSP contents and PRGF-supported program design) and intermediate effects (i.e., what institutional and policy changes has the new approach brought about and how well is the PRS linked to domestic budgetary and other country decision-making processes). It must be emphasized that existing policy papers provide little guidance as to how these changes are to be measured. Therefore, in carrying out our evaluation, we had to define indicators and benchmarks ourselves. This inevitably involves an element of judgment, but it is indispensable if the evaluation is to be objective.
- We do not address issues associated with the financing of the PRGF Trust Fund.<sup>10</sup>

<sup>10</sup>For a discussion of these issues and various options for the future structure of the PRGF instrument, see IMF (2004a).



**Figure I.1. Logical Framework of the PRSP Approach and IEO Evaluation of PRSPs and PRGF**



Note: The figure represents the logical framework of both the PRSP approach and the IEO evaluation of the PRSP and PRGF. As can be seen from the figure, we do not propose to examine final outcomes in detail. The evaluation proposes to examine the effectiveness of the approach by looking at the observable effects of the new policy framework on a range of variables relevant to the IMF mandate, and accounting for these effects by assessing (i) whether the initiative is implemented efficiently (both by country and as far as IMF inputs are concerned) and (ii) whether its design was relevant to address initial conditions. <sup>1</sup>Intermediate effects are expected across the whole range of conditions faced initially. Here we focus on the areas relevant to the IMF mandate.

**Table I.2. Country Case Studies for Evaluation<sup>1</sup>**

	HIPC Case?	Human Development Index Ranking <sup>2</sup>	Year of Full PRSP Completion	Year of "New" PRGF	Number of PRSP Progress Reports <sup>3</sup>	Number of Years of Implementation of PRSP <sup>3</sup>
<b>Joint IEO/OED</b>						
Mozambique	Yes	170	2001	*	1	2.3
Nicaragua	Yes	118	2001	2002	2	2.3
Tajikistan	No	112	2002	2002	0	1.1
Tanzania	Yes	151	2000	2000	2	3.1
<b>IEO only</b>						
Guinea	Yes	159	2002	2001	0	1.4
Vietnam	No	109	2002	2001	1	1.6
<b>OED only</b>						
Albania	No	92	2001	2002	1	1.6
Cambodia	No	130	2002	*	0	0.9
Ethiopia	Yes	168	2002	2001	1	1.3
Mauritania	Yes	152	2000	2003	2	2.9

\*New arrangement approved under ESAF regime in 1999.

<sup>1</sup>The IEO only and OED only case studies do not attempt to assess the role of the other parent institution, but do cover a number of issues of joint relevance. We will draw upon the "OED only" case studies in this report wherever they contain relevant information.

<sup>2</sup>According to UNDP (2002).

<sup>3</sup>As of end-2003.

One way of thinking about the scope of the evaluation would be in the context of a logical framework diagram (see White (1999) for an example of this approach). Figure 1.1 gives a broad indication of the different stages.

The evaluation mainly uses the following *types of evidence*:

- In-depth country case studies. The IEO undertook six country case studies, four of which were done jointly with the OED. An additional four case studies were undertaken by the OED alone (Table 1.2). The case studies were chosen to reflect diverse regional experiences, economic performance, and stages of the PRSP process.
- Each of the case studies involved field visits to consult with a broad range of national stakeholders, interviews with Fund and Bank staff, and a detailed review of both internal and public IMF documents.<sup>11</sup> The four country case studies undertaken jointly with the OED involved joint field visits and the preparation of a single country report. The coverage of topics varies between case studies, with IEO-alone cases re-

fraining from discussing Bank-specific issues, and OED-alone case studies refraining from evaluating IMF performance. However, the methodology applied was similar in all cases, which allows us to draw upon, where appropriate, evidence from all of the case studies.

- Cross-country analysis of countries with "full" PRSPs and of countries with PRGF-supported programs. Most of the analysis focused on the 23 countries that had completed their PRSPs by end-2002.<sup>12</sup> This analysis involved both quantitative and qualitative comparisons across countries. The latter inevitably involved some subjective judgments, but wherever possible we systemized these judgments by disaggregating them and then rating each issue according to a common scale, drawing upon standard codifications of what we would expect to see to warrant a particular rating. The purpose was to provide as much uniformity as possible to the overall cross-country judgments.
- A survey of a broad range of stakeholders in each of the case study countries, using a common survey format (see Annex 1).

<sup>11</sup>In addition, a joint IEO/OED workshop, hosted by the UN Economic Commission for Africa, was held in Addis Ababa on January 13–14, 2004 at which government and civil society representatives from the case study countries as well as several other countries discussed the case studies and the key messages emerging from the evaluation.

<sup>12</sup>The end-2002 cut-off was chosen in light of the terms of reference of the IEO, which call upon it not to interfere with ongoing operations. In addition to the case study countries, this sample includes Bolivia, Burkina Faso, The Gambia, Guyana, Honduras, the Kyrgyz Republic, Malawi, Niger, Rwanda, Senegal, Uganda, Yemen, and Zambia.

- A survey of IMF mission chiefs and resident representatives involved in the PRS and PRGF processes.
- Evaluations of aspects of the PRS process by other groups as well as evidence submitted directly to the IEO in connection with this evaluation.<sup>13</sup>

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<sup>13</sup>Evidence that was prepared specifically as inputs to the evaluation included Oxfam (2004) and CIDSE/Caritas (2004). Other evaluations that we have drawn upon are listed in the references.

The rest of this report is organized as follows. Chapter 2 discusses how the PRS principles are being applied in practice and presents an assessment of the contents of PRSPs. Chapter 3 discusses the role of JSAs. Chapter 4 discusses the PRGF and a number of program design issues. Chapter 5 assesses the IMF's way of doing business. Chapter 6 considers whether the new approach is making a difference vis-à-vis the intermediate and, where possible, final outcomes. Background details are provided in a number of annexes. The detailed country case studies will be available as separate documents.



## Implementation of the PRS Approach in Areas Relevant to the IMF Mandate

### Key Messages

*The design of the PRSP approach incorporates critical but largely unrecognized internal tensions: the PRS is to be country owned, but BWI policy assessments still obviously play a major role in financing decisions; it is to present strategic country aspirations, but also provide a sufficiently detailed operational guide for policymaking and external support; and it is to be country driven but meet various BWI-driven process requirements. An understandable desire to preserve flexibility has resulted in ambiguity about the intermediate objectives and hence the benchmarks against which to measure progress.*

*The result has been that, in practice, the underlying incentives focus too much on procedures and specific documentation, and that there are considerable divergences in expectations about what the initiative is meant to deliver.*

*PRS processes have generally been country driven to a much greater extent than previous approaches. However, BWI procedural requirements are widely felt to have too much influence. In a minority of countries, PRS processes are beginning to become sufficiently entrenched in domestic institutions to be self-sustained. In most cases, however, the PRS process is a long way from being one that adapts to unanticipated developments and where monitoring of implementation feeds back into policy design.*

*Participatory processes of varying nature and scope have been launched in all countries. Despite ambiguity about what such processes can or should deliver, in most cases stakeholders viewed them as an improvement over past practices. They have typically succeeded in improving poverty diagnostics and also, to an uneven extent, in improving transparency, public accountability, and influencing choices on public expenditure priorities. Their role in the area of macroeconomic and related structural issues has been marginal to date.*

*PRSP contents reflect value added over previous strategies in terms of comprehensiveness, results orientation and long-term perspective, although significant scope for progress remains even in “good practice” cases. The analytical bases of PRSPs are typically weak, most notably with regard to the macroeconomic framework and policies to promote growth.*

*Insufficient prioritization, inadequate costing, and a tendency to avoid controversial structural reform issues mean that most PRSPs do not yet provide an adequate framework for making strategic decisions on key trade-offs. An additional consequence is that PRSPs generally do not provide an adequate basis to guide the design of IMF-supported programs.*

*In some cases, progress is being made over time in ameliorating these various shortcomings, mainly in countries that have begun embedding the PRS process in domestic institutions.*

In this chapter, we examine how the PRS approach unfolded compared to original expectations, looking first at the PRS process and then at the contents of the PRSP document. Before turning to these assessments, we discuss briefly some internal tensions underlying the approach. The impact of the PRS approach on the broader policy formulation process and on policies actually implemented is discussed in Chapter 6.

## Tensions Underlying the PRS Approach

There are three potential tensions in the design of the approach. Reluctance to address explicitly the various trade-offs they involve has led to vagueness in some important aspects of the design. First, there is a tension between the principle that PRSPs should be country driven, and the externally imposed requirement for “broad-based participation,” which must be associated with an underlying—but unexpressed—judgment that existing political processes in the recipient countries are inadequate in some sense. This raises questions as to how the participatory process is supposed to mesh with existing domestic political processes and when these processes would be judged sufficient in and of themselves. Most observers would agree that, as a practical matter, policy processes in these countries would benefit from opening up to broader groups, especially those representing the disadvantaged, but there are obvious dangers in pushing participatory processes that supplant or bypass existing institutional structures. Recognizing this problem, the policy papers do not specify what broad participation should imply but only that the process should be managed by the country.<sup>1</sup>

Second, there is a tension between the two functions assigned to PRSPs, namely to present the strategic aspirations of the country with respect to poverty reduction and growth and to provide a sufficiently detailed operational strategy to enable the assistance programs of the BWIs to be anchored in the PRSP. This tension is reflected in debates over the nature of

<sup>1</sup>Ambiguity about precisely what is expected from countries reflects the lack of a mandate for the BWIs to impose a specific political “test.” Regarding the IMF, this reluctance derives in part from the principle under international law that an international organization only has the powers specifically conferred upon it in the relevant treaty. To the extent that the IMF’s expressed purposes (i.e., in Article I) are of a purely economic and financial nature, this has been interpreted to imply that the Fund should not interfere in political issues within member countries. In addition, the IMF’s Articles of Agreement make reference to respecting “the domestic social and political policies of members” in its surveillance of members’ exchange rate policies (Article IV, Section 3(b)).

the PRSP as a document and its audience. Is it meant to be a broad “strategic vision” paper emphasizing aspirations and strategy in general terms, with the general public of the country as primary audience or is it meant to be a more detailed operational road map, with government policymakers, BWIs, and bilateral donors as the primary audience? The tension became evident as subsequent preparation of various guidelines—beginning with those for Joint Staff Assessments (JSA) of PRSPs—elaborated on the expectations and of what PRSPs should contain. The result has been a quite complicated “architecture” of expectations/requirements (see Box 1.1 in Chapter 1) and, as we shall see, an excessive focus on BWI-oriented procedural aspects in actual implementation.

Third, there is a tension between the emphasis on country ownership of policies and the role of BWI policy assessments. This tension shows up in the question of how far the “policy space” should be broadened. While the initiative is meant to encourage the exploration of alternative country-driven policy options, there is still the basic requirement that the IMF (and the World Bank) must satisfy themselves on the soundness of country policies and the implicit assumption that they can help improve outcomes by influencing policy choices through (i) policy advice, drawing on good analysis and cross-country experience; and (ii) conditionality designed to monitor mutually agreed outcomes. A further potential aim is to encourage internal decision making in favor of reforms judged desirable by the BWIs. The latter aspect sits less comfortably with some notions of ownership, but the apparent conflict can be reconciled if there is a sufficient widening of the policy space to allow genuine ownership consistent with mutual agreement.

These unresolved tensions have led to considerable flexibility in implementation and variation across countries, which is desirable especially in the beginning. However, they made it harder to derive concrete benchmarks on what changes in processes the approach was trying to achieve. They also created great divergences in expectations on what some parts of the approach are meant to deliver, thereby exposing the IMF to criticism, especially from I-NGOs, that it is only paying lip service to some aspects of the initiative (e.g., ownership and participation).

## The PRS Process

We analyze the PRS process on the basis of the relevant key principles, focusing first on the extent to which it is country driven and then on the implementation of the principle of broad-based participation.<sup>2</sup>

<sup>2</sup>Implementation of the partnership principle, insofar as it relates to the IMF’s role, is discussed in Chapter 5.

### To what extent are PRS processes “country driven”?

Original policy papers do not define the notion of “country driven” but the spirit of the papers suggests that the definition has to do with how much control national stakeholders have over the structure, schedule, and outputs of the PRS process. We look at three types of evidence: (i) how the process was organized; (ii) stakeholders’ own perceptions; and (iii) to what extent the process became self-sustained beyond the formulation of the initial strategy document. In making this assessment, one needs to bear in mind the situation prevailing prior to PRSPs, when BWI concessional lending was supposed to be based on Policy Framework Papers (PFPs), which by the late 1990s had become widely criticized as not being country driven.

#### PRSP formulation process

In most of the country case studies the drafting of the PRSP was done by nationals of the country.<sup>3</sup> In three cases (Albania, Cambodia, and Nicaragua), the nationals in charge of drafting the PRSP were donor-funded consultants, which might have implied some donor control over the agenda. Indeed, in those three cases, the authorities complained about pressures from their international partners. By contrast, in Mozambique, the authorities refused any direct “support” from donors. In other cases, the authorities received some support from their development partners and indeed sought their feedback at various junctures in the process, but reported no complaints about feeling pressured by the latter.

Initially, the timing of the PRS process generally did not take into account domestic political cycles and planning processes but was driven by the timetable of the HIPC Initiative or, in non-HIPC countries, by the procedural requirements of the PRGF.<sup>4</sup> In two cases (Albania and Ethiopia) the PRSP happened to come at a very opportune time—in the sense that the country was ready and willing to engage in the formulation of a comprehensive poverty reduction and growth strategy—but this was fortuitous. In Vietnam, the PRSP followed the adoption of a new socioeconomic development plan, which provided the basis for several elements of the PRSP, although their priorities were not

well aligned. In several other cases, the timing of the PRSP proved to be a source of difficulties. In Nicaragua, there was a change of government shortly after the completion of the PRSP, bringing into office a team that did not endorse key aspects of the strategy. Lack of ownership by the incoming government critically diminished the relevance of the initial process. However, there was eventually a broader debate on key aspects of the development strategy (Box 2.1). By contrast, in Albania, many stakeholders interviewed reported that the PRSP provided an element of stability through a protracted political crisis and four changes of government. In Tanzania, the PRS process overtook the formulation of a homegrown external assistance strategy and led to it being temporarily set aside. Formulation of the latter strategy resumed later, although its purpose was modified somewhat to reduce redundancy with the PRSP.

Several countries in our sample had a well institutionalized planning tradition at the onset of the PRS process but the latter generally unfolded through different channels than these planning exercises, without integration of the outputs (Mozambique being one exception). The relationship between these traditional plans and the PRSP was unclear. In Cambodia and Vietnam, for instance, the PRSP was claimed to be the action plan operationalizing the National Development Plan. In practice, however, the plans are the more important strategic documents in the eyes of the authorities.

The role of parliaments in approving the PRSP was uneven: of the 29 PRSPs produced up to July 2003, the final draft of the document was formally sent to parliaments in only 13 cases, but was not always debated—let alone approved. In only 3 of the cases was the PRSP reviewed by a parliamentary committee.<sup>5</sup>

#### Stakeholders’ perceptions

In all country case studies, the authorities confirmed that the key initial driver for embarking on a PRSP process was the fact that it was a necessary condition for getting access to debt relief under the HIPC Initiative and/or to concessional lending from the IMF and the World Bank. However, in some of the cases (Albania, Ethiopia, Guinea, Mauritania, and Mozambique) the authorities rapidly came to perceive the exercise as an opportunity rather than an imposition. Tanzania also adapted the approach to its own needs, even though it was initially viewed as crowding out similar domestic initiatives.

<sup>3</sup>In most cases, the bulk of the drafting was done in English, with only final outputs translated in the local language. In Guinea and Vietnam, original drafts were in the official language. In Tajikistan, the I-PRSP was translated into Russian and served as a basis for some of the subsequent consultations.

<sup>4</sup>Access to PRGF resources (whether approval of a new arrangement or completion of a review) is conditional upon a country’s issuance of an I-PRSP, PRSP preparation status report, PRSP, or PRSP Progress Report in the previous 12 months.

<sup>5</sup>Among the 10 country case studies, the final PRSP was formally approved by parliament only in Mauritania and Tajikistan. A more detailed account of the role of parliaments in the PRSP process is given in Eberlei and Henn (2003).

### Box 2.1. Change of Government and Modification of PRSP Strategy: The Case of Nicaragua<sup>1</sup>

The Nicaragua case provides an interesting example of how “country ownership” interacted with a change in government. In the fall of 2002, the new Bolaños administration sought to modify the strategic priorities introduced by the previous government with the launch of a draft new development strategy. This initiative sought to change public expenditure composition in line with the new government’s vision on how to foster growth and employment creation. In essence, the debate revolved around the “growth pillar” of the PRSP and the new government’s greater emphasis on investment in areas that they viewed as having greater growth potential, but which were not always where the poor were found.

The government’s initiative, however, was marked by tensions in the process. The launching of the new strategy coincided with the agreement on a new PRGF-supported program and a new World Bank Country Assistance Strategy (CAS)—both of which were linked to the strategy in the earlier PRSP. The government felt constrained in its ability to pursue a revised strategy, while donors had expected the PRSP to bring a more

lasting policy framework, and were concerned that the new strategy had not been subject to sufficient participatory debate. Interestingly, the intention to modify the growth pillar was not a significant topic of debate during the electoral campaign, which raises obvious questions about the degree of integration of the PRS process with existing political mechanisms.

As a result of the mixed reception, the government decided to strengthen the original draft and broaden the consultation process. A planned Consultative Group meeting was postponed, and a consultation process on a shorter, revised document was set up. The authorities presented a revised growth strategy document during the Consultative Group meeting in October 2003. Moreover, the government indicated its intention to hold a workshop in early 2004 with stakeholders to discuss how to modify the PRSP based on the new strategy. Although still ongoing and too early to assess the outcome, recent developments point to changes in the right direction, including wider consultation and the broadening of policy dialogue.

This experience illustrates some of the potential tensions between different principles of the PRSP framework, notably between ownership—and the provision of greater policy space to the government—and other objectives such as partnership and participation.

<sup>1</sup>The background case study on Nicaragua provides a more comprehensive discussion.

The IEO/OED survey reveals interesting differences across groups on the extent to which the PRSP was driven by national stakeholders—from a clearly positive assessment by government stakeholders, to a negative one by I-NGOs and a neutral one by donors and local civil society. In 3 countries out of 10 (Mozambique, Nicaragua, and Tanzania), the average assessment across stakeholder groups was negative, whereas it was positive on average in the other cases.

#### **Implementation and sustainability of the PRS process**

A key test of the extent to which a PRS process is country driven is how it evolves beyond the formulation of the first full PRSP, in particular, whether the PRSP is being implemented and monitored, and whether it becomes as originally intended, a “living document,” periodically modified in the light of experience. A more demanding test is whether the process is sustained once there are no financial incentives directly attached to it. We examine each of these issues in turn.

As far as implementation is concerned, the case studies indicate that there was frequently a drop in

momentum immediately after the finalization of the PRSP, but implementation of some aspects proceeded relatively soon in most cases.<sup>6</sup> However, to the extent that a PRSP incorporated preexisting donor-funded program and reform strategies, implementing these aspects does not represent a particularly noteworthy development. Moreover, the very comprehensiveness of PRSPs and frequent lack of specificity and prioritization of their policy orientations also made it relatively easy to relate any new policy undertaking of the government to the PRS (see Box 2.2 on Guinea for illustration).

More generally, any assessment of implementation depends critically on the quality of monitoring and reporting systems. Reflecting the initiative’s emphasis on results orientation, most PRSPs envisaged ambitious monitoring systems, based on a large number of indicators. Actual institutional arrangements for monitoring PRS implementation have been set up in many of the case studies, sometimes building on existing structures (Albania, Ethiopia, and Mozambique), in other cases involving newly

<sup>6</sup>This is true even in cases where implementation was initially disrupted by political developments (e.g., Albania and Nicaragua) or by interruptions in aid flows (e.g., Guinea).



### Box 2.2. A Case of Observing PRS Principles Without Achieving Its Objectives: The Guinean PRSP

The Guinean PRSP, prepared by senior civil servants following a broad-based participatory process, was generally well regarded by the BWIs as a document, in the sense that it makes a comprehensive diagnosis of poverty, and presents a well-articulated strategy that takes a long-term perspective, is reasonably results oriented, and reflects some prioritization efforts.<sup>1</sup>

As a process, however, the PRS did not outlive the formulation of the PRSP itself. Dissemination of the PRSP within the country has been very restricted, so that there is little awareness—let alone ownership—of its contents. The participatory infrastructure set up for the formulation of the PRSP has been largely dormant since its completion, with the exception of two thematic groups, one focused on culture and communication, the other on evaluation and monitoring. The latter, however, only has a consultative role, and two years after the completion of the PRSP there are no well-defined transparent arrangements for the monitoring of PRS implementation. Mechanisms to update the PRSP are also lacking, and—with some exceptions in the year following the completion of the PRSP—the policy formulation process is driven by other considerations.

<sup>1</sup>The participatory process was broad in the sense that it included direct popular consultation at the grassroots level and involved representatives of civil society and donors in thematic working groups and occasional workshops. However, it did not lead to a meaningful policy debate in most areas, especially with respect to the macroeconomic framework and related structural reforms.

The PRSP had little impact as a strategic guide (especially in the macroeconomic and related areas), for the following reasons: (i) The macroeconomic framework outlined in the PRSP was superseded by events (including exogenous shocks, deviations from policy commitments, and withdrawal of external assistance) even before the PRSP was finalized. It was not subsequently updated to reflect changes in the external environment; nor did it incorporate contingency scenarios or broad orientations indicating how trade-offs should be resolved in the event of a changed environment. (ii) The PRSP was insufficiently prioritized, in the sense that the priority actions envisaged exceed both the capacity of the country to deliver and the resources available. In some areas, there is also a disconnect between the priorities outlined in the PRSP (e.g., governance) and the government's actual agenda. (iii) The PRSP initially had some links with the medium-term expenditure framework (MTEF) and, through it, the budget, but the budget actually implemented reflected only loosely PRSP priorities. (iv) The PRSP failed to discuss in any operational way structural reforms considered key for an improved macroeconomic performance, such as state-owned enterprise reform.

For reasons largely unrelated to the contents of the PRSP, the donor community has remained unwilling to provide financial support commensurate with the PRSP's needs and assumptions. The PRGF-supported program approved in 2001 went off track a few months after the PRSP was reviewed by the Boards of the BWIs, and the PRSP has not proved a useful guide to discussions between IMF staff and the authorities on ways to bring it back on track.

dedicated units (Cambodia, Nicaragua, Tajikistan, and Tanzania). In most countries, these institutional arrangements have yet to produce usable data, reflecting in part acute capacity constraints and difficulties in prioritizing indicators.<sup>7</sup>

The main evidence on which to base an assessment of PRS implementation are the PRSP Progress Reports (PRSP-PRs) that countries are required to prepare on an annual basis in order to have continued access to PRGF resources. The guidelines for JSAs of PRSP-PRs note that “with a view to minimizing the administrative burden on countries, it is expected that the reporting on progress could be integrated within regular government processes and be presented as short summary documents. The exact timing of the annual report is flexible, and could also change over time in order to become consistent with national

reporting and decision making processes.” However, PRSP-PRs issued to date suggest that, in practice, countries have not made use of the flexibility provided, nor in most cases have they integrated the preparation of PRSP-PRs with their own budget process. For instance, in Mozambique, the authorities wish to align substantive updates and revisions of the PRSP to the domestic political cycle, and they find it unfortunate that the production of a PRSP-PR follows a cycle driven by external procedural requirements.

As of February 2004, 12 countries had issued at least one PRSP-PR.<sup>8</sup> Many PRSP-PRs report good progress in the implementation of relevant structural reforms, often in the areas of public expenditure management, decentralization and privatization, and

<sup>7</sup>Issues related to monitoring of poverty and related indicators are discussed in greater depth in the parallel OED evaluation.

<sup>8</sup>Out of the 23 countries with over a year of experience under a PRSP. The 12 countries are Albania, Burkina Faso, Ethiopia, Honduras, Malawi, Mauritania, Mozambique, Nicaragua, Niger, Tanzania, Uganda, and Vietnam. Five of these countries have issued a second PRSP-PR and two have issued a third.

### Box 2.3. Too Much Paperwork?

The focus of the PRSP initiative on document production imposes a heavy burden on both country authorities and IMF staff. As the list below shows, both are asked to produce a series of papers with partially overlapping purposes and issues coverage. For the authorities, these paperwork requirements coexist with those of “homegrown” processes (e.g., budget documents, medium-term expenditure frameworks, and development plans).

Documents relevant to the PRS/PRGF initiative that are periodically produced by:

<i>Country authorities</i>	<i>IMF staff</i>
I-PRSP	PRGF staff report
PRSP	Article IV staff report <sup>2</sup>
PRSP Progress Report	Joint Staff Assessment (JSA) of PRSP <sup>3</sup>
Preparation Status Report <sup>1</sup>	JSA of PRSP Progress Report <sup>3</sup>
LOI/MEFP	Comfort/assessment letter <sup>1</sup>
	HIPC-related reports (three types) <sup>2, 3</sup>
	Country Strategy Paper <sup>1</sup>
	Ex post assessment <sup>1</sup>
	Progress in Implementation Report <sup>3, 4</sup>
	Global Monitoring Report <sup>3, 4</sup>

<sup>1</sup>Document to be produced only under specific circumstances, that is, not systematically required.

<sup>2</sup>Periodicity and other rules regulating the production of these documents are independent of the PRSP/PRGF initiative, but they are nonetheless highly relevant and have a high potential for overlap.

<sup>3</sup>Produced jointly with the World Bank.

<sup>4</sup>These reports are initiative-wide, but build on country-specific data. Their main authors are not the country teams responsible for the production of other reports listed.

in the setting up of working institutional arrangements to monitor PRS implementation. Only one country (Nicaragua) reported progress against annual quantitative targets.

The extent to which PRSPs are “living documents” varies considerably. At one extreme, the institutional arrangements that produced the PRSP have largely dried up (e.g., Guinea). At the other end of the spectrum, Tanzania has set up a process that allowed it to fill gradually the major gaps in its initial PRSP while also adapting it to changes in the macroeconomic environment. Mozambique has also made progress in institutionalizing the process. In between, most of the countries that have prepared PRSP-PRs have used it as an opportunity to update the initial strategy, often adding substantively to the original paper with regard to diagnostics (e.g., as the results of large-scale surveys became available) or with respect to specific sectoral strategies (e.g., in Mauritania, Nicaragua, and Vietnam).

To summarize, the extent to which PRS processes have been country driven varies substantially. In all cases, the primary driver was initially access to debt relief and concessional assistance, but in a number of cases country ownership appears to have strengthened over time. The extent to which the process has taken root, and brought about changes, also varies across sectors, being typically slimmest with respect to the

formulation of macroeconomic policies. Among the four country case studies that had reached their completion point under the HIPC Initiative at the time of writing, two (Mozambique and Tanzania) seem to have established processes now sufficiently entrenched that they are likely to be self-sustained.

#### Excessive documentation requirements

Another important message on PRS processes emerging from our evaluation—and one that was emphasized by both country authorities and IMF staff—is the excessive paperwork burden (see Box 2.3). Indeed, paperwork seems to have increased, rather than diminished, over time.

#### How effective has “broad-based participation” been in PRS processes?

##### What does “broad based participation” mean?

As noted above, the original policy papers were deliberately not very precise on what is meant by broad-based participation and there are a number of different concepts of participation in the literature. McGee and Norton (2000), for example, propose a ladder of degrees of participation consisting of (i) information dissemination; (ii) consultation (involving

**Table 2.1. Possible Categories of Participation and Their Objectives**

Possible Objectives of Participation	Is Objective Explicit in IMF Policy Documents?	(Minimum) Degree of Participation Required to Achieve Objective
A. Better design of poverty reduction/growth strategies A1. From improved diagnostics A2. From richer policy debate (considering broader range of alternatives)	Yes	Information exchange Consultation
B. Improved policy implementation B1. From enhanced accountability B2. From enhanced ownership /broader consensus	Yes	Information exchange Collaborative decision making
C. Empowering disadvantaged groups C1. By fostering a sense of inclusion C2. By strengthening the voice and influence of the poor in the domestic balance of power	No	Information exchange Collaborative decision making

a two-way flow of information); (iii) collaborative decision making; and (iv) initiation and control by stakeholders.<sup>9</sup> The degree of participation needed within this hierarchy depends upon the objectives sought. The matrix in Table 2.1 identifies different levels of objectives and indicates the level of participation relevant for each objective while also indicating whether the objective is explicitly mentioned in IMF policy documents. A review of IMF policy papers suggests that only objectives listed under A and B in the matrix are expected intermediate outcomes of the PRS/PRGF initiative. “Empowerment” receives more emphasis in external commentaries, but is not included among the explicit objectives of the initiative. Consistent with the concern not to impose a political test on countries, the JSA guidelines call for the staff to describe, not assess, the participatory process—with any assessment left to the Executive Boards, although the criteria on which such an assessment would be made are nowhere defined explicitly. In practice, the IMF Board rarely makes such an assessment. In the absence of specific standards, governments typically understood participation as information sharing or, at best consultation, with some variations across topics (see Annex 5 for details on the case study countries).<sup>10</sup>

<sup>9</sup>Other authors, while retaining similar categories, prefer defining participation as a continuum of approaches (e.g., Robb and Scott, 2001). The PRSP Sourcebook describes participation as “the process through which stakeholders influence and share control over priority setting, policy-making, resource allocations and access to public goods and services.”

<sup>10</sup>The idea of specific “standards” for participation appears to have been rejected during discussions in the early stages of the initiative, for two reasons. First, as in other areas, it was felt that imposing norms across countries would run against the initiative’s emphasis on country-driven processes; second, that such cross-country guidelines or standards would be meaningless because of

### **What has participation achieved in macroeconomic and related areas?**

Clearly, the appropriate or even feasible degree of participation will vary according to country circumstances (in particular, their “starting point” in terms of openness of the policy debate and literacy of the population), but also depending on the topic at stake. Thus, the yardstick of success is at least as much progress from the starting point as distance from the ultimate objective. With this in mind, we assess the impact of participation on policy issues where the IMF has primary responsibility among the BWIs.

*Did participatory processes contribute to a better design of poverty reduction strategies?* Most case studies suggest that the participatory process was instrumental in reaching a good diagnosis of poverty and in choosing related indicators to be included in the PRSP, by bringing out previously underemphasized dimensions such as vulnerability and other nonincome aspects of poverty. Beyond this admittedly important element, the impact of the participatory process on final strategies was generally not large, at least in areas of primary concern to the IMF.<sup>11</sup> It contributed to determining broad priorities in the composition of public expenditures in a number of cases and influenced policies in a few other areas (e.g., user fees for primary

the wide differences found between country contexts and political systems (a notion that is supported in the literature on participation). However, it is hard to see how at least clarifying what was expected from the participatory process (along the lines of the “ladder” discussed above) would have imposed more limits on the accommodation of country specificities than the current approach.

<sup>11</sup>This is reinforced by the broader sample. Only about one-fifth of the 23-country sample of PRSPs note any impact of the participatory process on policies.

schools) in several countries. In three of the case studies (Guinea, Mozambique, and Nicaragua), stakeholders noted that the prominence of governance in the strategy was a result of the participatory process. Beyond these specific examples, there is little evidence of a substantive impact of participatory processes on the macroeconomic and related structural policy choices embedded in PRSPs.<sup>12</sup> In a number of cases, some important but controversial structural policy issues did not surface in the broader debate around the PRSP (see the section “Contents of PRSPs in Macro-Relevant Areas.”). Consistent with these findings, our survey of PRSP stakeholders revealed that stakeholder groups outside of government disagree that alternatives were fully explored, and also generally disagree that the final document was modified to accommodate some of their viewpoints.

*What was the impact of PRS participatory processes on accountability and ownership?* In most of the cases studied, stakeholders felt that the participatory process leading to PRSP formulation represented a significant improvement over past practices, in particular by enhancing the transparency of government policies and access to government representatives. It also fostered a sense of inclusion that was new for many stakeholders. This effect was often short-lived, reflecting the ad hoc nature of the process, but it raised expectations that could, in some cases, be a driving force behind more sustained improvements in accountability going forward. Indeed, a number of civil society stakeholders we interviewed stressed that, viewed in a dynamic context, the process had opened up new windows to influence policy formulation and to provide feedback on implementation, which they viewed as a major value added even if the results had been more evident in some areas (e.g., some sectoral policies) than others. The case studies also suggest that the process created strong ownership of the strategy at least within the relatively narrow circle of those directly in charge of managing the PRSP formulation process. Ownership at the broader government level subsequently strengthened in many cases as implementation proceeded, at least in “priority” ministries (e.g., Albania, Ethiopia, Guinea, and Tanzania), but it remained elusive in other parts of government (especially at the local levels) and in large parts of civil society.<sup>13</sup>

<sup>12</sup>In several cases, a further broadening of the debate and of the policy space did occur over time, but the outcome was not necessarily reflected in the PRSP itself. This is discussed further in Chapter 6.

<sup>13</sup>This latter finding broadly echoes the conclusion reached, among others, by Booth (2003).

### **What were the main obstacles to more effective participation?**

*In most cases, the debate was not framed in a way that was conducive to effective participation* in the sense that participants were generally not made aware of key data and analytical underpinnings and of the trade-offs at stake, nor were they explicitly asked to prioritize their preferences. Moreover, the format of consultations limited participants’ ability to provide substantive inputs, in particular: lack of access to information before the meetings and of follow-up afterward; limited lead time to react to drafts submitted (especially in Cambodia and Guinea); implicit constraints to open expression of views by stakeholders (Cambodia, Guinea, Mauritania, and Vietnam); and, often, the advanced stage at which inputs were sought, implying little or no scope for discussion of alternative options and trade-offs.<sup>14</sup> Furthermore, in most cases, some key stakeholder groups (e.g., parliamentarians, the poor, and the business sector) did not take part in a meaningful way (see Annex 5 for details).

*Participatory processes typically did not address all building blocks of the PRS in the same depth, with policy areas of primary concern to the IMF receiving the least attention.* Poverty diagnostics were usually extensively covered, but macroeconomic policy and structural reforms were typically side-stepped or not discussed in any depth, with the important exception of the composition of public expenditures (Box 2.4). Still less participation and policy debate appears to have occurred in countries facing immediate macroeconomic stabilization challenges. Indeed, there was generally not even “information sharing” on some sensitive policy issues (e.g., bank restructuring and its fiscal consequences in Mozambique and Nicaragua). Many of these issues would be difficult to address substantively in “town-hall” type meetings, but except in a few cases there was little experimentation with other approaches to broadening the debate on macroeconomic issues (e.g., through involvement of local research groups, and more systematic discussion in relevant parliamentary committees). Countries where steps had been taken to establish more institutionalized processes did better in this respect (although as the Tanzania case suggests, even here there were limits to civil society involvement. We will return to this in Box 4.2). Not surprisingly,

<sup>14</sup>Similar problems are reported in external reviews of the PRSP experience in Bolivia, Cameroon, Ethiopia, Honduras, Mozambique, and Nepal (see, for instance, Stewart and Wang, 2003). While in most cases the pressure imposed by the schedule of the HIPC Initiative was reportedly an important factor, it cannot be an explanation for other cases.



### Box 2.4. Was Macroeconomic Policy Discussed in the Participatory Process? Insights from Case Studies<sup>1</sup>

**Tanzania.** Initial consultation involved some discussion of expenditure priorities but not of the broader macroeconomic framework or trade-offs involved. The situation changed dramatically afterward, with key macroeconomic issues now being debated in open forum in the Public Expenditure Review (PER) working groups. NGO involvement in those debates remains limited, however, at least in the macroeconomic area.

**Mauritania.** Limited involvement of NGOs in the activities of the working groups dealing with macroeconomic issues, due to lack of interest and capacity.

**Mozambique.** Macroeconomic policy not on the agenda of public consultations, but some issues surfaced nonetheless from NGO inputs, such as trade protection, industrial subsidies, and access to credit.

**Guinea.** One of six multi-stakeholder thematic groups set up to do the groundwork of PRSP formulation was dedicated to macroeconomic policy and growth sectors. Its participants reported having regular and active discussions throughout the PRSP formulation process. However, by their own account, these discussions were not very substantive. In particular, the overall macroeconomic framework in which the PRSP would be embedded was not discussed, nor were policy alternatives

or trade-offs. The main output of these meetings was to spell out broad policy objectives such as increasing domestic revenue mobilization, keeping inflation low, and enhancing the availability of micro credit.

**Vietnam.** Macroeconomic policy and some related structural reforms were not put on the agenda of consultations by the organizers of the process (notably the World Bank and I-NGOs, with the approval of the authorities) partly because they were not viewed as priority issues given prevailing macroeconomic stability.

**Tajikistan.** One of nine multi-stakeholder working groups set up to do the groundwork of PRSP formulation was dedicated to “macroeconomic management” and there was some discussion of macroeconomic issues in the consultation process. In particular, the poverty assessment report prepared by the NGO umbrella group does contain a number of recommendations related to macroeconomic policy, focused on transparency in public finances, tax policy, exchange rate management, and the fight against inflation. These inputs suggest there is scope for broadening participation in macroeconomic policy discussions.

**Ethiopia.** Discussions of the macroeconomic framework were generally viewed by stakeholders as insufficiently participatory, although they broadly acknowledged that the framework represented a step forward from earlier approaches.

**Cambodia.** The macroeconomic policy sections of the PRSP were not subject to any significant consultation with civil society representatives.

<sup>1</sup>Countries are listed in chronological order of completion of their PRSP (more recent last). Here, we define macroeconomic policy as including key medium-term macroeconomic assumptions, fiscal policy, the objectives of monetary policy, exchange rate, and related structural reforms (including reform of state-owned enterprise (SOE), financial sector reform, and trade policy).

therefore, most nongovernmental stakeholders surveyed disagreed that the macroeconomic framework of the PRS was derived in a participatory manner.

*The participatory process related to the formulation of the PRSP was conducted as an ad hoc exercise in most cases, not as one that would need to be sustained overtime. As a result, an initial drop-off in the level of participation generally occurred following completion of the PRSP. Efforts to disseminate the strategy to the general public once adopted have been limited.<sup>15</sup> In some cases (e.g., Albania, Mauritania, Mozambique, and Tanzania), this was fol-*

lowed by a gradual pickup at the monitoring and implementation stage, often as governments started preparing a PRSP-PR. In those cases, the development of participation was a dynamic one—gradually deepening over time as governments learned the advantages of such processes and various civil society groups began to identify various “entry points”—in particular the budget process—where they could have an influence on the decision-making process. In most other cases, however, the tapering off of participation has continued.<sup>16</sup>

In sum, the objectives requiring only information exchange (such as improved diagnostics, enhanced accountability, and greater sense of inclusion) were

<sup>15</sup>As of July 2001, of the 36 PRSPs and I-PRSPs documents produced by non-Anglophone countries, only 25 existed in an official language version and out of these 25, 17 were not published by the member country or by the IMF. Among the case studies, Mauritania and Tanzania are noteworthy exceptions. Resource constraints appear to have been an important factor in at least some cases.

<sup>16</sup>Across the 10 country case studies, civil society stakeholders surveyed generally disagreed that the government had continued to engage them in the PRS process beyond formulation. There was no apparent correlation between these perceptions and the maturity of the process.

often met to some extent. However, progress with respect to the objectives requiring a deeper form of participation—that is, richer policy debate and enhanced country ownership, strengthening the voice of the poor, and so on—was much less and was also uneven across countries and policy areas, with the least impact on issues where the IMF is more directly concerned. Some degree of institutionalization of the process seems essential to ensure continued stakeholder involvement and capacity building over time.<sup>17</sup> However, this also raises difficult questions on how to integrate the ad hoc PRS process with traditional democratic institutions, which, no matter how flawed initially, should take over the responsibility for the participatory process after a transition phase. In this connection, the very limited involvement of parliaments in PRS processes to date remains a cause for concern.

## Contents of PRSPs in Macro-Relevant Areas

We now turn to an assessment of the contents of the PRSPs in the areas most relevant to the IMF mandate based on a desk review of the 23 PRSPs and additional insights from the 10 IEO/OED case studies and external evidence.<sup>18</sup> We assess PRSP contents against four sets of criteria: first, compliance with the underlying PRS principles (see Box 1.2); second, whether the contents are so uniform that they imply conformity to BWI-driven policy approaches; third, the expectations and suggested characteristics established by the JSA guidelines; and finally, suitability as a basis for an IMF-supported program.

### Compliance with underlying PRS principles

#### Comprehensiveness

The principle of comprehensiveness applies both to the definition of poverty, and the policy agenda envisaged to tackle it. Our evaluation suggests that the principle has been implemented with greater success in the former area. The survey of stakeholders in case study countries indicates broad agreement that PRSPs make an adequate diagnosis of both the nature and causes of poverty. The case studies also revealed that stakeholders typically felt that the PRS approach had added value in this respect. JSAs also consider this area to be one of PRSP's main strengths in over two-thirds of cases.

<sup>17</sup>See Eberlei (2002) for a discussion of the defining characteristics of a fully institutionalized participatory process.

<sup>18</sup>Our focus here is on the PRSPs as documents. The impact of these documents on policymaking is discussed in Chapter 6.

Our assessment is much less positive with regard to the comprehensiveness of the policy agenda embedded in PRSPs. While virtually all PRSPs (in the 23-country sample) discuss growth, human capital development/social services delivery, and governance, these areas are generally not covered in the same depth. In most countries, significant efforts had already gone into defining strategies in the areas of health and education prior to the PRSP, resulting in more fully fleshed out strategies in these areas. There was typically much less emphasis on the broader obstacles to growth or on strategies in sectors such as agriculture or infrastructure. In some cases (e.g., Mozambique, Nicaragua, and Tanzania), strategies in the latter areas were completed post-PRSP. Strategies for private sector development were frequently underdeveloped. Fox (2003) notes that even though virtually all PRSPs assign a key role to the private sector as an engine of growth, less than a fifth outline concrete commitments in that regard (among the case studies, Vietnam is a noteworthy exception). Similarly, trade liberalization is an issue that, although of significance for growth and poverty, was discussed in some detail only in a minority of PRSPs.

Another problem revealed by the case studies is that the various components of the strategy are often poorly integrated, in the sense that the linkages and synergies between them are not fully discussed and that they do not necessarily fit in the macroeconomic framework of the PRSP. For example, in the minority of cases where it is spelled out, the total of expenditures required to implement all the parts of the strategy often exceed by far the available resource envelope (the Cambodia PRSP offers one of the starkest illustrations). Furthermore, in most cases, comprehensiveness was achieved at the expense of realism and operational relevance owing to a failure to prioritize the policy agenda (see next section).

#### Results orientation

Virtually all PRSPs discuss monitoring indicators and/or arrangements. Nevertheless, this area is identified by JSAs as a key weakness in 60 percent of PRSPs. A frequent problem revealed by our case studies is that the indicators and monitoring arrangements contemplated in PRSPs far exceed the administrative capacity to collect and analyze the underlying data (e.g., in Cambodia, Ethiopia, Guinea, and Vietnam)—a process that is very resource intensive and, realistically, will take many years to institutionalize in most countries. Furthermore, indicators are typically better defined for health and education strategies than in other areas, where inputs or process-based indicators tend to dominate, or indicators are simply lacking (e.g., in the area of structural reforms or governance). In some cases, there is no straightforward relation be-

tween the indicators monitored and the targets of the PRSP.

The most important obstacle to a greater results orientation of PRSPs is the still tenuous nature of links to the budget and medium-term expenditure frameworks (MTEF). Over half of the full sample of PRSPs lacked such links initially; among our case studies, only 4 countries out of 10 foresaw links in their PRSP, at least for expenditures in designated “priority sectors” (Albania, Ethiopia, Guinea, and Mozambique). In other cases (e.g., Tanzania), such links were successfully developed *ex post*. Where links between the PRSP and the MTEF existed on paper from the start, their effectiveness was weakened by the fact that the MTEF was itself only loosely connected with the budget actually implemented (e.g., in Guinea).<sup>19</sup> In Vietnam, efforts to establish a MTEF are only just beginning. These weaknesses reflect a combination of limited costing and prioritization in PRSPs and the poor state of public expenditure management generally—an issue we return to in Chapter 4.<sup>20</sup>

Despite these difficulties, interviews conducted as part of the case studies suggest that bringing some degree of results orientation to poverty reduction/development strategies has been one of the main value added of the PRSP approach.

### **Long-term perspective<sup>21</sup>**

Our survey of PRSP stakeholders suggests a general agreement (in 8 countries out of 10) that PRSPs provide an adequate road map to long-term goals, although I-NGOs and donors tend to be more skeptical than domestic civil society and government stakeholders. However, our evaluation suggests a more negative assessment. The linkages between medium-term, operational targets and longer-term ones are generally not well specified. In particular, most PRSPs do not provide an effective guide to how the strategy will need to be modified if the macroeconomic framework is disrupted, a decision that depends on how critical trade-offs are handled. We return to this issue later.

### **Are PRSP contents so uniform as to suggest implicit BWI-driven policy standards?**

While the JSA guidelines and the PRSP Sourcebook are explicitly not prescriptive, outside critics

<sup>19</sup>The approach taken in Uganda—to publish these documents as backing for the annual budget—seems to be the best one.

<sup>20</sup>Bevan (2004) provides a more detailed elaboration of these issues.

<sup>21</sup>Other aspects of this issue, including linkages between the PRSPs and the MDGs, are addressed in the OED evaluation.

have argued that there are implicit standards that countries feel obliged to abide by to ensure that the BWIs endorse their PRSPs.<sup>22</sup> We tested this hypothesis by reviewing the contents of the 23 PRSPs completed by end-2002. A high degree of uniformity could suggest the existence of implicit standards constraining the extent to which PRSPs can truly be country driven.

The desk review of 23 PRSPs does suggest some degree of uniformity, but not to such an extent as to prove the existence of implicit standards.<sup>23</sup>

- All PRSPs contemplate measures to increase domestic revenue mobilization, although the means envisaged vary by country: some mention side-by-side general increases in revenue, improvements in tax administration, broadening the tax base, and reforming tax legislation, while others choose to emphasize one or several of these avenues.
- A little over half the sample also considers measures on the expenditure side: in two cases, expenditure cuts; in other cases rationalization of expenditures or improvements in public expenditure management, alone or in combination.
- As regards key structural measures defined at a high level of generality, common themes do emerge: almost two-thirds of PRSPs envisage some form of privatization, and a little under half give some emphasis to financial sector reform (liberalization) and decentralization. The vast majority of PRSPs also put some emphasis on improving public sector governance. The coverage of all these areas in PRSPs may well reflect encouragements to that effect found in the JSA guidelines and the PRSP Sourcebook. Likewise, coverage of so-called cross-cutting issues, such as gender, environmental sustainability, and HIV-AIDS, was gradually mainstreamed after their absence in the first generation of PRSPs attracted repeated criticism from the Boards of the BWIs and was also mentioned in several of the staff reports on Progress in Implementation. But

<sup>22</sup>Strictly speaking, the IMF and the World Bank do not “approve” the PRSP. However, for countries to receive concessional lending (and, where relevant, debt relief) from them, the Boards of both institutions have to determine that the PRSP constitutes a credible poverty reduction strategy and a sound basis for their lending operations. In practice, most external stakeholders either are unaware of this subtle distinction, or regard it as irrelevant or misleading, in the sense that the positive signal from the BWIs is critical for external assistance in support of PRS implementation to materialize.

<sup>23</sup>The desk review involved recording in a matrix (not reported here) the following two elements for each PRSP: (i) key fiscal measures; and (ii) key structural policy measures in macro-relevant areas.

the policy choices made under these headings are country specific.

- PRSPs vary with respect to some fundamental policy choices. For instance, while a majority envisages a reduction of the role of government in the economy, about a third do not. In the area of trade policy, about a third of PRSPs envisage policies that directly contradict the policy advice given in the PRSP Sourcebook.<sup>24</sup>

There is also a widespread perception that the prominence given to governance in many PRSPs owed much to donor pressures. However, the case studies indicate that this high profile also accurately reflected the views expressed by many stakeholders during the PRS process.

While this evidence on content does not suggest an externally driven blueprint, perhaps of greater concern is what is *not* in the PRSPs. The case studies suggest that a number of issues that might be politically sensitive or where the authorities and the BWIs may have diverging views are given only a cursory treatment. Trade policy and state enterprise reforms were common examples; another area skirted over was issues associated with bank restructuring (e.g., in Nicaragua), although in this case there are practical reasons—avoidance of bank runs—why broader public debate would have been difficult. In any event, the fact that these issues were not dealt with adequately in the PRSP often led to “downstream” problems when the same issues arose in the context of PRGF negotiations. (We will trace through the impact of the policy debate on specific policy outcomes in Chapter 6.)

## Conformity to expectations set out in JSA guidelines

### Analytical basis

According to the JSA guidelines, PRSPs are expected to contain four key analytical elements: an assessment of the impact of past policies on growth and poverty reduction; an analysis of the key constraints to growth and poverty reduction; an analysis of the sources of growth; and poverty and social impact analysis of the key policies contemplated.

Most PRSPs are rather weak in their coverage of these aspects. No PRSP in the 23-country sample that we evaluated has all four analyses, and the largest group (43 percent of the cases) provides only one of the four elements. Two PRSPs (Burkina Faso

and the Kyrgyz Republic) that were accepted as providing a sound basis for concessional lending had none of these analytical elements. Of the four components, PSIA (loosely defined) is the least frequently found (in only 2 cases out of 23). Assessments of past policies and analyses of the sources of growth were the most frequent—undertaken in about half of all cases—but in a somewhat cursory way in most cases. Analyses of the key constraints to growth and poverty reduction are present to some extent in only 30 percent of PRSPs, with typically more emphasis on obstacles to poverty reduction than to growth.

It is important to recognize that these types of analyses are very demanding in terms of data availability and technical capacity and it is perhaps not surprising that the analytical basis is an area of weakness in most initial PRSPs. However, this weakness may limit the validity and relevance of the strategy adopted. Encouragingly, PRSP Progress Reports suggest that in several cases (e.g., Ethiopia, Nicaragua, and Tanzania) work is under way to remedy these knowledge gaps, but most PRS processes have not generated prioritized action plans on what the BWIs themselves should be doing to help fill these gaps.

### Prioritization, costing, and financing

JSAs identify costing, financing, and prioritization as one of the main weaknesses of PRSPs in two-thirds of the 23 cases. Costing of action plans is frequently attempted, but is usually partial and rudimentary.<sup>25</sup> Over a third of PRSPs lack a financing plan and/or a prioritized action plan.

The case studies reinforce these messages. While all PRSPs contain a policy matrix outlining elements of an action plan in various areas, these are frequently little more than wish lists resulting from the aggregation—without prioritization or costing—of the preferences expressed by various stakeholder groups in the participatory process (e.g., in Albania and Cambodia). Clearly, with practically no knowledge of the respective poverty impact of various measures and only imprecise estimates of their costs, it is difficult to achieve a meaningful prioritization of the action plan. In some cases, efforts have been made to assign degrees of priority to the various objectives of the PRSP, but the large number of “high-

<sup>24</sup>See Ladd (2003). This review also concluded that most PRSPs skirted many of the fundamental strategic choices involving trade policy.

<sup>25</sup>Bevan (2004) distinguishes three levels of PRSP “costing”—corresponding to rising standards: (i) wish lists of aspirations accompanied by tentative expenditure estimates where possible; (ii) aggregative and extrapolative expenditure estimates; and (iii) activity-based budgeting, based on unit costs. He concludes by stressing the very preliminary nature of what has been achieved in PRSPs against these standards, even in the strongest cases.



priority” objectives limits the practical value of this effort (e.g., in Guinea), and the actions considered to achieve each of these objectives are not, themselves, prioritized. Often, prioritization and costing are more advanced in “priority sectors” (typically health, education, and infrastructure) than in other areas. PRSP Progress Reports (for the whole sample of PRSPs) suggest that little progress is made in improving the prioritization and costing of PRSP action plans in the years following the completion of the full PRSP—Mozambique being a “good practice” exception.

### **Diagnosis of implementation constraints**

Most PRSPs fall short of expectations in discussing risks and implementation constraints. Less than one-fifth of cases provide such a discussion, even though our case studies indicate that administrative capacity constraints are severe and constitute a serious risk to implementation. Other risks, such as disruptions in aid flows or exogenous shocks, are also rarely discussed in detail, even though most countries experience them with some frequency. This assessment is echoed by our survey of PRSP stakeholders: in 6 countries out of 10, a majority of stakeholders surveyed do not agree that the targets and plans outlined in the PRSP are realistic, with I-NGOs and donors being the most skeptical groups.

### **Suitability as basis for IMF-supported programs**

As noted at the beginning of this chapter, the PRS initiative has established relatively few concrete benchmarks, in terms of intermediate objectives for changes in processes, against which progress of the initiative could be systematically assessed. Since PRGF-supported programs are supposed to be embedded in the PRSPs, one potential benchmark of particular importance to the IMF suggests itself: do PRSPs provide an effective strategic guide for policymaking in macroeconomic and related areas that would provide a suitable basis for IMF-supported programs? Existing IMF policy documents do not define explicitly which, among all of the expected or suggested components of a PRSP, are critical for them to constitute a sound basis for a PRGF-supported program. Our case studies suggest that the following characteristics are essential if PRSPs are to play this role:

- A macroeconomic framework (i.e., growth projections, revenue and expenditure projections, and balance of payments) that is realistic, internally consistent, and incorporates reasonable cost estimates for identified priority actions. It

should also identify how policies will be adjusted in response to unanticipated shocks;<sup>26</sup>

- A clearly articulated growth strategy, mindful of the trade-offs likely to arise and of their implications for poverty reduction.
- Prioritized public policy actions in macro-relevant areas, in particular related to the major structural policies that have been an issue in the past.

Very few PRSPs had satisfactory macroeconomic frameworks. In only 4 out of the 10 case studies (Albania, Vietnam, Mauritania, and Tanzania) did PRSPs present a realistic macroeconomic framework. In the case of the latter two countries, this was obtained by explicitly adopting in the PRSP the same framework as in the pre-existing PRGF-supported program. In the 6 other cases, the original macroeconomic framework was either superseded by events by the time the PRSP was discussed by the Board (Tajikistan, Guinea, Mozambique, and Nicaragua) or unrealistic (Ethiopia) or incomplete (Cambodia). In these cases, there was an understanding that annual PRSP Progress Reports would provide an opportunity for revisions of the macroeconomic framework.

In none of the 10 country case studies were alternative scenarios explored in the PRSP, and only in Cambodia did the PRSP consider, to a limited extent, the downside risks to the framework and their macroeconomic implications.<sup>27</sup> In most cases there were no contingency plans identified or even broad orientations outlined to indicate how the framework might be adjusted in response to adverse or favorable shocks.<sup>28</sup> Interestingly, these weaknesses were noted candidly in the respective JSAs, but did not prevent the staffs from reaching the unqualified conclusion that the PRSPs constituted sound bases for IMF and World Bank concessional lending. (We return to this issue in Chapter 3.)

<sup>26</sup>The idea is not for a PRS to offer detailed contingency plans attempting to address every possible type of shock that might arise, as experience shows that this is unrealistic and ineffective. Rather, the PRSP should set key strategic orientations that would provide guidance in solving the trade-offs that arise when policy adjustments are needed.

<sup>27</sup>Among the 23 countries that completed a PRSP by end-2002, only three (Niger, Rwanda, and Senegal) presented fully fleshed out alternative scenarios. Madagascar is another more recent example.

<sup>28</sup>The medium-term macroeconomic framework of the Tajikistan PRSP, for instance, was judged by staff to be conservative and therefore the JSA recommended to the authorities that they should flesh out a higher case scenario. In Guinea and Vietnam, the PRSP outlined broadly what additional expenditures would be undertaken in the event of higher resource availability. In the case of Guinea, the baseline scenario itself was optimistic, so the value added of an even more optimistic alternative scenario was limited.

### Box 2.5. Why Is It Proving So Difficult for the PRS Approach to Provide an Effective Operational Road Map on Macroeconomic Policy?

The evaluation suggests several reasons why the PRS approach has generally not been successful in using the new way of doing business implied by the PRS principles to generate a strategic guide to policymaking on macroeconomic issues.

1. *Problems of transition.* Many countries already had IMF-supported programs before their PRSP was finalized, and in these cases the macroeconomic strategy and framework was generally taken from the program and incorporated into the PRSP. Over time, more PRSPs are preceding the PRGF-supported programs, which would be the normal sequence (see Chapter 5).

2. *Capacity weaknesses,* especially in costing, public expenditure management, and budgetary processes. These weaknesses can be remedied over time, and some progress has been made but expectations need to be based on realistic assessments of each country's initial capacity in these areas. Major improvements will almost certainly take significant time.

3. *Insufficient change in the IMF's way of doing business.* The IMF's internal procedures have adapted, but there continues to be substantial differences between "average" and "best" practice. Moreover, the least change—in terms of exploring ways of opening up the policy debate to consider alternative options—has occurred in those circumstances where the IMF's role is likely to be most critical (e.g., in "difficult" cases where immediate macro-stabilization concerns are at the forefront). This suggests that additional efforts may be needed to apply the PRS principles in such cases, even when the PRSP itself is imperfect. We discuss these issues further in Chapter 5.

4. *Reluctance to address some controversial but macroeconomically critical issues in the PRS process.* Part of the solution to this and the preceding issue is to have clearer "rules of the game" on the nature of the policy debate.

5. *The nature of some macroeconomic policy issues makes it difficult to generate an effective, lasting operational guide.* Most low-income countries face especially volatile environments that complicate longer-term macroeconomic planning.<sup>1</sup> Consequently, detailed quantitative macroeconomic frameworks typically have a short shelf life. This means that discussions on how macroeconomic policies should respond to such shocks will inevitably take place at a much higher frequency than can be managed by the broader-based processes meant to drive the overall PRS. To be an effective operational guide, the broader strategy would need to incorporate guidance—in effect, contingency plans—for how to handle trade-offs in such circumstances. But there are deep political economy reasons why governments are reluctant in practice to spell out such contingency plans in advance.<sup>2</sup> The frequent result is that decisions on such matters are left within the traditional narrowly based framework of program negotiations.

6. *The operational role of the macroeconomic framework in the PRS is ambiguous.* In particular, it is unclear how the tension between "needs based" and "realism" aspects are to be resolved (see Chapter 5).

<sup>1</sup>For example, according to IMF (2004a) between 1992 and 2001, the average size of a negative commodity price shock (i.e., the decline in real price from the preceding year) was 22 percent for low-income countries and 16 percent for other developing countries. Such shocks also occurred with greater frequency in low-income countries. Low-income countries also suffer from more frequent and more costly natural disasters.

<sup>2</sup>This is illustrated by the fact that many discussions within the IMF on different aspects of program design call for a better specification of contingency plans as a means of dealing with uncertainty, but that such exhortation is rarely heeded in practice.

Most PRSPs also fell short of the requirement to articulate a comprehensive growth strategy and structural reform priorities. Either the policy agenda in some or all of the relevant areas lacked detail (Cambodia, Guinea, Nicaragua, and Tanzania), or it was insufficiently prioritized (e.g., Ethiopia and Mozambique), or both (Albania and Tajikistan). Only in Vietnam was the policy matrix found to be suitably detailed and prioritized, although even in this case some key issues (e.g., the pace and content of state enterprise reform and related program conditionality) resurfaced during program negotiations, reflecting disagreements between the authorities and IMF staff on the relative importance of key objectives.

Thus, none of the PRSPs for the 10 case studies would have met fully our suggested benchmark of providing a sound basis for design of a PRGF-sup-

ported program. See Box 2.5 for some possible reasons why. The survey of staff involved in PRSP/PRGF countries confirms these findings. Asked to assess various factors hindering the ability to align PRGF-supported programs on PRSPs, respondents almost universally responded that policies discussed in PRSPs are too imprecise to be an operational guide. Many also considered the lack of realism of macroeconomic frameworks as a key impediment to such alignment.

There is, however, some evidence of progress over time. A majority of PRSP-PRs indicate progress in the definition of the macroeconomic framework (especially in Albania, Mauritania, and Nicaragua). Progress in articulating an operational growth strategy and structural reform plans has been less frequent. Among the case study countries,

only Tanzania and, to some extent, Mozambique seem to have made substantive progress in that direction.

To conclude, the weaknesses identified in the first round of PRSPs were probably unavoidable given the learning process involved in their formulation. Moreover, although most still fall well short of expectation, there is a wide recognition that they are generally a significant improvement over previous BWI-fostered approaches (notably the PFP). The greatest changes in both processes and content so far have been with regard to various sectoral policies

(including health and education) and public expenditures. Changes in processes have been less in areas of macroeconomic policy formulation, and this is reflected in the contents of most PRSPs. “Good practice” cases—especially those where the PRS processes have begun to be embedded in domestic institutional arrangements—indicate continued progress, but in most cases the approach has not yet generated the sort of country-driven strategic frameworks in these policy areas that would help guide shorter-term decision making or provide an effective basis for the design of PRGF-supported programs.

## Joint Staff Assessments

### Key Messages

*On balance, Joint Staff Assessments (JSAs) do not perform adequately the many tasks expected of them.*

*JSAs generally cover most of the ground suggested by the guidelines, but the clarity, candor, and comprehensiveness of the assessment are uneven, with scope for improvement even in “good practice” cases. This partly reflects shortcomings in the guidelines themselves and a built-in bias to reach a positive conclusion given the “yes-no” character of the underlying judgment on suitability as a basis for concessional financing.*

*Their value added to the IMF as an internal governance tool is unclear, since decisions on access to IMF concessional financing, on the nature and scope of nonfinancial assistance, and on program design are made in separate contexts without being guided by the JSA.*

*JSAs of PRSP Progress Reports add little value to the Progress Reports themselves.*

*The JSA does provide useful feedback to countries about their PRS, but lack of awareness of the JSA among nongovernment stakeholders reduces its effectiveness.*

*JSAs have not contributed significantly to fostering coordination among development partners, reflecting in part shortcomings in coverage of issues, and in part the limited relevance of JSAs in the eyes of many donors, who would like a greater input into the assessments.*

An important part of the “architecture” of the PRS process is the JSA, by the staffs of both the IMF and the World Bank, which evaluates the strengths and weaknesses of a country’s PRSP and considers whether the PRSP provides a sound basis for concessional assistance from the BWIs and for HIPC debt relief. JSAs are submitted to the Executive Boards of the two institutions along with countries’ PRSPs and are always made public. In principle, they can serve three purposes:

- An internal governance function: providing the Boards with a basis on which to decide whether the country’s strategy deserves concessional support, which may include debt relief.

- A feedback and outreach function: informing the government and other domestic stakeholders of staff views on the strengths and weaknesses of the PRS.
- A partnership function: signaling to the donor community whether the BWIs view a particular PRS as worthy of support, what areas need strengthening, and so on.

The jointness of the assessment primarily reflected the perception that it was not sensible to dissociate the assessment of the macroeconomic components of the PRS from that of the developmental components, as they would succeed or fail together.



It was expected to improve Bank-Fund collaboration by ensuring that their staff reached a common perspective on the country.

Interestingly, when asked what *they* thought was the primary value added of the JSAs, IMF staff surveyed emphasized not the internal governance function, but the provision of feedback to the authorities and, to a lesser extent, of an independent expert assessment of the PRSP to interested parties.<sup>1</sup> Moreover, the increase in the amount of paperwork expected from IMF staff (Box 2.3) suggests that the JSA did not make any of the preexisting staff assessments redundant. In the remainder of this section, we discuss the contents of JSAs, assess how effective they have been in meeting their different purposes, and review possible factors underlying this performance.

## Contents of JSAs

The guidelines for JSAs of PRSPs indicate that the assessments should succinctly answer key questions about each of the four core elements of the PRSP (i.e., a description of the participatory process; poverty diagnosis; targets, indicators, and monitoring systems; and priority public actions), giving greatest weight to the priority public actions and to the arrangements for monitoring and evaluation of PRSP implementation, and paying due regard to the country's starting point. We assess how the JSAs handle the key questions asked by the guidelines in the areas relevant to the IMF's mandate.<sup>2</sup>

## Participatory process

While in general the guidelines call for JSAs to assess rather than describe or repeat the contents of PRSPs, in the case of participatory processes the guidelines note that "the Executive Boards have instructed the staffs to describe, but not evaluate, the participatory process." In practice, however, 22 JSAs out of 23 do assess the participatory process, and 16 of those identify the participatory process as one of the main strengths of the PRSP, while four mention it as one of the weaknesses.<sup>3</sup> In about half of the cases,

these assessments are not backed by an analysis of the participatory process and its impact on ownership. Several of the key questions asked by the guidelines in relation to the participatory process are frequently not addressed. Furthermore, based on our case studies, our overall judgment is that the JSAs tend to present participation in a more favorable light than warranted by circumstances (except in Cambodia, where the assessment is quite candid and in Tanzania, where the JSA refrained from assessing the participatory process). In particular, JSAs often overstate the extent and significance of civil society participation (e.g., in Mozambique, Nicaragua, and Tajikistan) and the degree to which the participatory exercises were country driven (e.g., Vietnam), while understating (and sometimes entirely overlooking) constraints to effective participation (e.g., in Guinea). A key reason why JSAs tend to present an insufficiently critical assessment of the participatory process is that (in keeping with the guidelines) they emphasize *who* was consulted and *how* without giving much information on *what* was discussed or whether the discussions were meaningful.

## Targets and monitoring

On average, JSAs provide a good description of PRSP targets and monitoring arrangements, along with some assessment of their adequacy. However, there are wide variations: the realism of targets and monitoring arrangements and the suitability of the indicators retained are generally assessed. By contrast, the transparency and participatory nature of monitoring arrangements are discussed in just over half of the cases, and the feedback of monitoring into policymaking is discussed only in a minority of cases. This pattern is common to both early and recent JSAs.

## Priority action plans

JSAs' treatment of priority actions plans was examined focusing on three areas that are particularly relevant to the IMF's mandate: the macroeconomic framework; key fiscal choices; and financing plans. In all three areas, JSAs offer a broadly satisfactory assessment, although with room for improvement.

- Almost all JSAs discuss the soundness and realism of macroeconomic frameworks. However, only half discuss their robustness to shocks, and only a minority of JSAs assess whether key trade-offs are discussed in the PRSP.

<sup>1</sup>Reflecting the ambivalent nature of the JSA, a relatively high percentage of respondents chose the "don't know" option when answering questions about its value added.

<sup>2</sup>This analysis is based on a desk review of JSAs issued through June 2003, with complements drawn from the case studies. The desk review involved using a standard assessment matrix to assess each JSA vis-à-vis the criteria outlined in the JSA guidelines. The coding scheme underlying this assessment and average ratings under each criterion are presented in Annex 6.

<sup>3</sup>We considered that JSAs assessed the participatory processes rather than just described them when a qualitative value judgment

was expressed and/or when the participatory process was listed among either the main strengths or the main weaknesses of the PRSP.

- With respect to key fiscal choices, the three dimensions highlighted by the guidelines—internal consistency; quality of costing estimates; and administrative capacity to deliver (including quality of PEM system)—are tackled in most cases.
- The assessment of financing plans is generally the weakest. A majority of JSAs discuss the realism of financing plans, but their sustainability is rarely addressed, nor is the existence of contingency plans.

The desk review results suggest that some learning over time has taken place with respect to the appraisal of macroeconomic frameworks, but not in the other areas.

### Other issues

Surprisingly, JSAs rarely discuss “gaps” in PRSPs, in the sense of critical policy issues that are not addressed. The analysis of key implementation risks is also limited. All JSAs identify at least a couple of such risks but most do not suggest remedial actions. Furthermore, the case studies (e.g., Guinea, Mauritania, and Mozambique) suggest that JSAs are sometimes insufficiently candid in their assessment of the seriousness of the risks to implementation, especially with respect to the implications of weak administrative capacity and of inadequate links between the PRS and normal government processes.

JSA guidelines require the staff to “take into consideration the country’s starting point.” Ideally, JSAs should give a sense of what initial conditions were in key areas and, based on that, of what could realistically be expected from the PRSP process, so that the PRSP would be assessed against *explicit* country-specific benchmarks. In practice, JSAs have generally not adopted such an approach. In about one-third of cases, there is a perfunctory discussion of starting conditions. In others, starting conditions are discussed adequately, but the implications for the PRSP are not clearly drawn out.

### JSAs of PRSP Progress Reports

According to the guidelines for JSAs of PRSP-PRs, these reports “must make an overall assessment for the Executive Boards as to whether progress in implementation has been satisfactory, and whether or not the strategy presented in a PRSP remains a sound basis for concessional assistance from the Fund and the Bank.” We assessed the JSAs of 12 PRSP-PRs issued through the first quarter of 2004.

Surprisingly, the key questions suggested by the guidelines for staff to consider in drawing their assessment are narrowly focused on the contents of

Progress Reports, rather than on actual progress in implementation. Reflecting the guidelines, JSAs focus on the PRSP-PR documents, and in many cases the latter are appraised exclusively on the basis of information reported by the authorities in the document itself.<sup>4</sup> A significant proportion of JSAs limit themselves to summarizing the Progress Report and assessing its strengths and weaknesses without attempting to remedy gaps in coverage (e.g., in assessing progress against the targets set in the PRSP itself), by bringing in information from other available sources, or making an independent assessment of progress. Only a small minority attempt to appraise progress in implementation of the strategy against the objectives of the initiative, such as broader ownership, better design of policies and priority setting, and the extent to which the PRSP is assuming a central role in the domestic policymaking process. Among the case studies, the JSAs for Tanzania and Ethiopia are examples of “good practices” in that regard.

## Value Added of the JSA

### Performance of the JSA as an internal governance tool

The usefulness of the JSA as an internal governance tool is limited by the fact that JSAs are constrained to reach a binary (yes/no) conclusion on whether the strategies presented in PRSPs constitute a sound basis for concessional lending by the BWIs, with the use of standardized language.<sup>5</sup> All JSAs to date have provided a “yes” signal and this conclusion has systematically been endorsed by the Boards—even when the PRSP did not in fact provide a satisfactory framework in which to anchor a PRGF-supported program. In these cases, the JSA

<sup>4</sup>Such exclusive reliance on the document produced by the authorities to assess progress in implementation is bound to give rise to candor issues (see, for instance, the somewhat rosy treatment of progress under the governance pillar in the JSA of Mozambique’s PRSP-PR).

<sup>5</sup>The use of a standardized conclusion was decided in the early days of the PRSP initiative, at a time when it was tightly linked to the implementation of the HIPC Initiative. In that context, the use of the standard sentence (“The staffs of the World Bank and the IMF consider that this PRSP presents a credible poverty reduction strategy and provides a sound basis for IDA and Fund concessional assistance”) was meant to avoid language that could have given the impression that the BWIs cleared or endorsed countries’ PRSPs, as this would have run counter to the new emphasis on country ownership. While the use of standardized language made sense in the context of the HIPC Initiative, where the amount and schedule of assistance are entirely determined on the basis of objective criteria, the same cannot be said of other BWI lending decisions. Nevertheless, the use of a standardized conclusion was confirmed in the guidelines for JSAs of PRSP Progress Reports.

typically noted serious weaknesses in the PRSP, along with encouragements to amend the PRS in a number of ways, but nevertheless reached a positive conclusion. Furthermore, what constitutes a sound basis for BWI concessional lending (or, more critically, what fails to constitute a sound basis) is not defined anywhere.

JAs have not contributed in any substantive way to the determination of the amounts of BWI assistance and detailed design of the programs.<sup>6</sup> All JAs identify a (varied) number of strengths and weaknesses in PRSPs, but not in a way that would allow the reader to get a sense of the overall strength of the PRSP, that is, by delivering a graduated assessment on the basis of explicit benchmarks. For example, our review of JAs shows that they listed more strengths than weaknesses for only 12 of the 23 PRSPs appraised up to end-2002. Sixteen PRSPs were considered “sound bases” even though they had among their main weaknesses at least two of the following—seemingly critical—dimensions: (i) costing, financing, and prioritization; (ii) public expenditure management; and (iii) implementation and monitoring. Five PRSPs were considered deficient in all three respects and yet the JAs concluded that they provided a suitable basis for concessional lending.

JAs typically do not discuss what the BWIs plan to do, both to support the country’s strategy and to help remedy any weaknesses (nor are they required to do so explicitly by the guidelines). In particular, they do not underline the implications of perceived weaknesses for the extent to which their own operations may be aligned on the PRSP, nor the priority actions that the BWIs themselves should take. The CAS is intended to fulfill this purpose in the World Bank. However, there is no clear equivalent in the IMF. As a result, the path from the JA to a PRGF arrangement is often not clear, and many key issues are left to be resolved in the context of PRGF-related negotiations.<sup>7</sup>

<sup>6</sup>The guidelines for JAs of PRSPs note that these elements are determined through the World Bank’s CAS and arrangements under the PRGF, but that “the JA contributes to these determinations through its assessment of the strengths and weaknesses of the strategy.” At the World Bank, the determination of lending levels continues to rely primarily on Country Policy and Institutional Assessment (CPIA) ratings (which do not incorporate information on status of the PRS process), while at the IMF access under PRGF arrangements takes into account, in a nontransparent manner, a variety of criteria (such as balance of payments need, strength of adjustment program, and track record with the IMF) that do not include PRS-related factors.

<sup>7</sup>This is in contrast with the process adopted in selected countries (including Mozambique and Tanzania) by donors who provide general budget support on the basis of a mutually agreed performance assessment framework (PAF) that builds heavily on the PRSP itself and forms the basis for annual Joint Partner Reviews (JPRs). For

### Box 3.1. Key Findings of the Review of JAs by the World Bank’s OED

As background to its evaluation of the PRSP process, the OED conducted a review of JAs, assessing how well each JA identified the strengths and weaknesses of a PRSP and signaled directions for improvements, using a four-point scale where “3” (out of “4”) indicates satisfactory treatment. This assessment was made for 11 issues, 7 of which are not listed as such in the JA guidelines but were deemed relevant based on the case studies and on the record of discussions of the World Bank’s Executive Board. The average overall rating given by OED to the 28 JAs reviewed was 2.7, with signs of tentative improvement over time in some respects. The topics most satisfactorily handled in a majority of JAs were endogenous and exogenous risks, structural and sectoral policies, and poverty diagnoses. The least well covered topics were capacity constraints, private sector participation in PRSP formulation, and donor partnerships issues.

The OED review also concurs with the IEO assessment of limited usefulness of the JA to local stakeholders and the overly optimistic or incomplete treatment of the value and contribution of the participatory process.

With regard to IMF–World Bank collaboration, the main value added of the JA reported by IMF staff was to foster the expression of a comprehensive, unified World Bank perspective in its areas of competence. Nevertheless, there is also a view among IMF staff that the need to reach a compromise with Bank staff on issues of shared interest is an important contributing factor to the lack of candor and clarity of the assessments conveyed in the JA. Some additional findings on the JA emerging from the OED review are summarized in Box 3.1.

As a result of these various limitations, the main value added of the JA from the perspective of internal governance seems to be of an informational nature, that is, by summarizing for Board members the main features of the PRSPs prepared by member countries. Even in this role, however, JAs face shortcomings because of their limited scope to focus on the dimensions of keenest interest to each BWI. For instance, the commentary on participatory processes found in JAs typically does not discuss whether macroeconomic policies and related issues at the core of IMF concerns were addressed, let

the IMF, there is no such straightforward mapping between PRGF conditionality, the PRSP policy matrix, and the JA.

### Box 3.2. Interactions with Local Stakeholders in the Preparation of JSAs

JSAs are meant to reflect the views of the staffs of the IMF and the World Bank and not those of a broader range of stakeholders (although the latter is not ruled out). Not surprisingly, only a small minority of JSAs (5 out of 23) make explicit references to lateral inputs, and these cases primarily reflect the views of the local donor community, although in two cases the views of civil society organizations on specific issues are also mentioned.

The case studies suggest that practice with respect to consultation with other stakeholders varies widely. For instance, in Cambodia, several key donors, including the AsDB and DFID, provided a joint review of a first draft of the JSA, and some comments were incorporated in the final version. Likewise, in Vietnam, a draft was circulated to donors and NGOs that were members of the Poverty Working Group and they commented on it (approvingly for the most part). On the other hand, the JSA for Tajikistan does not even allude to the existence of alternative views on the macroeconomic framework of the PRSP produced by an NGO umbrella group.<sup>1</sup> In Guinea, staff in charge of drafting the JSA had exchanges of views on the PRSP with local donors and selected representatives of civil society, but they did not consult them on the draft JSA itself. Our exchanges with these stakeholders indicated that they thought the JSA misrepresented ground realities and wished they had been given an opportunity to express that view prior to consideration by the Executive Boards.

<sup>1</sup>These views were provided as inputs into the PRSP formulation process rather than as ex post commentary on the PRSP. Nevertheless, they would have been a relevant reference had the staff sought to reflect the views of a broad range of local stakeholders in the JSA.

In most cases, the authorities were given an opportunity to react to a draft of the JSA. In some cases, this way of proceeding appears to have contributed to limiting the candor of the staff's assessment, either by introducing a bias favorable to the authorities as their comments—unlike those of any other stakeholders—were taken on board (e.g., in Guinea, on the participatory process) or by glossing over disagreements with a view to maintaining a good working relationship with the authorities (e.g., in Nicaragua).

This asymmetry is the source of considerable misgivings among both donors and NGOs, who feel that, at the very least, their views on the matters assessed by the staff should be brought to the attention of the Boards. Others go further by suggesting that, where donors provide most of their assistance in the form of direct budget support, and do so on the basis of a common PAF and a Joint Partner Review (JPR) of PRS implementation—as in Ethiopia, Mozambique, and Tanzania—the JSA and the JPR should be merged or at least closely aligned in timing.

The guidelines on JSAs of PRSP Progress Reports reflect a tentative evolution toward greater lateral consultations, as they explicitly suggest that staff seek inputs from local stakeholders when assessing progress in implementation of the PRS. A desk review of JSAs of PRSP-PRs suggests that this was done in just over half of cases, with some improvement over time.<sup>2</sup> However, in the three cases (mentioned above) where the joint donor assessment framework is most advanced, the JSAs make no reference to the JPRs, even though in all three cases such reports had been issued shortly before the finalization of the JSA.

<sup>2</sup>Among JSAs prepared in 2001 and 2002, only 2 out of 5 make references to local stakeholders' views, whereas among those prepared subsequently, the ratio is 7 out of 12.

alone report on the thrust of any debate that might have taken place.<sup>8</sup>

#### Performance of the JSA as a vehicle for feedback to countries

According to the guidelines, the JSA is expected to provide “constructive feedback to the country about how it might improve its strategy over time.” Performance in this dimension is mixed. As pointed out above, most JSAs make a relatively good diagnosis of the weaknesses of PRSPs and risks facing

<sup>8</sup>Interviews with IMF staff suggest that the drafting of the section of the JSA on the participatory process is typically led by the World Bank. This choice, however, should not prevent IMF staff from assessing the coverage of macroeconomic and related issues in the participatory process.

them, but they often fall short in suggesting implementable remedial actions. However, there is some evidence that the feedback has some impact since a comparison of weaknesses listed in the JSAs of I-PRSPs and PRSPs reveals that about half were addressed in the full PRSP.

There are other factors that reduce the effectiveness of JSAs. In particular, the fact that the guidelines effectively invite the staff to focus their assessment on the contents of PRSPs and by-products acts as an incentive for countries to concentrate their efforts in the production of a “good document,” at the expense of efforts to bring about durable improvements in underlying policy formulation and implementation processes.

Our case studies suggest that countries often face significant capacity limitations in responding to identified weaknesses in the PRSP. This problem



could perhaps be mitigated if the JSAs flagged clearly the areas where these constraints are particularly binding, so as to encourage the provision of technical support from development partners.

The JSA's larger role in providing "feedback to the country"—that is, not just the authorities, but rather all local stakeholders in the PRSP process—depends crucially upon availability of the JSA on the ground. All JSAs are in the public domain and are posted on the websites of the IMF and the World Bank when they are issued. No other staff report assessing member countries' policies has the same degree of automatic transparency, and this practice is welcomed by I-NGOs and donor representatives alike. However, beyond these constituencies, it is not clear that JSAs are de facto widely accessible. This is in part because the BWIs themselves typically do not make them available on their websites in languages other than English, and in part because active public dissemination on the ground largely rests on the authorities. Our case studies suggest that in most countries civil society stakeholders—along with a number of government representatives—are unaware of the JSA. When appraised of the thrust of the JSA, local stakeholders in several of the case studies (e.g., Ethiopia, Guinea, and Nicaragua) expressed the view that the JSA gave an overly favorable assessment, not in tune with ground realities. This view applied particularly to the treatment in the JSA of the participatory process, but it also reflects dissatisfaction with the JSA's focus on PRSP documents rather than on underlying realities.

### **Performance of the JSA in fostering partnership**

The JSA was also expected to provide a possible common reference around which the donor commu-

nity could coordinate its support to countries' poverty reduction strategies. Acceptance of the JSA in this role among donors generally remains limited. In several country case studies, donors questioned the candor of the JSAs and/or its relevance. More generally, many expressed the view that for the JSA to play a useful role in fostering a partnership approach, it would need to take on board donors' views explicitly rather than convey exclusively the perspective of the staffs of the BWIs. At present, JSAs typically only do the latter, although there are some exceptions (Box 3.2). While the internal governance function of the JSA requires that it primarily express the assessment of BWI staff, reporting on the views of other stakeholders, in particular donors, could only enhance the credibility and comprehensiveness of the assessment conveyed to the Boards.

The effectiveness of the JSA in fostering partnership is also adversely affected by some of the characteristics discussed earlier, in particular the absence of clear benchmarks and criteria on the basis of which to assess the PRS (i.e., both the contents of the PRSP and progress in its implementation). This effectively means the JSA is not, as presently implemented, an effective vehicle for providing inputs to the broader donor community on aid selectivity. Likewise, the absence of clear assessment in the JSA of the country's unmet needs (whether financial, analytical, or capacity-related) to implement its PRS and of any outline of the BWIs' intentions in terms of assistance strategy prevent the use of the JSA as an organizing framework for donors' support to the PRS.

Thus, in practice, even in countries where a number of donors have moved to budget support and make at least part of their lending decisions on the basis of a joint assessment, that assessment coexists with the JSA.

# PRGF-Supported Program Design

## Key Messages

*In most PRGFs, key strategic priorities and policy choices in both macroeconomic and structural areas in program design are still not guided by the PRSP. This largely reflects lack of specificity and other weaknesses in the latter.*

*The key features of the PRGF imply a much greater need than previous approaches for the IMF to draw upon other sources of expertise and integrate them in an effective and timely manner in program design. The actual record is mixed and the partnership framework of the PRS approach has not been used sufficiently to set and implement priorities in this regard.*

*Programs target smaller and more gradual fiscal adjustment than under the Enhanced Structural Adjustment Facility (ESAF) and give more weight to revenue increases than expenditure contraction. However, these changes are not always reflected in actual outcomes.*

*Program design does not exhibit generalized “aid pessimism,” that is, programs generally build in increases in net external financing, and targeted financing exceeds outcomes on average. However, there is still no effective operational approach to managing the tensions between “ambition” and “realism” in defining medium-term external resource envelopes, and what catalytic role the IMF is to play in practice remains vague.*

*Expenditures designated as poverty reducing have increased significantly under the PRGF, but the case studies suggest caution in concluding that all of it is truly “pro-poor.”*

*Programs exhibit a strong tendency to eliminate double-digit inflation, but there is no evidence of a systematic “disinflationary bias” when inflation is already low.*

*Country-specific analysis of how quickly the real economy responds to macroeconomic policy settings is limited. The IMF generally contributes little to inform or help the government inform the public debate on these issues, including by spelling out the assumptions underlying its program design.*

*PSIA is far from being “mainstreamed” in program design. Although some progress is evident, priority setting on what the BWIs themselves should be delivering in this area is lacking.*

*IMF structural conditionality has declined significantly under the PRGF and become more focused on core areas of expertise, but conceptual differences between Bank and Fund conditionality and a lack of systematic monitoring mean it is not possible to say what has happened to aggregate IMF–World Bank conditionality.*

*Evidence suggests only minor improvements in program implementation under the PRGF.*

**Box 4.1. Key Features of PRGF-Supported Programs<sup>1</sup>****1. Broad participation and greater ownership**

- The main elements of the PRGF are drawn from the country's PRSP.
- PRSPs will be produced by country authorities in a transparent process and with broad participation.
- Where relevant, JSAs/staff reports will highlight flexibility in accepting country choices.

**2. Embedding of the PRGF in the overall strategy for growth and poverty reduction**

- This feature demonstrates how macroeconomic and other policies have been influenced by growth and poverty objectives.
- Aspects of the PRGF program that promote private sector development will be highlighted.
- The PRGF contribution to the strategy should focus on areas within the IMF's area of expertise and responsibility.

**3. Budgets that are more pro-poor and pro-growth**

- Government spending should be reoriented toward activities that benefit the poor.
- Efficiency and targeting of spending in key sectors relevant to growth and poverty reduction should be improved.
- Tax reforms that simultaneously improve efficiency and equity should be stressed.
- Data and monitoring to track expenditures should be improved.

**4. Appropriate flexibility in fiscal targets**

- More normative macroeconomic projections to signal financing needs should be presented.

- Where warranted, commitments of higher aid flows should be sought and built into the program.
- The PRSP should be used to identify contingent expenditures that could be added if more aid were forthcoming.
- The program should indicate how fiscal targets would be modified in the event of key shocks.

**5. More selective structural conditionality**

- Structural conditionality should be limited to key measures, central to the success of the strategy.
- IMF conditionality should be confined to measures in the IMF's domain; exceptions must be justified.

**6. Emphasis on measures to improve public resource management/accountability**

- Fiscal policies and objectives should be open to public debate.
- Transparent monitoring systems to improve efficient delivery of public services should be developed.
- For HIPC, specific mechanisms for monitoring use of debt relief should be included.
- Selective conditionality on fiscal governance measures should be considered.

**7. Social impact analysis of major macroeconomic adjustments and structural reforms**

- The distributional effects of substantial macroeconomic adjustments or structural reforms should be considered.
- Countervailing measures to offset temporary adverse effects on the poor should be highlighted.
- The World Bank should take the lead if technical impact analysis is needed, but PRGF documents should indicate what work was done and how it influenced policies.

<sup>1</sup>Based on IMF (2000a); and Gupta and others (2002).

It is not possible at this stage to assess the effectiveness of PRGF-supported programs in achieving ultimate goals such as poverty reduction, since progress toward these objectives can only be measured over a longer time horizon.<sup>1</sup> However, we can

<sup>1</sup>Even when a longer time series is available, the methodological challenges associated with identifying the specific impact of programs on poverty, etc. will be considerable. See Easterly (2000) and Hajro and Joyce (2004) for different approaches to this issue for earlier adjustment lending programs.

evaluate progress against a number of intermediate objectives that are in turn expected to yield better growth and poverty outcomes. We organize the discussion broadly around six of the seven key features that PRGF-supported programs are expected to have (Box 4.1). (The first feature—greater ownership and broad participation—has already been addressed in Chapter 3.) We conclude with a discussion of some program design issues that have been the subject of frequent external commentary and an assessment of whether the new approach has improved program implementation.

## Alignment with the PRSP

PRGF-supported programs are supposed to be embedded in the overall strategy for growth and poverty reduction. The IMF has distinguished two aspects to this alignment: (i) temporal alignment (i.e., between the formulation cycles of the PRGF-supported program and the PRSP *and* between the PRSP and the national budget cycle); and (ii) policy alignment (i.e., of program content with the strategy and priorities of the PRSP). An obvious prerequisite is a well-articulated PRS so that the program has something to align with.

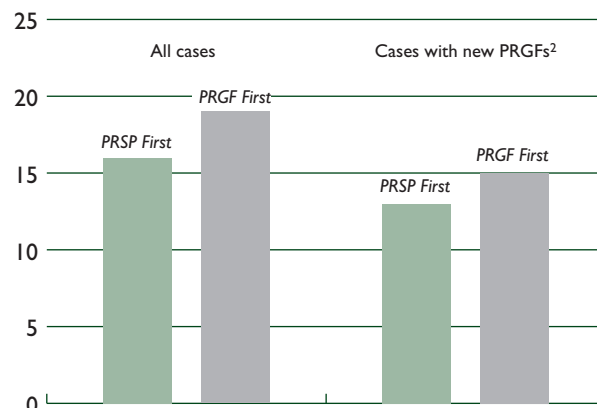
Thus far, most PRGFs do not meet the temporal alignment test because they preceded the PRSP (Figure 4.1). To a considerable extent, this is a transitional issue reflecting the “conversion” of previous ESAFs. But even in cases when new PRGFs were negotiated, slightly more than half were finalized *before* the PRSP. This does not necessarily mean the PRGF has not been informed by ongoing discussions on the broader strategy, but it does raise doubts about the claim that the program design is guided by the PRSP. In fact, the case studies suggest that the reverse influence is more common, with the PRSP drawing key elements of its macroeconomic framework from negotiations on a PRGF-supported program.<sup>2</sup>

To assess the extent of alignment for the major fiscal variables, we compared the macroeconomic forecasts in original PRSPs for the six IEO case study countries with those of the PRGF-supported program requests or reviews brought forward immediately prior to the adoption of the PRSP. Results varied from country to country, with no clear tendency in the extent or direction of alignment. Most PRSPs and subsequent PRGF-supported programs were presented within 6 months of each other, which should have facilitated alignment. Among the case studies, the exception was Nicaragua for which there was a 16-month gap between presentation of the Nicaragua PRSP and finalization of the PRGF-supported program (which likely explains the absence of alignment). The PRSPs for Tanzania and Vietnam were presented within a month of the subsequent PRGF review, but the macroeconomic forecasts differed noticeably. Mozambique presented mixed results, with the fiscal deficit forecast in the PRSP identical to that of the previous program review but the growth forecast significantly higher. In Guinea, the PRSP macroeconomic forecast was essentially extracted directly from the program request 8 months prior

<sup>2</sup>IEO/OED case studies where a “new” PRGF preceded a full PRSP are Ethiopia, Guinea, Tanzania, and Vietnam.

**Figure 4.1. Which Came First, the Chicken or the Egg? Sequencing of PRSPs and PRGF-Supported Programs<sup>1</sup>**

(Number of countries)



Source: IMF staff reports.

<sup>1</sup>Based on a sample of 35 countries with “full” PRSPs as of end-2003, comparing date of PRSP approval by country authorities with the start of new PRGF arrangements, if any.

<sup>2</sup>Excludes cases of PRGFs converted from ESAFs.

and was already out of date by the time of the PRSP. For Tajikistan, the program’s macroeconomic forecast was quite closely aligned to that of the PRSP prepared 5 months previously.

However, the more important question is not “are the numbers the same,” but whether the PRS drives key strategic trade-offs. This is hard to assess but qualitative evidence from the case studies suggests that, with the important exception of protection of priority expenditures, strategic macroeconomic priorities set out in the PRSP were not used to guide subsequent key policy trade-offs when the initial macroeconomic framework was thrown off track. As noted in Chapter 2, many PRSPs simply do not provide sufficient strategic direction to guide such trade-offs when the particular numerical targets of the PRSP are overtaken by events. However, Tanzania provides an interesting example where the framework of consultations established as part of the PER process did provide a guide for modifying the PRGF—even if the original PRSP document did not (Box 4.2).

The problems associated with determining an appropriate medium-term external resource envelope add to the difficulties of “aligning” the PRSP and PRGF. IMF staff is asked to assume a substantial role in the estimation of this envelope. Internal IMF guidance has advised staff to “present normative (often stable or increasing) projections of



### Box 4.2. Tanzania: Alignment, Fiscal Flexibility, and Program Design

Tanzania provides an interesting example of how an initial program design was modified to take account of increased aid availability. The initial macroeconomic framework underlying the 2000 PRGF-supported program heavily influenced that of the subsequent PRSP. The overall budget deficit (after grants) was targeted to remain at or under 1 percent of GDP during the three-year program. Although macroeconomic stability had been restored, the program continued to envisage negative net domestic financing of the fiscal position. There were signs early in the program's implementation that priority expenditures were being squeezed in order to maintain fiscal discipline. Donors and other stakeholders were concerned that the aims of the PRSP were not being met. Under the auspices of the public expenditure review (PER) system—an institutionalized system of consultations, including a macroeconomic subgroup whose membership includes government officials,

donors, and civil society—donors funded studies by an outside academic advisor that provided important inputs into the debate (see Bevan, 2000 and 2001).

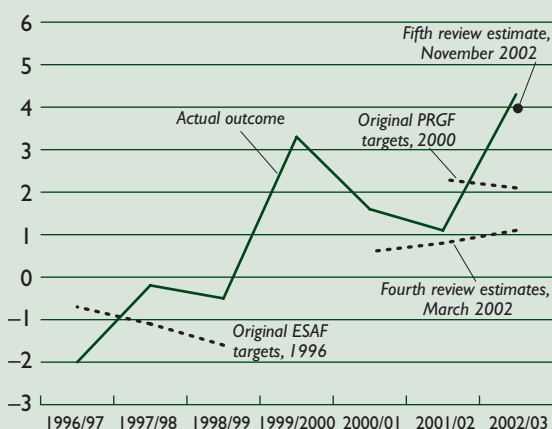
The debate centered around two issues. First, in light of higher concessional financing and a sharp accumulation of reserves, the medium-term expenditure framework required modification in order to accommodate these inflows. Second, the envisaged “crowding in of the private sector” via fiscal restraint that had characterized the initial program design had in practice overestimated the speed of response of private sector credit demand.

The IMF did show flexibility in adapting the financial program to the revised circumstances. The overall deficit (after grants) was allowed to increase almost threefold between 2000/01 and 2002/03 to 4.3 percent of GDP. Priority expenditures almost doubled as a share of GDP. The bulk of the expenditure expansion was financed by increased grants and concessional inflows, and the government ceased targeting negative net domestic financing.

Tanzania's experience suggests several important lessons. First, the consultation processes under the PRS did, over time, have a significant impact on the content of macroeconomic policies, and the PRGF-supported framework did show flexibility. In this sense, there was eventually an “alignment” with the key objectives of the PRS, although the process was not driven by preparation of the original PRSP document. Second, the process of interaction and debate that led to revisions in the framework involved some, but not all, stakeholders: government, donors, and the IFIs were involved, but civil society did not participate in any major way on this issue. This appears to have reflected in part their technical capacity constraints. But the example suggests that even this should not have been an insuperable obstacle, because one of the key inputs was provided by an outside academic advisor. This relative lack of civil society participation was unfortunate, since it has influenced civil society's perceptions of the process. Indeed, evidence from interviews and the stakeholder survey indicate a striking lack of recognition within civil society that the macroeconomic framework did adapt.

#### Overall Budget Deficit (After Grants): Targets and Outcomes<sup>1</sup>

(In percent of GDP)



Sources: IMF staff reports and WETA database.

<sup>1</sup>Positive number signifies deficit and negative number a surplus.

grants and concessional loans” and to “demonstrate efforts to seek higher aid commitments in cases where needed and appropriate.”<sup>3</sup> Staff is also expected to take account of the macroeconomic effects of additional external financing, including possible pressures for currency appreciation as well as absorptive capacity concerns. However, the op-

erational framework within which staff would help to formulate such projections remains unclear.<sup>4</sup>

<sup>3</sup>IMF (2000b).

<sup>4</sup>The problem is compounded by considerable uncertainty over the size and timing of aid flows. See, for example, Bulf and Hamman (2001) who conclude that (i) aid is more volatile than fiscal revenues—particularly in highly aid dependent countries; (ii) uncertainty about aid disbursements is large, being larger for program than project aid; and (iii) the information content of commitments made by donors is small—that is, official donor projections of aid are subject to large errors and exhibit a substantial upward bias.

### Box 4.3. Experiences with Setting the Medium-Term External Resource Envelope

A review of the country case studies reveals a range of experience but sheds little light on what might be a preferred operational approach to establishing medium-term external financing frameworks under the PRS.

In both Guinea and Vietnam, initial Fund projections for the external resource envelope turned out to be overly optimistic, albeit for very different reasons.<sup>1</sup> In Tajikistan—where the bulk of donor support was in the form of loans rather than grants—the PRGF-supported program projected a sharp fall in external financing due to a somewhat arbitrary limit imposed by staff on external borrowing. In Tanzania and Mozambique, staff initially incorporated an assumption of a decline in “aid dependence” into their forecast—partly because of the experience under ESAF when projections of external assistance proved too optimistic—but IMF staff eventually adapted to higher levels of aid.<sup>2</sup>

A few PRSPs (but none of the case study countries) have included more than one macroeconomic scenario. We reviewed the experience of Senegal and Madagascar. In Senegal, the PRSP described high, medium, and low case scenarios based on varying assumptions about the availability of external financing, the mobilization of domestic resources, and, most importantly, the capacity to absorb external resources. Medium and low case scenarios were apparently introduced at the request of the BWIs but, in keeping

with the desire to adopt a framework consistent with achieving the MDGs, the PRSP adopted the high scenario as its base case. Many donors considered this to be unrealistic, particularly given growth assumptions well above the historical average and the country’s capacity constraints to execute investment projects. Consequently, the PRGF-supported program was based on the medium case scenario. It is difficult to pronounce on whether the use of alternative scenarios added value to the PRSP process that warranted the additional effort on the part of the country. However, since the main problem appears to have been capacity constraints that impeded the full utilization of the resources made available, the higher (MDG scenario) does not seem to have played a significant catalytic role in practice.

Madagascar adopted two scenarios based on different growth assumptions. This was partly in response to the concern expressed in the JSA for the I-PRSP that growth assumptions were optimistic and that alternative scenarios would need to be developed. Neither scenario was identified as a base line. The first scenario was optimistic in the staff’s judgment, being based on what staff considered to be unrealistic assumptions of project implementation capacity; the second scenario—which was based on assumed failures to meet targets for mobilizing resources and for implementing the main reforms—was below staff’s assessment of what was likely over the medium term. As a result, the scenario that underpinned the PRGF-supported program takes a middle road between the two PRSP scenarios. Donors, for the most part, have taken a similar stance, awaiting evidence—perhaps in the context of the annual review of the PRSP—before moving in the direction of either of the two PRSP scenarios.

It is too early to draw definite conclusions from these limited examples whether the “alternative scenarios” approach can help catalyze additional aid flows.

<sup>1</sup>In Vietnam, because of low drawdown rates on aid commitments. In Guinea, because political considerations and doubts about the authorities’ track record led to a withdrawal of donor support.

<sup>2</sup>A number of external reviews by NGOs have criticized the Mozambique program for targeting declining aid levels in the face of massive MDG-related needs. In fact, aid was projected to be broadly unchanged in dollar terms over the medium term but declining as a share of rapidly growing GDP.

There is an obvious tension between ambition and realism. In 2003, the staff suggested a possible approach to resolving this tension, built around maintaining two macroeconomic frameworks within the PRSP (one based on more conservative estimates of aid flows and the other related to a more ambitious “business plan” to achieve desired poverty reduction goals).<sup>5</sup> At the time, many IMF Executive Directors felt that this approach would impose substantial additional costs on the countries concerned, for little practical gain. Most Directors preferred that the PRSP and PRGF be based on a common realistic macroeconomic framework, with policy responses

identified for both more favorable and downside risks. In practice, individual cases in which countries have chosen to present two alternative scenarios have been received quite favorably by the Board, but there remained considerable ambiguity about the operational approach that is supposed to guide the IMF staff’s role in this area (Box 4.3). In early 2004, IMF management endorsed an approach where staff would support country-led or donor-led initiatives to develop alternative frameworks aimed at showing what resources would be required for PRSP targets (including MDG-related goals) to be met, but it is too early to assess the impact of this decision.

Another aspect of alignment is whether the structural measures in PRGF-supported programs are derived from the PRSP. We have attempted such an

<sup>5</sup>IMF (2003c).

**Table 4.1. Alignment Between PRGF Structural Conditionality and the PRSP**

	Guinea		Mozambique		Nicaragua		Tajikistan		Tanzania		Vietnam		All Countries	
	Of which aligned	Average rating	Of which aligned	Average rating	Of which aligned	Average rating	Of which aligned	Average rating	Of which aligned	Average rating	Of which aligned	Average rating	Of which aligned	Average rating
Prior actions	4	1.3	7	1.1	3	2.0	5	2.2	0	...	6	5.0	25	1.8
Performance criteria	3	2.3	1	2.0	3	2.0	4	1.8	3	0	2	0	16	1.9
Structural benchmarks	3	1.7	3	2.3	9	2.3	5	1.4	5	4.0	9	4.4	34	2.0
Other	26	2.0	0	...	0	...	0	...	0	...	0	...	26	2.0
Total	36	1.8	11	1.8	15	2.1	14	1.8	8	2.5	17	4.1	101	1.9

Source: IMF staff reports.

<sup>1</sup>Percentage of conditions aligned with concrete policy action envisaged in PRSP (i.e., rating 3 in coding scheme).

Coding scheme for calculating average rating:

1 = No items in PRGF structural conditionality.

2 = Alignment of structural measure with broad objectives of the PRSP.

3 = Alignment of structural measure with concrete policy action envisaged in PRSP.

**Table 4.2. Targeted Fiscal Adjustment in ESAF- and PRGF-Supported Programs, 1995–2003<sup>1</sup>**  
(Averages, in percent of GDP)

	ESAFs				PRGFs			
	Level at T-1	Change from T-1 to			Level at T-1	Change from T-1 to		
		T	T+1	T+2		T	T+1	T+2
Fiscal balance, including grants	-4.1	0.7	1.4	2.0	-4.9	0.7	1.2	1.6
Fiscal balance, excluding grants	-8.2	0.9	2.2	3.0	-8.4	-0.2	0.6	1.5
Total revenues, excluding grants	17.8	0.5	0.9	1.3	18.5	0.4	0.9	1.6
Total expenditures and net lending	25.7	-0.3	-1.2	-1.6	26.9	0.5	0.2	-0.1
Grants	3.9	-0.2	-0.7	-1.0	3.6	0.8	0.7	0.1
Net external financing <sup>2</sup>	6.7	-0.6	-1.4	-1.9	6.4	0.7	0.8	-0.3
External current account balance (including official transfers)	-7.2	0.4	0.5	1.1	-7.3	-0.8	-1.7	-1.8

Source: MONA database and program documents.

<sup>1</sup>The maximum sample size of all arrangements is 88 (47 ESAFs and 41 PRGFs). However, because of missing observations, some of the averages are based on fewer observations than others.

<sup>2</sup>The sum of grants and net external borrowing in the government accounts.

assessment for the six IEO case studies (Table 4.1).<sup>6</sup> There is considerable cross-country variation but for the group as a whole, only one-fifth of structural measures listed in the program documents seem to be directly aligned with concrete policy actions described in the PRSP. A much higher proportion are associated with the broader objectives expressed in the PRSP, but such broad alignment is not difficult given the “broad tent” approach of most PRSPs. Program measures for Vietnam show the highest degree of alignment with the PRSP, while programs for Guinea and Mozambique have particularly weak alignment.

## Fiscal Flexibility and Fiscal Adjustment

An important feature of the PRGF is the recognition of the need for greater “fiscal flexibility,” which would include accommodation of higher aid flows and “pro-poor” public expenditures in support of PRSP goals while maintaining macroeconomic stability. Programs are also intended to allow greater flexibility in accommodating unexpected changes in revenue or financing, including aid flows. We look first at what happened to key program targets and then discuss fiscal outcomes.

<sup>6</sup>Alignment was assessed based on the first PRGF-related staff report that followed the completion of the PRSP. This exercise is subject to two important qualifications. First, some structural measures may be too detailed so as to be concretely aligned with the PRSP action plan (e.g., restructuring of one specific bank). Second, proposed conditionality may aim to deal with a problem (e.g., banking crisis) that occurred after completion of the PRSP.

## Fiscal targets in PRGF-supported programs: what has changed?

We analyze whether there have been significant changes in fiscal program design using data on a broad cross-section of PRGF- and earlier ESAF-supported programs. A comparison of key fiscal targets over a three-year horizon suggests the following (Table 4.2):

- *On average, PRGF-supported programs target a smaller and more gradual fiscal consolidation than under the ESAF.*<sup>7</sup> The magnitude of fiscal adjustment under PRGF is 1–1.5 percentage points of GDP smaller than under ESAFs.<sup>8</sup> Programs approved in 2002 and 2003 were more accommodating than those approved earlier (Table 4.3). This distinction is of importance when we discuss outcomes, because information is not yet available on whether the actual results for the later PRGFs match the more flexible targets.
- *The composition of envisaged fiscal adjustment is markedly different, with PRGF-supported programs relying on revenue increases for virtually all of the adjustment.* PRGF-supported programs, on average, target no expenditure cuts

<sup>7</sup>Based on adjustment in the fiscal balance excluding grants. Although grants are usually defined as part of *revenues* rather than as a component of *financing* of the fiscal deficit, it is sometimes useful to consider grants as another source of deficit financing. We have combined net external borrowing and grants into a single variable that can be used to test the “aid pessimism” hypothesis.

<sup>8</sup>The difference is statistically significant over a two-year horizon.

**Table 4.3. Targeted Fiscal Adjustment in PRGF-Supported Programs, 2000–03***(Averages, in percent of GDP)*

	Early PRGFs (2000 and 2001 Only)				Recent PRGFs (2002 and 2003 Only)			
	Level at T-1	Change from T-1 to			Level at T-1	Change from T-1 to		
		T	T+1	T+2		T	T+1	T+2
Fiscal balance, including grants	-5.4	0.9	1.7	2.2	-4.1	0.3	0.5	0.7
Fiscal balance, excluding grants	-9.1	0.0	1.1	2.4	-7.4	-0.5	-0.1	0.3
Total revenues, excluding grants	18.7	0.5	1.0	1.8	18.2	0.2	0.9	1.2
Total expenditures and net lending	27.8	0.5	-0.3	-0.8	25.6	0.6	1.0	0.9
Grants	3.7	0.8	0.7	-0.1	3.3	0.8	0.6	0.4
Net external financing <sup>1</sup>	6.6	0.9	0.8	-0.6	6.1	0.5	0.7	0.1
External current account balance (including official transfers)	-8.1	-0.5	-2.2	-2.3	-6.0	-1.2	-1.0	-1.0

Source: MONA database and program documents.

<sup>1</sup>The sum of grants and net external borrowing in the government accounts.

while their ESAF counterparts projected a significant reduction.<sup>9</sup> If we look only at the first two years of the targeted path, PRGF-supported programs provided for a small increase in expenditure. Once again, the adaptation in program design seems to have occurred over time: when we limited the sample to the “early” PRGFs, we found no statistically significant difference between ESAFs and PRGFs.

- *Projections of net external financing in PRGF-supported programs are substantially more optimistic than their ESAF counterparts.*<sup>10</sup> Under ESAF, average external financing as a share of GDP was projected to decline steadily over the three-year horizon. Under the PRGF, such financing was projected to increase over the first two years, with a small decline in the third year.
- *The difference between ESAFs and PRGFs is particularly pronounced with respect to grants.* PRGF-supported programs on average project a significant *increase* in the first year, falling off by the final year but remaining marginally positive, whereas a decline was projected each year, on average, under the ESAF.
- *PRGF-supported programs project a widening of the external current account deficit* (after official transfers) on average over a three-year horizon compared with a narrowing in the deficit under the ESAF.<sup>11</sup>

<sup>9</sup>The composition of programmed fiscal adjustment is discussed further in Annex 8.

<sup>10</sup>A frequency distribution of projected changes in external financing is presented in Annex 3.

<sup>11</sup>The difference is statistically significant at a 95 percent confidence level over two- and three-year horizons.

We used a regression framework to investigate potential determinants of targeted fiscal adjustment—for example, initial fiscal balance and targeted adjustment in the external current account—under ESAFs and PRGFs. The main results, which take account of the two-way relationship between targets for fiscal and external current account adjustment, are summarized below (more details are provided in Annex 7):<sup>12</sup>

- The initial fiscal balance was found to be a key determinant of targeted fiscal adjustment under both ESAFs and PRGFs and the nature of the relationship has not changed much (Figure 4.2).
- Under both ESAFs and PRGFs, projected increases in grants were translated almost fully into larger deficits (and vice versa).
- The targeted change in the external current account balance exerted a statistically significant influence on fiscal adjustment under ESAFs but not under PRGFs. In other words, under the PRGF, private sector investment-savings balances bore a greater share of the burden (or gain) from any change in the external current account.
- Projected growth was *not* found to exert a statistically significant influence on targeted fiscal adjustment in either ESAFs or PRGFs.

<sup>12</sup>We employed two-stage least squares to estimate targeted fiscal adjustment, with the first stage involving an estimation of the targeted change in the external current account. The regressions were estimated over the first two years of programs (rather than over a three-year horizon) in order to facilitate comparisons with outturns in the section “Evidence on program outcomes.”

### Evidence on program outcomes

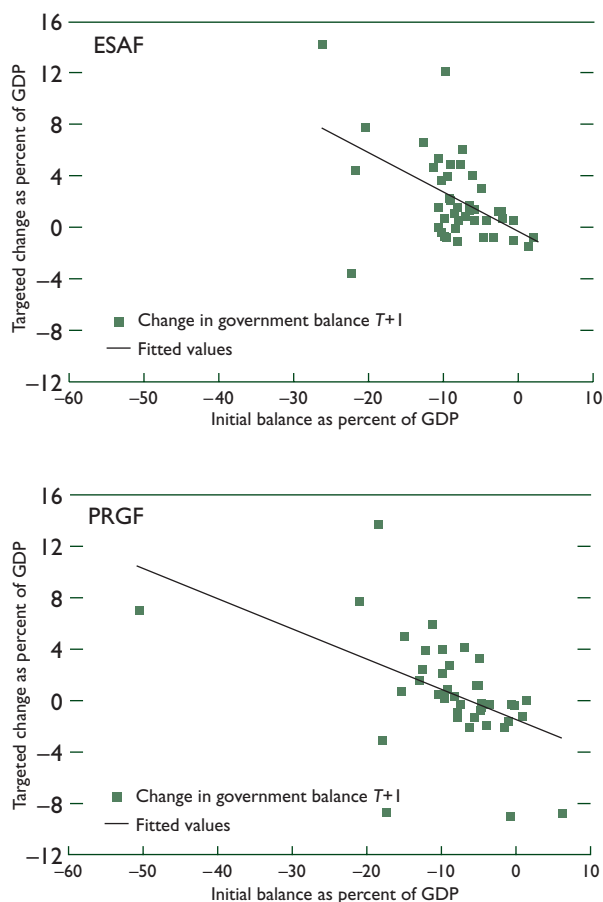
In sharp contrast to the findings regarding targeted fiscal adjustment, we found that on average, program outcomes under PRGFs recorded greater fiscal adjustment than those supported under ESAFs (Table 4.4). This is surprising, but limitations on outturn data—they are only available through 2002—meant that we relied on a truncated sample for the PRGF period. Thus, we may be picking up results that are valid for the early PRGFs which may change when outcomes data are available for those later programs where a more marked shift in fiscal targets occurred. Comparisons between outturns (see Table 4.4) and targets (see Tables 4.2 and 4.3) over the initial two-year horizon of programs suggested the following main points:

- Under the “early PRGFs,” the actual fiscal deficit declined on average by about 1½ percent of GDP—more than was targeted. Expenditures fell slightly, in line with projections, while revenues were slightly higher than projected.
- Actual outturns for net external financing were quite similar under the ESAF and the early PRGFs (i.e., a slight increase, on average), whereas programs under the ESAF had projected a decline and those under the PRGF had targeted a marked increase.

To summarize, program design under the PRGF did incorporate greater fiscal flexibility in the sense of targeting smaller and more gradual fiscal adjustment than under the ESAF, building in a projected increase in net external financing, and with a shift in the composition of targeted fiscal adjustment toward higher revenues rather than expenditure reduction. Most of this change appears to have occurred in “later” PRGF-supported programs (i.e., from 2002 onward), with much less change in “early” programs. However, information on program outcomes is only available for the “early” group—which shows much less change from outcomes under the ESAF. The evidence also suggests that, on average, program design allowed for larger external financing flows than actually occurred. This suggests that PRGF program design did not suffer from a systematic “aid pessimism” bias.<sup>13</sup>

<sup>13</sup>Clearly, such an analysis cannot address the broader issue raised by some external critics, of whether a more proactive “catalytic” role by the IMF could have mobilized additional financing.

**Figure 4.2. Relationship Between Initial Fiscal Balance at T-1 and the Targeted Fiscal Adjustment over a Two-Year Period (T-1 to T+1)**



Sources: IMF staff reports and IEO analysis.

### Strengthening Public Expenditure Management

Improvements in PEM, particularly measures that strengthen good governance by promoting transparency and accountability in the use of public resources, is another key feature of the PRGF. On average, PRGF-supported programs have included approximately one-third more measures (i.e., formal conditionality, triggers for HIPC assistance, and expressions of intent on the part of the authorities) to strengthen PEM systems than under ESAF-supported programs.<sup>14</sup> This is borne out in our country

<sup>14</sup>See Gupta and others (2002) and IMF (2002a).



**Table 4.4. Actual Fiscal Adjustment Under ESAF- and PRGF-Supported Programs, 1995–2003***(Averages, in percent of GDP)*

	ESAFs (N = 47)			PRGFs (N = 24) <sup>1</sup>		
	Level at T-1	Change from T-1 to		Level at T-1	Change from T-1 to	
		T	T+1		T	T+1
Fiscal balance, including grants	-3.5	0.3	-0.3	-5.1	1.2	1.9
Fiscal balance, excluding grants	-7.6	0.5	-0.1	-8.2	1.2	1.4
Total revenues, excluding grants	17.3	0.2	0.1	17.6	0.6	1.2
Total expenditures and net lending	24.9	-0.3	0.2	25.8	-0.6	-0.3
Grants	4.1	-0.2	-0.2	3.2	0.0	0.4
Net external financing <sup>2</sup>	7.1	1.1	0.3	6.9	1.3	0.1

Source: IMF staff reports.

<sup>1</sup>Excludes arrangements approved in 2002 and 2003, to allow coverage through horizon T+1. Outturn data are only available through 2002.<sup>2</sup>The sum of grants and net external borrowing in the government accounts.

case studies, almost all of which contain some formal conditionality in PRGF-supported programs intended to strengthen PEM. In this area, PRGF-supported programs are only one part of a broader array of initiatives through which the IMF supports improvements in PEM, and we also discuss these broader efforts, including diagnostic work and technical assistance.

Greater emphasis on PEM in low-income countries originated in implementation of the enhanced HIPC Initiative and the desire to ensure that the resources freed up from debt service would be used efficiently in support of spending in priority social sectors. In order to evaluate PEM capacity, the IMF and World Bank staff developed, in conjunction with country authorities, a system of 15 benchmarks intended to capture those aspects of PEM related to tracking poverty-reducing expenditures (Box 4.4). A key finding was the strong need to upgrade PEM systems in most countries. Of the 25 countries evaluated, 9 required “some upgrading” to be able to track poverty-reducing spending satisfactorily, and the remaining 15 required “substantial upgrading” (Figure 4.3).

The IMF is providing substantial technical assistance (TA) to strengthen PEM (Box 4.5). Based on recent internal assessments, there is scope to improve the effectiveness and sustainability of much of this TA by improving coordination with other providers, tailoring the TA to the more immediate and direct PEM needs of member countries, placing greater emphasis on follow-up to TA, and focusing TA resources where ownership is strongest.

In addition, a review we undertook of the IMF’s activities to help countries subscribe to standards for statistics dissemination and fiscal transparency assessments suggests that countries with PRSPs and PRGF arrangements were much more likely to have

undertaken such efforts than were other low-income countries.<sup>15</sup>

### Pro-Poor and Pro-Growth Budgets

The definition of a “pro-poor and pro-growth budget” continues to be subject to much debate and is closely related to the broader debate about the link between macroeconomic policies and growth/poverty outcomes. Even if one had a solid understanding of the links between policies and growth/poverty outcomes in a particular country (which is clearly not the case), terms such as “pro-poor” and “pro-growth” mask many difficult trade-offs that are frequently not acknowledged. The most obvious are (i) trade-offs over time (e.g., between immediate poverty reduction or greater poverty reduction in the future, if some “non-pro-poor” expenditures have high rates of return); (ii) trade-offs across groups (e.g., when policies help some groups move out of poverty but may adversely affect other poor groups); and (iii) trade-offs between social protection narrowly defined (i.e., preventing particular groups from falling into poverty because of policy measures or adverse shocks) versus the goal of moving as large a (net) share of the population out of poverty. How a particular country answers these questions depends on its own social choices, but they could yield markedly different fiscal (and other) policy choices, each of which could be legitimately characterized as pro-poor and pro-growth. These issues go beyond the scope of the current evaluation

<sup>15</sup>Specifically, the General Data Dissemination Standard (GDDS) and Fiscal Transparency Reports on Standards and Codes (ROSCs).

#### Box 4.4. IMF–World Bank Benchmarking Exercise on Public Expenditure Management

Preliminary assessments of 25 HIPCs' public expenditure management (PEM) systems and their ability to track poverty-reducing expenditures were undertaken by Bank and Fund staff in 2001.<sup>1</sup> The hope was that—by identifying weaknesses in PEM—it would be possible to prioritize needs in upgrading the capacity to formulate, execute, and audit/report on the budget.

Fifteen indicators were eventually selected to represent the basic standards necessary for PEM systems to effectively track poverty-reducing expenditures. Based on each indicator, specific benchmarks were adopted and grouped into three categories—budget formulation, budget execution, and budget reporting. At the time of the 2001 assessment, countries had met, on average, between seven and eight benchmarks.

On the basis of these assessments, action plans to improve PEM were prepared. Progress in implementing these action plans was reviewed by Bank and Fund staff in March 2003.<sup>2</sup> Based on the number of mea-

asures that had been fully implemented, and assuming no slippage in other areas, staff concluded that, on average, the countries had met one additional benchmark. However, across the full sample, only one-fifth of planned measures in the action plans had been fully implemented while a similar share had not been started. Also disappointing was the lack of progress in improving the coverage and reliability of the budget. At the same time, HIPCs had been particularly active in putting in place short-term bridging mechanisms mainly involving “tagging” poverty-reducing expenditures identified in the PRSPs to facilitate their immediate tracking while comprehensive PEM systems were put in place.

Bank and Fund staff is currently undertaking a more comprehensive review of country PEM capacity using the same benchmarks but the focus remains on the HIPC countries. According to staff, the significant human resource costs of the benchmarking exercise (estimated at an average of 0.5 staff years for each country) have prevented the extension of the exercise to other PRGF-eligible countries.

<sup>1</sup>IMF (2002a).

<sup>2</sup>IMF (2003a).

but they reinforce how complex and closely tied to specific social choices are judgments on the degree to which particular policy measures are pro-poor. Therefore, a country-driven, rather than a donor-driven, approach to these choices is especially important. We focus here on the subcomponents of the feature set out in Box 4.1.<sup>16</sup>

#### “Pro-poor” spending in PRGF-supported programs

Efforts have been made since the introduction of the PRGF/PRSP to derive a broad measure of poverty-reducing expenditure (PRE) to include relevant expenditures on health, education, rural infrastructure, water, sanitation, social assistance, and other spending deemed to be “pro-poor.” The determination of what constitutes PRE is country specific (albeit with common elements) and is contained in the country's PRSP. As a result, PRE estimates reflect a range of definitions across countries, the degree of transparency for which varies considerably. In a number of countries (e.g., Guinea and Nicaragua), there has been a tendency to include virtually all social sector investment—including many programs that were not especially targeted to the poor. Some stakeholders interviewed during the evaluation suggested that in-

centives created by HIPC conditionality have contributed to an overly broad classification of pro-poor spending.<sup>17,18</sup>

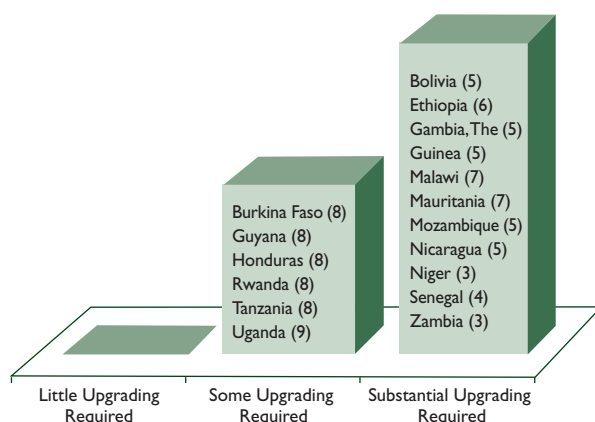
With these caveats in mind, *available data show that actual expenditure designated as poverty reducing has increased significantly between 1999 and 2002 and some modest further increases are tar-*

<sup>17</sup>The whole notion of identifying “priority” sectors that will benefit when additional resources become available or will be protected from cuts when shocks occur is a “second best” response to inadequate budgetary expenditure allocation mechanisms. It implies that an extra dollar spent in these areas yields a greater benefit than a dollar spent elsewhere, which raises the question as to why expenditures have not already been reallocated to eliminate the difference. Given political economy constraints on the budget process that can hamper desirable reallocations, such an approach may well be the most practical response. But, as Bevan (2001) and Bird (2004) have noted, the approach raises some uncomfortable questions, especially if maintained for long periods: does it reflect a pragmatic response to constraints on the speed with which governments can make desirable changes identified as part of domestic political processes or does it reflect an imposition of donor priorities that conflict with the idea of stronger domestic ownership?

<sup>18</sup>No IMF data base on *budgeted* PRE or its components has been maintained. For the 23 countries in our study, only staff reports for 7 countries (Albania, Bolivia, The Gambia, Guyana, the Kyrgyz Republic, Malawi, and Mozambique) contained separate and consistent projections of health and education as a share of GDP (3 others present figures for combined health and education spending). For this small sample average budgeted spending on health and education as a share of GDP is higher in PRGF-supported programs than in their ESAF counterparts by 0.6 and 0.8 percentage points, respectively.

<sup>16</sup>Aspects concerning improvements in the efficiency and targeting of expenditures within sectors are primarily the responsibility of the World Bank and will not be addressed here.

**Figure 4.3. Assessment Results on Adequacy of Public Expenditure Management, 2001<sup>1</sup>**



Source: IMF (2002a).

<sup>1</sup>Numbers in parentheses indicate total number of benchmarks (out of 15) met by country. Figure shows only those countries with full PRSPs as of December 2002.

ged through 2005 (Table 4.5 and Figure 4.4). Actual PRE expenditure rose by an average of 2.5 percentage points of GDP, with a further increase averaging about 1 percent of GDP targeted through 2005. It is not possible to say how much of this improvement can be attributed to the PRSP—or the HIPC Initiative. Indeed, there is some evidence that the trend toward higher expenditures in such areas began in the second half of the 1990s.<sup>19</sup>

### Efficiency and equity in tax reform

According to the IMF staff's assessment of PRGF program design, approximately two-thirds of tax measures under these programs dealt with improvements to tax administration.<sup>20</sup> Our case studies also show that conditionality (and IMF TA) has emphasized improved tax administration, an emphasis that seems appropriate given weaknesses in tax administration in many low-income countries. These weaknesses limit the authorities' ability to generate the revenue necessary to finance PRE and to use the tax system as a mechanism for promoting equity.

Changes in tax policy explicitly motivated by "equity" considerations have been less in evidence

in PRGF-supported programs. Most common have been reforms aimed at improving "horizontal" equity (e.g., to ensure equal treatment between domestic and foreign enterprises operating in a country or to remove distorting tax exemptions put in place to benefit politically well-connected individuals or enterprises). "Vertical" equity considerations are even rarer, a fact acknowledged by staff in their 2002 assessment. This was attributed to "the limited scope to implement progressive income taxes in low-income countries given administrative constraints and the high share of agriculture and the informal sector in economic activity."<sup>21</sup> Perhaps as a result, most tax policy measures have focused on consumption and trade taxes. That said, PRGF conditionality has rarely sought removal of a tax exemption explicitly on the basis of its regressive nature.

There does not appear to have been a systematic effort to assess the distributional impact of proposed tax changes in individual countries, although there are some "good practice" examples. A detailed PSIA on the VAT in Ethiopia undertaken recently concluded that replacement of the sales tax with a VAT would have had a small adverse impact on the poorest 40 percent of the population, which would be more than offset by the beneficial effects on the poorest groups if the reform financed higher health and education spending.<sup>22</sup> In Mozambique, a decision to increase fuel taxes was delayed until a poverty and social impact analysis was undertaken, the results of which were taken into consideration in the government's decision to increase petroleum prices in 2003. In Vietnam, Fund staff indicated, in early 2003, their intention to undertake PSIA on the effects of possible tax changes (although no work had begun as of early 2004).

Our case studies also revealed opportunities to promote greater vertical equity that were not actively pursued in PRGF-supported programs. In Guinea, for example, widespread tax exemptions were contributing to a very low revenue yield (and a consequent shortage of resources for PRE). However, while the PRSP expressed the authorities' intention to "sharply reduce exemptions," the PRGF-supported program stopped short of using conditionality to promote the removal of costly tax exemptions that were not intended to assist the poor.<sup>23</sup>

<sup>21</sup>See Gupta and others (2002, p. 18).

<sup>22</sup>See Munoz and Cho (2003).

<sup>23</sup>Indeed, the initiative to streamline conditionality would call for such an approach, if the exemptions were not judged to be "macro-critical."

<sup>19</sup>See, for example, OED (2003).

<sup>20</sup>Gupta and others (2002). See also Chu, Davoodi, and Gupta (2000).

### Box 4.5. IMF Technical Assistance Support for Strengthening Public Expenditure Management

Since FY1999, the number of person days devoted each year to PEM technical assistance (TA) in our sample of 23 countries has increased by two-thirds, almost 90 percent of which went to the HIPC. However, concerns have been expressed about the *efficacy* of that TA. IMF staff (in the context of recent evaluations of technical assistance on PEM reform to Anglophone and to Francophone African countries)<sup>1</sup> identified a number of shortcomings, including with respect to TA design and coordination among providers:

- No low-income African country (except Tanzania and Uganda) has a financial accounting system adequate to provide information necessary for policymaking.
- While the quality and relevance of TA provided by the Fund (and others) was recognized by stakeholders, weak ownership of PEM measures was a serious problem for implementation of TA recommendations. This is a serious concern, since the

central thrust of the PRS approach is to strengthen ownership.

- There is a need for better coordination of PEM TA, particularly with bilateral providers. Coordination between the Bank and the Fund was somewhat better with IMF TA often being used to fill a “temporary gap,” while the Bank worked on larger, more complicated and longer-term reforms.
- In Francophone Africa, PEM measures proposed by IMF TA may have been too general with insufficient attention paid to implementation constraints and the need to pitch recommendations at an accessible level.
- One of the major sources of weakness in PEM systems in Anglophone Africa was the tendency of governments (with the encouragement of the donor community) to burden themselves with functions and tasks beyond their capacity to execute.
- There had been little follow-up to Fund TA for PEM, particularly in Anglophone Africa. This was attributed in part to insufficient TA resources within the Fund.

<sup>1</sup>Diamond and others (2003a and 2003b).

**Table 4.5. Changes in Poverty-Reducing Expenditures, 1999–2002, and Projected Changes, 2002–05<sup>1</sup>**

(Means in percent of GDP)

	2002 Level	Change	Projected Change
		1999–2002	2002–05
“Early” PRSP cases (i.e., 2002 or earlier)	10.7	2.9	1.0
“Late” PRSP cases (i.e., 2003)	9.0	2.2	1.2
African PRSP countries	9.2	3.0	1.0
Average	9.7	2.5	1.1

Source: IMF staff estimates.

<sup>1</sup>Sample comprises 19 countries, of which 13 are in Africa, 8 are countries with “early” PRSPs, and 11 with later (i.e., 2003) PRSPs.

## Poverty and Social Impact Analysis

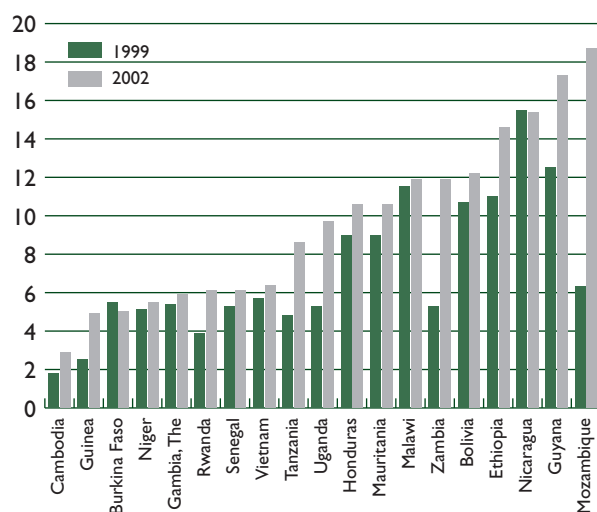
Our review confirmed the findings of other studies—that efforts to conduct PSIA have been slow to start and the integration of these results into program design even slower. Staff papers for 5 of the 23 countries reviewed (all outside Africa) made virtually no reference to PSIA. Most others simply made reference to the need to undertake PSIA for at least one major reform area. Only a few present more than

cursory results (Guyana, Mozambique, Vietnam, and Zambia) and even here, much of the analysis was very general.

The six IEO case studies revealed a considerable range of experience, with PSIA of varying quality undertaken at varying stages in the policy design process.

- In *Guinea*, a joint IMF–World Bank mission in 2001 discussed with representatives of trade unions, NGOs, the business community, and

**Figure 4.4. Poverty-Reducing Expenditures**  
(In percent of GDP)



Source: IMF staff reports.

parliament the likely social impact of the anti-inflation stance of monetary policy, the introduction of flexible petroleum prices, and restructuring and privatization of state-owned enterprises (SOEs) and in the financial sector. However, owing partly to the lack of data, there was no supporting analysis and it did not have a discernible impact on program design.

- In *Mozambique*, PSIA was undertaken in 2002 (partly funded by DFID) on the impact of raising taxes on petroleum products. It found that the impact on poverty would be modest and, if the proceeds went toward PRE, more people would be lifted out of poverty than would be hurt by the tax. Other studies undertaken included a Food and Agriculture Organization study in 2000 on protection of the sugar industry and a World Bank–sponsored study on restructuring the cashew industry. While Bank and Fund staff reportedly did not agree with the results of the study or the FAO’s call to protect the sugar sector, neither institution sought to block the government from following the FAO recommendations. PSIA on the cashew industry formed the basis of a government policy to provide a transfer payment to various companies to pay for accumulated liabilities to the labor force. The authorities have agreed with the World Bank on future PSIA needs but not yet on a timetable for undertaking the work.

- In *Nicaragua*, while the PRGF-supported program was approved in December 2002, preparation of PSIA to inform policy design was delayed, partly because of the time taken by the authorities to identify policies they considered to be of priority for such analysis. Recent developments, including the completion of PSIA on the tax reform and the Education for All Initiative and the undertaking of PSIA on the Public Investment Program and Decentralization indicate that some of the initial obstacles have been overcome.

- For *Tajikistan*, no PSIA was undertaken on key reforms in the PRGF-supported program despite the recognition by IMF staff that measures aimed at eliminating quasi-fiscal deficits in the energy sector would have severe adverse effects on the well-being of a large part of the population. The World Bank was to have undertaken PSIA on energy sector reforms in 2002 and 2003 but work was delayed ostensibly due to a lack of financial resources and other demands on staff.

- As of end-2003, little PSIA had been undertaken for *Tanzania* despite the identification by Fund staff of a need related to increased electricity tariffs, retrenchment in the parastatal sector, civil service reform, and the VAT. The authorities have expressed doubt about their own ability to undertake PSIA, partly due to a lack of analytical capacity and partly due to financial constraints. Until early 2004, a lack of budgeted resources and/or available staff was reported as preventing the Bank and Fund from undertaking PSIA. In practice, therefore, PSIA has not been a priority.

- PSIA on the impact of SOE reform on displaced workers was undertaken in 2000 for *Vietnam* with support from the World Bank and prior to agreement on a PRGF-supported program. The costs of mitigating measures were integrated into the fiscal framework in the PRGF-supported program. In the spring of 2003, Bank and Fund staff reached agreement on an agenda for PSIA priorities, including on possible future tax reforms. However, clear deadlines for completion of this work have not yet been set.

The overall message that emerges from this brief review is that PSIA is only gradually becoming an input to program design. These efforts are not yet systematic in the sense that PSIA needs are being derived from country priorities within a results-based framework indicating who should address them and by when. Furthermore, many key reforms are still falling through the gaps.



### Obstacles to “mainstreaming” PSIA in PRGF-supported programs

The slow pace of implementation of PSIA is noteworthy since calls for IMF staff to integrate such analysis into program design started well before the launch of the PRSP/PRGF initiative. As early as 1991, the IMF’s Managing Director had instructed staff to address the concerns of the poor “as a matter of course...[which] should be an integral part of designing Fund-supported and Fund-monitored programs.”<sup>24</sup> Similar guidance was given in 1998 by the Executive Board in the context of its response to the External Evaluation of the ESAF. The fact that progress has been so slow suggests the existence of serious obstacles.

The obstacles most often cited in internal reviews were data limitations and national capacity constraints.<sup>25</sup> Both are undoubtedly important, but they should not be overstated. A paper prepared in the IMF’s African Department concluded that “it is possible to assess some of the potential poverty effects even in countries with limited data and therefore contribute to a more informed policy debate and design.”<sup>26</sup> This echoed a similar conclusion reached in 2001 in the context of joint work undertaken by the World Bank and IMF for 12 PRSP countries.<sup>27</sup> In August 2003, internal staff guidelines were circulated identifying types of policies that were (or were not) conducive to PSIA by the IMF. Among those policies considered conducive to PSIA and part of the IMF’s area of core competence were tax policies (e.g., introduction of VATs and changes in tax rates), customs tariff policies, and exchange rate policy (including devaluation).

Another important set of explanations revolves around the fact that, although PSIA was recognized as a central element of the new approach, the arrangements for setting and delivering on priorities for such analysis within a broader partnership framework were not well specified. The result was (i) a lack of resources allocated to this purpose in the BWIs, and (ii) coordination problems with the World Bank. Our survey of IMF staff indicated that a lack of funding and/or staff resources at the BWIs was a major reason for lack of progress in integrating PSIA into program design. Guidance given to IMF staff makes clear they are expected to draw on the work of the World Bank and other development partners.<sup>28</sup>

However, our case studies illustrate that this is often easier said than done. The implicit assumption that the World Bank will act as the “agent” for the IMF in implementing or coordinating PSIA in areas of importance to the Fund can pose problems. If the Bank is not actively engaged in lending associated with a particular area, it has little incentive to devote its own scarce resources to analyzing the issue. The Bank’s timetable may also not fit with that of IMF program design. The solution to these resource and coordination problems seems to lie in a clearer identification of priorities for PSIA—driven by the countries’ own priorities for such analysis arising from the PRS process—along with an explicit identification of responsibilities for who does what and by when (see Box 4.6 for some useful lessons on timing).<sup>29</sup>

### Is Structural Conditionality More Selective?

As part of the streamlining initiative, PRGF-supported programs are expected to focus structural conditionality on the IMF’s core areas of expertise.<sup>30</sup> The only exception would be where a structural measure outside these core areas was deemed critical to the success of the program. This initiative has been complemented by ongoing efforts to improve coordination with the World Bank, including designation of a “lead agency” responsible for the design and monitoring of conditionality in a particular policy area. We examine here what has happened in practice.

#### Structural conditionality in PRGF-supported programs

There is clear evidence of progress in streamlining structural conditionality under the PRGF (in

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or structural reforms have been considered (*generally based on analysis by World Bank*)” (italics added).

<sup>29</sup>Adam and Bevan (2001) argued that “the current separation [of responsibilities in the preparation of PSIA] seems excessive. There is, after all, a substantial tradition of tax and expenditure incidence whose conceptual roots lie in the type of fiscal arena within which the Fund has substantial expertise.” A small unit was recently established in the Fiscal Affairs Department (FAD) with responsibility to coordinate (and, in some areas, produce) PSIA. However, there are divergent views on this issue within the IMF’s Board, with some arguing that budget constraints and considerations of comparative advantage argue for such activities to be concentrated in the World Bank, with greater efforts to ensure effective collaboration.

<sup>30</sup>Efforts to streamline IMF structural conditionality have been under way since the fall of 2000 and cover all programs, not just those under the PRGF. The final results of these efforts were revised guidelines on conditionality. They are available at [www.imf.org/External/np/pdr/cond/2002/eng/guid/092302.pdf](http://www.imf.org/External/np/pdr/cond/2002/eng/guid/092302.pdf).

<sup>24</sup>See IMF (2001b).

<sup>25</sup>Gupta and others (2002), and World Bank and IMF (2003c).

<sup>26</sup>Robb (2003).

<sup>27</sup><http://www.imf.org/external/np/prsp/2001/091401.htm>.

<sup>28</sup>IMF (2002c). Also, an internal checklist for staff with respect to the key features of the PRGF calls on Fund staff to “demonstrate that distributional effects of substantial macro-adjustments



**Box 4.6. PSIA in “Real Policy Time”**

Among bilateral donors, DFID has been particularly active in supporting the generation of PSIA in PRGF-supported countries. In 2002, and in collaboration with the World Bank and IMF, they undertook PSIA pilot studies for Rwanda, Mozambique, Indonesia, Armenia, Uganda, and Honduras in an effort to demonstrate the circumstances in which PSIA could be useful to policymakers.<sup>1</sup>

An interesting element of DFID’s terms of reference was the placement of time limits on the conduct of PSIA to ensure that the analysis was undertaken in “real policy time.”<sup>2</sup> While DFID reported some concern on the part of IFIs with respect to the quality of PSIA undertaken over a relatively short period of time, the notion of “time bound” PSIA—if it can result in quality work—may respond to concerns that PSIA is not available earlier enough to be an input to program design.

<sup>1</sup>See DFID (2003).

<sup>2</sup>The terms of reference also required the use of both international *and* local consultants combining both economic and social expertise in the conduct of PSIA. This is consistent with Robb (2003), who emphasized that the most productive avenue to pursue PSIA was through the combination of skills embodied in various disciplines within the social sciences.

**Table 4.6. Number of Structural Conditions<sup>1,2</sup>**

	ESAF (N = 33)	PRGF (N = 32)
Prior actions	4.8	4.5
Performance criteria	4.0**	2.7**
Structural benchmarks	8.4**	4.9**

<sup>1</sup>Based on a sample of annual ESAF arrangements approved during 1996–99, and new PRGF arrangements approved during 2000–02.

<sup>2</sup>\*\* denote statistically significant difference in means between ESAFs and PRGFs.

terms of reducing the number of conditions, although the number itself does not necessarily translate into a good measure of the burden of conditionality). There have been statistically significant reductions in the number of performance criteria and structural benchmarks but no change, on average, in the number of prior actions (Table 4.6).

These patterns varied considerably among countries, as is evident in our case studies. Three of the six IEO case studies (Guinea, Nicaragua, and Tajikistan) experienced declines in the number of formal

structural conditions. On the other hand, Mozambique registered an increase in the number of structural conditions, particularly in the financial sector. Vietnam and Tanzania initially saw no marked change in the overall quantity of structural conditionality. We were unable to detect any clear linkage between this experience and previous “track records” on implementation.<sup>31</sup>

**What has happened to aggregate IMF–World Bank conditionality?**

A number of critics have argued that while the IMF has withdrawn from imposing structural conditionality in some policy areas, the World Bank has replaced it, resulting in no net reduction in the burden of conditionality, which they see as inconsistent with the emphasis on stronger country ownership. Others have argued that, since the fundamental problems impeding faster growth and poverty reduction in low-income countries are primarily structural in nature, it is reasonable to ask countries to establish benchmarks for monitoring their progress in the context of BWI lending, provided the benchmarks are derived from a country-driven strategy. We sought to investigate what has happened in practice as part of our evaluation. Several key messages emerge.

First, the BWIs do not have an explicit objective with respect to the burden of aggregate Bank-Fund conditionality. In July 2001, the Boards of both institutions endorsed a strategy to strengthen Bank-Fund collaboration on conditionality and called for the formulation of “mutually supportive and harmonized conditionality (but not cross conditionality) in PRGFs and Poverty Reduction Support Credits (PRSCs) (and IDA lending instruments)” and committed “to streamline and focus conditionality on the key actions crucial to success.”<sup>32</sup> This strategy resulted in the production of a joint Bank-Fund “Staff Guidance Note” that described the motivation for greater collaboration on conditionality as the avoidance of duplication.<sup>33</sup> However, reduction of the burden of aggregate conditionality was not explicitly identified as an objective.

Second, we found it enormously difficult to track what has happened to aggregate (Bank-Fund) conditionality in specific countries. The difficulties en-

<sup>31</sup>The explanation for the decline in Guinea, despite its poor track record, is that a large number of “informal” conditions were introduced in the context of several short-term consolidation exercises designed to put the PRGF-supported program back on track. These consolidation exercises, and the associated informal conditionality, were not linked in any significant way with the PRS.

<sup>32</sup>World Bank and IMF (2001c).

<sup>33</sup>World Bank and IMF (2002c).

countered suggest that systematic monitoring of developments in this area has not been a priority for either institution. Key problems include:

- (i) There is no simple “unit of account” with which to measure conditionality across the two institutions.<sup>34</sup> Moreover, “counting conditions” is a very crude measure of the burden of conditionality because of the potentially large differences in the political and technical challenges involved in implementing any one condition.
- (ii) While the IMF has a single instrument for supporting low-income countries (the PRGF), the World Bank has several, including PRSCs as well as sectoral adjustment and other program lending instruments, and it is difficult to track conditionality across this entire lending program.
- (iii) IMF and World Bank databases to track conditionality are not compatible and—even within each institution—are not always internally consistent.<sup>35</sup>
- (iv) For a number of the case study countries, no Bank adjustment credits had been approved post-PRSP, making a comparison of aggregate conditionality pre- and post-PRSP not meaningful.

Reflecting these constraints, we were able to obtain information on aggregate Fund-Bank conditionality for only four countries (Albania, Mozambique, Tanzania, and Vietnam) within the 10 IEO/OED case studies.<sup>36</sup> (A more detailed analysis is contained in each of the respective case study reports). The evidence from this admittedly very small sample is mixed but suggests a number of tentative messages:

- (i) There were decreases in the number of total Bank-Fund conditions after the PRSP in all four countries. This ranged from an almost 50 percent reduction in Albania to a 6 percent decline for Tanzania. The average across the four

<sup>34</sup>There are also differences between the nature of Bank conditionality under the PRSC and IMF conditionality under the PRGF that can blur the meaningfulness of simply adding the number of Bank and Fund conditions together.

<sup>35</sup>The IMF’s database is MONA (Monitoring of Arrangements) and the Bank’s ALCID (Adjustment Lending Conditionality Implementation Database). The IMF recently altered the classification system of its MONA database to improve its ability to monitor structural conditionality but the changes were not made retroactively.

<sup>36</sup>We looked at both PRSCs and other Bank adjustment loans. Since the evolution of Bank policy on conditionality was not concurrent with the adoption of the PRGF, we chose the date at which the full PRSP was adopted for the purposes of assessing changes in aggregate conditionality.

countries was a reduction of about one-third.<sup>37</sup> However, almost the entire decline was due to a reduction in Bank conditionality (the number of IMF conditions decreased only in Albania). This is surprising in light of the more explicit emphasis in the Fund on reducing the number of conditions and the results from the broader sample of PRGF-supported programs, which indicates such a reduction has occurred. It suggests that the countries for which we were able to undertake a comprehensive analysis are not typical, at least as far as the number of IMF conditions are concerned.

- (ii) There were significant changes in the division of labor:
  - With respect to *fiscal conditionality* (both revenue and expenditure), the IMF increased its focus, while the Bank reduced its emphasis (except for a modest increase in emphasis on treasury systems).
  - The Bank withdrew from setting conditionality on the *foreign exchange system* and on *central bank reform*.
  - The Fund withdrew from setting conditionality in the *agricultural sector* and reduced its already weak emphasis on *civil service reform*.
  - Bank conditionality in the *social sector* as a share of total Bank conditionality increased markedly.
  - *Financial sector reform* increased as a share of both Bank and Fund conditionality.
  - Both the Fund and the Bank reduced the shares of their conditionality on *SOE and trade reforms* but increased the share targeted to *institution building and legal and regulatory reforms*.

These observations are consistent with an increased emphasis on core areas of expertise by the two institutions.

The case studies also suggest that streamlining can involve unexpected pitfalls—linked to “principal-agent” difficulties—resulting in some structural issues not being handled well by the joint efforts of the BWIs. Specifically, it cannot be assumed that IMF and World Bank objectives and priorities in areas of overlapping interest are identical. The estab-

<sup>37</sup>These results are consistent with the responses the Bank and Fund received to a recent survey of country authorities, which indicated that two-thirds of respondents had reported a reduction in the number of combined program conditions. While these results were for both low- and middle-income countries, they do shed some light on the evolution of aggregate conditionality for PRSP/PRGF countries.

lishment of conditionality on SOE reform in Vietnam provides a good illustration. Consistent with an agreed division of labor, the Bank took the lead in designing and monitoring conditionality on SOE reform. The IMF's primary interest in the SOE sector was on the potential consequences for the budget and the soundness of the financial sector of weakness in the large SOEs. The Bank's primary interest, on the other hand, was private sector development and the demonstration effect of privatizing even small SOEs, a position that was consistent with the government's own priorities. As a result, SOE conditionality established by the Bank did not target the most fiscally significant SOEs.

Finally, surveys of IMF and World Bank staff conducted in late 2003 as part of an internal review of progress in strengthening Bank-Fund collaboration suggest some promising signs regarding the impact of the PRSP framework on collaboration. In countries that have embraced the PRS framework:<sup>38</sup> (i) IMF staff interacts to a greater extent with World Bank staff in the formulation of conditionality, and that involvement is perceived as more effective than in other countries. (ii) There is greater duplication of conditionality in PRGF-eligible countries than in others, but two-thirds of mission chiefs attribute this duplication to the fact that the measure is critical to both institutions' programs. (iii) The view that the IMF and the World Bank have developed a shared perspective on the necessary reforms is more prevalent among mission chiefs for PRGF-eligible countries than those for other countries.

### Some Program Design Issues

One aspect of program design that is much criticized is the lack of sufficient attention paid to macro-micro linkages and sources of growth. The critics have argued that the IMF's traditional approach to program design (or "financial programming"<sup>39</sup>) does not take sufficient account of the underlying determinants of growth and of the factors influencing the economy to macroeconomic policies—as well as of the potential feedback of macroeconomic policy actions on poverty—and that this can lead to mistakes in macroeconomic policy design.

<sup>38</sup>All the cited findings reflect statistically significant differences between the answers provided by mission chiefs for PRGF-eligible countries and mission chiefs to other program countries. In cases where the same question had been asked for the 2002 review of Bank-Fund collaboration, the significance of the difference increased over time.

<sup>39</sup>See Baqir and others (2003) or Khan and Knight (1985) for a description of the financial programming framework.

The goal of embedding PRGF-supported programs in the overall strategy for growth and poverty reduction aimed to address this criticism by seeking to base programs on fully integrated macroeconomic, structural, and social policies. As Adam and Bevan (2001) note, "This is a pretty tall order. This type of integrated framework is one which the economics profession, at least, has conspicuously failed to deliver over the last thirty years, despite much trumpeting of micro-macro frameworks. The short answer is that our understanding of these relationships, while not wholly lacking, is very far from being 'integrated.'" Nevertheless, more analysis of these linkages—and an explicit setting out of the underlying rationale for a particular program design—can foster a more constructive debate and modifications in the light of new evidence. Several relevant messages emerge from our evaluation and from recent analytical work undertaken in the IMF.

Discussions with IMF staff and analysis of briefing papers suggest that efforts in the World Bank and elsewhere to spell out the macro-micro linkages to growth and poverty have had limited impact so far on program design by the IMF.<sup>40</sup> The concerns typically expressed by Fund staff are that such approaches require too many assumptions about underlying economic and structural relationships, especially in low-income countries where the data often do not exist. While this is certainly true, it should not prevent additional analysis that can help throw light on some of the underlying linkages. The IMF does not have to produce the analytical inputs itself, but can help identify the major knowledge gaps in each country. If done in a collaborative manner with local researchers, such efforts can stimulate domestic capacity to analyze such matters.

Country programs are typically based on a number of assumptions about behavioral relationships (e.g., with regard to the response of investment and savings, or absorptive capacity with respect to aid inflows) and these often rely largely on judgment. The case studies show that while *qualitative* arguments were often made in support of the need for a particular design, staff reports or other program documents rarely spelled out systematically the full rationale, and implicit behavioral assumptions, underlying program design.<sup>41</sup> Since the consistency of program design depends critically upon these assumptions, a fuller statement would help generate a more informed debate and also more effective responses at the stage of program review. The Tanza-

<sup>40</sup>Gunter (2002) provides a summary of some of this work as well as similar work under way elsewhere using computable general equilibrium (CGE) and other models.

<sup>41</sup>The recent IEO evaluation of *Fiscal Adjustment in IMF-Supported Programs* (IEO, 2003) came to a similar conclusion.

### Box 4.7. Do PRGF-Supported Programs Have an Excessive Disinflation Bias?

A number of critics have argued that many PRGF-supported programs are excessively focused on disinflation, with potentially adverse effects on growth and poverty reduction.<sup>1</sup> Different cross-country analyses come to different conclusions as to what the “threshold” level of inflation might be above which it entails a trade-off with growth, but there appears to be a broad consensus that “double digit” inflation is likely to be harmful. Two recent studies suggest ranges of 2–3 percent per annum (Ghosh and Phillips, 1998) and 7–11 percent for developing countries (Khan and Senhadji, 2000). On the specific issue of disinflation, Ghosh and Phillips found that “starting from inflation rates above 6 percent, only the most drastic disinflations (at least halving the inflation rate in a single year) are associated with any negative impact on growth . . .” However, they also found that starting from rates below 6 percent, rapid disinflation (a halving of the rate in a year) was associated with a fall in real GDP growth.

Our evaluation indicates that PRGF-supported programs projected a smaller average reduction in inflation levels than ESAF-supported programs, but this

largely reflects much lower initial inflation rates. Under ESAFs, inflation was targeted to fall from 22 percent on average in the year immediately preceding the program to about 10 percent and 5½ percent in the first and second program years, respectively. By contrast, under PRGFs, the corresponding path was from 9 percent to about 6 percent and then to 4 percent.

Looking at disaggregated data, we found a strong tendency in program design against tolerating double-digit inflation, but detected no systematic disinflation tendency when inflation is already low. Out of 41 PRGF-supported programs in our sample, more than half had initial annual inflation rates of 5 percent or lower, and about one-quarter had initial inflation rates of 10 percent or higher. In all the latter cases, the program targeted a decline in inflation. In contrast, in the majority of cases where initial inflation was 5 percent or less, inflation was projected to go up. In those cases where initial inflation was between 5 percent and 10 percent, about two-thirds targeted lower inflation. This pattern is largely unchanged from that of ESAF-supported programs (except that the latter had fewer cases with initial inflation below 5 percent).

These results do not suggest an excessive “deflationary bias” with regard to inflation targets.

<sup>1</sup>See, for example, Oxfam (2004).

nia case discussed in Box 4.2 is one example. Another is Vietnam, where in the context of discussions on the pace of SOE reform, IMF staff initially sought more aggressive reform of SOEs, believing that future growth in the private sector would be sufficient to absorb much of the resulting displaced labor. The authorities took a more gradualist approach, partly based on a more conservative view of the pace of private sector growth and their associated desire to maintain social stability by containing the rise in unemployment. The disagreement with staff was not so much on the need to reform SOEs but the speed at which this could happen given the authorities’ expectation that the private sector would not be in a position to readily absorb displaced labor. In this regard, assumptions about growth in the private sector and its ability to absorb surplus public sector labor were key. That said, there appears to have been little analysis undertaken by either the authorities or staff (either in the IMF or World Bank) to investigate their implicit assumptions.

At a more general level, the assumption of rapid “crowding in” of private sector aggregate demand (as external resource requirements are relaxed or fiscal deficits are reduced) is a common feature in PRGF-supported program design. This has meant that the shift away from targeting reductions in the

external current account deficit has been accompanied by much less change in targeted fiscal deficits. Implicitly, the rationale of the program design appears to be that the more relaxed external stance accommodates stronger private sector demand. While this would be consistent with a strategy where the private sector will be the primary engine of growth, achieving this outcome depends upon the speed of response of the private sector. Assumptions on this aspect need to be verified and, if necessary, modified in light of experience.

A related issue is the extent to which PRGF-supported programs target inflation reduction and whether, as some critics have argued, program design is unduly restrictive by targeting excessive reductions in inflation—going beyond the evidence on what inflation thresholds are harmful to growth and poverty reduction. Our analysis of PRGF-supported programs suggests that programs do systematically target lower inflation when initial inflation is 10 percent or higher, but that there is much greater variation when initial inflation is 5 percent or less; in a majority of such cases, inflation was projected to increase (Box 4.7). This is generally consistent with the broader cross-country evidence on when inflation becomes harmful to growth and does not suggest an excessive “disinflation” bias.



## Has Program Implementation Improved?

An important premise in the transformation of the ESAF to the PRGF was that greater country ownership of programs would improve prospects for implementation. We examined a range of indicators—disbursement ratios, the incidence of program interruptions, and compliance with conditionality (performance criteria)—to see whether program implementation had improved under PRGFs. The main results from cross-country evidence are:<sup>42</sup>

- Among arrangements that have run their course (i.e., expired), the mean disbursement rate was about 75 percent, with no statistically significant difference between ESAFs and PRGFs.<sup>43</sup>
- There is hardly any difference between ESAFs and PRGFs in the relative frequency of program interruptions, although, on average, PRGFs exhibit a slightly shorter time between key program events.<sup>44</sup>

<sup>42</sup>Based on arrangements approved during 1995–2003.

<sup>43</sup>The subsample of expired arrangements was divided into those that had been either ESAFs or PRGFs for most or all of their duration.

<sup>44</sup>Typically, indicators of “program interruption” measure delays between scheduled and actual dates for completing program reviews (and approval of annual arrangements under the ESAF). For this report, we define interruption in terms of the actual time between key events rather than through a comparison of scheduled and actual dates. Key events are approval of multiyear or annual arrangements, completion of program reviews, and expiration dates (when they occurred more than 12 months after either

- The fraction of quantitative (i.e., macroeconomic/financial) performance criteria that were met increased slightly under PRGFs (to about 85 percent, compared with less than 80 percent under ESAFs). There was no statistically significant difference in the compliance rate with respect to structural performance criteria.

Overall, the indicators suggest a rather modest improvement in implementation under PRGFs. This finding is consistent with the evidence of mixed performance from the four IEO case studies—Guinea, Mozambique, Tanzania, and Vietnam—which had completed both ESAF and PRGF arrangements as of May 2004.<sup>45</sup> For example, of the four countries, Tanzania had no program interruption in either regime, while Guinea had major interruptions under both regimes. Mozambique had no formal program interruption under either regime but there were more delays in completing reviews under the PRGF than there was under the ESAF. For the Vietnam ESAF (1994–97), no agreement could be reached on a third annual arrangement. Performance under the PRGF (2001–04) was good but the arrangement was interrupted on account of issues that were not directly related to performance under the program.

the completion of the last review or approval of the arrangement). The averages are about 9½ and 9 months for ESAFs and PRGFs, respectively.

<sup>45</sup>Guinea (ESAF 1997–2001, PRGF 2001–04); Mozambique (ESAF 1996–99, ESAF/PRGF 1999–2003); Tanzania (ESAF 1996–2000, PRGF 2000–03); and Vietnam (ESAF 1994–97, PRGF 2001–04). For Mozambique, we count the ESAF/PRGF as a PRGF.



## The IMF's Way of Doing Business

### Key Messages

*The 1999 policy papers launching the PRSP/PRGF called for far-reaching changes in the nature of the IMF's involvement in low-income countries. These expectations were probably overambitious without much deeper organizational changes—and more administrative resources—than have occurred so far. Actual change has fallen well short of these expectations, although there are marked differences between “good” and “average” practice.*

*The heavy procedural requirements of the PRS process are absorbing much of the time of relatively small staff country teams at the expense of analytical and capacity-building activities.*

*IMF general policy advice, reflected in the PRSP Sourcebook, allowed for an appropriate broadening of the policy space. So has the country-specific internal IMF policy formulation process—at least in countries with a good policy implementation record and macroeconomic stability. There is some evidence of continued progress over time. However, staff has generally not viewed the participatory elements of the PRS process as a vehicle for exploring and resolving controversial policy issues.*

*IMF staff involvement has generally fallen well short of active participation in informing the broader policy dialogue. A lack of clarity about what was expected of staff generally led to a “hands-off” approach, in the interests of domestic ownership, even when key issues were not being addressed.*

*Despite greater sensitivity to the social implications of macroeconomic policy advice, there is not yet a systematic effort to identify and fill country-specific knowledge gaps on macro-micro linkages and PSIA and to integrate the resulting evidence into program design. The PRS process has not been used to generate systematic priorities on what the IMF itself should be delivering.*

*There is no systematic guidance for the role of resident representatives in the PRS process. The scope of their contribution varies widely, depending on individuals, not institutional arrangements.*

*The IMF's contributions to the broader partnership framework implied by the PRS approach have been limited by a lack of clarity on what this framework means for the IMF's way of doing business. This includes the IMF's “signaling” role, the role of conditionality in a longer-term framework, and operational approaches to setting the medium-term external resource envelope.*

The PRS/PRGF initiative called for significant changes in the IMF's way of doing business. This chapter asks how much has changed in practice. We begin with a discussion of what the original policy papers as well as subsequent internal guidance indicated were the major expected changes in the Fund's operating approach. We then assess: (i) the extent to which the IMF's general policy advice to low-income countries allows for greater "policy space" and how much the IMF's own internal policy formulation has changed in light of the new approach; (ii) how much the IMF's approach on the ground has changed, according to the case studies; (iii) the role of resident representatives; and (iv) the contribution of IMF surveillance. We conclude by discussing some of the main obstacles to enhancing the effectiveness of the IMF's role.

## What Was Expected of the IMF Under the New Initiative?

The original policy papers envisaged substantial changes in the nature of the IMF's involvement in PRSP countries for the new initiative to be successful. The expected changes in some critical areas are illustrated in the quotations (below) from these papers.<sup>1</sup>

- *Openness to homegrown adjustment and reform: expanded policy space*

The staffs must be open to more flexible, home grown adjustment and reform paths, which reflect country ownership without prejudicing the goal of poverty reduction and faster growth.

The Fund will need to be ready to assess new approaches and to recognize and support a healthy process of experimentation and innovation. Fund staff will be open to considering alternative adjustment paths, taking into account their impact on the poor.

- *Active participation in the domestic policy debate*

Bank and Fund staff should be prepared to share their analyses and the key elements of their policy positions in the consultative process, even during the early stages of the policy dialogue. Missions would learn from the policy dialogue, and should be ready to consider modifying their analysis of the problems and policy options accordingly. Staff would need to play an active role in supporting the

process, to ensure that domestic dialogue is well-informed.

Discussions on the macroeconomic framework will become more open and iterative. Fund staff can expect to be requested by members to participate in broad-based consultations organized by the member in preparing its poverty strategy and the macroeconomic framework underpinning it. Key macroeconomic policies, including targets for growth and inflation, and the thrust of fiscal, monetary, and external policies, as well as structural policies to accelerate growth, would be subjects for public consultation.

- *Contribution to expanding knowledge on the linkages between macroeconomic policies and growth/poverty reduction*

[There is a] need for Bank and Fund staff to work closely together to improve our knowledge of the general link between the macro framework, growth, and poverty reduction, particularly over the medium-term so as to understand better the general issues raised.

- *Inputs into determining the external resource envelope*

Early in the process, the staffs should seek a common perspective . . . on . . . an initial view of the current resource envelope and, within this, the possible scale of expenditures for poverty reduction; [and] a discussion of the current levels and nature of external assistance, and the prospects for increased aid over the medium-term.

One key component will be to mobilize external support, and here Fund staff will need to redouble efforts to identify sustained increases in resources for countries where these can be used most effectively.

The initial policy papers put little emphasis on capacity building, but as time went by it became clear that weak country capacity was a major constraint to effective preparation and implementation of PRSs. Accordingly, at the time of the 2002 review, the Board encouraged the staff to step up its efforts at capacity building in the IMF's areas of expertise.

How these broad—and challenging—expectations were to be translated into specific operational approaches for IMF staff was not spelled out initially, although some guidance was eventually issued later (Box 5.1). There was an understandable concern not to overprescribe a common operating approach that might conflict with the emphasis on country-driven processes and the need for "learning by doing." However, this reluctance to be overprescriptive translated in practice into a lack of concrete indicators on precisely what the IMF should be delivering—either initiative-wide or in individual countries.

<sup>1</sup>The quotations are taken from IMF (1999a); World Bank and IMF (1999c); and the Concluding Remarks by the Chairman of the IMF's Executive Board, IMF (1999b).

### Box 5.1. Internal Guidance to IMF Staff on the Implementation of the PRS Approach

This box addresses two related issues: (i) what internal guidance says about IMF staff's role in the PRS approach. It should be emphasized that a large share of this guidance was developed recently (i.e., in 2003) and therefore was not available to guide staff work for most of the period under review; and (ii) what staff think their role is and whether they think the guidance is clear.

#### General guidance on role of staff in PRS approach

Early policy papers recognized that substantive changes in the organization of mission work would be required, but this was not translated into specific operational guidance until a relatively late stage.<sup>1</sup> In August 2003, the Policy Development and Review Department (PDR) circulated a note to IMF mission chiefs on how to handle key challenges raised by the PRS approach. Key suggestions included: (i) engaging early on in the PRS process, with staff visits planned in line with domestic processes; (ii) encouraging and helping (through capacity-building efforts) the authorities to base their PRSP on realistic growth projections, to integrate it with the budget and medium-term expenditure framework, and to incorporate contingency spending plans; (iii) discussing with the authorities the macroeconomic implications of higher aid flows, to determine whether the negative macroeconomic consequences of higher externally financed poverty-reducing spending outweigh its benefits; and (iv) synchronizing the PRGF and PRS cycles by initiating a new three-year PRGF arrangement shortly after the completion of a new PRSP. The same memo also encouraged staff to use IMF Country Strategy Papers and Article IV consultation reports as vehicles to provide their assessment of the sources of and obstacles to growth, drawing upon the analyses of the World Bank and others.

#### Guidance on outreach

On the occasion of a review of the IMF's external communications strategy in early 2003, Executive Directors, while not distinguishing between PRS countries and others, supported a more active role for resident representatives and mission chiefs in outreach. The "Guide for Staff Relations with CSOs" (IMF, 2003i) suggests to "treat public outreach as vital, but (given resource constraints) not [to] compromise

other tasks." The purposes of such relations are defined broadly and include explaining the Fund and its activities; obtaining policy inputs from nongovernmental sources; gauging forces for and against IMF-supported policies; and building national support and initiative toward IMF-backed policies. It is suggested that staff meet with CSOs early enough in the process so that the consultation is meaningful, to ensure ample opportunity for questions and comments, and to debate options. The guidelines also emphasize that relations with CSOs should be handled in ways that do not alienate or put indirect pressure on governments.

#### Staff views on their own role in PRS approach<sup>2</sup>

*Why has there been only limited change in the IMF's way of doing business?* Respondents on average were of the view that the main factors were staff resource constraints, the demands of the review process, or doubts about the value added of the new approach. Among the factors constraining staff's outreach efforts toward civil society were limited mission size and length and absence of suitable internal incentives. Absence of clear guidance on what was expected was generally considered a less important factor. Only about one-fifth of respondents to the survey of IMF staff agreed that the PRS/PRGF initiatives had led to significant changes in the way initial policy positions are discussed within the Fund.

*Role of IMF staff in PRSP participatory process.* One-half of respondents considered their role as participating only to the extent requested by the authorities. Only about two-fifth of respondents saw their role as implying active participation throughout the process, while one in ten defined their role as entirely passive.

*Main changes in IMF's way of doing business.* Of the key features of the PRGF, staff thought the ones that had the most impact on their work were the requirements for more selective structural conditionality and for broad participation and greater ownership. All key features were found to have had a significant impact on staff work, PSIA excepted. Two aspects of staff work were highlighted as having undergone the most significant changes: collaboration with the World Bank (in the sense that it was improved both at headquarters and, even more, in the field) and interactions with civil society. Regarding obstacles to PSIA, funding/staffing constraints in the IMF and the World Bank and capacity constraints in member countries were emphasized.

<sup>1</sup>Interviews with area department staff suggest that the general policy line was that staff should take a hands-off approach, out of concern not to undermine country ownership, or be seen as doing so.

<sup>2</sup>Based on survey of a group of IMF staff members with current or prior involvement in PRSP/PRGF countries. See Annex 2 for details.

## Have the IMF's Policy-Formulation Processes and Advice Changed Under the PRSP/PRGF?

We looked at two types of evidence to see what had changed in the IMF's own processes. First, we reviewed the IMF's general policy advice on macroeconomic issues in low-income countries to assess whether it gives greater "policy space" for the consideration of alternative policy options. Second, we examined what happened during the internal policy formulation process for all countries in our sample to see how the new approach was applied in practice.

### General IMF policy advice: what has happened to the "policy space"?

As noted in Chapter 2, the policy papers establishing the PRS/PRGF approach never explicitly address the potential tensions between ownership and the BWIs' own judgments on what policies are good for growth and poverty reduction. But a greater emphasis on ownership was not meant to imply the acceptance of *any* homegrown policy package. The aim was to create greater scope for country-driven alternatives and investigation of alternative strategies by expanding the policy space acceptable to BWIs, especially on issues where the evidence on links from policies to growth and poverty reduction is not well established or is likely to depend on circumstances in a particular country.<sup>2</sup> We reviewed one particular template for the provision of general policy advice—the chapter on "Macroeconomic Issues" in the PRSP Sourcebook—to assess whether the policy space was indeed widened.<sup>3</sup> Our overall judgment is that the Sourcebook generally achieves its objective of discussing the fiscal, monetary, and exchange rate policies that would be supportive of sustainable growth and poverty reduction in a manner that provides adequate room for different approaches, perhaps arising from the circumstances in each country (see Annex 4 for details).

However, on a few issues the discussion appears to be overprescriptive. For example, while recognizing that the pace of adjustment to external

<sup>2</sup>Bird (2004) makes a similar point.

<sup>3</sup>Available at <http://www.worldbank.org/poverty/strategies/sourcetoc.htm>. Like the rest of the Sourcebook, the chapter appropriately emphasizes that it is not intended to be prescriptive and is only to be used selectively as an informational resource. A broader overview of recent IMF macroeconomic research on low-income countries is given in IMF (2003b). The purpose of our review was not to provide a detailed judgment on the merits of specific policy advice per se, but rather to ask two questions about the degree of "policy space" for each policy issue: (i) how detailed are the prescriptions in the Sourcebook; and (ii) how strong is the broader evidence supporting these prescriptions.

shocks will be influenced by the availability of financing, the Sourcebook essentially endorses an approach for fiscal policy to "treat every favorable shock as temporary and every adverse one as permanent." This appears too sweeping, especially once one considers aspects of the nature of poverty that emerge from poverty assessments undertaken as part of each PRSP whereby temporary contractions can have adverse permanent effects on growth and poverty (if, for example, children are pulled out of school).

Another area where the PRSP Sourcebook is overprescriptive relates to exchange controls. It argues that relaxing controls that force assets to be held in domestic currency could give the poor access to safer assets, such as foreign currency, that can protect them from devaluations. Asserting a direct poverty-reduction dimension to such liberalization without recognizing the complexity of the policy choice involved, which depends critically on much larger sequencing issues, goes beyond the available evidence.<sup>4</sup>

Interestingly, the views of various I-NGOs on the general policy advice contained in the PRSP Sourcebook are much more negative than our own assessment. We discuss what seem to be the main areas of contention in Box 5.2.

### Changes in internal IMF policy formulation processes between the PRGF and ESAF

We examined in detail the IMF's internal "briefing paper process" to see whether its approach to policy formulation has adapted to the new approach. Under IMF internal procedures, the area department prepares a briefing paper prior to every staff mission to a country. Each brief presents an assessment of the country's economic challenges, and identifies the key issues that the mission plans to take up with the authorities, along with main features of the anticipated program or policy advice. The brief is commented on by several IMF reviewing departments and is cleared by management. It is not seen by the IMF's Board or the authorities. This internal clearance process is much more centralized than that of other IFIs and provides a rich source of material for assessing whether internal processes are moving in the directions called for by the PRS/PRGF approach.

We compared briefing papers from the ESAF and PRGF periods, along with reviewing departments' comments on these briefs, for missions to the sample

<sup>4</sup>The IMF's own work on the effects of financial integration and liberalization suggests much less definitive conclusions. See IMF (2002e, Chapter 3).



### Box 5.2. Views of NGOs: What Is the Nature of Their Policy Differences with the IMF?

As part of the effort to encourage broad-based inputs into the evaluation, we invited the views of a number of groups on the thrust of the macroeconomic policy advice contained in the PRSP Sourcebook. It is interesting to discuss the reaction of some I-NGOs, not to suggest that we necessarily share their judgment but because their response helps to understand the nature of their policy disagreements with the IMF:<sup>1</sup>

*Concept of macroeconomic stability and degree of trade-offs with other objectives.* While recognizing that large macroeconomic disequilibria can be an obstacle to poverty reduction, some critics argue that macroeconomic stability may compete, and even be in conflict, with other objectives, such as government spending to meet the MDGs, and that poverty reduction, not the macroeconomic objective, should be given priority. For example, they argue that a more flexible approach to the threshold inflation objective may be warranted, depending on the trade-offs in particular countries. We discussed this latter issue in Chapter 4 and came to the conclusion that there is no evidence that programs systematically target excessive disinflation.

*Assumed supply-side responses to macroeconomic adjustment.* Critics argue that the IMF's policy advice

<sup>1</sup>The discussion here draws in particular on comments submitted to the IEO by the EURODAD secretariat, but the submission by Oxfam (2004) makes a number of similar points.

implicitly assumes that the private sector will respond rationally to macroeconomic adjustments, which understates the potential impact of extensive market imperfections in developing countries. The speed of private sector response is one of the key "macro-micro" linkages, and the discussion in Chapter 4 suggests that program design is indeed sometimes based on assumptions not backed by strong evidence.

*The efficacy of social safety nets.* Critics argue that the effectiveness of such safety nets in protecting the poor from adjustment costs is questionable. In particular, they argue the introduction of such safety nets at the time of a crisis or shock rarely works well and a more effective strategy would be to develop longer-term programs in advance, along with ex ante PSIA of adjustment policies. This is a point now recognized by the IMF. Indeed, the recent IEO evaluation of the role of fiscal adjustment in IMF-supported programs recommended that, as part of its surveillance activities, the IMF invite countries that so wish to discuss how such programs might be protected in the event that extensive adjustment is required.

*Greater focus is needed on what the IMF can do to improve the external environment for sound macroeconomic policies,* including the problems caused by the unpredictability and volatility of aid flows and the trade environment faced by low-income countries. We take up the latter issue in the discussion below on the IMF's surveillance role.

of 23 countries according to a set of uniform criteria on what we expected to see in terms of changes in approach.<sup>5</sup> There were wide variations between "average" and "best" practice, but the following messages emerge:

- (i) *Increased attention to protection of key social objectives.* A majority of PRGF briefs considered various ways of protecting key objectives in the event of unanticipated shocks, including those of a global slowdown and reductions in aid disbursements. In particular, they discussed ways of protecting priority expenditures, even where this required some expansion of the fis-

cal deficit. This contrasted with earlier briefs that often indicated the potential sources of shocks but without any strategy to protect priority expenditures.

- (ii) *More limited opening of policy space in macroeconomic areas, except in countries with a strong policy implementation record and macroeconomic stability.* Only about a quarter of the PRGF briefs indicated an increase in policy space in the sense of acknowledging that some issues should be addressed through homegrown options without the IMF staff pushing for a particular approach. On macroeconomic stabilization measures and structural issues, some space for the discussion of alternative options was already evident under the ESAF; on average, there appears to have been only a modest further expansion of such policy space under the PRGF, concentrated in countries with good macroeconomic performance. The most clear-cut examples of increased willingness to defer to the view of the authorities were in the

<sup>5</sup>See Tables A4.1 and A4.2 of Annex 4 for details. For each criteria, the processes were rated on a four-point scale in terms of degree of consistency with the PRS/PRGF principles. It should be stressed that this assessment focused on the contents of the briefing papers, not on final outcomes of negotiations. There is no suggestion that ESAF briefing could or should have been "consistent" with approaches that were only developed later, but the comparison gives an indication of what changes have taken place over time.



areas of public finance and, to a lesser extent, financial sector reform.<sup>6</sup> An important positive sign of change was that review departments were generally less inclined to suggest increases in conditionality as a means of resolving outstanding policy issues than had been the case under the ESAF, except for countries with a history of poor economic policy performance.

- (iii) *Broader participation was generally not viewed as a significant avenue for exploring macroeconomic policy alternatives.* On the whole, PRGF briefs did not accord participatory processes under the PRS much significance as a vehicle for resolving key macroeconomic policy issues, typically not looking to such processes as a means of easing political economy constraints or generating alternative policy options. However, in the few cases where the importance of a participatory process was recognized, the briefs envisioned greater consultations by IMF staff with domestic stakeholder groups, including the private sector, and aimed to use outcomes from such discussions in the design of the program.
- (iv) *Broader call for PSIA, but still not a regular part of ex ante program design, and vagueness about responsibility for delivering the analysis.* PRGF briefs in most cases pay greater attention to the idea of PSIA, in many cases highlighting where such analysis should be done. Some briefs suggested the setting up of national committees for coordinating PSIA work, to enable a more systematic scrutiny of the poverty impact of policies. The approach was premised on the assessments being undertaken outside the IMF (by governments themselves, the World Bank, or other donors), but often with considerable vagueness as to when such inputs might be delivered.
- (v) *Heightened flexibility to accommodate external financing.* The PRGF briefs indicated more explicitly than earlier briefs a willingness to accommodate higher aid inflows. The scope for a higher fiscal deficit was recognized, although few briefs linked this systematically to program design issues or discussed in detail the rationale for a particular proposed fiscal

path. Generally—and partly as a legacy of the HIPC-oriented process—the briefs held to the view that the bulk of the new external financing had to be targeted to priority sectors, notably health and education, while the impact of alternative expenditure patterns was generally not explicitly considered.

## The IMF's Contribution on the Ground: Evidence from Case Studies

The case studies provide our main source of evidence for what has actually changed on the ground with regard to the IMF's role. There appears to be a wide variation in country experience, but in general the involvement of IMF staff has fallen far short of the active participation in the consultative process and resulting policy dialogue suggested by the policy papers establishing the PRS/PRGF approach. As noted earlier, these papers anticipated a more active role in the form of early involvement; active staff support for well-informed domestic dialogue; open and interactive process; and staff participation in broad-based consultations. In none of the case studies did the IMF meet these expectations fully, although it made progress in a number of areas:

- The staff in all cases engaged in some early interaction, but this was typically limited to its traditional interlocutors (the ministry of finance and central bank). The Fund also generally adapted its mission timing to the government's own policy cycle, including that for the budget.
- In cases where a PRGF arrangement was already in place before the PRSP,<sup>7</sup> the macroeconomic framework was typically taken from the former with limited efforts to “open up the policy debate.” Beyond this transitional phase, there are some examples—most notably Tanzania, but also Mozambique—where the staff did engage in a more interactive dialogue on some policy aspects. It is hard to generalize from these few cases, but they do suggest that such changes in approach can add significant value in terms of better policy outcomes. (We will illustrate this in Chapter 6 when we trace through the impact of the approach on a number of specific policy issues and outcomes.)
- There were few cases where the IMF staff had identified issues that it viewed as critical and successfully pushed for them to be on the menu

<sup>6</sup>Examples include upward revisions of the fiscal deficit in Bolivia and Mauritania to bolster social expenditure; formulation of an alternative to VAT on agricultural produce in the Kyrgyz Republic; and the modification to pace and sequencing of financial sector reforms in a number of African countries to allow for the evolution of a domestic consensus on the issue.

<sup>7</sup>Often a “converted” ESAF.

of the broader policy debate around the PRS—which would seem to be a central element of ensuring a well-informed dialogue. SOE reform in Vietnam was one exception, but this was an issue where the government already had strong ownership.

- The donor community was generally critical of the IMF's preference to remain in the background, instead of helping to explain to stakeholders the implications of the policy measures it was recommending to governments. In a number of cases, however, there have been increased efforts in recent years to explain the rationale of Fund advice (e.g., Nicaragua, Tanzania, and Vietnam), typically led by the resident representative.
- IMF staff (especially resident representatives) now meet a broader range *civil society* on a more frequent basis, although the substantiveness of these discussions varies considerably. It is most substantive in cases where the government has established an institutional framework for a broader dialogue on policy issues.

The case studies support the conclusion that there is somewhat greater openness to considering alternative policy courses and trade-offs, but only after immediate macrostabilization issues had been addressed (e.g., Nicaragua and Mozambique). In contrast, when programs went substantially off track (e.g., in Guinea), the staff's focus was on traditional stabilization approaches that drew little from the broader PRS debate—with the important exception that significant attention was given to protecting priority expenditures.

There is also some evidence of progress over time in consideration of alternative options, although it is hard to make broad generalizations. Continued Fund involvement in the update of the macroeconomic policy framework resulted in reconsideration of elements of the strategy in some cases (e.g., Tanzania—see Box 4.2—and Mozambique). In addition, several cases show progress over time in opening up the policy space on particular issues (e.g., the approach to tax reform in Nicaragua; fiscal flexibility in Tanzania; and tariff policy in Mozambique).

Interviews with staff and evidence from the case studies suggest that, despite some efforts to broaden the investigation of linkages between macroeconomic policies and growth/poverty outcomes, there is not yet a systematic effort to integrate such evidence into macroeconomic program design. In this connection, a recent review of the IMF's African Department reached a similar conclusion that there has been not enough emphasis on filling the gap between broad macroeconomic prescriptions from general

cross-country evidence and specific country work on PRSP-relevant issues.<sup>8</sup>

## IMF Contributions to the Broader Partnership Framework

The general objective of the partnership principle of the PRS approach is to help countries overcome long-standing problems of donor coordination. We address here three implications for the IMF's role: (i) conditionality and performance monitoring; (ii) determination of the external resource envelope; and (iii) capacity building.<sup>9</sup> In all cases, our evaluation suggests that the implications for the IMF's way of doing business of the broader partnership framework are still insufficiently developed.

On *conditionality and performance monitoring*, there are two major shortcomings:

- The potential of the JSA as a common reference among development partners has largely failed to be realized, for reasons discussed in Chapter 3: first, the clarity of the IMF's assessment in the JSA varies considerably, weakening its role as a signal to other donors. Second, efforts to incorporate inputs from other donors also vary widely but are inadequate in most cases.
- The “signaling” role of IMF-supported programs is often ambiguous. For example, the traditional short-term IMF conditionality may not fit well with a framework where the international community is “in for the long haul.”<sup>10</sup> Indeed, no one—including the IMF—would want a situation where short-term interruptions in programs lead to excessive “on-off” signals for other financing flows even when all stakeholders recognize that the issues involved in the interruption are of legitimate concern. We have not been able to obtain systematic evidence on the effects of program interruptions on such financing flows, but the limited evidence available from the case studies suggests a mixed pic-

<sup>8</sup>See “Report of the Task Force on the Organization and Management of the African Department” (IMF, 2004c). The report proposed and management accepted a departmental reorganization, including enhanced staff resources, that would give greater prominence to such policy issues.

<sup>9</sup>Other issues with regard to donor coordination are addressed in the OED report.

<sup>10</sup>In a few countries (including Tanzania and Mozambique), groups of bilateral donors providing general budgetary support have agreed on common PAFs to streamline and coordinate conditionality. The World Bank has begun to join such groups. The PAFs sometimes draw upon IMF conditionality or program targets, but there have been no efforts toward broader integration or streamlining.

ture. In some cases, donors' decisions about the extent and modalities of their support were only loosely tied to performance under IMF-supported programs (e.g., in Guinea, donors proved unwilling to commit to much support even when the PRGF-supported program was on track, whereas in Vietnam they provided substantial support regardless of the program status).

With regard to the *determination of the external resource envelope*, two factors appear to have constrained the IMF's role in helping to mobilize financing. First, the approach to balancing "ambition" and "realism" in PRS macroeconomic frameworks is unresolved (see Chapter 4). In practice, there have been only limited efforts to integrate systematically macroeconomic frameworks and sustainability analysis (areas where the IMF has a comparative advantage) with realistic costings of other aspects of the growth and poverty reduction strategy and with assessments of absorptive capacity (areas where the IMF does not have a comparative advantage and inputs should be taken from other partners). Second, procedures for giving feedback on each country's PRS, through the JSA, provide no mechanism for "treating different countries differently" (i.e., for signaling that some sets of policies deserve more support from the donor community). The standard language used to conclude all JSAs, as discussed in Chapter 3, mitigates against such signaling, even though the original expectation was that the JSA would play such a role.

In other words, there is little in the PRS approach as presently designed and implemented that provides for effective signaling with regard to aid selectivity, let alone collective decision making on a reasonable level of aid flows to assume in formulating the medium-term macroeconomic framework for PRSPs. Consequently, the calls in the original policy documents for the IMF to play a larger catalytic role in mobilizing such financing have little practical backing in terms of operational mechanisms.<sup>11</sup>

Recent internal reviews have underlined that PRSPs should provide the basis for setting technical assistance (TA) needs and country-owned priorities for *capacity building*.<sup>12</sup> However, this recognition is relatively new. The IMF policy statement on TA, adopted in April 2001, does not mention the

<sup>11</sup>The IMF has made some progress in developing an analytical framework for debt sustainability to help the country (and its aid partners) avoid borrowing paths—even at concessional rates—that involve a significant risk of entering into new debt problems. See, for example, IMF (2004b).

<sup>12</sup>See IMF (2004d). This issue will be reviewed in more depth in the context of the ongoing IEO evaluation of IMF TA. The discussion here draws upon interviews with TA coordinators in various IMF departments.

PRSP/PRGF approach in its discussion of filters and priorities for enhancing the effectiveness of IMF TA. In practice, the record suggested by the case studies is mixed:

- To date, the bulk of IMF TA activities—and thus the nature and scope of capacity building—has been more influenced by the demands of IMF-supported programs than long-term capacity-building needs of the countries. The planning of TA supply remains driven by functional rather than area departments, and inputs from the latter are typically not anchored in the PRS (although there are signs that this is changing as far as the African Department is concerned). The planning horizon is yearly at best, which does not mesh well with the longer-term perspective of the PRS approach.
- Few PRSPs provide systematic guidance on capacity-building needs in macroeconomic and related areas. Most JSAs, by contrast, do offer some discussion of capacity constraints. But there is no indication that this has been used as a basis to orient the provision of IMF TA, let alone coordinate TA supply with other providers.
- Nevertheless, the case studies do suggest that the broad areas in which the IMF is delivering TA are reasonably aligned with PRS priorities, taking account of the IMF's comparative advantage. They also suggest that efforts to coordinate IMF TA delivery with other donors have improved, but in no case is such TA fully integrated into a common framework focused on longer-term objectives.

## Role of IMF Resident Representatives

The presence of a resident representative in countries participating in the PRS/PRGF initiative can significantly enhance the IMF's ability to understand the political and social context in which policy is made and facilitate earlier and less formal dialogue on policy issues.<sup>13</sup> We review here what guidance is given to resident representatives, and summarize evidence on their actual role from the case studies and the staff survey.

There is no Fund-wide guidance to resident representatives on the role they are expected to play in the PRS process. Area departments prepare terms of reference (TORs) for each representative. These TORs

<sup>13</sup>IMF resident representatives are present in most countries engaged in the PRSP and PRGF. Of the 23 countries in our sample, only Yemen and The Gambia did not have resident representatives at any time since 1999.

are agreed with the host country and, in principle at least, could be a vehicle for spelling out some of the “rules of the game” for IMF involvement in the broader policy dialogue. We reviewed all TORs for resident representatives in PRS countries over the last four years and, with a few noteworthy exceptions, they provide remarkably little guidance on what was expected vis-à-vis the PRS process. The issue was not mentioned in most TORs for resident representatives outside Africa. For postings in Africa, instructions varied considerably. While some made no reference, others referred to “liaising with civil society in the context of the PRSP process.” In only a minority of countries (all in Francophone Africa) did the TORs describe explicitly a proactive role for the resident representative.

The case studies throw light on two aspects of the representatives’ role: (i) their involvement in the broader policy dialogue and participatory process on macroeconomic and related issues; and (ii) their inputs into the formulation of the IMF’s own policy formulation and program design.

The case studies show a wide variation in the role played by resident representatives in the broader policy dialogue. In Vietnam and Nicaragua, representatives were active contributors to discussions among a broad range of stakeholders, and were praised by some local stakeholders for their ability to discuss complex macroeconomic issues in a manner that was accessible to noneconomists. In Mozambique, the donor community was equally complimentary, but the civil society organizations (CSOs) considered the IMF to have been “invisible.”<sup>14</sup> In some other countries (e.g., Guinea), resident representatives interpreted the emphasis on country ownership to imply a more “hands-off” approach, and members of the donor community and civil society expressed a desire to have more substantive interactions.

The institutional context within which each resident representative operates has a significant influence on the modalities for involvement in domestic participatory processes. In some countries, like Mozambique, Tanzania, and Vietnam, well-established forums exist within which the representative could engage with CSOs and donors. The scope in Tajikistan was more limited given the nascent state of civil society and the small number of donors on the ground. In Guinea, dialogue with CSOs was limited partly because the authorities had reservations about the extent of formal consultation between the representative and civil society.

That said, the evidence suggests that it is possible for the resident representative to engage meaningfully with key stakeholders. This requires an ability

and interest on the part of the representative to communicate openly and substantively with groups that have varying degrees of technical sophistication. It also requires the right structure of incentives. Our discussions suggest that these kinds of communication skills were not sufficiently recognized or rewarded by the IMF.

It is difficult to assess comprehensively the impact of representatives on the IMF’s internal policy formulation because it is mostly channeled through informal exchanges between the representative and IMF headquarters staff (especially the mission chief). Experience varied substantially, but the following points are worth noting: (i) In all cases, the representative reports through the headquarters-based mission chief. (ii) Internal briefing papers are always prepared in Washington; the representative is usually (but not always) asked to comment, but these inputs stay within the area department. (iii) Experienced and well-informed resident representatives can have a significant input into the Fund’s policy advice and program design, but it depends on the individuals involved. Nothing in current institutional arrangements systematizes such an input.

## Role of Surveillance

Surveillance can contribute to the success of the PRS process in two ways: (i) in PRSP countries, it can foster contributions to the broader policy debate that could feed into the PRS process; and (ii) bilateral surveillance of advanced countries and multilateral surveillance can identify ways in which policies in advanced countries constrain the achievement of growth and poverty reduction objectives in low-income countries. How well has the IMF performed these roles?

Article IV surveillance in low-income countries would seem to be a natural vehicle for addressing longer-term strategic issues in the IMF’s area of responsibility as well as for providing an input into the broad public debate. To assess what role the IMF has played in practice, we analyzed staff reports and background issues papers for surveillance in PRS cases to identify what types of issues were examined in depth, including the following categories: growth and development issues (e.g., obstacles to private sector development and identification of trade-offs), sustainability and consistency between longer-term plans and macroeconomic conditions (e.g., aid envelope and path of fiscal consolidation, Dutch disease/aid dependence), transition and sequencing issues, and obstacles to growth from market access restrictions of advanced countries. In most instances, surveillance was carried out in conjunction with PRGF program activities. For the 23 countries with a

<sup>14</sup>See Nordic Countries (2003) for a donor assessment.



full PRSP by end-2002, there were only 9 stand-alone Article IV consultations (out of over 100 consultations) in the last 4 surveillance cycles (2000–03). The case studies suggest that surveillance generally centered preponderantly around issues directly related to the program, with more limited attention to other issues that the PRS would have needed to address.<sup>15</sup> However, surveillance in a number of the case studies did pay attention to various aspects of the problem of weak economic institutions, including regulatory and supervisory frameworks for the financial sector and budgetary processes, and governance issues.

A review of recent Article IV staff reports of major industrial countries suggests that surveillance referred to the impact of these countries' market access and subsidy policies on low-income countries in only a very general manner. In no case was there a systematic assessment of the impact of these policies on groups of low-income countries, drawn from work done in the IMF or elsewhere. Moreover, the scope of coverage of market access issues in surveillance documents included only a partial treatment of key areas identified by multilateral surveillance, and has varied across country documents.<sup>16</sup> Treatment of the relevant trade and subsidy issues gives relatively limited consideration to the impact on low-income countries, with no sense of magnitude of the effect of the country's policies.

IMF multilateral surveillance (e.g., the World Economic Outlook) has clearly identified key market access issues affecting developing countries.<sup>17</sup> The policy instruments that have the most impact on market access for low-income countries comprise tariff and nontariff barriers (mostly on textile and apparel), subsidies (principally to agriculture), and tariff escalation on various industrial goods. This has not translated, however, into analyses of the impact for particular low-income countries. For example, there do not appear to have been any attempts to link systematically the discussion of the individual PRSP country's strategies and export projections with the constraints implied by advanced economies' trade and subsidy policies. Such an analysis would be a useful contribution by the IMF to help expand the

“partnership” principle so that the policy actions by advanced economies that would most support each country's growth and poverty objectives would be identified as part of the PRSP process.<sup>18</sup>

## Obstacles to Further Progress in Adapting the IMF's Role

The evaluation indicates a number of obstacles to adapting the Fund's role to meet the expectations of the new initiative:

(i) *The original policy documents raised highly ambitious expectations about the IMF's role that may have been unrealistic and, in any event, would require much deeper organizational changes—and more resources—than have occurred so far.* The quotations cited earlier clearly imply a radical change in the IMF's own way of doing business, and it is easy to understand why the expectations of outside groups were so high. Discussions with IMF staff, both for the case studies and more generally, indicate that many believe that the initiative is overpromising on what can be delivered in the areas of the IMF's primary responsibility given *existing organizational constraints*, which include:

- A lack of clarity/guidance on how to operationalize a number of aspects of the new approach. These aspects included (a) the role of the IMF in the broader PRS debate;<sup>19</sup> (b) the IMF's contribution to determining an appropriate medium-term external resource envelope; and (c) the IMF's broader signaling role and how in practice the trade-offs between selectivity (in financial support) and domestic ownership are to be resolved.
- There has been only a moderate reallocation of resources to address all of the expected new tasks. The share of total IMF administrative expenses devoted to PRSP/PRGF issues was 11.5 percent in FY2003, only slightly higher than the 10.8 percent allocated to

<sup>15</sup>The most notable exception is Vietnam, which did not have a program for over four years. In a number of other cases, surveillance documents have included sections on issues relevant for longer-term growth (e.g., on competitiveness and exports in Guinea, and on agriculture and trade issues in Tajikistan), although such analysis receives only limited attention in the staff appraisals.

<sup>16</sup>See, for example, World Bank and IMF (2003a).

<sup>17</sup>See also World Bank and IMF (2002e). More recently, the *Global Monitoring Report* (World Bank and IMF, 2004a) has provided a more systematic discussion of the obstacles to reaching the MDGs originating in the policies of developed countries.

<sup>18</sup>This does not imply that the IMF staff itself has to do the detailed empirical work to make such assessments. Moreover, the impact of a general liberalization of market access would likely vary across low-income countries, since some would be more adversely affected by the loss of existing preferential access.

<sup>19</sup>Although IMF staff surveyed for the evaluation identified absence of clear guidelines as of only moderate significance in explaining why there has not been more change in the IMF's way of doing business, the case studies and interviews with staff indicate that this is because the general assumption has been one of a “hands-off” approach to the broader policy debate.



ESAF activities in FY1999.<sup>20</sup> PRGF countries in Africa appear to have received even less staff resources than other PRGF countries: on average of 2¾ full-time equivalent staff years a year as against 3¾ staff years for non-African countries.<sup>21</sup> These are small teams to conduct all of the tasks now expected. Not surprisingly, IMF staff surveyed for the evaluation identified internal resource constraints as one of the major factors constraining changes in the Fund's role. Indeed, the general impression we received during interviews was that staff often feel overwhelmed by the various procedural requirements, with too little time to devote to analytical and capacity-building activities.

- The implications of the new approach for the modalities of the IMF's work have not been fully examined, in particular the relative weight to be given to "informing the debate" and "direct negotiation" activities and the relative roles of resident representatives and missions from headquarters.

(ii) *Vague criteria for assessing IMF performance have resulted in mid-course assessments of the initiative that give insufficient feedback on*

<sup>20</sup>Data are taken from the IMF's internal Budget Reporting System. These costs vary from year to year, depending on the intensity of PRGF operations and HIPC-related activities. However, a similar result was obtained for FY2002.

<sup>21</sup>Figures are from the "Report of the Task Force on the Organization and Management of the African Department" (IMF, 2004c). They include staff from nonarea departments (e.g., PDR) regularly assigned on a part-time basis to missions, but do not include resident representatives.

*what the IMF should be doing differently.* The lack of concrete indicators on what the IMF is expected to be delivering limited the changes in the IMF's way of doing business, in the sense that specific priorities for program and surveillance activities were rarely spelled out or linked systematically to the countries' own priorities, as indicated in the PRS. A lack of sufficient accountability and feedback is present both at the country level and initiative-wide. It also reflects the fact that neither JSAs, nor reports on Progress in Implementation of the PRSP approach (which usually build on the former) undertake to assess systematically IMF performance.

- (iii) *Government reluctance to open the policy debate.* Some country case studies indicate that a major obstacle to progress has been the government's reluctance to open up the process to a broader domestic debate on macroeconomic policy issues—as opposed to social sector and some other sectoral areas where much greater progress has been made. More generally, a country's political and institutional conditions may not be conducive to the change in the mode of IMF engagement envisaged by the PRS approach. Countries that have made most progress in this regard have established an institutionalized structure for seeking the views of stakeholders (e.g., Tanzania and Mozambique). The establishment and functioning of such a framework requires first and foremost government willingness and active engagement. The IMF can encourage the process, but cannot substitute for the government in initiating it.

## Is the New Approach Making a Difference?

### Key Messages

*The most significant improvements in domestic policy processes include a better diagnosis of the nature of poverty and greater inclusion of various groups. The latter indicates some strengthening of ownership, but in macroeconomic policy areas it remains narrowly based.*

*Feedback into the broader policy debate in macroeconomic and related structural areas remains limited. However, when a more informed debate and broadening of the policy space did take place on these issues, the policy outcome was generally positive. In contrast, when controversial issues involving difficult trade-offs were avoided during the PRS process, the consequences for “downstream” policies were generally unfavorable.*

*There has been some strengthening of domestic public accountability—an essential element in the approach—but there is also evidence that undue focus on BWI procedures hampers the development of systems of domestic accountability. The lack of involvement of parliaments is a concern, as is the disconnect in some cases between the “participatory” framework and normal political processes. In most countries, the PRS process is still a long way from providing a strategic “road map” for setting priorities and resolving trade-offs, backed by institutional arrangements for implementation.*

*BWI measures of the quality of policies and institutions suggest that PRS countries generally started out in a better position than non-PRS countries but did not improve at a faster pace. Important exceptions are public sector management, transparency, and accountability, where some gains have been made, but there is still a long way to go. Trade restrictiveness has also declined more in PRS/PRGF countries than in other low-income countries.*

*Short-term growth outcomes for PRS/PRGF countries do not show much change from earlier periods, although these countries seem to have weathered the worsening of the external environment in 2000–02 better than other low-income countries.*

*Evidence on poverty-related outcomes, drawn from the parallel OED evaluation, are still too limited to draw definitive conclusions. The most notable improvements are with respect to various input- and output-related measures (e.g., construction of schools and number of teachers, school enrollment, vaccination rates, and expansion of water facilities). But outcomes such as maternal and infant mortality rates have generally not improved.*

Thus far, we have examined the PRS/PRGF process commenting on intermediate-stage inputs and outputs and the role of the IMF. As pointed out in Chapter 1, progress toward the ultimate objectives such as poverty reduction can be credibly assessed only over a much longer time frame. However, it is possible to evaluate what has changed with respect to the two key intermediate outcomes that are likely to be critical to the achievement of longer-term goals: (i) the nature of domestic policy processes; and (ii) actual policies. We also examine the available evidence on aid flows and short-term growth response as well as the initial limited evidence on various poverty indicators. It should be borne in mind that prudence is required in attributing the changes observed to the PRS approach, as the nature of the changes and data limitations make it impossible to test causality in any robust way.

### Changes in Nature of Domestic Policy Processes in Macroeconomic and Related Areas

The adoption of the PRS and PRGF frameworks was expected to improve domestic policy processes because of (i) improved diagnostics feeding into a policy debate that considers a wider range of policy options and pays greater attention to poverty and growth effects; (ii) a deeper sense of ownership and national commitment regarding the poverty reduction and growth strategy; (iii) improved public accountability; and (iv) clearer priorities and design of public actions. Many aspects of these intermediate objectives have been discussed in earlier chapters. Here, we summarize a number of core messages, drawing upon additional evidence from the case studies. In particular, we have traced through the effects of the new approach on a number of specific policy issues in each of the case studies, asking whether a broader policy debate took place on each particular issue; whether a consideration of alternative options was triggered (i.e., was the “policy space” broadened); and what was the outcome in terms of policies actually implemented. We also reviewed evidence from the case studies on the extent to which institutional arrangements in three areas—macroeconomic policy formulation, policy implementation (especially links to the budget process), and monitoring and evaluation—are adapting to the PRS/PRGF approach. The country-specific assessments are summarized in Annex 9. The following main messages emerge:

- (i) *The quality of poverty diagnosis has improved in most cases with more attention to non-income aspects, but there has been less progress*

*in improving other analytical inputs into growth strategies. Significant feedback into the broader policy debate in macroeconomic and related structural areas has been relatively infrequent.*<sup>1</sup>

When a more informed debate and a broadening of the policy space did take place (e.g., the fiscal strategy in Tanzania, petroleum taxation in Mozambique, and tax reform in Nicaragua), the policy outcome was often positive, but these instances were not very frequent. A more common occurrence was for controversial structural issues to be avoided during the PRS process—typically with the result that “downstream” policy discussions were handled in traditional negotiating frameworks, often resulting in failure of policies to address adequately the underlying issue.

- (ii) *There is some limited evidence of strengthened ownership, but it remains more narrowly based in the areas of macroeconomic and related policies and should not be taken to imply “consensus.”*

Despite its limitations, the participatory process does seem to have added value in most cases—including through fostering a greater inclusion of various groups. Once again, this impact was greater on policy issues outside the macroeconomic area but there is some evidence of enhanced ownership of macroeconomic policies *within* the narrow official circle. The case studies suggest that the potential value added of the PRS approach with regard to this objective varies enormously depending on a country’s circumstances and political structure. The approach as implemented did not allow sufficiently for these differences. In cases (e.g., Vietnam) where there was already a strongly country-owned approach to the development strategy, the potential contribution of a separate PRS approach to developing a “shared vision” was limited; alternative approaches aimed at adapting/influencing the existing domestic process may have achieved similar results more effectively, avoiding the creation of parallel processes.

The most desirable situation is one where the PRS approach strengthens ownership by working through normal political processes. The evidence on how well this has been achieved is mixed. On many issues there does not appear to have been much connection between the “participatory” framework and

<sup>1</sup>In areas beyond the IMF’s primary responsibility, the OED evaluation notes that strategies in the health and education sectors are most developed, although some of this predates the PRSP. There has also been some improvement in coordination across sectoral strategies.

the regular political process. The debate over Nicaragua's growth strategy is one obvious example. In this context, the lack of involvement of parliaments is a concern. However, in some cases, issues concerning the overall strategy have begun to be addressed as part of the electoral process (e.g., user fees in several African countries), and electoral and PRS processes seem to have reinforced each other in raising the profile of governance issues in many countries.

(iii) *There has been some success in achieving greater public accountability but there is a long way to go.*

Individual country experiences vary widely, but overall the PRS approach (and the HIPC Initiative) has generated some momentum toward public accountability through a delineation of concrete expected results and participatory monitoring and evaluation of these results. However, starting conditions were such that deep institutional changes will be required, of which only the first steps are under way even in best performance case.

Significant efforts have been made to put monitoring and evaluation systems in place, and gradual progress continues to be made over time. However, some efforts have been overelaborate for existing domestic capacity.<sup>2</sup> Workable institutional linkages for taking monitoring results and feeding them into the domestic policy (e.g., budgetary) process are crucial. Most countries are still not at this stage, but some of the more mature PRS cases (e.g., Mozambique and Tanzania) have made progress. In terms of budgetary accountability, strengthened public expenditure management systems are the key. Here the evidence suggests that progress is being made, albeit gradually. Most countries for which assessments are available are still a long way from achieving "good" standards (see Chapter 4).

It is important that the focus should be on building capacity by improving *domestic* systems and not on generating reports on the PRS for the BWIs and other donors. There are some suggestions in the case studies that concentration on ad hoc efforts to satisfy reporting requirements to the BWIs may hamper improvements in domestic accountability systems, which need to be anchored on improved regular budgetary processes.

(iv) *A mixed picture on improved setting of priorities and design of public actions.*

The process was expected to lead, over time, to the establishment of an operationally meaningful

<sup>2</sup>The parallel OED evaluation discusses monitoring systems in more detail. It highlights as a common problem attempts to track too many indicators.

growth and poverty reduction strategy composed of (i) *strategic guidance, or a "road map," for setting priorities and resolving trade-offs* between competing objectives; and (ii) *working institutional arrangements for implementing, monitoring, and updating this road map*. Our findings for each of the IEO country case studies are summarized in Table 6.1. The following messages emerge:

- To date, no country has both components of such an operational framework. Vietnam comes closest, but the development plan—rather than the PRS per se—provides much of the strategic framework.
- Progress is being made over time in some countries (e.g., Mozambique and Tanzania) to put in place the institutional arrangements for implementing/updating the strategic road map.
- More generally, the three-way linkage between the PRSP, medium-term expenditure framework, and budget is typically poor, reflecting some combination of limited costing and prioritization in the PRSP and the generally poor state of PEM.<sup>3</sup> Of these, the PEM weaknesses are probably the most fundamental challenge, requiring comprehensive institutional reforms and capacity improvements without which any enhanced prioritization in the PRSP will remain wishful thinking.

One would not necessarily expect very rapid progress toward a fully fledged operational road map and implementation framework in, say, the first round of a country's PRSP. However, it is hard to see how the central elements of the PRS initiative could be achieved without substantial progress toward such a framework.<sup>4</sup> The evaluation suggests three important elements that must be part of any way forward. First, PRS-specific institutional arrangements operating in parallel with existing domestic processes are unlikely to be able to cope in a sustainable manner with the breadth and complexity of issues at stake and may well distract from efforts to strengthen existing domestic processes that should be the primary focus of attention. Second, the PRS must include a discussion of key elements of the macroeconomic strategy, and of what priorities will

<sup>3</sup>This point draws on Bevan (2004).

<sup>4</sup>The Joint Note on Supporting the PRS Process in Africa, prepared by the staffs of the European Commission and World Bank comes to a similar conclusion. See European Commission and World Bank (2003). Indeed, they argue that establishment of a common operational framework, including modalities for donor commitments of budgetary support, is essential for moving toward a more effective partnership model without which "there is a very real risk that the PRSP could become just another fad, adding work rather than reducing transaction costs."

**Table 6.1. Assessment of Progress in the Country Cases Against Two Possible Intermediate Objectives<sup>1</sup>**

Country	Is there a country-driven strategy and decision-making process that provides an operational road map for achieving growth and poverty reduction and resolving trade-offs? <sup>2</sup>	Are working arrangements in place for implementing, monitoring, and updating this road map? <sup>2, 3</sup>	Is progress toward these two objectives continuing and what should the IMF be doing to help the process?
Guinea	Country-driven strategy includes some macroeconomic policy and related structural reform elements. However, the strategy provides limited strategic guidance to decision making for lack of relevant macroeconomic framework and discussion of trade-offs and contingency plans. The strategy mostly consists of broad objectives, with little detail as to their operationalization or indication of how trade-offs would be handled.	<p>No specific arrangements for implementation; proceeding in piecemeal manner.</p> <p>No comprehensive monitoring arrangements outside of standard budget monitoring; some preexisting outcome indicators monitored.</p> <p>No arrangements for feedback of monitoring into policy formulation or updating of strategy.</p>	Process is stalled. IMF could help improve diagnostics base and strengthen capacity in its areas of competence and, on that basis, help operationalize the broad objectives/intentions stated in strategy. However, IMF has limited leverage on degree of institutionalization of the process and willingness of other donors to provide adequate funding.
Mozambique	The PARPA (PRSP) provides a country-driven strategy. Key operational decisions are made in the context of the preparation of the annual state budget and the accompanying annual Economic and Social Plan.	<p>Monitoring is geared to the preparation of reports to parliament on budget execution (quarterly) and review of the Economic and Social Plan (annual). The analytical content of the reports to parliament is weak.</p> <p>Capacity constraints are hindering implementation and monitoring. Monitoring by a group of donors providing direct budgetary support is by means of a common performance assessment framework (PAF).</p>	<p>A multifaceted program of public sector reforms is under way, including with technical assistance in PEM-related areas from the IMF.</p> <p>A Poverty Observatory (established in April 2003) is intended to focus on learning lessons from experience with implementation and providing feedback to policy formulation and implementation.</p>
Nicaragua	Initial strategy paper lacked fully developed growth chapter and the macroeconomic framework was superseded by events. Thus, there was little guidance for decision making in these areas. Relevant structural issues were mentioned (e.g., tax reform, and banking sector resolution) but not in a manner that provided strategic guidance.	Arrangements for implementation and monitoring are in the process of being strengthened but remain weak and uncoordinated. Updating of strategy, in particular the growth pillar, was difficult initially but has improved recently.	Modification of strategy is now under way after broadening of consultation in Nicaragua and discussions with donors. IMF could contribute to analysis of growth and macro-micro issues, and informing broader debate. PEM remains a key obstacle to implementation, and collaborative efforts to strengthen this area would be an important contribution.
Tanzania	As a document, the PRSP had large gaps and was primarily focused on social sector issues. As a process, however, institutional arrangements have been strengthened. The public expenditure review/medium expenditure framework (PER/MTEF) has in the past five years become the main avenue for public policy debate and strategy formulation. A macro subgroup focuses on macroeconomic issues. The PER/MTEF framework is credited for preserving priority expenditure in the face of sharp shortfalls in donor disbursements.	The updating of the “road map” is implicit in the structure of the PER/MTEF activities. Frequent meetings ensure that discussions remain current, while a national consultative meeting is held once a year to discuss issues and gather views from a broader constituency. A Poverty Reduction Support Group, comprising like-minded donors, monitors developments together with the government and the World Bank on the basis of a performance assessment framework (PAF). However, inputs of civil society on macroeconomic issues are still limited.	Although the PER/MTEF approach is generally deemed to be a success, with the country registering improvement in its expenditure management system (PEM), doubts have been raised on how efficiently PER/MTEF analyses (and thus priorities) are reflected in the budgets. Delays in donor disbursements are still a factor, domestic technical capacities are low, and politics often override these processes. The IMF could participate more in these broader processes—providing guidance on macroeconomic issues and requisite TA to boost capacity.
Tajikistan	The PRSP is not sufficiently prioritized to provide an operational road map.	<p>Neither the PRSP nor the public investment program is well integrated into the budget process.</p> <p>Arrangements for monitoring are not yet fully operational. A core set of intermediate indicators for measuring progress in implementation is yet to be established.</p>	There is ongoing work to strengthen the MTEF and to use it for integrating the public investment program into the budget process.



**Table 6.1 (concluded)**

Country	Is there a country-driven strategy and decision-making process that provides an operational road map for achieving growth and poverty reduction and resolving trade-offs? <sup>2</sup>	Are working arrangements in place for implementing, monitoring, and updating this road map? <sup>2, 3</sup>	Is progress toward these two objectives continuing and what should the IMF be doing to help the process?
Vietnam	Country-driven strategy for setting broad policy direction remains the regularly updated socioeconomic development plans. However, these plans are not well tied to clear actions or monitorable benchmarks. The PRS process has helped enhance the transparency of the policy debate and implementation of broad policy objectives. Originally, the PRSP was not well aligned with parts of the development plans, including the public investment program. An “infrastructure” chapter was added to the PRSP later.	An extensive system of indicators was developed to monitor implementation of the PRSP. However, the system—while comprehensive—is excessively ambitious relative to implementation capacity.	Increased transparency and monitoring of strategy, as well as expanded participation in deliberations, are helping make the government’s strategy more “operational.” There is significant interest within the government and civil society and among donors for the IMF to help build capacity across the various stakeholder groups to understand and participate in discussions of macroeconomic policy issues.

<sup>1</sup>The focus is on progress in the areas of macroeconomic and related structural issues. In all cases, the assessment is of what is happening with actual policy processes in the country, not on what the PRSP says as a document.

<sup>2</sup>See text for full definition of the objectives.

<sup>3</sup>For countries where they are available (i.e., HIPC cases), this assessment draws, inter alia, upon the results of the PEM benchmarking exercise

guide policies in the event of unanticipated developments. Third, most countries face tremendous technical capacity challenges in developing such a road map, often spanning several of the following critical areas: setting up databases, analyzing data, policy formulation, policy implementation and monitoring, developing macroeconomic frameworks, and mobilizing adequate external assistance. The BWIs should play a key role in helping countries diagnose the key capacity bottlenecks and mobilize support (including, where appropriate, through direct TA) to alleviate them.

## Evidence on What Has Happened to Actual Policies and Final Outcomes

In this section, we give our assessment on three questions. First, is there any evidence that the types of policies implemented in PRS/PRGF countries are different, in aggregate, from those implemented prior to the new approach, or from policies in low-income countries that have not availed themselves of the new initiative?<sup>5</sup> Second, what is happening to overall aid flows to countries engaged in the approach? Third, what is the preliminary evidence on growth and poverty reduction outcomes?

<sup>5</sup>Such “before-after” and “control group” comparisons are subject to well-known methodological problems and should not be interpreted as proving causation.

## Policy outcomes<sup>6</sup>

One way of assessing policy outcomes is to ask whether policies in PRS countries are moving in the direction that the BWIs themselves judge as appropriate. This clearly cannot be the only benchmark of initiative-wide progress, given the importance of domestic ownership and the tenuous nature of our understanding about country-specific links between policies and growth/poverty reduction, but it provides one useful frame of reference.

The most comprehensive available measure is the World Bank’s Country Policy and Institutional Assessment (CPIA) scores.<sup>7</sup> We draw on an OED analysis for groups of PRSP and non-PRSP countries to see

<sup>6</sup>Fiscal policy outcomes have already been discussed in Chapter 4.

<sup>7</sup>The CPIA gives the World Bank staff’s assessment of the quality of a country’s present policy and institutional framework. It includes 20 equally weighted dimensions in the overall rating of policy, encompassing economic management (comprising management of inflation and macroeconomic imbalances, fiscal policy, management of public debt, and management of the development program); structural policies (broadly covering trade, financial sector, and regulatory policies that determine the enabling climate for the private sector, as well as policies for environmental sustainability); policies for social inclusion/equity (covering policies for human resources development, gender, social protection, and equity of resource use); and public sector management and institutions (comprising public financial management, quality of public administration, control of corruption, and rules-based governance). Each dimension is rated on a six-point scale. The ratings for individual countries are not made public.

**Table 6.2. CPIA Ratings for PRSP and Non-PRSP Groups of Low-Income Countries**

	PRSP Countries <sup>1</sup>			Non-PRSP IDA Countries <sup>2</sup>		
	1999	2003	Percent change	1999	2003	Percent change
Overall rating	3.36	3.47	3.3	2.78	2.91	4.7
Rating by policy category						
Economic management	3.76	3.77	0.3	2.91	2.93	0.7
Structural policies	3.43	3.46	0.9	2.83	3.01	6.4
Social inclusion policies	3.33	3.53	6.0	2.83	3.00	6.0
Public sector management	2.99	3.19	6.7	2.57	2.68	4.3
Memorandum items (selected components of rating categories)						
Competitive environment for the private sector <sup>3</sup>	3.54	3.60	1.7	2.84	2.96	4.2
Quality of budgetary and financial management <sup>4</sup>	3.12	3.46	10.9	2.54	2.73	7.5
Transparency, accountability, and corruption in public sector <sup>4</sup>	2.81	3.08	9.6	2.45	2.61	6.5

<sup>1</sup>Thirty-five countries with PRSPs at end-2003.

<sup>2</sup>Covers 28 IDA countries without PRSPs at end-2003; excludes small island states.

<sup>3</sup>A component of the “structural policies” category.

<sup>4</sup>A category of the “public sector management” category.

whether countries that successfully entered the PRS process had a different experience with respect to the “quality” of policies and institutions as measured by these scores. The results suggest the following:<sup>8</sup>

- Countries that entered the PRS process during 1999–2003 (i.e., 35 countries) already had, at the outset, stronger average policy settings, as measured by the CPIA ratings, than other low-income countries (Table 6.2).
- Improvements in the overall policy rating from 1999 to 2003 have been modest for low-income countries as a group, and there was no significant difference between PRSP and non-PRSP countries.
- The only area where PRSP countries improved their CPIA performance more than non-PRSP countries was with regard to public sector management and institutions, even though they already started out with a better policy setting in this area. The largest improvements were in the areas of the quality of budgetary management and transparency, accountability and corruption in the public sector. This suggests that the emphasis on public expenditure management issues is producing some benefits.
- With regard to structural policies, PRSP countries had “better” policies than non-PRSP countries

at the outset, but the gap is closing. With regard to external trade, however, a different data set, drawing on IMF measures of trade restrictiveness and average import tariff rates, suggests that trade regimes in countries with PRSPs and/or PRGF-supported programs were liberalized at a somewhat faster pace, on average, than in other low-income countries (Table 6.3).<sup>9</sup>

- Since improvements in the quality of policies and institutions take time, one might expect that our sample of 23 “mature” PRSP countries (i.e., with over a year of implementation experience) would have stronger gains than more recent PRSP countries (i.e., those finalized in 2003). However, this was not the case. In the area of “economic management” policies, which are of most direct relevance to the IMF, only countries with later PRSPs showed policy gains.

These findings call for some caution in attributing to the PRS process credit for institutional and policy improvements across low-income countries.

### Aid flows

To examine what has happened to aid flows to countries involved in the PRS/PRGF approach, we divided the sample of low-income (i.e., PRGF-eligible) countries into three groups: (i) the 46 countries with PRGF (or converted ESAF) arrangements in place

<sup>8</sup>We focus on areas within the IMF’s primary responsibility. Such statistical associations do not prove causation, especially given the likelihood of two-way influences (i.e., countries may have PRSPs because they have “better” policies, as judged by the BWIs, rather than vice versa).

<sup>9</sup>This comparison is only to determine what actually happened vis-à-vis these aspects of trade regimes. We make no judgments as to whether the sequencing, and so on was appropriate, which would go beyond the scope of this evaluation.

**Table 6.3. Selected Policy and Outcome Indicators for PRGF-Eligible Countries<sup>1</sup>***(In percent of GDP and period averages, unless otherwise indicated)*

	PRGF 2000–02					
	Total <sup>2</sup>		Of which PRSP 23 <sup>3</sup>		Other PRGF eligible <sup>4</sup>	
	1997–99	2000–02	1997–99	2000–02	1997–99	2000–02
Fiscal balance including grants	–4.8	–4.7	–3.6	–4.9	–4.1	–5.4
Government revenues and grants	20.8	22.2	20.4	21.5	25.7	26.4
Government expenditure and net lending	25.5	26.9	24.0	26.5	29.8	31.8
Current account balance	–8.9	–8.0	–8.3	–6.9	–8.3	–6.0
International reserves (months of imports; end of period)	3.5	4.7	3.8	5.0	3.5	4.1
External debt (end of period)	105.8	99.7	97.9	92.2	58.6	57.9
GDP growth (in percent)	3.8	4.0	4.8	4.4	4.3	1.8
Change in terms of trade	0.7	–0.6	1.4	–2.0	3.0	3.1
Trade restrictiveness rating (end of period) <sup>5</sup>	4.0	3.1	3.7	2.1	5.5	5.0
Average tariff rate (end of period)	15.2	13.0	14.0	12.6	20.2	20.7

Sources: IMF (2002e and 2003d).

<sup>1</sup>Covers 72 countries for which data are available in WEO.<sup>2</sup>Covers 46 countries that had ESAF/PRGF arrangements in place during 2000–02.<sup>3</sup>Covers 23 countries that had full PRSPs at end-2002.<sup>4</sup>Covers 26 PRGF-eligible countries that did not have a PRGF arrangement in place during 2000–02.<sup>5</sup>Based on the IMF's "Trade Restrictiveness Rate." Countries are rated on a scale of 1 (few restrictions) to 10 (highly restrictive).

during 2000–02; (ii) the subgroup of 23 countries with full PRSPs at end-2002; and (iii) other countries that had not used the approach.<sup>10</sup>

On average, the PRSP countries received higher aid flows than non-PRSP countries, and program countries received more aid than non-program countries, but much of this difference reflected starting conditions (Figure 6.1). For example, the PRSP group of countries were already commanding a higher proportion of aid flows on a per country basis at the outset of the initiative.<sup>11</sup>

Since an analysis using broad groups cannot distinguish the influence of the precise timing of the PRSP, we also looked at the aid paths for individual countries. Only nine countries with full PRSPs had sufficient data to make an assessment of pre- and post-PRSP aid flows.<sup>12</sup> Of these, six countries received

higher aid after the PRSP (Bolivia, Burkina Faso, Mauritania, Mozambique, Tanzania, and Uganda), while average aid flows declined in three cases (Albania, Honduras, and Nicaragua).

This evidence is inconclusive regarding the impact of the PRSP process so far on the overall selectivity of aid flows. In contrast, evidence discussed in the OED report indicates that World Bank lending to PRSP countries did expand faster than to other IDA countries.

### Growth and poverty outcomes

Although it is too early to judge the impact on long-term growth and poverty reduction, there is some evidence on short-term outcomes, especially for growth. However, one has to bear in mind what was happening to the overall external environment. The period immediately preceding the introduction of the PRSP/PRGF was characterized by a favorable external environment, reflected in improving terms of trade (Table 6.3 and Figure 6.2). In contrast, the 2000–02 period was characterized by a deteriorating terms of trade for countries involved in the PRSP/PRGF approach. Despite this deterioration, average growth in these countries was largely unchanged. (It improved marginally in the group of countries with PRGF-supported programs and declined marginally in the subgroup of countries with full PRSPs.) In sharp contrast, growth performance deteriorated significantly for countries not participating in the approach, even though they were the only group that did not suffer a

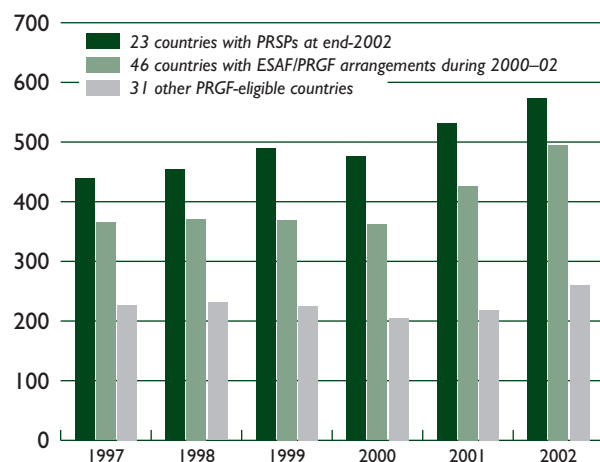
<sup>10</sup>Data on net official development assistance (ODA) is from the OECD Development Assistance Committee (DAC) database and is only available on a comprehensive basis through 2002. Consequently, we are not yet able to assess systematically what has happened to aid flows for later PRSP cases.

<sup>11</sup>Distinguishing PRSP countries by the maturity of their involvement in the process does not appear to alter this result: OED results suggest that the more "mature" PRSP countries were larger aid recipients at the outset but that overall aid to them did not expand faster than to other IDA countries.

<sup>12</sup>We compared average aid flows in the three years before the PRSP to average flows in the years after the PRSP. The comparisons can be distorted by aid associated with natural disasters. This factor tends to bias upward "post-PRSP" aid in Mozambique and bias it downward in Nicaragua and Honduras.

**Figure 6.1. Average Net ODA Flows to Groups of Low-Income Countries**

(In millions of U.S. dollars)



Source: OECD.

deterioration in the external terms of trade. However, while such patterns reveal interesting associations, they cannot prove causation. They suggest that countries involved with the PRS/PRGF approach have done better than other low-income countries in these early stages, but there has not yet been a marked pickup in growth that will be necessary for a substantial lasting impact on poverty levels.

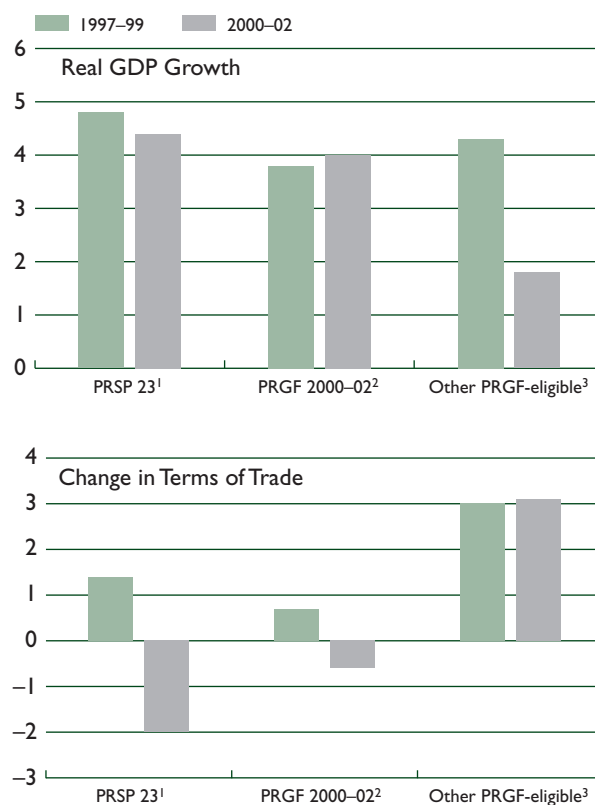
We relied upon the parallel OED evaluation for assessments of progress toward the various poverty indicators and, more generally, toward the MDGs. We also draw upon the recent *Global Monitoring Report* (World Bank and IMF, 2004a). An overriding message is that very limited data is available yet for assessing progress vis-à-vis these fundamental objectives. However, the following broad messages put the overall initiative in context:

- At the global level, the first MDG goal of halving income poverty between 1990 and 2015 will likely be met. However, this largely reflects improvements in Asia, especially in two countries (China and India) that are not involved in the PRS approach, sub-Saharan Africa is seriously off track—with only 8 countries representing only 15 percent of the region's population projected as likely to achieve the goal (Table 6.4).<sup>13</sup>

<sup>13</sup>See World Bank and IMF (2004a, Chapter II). These projections are based on long-term economic scenarios prepared by World Bank staff and on specific assumptions about income distribution (i.e., essentially unchanged, as measured by the Lorenz

**Figure 6.2. Growth and Change in Terms of Trade**

(In percent)



Sources: IMF (2002e and 2003d).

<sup>1</sup>Twenty-three countries with PRSPs at end-2002.

<sup>2</sup>Forty-six countries with ESAF/PRGF arrangements during 2000-02.

<sup>3</sup>Twenty-six other PRGF-eligible countries.

- The risks of shortfalls are more widespread with respect to the human development goals. With current trends, several regions will achieve or approach the goal of providing universal primary education, but shortfalls are likely in sub-Saharan Africa and possibly in South Asia, and Middle East and North Africa as well. Prospects are gravest in health; only a small proportion (15–20 percent) of countries is likely to reach the goals for reducing child and maternal mortality or for access to safe drinking water and basic sanitation by 2015.
- These global and regional trends mask considerable variation across countries. Among the case

curve, except for China and India). Such projections are inevitably highly tentative.

**Table 6.4. Progress Toward the Income Poverty Goal**

	Annual Average Growth Rates (2004–15) Scenario		Population Living Under \$1 a day					
	Per capita		Headcount (In percent)			Number of persons (In millions)		
	GDP	GDP	1990	2000	2015	1990	2000	2005
East Asia and Pacific	6.0	6.3	29.4	14.5	2.3	470	261	44
Europe and Central Asia	3.9	3.8	1.4	4.2	1.3	6	20	6
Latin America and Caribbean	2.3	3.7	11.0	10.8	7.6	48	56	46
Middle East and North Africa	2.3	4.1	2.1	2.8	1.2	5	8	4
South Asia	4.0	5.3	41.5	31.9	16.4	466	432	268
Sub-Saharan Africa	1.8	3.8	47.4	49.0	42.3	241	323	366
Total	3.7	4.7	28.3	21.6	12.5	1237	1100	734
Excluding China	3.0	4.1	27.2	23.3	15.4	877	896	692

Source: World Bank staff estimates, taken from World Bank and IMF (2004a).

**Table 6.5. Progress Toward Meeting the Millennium Development Goals in 12 Mature PRSP Countries<sup>1</sup>**

	Number of Indicators Specified	Availability		Improvement Between 1999 and 2003?
		Number of indicators	Number of countries	
1. Eradicate extreme hunger and poverty	6	1	3	Yes
2. Achieve universal primary education	4	1	12	Yes
3. Promote gender equality and empower women	4	3	8	Yes (2 of 3)
4. Reduce child mortality	3	3	12	No (3 of 3)
5. Improve maternal health	2	0	0	Unknown
6. Combat HIV/AIDS, malaria, and other diseases	10	1	8	Yes
7. Ensure environmental sustainability	8	1	12	Yes
8. Develop a global partnership for development	17	4	8	Yes

Source: OED (2004).

<sup>1</sup>The 12 countries are Albania, Burkina Faso, Ethiopia, Honduras, Malawi, Mauritania, Mozambique, Nicaragua, Niger, Tanzania, Uganda, and Vietnam.

study countries, the most spectacular progress was made in Vietnam, which reduced income poverty from 51 percent to 14 percent in little more than a decade.

- For the PRSP countries, the OED analysis focused on the set of 12 countries that had issued at least one PRSP progress report. Nine of these country progress reports contained data on quantitative targets linked to poverty reduction. The data indicate notable improvements with respect to some inputs and outputs, but not much change with respect to final outcomes. Thus, for example, there have been (i) increases in gross primary school enrolment rates, the construction of schools, and the number of teachers; (ii) some improvements in the supply of drugs to health centers and in vaccinations; and (iii) expansion of water facilities. By contrast, out-

comes such as maternal and infant mortality rates have remained stagnant, and in many countries the poor quality of service delivery in both education and health continued.

- OED analyzed progress toward the MDGs in the same set of 12 countries. As Table 6.5 indicates, relevant data are available for only about one-third of the 49 specified UN indicators. In critical areas such as extreme poverty and maternal health, data are available only in a few countries or for a few years or for a single indicator. OED concludes that, based on these limited data, there have been modest improvements in literacy rates, including those of women, and the control of tuberculosis, but that infant mortality rates appear to have stagnated, a finding echoed by the case studies.





## Survey of PRSP Stakeholders

### Global Results

As part of the OED and IEO evaluations of the PRSP process and the PRGF, a survey of PRSP stakeholders was administered in each of the ten countries where a case study was undertaken. The objective of the survey was to obtain perceptions of the PRSP process and the role of the World Bank and IMF in supporting the initiative.

A standard survey of 39 questions was administered in each country. The full questionnaire can be found on both of the evaluation websites: [www.worldbank.org/oed/prsp](http://www.worldbank.org/oed/prsp) and <http://www.imf.org/external/np/ieo/2002/prsp/index.htm>. The survey consists of four main components: information on respondents; the PRSP process (covering ownership, results orientation, comprehensiveness, partnership orientation, and long-term perspective); World Bank performance; and the role of the IMF. In most cases, respondents were asked to indicate the extent of their agreement with statements on a five-point scale.<sup>1</sup> The survey was translated, into local languages, where necessary, and pre-tested. A local consultant with survey experience was engaged in each country to assist with administration of the survey. Survey results were coded by the local consultant and sent back to Washington, and an outside contractor, Fusion Analytics, was hired to analyze the data.

The survey was targeted at key groups within the three main categories of PRSP stakeholders: government, civil society, and international partners.<sup>2</sup>

<sup>1</sup>The five-point scales used in most questions offered a range from 1: “Completely Disagree” to 5: “Completely Agree.” Respondents could also mark 0 for “Don’t Know or Unsure.”

<sup>2</sup>Fourteen stakeholder groups were identified: government—central government, line ministries, and sector agencies, local government, parliament; civil society—local NGOs, business sector, labor unions, academia, media, religious organization, political party; and other international partners—donor, I-NGO.

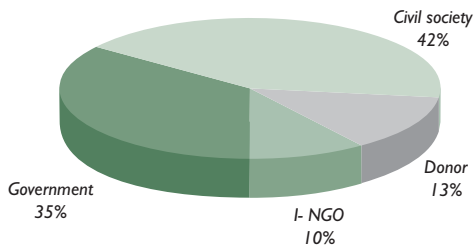
Within each group, the survey sought to obtain an *institutional view* and was targeted at the most knowledgeable individuals. Respondents were asked to define the nature of their involvement in the PRSP process, and their level of familiarity with the PRSP document, the Bank, and the IMF. Given the targeted nature of the survey, respondents who were “Not Aware” of the PRSP process were excluded from the results. The specific samples were selected using three main inputs: information gained through the country case study mission; participants listed in the PRSP document; and input from the local consultant. In some cases, samples were circulated to obtain broader input on their composition. The study teams also identified a set of highly relevant respondents in each country for whom a survey response was required. These included core ministries and agencies (such as finance, economy, and central bank), key PRSP-related ministries (such as health, education, agriculture), and major donors. Survey questionnaires were tracked in order to ensure responses were obtained from key groups; however, individual respondents could choose to remain anonymous.

The following section presents aggregate findings from the survey applied in *all ten countries*. Section A provides an overview of the survey respondents, including the nature of involvement and familiarity with the process. Section B provides an aggregated snapshot of stakeholder perceptions of the PRSP process across each of five main subcategories. Section C provides the mean results for all questions concerning the role and effectiveness of Bank and Fund support. Section D presents results for questions with the most positive and negative responses and questions where there was the greatest consensus or disagreement on issues.

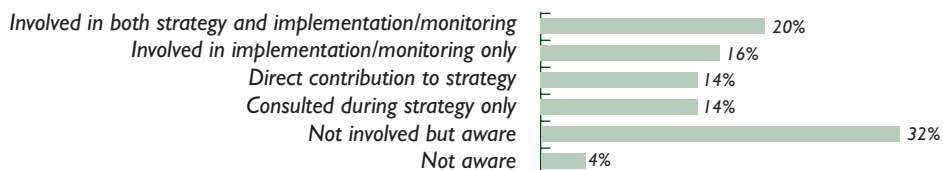
Results at the stakeholder group level will be presented in the aggregate analysis across all countries.

### A. Respondent Characteristics

1. Composition of respondents  
(n = 779)



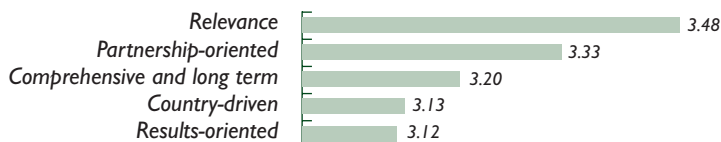
2. Nature of involvement  
(In percent)



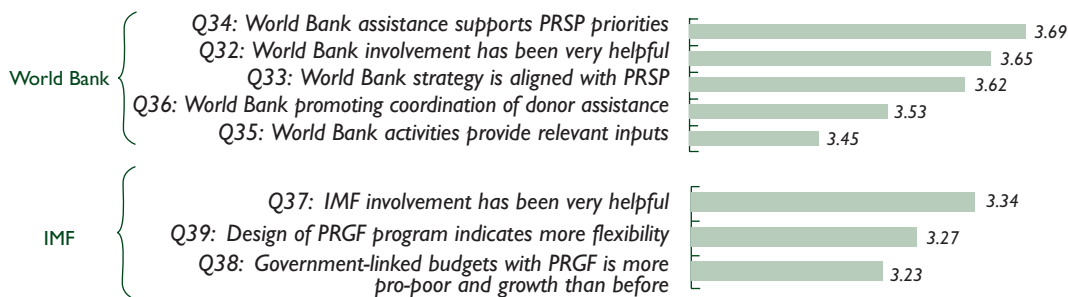
3. Level of familiarity

PRSP document	56 percent
World Bank	51 percent
IMF	33 percent

### B. The PRSP Process<sup>1</sup>



### C. World Bank and IMF<sup>1</sup>



<sup>1</sup>Based on a five-point scale, where 1: "Completely Disagree" to 5: "Completely Agree." Respondents could also mark 0 for "Don't Know or Unsure."

## D. Composite Results Table

	Percent “Agree” or “Completely Agree” (4 or 5)	Percent Neutral (3)	Percent “Disagree” or “Completely Disagree” (1 or 2)	Mean	Standard Deviation	Percent “Don’t Know or Unsure” (0)
<b>Most positive</b>						
Q8: Relevance: PRSP is a good model	59	30	11	3.69	1.06	7
Q9: Relevance: PRSP adds value	58	28	14	3.64	1.08	9
Q10: Relevance: PRSP improves on past modalities	57	30	13	3.61	1.05	11
Q25: Partnership-oriented: Donors supported formulation	56	24	20	3.57	1.15	16
Q16: Results-oriented: Outcomes benefit poor	55	26	19	3.56	1.15	8
<b>Most negative</b>						
Q18: Results-oriented: Structure to monitor results	28	31	41	2.84	1.17	21
Q19: Results-oriented: Results feedback	31	32	37	2.96	1.16	24
Q22: Comprehensive: Macroeconomic framework participatory	38	27	35	3.03	1.25	17
Q17: Results-oriented: Realistic targets and plans	38	28	34	3.14	1.16	9
Q21: Comprehensive: Alternatives fully explored	35	32	33	3.01	1.12	18
<b>Most polarized</b>						
Q15: Country-driven: Government continues to engage stakeholders	48	19	33	3.23	1.42	13
Q13: Country-driven: Your stakeholders were consulted	45	22	33	3.20	1.33	11
Q14: Country-driven: Final document was modified to accommodate viewpoints	44	25	31	3.16	1.29	19
Q22: Comprehensive: Macroeconomic framework participatory	38	27	35	3.03	1.25	17
Q12: Country-driven: PRSP driven by national stakeholders	42	28	30	3.24	1.25	8
<b>Greatest consensus</b>						
Q30: Partnership-oriented: Quality of Bank-Fund collaboration	52	32	16	3.44	1.01	46
Q28: Partnership-oriented: Current donor coordination	34	39	27	3.03	1.02	18
Q29: Partnership-oriented: Coordination between World Bank and IMF improved	46	35	19	3.36	1.04	48
Q10: Relevance: PRSP improves on past modalities	57	30	13	3.61	1.05	11
Q8: Relevance: PRSP is a good model	59	30	11	3.69	1.06	7
<b>Most unfamiliar</b>						
Q29: Partnership-oriented: Coordination between World Bank and IMF improved	46	35	19	3.36	1.04	48
Q30: Partnership-oriented: Quality of Bank/Fund collaboration	52	32	16	3.44	1.01	46
Q19: Results-oriented: Results feedback	31	32	37	2.96	1.16	24
Q27: Partnership-oriented: Donor coordination improved	52	26	22	3.43	1.11	22
Q18: Results-oriented: Structure to monitor results	28	31	41	2.84	1.17	21

Note: The percentages of those who “Agree,” are “Neutral,” or “Disagree” relate to the total that responded to each question. The percentage of “Don’t Know or Unsure” is calculated on the basis of the total respondents in the survey (779). “Most Positive” were chosen on the basis of the highest percentage who agreed or completely agreed, picking the top five means—but with the number of respondents in each case determining the ranking. Likewise, “Most Negative” were selected on the basis of the highest percentages who disagreed or completely disagreed and the five lowest means. The “Most Polarized” responses and those indicating “Greatest Consensus” were those with the five highest and lowest standard deviations, respectively. “Most Unfamiliar” were the highest percentage of responses indicating that they “Didn’t Know or Were Unsure.”

## ANNEX 2

# Results from Survey of IMF Staff<sup>1</sup>

### Methodology

The survey was undertaken during December 2003 and January 2004. It targeted mission chiefs and resident representatives for PRGF-eligible countries. A total of 75 IMF staff responded, about 40 percent of the targeted universe. The questions focused on the formulation of the PRGF-supported program, the role of the Fund in the implementation of the PRSP/PRGF initiatives, JSAs and Bank-Fund collaboration, and internal IMF procedures and incentives.

### Main messages

- While there was broad consensus among staff on the impact of the PRSP/PRGF initiatives on the Fund's way of doing business, that is, that it meant a better orientation toward poverty reduction (Figure A2.1), positions were generally more divergent with regard to issues of attribution—notably the causes of the policy gaps and slow implementation of the various facets of the new approach.
- The staff's overall assessment of the various aspects of the PRSP/PRGF process is positive.

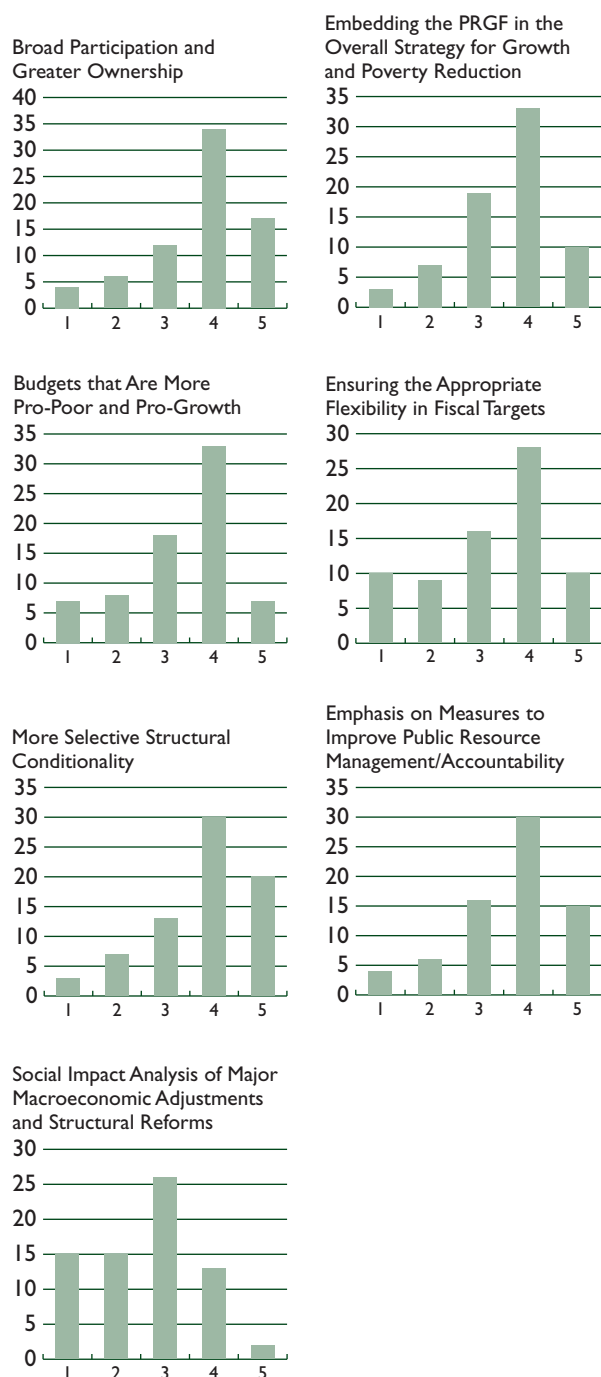
<sup>1</sup>Most questions featured a five-point scale, where 1 was the lowest degree and 5 the highest. A "Don't Know/Not Applicable" category was also available for cases where the respondent's own experience did not allow for a response. This annex summarizes the results. A more detailed presentation will be put on the IEO website as a background document when the main report is published.

However, on a number of issues considered integral to the process, such as a participatory approach or PSIA, IMF staff indicated a lack of clarity as to the level and extent of IMF involvement.

- Staff perceived that the PRSP/PRGF process had, as a whole, improved the manner in which they conduct Fund business, both within the IMF itself—poverty issues are now highlighted to a greater degree in the process of program design—and in their collaboration with the World Bank and interaction with the broader donor community during program implementation. Notably, the factors driving these processes were seen by staff to be broader than the mere streamlining of conditionality.
- Respondents indicated that further progress is impeded by the slow change in IMF institutional culture. Missions are still constrained in terms of size and time, and the new approach has not led to more policy space for country-driven options. Generally, respondents did not support the view that the PRSP/PRGF process had led to a significant change in the way initial policy positions are discussed and established within the IMF.
- JSAs were found by IMF staff to be useful in providing feedback to the authorities and as an independent expert assessment of the PRSP to third parties, notably civil society and donors. Moreover, the majority of staff considered them to be candid.

### Figure A2.1. IMF Staff Responses on the Impact of the Key Features of PRGF-Supported Programs on Their Conduct of Fund Business<sup>1</sup>

(1=No impact; 5=Highly significant impact)



Source: IMF staff survey database for this evaluation.  
<sup>1</sup>Y-axis represents number of responses.



ANNEX  
**3**

# PRSP Sourcebook: Does It Provide Adequate Space for Policy Flexibility, and Is It Based on Strong Empirical Evidence?

Policy Prescription in the PRSP Sourcebook <sup>1</sup>	Does the Policy Prescription Allow an Appropriate Degree of Flexibility in the Policy Space? <sup>2</sup>	Is the Policy Prescription Well Supported by Empirical Evidence on the Links Between Policies and Growth or Poverty Reduction? <sup>3</sup>
<b>A. Macroeconomic stability</b>		
1. Macroeconomic stability is necessary for growth. (12.2.2)	Yes (statements are very general).	Yes—but debates about what stability “thresholds” should be.
2. Macroeconomic instability hurts the poor – Inflation hurts the poor (a regressive tax) and, beyond certain thresholds, curbs output growth. (12.2.3) – Economic crises/instability have a longer-term adverse impact on poverty (e.g., through hysteresis effects). (12.2.3)	Yes (acknowledges substantial “gray area”).  Yes.	Robust cross-country evidence is limited, but statements are quite contrary.
3. For countries where macroeconomic imbalances are not severe, a range of possible macroeconomic targets is consistent with the objective of stabilization. (12.2.5 and 12.3)	Yes.	Yes.
4. In adjusting to external shocks, since there is inevitable uncertainty about whether they are temporary or permanent, it is usually wise to assume that an adverse shock will persist. Countries in macroeconomic crisis typically have little choice but to stabilize quickly, but for countries in gray area of partial stability, finding the right pace may prove difficult. In some cases, a lack of financing will drive the pace of stabilization. (12.3.2)	Partial (overly prescriptive on how to respond to shocks).	Too country-specific to generalize.
5. In some cases, lack of financing will drive the pace of stabilization. Where financing is not a constraint, policy makers will need to weigh various factors on a case-by-case basis when choosing the most appropriate pace of stabilization. (12.3.3)	Yes—quite general, but acknowledges critical role of financing availability.	Yes.
<b>B. Fiscal policy</b>		
1. There are no rigid predetermined limits on what would be an appropriate fiscal deficit, which should be assessed on the basis of the medium-term outlook and the scope for external budgetary assistance. (12.4.1 and 12.4.2)	Yes.	
2. Governments can reduce the procyclical nature of their fiscal policies by saving the windfalls that follow positive shocks and using the savings as a buffer for expenditure against negative shocks. A cautious approach would be to treat every favorable shock as temporary and every adverse one as permanent.	No (too prescriptive on the fiscal policy response to shocks).	No.

Policy Prescription in the PRSP Sourcebook <sup>1</sup>	Does the Policy Prescription Allow an Appropriate Degree of Flexibility in the Policy Space? <sup>2</sup>	Is the Policy Prescription Well Supported by Empirical Evidence on the Links Between Policies and Growth or Poverty Reduction? <sup>3</sup>
3. There is a strong case for allowing higher grants to translate into higher spending, to the extent that those grants can reasonably be expected to continue, but there may be absorptive constraints. In the absence of medium-term commitments, policymakers should be cautious in aid projections. (12.4.2)	Yes.	
4. Tax policy should move toward a system of easily administered taxes with broad bases and moderate marginal rates. (12.4.2 and Box 12.4)	No (the description of the contents of the “best tax systems” is quite detailed and does not discuss potential trade-offs).	Considerable case study experience on components of an effective tax system, but poverty effects of decisions on coverage etc. can be very country specific (e.g., Ethiopia PSIA of tax reforms).
5. Governments should take into account the extent to which public sector borrowing crowds out the private sector’s access to credit, but at times public sector borrowing can “crowd in” private investment by financing critical infrastructure. Domestic budgetary financing should take account of the relative productivity of public and private investment. (12.4.2)	Broadly yes—but no acknowledgment of risks that speed of response of private sector may be overstated.	
<b>C. Monetary and exchange rate policies</b>		
1. Set a single objective for monetary and exchange rate policy: the achievement of low and stable inflation (i.e., a single-digit rate, the precise target depending on a country’s inflation history and level of development). (12.4.3)	Broadly yes; single-digit threshold for inflation.	Yes—although there is some debate on the precise inflation threshold linked to good growth performance, and evidence on poverty links are less robust.
2. Credibility can sometimes be enhanced by imposing restrictions on policy (e.g., limiting the discretion of the monetary authorities, including through various nominal anchors) or by adopting specific institutional arrangements. In the long run, however, only policies to which the authorities are fully committed can be credible, and imposing restrictions on policy in the absence of such commitment can be disastrous. (12.4.3)	Yes.	
3. The pros and cons of fixed versus flexible exchange rate regimes need to be assessed carefully—there is no universal right answer. (12.4.3).	Yes.	Very general statement.
<b>D. Policies to insulate the poor against shocks</b>		
1. The resources allocated to social safety nets should be protected during adjustment, when fiscal tightening may be necessary. (12.4.4)	Yes.	
2. It is important that safety nets be operating before an economy is hit by a shock. However, if they are not, “second best” social protection policies may be necessary. (12.4.4)	Yes.	
3. Relaxing foreign currency controls in a well-managed fashion can give the poor access to safer assets, such as foreign currency, that can protect them from shocks that lead to devaluation. (12.4.4)	No (overly prescriptive—goes beyond the evidence).	No.
4. Severe financial repression, such as controlled interest rates, can impede the ability of the poor to save. Properly managed, financial liberalization policies can have the additional benefit of increasing self-insurance for the poor. (12.4.)	Partial (broader risks associated with a mishandled sequence of financial liberalization are not emphasized).	

<sup>1</sup>The policy prescriptions described here are a summary of those contained in Chapter 12 (“Macroeconomic Issues”) of the PRSP Sourcebook. The policy recommendation assessed is the more complete description contained in the Sourcebook and not just the summary given here. Section references are to the Sourcebook chapter.

<sup>2</sup>The purpose is not to provide a judgment on the merits of the policy advice per se, but to assess whether it can be interpreted as signaling a reasonable degree of policy flexibility to guide a homegrown policy debate.

<sup>3</sup>In some cases, no entry is made on the “supporting evidence” because the policy prescription in the preceding column is very general and essentially calls for a case-by-case assessment.

ANNEX  
**4**

# Assessment of the Adaptation of the IMF's Internal Policy Process

**Table A4.1. An Assessment of the Adaptation of the IMF's Internal Policy Process Between the ESAF and the PRGF Based on Briefing Papers for a Sample of 23 PRGF-Eligible Countries Between 1999 and 2003**

Issues for Assessment	Comments on Changes in Policy Approach as Indicated by Comparisons of ESAF- and PRGF-Related Benchmark Briefing Papers	Average Rating of ESAF and PRGF Benchmark Briefing Papers and Highest Scoring Briefs <sup>1</sup>			
		ESAF		PRGF	
		Average rating of brief (1–4)	Percentage of briefs scoring 3 and above	Average rating of brief (1–4)	Percentage of briefs scoring 3 and above
<b>A. Briefing papers</b>					
1. Does the brief discuss links between the PRSP and the PRGF objectives?	Not done under ESAF. PRGF links to the PRSP are discussed in detail by majority of PRGF briefs.	n.a.	n.a.	3.18	82
2. In resolving the key issues identified by the mission does the brief leave room for discussions on the specific policies to be adopted to achieve the objectives of the poverty reduction strategy (i.e., are a range of possible policy options considered in key areas?)					
1. Macro stabilization	Overall, PRGF briefs did not present a broader range of possible policy options to the authorities than those of the ESAF nor did they leave room for discussion on specific policy issues. PRGF briefs were generally prescriptive and change was incremental at best.	2.1	38	2.2	35
2. Public finance		1.7	9	2.3	35
3. Financial sector		1.9	9	2.2	31
4. Macro-critical <sup>2</sup>		2.2	50	2.1	21
5. Structural areas <sup>3</sup>		1.7	6	1.8	9
<i>Overall</i>		1.9	22	2.1	26
3. Are alternative macroeconomic frameworks and the trade-offs between them considered?	Given the complex nature of the actual and potential shocks facing the sample countries, alternative macroeconomic frameworks were not fully fledged and trade-offs were rarely sufficiently discussed.	1.4	4	2.1	39
4. Does the brief discuss how the program will protect key objectives in the event of unanticipated negative shocks?	A large number of PRGF briefs address the issue of protecting key objectives in the event of unanticipated shocks, including adjustments in the expenditure framework.	1.8	30	2.3	52
5. Does the brief allow for flexibility to use additional concessional external financing if available?	Considerable flexibility in the use of additional concessional external financing was already achieved under the ESAF, and there was not much change under the PRGF.	2.4	57	2.3	52
6. Is a participatory process in resolving key issues considered?	Key policy discussions were generally confined to official circles and there was very little attempt to seek input from other stakeholders.	n.a.	n.a.	1.9	22

Table A4.1 (concluded)

Issues for Assessment	Comments on Changes in Policy Approach as Indicated by Comparisons of ESAF- and PRGF-Related Benchmark Briefing Papers	Average Rating of ESAF and PRGF Benchmark Briefing Papers and Highest Scoring Briefs <sup>1</sup>			
		ESAF		PRGF	
		Average rating of brief (1–4)	Percentage of briefs scoring 3 and above	Average rating of brief (1–4)	Percentage of briefs scoring 3 and above
7. Does the brief identify policy issues where poverty and social impact analysis (PSIA) inputs would be necessary/useful? (Explain precisely what was proposed/done on PSIA in comments section.)	The importance of PSIAs is highlighted by many briefs. However, inputs during implementation were assumed to come from the government and other agencies, while methodological and capacity constraints were not discussed.	n.a.	n.a.	2.6	57
<b>B. Review departments' comments</b>					
8. Is the need for more “policy space” for homegrown options recognized in the review process? (The focus of this question is not on the magnitude of adjustment but on how prescriptive review comments were.)	The review process did not put much emphasis on creating policy space for homegrown options—by, for example, encouraging a more participatory approach to policy formulation. This was then mirrored in the briefs' relatively inflexible approach to policy formulation, as indicated above.	1.2	4	1.9	22
9. Are poverty issues discussed or their absence highlighted in review departments' comments?	Review departments insisted on raising the profile for poverty and social expenditure issues, including PSIA, in the majority of briefs, explaining to a large extent the increased emphasis on poverty and related issues seen in the PRGF briefs.	1.8	26	2.5	52
10. Did review departments press for more or less conditionality (prior actions, performance criteria, structural benchmarks) in the policy areas specified by the mission?	Compared to the ESAF briefs, PRGF briefs were less inclined to press for more conditionality. However, this is mostly true for countries that had established credibility with the IMF (via a successful ESAF program, for example). For “early stabilizers” conditionality did not decline by much.	1.4	13	2.4	48

<sup>1</sup>The ranking scheme is based on the degree of consistency with the PRSP/PRGF approach: 1 = Highly inconsistent; 2 = Inconsistent; 3 = Consistent; 4 = Highly consistent (see Table A4.2 for the criteria used in the ranking).

<sup>2</sup>Including governance (financial transparency and anticorruption), trade liberalization, and debt sustainability.

<sup>3</sup>Including privatization and SOE reform, public sector reform, private sector development, capacity building, agricultural sector and land reform, forestry sector policy, industrial sector reform, and other reforms.

**Table A4.2. Coding Scheme for the Cross-Country Task on Briefing Papers and Department Reviews<sup>1</sup>**

Numbers in Parentheses Refer to Assessment Reached	
<b>Section I. Briefing paper</b>	
<b>A. Issues and timing</b>	
(i) Key policy issues to be addressed by the mission (specify in each case, with a focus on major issues).	Examples of policy issues (but add specifics in “comments” section): Fiscal policy Trade liberalization Privatization Civil service reform Public expenditure reform Monetary policy Financial sector reform Governance
(ii) Was PRGF launched before full PRSP?	Yes/No; provide date of full PRSP.
<b>B. Contents of briefs</b>	
(i) Does the brief discuss the links between the PRSP and the PRGF objectives?	(1) No linkage (mere mention of poverty not enough). (2) Discussion of poverty issues and references to PRSP but no indication of how the two are linked. (3) Some discussions of PRSP strategy and objectives and of links with PRGF proposals, but not comprehensive. (4) Comprehensive discussion of key objectives and strategy of PRSP and of how proposed PRGF program will be integrated with them.
(ii) In resolving the issues identified in A above does the brief leave room for discussion, based on domestic policy debate, on the specific policies to be adopted to achieve the objectives of the poverty reduction strategy? (i.e., are a range of possible policy options considered in key areas?) (specify for each policy issue).	(1) Brief leaves no policy space (i.e., sets objectives and specifies policies). (2) Brief leaves room for discussion of a narrow range of policy alternatives. (3) Brief leaves room for discussion of a broad range of policy alternatives. (4) Policy options not restricted in discussions of objectives and analyses of key trade-offs.
(iii) Are alternative macroeconomic frameworks and the trade-offs between them considered?	(1) No discussion of alternative frameworks. (2) Limited discussion of an alternative macroeconomic framework (but no discussion of potential trade-offs). (3) Alternative macroeconomic framework and trade-offs discussed but implications for PRSP objectives not analyzed in depth. (4) Alternative macroeconomic frameworks, potential trade-offs between them, and their implication for overall PRSP objectives clearly analyzed.
(iv) Does the brief discuss how the program will protect key objectives in the event of unanticipated negative shocks?	(1) No discussion of potential shocks or of how program would adapt to them. (2) Risk of shocks is discussed but no discussion of trade-offs between adjustment and financing or how to protect key objectives. (3) Potential shocks are identified and mix of financing and adjustment discussed, but no significant discussion of implication for key objectives and how to protect them. (4) Potential shocks are identified; trade-offs between adjustment and financing clearly analyzed; and potential strategy for preserving key objectives is set out.
(v) Does the brief allow for flexibility to use additional concessional external financing, if available?	(1) Brief proposes a specific fiscal deficit target, with no flexibility for use of additional concessional financing. (2) Some limited flexibility to accommodate additional inflows. (3) Proposed program allows for significant flexibility in accommodating additional financing, but no systematic discussion of implications for key PRSP objectives. (4) Brief discusses implications of different levels of external financing for achievement of PRSP objectives, and lays out an explicit strategy on how the program will accommodate additional inflows.
(vi) Is a participatory process in resolving key policy issues considered?	(1) Not discussed. (2) Consultations with donors, NGOs etc., by Fund staff are suggested but no indication of how the results will be incorporated into program design. (3) Discusses a broad strategy for seeking views of all key stakeholders on the major program design issues. (4) Clear recognition that program design issues should draw upon a participatory process included in the PRSP and sets out a clear strategy for Fund participations in such a debate.
(vii) Does the brief identify policy issues where poverty and social impact analysis (PSIA) inputs would be necessary/useful? (Explain precisely what was proposed/done on PSIA in comments section.)	(1) No discussion of PSIA. (2) Identifies broad policy issues where poverty/social impact may be significant, but no discussion of actual impact or of how PSIA will be brought to bear on these issues. (3) Areas where PSIA is needed are identified, but no comprehensive strategy for use of PSIA is set out. (4) PSIA undertaken, even if in limited manner, before policy decisions are taken.



**Table A4.2 (concluded)**

Numbers in Parentheses Refer to Assessment Reached	
<b>Section 2. Department Reviews<sup>2</sup></b>	
(i) Is the need for more “policy space” for home-grown options recognized in the review process? (The focus of this question is not on the magnitude of adjustment but on how prescriptive review comments were.)	<ul style="list-style-type: none"> <li>(1) Review comments remain highly prescriptive in content.</li> <li>(2) Reviews suggest some limited alternative policy options, but no recognition that authorities should be given more “policy space.”</li> <li>(3) Significant range of alternative policy options suggested.</li> <li>(4) Explicit recognition in review comments that approach should be one of identifying broad objectives and helping authorities implement homegrown options to achieve these objectives.</li> </ul>
(ii) Are poverty issues discussed or their absence highlighted in review department comments?	<ul style="list-style-type: none"> <li>(1) Not discussed.</li> <li>(2) Poverty issues mentioned but discussion shallow.</li> <li>(3) Review comments on macro and related policies are explicitly linked to the broader poverty objectives.</li> <li>(4) Staff urged to be more proactive in the poverty reduction strategy (e.g., references to “key features of PRGF-supported program”).</li> </ul>
(iii) Did departments press for more or less conditionality (prior actions, performance criteria, structural benchmarks) in each of the areas specified in A? (specify) <sup>3</sup>	<ul style="list-style-type: none"> <li>(1) More conditionality demanded, with no indication of priority or streamlining.</li> <li>(2) Recognition that streamlining (to the Fund’s core areas) required, but wide conditionality pressed for in core areas and requests that Bank strengthen its conditionality in other areas.</li> <li>(3) Strong emphasis on streamlining conditionality, but no link to ownership or consideration of aggregate level of Bank-Fund conditionality.</li> <li>(4) Review departments recognize that ownership and streamlined conditionality are linked, and that any conditionality should be closely associated with PRSP core objectives. Aggregate level of Fund-Bank conditionality explicitly considered.</li> </ul>

<sup>1</sup>The grading scheme had the following scale: 1 = Highly inconsistent; 2 = Inconsistent; 3 = Consistent; 4 = Highly consistent.

<sup>2</sup>Coverage of review department comments will be mainly on the basis of PDR, but comments from other departments (such as PDR, FAD, MFD, and RES) where substantive program design issues are raised are also noted.

<sup>3</sup>“Not applicable” could be used here to indicate that conditionality was not discussed at all.

## ANNEX 5

# Modalities of Participatory Processes: How Broad-Based Has Participation Been?

Many of the countries concerned had no tradition of participatory policy formulation (e.g., Albania, Cambodia, and Tajikistan). Others did have a participatory tradition or experience, but a separate participatory process was launched nonetheless, in order to comply with HIPC/BWI conditionality (e.g., Mozambique and Vietnam).

The participatory process was generally organized by the authorities according to modalities of their own choosing. However, in practice, donors—including the World Bank, but not the IMF (which rarely intervened in discussions on modalities of the participatory process) frequently had a strong influence on the process, primarily because they funded it, but sometimes also because the authorities themselves did not show much interest, at least initially (e.g., Nicaragua and Vietnam), and/or did not know how to proceed, especially in the absence of organized representation of civil society (e.g., Albania, Tajikistan, and Vietnam).

### Who Participated?

In all the country case studies, good efforts were made to involve government stakeholders beyond the department coordinating the process, as well as the donor community. The involvement of civil society was generally more patchy. It is to be expected that country choices vary with respect to the involvement of specific interest groups (such as religious organizations and indigenous groups) according to their relevance in each country. However, the following crosscutting issues surfaced from both our case studies and broader evidence from outside sources:

- (i) Parliaments were generally not significantly involved.<sup>1</sup>

<sup>1</sup>In Ethiopia and Nicaragua, the authorities view parliamentarians as key stakeholders, but in the latter case opposition parties refused to engage for political reasons. In Guinea, Tanzania, and Vietnam, parliaments were given an opportunity to review the final document. This finding is consistent with those of external literature (see, for instance, Stewart and Wang, 2003).

- (ii) Criteria for selecting civil society representatives lacked transparency and/or a clear rationale, giving rise to criticism of poor representativity and pro-government political bias of the stakeholders chosen (especially in Guinea and Mauritania).
- (iii) The involvement of the business sector was often unsatisfactory, either because they were not called in to participate in the participatory process (in Tajikistan) or because they felt that the modalities of their involvement did not allow them any substantive role (in Albania, Mauritania, and Nicaragua), leading to their withdrawal. In some cases, however (Guinea and Ethiopia), private sector representatives were relatively satisfied with both their involvement and their contribution to the process.
- (iv) Involvement of stakeholders at the decentralized level was sometimes neglected (e.g., in Mauritania).
- (v) Also left out of the process in most cases were the poor themselves. As a result, some commentators have characterized participatory processes as opening up policy space only to the benefit of a technocratic elite expert in development issues, but little qualified to speak for the poor.<sup>2</sup>

These limits are echoed by the results of the survey of PRSP stakeholders, with government stakeholders and donors broadly agreeing that their respective interest groups were adequately consulted, and civil society in mild disagreement with that view.

### How Was Participation Organized?

In most cases, several modalities of consultation were used in combination. The most commonly used

<sup>2</sup>See, for instance, Bretton Woods Project (2003).

Table A5.1. Summary Evaluation of the Types of Participation in Macroeconomic and Related Areas<sup>1</sup>

Country	PRSP Design Stage <sup>2</sup>				PRSP Implementation Stage <sup>3</sup>			
	Information sharing?	Consultation?	Joint decision making?	Initiation and control by stakeholders?	Information sharing?	Consultation?	Joint decision making?	Initiation and control by stakeholders?
IEO case studies								
Guinea	Partial	Yes	No	No	Limited	No	No	No
Mozambique	Yes <sup>4</sup>	Yes	No	No	Yes	Yes	No	No
Nicaragua	Yes <sup>4</sup>	Yes	No	No	Yes	Partial	No	No
Tajikistan	Yes	Yes	No—but detailed recommendations by civil society	No	Partial	Limited so far	No	No
Tanzania	Yes	Yes	No	No	Yes	Yes	Partial—some institutionalized feedback	No
Vietnam		No <sup>5</sup>	No	No		No <sup>5</sup>	No	No
OED-only case studies <sup>6</sup>								
Albania	Partial	Yes	No	No	Partial	No	No	No
Cambodia	Partial	Partial	No	No	n.a.	n.a.	n.a.	No
Ethiopia	Yes	Yes	No	No	Yes	Partial <sup>7</sup>	Partial <sup>7</sup>	No
Mauritania	Partial	n.a.	No	No	n.a.	n.a.	n.a.	No

<sup>1</sup>This table summarizes the IEO assessment of the extent to which different types of participation were implemented in each of the case studies. It draws upon the detailed discussion of the participatory process described in the individual country reports, but uses the categories of possible intensities of participation discussed in McGee and Norton (2000). In each case, the assessment is of the extent of participation in macroeconomic and related areas (including the composition of budgetary expenditures). Assessments of the intensity of participation would probably be higher in some social sector policy areas (e.g., health and education).

<sup>2</sup>McGee and Norton (2000) propose a more detailed disaggregation of the stages of the “design” cycle into “Diagnosis,” “Formulation,” and “Approval.” However, the intensity of the participatory process does not seem to have varied widely between such potential subcategories, so we have used a simpler classification.

<sup>3</sup>Includes monitoring and evaluation.

<sup>4</sup>In the case of Mozambique and Nicaragua, information about the fiscal consequences of banking crises—which had important implications for macroeconomic policy design and key trade-offs—were not shared with a broader group of stakeholders.

<sup>5</sup>Consultation on fiscal/monetary policy was limited in Vietnam, but this seems to have partly reflected a mutual agreement that the more pressing issues were elsewhere. Debate on key issues such as pace of state enterprise reform was significant, but took place within the traditional framework of the party.

<sup>6</sup>We have drawn upon the descriptions in the four country case studies undertaken by the OED alone to make an assessment of the degree of participation in the macroeconomic policy area. However, the summary judgments provided here are the responsibility of the IEO alone. In some instances, there is not enough information in the case study to make such a judgment and these have been indicated as “n.a.”

<sup>7</sup>In Ethiopia, the private sector influenced PRSP implementation via business organizations but there was no institutionalized dialogue mechanism for civil society.

format was large attendance workshops and conferences held at the national and, in most cases, also at the regional level, with large variations in stakeholder coverage and number of workshops organized. In several countries, a lot of background work for the PRSP—and some of the material subject to broader consultation—was prepared in working groups involving at least two of the three main stakeholder groups (i.e., government, civil society, and donors). While in Guinea and Mauritania these groups were ad hoc and ceased to meet after the formulation of the PRSP, a permanent structure has been put in place in Tanzania, building on the preexisting PER working groups. In Nicaragua, such a group was recently constituted on an ad hoc basis, to explore tax reform issues.

Several countries made attempts to hold direct consultations with NGOs and grassroots organizations, but these efforts were often impaired by the lack of organization of the sector. However, where

civil society already had a form of institutional representation (e.g., miscellaneous government sponsored NGO umbrella groups in Guinea, CONPES in Nicaragua, and mass organizations in Vietnam) consultation of these institutions formed a core part of the participatory process. In others, such CSO umbrella organizations were established for the occasion of the PRSP, either by the government (e.g., in Albania) or independently of it, with donor support (e.g., in Ethiopia, Nicaragua, and Tajikistan). In many of these cases, these (or other) civil society groups managed to prepare substantive inputs into the PRSP. Such inputs, while rarely called for, were welcomed in most cases (though not always taken into consideration). However, in Nicaragua, it was dissatisfaction with the official participatory process that led certain groups (in particular an NGO umbrella group and a group of municipalities) to develop their own alternative version of the PRSP.

# Qualitative Appraisal of Joint Staff Assessments

The IEO undertook a desk review of the 28 JSAs of full PRSPs issued through May 2003, involving a systematic analysis of their contents in areas of interest to the evaluation team. The table below pre-

sents the criteria used in assigning quality ratings to selected aspects of JSAs, as well as the average and median ratings obtained by JSAs in our sample for each of these aspects.

<b>JSA Assessment Matrix: Coding Scheme</b>	<b>Mean</b>	<b>Median</b>
I: Highly unsatisfactory    2: Unsatisfactory    3: Satisfactory    4: Highly satisfactory		
<b>Analysis of Risks to Successful PRSP Implementation</b>	<b>3.18</b>	<b>3</b>
1. Risks to PRSP implementation not discussed		
2. Discussion of risks is limited		
3. Risks adequately discussed but no remedial actions suggested		
4. Risks exhaustively discussed along with remedial actions		
<b>Clear and Candid Assessment of the Following Key Areas:</b>		
<b>A. Ownership and Participation</b>	<b>2.43</b>	<b>2</b>
1. Little or no description of participatory process and no discussion of ownership at all		
2. Incomplete discussion of country ownership and participation		
3. Good description of participatory process and discussion of ownership		
4. Extensive description of country ownership and participation and its impact on the content of the strategy		
<b>B. Targets, Indicators, and Monitoring</b>	<b>3.36</b>	<b>3.5</b>
<b>Criteria: (i) Realism, (ii) Consistency with priorities, (iii) Transparency/ Participatory methods for monitoring the PRSP, and (iv) Feedback into policy decisions</b>		
1. Partial description without assessment		
2. Good description but no assessment		
3. Good description and some assessment (1 or 2 criteria met)		
4. Full description and good assessment (3 or 4 criteria met)		
<b>C. Priority Public Actions</b>		
<b>C1. Macroeconomic Framework</b>	<b>3.04</b>	<b>3</b>
<b>Criteria: (i) Soundness, (ii) Realism, (iii) Trade-offs, and (iv) Robustness</b>		
1. No assessment at all		
2. Assessment of soundness only		
3. Assessment of soundness and some qualitative assessment		
4. Assessment covers soundness, realism, robustness, and discussion of trade-offs		
<b>C2. Fiscal Choices</b>	<b>3.14</b>	<b>3</b>
<b>Criteria: (i) Internal consistency, (ii) Quality of data and cost estimates, and (iii) Administrative capacity to deliver</b>		
1. No discussion at all		
2. Assessment covers only one criterion		
3. Assessment covers two criteria		
4. Assessment covers all three criteria		



<b>JSA Assessment Matrix: Coding Scheme</b>	<b>Mean</b>	<b>Median</b>
<p><b>C3. Financing Plan</b>  <b>Criteria: (i) Realism, (ii) Sustainability, (iii) Alignment, and (iv) Contingency plans</b></p> <p>1. No discussion at all                      2. Assessment covers only one criteria                      3. Assessment covers two criteria                      4. Assessment covers three or four criteria</p>	<b>2.79</b>	<b>3</b>
<p><b>Due Consideration of Country Situation</b></p> <p>1. No discussion of initial conditions                      2. Limited discussion of domestic context with respect to the PRSP                      3. Discussion of the country situation is adequate, but weakly linked to PRSP                      4. Country situation is well discussed as well as its links to the PRSP</p>	<b>2.81</b>	<b>3</b>

# Determinants of Targeted and Actual Fiscal Adjustment

This annex presents details of regression analyses that underlay some of the results discussed in Chapter 4. The regressions were based on data from 88 new arrangements approved by the IMF under either the ESAF or the PRGF during 1995–2003; 47 of the arrangements were approved as ESAFs and the rest as PRGFs.

## Methodology

In order to examine the relative importance of various factors in the setting of targets for fiscal adjustment in ESAF- and PRGF-supported programs, we estimated a regression model of the size of the targeted change in the government balance excluding grants, over the first and first two years of the program—that is, changes between  $T-1$  and  $T$ , and between  $T-1$  and  $T+1$ , respectively. We used the following as regressors: (i) the initial level of the government balance [ $g_{bal}(T-1)$ ]; (ii) the targeted change in the external current account balance [ $\Delta cab$ ]; (iii) the initial level of grants in the government budget [ $grants(T-1)$ ]; (iv) the projected change in the level of grants [ $\Delta grants$ ]; and (v) projected growth [ $growth$ ].<sup>1</sup>

We postulated a two-way relationship between targeted fiscal adjustment and targeted external cur-

rent account adjustment, and employed two-stage least squares (with robust standard errors) to account for the endogeneity of the targeted change in the external current account.

We replicated the regressions using outturn data in place of targeted/projected data in order to compare the determinants of targeted and actual fiscal adjustment.

## Results

We obtained broadly similar results for targeted fiscal adjustment under ESAFs and PRGFs over a two-year horizon: the targeted magnitude of fiscal adjustment was inversely related to the initial level of the fiscal balance and to the projected change in the level of grants (top half of Table A7.1). Specifically, over the two-year horizon, the targeted fiscal adjustment reflected a near-halving of the initial fiscal deficit and a full adjustment to projected change in the availability of grants.

The estimations using outturn data indicated significant influence of the initial fiscal balance and change in the level of grants as determinants of actual fiscal adjustment, but only for the initial program year of ESAFs (bottom half of Table A7.1). The limited number of observations for outturns under the PRGF suggest caution in interpreting the results for the PRGF, but the influence of the initial level of fiscal balance is no longer significant.

<sup>1</sup>All variables were measured as ratios to GDP, except growth, which was measured in percent a year.

**Table A7.1. Determinants of Targeted and Actual Fiscal Adjustment in ESAFs and PRGFs**

	ESAFs		PRGFs	
	Horizon T	Horizon T+1	Horizon T	Horizon T+1
Dependent variable: targeted fiscal adjustment				
Constant	-1.60*	-2.6	0.56	2.53
<i>gbal</i> (T-1)	-0.25**	-0.46***	-0.29	-0.52**
$\Delta cab$	0.33	0.32*	0.52	0.22
$\Delta grants$	-0.43**	-0.98**	-1.04*	-1.11***
<i>grants</i> (T-1)	-0.16	-0.51**	-0.43	0.65
<i>growth</i> (T)	0.19	-0.08	-0.08	0.48
<i>growth</i> (T+1)		0.47		-0.96
N	44	43	40	39
Dependent variable: actual fiscal adjustment				
Constant	-1.6**	-1.97	-5.15	-6.37
<i>gbal</i> (T-1)	-0.32**	-0.14	-0.60	-0.31
$\Delta cab$	-0.13	-0.36	1.02	0.89
$\Delta grants$	-0.46**	-0.52	1.23	0.32
<i>grants</i> (T-1)	-0.27	-0.11	-0.20	0.46
<i>growth</i> (T)	0.13	-0.06	0.14	0.14
<i>growth</i> (T+1)		0.29		0.29*
N	45	45	32	23

Note: The asterisks denote levels of statistical significance: \* = 10 percent, \*\* = 5 percent, and \*\*\* = 1 percent.

ANNEX  
**8**

# Composition of Targeted Changes in Expenditures and External Financing in IMF-Supported Programs

## The Composition of Programmed Fiscal Adjustment

As discussed in Chapter 4, *PRGF-supported programs target, on average, greater increases in revenues and smaller expenditure cuts than their ESAF counterparts*. These results are reinforced by looking at the distribution of targeted changes in expenditures in ESAF- and PRGF-supported programs. Figure A8.1 shows that whereas most ESAF arrangements project expenditure reductions (Panel A), a majority of PRGF-supported programs accommodate higher expenditures (Panel B).

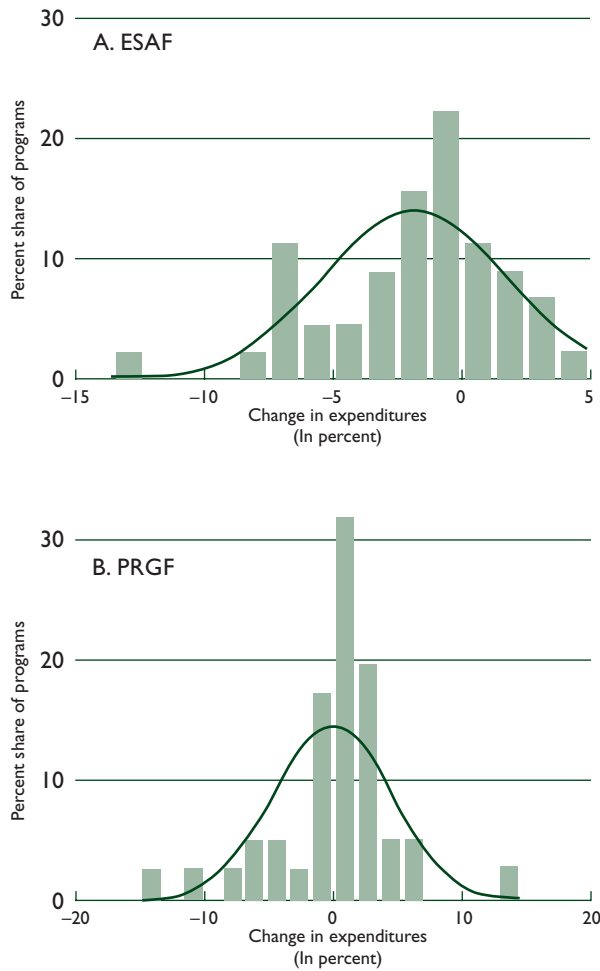
Another way of studying the evolution of projected revenues and expenditures in PRGF-supported programs is to regress the programmed change in expenditures (or revenues) on a number of variables that might be expected to affect these targets (i.e., previous expenditure/revenue levels, GDP growth, targeted fiscal adjustment, etc.) and include a dummy variable to measure the impact of PRGF-supported programs. The dummy variable should capture changes in programmed expenditures (or

revenues) due to the introduction of the PRGF, controlling for other factors that might be expected to influence the setting of expenditure (or revenue) targets. The results of this exercise suggest that, *holding all else constant, PRGF-supported programs target total expenditure levels about 1.6 percent of GDP higher than their ESAF counterparts*. Similarly, controlling for all else, PRGF-supported programs target a similar increase in revenues.

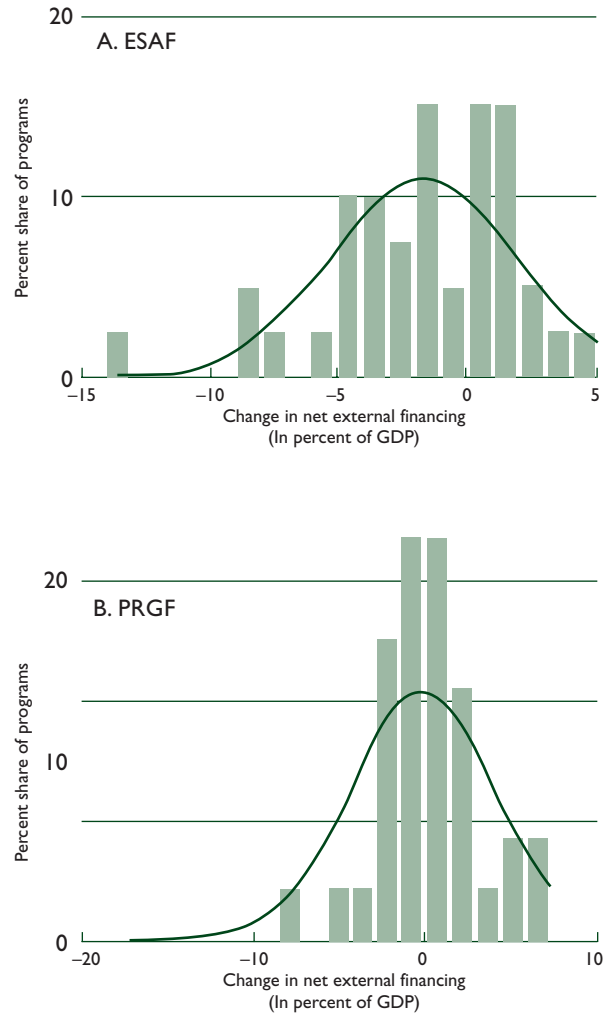
## The Availability of External Financing

Figure A8.2 shows that there is a great degree of variability in the projected amounts of net external public sector financing in both ESAF- and PRGF-supported programs. However, the center of the distribution shifts substantially to the right in the case of PRGF-supported programs. On average, while PRGF-supported programs project increases in the availability of external budget financing in the first two program years, they project a strong decline in the third year.

**Figure A8.1. Distribution of Programs According to the Targeted Change in Expenditures**



**Figure A8.2. Distribution of Projected Changes in the Availability of Grants and Concessional Loans in ESAF- and PRGF-Supported Programs**





## Changes in Domestic Policy Processes and Institutions: Evidence from Case Studies

**Table A9.1. What Happened to Domestic Policy Formation Under the PRSP Approach? Some Examples from the Case Studies**

Country and Policy Issue	Did a Broader-Based Policy Debate Take Place on the Issue?	Did the Debate Lead to a Broadened Policy Space, e.g., Considering Additional/ Alternative Options?	Outcome
<b>Guinea</b>			
1. State enterprise reform	No.	No.	Still no country-owned strategy that could be supported by the IFIs.
2. Governance	Yes, initially under the pressure of donor conditionality. Debate started prior to PRSP process but was substantially amplified by it.	Yes. Debate led to large range of solutions being considered, taking a very broad view of governance problems.	Comprehensive strategy defined, emphasizing decentralization and capacity building as a solution. Very limited progress in implementation. Governance problems remain pervasive, at all levels of government. Local CSOs supported BWI conditionality in this area.
<b>Mozambique</b>			
1. Petroleum tax increase	No broad-based debate but the IMF and the authorities agreed to await the outcome of a PSIA on the impact of the measure before its implementation.	The PSIA considered two main scenarios on updating the specific tax that had not been adjusted for five years: (i) increase the tax in line with exchange rate movements (a 100 percent increase in the tax); and (ii) increase the tax in line with domestic inflation (a 65 percent increase in the tax).	The PSIA concluded that “the aggregate short-term impact of a rise in fuel tax on poverty is modest.”  The tax on petroleum products was increased by an average of 62.5 percent in May 2003.
2. Rationalization of tax incentive and exemptions	No broad-based debate; the measures were recommendations of an IMF technical assistance mission.	No.	The government initially complained to the IMF that the recommendations were “unhelpful” but was subsequently persuaded to implement some of the measures.
<b>Nicaragua</b>			
1. Growth strategy	Not initially, but consultation later on pushed by donor community (see Box 2.1).	Initially, the debate was not opened up, as the new government chose not to “rock the boat” (and delay progress on HIPC debt relief) even though it disagreed with the growth strategy in the PRSP. Subsequently, however, a broader debate did begin.	New growth strategy endorsed at Consultative Group meeting and work in progress to determine how to modify PRSP.
2. Tax reform	Debate took place in the context of a technical commission comprising representatives of various domestic stakeholders.	Yes, IMF showed greater flexibility to reform design, provided expected net revenue was maintained.	Tax reform approved. Passage of reform in assembly eased by IMF flexibility to design considerations.
3. Bank restructuring	No—but proposed approach was “owned” by key government officials.	No—although some debate did take place ex post on the choices made on “burden-sharing.”	Strategy for bank restructuring was determined by the authorities.

**Table A9.1 (concluded)**

Country and Policy Issue	Did a Broader-Based Policy Debate Take Place on the Issue?	Did the Debate Lead to a Broadened Policy Space, e.g., by Considering Additional/Alternative Options?	Outcome
<b>Tajikistan</b>			
1. Gas tariff reform and compensation to poor households	No broad-based debate.	No.	Provision was made in the budget for some compensation to poor households. However, the initial compensation scheme was ill-designed. It would have been better to have undertaken a proper PSIA before implementation of the tariff increase.
2. Limit on external borrowing to finance PIP	No broad-based debate.	No. Although not part of the formal conditionality in the PRGF-supported program, it is generally understood to be an important condition for completing program reviews.	The authorities went along with the limit, albeit reluctantly, because they thought it constrained their use of available concessional loans for growth-promoting public investments.
<b>Tanzania</b>			
1. Macroeconomic program design	Yes—but not as part of initial PRSP. Debate took place later within domestic framework (PER system).	Yes. A serious debate on fiscal and monetary policy design ensued, involving government, donors, and the IMF. Civil society largely uninvolved.	Substantial changes to program design were eventually made (see Box 4.2).
2. Trade policy	No. The bulk of trade-related reforms were undertaken before the launch of the PRGF and PRSP in 2000. Subsequently, no trade policy debate that was distinct from the broader macroeconomic issues has emerged.	Trade issues were mentioned with very little specificity in the PRSP, although the importance of ensuring that the poor shared in the benefits of globalization was stressed. In the absence of a broad domestic discussion—even the broadly participatory PER process has given it less attention than other issues—no alternative policy approaches were discussed.	Trade policy remains amenable to protectionist pressure from local producers. IMF staff have argued against such measures, but PRGF-supported programs have not included any trade-related conditionality.
3. Fiscal federalism	Although under implementation for close to a decade, local self-governance received renewed impetus under the PRS process—seen as a key point of departure for poverty eradication. Financial decentralization and the need to create local capacity for the management of public funds were natural consequences.	The IMF adopted a cautious stance on fiscal decentralization, warning that capacities at the local level were still very weak, and that expanding the process would have implications for the integrity of the central budget. The IMF did not press the government to abandon its plans, but did warn against rapid implementation and pushed for introduction at local levels of a more transparent and efficient financial management system.	Capacities at the local level have remained low, affecting the ability to monitor priority expenditures. The government has embarked on the training of local-level staff, with the assistance of local NGOs.
<b>Vietnam</b>			
1. State enterprise reform	The PRSP represented an “action plan” for the implementation of the five-year socioeconomic development plan that was approved at the Party Congresses in which various “mass organizations” were represented. Meaningful discussion affecting policy formulation did not take place in the context of the PRSP participatory exercise.	No, but the policy debate and resulting options were clearly country-driven.	Bank and Fund came to accept the authorities’ approach to SOE reform, albeit not until after pressing a privatization/equitization agenda at the start of the PRGF-supported program and in the context of the first PRSC.

**Table A9.2. Institutional Changes: Evidence from Case Studies**

Country	Macroeconomic Policymaking	PRSP Links to Budget	Monitoring and Evaluation
<b>Guinea</b>	Analysis and discussion of macroeconomic conditions and policies are conducted within a very narrow circle around the Minister of Finance and Governor of the central bank.	There are no systematic links between the PRSP policy matrix, sectoral strategies, expenditure plans of line ministries, and regional poverty reduction strategies. Nevertheless, budget allocations to designated priority sectors have been relatively protected from ad hoc cuts.	PRSP itself did not provide much detail on institutional arrangements for Monitoring and Evaluation. But a group was set up in October 2002 to: (i) determine set of indicators to be monitored; (ii) arrange for their production if not already available; and (iii) propose institutional arrangements for publication of indicators and for providing feedback from monitoring to updating and improving the PRSP.
<b>Mozambique</b>	There continues to be little public discussion of macroeconomic policy issues. Donors providing general budget support have formed a macroeconomic working group that discusses macroeconomic policy issues, but membership is limited to the donor community.	Integration of the PARPA (Mozambique's PRSP) into the government's planning, budgeting, and reporting processes is under way but at a slow pace.  An annually updated MTEF is the main instrument for translating PARPA priorities into budgetary allocations. But PEM system needs strengthening to ensure that budgeted funds reach spending units and that funds are spent as budgeted.	Targets vary considerably in scope and precision. In a few areas targets are yet to be specified (e.g., anticorruption).  Weak institutional capacity is adversely affecting the quality of monitoring.  A Poverty Observatory has been established to review PARPA implementation annually, with a focus on drawing lessons and making recommendations for improving implementation.  Role of nongovernment actors in PARPA monitoring not yet well defined.
<b>Nicaragua</b>	No significant movement toward opening up debate on the macroeconomic framework and alternative policy trade-offs. Recently, there seems to be some movement in the context of the new development plan.	Little linkage between the PRSP and the budget process.  Poor PEM system is a major hindrance to implementation of the PRSP.  Fragmentation of policymaking has generated problems for coordination and control over public finances.	The PRSP included a comprehensive set of targets and indicators for monitoring the impact of policies on the poor. Links between goals and intermediate indicators are clearly set out in the social area, but there are no intermediate indicators for the economic/production sectors.  A comprehensive system for monitoring and evaluation of PRSP implementation is being set up (SECEP, SINASIP).
<b>Tajikistan</b>	There was some public discussion of macroeconomic policy issues during the formulation of the PRSP process. But macroeconomic policy formulation on an ongoing basis seems to revolve around discussions between IMF staff and a handful of government and central bank officials.	There is a disconnect between the PRSP, the PIP, and the government budget process. In particular, the PRSP and the PIP appear to have different priorities (the former heavily tilted to social sectors and the latter to infrastructure).  Initial effort at an MTEF was based on only three sectors. Efforts are under way to broaden its coverage.	Five of nine main poverty reduction targets are linked to the MDGs.  The PRSP policy matrix contains some 200 indicators, most of which refer to processes and policy measures, rather than to outcomes. Work is under way to develop a more focused set of intermediate indicators.  A PRSP Implementation and Monitoring Unit has been established in the Presidency to coordinate monitoring and evaluation activities.
<b>Tanzania</b>	Macroeconomic policies now more frequently and openly discussed in broadly inclusive forums, but little impact of nongovernment actors on policy choices.	The PRS has provided a poverty-focused policy framework for budgeting that was lacking before. But spending within sectors is not always well targeted.  Establishing a realistic mechanism for implementation at the subnational level remains a major challenge.	The PRS process has substantially enhanced national processes for poverty monitoring, although there are some inconsistencies in the follow-through of actual PRS targets.  There is a major gap between PRS monitoring and feedback to policy formulation.  IFMS is a major instrument for improving PEM and accountability.

**Table A9.2 (concluded)**

Country	Macroeconomic Policymaking	PRSP Links to Budget	Monitoring and Evaluation
<b>Vietnam</b>	Limited public discussion of macroeconomic policy issues.	<p>The CPRGS (Vietnam's PRSP) is linked to the socioeconomic development plans—the SEDPs (products of Vietnam's indigenous planning process). However, the CPRGS falls short of being an “action plan;” in some important areas (e.g., SOE reform) the strategy is not sufficiently operational.</p> <p>There is no fully costed and prioritized MTEF.</p>	<p>Institutionalization of CPRGS monitoring and evaluation of implementation is at an early stage. An interministerial steering committee has been established, headed by the Deputy Prime Minister. Each ministry has responsibility for monitoring a specified set of indicators and to report back to the steering committee.</p> <p>The CPRGS contains an extensive system of 136 indicators to monitor economic developments and poverty reduction at both program and aggregate levels.</p> <p>At end-2003, there was not yet in place a framework of indicators for monitoring the linkages between policy measures and outcomes. Also, for about one-third of the indicators, information was either not available or of poor quality.</p>

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**Statement by the Managing Director  
IMF Staff Response  
IEO Comments on Management/  
Staff Responses**

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**Summing Up by the Acting Chair**

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**STATEMENT BY THE MANAGING DIRECTOR ON THE  
INDEPENDENT EVALUATION OFFICE REPORT ON THE EVALUATION OF  
POVERTY REDUCTION STRATEGY PAPERS AND THE  
POVERTY REDUCTION AND GROWTH FACILITY**

**Executive Board Meeting  
July 21, 2004**

The Independent Evaluation Office is to be commended for its wide-ranging and informative report on the Poverty Reduction Strategy Paper (PRSP) approach and the Poverty Reduction and Growth Facility (PRGF). The report has generated considerable debate within the Fund and provides useful material for our continuing assessment of effective modes of engagement with low-income countries through the PRSP approach and the PRGF.

Relatedly, earlier this year, Ms. Krueger formed an interdepartmental Committee on Low-Income Country Work (CLICW) to strengthen the Fund's work on low-income countries. This committee, chaired by her and consisting of Deputy Managing Directors and Department Directors (AFR, FAD, MCD, PDR, RES, WHD), will coordinate further work by staff on these issues, with the aim of preparing concrete proposals for Board consideration at a later date.

I have asked staff to prepare a statement presenting our views on the IEO report's recommendations and indicating how we envisage taking up these recommendations subject to the conclusions of the Board discussion. While the staff statement outlines some broad options for modifying the PRSP approach and PRGF, the forthcoming annual Bank-Fund PRSP Progress in Implementation Report will give specifics of these options. Following these Board discussions, staff will come back to the Board with cost estimates of any new initiatives, possible avenues for savings on other Fund outputs, and the appropriate pace of phasing in of any new initiatives.

I look forward to the Board discussion, which will provide an opportunity to explore the options for adapting the Fund's policies and procedures with respect to the PRSP approach and PRGF, bearing in mind resource costs.

# STAFF RESPONSE TO THE INDEPENDENT EVALUATION OFFICE REPORT ON THE EVALUATION OF POVERTY REDUCTION STRATEGY PAPERS AND THE POVERTY REDUCTION AND GROWTH FACILITY

Executive Board Meeting  
July 21, 2004

## I. Introduction

1. *The Independent Evaluation Office (IEO) report offers a trenchant analysis of the Poverty Reduction Strategy (PRS) approach.* The report concludes that the PRS approach has had some success in improving country ownership, enhancing participation, and providing better quality strategies. Nonetheless, its achievements so far fall short of its potential to deliver credible, effective, and country-owned strategies for growth and poverty reduction. Staff broadly support the IEO's recommendations, some of which were identified in previous assessments by the staff. However, staff differ with the IEO on how best to manage the tensions inherent in the PRSP approach.

2. *The IEO report represents a welcome opportunity to reflect on the accomplishments and challenges of the PRSP/PRGF approach.* It has generated substantial discussion within the Fund staff about the PRSP as a framework for Fund interaction with low-income countries. In view of the importance and complexity of the questions raised by the IEO, further reflection on these issues will be necessary. Given the joint nature of the PRS approach, the Bank and the Fund will need to cooperate closely in moving the initiative forward. The Bank's Operations Evaluation Department (OED) has completed a parallel review of the PRSP process and the Bank's role. The OED report, and the response of Bank management, will be discussed by the Committee on Development Effectiveness on July 19, 2004. The next opportunity for the Board to consider related issues will be in September 2004 in the context of its upcoming discussion of the annual Bank-Fund PRSP Progress in Implementation Report.

3. *One overarching implication of the analysis and various recommendations put forward in the IEO report is that staff resources allocated to low-income work are insufficient for the strategic approach endorsed by the Board.* Staff agree that the

ability of the Fund to play a more effective role in low-income countries depends on its staff being able to contribute constructively to the analytical discussion and policy debate in the PRSP process. Any resultant increased demands on staff time will then need to be balanced by more overall resources or a reduction in other activities. Alternatively, the Fund's role could be adapted to the resource constraint. At this stage, the IEO's recommendations are too diffuse to provide estimates of their resource implications, although their resource costs are likely to be sizable based on preliminary reactions of the area departments.

4. The next section summarizes the IEO assessment of the PRSP/PRGF approach. Section III gives staff views on the IEO evaluation and recommendations, and Section IV outlines elements of a strategy for moving forward. Section V presents some initial reflections on resource implications of the IEO recommendations.

## II. A Summary of the IEO Evaluation of the PRSP/PRGF Approach

5. The IEO report comes out strongly in favor of maintaining the PRS approach, and observes *important achievements . . .*

- Ownership of the PRS has improved over previous approaches.
- Participation in the formulation of PRSPs has been more broadly based than in the past.
- Compared to previous development strategies, PRSPs provide more comprehensive and integrated poverty reduction strategies, with a longer-term perspective. They thus provide a better framework for coordination with donors and civil society.

. . . but also *shortcomings.*

- The perception remains widespread that the new approach is externally driven and dominated by document preparation, especially related to the HIPC Initiative.
- Institutions for policy formulation have not in general been strengthened. Stakeholder and country participation in the formulation of the macroeconomic framework has been narrow.
- The quality of PRSPs remains weak in many areas. For example, most PRSPs lack a strategic vision, especially in the area of macroeconomic and related structural policies. Many PRSPs avoid confronting strategic choices, such as critical structural reforms and prioritization of spending programs aimed at poverty reduction.
- The PRS approach has not in general delivered on its promise of improving donor coordination.
- The Fund's contribution to the PRSP process has varied considerably across countries, falling short of the goals set in the original policy documents.
- The role of the Joint Staff Assessment (JSA) is not sufficiently clear. Consequently, JSAs have not always provided effective feedback to the authorities on weaknesses in the PRS; they have had little impact on the broader policy debate, and JSAs do not provide a satisfactory basis for making judgments on lending decisions.

6. *The IEO also provides a useful perspective on the PRGF.* It finds that program design has improved in many ways . . .

- fiscal targets are more flexible;
- projections do not suffer from a systematic “aid pessimism” bias;
- pro-poor expenditures have increased;
- there is no evidence of an excessive disinflationary bias.

. . . but concludes that too little has changed.

- program design has continued to lack an understanding of micro-macro linkages;
- too few PSIA's have been conducted, and the integration of the results into program design has been too slow;
- alignment of the PRGF with PRSPs thus far has been limited.

7. The IEO report is more suggestive than prescriptive in laying out the operational implications of its recommendations. Nonetheless, *a central thrust of the IEO's recommendations is to clarify and, in*

*staff's view, to strengthen the links between the Bretton Woods institutions' (BWIs) lending decisions and the PRS framework, while at the same time deepening the reach of the PRS framework into domestic policymaking processes.* In particular:

- Countries should define their own benchmarks for improving their policymaking process. The BWIs should then evaluate progress, and suitability for continued lending, based on these benchmarks.
- The Fund should be more involved in the PRS process, including in the public debate, but with a scope limited to its areas of comparative advantage.
- The IMF could restructure its conditionality to fit within a broader “partnership” approach to monitoring and assessing progress in implementing the PRS.

### III. Views on the IEO Evaluation and Recommendations

8. *The IEO's diagnosis of problems with the implementation of the PRSP approach overlaps substantially with that of previous Board and staff assessments.*<sup>1</sup> The PRSP is an instrument charged with multiple objectives, which result in tensions—for example, long-term ambition versus immediate budget constraints; comprehensiveness in addressing the different dimensions of poverty versus focus and prioritization; and meeting the expectations or requirements of the international community versus country ownership.

9. *The Fund shares the broad objectives underlying the IEO's recommendations, including:*

- Higher quality outputs of the PRS process, particularly in terms of priorities, costing, and policy analysis, and a more constructive Fund role in its areas of competency;

<sup>1</sup>“Poverty Reduction Strategy Papers – Progress in Implementation” (SM/02/250 and SM/03/279), “Review of the Poverty Reduction Strategy Paper Approach—Early Experience with Interim PRSPs and Full PRSPs” (SM/02/54, 3/27/02); “Aligning the Poverty Reduction and Growth Facility (PRGF) and the Poverty Reduction Strategy Paper (PRSP) Approach: Issues and Options” (SM/03/94); “Role of the Fund in Low-Income Member Countries Over the Medium Term—Issues Paper for Discussion” (SM/03/257); “Review of the Poverty Reduction and Growth Facility—Issues and Options” (SM/03/51, 3/15/02); “The Fund's Support of Low-Income Member Countries—Considerations on Instruments and Financing”(SM/04/53, 2/24/2004); and “Fund Assistance for Countries Facing Exogenous Shocks” (SM/03/288, 8/11/2003).



- Strengthened country ownership and greater integration of the PRS process with domestic political and policy processes, particularly the budget;
- Reduced “mismatch of expectations” of various stakeholders (governments, civil society, IFIs, donors) of the PRS approach;
- Better alignment of the PRGF with the PRSP, and more clarity on what happens if the PRSP is too weak or unrealistically ambitious to serve as a framework for a PRGF;
- Better fit of the focus and mix of policies in PRGF-supported programs to country circumstances, based on a deeper understanding of micro-macro linkages.

10. *An important consideration for any evaluation of the PRS approach relates to how quickly results from this new approach can be reasonably expected to emerge.* The PRS approach attempts to improve the entire framework for, and direction of, policy formulation in low-income countries. This approach is only five years old. Any assessment, and recommendations, should recognize the variety of country experiences, including important successes, the evolving nature of the initiative, the multiplicity of objectives, and the novelty of the approach in a long-established multipartite international setting. The implication is that substantial scope exists for better implementation of the current approach, with appropriate mid-course corrections.

11. In light of the similarity of diagnosis and objectives, Fund staff supports many of the IEO’s suggestions. *However, in some cases, the objectives are shared, but the staff questions the feasibility of some IEO recommendations. After a discussion of the common ground, the implications of key differences in perspectives are explored. The Appendix provides specific staff reactions to each IEO recommendation. Section IV presents our approach designed to achieve key objectives.*

#### A. Areas of Broad Agreement

12. With respect to *the design and implementation of the PRS approach*, staff agree that countries should themselves decide how policy formulation, implementation, and monitoring processes will be conducted and built up over time. Countries should also determine the choice of output of the PRS process, in terms of documents and their periodicity, relying as much as possible on domestic institutional arrangements and reporting vehicles (IEO Recommendation 1). The key issue is how donors should react in cases where they believe that the country could aim higher, or commitment is insufficient. More candid and graduated assessments by Bank

and Fund staff and donors are key for appropriately balancing the need for ownership against the expectations of the international community.

13. With respect to the *Fund’s role*, the staff has been attempting to clarify further the intensity and scope of the IMF’s role in the PRS approach, along the lines of the IEO suggestions and earlier Board guidance. In particular, staff recognizes the need to give more emphasis to Fund staff involvement in the domestic policy debate over macroeconomic policy and to open the rationale for IMF policy recommendations to broader scrutiny (Recommendation 4). The staff is also trying to explore in a more systematic way the linkages between macroeconomic policies and poverty reduction.

14. *One area where progress has been made is in poverty and social impact analysis (PSIA) of proposed policy changes.* The Fund’s FY2004/05 budget includes dedicated additional budgetary resources to broaden and deepen the use of PSIA and to eventually mainstream PSIA into the design of PRGF-supported programs. Nonetheless, care should be taken to avoid building unrealistic expectations as to what the Fund can deliver in PSIA in the near future, in part because of resource limitations discussed below.

15. *Staff agree that the Fund should focus on areas in which it has a comparative advantage, that the Fund can play an important but only supporting role in developing alternative aid and policy scenarios, and with the recommendation to avoid undue “on-off” signals from the Fund for donor financing (Recommendations 5 and 6).* Strengthening the Fund’s accountability for its own commitments in the context of the PRS process is also an attractive goal, particularly in ensuring the Fund’s contributions are consistent with needs identified in country PRSPs.

#### B. Differences with IEO Recommendations

16. *The most important difference is over managing the tensions between country ownership of the policies and programs in the PRSPs and the need of donors and IFIs for minimum standards.* In particular, the donor community wants to use the PRSP as the basis for selectivity of resource allocation.

17. *The IEO recommends that countries set explicit criteria for judging progress towards key intermediate objectives related to the domestic policy formulation, implementation, and monitoring process, and that BWI staff provide candid assessments of those benchmarks (Recommendations 1 and 2).* Donor decisions on the volume of resources provided would then be linked to the progress countries are making under the approach. The IEO contends that the PRSP approach already involves requiring

the countries to adopt various changes in their policy processes in return for financing and debt relief, in particular from the Fund and the World Bank. It also suggests that the Fund's criteria for making such decisions are unclear, and in particular are obscured by the focus on documentation requirements. In the concluding section on the role of the Fund, the IEO proposes that the IMF could restructure its conditionality to fit within a broader "partnership" approach to monitoring and assessing progress in implementing the PRS. The precise operational modalities are not discussed.

18. Staff agrees that the quality of the PRS approach should be a critical factor in donors' resource allocation decisions, in order to enhance aid effectiveness. Such selectivity will appropriately encourage stronger PRSPs. *In our view, however, the IEO recommendations imply excessive Fund involvement in assessing the country's decision-making processes.* The IEO suggests that the BWIs could assess achievement of country-defined process benchmarks. Combined with the suggested tighter link to financing, this could be seen as a kind of process conditionality, which could undermine the legitimacy of these domestic institutions and decision-making processes. The IEO report itself underscores the costs associated with the perception that the PRSP process is BWI-driven. Moreover, good policymaking processes are no guarantee of good policies.

19. *In staff's view, the BWIs should continue to emphasize the country ownership of the PRS process.* It will take time and effort for domestically anchored processes to result in high-quality, prioritized PRSPs, and the BWIs can and should contribute to this institution building. The Fund will continue to work with the World Bank to develop and promote best practices for improving domestic policy processes, but the Fund should stop short of measuring countries against specific benchmarks in this area. Instead, the Fund's role should focus on assessing the quality of macroeconomic frameworks, and in providing advice and support for the development of sound frameworks.

#### IV. Options for Moving Forward

20. A promising strategy for creating a higher-quality and more fully country-owned PRS approach would be *to make the Fund's contribution more substantive and less procedural.* Currently, as the IEO notes, too much emphasis is placed on Fund assessment of PRS documents such as PRSPs and annual performance reports on PRSP implementation (APRs). In our view the direction forward is to lighten reporting requirements, while increasing the scope for the Fund to make substantive contributions. The em-

phasis should be on providing more effective advice on the formulation of the macroeconomic strategies underpinning PRSPs, particularly with respect to their budget implications, and on providing frank opinions on such strategies as the PRS process unfolds.

21. *The links from the PRS to Fund financing, signaling to donors, and HIPC debt relief could be made more flexible, in order to provide more policy space and development of domestic policy processes.* The incentives for the country to produce a good PRSP must come from its benefits in terms of better policy formulation and from donors, including the Fund and the World Bank, respecting the views outlined in a well-prioritized, domestically-driven PRSP and (in the case of development assistance) allocating more resources to countries that have high-quality PRSPs.<sup>2</sup> This could increase ownership and encourage integration of the PRSP with the budget and other domestic processes while still providing financial incentives.

#### A. Improving the PRS Approach

22. *As noted above, staff agrees with the IEO that the staffs' assessments of the countries' PRSPs need to be more candid and more graduated.* The current operational requirement is that the JSA conclude by finding either that the PRSP does or does not provide a credible basis for BWI lending. This can hamstring the potential candor of the assessment and puts all PRSPs into one of two categories (and in practice only one). PRSPs are seen by staff as becoming longer, more detailed, and more resource intensive, while providing little of apparent value to staff, the authorities, or donors.

23. *A reformulation of the instrument used by BWIs to assess PRSPs is needed.* As noted before, staffs intend to come back to the Board with more specific recommendations in the context of the PRSP annual implementation report, but early Board guidance would be appreciated. Bank and Fund staffs are currently considering three elements of such a reformulation.

- *What is the purpose of the assessment:* to shape Fund lending decisions; to provide candid feedback; and/or to help coordinate with the Bank (and donors)?
- *Who is making the assessment?* If the assessment is meant to provide a basis for the BWI lending decisions, then presumably Board endorsement would be necessary. If it is meant to

<sup>2</sup>This idea was at the origin of the PRSC, which was originally thought of in part as a vehicle to reward countries with sufficiently good PRSPs with an appropriate reduction in traditional red tape and conditionality.

give candid feedback to the country or to donors, then would it be more appropriately treated in a similar manner to assessment letters and sent to the Board for information? If coordination of donors is an important objective, are there continued benefits to a joint assessment? Could other donors be involved in the assessment? What is the role of the low-income country itself?

- *What is being assessed?* Should the assessment evaluate the process by which the document was formulated, the policies in the document, the authorities' commitment to it, and/or the donors' commitment to financing the strategy?

24. *Besides modifying the JSA, the Fund could participate more fully in the PRSP process* through providing policy advice and, where appropriate, participation in the public discussion leading to the formulation of PRSPs, particularly encouraging and participating in discussions of the macroeconomic options and the options for structural reforms that are macro relevant. There are important roles to play both as participants in the public debate, and in helping the government make its case for its macroeconomic policy choices. This would include bringing the results of any relevant poverty and social impact analysis (PSIA) into the discussions of overall macroeconomic frameworks and related policies. In its ultimate assessment, however, the Fund should make clear its views on macroeconomic frameworks ultimately included in PRSPs and be prepared to provide convincing arguments for any proposed revisions.

25. *In this context the Fund's efforts to build capacity and strengthen institutions through technical assistance will be particularly important.* Further efforts will be needed to provide appropriate advice and technical assistance where required to strengthen budget policies and processes aimed at promoting sustainable growth and poverty reduction.

26. *One underemphasized issue has been the role of building capacity through technical assistance (TA), which is central to the vision of the Fund as a service provider in the context of the PRS approach.* In its recent review of TA, the Board pointed to progress in pursuing strategic focus and enhancing effectiveness.<sup>3</sup> Nonetheless, further work needs to be done to better coordinate with other TA providers and integrate Fund TA into the broader agenda of the Fund's relationship with low-income countries. In this regard, AFRITACs (Africa Regional Technical Assistance Centers) and the forthcoming Middle East Technical Assistance Center can play an important role. Area departments will also need to take a

<sup>3</sup>"Review of Technical Assistance" (SM/04/41, 2/17/04).

more strategic view of the technical assistance needs of member countries in close consultation with country authorities.

#### *B. Implications for Fund-Supported Programs*

27. *The Fund Board previously considered issues in working towards a better alignment of PRGF-supported programs with country PRSPs.*<sup>4</sup> The Board stressed that the process of alignment will need to be implemented pragmatically and flexibly, taking due account of country-specific circumstances and capacity constraints, as well as the need to ensure that PRGF-supported programs continue to be strong and designed to help countries accelerate growth and the pace of progress towards the Millennium Development Goals.<sup>5</sup>

28. *In the staff's view, a key element in improving the Fund's contribution to the PRS process is to introduce flexibility in the link between PRGF-supported programs and the PRSPs, based on country-specific circumstances.* PRGF-supported programs would continue to be drawn from the macroeconomic frameworks in PRSPs to the extent possible. Where a PRSP provides a good operational road map, the PRGF should be tightly linked to its framework. Program and mission cycles should be aligned with the PRSP/budget cycles and other domestic processes as much as possible.

29. *However, some countries may not be able to produce operationally viable PRSPs for some time.* A PRSP would still be required for Fund (and Bank) financial support, but the emphasis in these cases, for the Fund, would shift from artificially insisting on immediate tight alignment between the PRGF-supported program's macroeconomic framework and in the PRSP. Rather, Fund staff need to work with countries to strengthen the macroeconomic frameworks in their PRSPs so as to move toward alignment over time. Areas that required work could be clearly highlighted in the assessment of the PRSP. The Fund would still seek to apply the PRSP principles to the Fund's role. This would include (i) seeking to open up the policy debate on a few key priority issues (for example, through analytical inputs and prioritization of PSIA that would be designed to explore various policy options); and (ii) contributions to capacity development that follow country-driven priorities and understandings on what a rea-

<sup>4</sup>"Aligning the Poverty Reduction and Growth Facility (PRGF) and the Poverty Reduction Strategy Paper (PRSP) Approach: Issues and Options" (SM/03/94).

<sup>5</sup>"Concluding Remarks by the Acting Chair, Aligning the Poverty Reduction and Growth Facility (PRGF) and the Poverty Reduction Strategy Paper (PRSP) Approach—Issues and Options" (BUFF/03/55).



sonable road map toward a operationally oriented PRSP would be.

30. *In such cases, the PRGF-supported programs would provide additional coherence, precision, and clarity to the authorities' policy intentions, and staff would need to affirm that the authorities' commitment to the resulting framework is nonetheless adequate.* Rather than derailing the incipient participatory processes by integrating them into PRGF-supported program discussions, in this manner the Fund could continue to seek to approve arrangements with such countries on the basis of adequate PRGF-supported programs that would still be linked to PRSPs, albeit with clearly explained modifications.

31. *The introduction of such flexibility in the link between the PRSP and PRGF is seen as a way to strengthen the Fund's involvement in the formulation and implementation of macroeconomic policies in the PRS approach.* Making the Fund's concerns with the PRSP macroeconomic framework transparent in the assessment will give the authorities and their development partners a more precise and nuanced assessment of the country's macroeconomic challenges. It will also underscore the evolving nature of the macroeconomic framework in the PRGF-supported programs, which are inherently dependent on shorter-term considerations such as availability of donor financing. *Of course risks will also need to be addressed.* In particular, the existence of different macroeconomic frameworks in the PRSP and the PRGF-supported program could be seen as evidence of Fund intrusion in domestic policy setting or of the Fund undermining of the PRSP process. Thus, the government should clearly demonstrate its ownership of the program, and the Fund its commitment to the PRS process, by explaining clearly their position to other development partners and domestic stakeholders.

32. *As part of the effort to strengthen its involvement in the PRS process, the Fund will also continue to seek ways in which to improve PRGF-supported program design.* More can be done, and the Fund will take due consideration of the IEO's report in its forthcoming work on the design of PRGF-supported programs. This review of program design will seek to provide recommendations on how to increase these programs' effectiveness in enhancing growth and reducing poverty. In this regard, it is important that the Fund be sufficiently selective in its allocation of PRGF resources. Areas where the design of PRGF-supported programs might be refined include:

- ways in which programs, along with TA, can help build the institutions necessary to underpin

sustainable growth, particularly in the monetary and fiscal areas most directly related to the Fund's comparative advantage;

- appropriate strategies to facilitate development of the private sector, including monetary frameworks for facilitating higher private sector credit growth;
- means by which macroeconomic frameworks can best accommodate higher aid inflows.

## V. Resource Implications

33. *In considering the IEO recommendations, resource constraints must be taken into account.* The Fund's participation in the PRS approach can, depending on its nature, require substantial Fund resources, including staff time and travel, in addition to that necessary to carry out the Fund's other responsibilities. These demands have a tendency to crowd out critical analytic and substantive work.

34. *Many of the IEO recommendations would increase Fund responsibilities considerably.*<sup>6</sup> The IEO suggests that staff become more systematically and directly involved in the PRS process, including in the public debate surrounding the PRSP and APR. In countries where policy formulation procedures are weak, considerable additional Fund resources would be needed to deepen the policy dialogue. In such cases, the IEO recommendations would represent a major additional demand on staff time. Thus, internal Fund discussion is needed on how to balance these needs against other priorities. The suggestions in Section IV are formulated in part with a view to reducing the procedural burden on staff of the PRS process.

35. *The staff resource implications of deeper substantive involvement in the PRS process would need to be considered carefully.* In the context of a desire to maintain closer and more informal contacts with a large number of stakeholders, one question is whether, as the IEO has suggested, consideration should be given to adjusting somewhat the mix of headquarters and resident staff. In particular, the role of the resident representatives requires careful consideration.

<sup>6</sup>The IEO considers that none of its proposals are outside the original framework of the PRSP approach as reflected in the Board documents.

## STAFF VIEWS ON THE SPECIFIC IEO RECOMMENDATIONS

## A. Recommendations Relating to the Design and Implementation of the PRS Approach

IEO Recommendation	Staff Response
<p>I. Introduce greater flexibility in the implementation of the PRS approach to fit better the needs of countries at different stages of the process and with different capacities and political and administrative systems. Countries need to be put even more firmly in the driver's seat by determining themselves:</p> <p>(a) How the policy formulation, implementation, and monitoring processes will be conducted and built up over time, and with what rules of the game (e.g., for opening up the policy process to previously excluded groups or strengthening budgetary processes). Progress would be monitored against an explicit set of country-determined intermediate benchmarks;</p> <p>(b) What the output of these processes will be in terms of documents (e.g., PRSP, Progress Reports, etc.) and on what periodicity they will be prepared, relying as much as possible on domestic institutional arrangements and reporting vehicles. IMF process requirements (e.g., linking reviews under the PRGF to completion of specific PRSP documents) should be minimized and oriented around domestic processes.</p>	<p>Staff agrees that countries should be encouraged to customize the PRS approach to country circumstances. This notion was embedded in the PRSP approach at its inception, and was reiterated in the 2002 review of the PRSP, which stressed that the approach should reinforce—not undermine—existing national institutions, processes, and governance systems. That this has not happened to the extent that might be wished may have more to do with broader questions of ownership than with a failure to articulate this objective. As staff argues in the text and with respect to Recommendation 2 below, other aspects of the IEO's recommendations risk further reducing the extent to which the process is country-driven.</p> <p>Moreover, leaving the criteria for the documents entirely to countries raises a number of issues. The report does not clarify how donors (including the BWIs) should react in cases where they believe that the country could aim higher, or where they view the pace of progress chosen as indicative of a lack of commitment on the part of the authorities to objectives donors can support.</p>
<p>2. Shift the emphasis of the initiative from the production of documents to the development of sound domestic policy formulation and implementation processes. This means:</p> <p>(a) <i>Build in greater results-orientation.</i> Countries should be encouraged to establish (with help from BWIs where needed) substantive criteria for judging progress toward key intermediate objectives such as developing (i) an operational road map that provides strategic guidance for setting priorities and resolving trade-offs; and (ii) effective institutional arrangements for formulating, implementing, monitoring, and updating this road map, with a firm link to budget processes. The choice of the criteria/benchmarks judged to be most important would likely vary by country, but in some areas broad guidance could be developed by BWI staff or others, upon which countries could draw as a starting point. However, the types of benchmarks chosen by each country will depend on the improvements that their PRS process identifies as a high priority.</p> <p>(b) <i>Shift in emphasis of the incentives structure</i> faced by countries from procedural aspects and production of documents to achieving substantive changes in domestic processes and policies objectively measured as described in (a) above. The new set of incentives would include: (i) Countries should present their intentions and objectives, along with the benchmarks selected to monitor progress in a manner open to public scrutiny; (ii) IMF (and World Bank) staff would be responsible for providing clear and candid assessments of the progress made by each country in implementing the PRS approach, both in relation to the goals set by the country itself and against initiative-wide benchmarks; (iii) IMF (and World Bank) staff would help countries identify key constraints in making progress towards PRS objectives and support efforts to ameliorate them; (iv) Ideally, donor decisions on the volume of resources provided should be linked to the progress countries are making under the approach. To facilitate this, IMF assessments in its area of expertise need to provide as clear and candid a signal as possible. The criteria guiding the IMF's own lending decisions under the PRS approach could also be improved in this regard.</p>	<p>Staff agrees that the PRS process is too document-driven and that PRSPs should be more tightly integrated with domestic policy process and institutions. It is also desirable that the quality of the PRS approach be a critical factor in donors' resource allocation decisions.</p> <p>However, the thrust of this recommendation is to attempt to use the financial leverage of the BWIs to improve domestic policy processes. This effort is unlikely to succeed. As the IEO report itself underscores, one reason the PRS process remains separate from domestic modalities is the perception that it is BWI-driven. It will take time and effort for domestically-anchored processes to result in high-quality, prioritized PRSPs. The IEO recommendations risk weakening domestic ownership (if the BWIs ask for minimum standards in the PRSPs) or weakening the programs supported by the BWIs (if the BWIs do not set minimum standards for lending).</p> <p>The recommendation also raises a variety of issues that reflect these tensions. It is not clear who would be doing the proposed monitoring of country-chosen progress benchmarks. If countries do the monitoring themselves, donors may seek to establish their own benchmarks to ensure the country is in fact doing what it says.</p>

IEO Recommendation	Staff Response
<p>3. Clarify the purpose of the JSA and redefine the vehicle accordingly. The JSA is a useful concept whose potential has not been realized. The IEO recommends making the following changes:</p> <p>(a) JSAs should focus on the adequacy of domestic policy choices and the quality of domestic processes as well as actual progress towards intermediate objectives, and less on the quality of the PRSP as a document.</p> <p>(b) To foster clear and candid assessments, we propose: (i) making explicit the criteria and benchmarks used by staff to form their judgments; (ii) reporting on the views of third parties (especially local stakeholders and donors) when available, and discussing differences of view; and (iii) eliminating the need for JSAs to reach a binary (yes or no) conclusion as to the adequacy of the PRS as a basis for BWI concessional lending. JSAs should aim to provide a <i>graduated</i> assessment of the strength of the PRS and related processes as well as of the quality of policies.</p> <p>(c) The effectiveness of the above recommendations could be enhanced if JSAs were produced on an independent schedule (e.g., once a year), rather than being linked to a specific PRSP document.</p> <p>(d) The JSAs would be more effective if, in addition to flagging weaknesses in the PRS, they indicated clearly what are the main obstacles to overcome; what the IMF proposes to do to help address them in its areas of responsibility; and what needs remain un-addressed, especially in the area of capacity building.</p>	<p>This recommendation includes many shared objectives for the JSA and indeed for Fund analysis more broadly, such as candor, reporting the views of other stakeholders, and pointing out areas of weakness in the PRSP and how to address them.</p> <p>By expanding the reach of the JSA to include “the quality of domestic processes,” the IEO would significantly increase the resource costs of the JSA and its overlap with other documents, such as Article IV staff reports. At the same time, the attempt to tighten the link between BWI assessment and these domestic processes is likely to be counterproductive, as described in staff’s response to Recommendation 2.</p> <p>Staff agrees with the suggestion to eliminate the binary conclusion in the JSA. Section IV of the staff response goes further and discusses elements of a possible reformulation of the instrument used by BWIs to assess PRSPs, in order to increase the scope for candor and textured assessments, allow for more effective feedback, and counter the perception that the PRSP and the APR are mainly instruments of BWI conditionality.</p>

### B. Recommendations Relating to the Fund’s Role in the PRS Approach

IEO Recommendation	Staff Response
<p>4. Clarify what the PRS approach implies for the IMF’s own operations and strengthen the implementation of the agreed role.</p> <p>(a) <i>IMF engagement in the PRS process:</i> (i) More emphasis should be given to IMF activities that help to better inform broad-based policy discussions in its areas of competence. Guidelines to staff need to be clarified so as to encourage more active inputs to such discussions, including analyzing alternative policy options and trade-offs; (ii) Rather than establish uniform “standards” for the IMF’s role, expectations should be tailored to country-specific circumstances, including the government’s wishes. These country-specific “rules of the game” should be made public and could describe how IMF staff expected to participate in the broader policy debate, including what supporting analytical work they will undertake. This is also likely to require a combination of more “stand alone” missions, set apart from program negotiations, and enhancing the role of resident representatives; (iii) There should be more systematic explorations of country-specific macro-micro linkages; (iv) Article IV surveillance reports should be used systematically as a vehicle to convey the IMF’s own thinking and analysis on key issues; (v) Assess systematically, as part of broader IMF surveillance activities, obstacles to the achievement of PRSP objectives originating in trade and subsidy policies of main trading partners.</p> <p>(b) <i>PRGF-related activities:</i> (i) The rationale for IMF policy recommendations and program design should be subjected to broader scrutiny and debate; (ii) Clarify the approach to be taken by the IMF in those cases where the PRS approach has added some value but has not yet produced an operational road map or the necessary institutional framework for implementation; (iii) Clarify what the BWIs are trying to achieve jointly through the streamlining of conditionality and how this fits with stronger domestic ownership; establish a system for the monitoring of aggregate Bank-Fund conditionality at the country level.</p>	<p>(a) <i>PRS process.</i> Staff shares the objectives of clarifying the expectation about the IMF role under the PRS approach and finding ways to improve its effectiveness in meeting these expectations. The Fund should participate in the PRSP process through providing policy advice and, where appropriate, participation in the public discussion leading to the formulation of PRSPs, particularly encouraging and participating in discussions of the macroeconomic options and the options for structural reforms that are macro relevant. The Fund should provide advice and technical assistance where required to strengthen budget policies and processes aimed at promoting sustainable growth and poverty reduction. Resource implications of further initiatives to strengthen Fund involvement in the PRS process would, however, have to be carefully considered.</p> <p>(b) <i>PRGF-related activities.</i> Staff agrees with these objectives. Staff considers that the Fund should make clear its views on macro-economic frameworks ultimately included in PRSPs and be prepared to provide convincing arguments for any proposed revisions in a PRGF-supported program.</p>



IEO Recommendation	Staff Response
(c) Streamline IMF documentation and Board scrutiny of PRS documents.	(c) Staff agrees with the need to streamline documentation and the procedural burden of the PRS more broadly. Indeed, this represents an important disadvantage of those IEO recommendations that would seem to move in the other direction (increasing the importance and areas of coverage of the JSA, for example).
<p>5. Strengthen prioritization and accountability on what the IMF itself is supposed to deliver within the broader partnership framework, built around the priorities emerging from the PRS process, and ensure resources match commitments. Prioritization and coordination could be improved as follows:</p> <p>(a) Generate, as part of the PRS process, specific priority actions for the IMF to assist the country concerned to reach its objectives, including for analytical inputs and long-term capacity building. If the IMF is not well-suited to produce a particular input (e.g., some PSIA), but this input is judged critical for program design, a clear identification of who has agreed to do what and by when would strengthen incentives. Such key deliverables would be agreed with the government and made public. These priority actions would then be the basis for evaluations of IMF performance, both at the country level and in aggregate.</p> <p>(b) The IMF's own budget decisions on allocation of administrative resources should be geared to these priorities. Linking realistic resource allocation decisions to a more explicit set of priorities should help improve decision making and make clearer to all what the IMF has committed to, and what it has not.</p> <p>(c) Experiment with broader "external reviews" of the PRS/PRGF process, monitoring in particular the performance of donors and IFIs in providing support, and not just performance of the national authorities.</p>	<p>Again, staff agrees with the objectives of prioritization and accountability, and takes note of the IEO's suggestions.</p> <p>However, while the IEO acknowledges the need to prioritize, many components of the IEO's recommendations (e.g., greater staff role in "framing the policy debate" and more exploration of macro-micro linkages) would require substantially more staff resources, while suggestions for reducing activities are few.</p> <p>Section IV of the response provides a broad outline of how staff sees the Fund's role in the PRS approach, emphasizing substantive contributions to the formulation and debate of macroeconomic frameworks in PRSPs. The Fund has also been moving towards more systematic explorations of micro-macro linkages through the use of poverty and social impact analysis of proposed policy changes. However, care should be taken to avoid building excessive expectations as to what the Fund can realistically deliver in this area in the near future.</p> <p>The Fund is accountable to its members and reports to them, through the Executive Board, on a regular basis. Strengthening the Fund's accountability for its own commitments in the context of the PRS process is desirable; putting it into practice is a challenge. For example, a large part of the Fund's deliverables would be the provision of technical assistance and policy advice, but measuring the outcome of these activities is difficult at best. At a minimum, it is important to work to ensure that the Fund's contributions are consistent with needs identified in country PRSPs.</p> <p>Staff continues to welcome external reviews of all aspects of the PRS/PRGF process.</p>
<p>6. The IMF should encourage a strengthening of the framework for establishing the external resources envelope as part of the PRS approach. The country itself, not the IMF or World Bank, should eventually play the central role in elaborating macro frameworks and catalyzing donor support. The IMF role would be to provide debt and macroeconomic sustainability assessments and judgments on the policy framework, but it would not be responsible for the "normative" judgment on appropriate aid levels over the medium term. The tension between "ambition" and "realism" in determining the external resource envelope can perhaps be handled by presentation of alternative projections. The IMF should provide increased analytical support for such approaches when requested. But the choice to prepare alternative projections should remain with the country and not be a uniform requirement.</p> <p>Improving aid predictability is a wider problem that the IMF cannot resolve on its own. The challenge is how to reconcile PRSP countries' concern for aid predictability with donors' concern for aid effectiveness, which implies some performance-based selectivity. For the IMF, this requires finding a way, perhaps through a strengthened JSA, to provide signals to the donor community on macroeconomic performance that are sufficiently calibrated, and take account of the longer-term framework of donor involvement, to be a useful input into selectivity decisions without providing excessive "on-off" signals for financing.</p>	<p>This recommendation is consistent with staff's views on the appropriate substantive role of the Fund. The Fund should focus on areas in which it has a comparative advantage. The Fund can play an important but only supporting role in developing alternative aid and policy scenarios. Staff should aid country authorities wherever possible in elaborating alternative macroeconomic scenarios.</p> <p>Staff also agrees that the Fund should avoid giving excessive "on-off" signals for donor financing. The Fund is working with low-income countries and the entire development community to improve donor coordination and provide sufficiently calibrated signals. The Board will have an opportunity after the Annual Meetings, for example, to consider options for signaling Fund assessments of low-income country policies.</p>

## **INDEPENDENT EVALUATION OFFICE COMMENTS ON MANAGEMENT/STAFF RESPONSES TO THE EVALUATION OF POVERTY REDUCTION STRATEGY PAPERS AND THE POVERTY REDUCTION AND GROWTH FACILITY**

**Executive Board Meeting  
July 21, 2004**

The comprehensive nature of the management/staff responses is welcome. They provide a basis for a substantive debate on the major issues raised in the evaluation. The staff has noted a number of areas where it broadly agrees with the messages and recommendations contained in the evaluation report, but also areas of disagreement. Since the evaluation and the management/staff response inevitably cover a lot of ground it might be useful to highlight a few key questions of particular interest:

- Whether and how to modify the design of the PRS approach to give more emphasis to the intermediate objective of improving domestic processes for policy formulation, implementation and monitoring, in a way and at a pace that best fits each country's circumstances.
- Whether and how to ensure that incentives faced by participating countries—especially those resulting from BWI procedural requirements, assessment procedures, and provision of assistance—are aligned with this objective and are transparent.
- How the BWIs should assess PRSPs and the nature of the instrument they should use. (In this context, we think the questions posed by the staff in para. 23 are the right ones.)
- How to clarify or adjust expectations about the extent and nature of the IMF's involvement in the PRS process, and ensure that commitments are consistent with available resources.
- How the IMF's "way of doing business," including in the context of the PRGF, needs to be modified in support of the PRS approach, both in relatively mature cases and in those "difficult" cases where the PRSP is unlikely to provide an effective operational road map for the foreseeable future.

To facilitate this discussion, our comments will focus on a few issues where we see the messages

emerging from the evaluation as somewhat different than those emphasized by the staff and will respond to several concerns raised about our recommendations. Paragraph references are to the staff comments.

The staff observes (para. 8) that the IEO diagnosis of problems with implementation of the PRSP approach overlaps substantially with those of earlier internal reviews. In our view, the evaluation raises two issues that are more fundamental than those raised in previous assessments and that will not be resolved merely by allowing more time for the approach to have an impact. First, some significant design problems have emerged as the approach has been implemented. While some of the tensions that gave rise to these problems (e.g., between country ownership and BWI/donor selectivity) have been acknowledged previously, how best to deal with them has not been adequately addressed. Second, the IMF "way of doing business" in low-income countries has not adapted sufficiently to the implications of the PRS approach—an issue that goes beyond resource availability.

We agree, however, that the issue of staff resources is a critical one. What the IMF is expected to contribute to the PRS approach needs to be tailored to fit the resources that can reasonably be expected to be available. Contrary to the staff's observation (para. 34), none of our recommendations involve an expansion of the IMF's "responsibilities" beyond what was indicated in the original policy papers establishing the PRSP and the PRGF. The discussion in [the section "What Was Expected of the IMF Under the New Initiative?"] of the evaluation report illustrates how bold were the original expectations on the IMF's role. If these expectations are now judged to have been too ambitious, it would be better to clarify that role explicitly. But whether a "larger" or a "smaller" role for the IMF is expected in low-income countries in the future, it should not be a "business as usual" role; if the PRS approach is to be the key framework for IMF involvement in

low-income countries, IMF activities will need to adapt accordingly.

In this context, the most effective approach to matching expectations with resources is to introduce greater scope for customization of the IMF's role to country needs, building on the twin principles of prioritization and partnership. Prioritization implies that the key deliverables from the IMF (e.g., for analytical work to strengthen the broader policy debate or assistance with capacity building) should themselves be derived—to the extent possible—from the country-driven PRS strategies. This would then feed into more transparent budgetary choices within the IMF and realistic indications of what can and cannot be delivered. The partnership element means that strong coordination with other donors is needed, built around the country-driven strategy and priorities, and that “stand alone” approaches should be resisted, even if they appear administratively easier in the short run.

The staff agrees that managing the tension between ownership and selectivity is a central one for the design of the PRS approach but disagrees with the approach proposed in the evaluation report (paras. 17–19). Clearly, different solutions to this problem are possible, but we would like to emphasize two points. First, the solution proposed in the report is based on (i) greater scope for, and openness to, country-driven choices on the road map for implementing the core principles of the PRS approach; (ii) transparency about the choices (so other stakeholders, including civil society, can contribute and indicate where they disagree) along with clear country-driven benchmarks for monitoring progress; (iii) candid assessments by the BWIs of the country-driven choices and progress made; and (iv) transparent BWI and donor decisions on financing selectivity, drawing *inter alia* on these assessments. We do not propose an approach based on universal minimum standards, for reasons given in the report. Second, we are not suggesting that the IMF (or World Bank) artificially force the pace of reforms of domestic processes through conditionality; on the contrary, the thrust of our recommendations is to allow greater scope for country

diversity, recognizing the wide divergence in starting conditions and political structures. While we agree that our proposal could be seen as a kind of “process conditionality” (para. 18), this is inherent to the whole approach of requiring countries to produce a PRSP. Our proposal has the merit of allowing greater customization of the process to country needs and circumstances. While everyone recognizes that country ownership is critical, a candid discussion is needed of how best the design of the approach can manage operationally the tensions between ownership, BWI assessments, and selectivity in financing decisions. As illustrated in the report, such judgments are obviously made in practice, but in a manner that is less transparent than under our proposal, and that gives too much weight to meeting BWI procedural requirements rather than more fundamental improvements in domestic policy processes.

We agree that a key challenge for the IMF is how to apply PRS principles in “difficult” cases, including those where there is not yet an operationally viable PRSP. The particular steps mentioned by the staff in para. 29—opening up the policy debate on a few key priority issues, including through PSIA designed to explore various policy options, and contributing to capacity development following country-driven priorities—follow the thrust of our recommendations and would be very helpful. However, it is important that PRSP and PRGF-related activities not be seen as proceeding on separate tracks, as the staff's proposal in para. 30 seems to imply. In particular, we do not see how efforts to better integrate the two sets of activities would risk “derailing the incipient participatory process.” Quite the contrary, the aim should be to seek opportunities to use the PRS principles, including through informing a broader policy debate, to ease political economy constraints that have made progress so difficult in such cases. Otherwise, there is a serious risk that delinking PRSP and PRGF activities would eliminate a key incentive—both for countries and for the Fund as an institution—to make progress on the PRSP front, while reverting to a “business as usual” mode on the PRGF side.

## THE ACTING CHAIR'S SUMMING UP

### EVALUATION REPORT OF POVERTY REDUCTION STRATEGY PAPERS AND THE POVERTY REDUCTION AND GROWTH FACILITY BY THE INDEPENDENT EVALUATION OFFICE

Executive Board Meeting  
July 21, 2004

#### General Remarks

Executive Directors welcomed the timely report of the Independent Evaluation Office (IEO). The report has a number of constructive recommendations, which will require careful further follow-up and implementation with a view toward strengthening the PRSP approach, clarifying the Fund's role in this approach, and enhancing the Fund's advice and assistance to low-income countries. More broadly, the IEO report is a valuable contribution to the ongoing review of how to improve the effectiveness of the Fund's engagement with low-income countries.

Most Directors considered that the PRS approach has had a positive impact on economic policy design and implementation in low-income countries. It has helped to improve country ownership, enhance participation, and provide better-quality strategies, and it is generally evolving in the right direction. At the same time, Directors stressed that substantial scope exists for better implementation of the current approach, based on the evolving experience and the directions for change identified in the IEO report. In this context, Directors noted that the report found that PRSPs suffer from a multiplicity of objectives, which contribute to significant weaknesses in their implementation, observing that: the approach is perceived to be externally driven; participation sometimes has been narrow, particularly in formulation of the macroeconomic framework underlying the PRSP; and that PRSPs often have lacked operationally viable strategies. At the same time, Directors cautioned against drawing premature conclusions about the ultimate success of the PRSP approach based on only five years of experience with its implementation. It was noted that resolving the mismatch between the ambitions of this approach and what can realistically be achieved will continue to remain a challenge. In light of this, the

staff should draw on the IEO's recommendations in various aspects of its work on the role of the Fund in low-income countries to deepen and refine its analysis on ways to enhance the effectiveness of the PRSP approach. In particular, the upcoming Annual Bank-Fund PRSP Progress in Implementation Report, and forthcoming discussions on the role of the Fund in low-income countries, will offer such opportunities.

Directors agreed that the report provides a useful perspective on the PRGF. They were encouraged that PRGF-supported programs increasingly are being aligned with the country-owned PRSP, even though such alignment is still somewhat limited. They welcomed the finding that the design of these programs has improved in a number of ways. For example, fiscal targets have become more flexible to accommodate increased expenditures on pro-poor programs, and there is no evidence of an excessive disinflationary bias. At the same time, Directors noted the challenge of basing Fund-supported programs on a full understanding of micro-macro linkages, which are by their nature quite complex. Directors also considered that more should be done to integrate the results of poverty and social impact analysis. They noted that, as is the case with the PRSP process, the Fund's adaptation of its programs and policy advice in low-income countries toward growth and poverty reduction is an evolutionary process. In this context, they looked forward to the recommendations of the management-led Committee on Low-Income Country Work to provide new impetus and focus to Fund work on low-income countries. Directors also considered that further staff analysis will be needed on improving the design of PRGF-supported programs, and gearing them to address macroeconomic policy challenges of achieving the Millennium Development Goals (MDGs).

Directors welcomed the IEO report's discussion of the broader implications of the PRS approach for

the Fund's role in low-income countries. They looked forward to work on refining the role of the Fund in low-income countries, including the paper on instruments and financing in August, and better defining the Fund's strategy to help low-income countries make progress toward meeting the MDGs. The joint paper with the Bank on aid, aid effectiveness, and financing of the MDGs will discuss how aid might be better mobilized. The upcoming discussion on PRGF financing and instruments will consider how to finance PRGF operations beyond 2005 and will discuss proposals for instruments to allow the Fund to respond more effectively to low-income countries faced with shocks. The Board will also have an opportunity after the Annual Meetings to discuss the Fund's role in providing appropriate signals about low-income members' macroeconomic policies in the absence of a need for Fund financing.

### Individual Recommendations

*Recommendation 1. Introduce greater flexibility in the implementation of the PRS approach to better fit the needs of countries at different stages of the process and with different capacities and political and administrative systems.*

Directors agreed that the PRS approach will need to be implemented pragmatically and flexibly, taking due account of country-specific circumstances and capacity constraints as well as the need to ensure that Fund-supported programs continue to be designed to assure macroeconomic stability and help members accelerate the pace of progress towards the MDGs. In this regard, it will be important to have a clear idea of the core objectives of the PRS approach.

Directors noted that the PRGF should be linked tightly to PRSPs that provide a sound operational road map. However, where PRSPs are not yet operationally viable, the Fund should not insist on immediate tight alignment between the PRSP and the PRGF-supported program. Instead, Fund staff should work with these members to strengthen the macroeconomic frameworks in their PRSPs so as to move toward eventual alignment. In this context, Directors noted that the Fund's efforts to build capacity and strengthen institutions through country-driven and properly targeted technical assistance to these members will be particularly important. At the same time, Directors cautioned that increased flexibility should not imply delinking the PRGF from the PRSP process, and noted that the Fund would still seek to apply the PRSP principles in its program work. Moreover, maintaining a link between the PRGF and the PRSP provides a key incentive for members and the Fund to improve the PRSP process.

*Recommendation 2. Shift the emphasis of the initiative from the production of documents to the development of sound domestic policy formulation and implementation processes.*

Directors agreed that the PRS approach has the potential to encourage the development of country-owned and credible long-term strategies for growth and poverty reduction. To accomplish this objective, there should be less emphasis on document preparation, and more emphasis on improving the capability of countries to develop and implement policies supportive of growth and poverty reduction. Directors underlined that governments are expected to be in control of the development process and policy options.

Directors noted that managing the tension between country ownership of the policies and programs and donor selectivity is central to the design of the PRS approach. Some Directors agreed with the report's recommendation that countries should set explicit criteria for judging progress towards key intermediate objectives related to the domestic policy formulation, implementation, and monitoring process for their PRSPs, and that Fund and Bank staff should provide candid assessments of those benchmarks. Many Directors cautioned, however, that this could imply excessive Fund involvement in assessing the country's decision-making processes, and establish an unwarranted direct linkage between such assessments and the Fund's lending decisions. They believed that the use of such conditionality by the Fund to improve domestic policy processes is inappropriate because it could undermine the legitimacy of domestic institutions and processes. Directors noted that further reflection and discussion will be needed on how the Fund should react in cases where it believes that the member could aim higher, or where the pace of progress chosen is not ambitious enough.

*Recommendation 3. Clarify the purpose of the JSA and redefine the vehicle accordingly.*

Directors emphasized the need for a reformulation of the Joint Staff Assessment—the instrument used by the Fund and the Bank to assess PRSPs, with an emphasis on graduated rather than binary assessments. Many Directors noted that the purpose of the staff assessment of PRSPs should be to provide candid feedback to countries and to help coordinate with the Bank. They believed that not using the assessment to shape Fund lending decisions and removing the requirement of Board endorsement would help enhance country ownership of PRSPs. In the absence of any other coordination vehicle, Directors favored keeping a joint instrument for the assessment. They noted that any reformulation of the



assessment instrument should reflect and maintain the two institutions' commitment to the PRSP initiative, while reducing the documentation requirements for the PRSP process and utilizing the limited staff resources more effectively. Directors looked forward to discussing specific recommendations by the staff on options for the assessment instrument in the context of the Annual Bank-Fund PRSP Progress in Implementation Report.

*Recommendation 4. Clarify what the PRS approach implies for the IMF's own operations and strengthen the implementation of the agreed role.*

Directors agreed that the Fund needs to set out more clearly its own role in the PRS approach in each country, based on the Fund's core mandate in macroeconomic and related structural policy issues, and use the tools—including surveillance and other monitoring mechanisms—that are best suited to the individual case. In doing so, the Fund would need to continue to strengthen its collaboration with the World Bank and other donors. While Directors welcomed the streamlining of Fund conditionality, some stressed that aggregate Fund-Bank conditionality needs to be monitored and reduced as well.

Many Directors also supported a more active role for the Fund in the public debate on macroeconomic policy design and implementation—especially regarding assumptions, alternative policy scenarios, and trade-offs. This role could be facilitated through Fund analysis and research, the Article IV consultation process, the provision of technical assistance, and a better-defined and enhanced role of resident representatives. These Directors believed that such a role should be fully compatible with country ownership of programs and policies. However, other Directors were of the view that a more proactive public role could be seen as influencing the political decision-making process, which is not part of the Fund's mandate. Some of these Directors also commented on the limitations of the participatory approach, including a tendency to produce broad and unfocused documents.

*Recommendation 5. Strengthen the prioritization and accountability on what the IMF is supposed to deliver within the broader partnership framework, built around the priorities emerging from the PRS process, and ensure resources match commitments.*

Directors welcomed the IEO report's emphasis on the need to define priorities for the work of the Fund in low-income countries in the context of its resource constraints. In this regard, the prioritization of budget resources must be guided by the Fund's overall mandate. Directors called for a careful assessment of the resource implications of adapting the Fund's role along the lines of the report's recommendations. Some Directors felt that many of the report's specific recommendations—in particular, more direct and deeper involvement in the PRSP processes—would increase the call on the Fund's staff resources considerably, and would require balancing these additional demands against other priorities. Some others thought that the report's recommendations would not involve an expansion of the Fund's responsibilities beyond what was indicated in the original policy papers establishing the PRSP and the PRGF. They noted the need to discuss the extent to which the original expectations for the Fund's role were too ambitious. Several Directors felt that there is scope for changing the Fund's way of doing business in low-income countries within existing resource constraints. Directors looked forward to staff views on ways to improve the Fund staff's involvement in the PRSP in the forthcoming Annual Bank-Fund PRSP Progress in Implementation Report and in the review of the resident representative program.

*Recommendation 6. The IMF should encourage a strengthening of the framework for establishing the external resources envelope as part of the PRS approach.*

Directors stressed that adequate, timely, and predictable donor support is crucial to the success of the PRS approach and the Fund should play a supportive role with donors and low-income members to help ensure adequate provision of aid to achieve the MDGs. In this regard, the Fund needs to consider how its signals can be clear and useful to its members. In particular, Fund signals should not lead to the inappropriate interruption of long-term development and poverty reduction finance. The Fund should also work with the donor community to enhance aid coordination and encourage medium-term support linked more effectively to country-owned poverty reduction strategies.