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
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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 PSIAs 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*.[1] 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;

[1]"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 recommendations. 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 PSIAs 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 emphasis 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.[2] 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

[2]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.[3] 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 more strategic view of the technical assistance needs of member countries in close consultation with country authorities.

[3]"Review of Technical Assistance" (SM/04/41, 2/17/04).

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.*[4] 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.[5]

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-

[4]"Aligning the Poverty Reduction and Growth Facility (PRGF) and the Poverty Reduction Strategy Paper (PRSP) Approach: Issues and Options" (SM/03/94).

[5]"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.*[6] 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.

[6]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
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. Countries need to be put even more firmly in the driver's seat by determining themselves: (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; (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.	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. 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.
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: (a) *Build in greater results-orientation.* 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. (b) *Shift in 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 (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.	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. 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). 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.

IEO Recommendation	Staff Response
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: (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. (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 *graduated* assessment of the strength of the PRS and related processes as well as of the quality of policies. (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. (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 unaddressed, especially in the area of capacity building.	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. 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. 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.

B. Recommendations Relating to the Fund's Role in the PRS Approach

IEO Recommendation	Staff Response
4. Clarify what the PRS approach implies for the IMF's own operations and strengthen the implementation of the agreed role. (a) *IMF engagement in the PRS process:* (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.	(a) *PRS process*. 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.
(b) *PRGF-related activities:* (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.	(b) *PRGF-related activities*. Staff agrees with these objectives. Staff considers that 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 in a PRGF-supported program.

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).
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:	Again, staff agrees with the objectives of prioritization and accountability, and takes note of the IEO's suggestions.
(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.	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. 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.
(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.	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.
(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.	Staff continues to welcome external reviews of all aspects of the PRS/PRGF process.
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. 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.	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. 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.