THE ‘STREAMLINING’ OF IMF CONDITIONALITY: ASPIRATIONS, REALITY AND REPERCUSSIONS

A report for the Department for International Development

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I - INTRODUCTION AND MAIN CONCLUSIONS

This paper comments on various topics relating to the current IMF initiative to 'streamline' its conditionality, setting this in the context of various other changes occurring simultaneously and of the responses of the World Bank. It undertakes a necessarily preliminary 'reality check' on the basis of brief studies of recent Fund and Bank programmes in six low-income countries:

Albania	Ghana
Kenya	Mozambique
Vietnam	Zambia

The paper additionally draws upon recent documentation relevant to this topic and on conversations in Washington with staff members of the IMF and World Bank.

For reference, questions below which are set out in bold italics are taken from my ToR (but in a reordered sequence). Questions not italicised have been added by me as possibly useful. The main attention throughout is with respect to low-income countries and, therefore, the PRGF. Less attention is paid to likely impact on middle-income and transition economies, and on stand-by credits.

Some of the principal conclusions include:

- Streamlining is narrowly conceived and supply-driven. It responds to only some of the accumulating reasons for change and not necessarily the most important. It seeks to reverse the proliferation of structural conditions, calls for greater clarity in programme documents about what constitutes Fund conditionality, and seeks to ensure that, in countries where both agencies are operating, there will be a clearer division of responsibility on policy matters between the Fund and the Bank. The evidential basis for expecting streamlining to raise programme effectiveness is rather slight and overall it is conceived as a fairly limited exercise. Streamlining is not being dovetailed with the changes intended to result from the introduction of the PRGF nor with concerns about ways of enhancing ownership. A more 'joined-up' and demand-oriented approach might well help to reduce some of the weaknesses identified here.

- Streamlining is confined exclusively to 'structural' conditionality. There is no comparable re-examination of its traditional quantitative macroeconomic stipulations. While it is true that much of the proliferation occurred in 'structural' conditions, the limited nature of the streamlining exercise missed an opportunity to re-visit the appropriateness of the Fund's conventional macro conditions.

- Results reported so far indicate substantial differences between the aspirations of the Fund's management and actual changes so far achieved. There has been real streamlining of conditionality in some countries but in others it has largely been business as usual, particular among those with 'old' (former ESAF) PRGFs. That streamlining has occurred in some cases suggests that the basic concept and the guidance provided have been practicable, although there remain difficulties about defining what constitutes a 'critical' structural policy condition and in what circumstances streamlining is the most applicable. On average, the number of structural conditions in PRGFs has so far been reduced by about a quarter, although the extent of this has been very context-dependent, with large reductions in some programmes and no change in others. We find little progress in the intended clarification of the content of Fund conditionality within programmes.

- Pronouncements and documentation on streamlining make little reference to ownership. Cutting back on the number of detailed structural conditions should be helpful but there may be countervailing factors and it is by no means clear that streamlining will bring any net encouragement to ownership. It was designed for a different purpose and questions of negotiating processes and styles would need also to be addressed if the ownership factor was to be addressed satisfactorily.

- It appears that 'new' PRGF programmes - but not 'old' ones - are paying more attention to the specifics of social sector spending. It seems also that the content of conditionality in the former is changing to some extent. Detailed structural conditionality is diminishing but there has simultaneously been greater attention to governance and public expenditure management. There also appears to have been some greater accommodation of budget deficits but little movement with respect to consideration of alternative budget scenarios.

- As regards PRSPs, early evidence suggests that this experiment is not yet working fully as planned. It appears so far that PRSPs have tended to be rather general, weakly prioritised and of variable quality. Such defects reduce their value as templates within which IFI programmes can be designed. In some cases, there are questions about the degree of government commitment to these strategies and this problem has been aggravated by the perverse effect on incentives of the link between PRSPs and HIPC debt relief.

- Although the World Bank has made statements in favour of streamlining, it appears that, in fact, there is little going on in the Bank comparable with the Fund exercise. There appears to be no institutionalised attempt to further reduce the quantity, or narrow the focus, of the Bank's conditionality. What may happen is that many of the more important structural conditions dropped by the Fund will be taken up in Bank programmes, which may then drop some of its own less central conditions.

- Fund-Bank collaboration appears to be working quite well, although there are apt to be problems of sustainability, there may be difficulties in establishing which is the be the 'lead agency' in particular instances, and it may be more difficult to achieve co-ordination in countries which do not have a PRSP.

- There is a good deal of cross-conditionality between the two institutions at the level of broad performance, probably more so than was in existence before the introduction of streamlining and the new credit facilities. At the same time, both institutions seem clear that cross-conditionality should *not* be applied to policy specifics within either programme.

- Overall, many borrowing governments which are also subject to HIPC conditions have probably found themselves in a tighter policy straight-jacket, notwithstanding the possibility of some net reduction in the combined Fund-Bank quantity of conditionality. This trend sits ill with the growing appreciation of the limitations of the modalities of conditionality. For them, it would be very difficult to state with confidence that they now have more freedom of policy choice than they had, say, two years ago, although the evidence does not yet permit any firm conclusions. Reduced policy freedom could scarcely fail to impact adversely on ownership. It would also almost certainly increases the transactions costs to governments of accessing the assistance on offer, a feature worsened by an apparent absence of serious efforts at the co-ordination of PRSP-IMF-World Bank-HIPC conditionality and the resulting monitoring and reporting requirements.

- In principle, governments now have, in the PRSP, a vehicle for influencing the framework of conditionality but we have found no examples of governments seeking to use it in that way. A probably more common pattern is that they have drafted their papers to second-guess what they think the IFIs/creditors would like to see, and that papers have so far been too unspecific to make much difference to conditionality. The IMF appears not to have engaged in much bilateral discussion with borrowing governments concerning the design of streamlining.

- Our evidence suggests that neither the small number of PRGF or PRSC programmes so far negotiated have differed markedly in design from their predecessors, although in some PRGFs the extent of structural conditionality has been much reduced. This again suggests that borrower influence on the programmes may be little changed. However, the PRSP experiment is still young and the crucial test will be if a government produces a full PRSP, based on wide consultation, whose policies differ materially from what either IFI would choose.

Policy recommendations are made at the conclusion of the paper.

II - ON IMF STREAMLINING

Q1: To what questions is streamlining addressed?

Current Fund actions concerning its conditionality are the outcome of a variety of pressures for change. The following factors can be identified:

(a) An unplanned growth in the number of 'structural' policy stipulations per IMF programme. Goldstein (2000:82) quotes mean figures of two structural conditions per programme in 1987, seven in 1994 and 14 in 1997-99.[2] He further records that even Fund staff regarded only about a third of such provisions as critical to programme success. There has also been an increasing trend in the use of prior actions, particularly with respect to

[2] See also IMF, 2001A, Fig 2, for alternative data on the rise of structural conditionality, also showing a sharp rise.

structural conditions and a recent Fund paper shows that 17 of programmes initiated in 1995-99 had more than 10 prior actions. Most of these cases were transition economies but four were PRGF countries (IMF, 2002: Table 1).

(b) Accompanying this, an increasing lack of clarity about what constitutes Fund conditionality and what does not, with particular uncertainty about the status of measures included as structural benchmarks: not formally part of programme conditionality but widely taken to be so.

(c) Growing internal Fund acceptance of long-standing external criticisms that it has serious difficulties in securing compliance with programme conditions, which produce only mixed results, even in the macroeconomic area. Two recent IMF *Working Papers* provide further evidence of such difficulties. Mussa and Savastino (1999: Table 2) rate as failing programmes where actual disbursements are less than half of agreed amounts and show a rising proportion of programmes failing this test over the last two decades, after an earlier period of apparently improving outcomes (percentage of programmes less than 50% disbursed):

1983-87	29%
1988-92	33%
1993-97	46%

Ivanova *et al* (forthcoming, Table 1) similarly show that in 1992-98 only a quarter of ESAF/PRGF programmes were *not* subject to some interruption and that nearly half (45%) experienced irreversible interruptions.[3]

(d) Following the growth of an empirical literature on the centrality of country 'ownership' in aid effectiveness, recent Fund acknowledgement of the relevance of this to its own operations. Econometric analysis by Ivanova *et al* (forthcoming) show the dominance of domestic political-economy factors in determining Fund programme success and also that neither heightened 'effort' by Fund staff nor even increased resort to prior actions could substitute for favourable political-economy conditions and exerted no significant influence on the likelihood of programme implementation (Thomas, forthcoming). Associated with this, a Fund paper on conditionality policy issues (IMF, 2001B:55) asserted the position, apparently with approval, that the primary role of IFIs "is to identify reformers, not to create them" and that "IFIs should have no illusions that their conditionality will appreciably affect the probability of reform." Indeed, the Fund's own

[3] They also show an apparently more satisfactory 73% compliance with programme conditions but this figure is hard to interpret because the authors regard this figure as biassed upward. For a useful very brief review of other evidence on programme effects see IMF 2001A:45-46.

Executive Board is on record as stating that "conditionality cannot compensate for a lack of programme ownership". These influences have led to a recent Board paper on the strengthening of country ownership in Fund programmes (IMF, 2001C).

(e) Because of the growth of longer-term lending, via ESAF and now PRGF, and associated structural conditionality, and despite efforts to achieve greater co-ordination, there has been a growing overlap between the structural adjustment activities of the Fund and the World Bank. This is seen as having resulted in a loss of clarity about which institution is responsible for certain policy areas in a given country, to which the introduction of PRSP and HIPC-related conditionality has added further layers of complexity.

Turning now to the streamlining exercise, it is evident that this only responds to some of the above factors, and not necessarily the most important ones. In the words of the Fund's *Annual Report* for 2001 (IMF, 2001D:45), "the main goal of streamlining was to make conditionality more efficient, effective and focussed..." There is virtually no reference here or in other Fund documentation on streamlining to the ownership issue, and that streamlining will raise programme effectiveness is apparently taken as axiomatic, with little supporting discussion. Of the factors listed above, streamlining directly addresses (a), (b) and (e). It seeks to reverse the proliferation of structural conditions, calls for greater clarity in programme documents about what constitutes Fund conditionality, and seeks to ensure that, in countries where both agencies are operating, there will be a clearer division of responsibility on policy matters between the Fund and the Bank.

Note here that the Fund's streamlining is confined exclusively to what they classify as 'structural' conditionality. There is no suggestion of any comparable change in its traditional 'quantitative' or macroeconomic stipulations. No doubt the Fund would justify this because it has been in the 'structural' area that much of the conditionality proliferation has occurred, with less change in macro components. Nevertheless, the streamlining exercise, and the debates it sparked, would have been an opportunity to re-visit the appropriateness of conventional programme macro conditions, both as to design and extent, and it is a pity that this opportunity appears to have been missed.

We shortly take up the question of the extent to which streamlining is liable to make much contribution to country ownership and suggest that any effect is apt to be rather slight (see Q.3). This is a reason for not expecting large improvements in programme compliance and effectiveness. In fact, and rather surprisingly, there is little evidence that the quantity of conditionality has much influence on programme outcomes, raising questions about the likely impact of streamlining on programme effectiveness. Galbis (2001:176) cites Fund evidence showing the rate of programme implementation to be constant with respect to the number of conditions; Ivanova *et al* (forthcoming:31) do find outcomes to be inversely and significantly affected by the number of conditions per programme year but, overall, find this and other variables under the Fund's control to be dominated by in-country political-economy variables. Evidence from the Bank is similar. One study (Dollar and Svensson, 2000, Table 3) finds the number of conditions in Bank adjustment programmes to have no significant influence; a subsequent investigation (World Bank, 2001A:80) finds an inverse relationship between the number of conditions and programme outcomes but points out that the causality could run either way, with a tendency for weakly-performing countries to receive more intensive conditionality.

Streamlining, in other words, is conceived as a fairly limited exercise and it would, therefore, be unwise to expect it to make more than a modest contribution to the success of Fund programmes.

One other factor to bear in mind is that there may be a tendency for Fund practices to regress and for the extent of structural conditionality to begin to increase again after the present initial phase of streamlining. The history of the Bank's adjustment lending until the late 1990s showed the strength of institutional resistances to cutting back on the number of conditions. The proliferation of Fund conditionality arose chiefly from a trend towards ever-more detailed monitoring of structural reforms, and pressures to again move in that direction may reassert themselves unless a sustained effort is made to avoid it, not least because of some reported staff scepticism about the desirability of streamlining (see Q.2 below).

Q2: Has the Fund developed a clear policy on streamlining conditionality? How have tensions between different approaches to streamlining been resolved? Are the revised guidelines on streamlining conditionality practicable and useable? Are there clear and useful differences between conditions that are critical rather than just relevant to the success of a programme?

There seems no question about the commitment of the Fund's management in pursuing its streamlining agenda. The documentation prepared to guide this effort, such as the 'Interim Guidance Note', has been of good quality and there appears to have been a serious effort to follow this through, e.g. in terms of the documentation to be prepared for the Board. The Fund's Legal Department is reported as requiring missions to justify the macroeconomic relevance of remaining structural conditions. Programme submissions are expected to demonstrate reduced structural conditionality, with careful justification of such conditionality as remains, and the specific content of the programme's conditionality is required to be explicitly defined.

At the same time, it is well known that the Fund Board is divided on how far the reduction in structural conditionality should go. It specified a number of issues for further examination and gave the Managing Director less than full-blooded backing. Staff members are, of course, aware of these reservations and those opposed to the changes may be emboldened in resisting change. Note, however, that the disagreements are about where the balance should be struck between limiting the extent of conditionality and safeguarding the implementation of desired structural reforms, rather than about some alternative model of streamlining.

The main practical difficulty - and a potential threat to the sustainability of the exercise - has arisen in attempts to define what constitutes a 'critical' policy condition in an approach that requires that structural conditionality should be confined to measures regarded as critical to success, in the sense that if they were not carried out they would jeopardise the entire programme. The difficulty, as is widely recognised, is that what is critical requires a good knowledge of each specific economy and how it is likely to respond to policy changes. 'Criticality' is necessarily a matter that can only be decided case-by-case, which leaves a large amount of discretion to Mission Chiefs. In order to develop a more generic approach, Fund staff plan to prepare a Board paper on the definition of criticality during the next few months. This will seek to derive general principles and practical guidance from the country experiences that have accumulated by then. It also appears that there is quite a lot of looseness about what is understood as 'structural', although it did not appear that this is regarded as a problem by the staff.

Although, by common consent, it is too early to make more than the most preliminary judgements, results reported so far indicate that some, undramatic, changes have been effected.

This suggests that the basic concept and the guidance provided has been practicable. The first internal report on progress with streamlining indicates that, by comparison with 1997-99, the average total number of structural conditions per 'new' PRGF programme (i.e. programmes not merely converted from pre-existing ESAFs) was down from 14.7 to 11.0, or by a quarter (IMF, 2001H). There is more to streamlining than merely reducing the number of conditions but the same report also claimed that these reductions had been accompanied by an improved focus on the Fund's core areas of expertise - financial, exchange rate and, especially, fiscal policies - so that the proportion of conditions falling into these subject areas had risen from about a half of the total to about two-thirds. Moreover, the detailed figures indicate that the reductions have not merely occurred with the 'easy targets' of structural benchmarks: the number of prior actions and performance criteria has gone down in roughly the same proportion as the benchmark conditions.

Independent corroboration of genuine reductions is provided by Adam and Bevan (2001), who point out, however, that the extent of this has been very context-dependent, with large reductions in some programmes and little change in others. They make a distinction between countries that are 'stabilisers' and 'post-stabilisers' (plus a third category to catch countries that fit easily into neither of these classes). It was among the post-stabilisers that they observed the largest reductions; much less so among countries whose problems remain the classical IMF ones of macroeconomic imbalances.

Our own country studies reveal an extremely mixed picture. The most spectacular example of streamlining is provided by *Mozambique*, where the number of conditions is reported to have been reduced from 30 in the previous programme to just three, all of which were macro-relevant. *Albania* is another case, with a PRGF containing only three (macro-relevant) structural conditions. Both these countries could be described as belonging to the post-stabilisation category. However, *Kenya* could also be regarded as post-stabilisation, in that the macro situation is quite sound and the budget is under control, but Kenya nevertheless has a PRGF with a very large number of structural conditions. There is, of course, a long history of troubled relations between the Kenyan government and the IFIs, which suggests the plausible hypothesis that it may be *reputation* which is the crucial variable in determining the extent of streamlining, rather than stabilisation as such. Between early-1999 and mid-2001 little change was observable in the extent of conditionality in *Ghana's* PRGF, while the position in *Zambia* is that the number of macro conditions has been reduced (from seven to four) but structural benchmarks have *risen* from one to seven. Both these countries have had reputational problems in the past but now have new governments which have yet to establish a track record, good or bad.

Streamlining hence emerges as highly contingent. Most of the programmes from which the above information is derived are 'old' PRGFs, i.e. converted from former ESAFs. It may be, therefore, that a more consistent application of streamlining will emerge in due course from the 'new' PRGFs, i.e. post-September 2000. However, this should not be taken for granted, for, if the Fund wished to streamline its old PRGFs it has a ready instrument for doing so, in the form of its periodic (usually semi-annual) review missions. For example, the present Zambian programme was originally negotiated as an ESAF but has since been the subject of three full-scale reviews by Fund staff, each of which set out the policies and conditionalities for the next period. One of the functions of such reviews, and the new Letters of Intent which accompany them, is to keep programmes in line with contemporary Fund policies. On a strict interpretation, therefore, it should be appropriate to judge old PRGF programmes by the same standards as new ones. On the other hand, it seems reasonable to expect that the original programme would leave some footprints, even after successive reviews, and this should moderate the extent to which old programmes should be judged by the 'new' standards.

An aspect of the streamlining exercise which has been less than impressive relates to the clarification of what constitutes the Fund's conditionality in a given PRGF. In its original intention, this particularly related to the growth in the use of structural benchmarks and the ambiguous status of these. According to the Fund, these should not be regarded as formally part of PRGF conditionality but are, in fact, widely regarded as such. This was illustrated for the present writer by the fact that when he separately asked two Fund Resident Representatives whether they regarded such benchmarks as part of conditionality one replied Yes, the other No. This illustrated that clarification was indeed desirable. Unfortunately, however, the Fund appears recently to have been rowing back from that aspect of streamlining, for a recent paper (IMF, 2002: para 73) asks that Letters of Intent and Staff Reports place all elements of conditionality in one place, including "the areas on which program reviews will focus, indicating any structural benchmarks against which performance will be assessed." Does this make benchmarks part of conditionality or not? Seemingly so but ambiguously. How should borrowing governments regard such provisions?

Q.3: How would the guidelines on streamlining fit with the drive to increase country ownership? How can streamlining strengthen ownership? How have they changed the relationship between the Fund and the countries?

Fund staff have begun to interest themselves in the issue of how to increase national ownership of Fund-supported programmes, as shown by the paper on this topic (IMF, 2001C) recently presented to the Board. This appears to be an important 'first' and will hopefully lead on to substantial further debate. However, a search of the key documents reveals that this interest is little shared by those driving the streamlining exercise. Thus in the *Interim Guidance Note* issued to staff and in the staff review of initial experiences with streamlining (IMF, 2001H), as in the Managing Director's presentation of this to the Board, there is very little reference to ownership. The recent ownership paper just mentioned does see a connection, arguing that streamlining can increase domestic ownership by increasing the Fund's flexibility (although the meaning of that is unclear) and by reducing its micro-management of structural measures, thus increasing national control over non-critical structural policies and their implementation.[4] That is really the sum total of what Fund papers have to say on the ownership-streamlining connection. The beneficial effects of reduced micro-management is a perfectly valid point but a rather limited one, especially if the Bank will be taking over much of the 'structural' conditionality now dropped from Fund programmes (see Q.9). It is also a point that is silent on the issue of the *rigour* of the remaining conditionality. Since streamlining is essentially intended as an efficiency-improving exercise, it seems likely that the conditionality which remains (and we should again bear in mind that streamlining is not intended to do anything about macroeconomic conditionality) will be monitored and enforced with increased rigour. If so, it is by no means clear that governments will feel any net increase in their freedom of choice.

[4] See also Khan and Sharma, 2001:21 for a similar argument.

To a very substantial extent, ownership is about *process*. It is precisely one of the strong points of the PRSP initiative that it addresses this and sets up processes intended to enhance national ownership. But what about the Fund's own negotiation style? The streamlining guidelines are silent on this, as distinct from substantive programme content. This is unfortunate, since members of the Executive Board are on record as being concerned that the Fund's regular programme processes "sometimes short-circuit national decision-making and ownership" (IMF, 2001G:2). Even if we look more widely at programme types that, being linked to the PRSP initiative, might be expected to show more sensitivity to these issues - notably the PRGF - there is accumulating evidence that little is happening to styles of negotiation. A major, if necessarily preliminary, review of experiences with PRSP processes commissioned by the SPA concluded on the Fund that, while it was too early to expect much change of substance, there was also little evidence from eight detailed African country studies of a change of style, with negotiations remaining confined to a small number of policy actors, and with non-transparent negotiations and outcomes (Booth, 2001:27-28). A December 2001 report based on studies of Bolivia, Honduras, Zambia and Cameroon by the Catholic Relief Services (2001:13) has similar complaints.

Our own country studies reported similarly. In all six countries, no substantive changes in process were reported. What was reported for *Zambia* is essentially valid for all the other countries too: "It appears that negotiation processes have changed little and remain essentially closed-doors affairs with the Ministry of Finance and central bank. It appears that there has been little or no consultation with wider audiences, either in civil society or even with other government departments." This does not necessarily mean that the governments in question were not committed to the resulting PRGF programmes, however. Commitment varied from weak or suspect (Kenya, Zambia) to quite strong (Albania, Mozambique and Vietnam). Often, however, this commitment was strongly concentrated in a few central ministries and agencies, and the point here is that there is no evidence of changes in Fund processes designed to broaden and deepen country ownership of the programmes they negotiate.

We enquired whether the governments in our sample of countries had expressed any strong views on streamlining and had participated in the recent Fund review of its conditionality. Perhaps surprisingly, there was a nearly nil return on this. Only in *Zambia and Kenya* were there any recorded views but the Kenyan one appeared designed for a local political audience rather than to make a serious contribution to the debate. This nearly 'nil return' perhaps reflects the fact that, apart from a number of wide-ranging consultative meetings involving a large number of different stakeholders, the Fund has not sought to engage bilaterally with member (or debtor) governments in order to actively solicit their responses to the streamlining initiative.

However, the Kenyan case revealed an interesting phenomenon (with some echoes also in Zambia), of CSOs siding with the IMF against their own government:

> Frustrated by the political hegemony of one party since independence, two decades or more of resistance to reform and democratisation, and the absence of self-correcting mechanisms within the political process, civil society and the wider public have come to see the conditionality of the IMF and other donors as their best hope for change. There is hence much support for what the IMF is trying to achieve and a desire that they should not provide more financial

> assistance to the incumbent regime. Indeed, for the past three years civil society organisations have petitioned the IMF *against* providing any more credits to the Moi government. The types of change on which the IFIs have conditioned renewal of their programme support are popular among the Kenyan public, who want the IFIs to stand firm.

In their campaigning, however, they have received scant encouragement from the Fund. Overall, it is doubtful whether streamlining, *per se*, does much to enhance national ownership of Fund-supported programmes. Cutting back on the number of detailed structural conditions should be helpful, as should greater clarity about the content of programme conditionality. But we have already suggested that the extent of actual clarification appears to be limited and, overall, it is by no means clear that streamlining will bring any net benefit to ownership. Simply, it was designed for a different purpose and a more widely-based approach which addresses the process issue would be necessary if streamlining were to become a major ally of ownership.

Q.4: How different are PRGF programmes? *Have poverty reduction and growth objectives constrained the design of streamlined macroeconomic programmes?*

These questions perhaps beg the prior issue of how much change it is appropriate to look for. This arises partly because it is too early to form more than a very preliminary view but also because there may have been a tendency to exaggerate how much change the PRGF was likely to introduce. Adam and Bevan (2001:3, 28), for example, warn that one should not expect to find major changes because PRGFs do little more than incorporate already-existing best practice under their ESAF predecessors, although they do add that the shift from PFPs to PRSPs is potentially important. Their position is rather reinforced by the Fund's own statement of the PRGF's 'key features' (IMF, 2000:1). This provides an admirable explanation of what the PRSP initiative is trying to achieve in enhancing ownership...

> The PRSP approach is intended to bring about substantive changes in the way countries' programs are formulated. The core objective is to arrive at policies that are more clearly focussed on growth and poverty reduction, in which the poverty reduction and macroeconomic elements of the program are fully integrated, and that embody a greater degree of national ownership, thereby leading to more consistent policy implementation. One implication of this is that agencies providing external assistance will need to change the way in which their programs support the efforts of national authorities.

... but is notably unspecific about how the IMF should "change the way" of negotiating PRGFs.

We have already remarked that, on the evidence so far available, there is little sign that PRGF processes are changing. Perhaps the most notable change in the intended *content* of PRGF programmes is that these are supposed to result in national budgets more helpful to poverty reduction and growth, e.g. through tax reforms, reorientation of government spending and improved targeting on the poor. There are indeed some reports that 'new' PRGF programmes are paying more attention to the specifics of social sector spending (e.g. CRS 2001:14) but our country studies found scant evidence of programme designs that had been in any way constrained, or even influenced, by the poverty reduction objective. The only exception to this was a report on *Albania* that "the Fund appear to have insisted on provisions in the privatisation of the Savings Bank about notification of the closure of Rural Branches and appear to have taken the decision on electricity subsidies partly influenced by social impact." That is all.

However, the *Zambia* study threw up a general issue of some importance. It observed that, while Fund staff had continued to concentrate on putting together conventional ESAF-type programmes little influenced by the poverty reduction objective, the latest PRGF does contain substantial references to the I-PRSP and HIPC-related policies, and one of the programme's conditions is that government produces the progress report agreed under HIPC to facilitate tracking of HIPC-related expenditures. This raises a more general issue about the desirable links between PRGF and HIPC programmes. In effect, the Fund in Zambia has been using the existence of a HIPC agreement to maintain a fairly conventional programme of its own. Given the desire to focus the Fund more on its core areas, this seems reasonable for HIPC countries, but has this linkage been thought through?

It does seem that the content of conditionality is changing to some extent, subject to the qualification that there are large variations across countries (Adam and Bevan, 2001, *passim*). In line with the streamlining policy, detailed structural conditionality is diminishing in some cases and is tending to become more focussed on macroeconomic issues, but Fund sources suggest that there has simultaneously been greater attention to conditionality relating to governance and public expenditure management (a feature also strongly evident in our *Kenya* case study)[5] - scarcely one of the Fund's core areas of competence.

There is also reported to be a proportionate increase in the use of prior actions, although a recent Board discussion called for less of this.[6] Part of the Fund's rationale for prior actions is that they provide an opportunity to "demonstrate the authorities' determination and political will to implement the programme as formulated"[7] and this rationale was reflected in the recent Board discussion just mentioned. The reasoning here is obscure. It seems to this writer that prior actions are a device for exerting the maximum available financial leverage on a borrowing government to undertake an action which there must be a presumption they would not otherwise implement (otherwise it would not need to be a programme condition). Nothing positive can be inferred from a Prior Action about the government's attitude towards the measure in question. A more common sense view sees a requirement for a prior action as the ultimate signal of distrust,

[5] See notes of HMT/DFID meeting on the IMF PRGF review, 14 November, 2001.

[6] From notes on Board meeting of 28 January 2002.

[7] From a 1996 policy paper, cited in IMF, 2002, note 37.

an acknowledgement of differences between the preferences of the Fund and borrower. As such, it creates strong doubts about the extent of local ownership. These are IMF-owned measures *par excellence*.[8] Furthermore, as a modality, because of its gun-at-the-head nature, it seems particularly likely to generate local resentment and not to fit in with local political decision-making. It is to be hoped, therefore, that the use of prior actions will diminish as a result of streamlining.

A clear distinction should be drawn here between the use of prior actions and what is often referred to as *ex post* conditionality, i.e. the provision of a credit largely on the basis of a government's already-established track record of macro management and policy reform. Of course, such a track record, having previously been freely adopted by the government, does indeed demonstrate ownership and political determination. However, with few exceptions, the Fund and its Board have been reluctant to go far down the route of *ex post* conditionality.

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[8] In support of this line of argument, see Box 5 (p.31) of IMF, 2002, summarising how prior actions had been used in a sample of 12 countries.

In response to criticisms that past Fund budget ceilings have been set too low in countries without acute macro disequilibria, PRGF programmes are intended to embody "greater flexibility in accommodating rising budget deficits..." (IMF, 2000:4). Here too there appears to have been progress. Adam and Bevan (2001) report this in the programmes of a number of the countries they studied (Rwanda, Uganda, Vietnam) and there are reasons for predicting this as a more general result. According to a Fund spokesman, 17 new PRGFs have more flexibility than in other programmes, and, in specified circumstances, allow governments to increase spending without the need to seek Fund permission.[9] On the other hand, we found little evidence of such a trend among our case studies. One of the intended features of PRGF negotiations is that Fund staff are encouraged to engage in discussions of alternative fiscal scenarios but this had not happened in our cases. In *Kenya* it was publicly ruled out by a visiting Mission Chief. The only partial exception to this 'nil return' was *Mozambique*, where it was reported that alternative scenarios were discussed internally between the Fund and the Ministry of Finance, although it is not clear what they covered. However, the Joint Staff Assessment for the PRSP called for a low-growth scenario to be included as a contingency if the high 'central' projection did not materialise but this did not happen.

To the extent that there is indeed increased flexibility, this is partly because of Fund changes in how they calculate the budget deficit, now including ODA grants where formerly these were 'below the line'.[10] It may also arise because of the frequent linkage of PRGFs to HIPC debt relief arrangements, where the potentially considerable relief can further augment budgetary resources, especially those devoted to social sector spending. For this to have its maximum effect, however, this relief must be 'new money' with no offsetting falls in other forms of ODA but there is evidence that some donors are reducing new aid as an offset to the budgetary cost of debt relief (Gunter, 2001). There may also be greater willingness on the part of the Fund to accommodate unforeseen shocks. Lastly and although the Fund is naturally coy about stating so publicly, there probably has been some greater permissiveness in its attitude towards the budget deficit-price stability tradeoff. No-one claims this to be more than a marginal relaxation but at least in this regard it could be said that the poverty-reduction objective is influencing, if not actually constraining, the design of PRGF programmes.

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[9] Source as for note 4.

[10] Note, however, that the Fund has not yet taken the extra step of counting the grant elements of concessional loans, notably by IDA, as urged by HMG.

One respect in which PRGFs are supposed to improve on their predecessors is by the inclusion in programme documentation of poverty and social impact analysis (PSIA), with the 'Key Features' document stating that when a programme is liable to have adverse effects on groups of the poor "it is *essential* to demonstrate that these effects have been carefully considered" and, if possible, countervailing measures built in. In practice, however, it is unclear how much progress has so far been achieved, with the Fund (and Bank) still struggling with the methodological issues arising. Among our country studies, some PSIA work had been undertaken in Vietnam and this may have been true in one or two other of our countries. This is probably an area which will see more progress in the future but for the time being, as a spokesman put it, cultural issues within the Fund mean it is still sometimes hard to see how a programme has changed as a result of poverty impact analysis.[11] There is little point in undertaking PSIA work unless this results in changes in programme design.

Q.5: ***What are the risks in streamlining? Has the Fund retained an understanding of structural issues even though passing responsibility to the Bank for some reforms?***

Perhaps the biggest risk in streamlining is that too much will be expected of it, so that what turns out to be a modest but sensible efficiency measure will unjustifiably come to be seen as a failure. Relatedly, there is the risk of institutional regression discussed under Q.1, i.e. a tendency after a while for an escalating trend of conditionality to re-establish itself. We do not see a risk of a major weakening in efforts towards structural reforms (a) because the Fund is firm in the desire to retain (stricter?) conditionality in structural areas it regards as critical to programme success; (b) because a good deal of conditionality relinquished by the Fund is likely instead to be taken up by the Bank and perhaps bilateral donors; and (c) because it is extremely easy to exaggerate the effectiveness of past 'non-critical' structural conditionality.[12] There is some concern within the Fund that the Bank's structural conditionality will not prove as effective as its own, but that may be little more than an expression of institutional bias and may be based on an exaggerated view of what was previously achieved by the Fund's own conditionality (see Q1). There might be a tendency for the Fund to lose some expertise and knowledge in subjects outside its own core areas of expertise but a more positive way of viewing this is to say that the Fund-Bank division of labour is likely to improve.

One other risk that might be mentioned concerns the situation of countries where the Bank is not

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[11] Source as in note 4.

[12] For example, IMF, 2002, Fig. 1 (p.24), shows that waivers are granted for 30-40 percent of all structural performance criteria.

also simultaneously undertaking adjustment operations. In such situations the Fund is expected to retain the full pre-streamlining range of structural conditionality but upon the advice of the Bank "or other relevant institution".[13] The risk here is that the proposed consultative arrangements may not work well, leaving the Fund seeking to determine policies that lie outside its own admitted areas of expertise. However, this is probably relevant to only a small number of low-income countries.

Q.6: ***Have the Fund adhered to the principle of the PRSP as the overarching framework of conditionality? How has this happened in practice, for example has the PRGF review been clearly linked to the PRSP review? Have benchmarks in the PRSP replaced the old-style PRGF structural benchmarks?*** **Have the PRSPs that have emerged so far been of such a quality as to permit their desired relationship with IFI programmes to be achieved?**

Answers to these questions have to be set against available (but necessarily preliminary) assessments of how well the PRSP experiment has worked so far. The most substantial independent review is contained in the ODI study (to which the present writer contributed) commissioned by the SPA donors, based on eight detailed country studies and recently synthesised by Booth (2001:57,59) whose overall conclusions are carefully measured:

> All of the main messages from our country reports are about the need for realism. The international community must keep its feet firmly planted on the ground and avoid being carried away by its own rhetoric on PRSPs. Realism is needed, moreover, on both sides of the aid relationship. Donors should ensure that they do not set excessively high standards of PRSP performance as preconditions for their support. Governments and other national stakeholders should not overestimate the likely scale of additional resources that are going to be generated. ... It seems evident that the adoption of PRSPs has brought some limited but important gains in all cases. The mainstreaming of poverty reduction – its integration with macro policy and with the budget – is a palpable step forward... [but] ...those interested in a successful outcome of the PRSP experiment may need to bide their time and look to the slightly longer term. Overall, there is a need for expectations about PRSPs to be well managed.

NGO reactions to progress with PRSP processes so far tend to be rather less positive. There was always a tension between the aspirations under the PRSP initiative for a 'transfer of programme ownership' to recipient countries and the fact that this was essentially a donor initiative. This qualified the possibilities of ownership transfer by, in effect, specifying to recipients that poverty reduction was to take centre stage in their economic and social policy making. It is therefore perhaps not surprising to find in a recent report on the ownership situation by an influential NGO

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[13] Interim Guidance Note on streamlining, section 9.

umbrella organisation (Eurodad, 2001:6, italics in original) the complaint that:

> *Despite the changes in IFI rhetoric, true ownership in development cooperation has yet to be established. There is still a critical 'credibility gap', which is increasingly leading civil society groups in many Southern countries to question the value of their participation in the PRSP process.*

This latter point is consistent with this writer's own information, that NGOs are finding it a higher priority to seek to become involved in IFI programme negotiations than to devote scarce expertise to their governments' PRSP processes. While Booth (2001:60) reports that IFI staffs have been "delicate" and appropriate in their handling of PRSP processes so far, meetings of HIPC ministers and PRSP Directors are reported as complaining that:

> The attitudes of staff of the international financial institutions have varied widely. While many have made commendable efforts to pass leadership to countries and to change the content of PRSPs compared to PFPs, too many have intervened too deeply and too early in the process, and continued to act in the manner of former PFP negotiations, with only incremental changes to policy matrixes and minimal macroeconomic flexibility.[14]

Eurodad similarly complains of excessive IFI influence over agenda-setting, and that governments limit the content of their PRSPs to measures they anticipate will be acceptable to the IFIs and their Boards. A recent report by the CRS (2001:8), based on studies of four low-income countries, similarly questions, "the degree to which true ownership of the PRSP can be transferred to the country level as long as the final endorsement rests with the international financial institutions..." Lastly, the findings of a study of HIPC Completion Point conditionality indicate a strong IFI hand in the design of this, with the implication that *either* this conditionality is not closely related to the content of PRSPs *or* that the IFIs also had a strong hand in the PRSPs themselves.[15]

Authors of our country studies were asked about the suitability and influence of PRSPs on PRGF design. The responses to this were, however, influenced by the fact that only one country (*Mozambique*) had a full PRSP available when the PRGF was negotiated. In that case, there is evidence that Fund and Bank conditionality was modified as a result of the contents of the PRSP, with less on trade matters and more on justice and corruption. The only country whose I-PRSP was thought to have had a discernable influence on PRGF design was *Vietnam*, whose PRGF was described as "designed to support" the I-PRSP. This was not the case in the other four countries, for a variety of reasons. In some cases, there was a reportedly quite close relationship between the I-PRSP's macro framework and that of the PRGF but probably because the PRGF's view was incorporated in the I-PRSP, rather than the other way round. Indeed, in connection with a recent review of PRGF experiences, the Fund itself admitted a tendency in this direction, from PRGF to PRSP.

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[14] From Debt Relief International, n.d., p.3.

[15] See 'Concluding Remarks' of SPA Task Team (2001). Note, though, that this study was confined to I-PRSPs.

Views expressed within the Bank also strike a cautious note. The IFIs seem genuinely to want change and Bank people, at least, see PRSPs as beginning to effect some genuine transfer of ownership. But much obviously depends on (1) the level of government commitment to the PRSPs and (2) the quality of these documents. On these the view is that the jury is still out. At least in Africa, probably only a minority of governments is regarded as being genuinely committed. Moreover, the quality of the full PRSPs so far prepared is regarded as variable (although none have been rejected by the IFI Boards), but respondents added that this is only the beginning of a longer-term process. The annual PRSP reviews can be used as a device for improving quality over time - producing a type of rolling PRSP. However, there may be a particularly large risk here of a growing IFI influence in strategy changes, at the expense of ownership.

For the purposes of transferring ownership and improving programme implementation, the issue of national and government commitment is clearly critical. Booth (2001:22-23) draws a rather nuanced picture:

> Governments are committed to PRSP processes for different reasons, some narrowly instrumental, others containing some medium-term vision. In several countries, stakeholders perceive the PRSP exercise as being overwhelmingly motivated by getting access to debt relief and having little further significance... These kinds of concerns notwithstanding, governments in all eight of the countries covered by this study have invested substantial effort in doing what they think to be required to produce a good PRSP. The degree to which such effort signals commitment at all levels of the political and administrative hierarchy in our countries is difficult to assess. In Kenya, Malawi and Benin, for example, an energetic process has been driven primarily at the technical level, and political commitment is unclear or non-existent. Elsewhere (Mali, Mozambique, Rwanda and Tanzania) political commitment to poverty-reduction goals seems less worrying than the commitment to implement significant change that will be found in the ministries and civil service outside the core team.

Our own country studies rather reinforce this conclusion. *Mozambique and Albania* are mentioned as countries with strongly committed governments (but see below on Albania); *Vietnam* too but with the qualification that this is largely concentrated on a few central ministries. *Kenya and Zambia* are strikingly similar to each other, in that both went through exemplary processes of consultation with wider society but possess political elites regarded as apathetic, perhaps hostile, to the poverty-reduction objective. In *Ghana* the position is less clear but the suspicion is that the recently-elected government, while not at all hostile, is more interested in the objectives of wealth-creation and private sector development.

The *Albanian* case raises an issue of wider importance, arising from its negotiations to accede to membership of the European Union:

> The Government of Albania is intertwined with the EU which is *acqui* (and not PRSP) driven. With this in mind a useful question to ask is the relationship between the Fund and the EU. According to a recent EU evaluation, there is poor co-ordination between the Bank, EU and Fund. Certainly PRGF documentation pays very little attention to the

> structural agenda in the Stability Agreement or in the Stabilisation Association Agreements (the SAA has its own structural agenda). This is a wider question of general concern about the relationship of the PRSP and PRGF process to SAAs in many accession countries. The structural agenda of SAAs is driven by a set of EC concerns but is clearly the prime structural agenda. SAA structural concerns have not been integrated into PRGF and PRSP processes.

Turning now to the specific questions posed earlier, it is clear from the above account that, at least at this early stage, things are not working out entirely as planned. To the extent that PRSPs can be fairly described as rather general, often weakly integrated with budget processes and of variable quality, this reduces their value as templates around which IFI programmes can be designed. Given the limited capabilities of the public administrations of many low-income countries, particularly in the area of policy analysis, some trade-off between ownership and quality was inevitable. If initially indifferent quality signals strong ownership this is arguably a price well worth paying.

As things stand, however, the broad, rather unspecific, nature of some PRSPs has made it easy for Fund and Bank staff to present their programmes as derived from the strategy paper because such derivation does not constrain them much in the specifics of their programmes. Both can assure their Boards that their programmes are based upon the PRSPs but such assurances may mean little in terms of ownership transfer. Our country studies suggest that it has so far been rare for the content of PRGFs to be modified significantly by the existence of a full or interim PRSP.

On the other hand, it is often genuinely difficult for them to use the PRSPs, for example as benchmark provisions, in designing their own programmes and it is consistent with this that Eurodad (2001:7) reports "the additional specification of policies and reforms in documents other than the PRSP. This has come up as an issue in the first couple of PRSCs, where there has been a tendency to make up for the lack of specification in the PRSP by adding additional details in the... Letter of Development Policy." Consistent with this, a recent SPA study of Interim PRSPs indicates that HIPC Completion Point conditionality is similarly not always based on the content of IPRSPs (SPA Task Team..., 2001:9).

The difficulties are compounded when the level of national and government commitment to their PRSPs is itself in question. To quote Booth (2001:60) again:

> Donors and IFIs are being encouraged quite rightly to take some risks in introducing aid modalities that give recipients better value. But in this respect much depends on whether PRSPs give a tough-minded and credible account of what needs to be done to reduce poverty and how this is to be done. Only if they do this can they begin to displace and make redundant externally-imposed preconditions and performance benchmarks.

Lastly, however, we should remember that PRSPs are still in their infancy and that there is a review process through which these can be strengthened in the future, especially if government knowledge and expertise improve over time. There is hence a prospect that they can begin to exert a more tangible influence in future - always provided that IFI staffs can resist the temptation to get so involved in the reviews that they undermine national ownership, and that the institutions they work for will maintain incentive systems which discourage such over-involvement.

Q.7: What issues is the Fund facing in applying streamlining in low-income countries?

With one major exception, it is not obvious that the Fund faces any special problems in applying streamlining in low-income cases. There is, of course, the perennial problem of weak domestic capacities for policy formulation and execution. That is not specific to the PRSP and streamlining exercises, although the former has created large additional needs for data, analysis, policy design and monitoring. In this respect, we should note the constructive response (to the extent that it is acted upon) of the Fund. Recognising that poor domestic capacities weaken local ownership, its recent Board paper on this topic (IMF, 2001C:41-42) suggests a reorientation of its technical assistance efforts in these countries, away from specific programme-related assignments and in favour of broader capacity-building activities. Another perennial problem which complicates the application of streamlining, is that this is likely to be much more difficult in countries with governments which the Fund does not regard as a reliable partner. On the basis of our country studies, we suggested earlier that the pace of streamlining has so far been strongly influenced by reputational considerations. Of course, this is not a problem unique to low-income countries, but it may well be that there is a larger proportion of low-reputation governments within this group than in the middle-income group.

A major difficulty particular to low-income countries, however, relates to the linkage between the PRSP-PRGF-PRSC efforts, on the one hand, and HIPC II debt relief, on the other. It is universally observed that this linkage is tending to undermine the PRSP initiative by distorting selection criteria and incentives.[16] In particular, and despite provisions for IPRSPs and transitional relief, debtor governments perceive that it is in their interests to hurry through the production of a full PRSP so as to bring nearer their Completion Point and its irrevocable commitment of debt relief. This felt imperative has been widely reported as working against adequate processes of consultation and participation involving civil society and even government departments outside the 'usual suspects' of the Ministries of Finance and Development and the Central Bank. It has also placed at a disadvantage those arguing the desirability of concentrating on production of a top-quality strategy paper; and it seems likely that the same factor has told against the data collection, information and monitoring aspects of the task, which were found by Booth and his associates to be especially weak aspects of PRSP efforts so far. The linkage may also have led to a species of rent-seeking, in which governments with little past revealed interest in poverty reduction have nonetheless jumped onto the PRSP bandwagon in order to secure debt relief, and may have led creditor governments and agencies to endorse sub-standard PRSPs because of an anxiety to avoid delaying debt relief and the financial and political difficulties that would result from delays.

III - WORLD BANK RESPONSES

Q.8: ***How will the World Bank adapt to the streamlining agenda? Is it set up to deliver in areas where the Fund may withdraw? Will the Bank's programming of its country budgets be able to adapt to changes in the Fund? How will the Bank use the PRSC in the light of the review of conditionality? Will it be used to support structural policy reform, or for medium term financing to help countries meet public service delivery targets in their PRSPs?***

[16] For example, see Fund-Bank, 2002:14, describing this as one of the most common criticisms.

Although its interim PRSC guidelines (World Bank 2001B:6) state the principle that conditionality should be selective and focus on a few key measures, this principle is not subsequently elaborated and it appears that, in fact, there is little going on in the Bank comparable with the Fund streamlining exercise. There appears to be no institutionalised attempt to further reduce the quantity or narrow the focus of the Bank's conditionality, although there is concern to improve its concentration on essentials - the so-called 'big ticket' items. What may happen, therefore, is that many of the more important structural conditions dropped by the Fund will be taken up in Bank programmes, which may then drop some of its own less critical conditions.

The Bank would argue the importance of setting its current apparent passivity in this area against a record of a declining quantity of conditionality per adjustment programme which preceded the IMF's adoption of a streamlining agenda. The Bank's recent *Adjustment Lending Retrospective* (2001A:80) records a sharp rise in the number of conditions per programme during the later 1980s but then a decline in the latter half of the 1990s. By 1998-2000 the average number of conditions per programme stood at 36 (a high enough figure in all conscience!), down from a peak in 1988-92 of 58. However, the biggest reductions occurred in what the Bank calls 'non-binding' conditions (from 23 to 8) with a smaller proportionate reduction in 'legally-binding' conditions (35 to 28). This latter figure is still excessive. It is well above the numbers prevailing in the earlier-1980s and, even in the relatively low-conditionality period of 1998-2000, Bank staff regarded only 37% of all conditions as 'very relevant' to the attainment of loan objectives (a criterion similar to the Fund's idea of 'critical' conditionality). There is, in short, ample scope for further streamlining action by the Bank but there are no strong signals that this will occur. Unfortunately, the *Retrospective* report does not examine the factors underlying the trends just described. It seems that they were more or less spontaneous, rather than the result of considered Bank decisions.

What of the role of the PRSC? In common with the PRGF, this is intended as a vehicle for aligning the Bank's programme lending operations with the borrowing country's poverty reduction strategy but has so far been rather slow in getting off the ground. This is partly because the Bank's response was tardy but may also reflect a desire, which is something of a *leitmotif* of the *Interim Guidelines* (e.g. see 2001B:9), to use the PRSC *selectively*. There are numerous references to eligibility criteria, with PRSCs being grounded in the Bank's "careful assessment of risks and rewards" and confined to countries with "strong" programmes. Where a country had a poor record in programme implementation "PRSC would be used only if there is evidence of a turnaround." As a result, the PRSC lending programme is expected to build up only rather gradually, with up to 10 countries expected to be added each year for the next three years (*ibid*, para 12).

Two questions pose themselves. First, if we take the *Guidelines* at face value, it would appear that the Bank proposes a more stringent approach than the Fund, leaving uncertain the position of countries regarded as eligible by the Fund but not the Bank. Presumably, such countries would continue to be covered by conventional Bank structural adjustment credits, even though the Bank's self-belief in the efficacy of these in low-income countries appears to have waned. (Incidentally, from my conversations in the Bank, it appeared that nothing was happening to streamline or otherwise change the nature of the Bank's traditional adjustment conditionality.) Second, however, there are bound to be doubts about the Bank's ability to sustain a policy of selectivity in such circumstances and when in Washington I was unable to obtain any clear sense as to whether this was still a major element of PRSC policy.

A specific query within Q.8 asks about the purposes for which PRSCs will be used. The answer appears to be that it is being treated by the Bank as an adjustment instrument and will be used for a combination of on-going structural reform and support of the poverty-reduction policies set out in countries' PRSPs. That is to say, the choice of subject coverage within a given programme is potentially very wide and there does not seem much danger of PRSC programmes being too narrow in conception. There is, however, a strong emphasis on public expenditure accountability, as is also the case with the PRGF. This reflects the key importance of the standard of public expenditure management for any switch, especially by bilateral donors, towards a higher proportion of programme assistance. Nevertheless, there are a lot of other areas of policy and institutional development that are also important, and such a strong emphasis on this one area raises questions whether the right balance has been struck and whether it is not time for a little re-balancing. As regards the PRSC, only three have so far been approved. That with Vietnam is apparently regarded as a special case. The other two, in Burkina Faso and Uganda, were described in the Bank as differing little from conventional structural adjustment programmes. Unfortunately, our own country studies threw no additional light on these topics.

IV - FUND-BANK COLLABORATION

Q.9: ***What is the state of Fund-Bank collaboration? How is cross-conditionality emerging? To what extent has the observed streamlining merely taken the form of a shifting of conditionality from the Fund to the Bank? Have the Fund and the Bank lost impact by shifting key structural issues from the Fund to the Bank?***

By common consent, the Fund's streamlining initiative and the efficient introduction of the new PRGF and PRSC programmes will demand close collaboration between two institutions whose differing cultures and time horizons have often proved an obstacle to smooth collaboration in the past. This has led to the warning that streamlining is at risk of turning a problem of proliferation into a problem of co-ordination. There is undoubtedly a real risk here but there are also some positive factors to consider.

First, the two institutions have already established a track record of working more closely together, e.g. in connection with the design of structural adjustment programmes, in the Financial Stability Assessment Program, and in the design and execution of the HIPC I and HIPC II initiatives, as well as in producing a succession of carefully worked-out joint statements on the principles of collaboration between them. While it would no doubt be easy to point to examples where collaboration has worked poorly - and one should never underestimate the influence of individual personalities in this connection - it does not seem to be the case that collaborative arrangements have emerged as so weak as to threaten the success of the various initiatives just mentioned. It appears that collaboration is generally working quite well, and a good deal better than in earlier periods.

This appearance is largely confirmed by our country studies. In most, the level of co-operation was reported as good; only in two countries were serious deficiencies reported and these were partly a result of personality questions. At the Headquarters level, the creation of a Joint Implementation Committee for co-operation in HIPC/PRSP countries and a joint Financial

Sector Liaison Committee are further evidence that both institutions are seized of the importance of smooth co-operation. On the other hand, our country studies were unable to report any instance in which Fund and Bank co-operation had reached the point where they were combining or co-ordinating their review processes, in order to reduce countries' transactions costs.[17]

Permanently smooth co-operation should not be taken for granted, however. First, experience suggests that early good intentions may be difficult to sustain in the face of the institutional cultural and time-frame differences. In this connection, a recent Fund-Bank staff paper on collaboration (IMF-World Bank, 2001A:13) stresses "the critical importance of Management and Board support and guidance..." Second, the country-level practicalities of close collaboration are likely to be easier in countries with PRSPs, for this should provide the over-arching framework within which both organisations will operate (but see comments in Q.6 on how PRSPs are working out in practice). There may be more difficulties in other, mainly middle-income, countries which lack such an organising framework. Finally, although the two agencies are agreed on the desirability of clearly establishing in any given country which of them is in the lead on a specific policy area, the joint paper referred to above is silent on the criteria that will be used in deciding who is to lead on what. No doubt, the answer will be obvious in most country applications but there are apt to be grey areas (e.g. on financial sector and/or budgetary matters) where disputes could arise.

One question, of particular interest to borrowing countries, is whether the Fund's streamlining initiative will merely take the form of 'passing the parcel', i.e. a transfer of responsibility for structural conditionality from the Fund to the Bank. The position is complicated but some relevant factors include:

- The Bank has in the most recent years already reduced the number of policy conditions in its adjustment lending but currently there is nothing going on in the Bank comparable with the Fund streamlining exercise (Q.8).

- Both Bank and Fund are concerned to improve their concentration on essentials, however. What is likely to happen is that many of the more important structural conditions dropped by the Fund will be taken up in Bank credits, with the Bank then dropping some of its own less critical conditions. According to a Fund staff report on initial experiences with streamlining

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[17] The closest to such co-ordination among our six cases was in *Mozambique*, where the PRGF, PRSP and HIPC Completion Point documents were all presented on the same day, but that did not require the same degree of Fund-Bank co-operation.

(IMF, 2001H:17, 34), the Bank is "strengthening" its conditionality in areas, such as privatisation, health system reform and public sector reform, from which the Fund is scaling back. In a number of cases, the report states, "measures no longer covered by Fund conditionality were incorporated as conditions by the Bank, but in others this was not the case. There should be no presumption that everything the Fund ceases to cover under conditionality is subsequently covered by the Bank, since under these circumstances, countries would not benefit from increased flexibility in policy implementation."

- One should not, in any case, exaggerate the extent to which the Fund has actually reduced its structural conditionality - this is down overall by only a quarter so far, although much more in specific cases and much less in others. And Fund streamlining applies exclusively to 'structural' conditions; nothing has happened with respect to macro conditionality.

- IFI staff acknowledge there may be institutional pressures to reverse any reduction of conditionality over time, so that vigilance will be necessary to avoid this (see Q.1).

As regards cross-conditionality, the formal position has been set out in a joint paper in the following rather elaborate statement which is worth reproducing at length (IMF-World Bank, 2001A:26):

> Each institution remains separately accountable for its lending decisions, and any conditionality that is critical for the success of one institution's program would continue to be specified in that institution's own arrangement. That said, the Bank would normally regard the presence of an on-track PRGF as adequate evidence that the macroeconomic framework is appropriate, and the Fund would normally regard the presence of an on-track PRSC as adequate evidence that the social and structural program is appropriate. When a PRSC is under consideration or performance under a PRSC is being reviewed without a companion PRGF in place, Bank staff will ascertain, before formulating their own assessment, whether Fund staff have any major outstanding concerns about the adequacy of the country's macroeconomic policies. Fund staff will communicate any such concerns to the Bank in time to be reflected in Bank reporting to its Board. Similarly, when a PRGF is under consideration or performance under a PRGF is under review without a companion PRSC, Fund staff, before formulating their own assessment, will consult with Bank staff to ascertain whether the Bank has major outstanding concerns about the adequacy of the country's poverty reduction strategy, the social impacts of the macroeconomic policies supported by the PRGF, or the country's performance in meeting structural and social conditions in the areas of competence of the Bank. Bank staff will communicate any such concerns to the Fund in time to be reflected in Fund reporting to its Board....

In short, there is a good deal of cross-conditionality at the level of broad performance, as just described - probably more so than was in existence before the introduction of streamlining and the PRSC. At the same time, the Boards of both institutions seem clear that cross-conditionality should *not* be applied to policy specifics within either programme, with each institution "separately accountable for its lending decisions..."

Among our case study countries, cross-conditionality did not appear to give rise to any particular difficulties, except in *Kenya*. Of the two IFIs, it seems likely that the Fund is likely to want to move the more quickly to reactivate its programme there, probably after the election due this year. On present cross-conditionality rules, it will be unable to do so, however, unless in the meantime the GoK takes sufficient action to put itself in good standing with the Bank's adjustment credit. There is a substantial list of Bank conditions that have not been complied with and it is unclear how easy it would be for the GoK to rectify this, and how quickly they could do so - an important matter because the agreement formally expires in June 2002.

The last part of Q.9 above asks whether the Fund and the Bank have lost impact by shifting key structural issues from the Fund to the Bank? It is too early to tell. The answer under Q.5 above reported Fund staff concerns that the conditionality taken over by the Bank may prove less effective than it was within the Fund but it suggested reasons why that concern might be discounted. There is really nothing to add here, except to state that some improvement in the efficiency of conditionality is likely to result from any greater clarity in the Fund-Bank division of labour brought about by the streamlining initiative.

Q.10: What can be said about the net effect of streamlining on country transactions costs and freedom of policy action? *Have borrowing countries been able to influence conditionality frameworks. Are they happy about the division of labour with the Bank?*

The above discussion of the cross-conditionality issue are, of course, highly relevant to the question of net changes in transactions costs and freedom of choice. We have suggested earlier that the extent of IMF streamlining has so far been highly contingent, with large reductions in some cases and little change in others. We have also suggested that borrowing governments may find themselves in a somewhat tighter straight-jacket of cross-conditionality but that, even so, there is apt to be some net reduction in the combined Fund-Bank quantity of conditionality.

Unfortunately, this is not the end of the story, for borrowing governments, in many cases, will also have to concern themselves with further conditionality arising from the Bank's Country Assistance Strategy papers, as well as that specific to the HIPC completion-point arrangements,[18] to say nothing of the stipulations of other multilateral lenders and bilateral donors. Countries, like Albania, which aspire to membership of the EU also have the conditionality of that institution to worry about. HIPC conditionality alone is potentially both onerous and wide-ranging, with its content recently summarised as normally centred around macroeconomic issues, structural reforms, social sectors and 'other poverty reduction requirements,' especially governance and budget management issues (SPA Task Team..., 2001:9). Not much is left out there! There are also reports of bilateral donors picking up structural conditions being dropped by the Fund as a result of streamlining (Debt Relief International, n.d., para 13).

The authors of our country studies found it difficult to provide information on changes in transactions costs and governments' freedom of policy action. However, two are worth quoting. First on *Zambia*:

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[18] For example, at a Commonwealth Secretariat-IMF consultation in July 2001, the Tanzanian delegate reported that his government was confronted with no less than *thirteen* specific HIPC completion point conditions, over and above those of the IFIs.

> ...the net effect of IMF conditionality changes is ambiguous, with fewer performance criteria and more structural benchmarks. The conditionality written into the Bank's adjustment credit is also substantial: 12 prior actions before commencement of the credit; 14 second tranche conditions and a further 4 floating tranche conditions. However, Bank conditionality has not been affected by changes on the Fund side. There is also a new element, in the form of HIPC conditionality (in the design of which Fund staff have taken the lead role). This specifies eleven conditions for reaching Completion Point, plus 4 repeated from the IFI programmes and one other which goes beyond what is written into the Bank agreement. There is also the usual substantial micro-conditionality associated with bilateral aid. It is clear that, taking these provisions together, there has been a net increase in the total volume of conditionality. The government is more hemmed around than it was, say, two years ago and a small number of officials is having to cope with this additional burden. However, this should be set against the troubled past history of relations between Zambia and the IFIs and bilateral donors. There is only limited trust and that is reflected in the situation just described, although past attempts to use conditionality as a substitute for GoZ commitment have produced poor results.

Secondly, there is *Albania*:

> The current World Bank CAS and related instruments seem to have a very heavy framework of conditionality, albeit of a different nature to Fund performance criteria. The PRSP has a very detailed policy matrix and, although there doesn't seem to be an explicit process of extracting a core policy set, this has been partly achieved by the PRSC. Overall, it looks as if Albania is subject to a fairly heavy and detailed set of performance criteria (including from the EU's Stabilisation Association Agreement).

The report on *Mozambique* also refers to a "very great donor burden on the government" but does not elaborate.

A difficulty here is that streamlining has been motivated by a desire to raise the efficiency of the IMF (see Q.1), not by a desire to achieve a net reduction in the overall burden on conditionality on borrowing governments. No agency has an overview of the aggregate volume of conditionality, let alone responsibility for ensuring this is internally consistent and is kept within reasonable bounds. At least for HIPC countries, it seems that some governments today have less freedom of policy choice than they had, say, two years ago, and that the transactions costs of accessing assistance may have escalated. Freedom of action should also be judged according to the importance of the various areas of policy action. Since streamlining is about ensuring that conditionality is focussed on the most critical policy areas, and with both institutions tending to cut back most heavily in the grey area of second-order benchmark, or non-binding, conditionality, here too governments may well be in a more constrained situation, rather than an improved one. Not long ago, the present writer expressed fears that the HIPC II-PRSP arrangements might prove a vehicle for further increasing conditionality, despite all the rhetoric of ownership (Killick, 2000). These fears remain alive and well but there is not yet enough evidence to form a firm view.

The above question concerning countries' ability to influence conditionality frameworks has perhaps been answered under Q.6. In principle, governments now have, in the PRSP, a vehicle for influencing the framework but it was suggested there that governments have tended in drafting their papers to second-guess what they think the IFIs/creditors would like to see and that papers so far prepared have tended to be too unspecific to make any large material difference to the content of conditionality. We also report in Q.6 NGO disillusionment with the value of participating in the PRSP exercise, preferring instead to try to influence the IFIs directly. And we have suggested that neither the limited number of PRGF (Q.4) or PRSC (Q.8) programmes so far negotiated have differed markedly in design from their predecessors, although in some cases the extent of structural conditionality has been substantially reduced. The limited extent of change again suggests that borrower influence on the programmes may be little increased.

The crucial test will be when a government produces a full PRSP, based on wide consultation, whose policies differ materially from what either IFI would choose. Whether their staffs would be willing to recommend such a document, whether their Boards would prove sufficiently committed to the ideal of ownership to endorse it, and whether the subsequent design of IFI conditions would be based upon it are questions that remain to be tested.

V - POLICY POINTS ARISING

My terms of reference ask me to make policy suggestions for DfID and HMT. These are set out below and are intended to flow from the main points arising above, as summarised at the beginning of the paper

Relating to the IMF

One of the strongest implications emerging is that *the Fund should adopt a more joined-up approach to the changes which it is introducing.* This paper is principally about the streamlining initiative but going on simultaneously are the changes associated with the move from ESAFs to PRGFs and, more recently, the staff guidance which is in preparation on ways of enhancing country ownership of Fund-supported programmes. Also highly relevant is the implementation of HIPC II arrangements, in which the Fund has a central role. HMG should urge the Fund to adopt a more integrated approach. This should result in a statement of policy which, for example, is concerned with:

- Broadening the concept of streamlining to address issues of *process*, for example in order to foster ownership.

- Examining the relationship between the streamlined conditionality in PRGF programmes and the conditionality associated with HIPC Decision and Completion points.

- The case for reducing the use of prior actions, not only because they have been shown by recent Fund research not to enhance programme implementation but also because of their deleterious effects on ownership and because of reports that their usage has been creeping up in recent times.

The desirability of *narrowing the gap between the management's aspirations and the practice in the field* also emerges strongly from the foregoing. For example, it emerges that, at the country level, the extent to which streamlining is making much difference is highly contingent on borrowing country circumstances. This is not intrinsically unreasonable but the suspicion emerges from the country evidence that, to an undesirable extent, implementation of streamlining is strongly influenced by the attitudes towards it of Mission Chiefs and other staff members. It would be desirable for the Fund to clarify what it regards as the key principles in decisions about the extent of streamlining at the country level and for its management to take further steps to ensure that it is carrying the staff with it on the desirability of streamlining.

The above analysis also draws attention to the desirability of instituting safeguards against the danger of regression, or 'conditionality creep', whereby the previous trend towards ever-increasing conditionality reasserts itself.

Another matter that should be addressed concerns the position, *vis a vis* streamlining, of 'old' (ex-ESAF) PRGFs. A more forceful policy would be desirable of using periodic review missions to bring old PRGFs into line with best-practice intentions for new programmes, and to get rid of non-critical structural conditions which linger on in old programmes.

A further aspect of the streamlining exercise that is less than satisfactory concerns the clarification of what does, and does not, constitute the conditionality of a given programme. It is pointed out above that there remains considerable ambiguity about the status of structural benchmarks and that that should be clarified as part of the streamlining process.

There is, of course, a much larger issue about the Fund's policies with respect to conditionality, in that these have not kept pace with emerging evidence on the limitations of what conditionality can achieve (although the Fund's recent 'ownership' paper was a welcome fuller recognition of the problem). The Briefing Note prepared on this subject by DfID staff for the Secretary of State to use at the 2000 Fund-Bank Annual Meeting sets out a more appropriate view of conditionality and it would be desirable for this view to be actively promoted by HMG at meetings of the Fund Board. As a beginning, HMG could urge the Fund to extend its concept of streamlining by stating the principle that it is willing to negotiate low-conditionality programmes with governments that have already established a good track record of reform and compliance, using the record of the recent past as a predictor of the future, unless there are obvious reasons why that would not be appropriate.

A number of the problems identified here might have been avoided had the Fund sought more actively to engage member- (or borrower-) governments to elicit their views on streamlining and related initiatives, at the bilateral level, in addition to the more wide-ranging consultations it has already conducted. As it stands, these initiatives are overwhelmingly 'supply-driven'. A more user-oriented approach might well have resulted in material changes and, perhaps, narrowed the aspiration-reality gap. Moreover, a widening of the streamlining debate to include the Fund's traditional macroeconomic conditions would have been a good occasion for re-visiting what, after all remains the core of almost all Fund programmes.

A major and glaring respect in which in-country practice is falling far short of stated management aspirations relates to the promotion of poverty reduction. There are two specific shortcomings which need urgent rectification:

- Much fuller inclusion of PR concerns in programme designs. Although it is asserted from Washington that this is being done, chiefly by way of detailed provisions to ensure more pro-poor expenditure profiles in government budgets (and there is some evidence that this is happening in 'new' PRGF programmes), our country studies found almost no evidence that programme designs had been in any way constrained, or even much influenced, by the poverty reduction objective. This may well be one of the ways in which practices in 'old' programmes need to be brought into line with new ones, via review processes.

- Second, the insistence in the Fund's PRGF 'Key Features' document that it was "essential" that programmes carefully consider likely impacts on poverty groups is, on the basis of our limited evidence, often being ignored in practice. Our country studies found little evidence that this had been done. There are admittedly difficulties about the full implementation of PSIAs but *the short-term impracticability of full-blown studies is not a good reason for not trying to form a judgement by such second-best methods as are available.*

As a further instance of uneven application of the intended principles of PRGF programmes, it appears that Fund staff are only exceptionally discussing alternative fiscal scenarios with borrowing authorities. Our case studies uncovered only one partial exception, and one country in which the visiting Mission Chief publicly ruled out such a possibility. Here again, there are questions about the extent of staff support for intended changes, which may also relate to internal Fund training arrangements.

There are, additionally, a number of ideas in the recent Fund paper on ownership (IMF, 2001C) to which DfID might wish to lend its public support with a view to reducing the existing tensions between the Fund's conditionality and the principle of country ownership. Candidates include:

- Tentative support for greater use of results-based conditionality (para 37) but tempered with the caution that this type of conditionality is most appropriate in the rather limited situations where an economy's responses to a given policy change can be predicted with confidence and some accuracy. Also, greater use of 'floating tranche' conditionality, where feasible.

- The suggestion in the paper (para 36) that the Fund "should apply more systematically the general presumption that authorities should have the initial responsibility for proposing a reform program." DfID might wish to take this further and urge the principle that *country authorities ought to produce first drafts of the Letters of Intent* which are ostensibly from them in any case. There are elements within the Fund who support this but others who oppose.

- That in future the Fund should re-focus its programme reviews and evaluations around the ownership question and that independent *ad hoc* groups have a role to play in this (para 45).

- The Fund should re-orient its technical assistance efforts away from programme-specific activities in favour of longer-term capacity building within borrowing countries (paras 41-42) .

- The Fund should strengthen its capabilities in issues of political economy (para 40).

A further desirable reform, but one which goes beyond the Fund's paper, is that the Fund should consider a greater decentralisation of its activities, just as the Bank has with good effect. As a non-controversial beginning, HMG could suggest a study of decentralisation for the Fund, i.e. delegation of more authority to country resident representatives, with a view to promoting greater local ownership and closer harmonisation of Fund activities with local conditions.

Finally on the Fund, DfID/HMT should continue to press the desirability of putting the grant element of concessional loans 'above the line' when calculating financing gaps and permissible levels of government spending, as further helping to reduce the tension between the macroeconomic, growth and poverty reducing objectives of PRGFs.

Relating to the World Bank

As spelled out earlier, the response of the World Bank to the IMF's streamlining exercise and the parallel changes in response to the PRSP movement, has not been very explicit. It would therefore be desirable for HMG to press for greater clarity in respect of a number of questions:

- It is not clear whether streamlining extends in reality to the Bank, despite rhetoric to that effect. It would be desirable to have a clear statement of the Bank's position on this and on how any future streamlining of its conditionality is to be institutionalised and monitored.19

- It would also be desirable to clarify the issue of potentially differing country eligibility criteria for the PRGF and PRSC, with the latter apparently aspiring to a more selective approach. The key issue here is how to deal with countries considered eligible for one but not the other.

- Both the above points are closely related to the future of conditionality in conventional structural adjustment programmes. Is structural adjustment lending to continue as before, where there is no PRSC, or is this to be reviewed? There appears to be a strong *prime facie* case for extending the principle of streamlining to SAL and SECAL conditionality.

- The two Bretton Woods agencies should formulate a joint position regarding the co-ordination of their monitoring and review processes, in order to reduce the burdens upon the administrations of borrowing governments. This should also take into account the processes relating to the review of PRSPs and HIPC programmes with a view to synchronising with these.

- Also for both institutions, DfID could suggest the desirability of instituting safeguards against the danger of a renewed trend towards the increasingly detailed monitoring of structural reforms that led to the earlier proliferation of conditionality. One possibility might be a requirement for each to present an annual report to the Board on trends in conditionality and on progress with streamlining.

Other matters

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19 From information obtained after writing this paper, it does now appear that the Bank is likely to engage in a substantial streamlining exercise, in connection with a planned reorientation of its policy-based lending (TK, 18.7.02).

The evidence gathered for this paper points strongly to the probability, at least among HIPC countries, that, despite IMF streamlining, the net effect of the various changes of the last two years has been to leave some governments with a significant net increase in the volume of conventional conditionality, notwithstanding the increasing recognition by both institutions of the failings and limitations of this modality. Streamlining in the Fund has been seen primarily as an efficiency-raising device, not as an opportunity to reduce burdens upon borrowing governments and this has been compounded by the probability of a 'pass the parcel' effect, with the Bank (and reportedly some bilateral donors) taking up 'structural' measures dropped by the Fund. Along with this goes an almost inevitable increase in the transactions costs to borrowing governments of accessing the assistance in question - an increase made all the greater by the absence so far of action to rationalise the respective monitoring requirements of the IMF, World Bank and those responsible for HIPC implementation.

It is a major defect in the present architecture of donor/IFI-recipient relationships at the country level that no agency is responsible for obtaining an overview of the burden of IFI and other conditionality, and for ensuring that this is both internally consistent, reasonable in its totality and does not make avoidable calls upon the scarce informational and administrative capacities of governments. HMG should raise this systemic issue and should perhaps suggest that a first step would be to bring this formally and systematically within the purview of country-level donor aid co-ordination arrangements.

The above problem particularly affects HIPC countries but our country studies revealed a related problem as it affects countries which are in receipt of Fund-Bank credits and are simultaneously pursuing accession to membership of the European Union. In the case of Albania, virtually no co-ordination was found to exist between the Bretton Woods institutions and the structural provisions in the EC's Stability Agreement and Stabilisation Association Agreements. It is not clear how many other countries may be affected by this weakness, but this is a matter HMG should consider taking up both with the BWIs and within the EC.

Lastly, it was suggested above, as is now becoming a commonplace, that the existing link between HIPC II debt relief and PRSPs is having a debilitating effect on the PRSP initiative, which, in turn, will undermine ownership and the attempted streamlining of conditionality. HMG should consider ways in which this linkage could be avoided in future, or its perverse incentive effects reduced.

(end)

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