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## HEALTH FINANCING IN LOW-INCOME COUNTRIES: A ROLE FOR SOCIAL CAPITAL?

*The notion of 'social capital' has hovered around the edges of policy debates on sustainable health financing systems in low-income countries, but – hitherto – has failed to become a widely used analytical concept. The main reason is that no one is quite sure what social capital is. Nevertheless, the concept does hold some appeal, not least because it draws health economists towards an insightful literature not otherwise considered. Putting aside definitional problems, the usefulness of social capital (or rather the set of concepts and ideas related to it) for the development of health financing systems is somewhat ambiguous. Matt Jowett offers a brief exploration of these issues.*

The first major attempt to develop a link between social capital and health financing in low-income countries was made in 1995 by W Hsiao, of Harvard University's School of Public Health. In an unpublished paper on co-operative health care organisations in China, Hsiao suggested that social capital is a critical element in the development of such 'risk-sharing' arrangements within communities. By implication, community-based health insurance schemes are more likely to succeed in communities with a high stock of social capital. If evidence could be found to support this proposition, it would constitute valuable information for policy-makers.

Hsiao's paper drew directly on the theoretical framework developed by J S Coleman in his *Foundations of Social Theory*, published in 1990. Coleman's theory of social capital emerged from his sociological study of collective action, particularly the prevalence in much of the developing world of rotating savings and credit associations (ROSCAs). Coleman argued that membership of a ROSCA demonstrated a high level of inter-personal trust which, in turn, facilitated co-operative or collective action. Hsiao's paper extended this idea to risk-sharing mechanisms in the health sector.

### What is 'social capital'?

Such arguments beg the question of the meaning of social capital. French sociologist Pierre Bourdieu is generally credited with making the first attempt to define the concept. In *The Forms*

*of Capital* (1985), Bourdieu defined social capital as:

"... the aggregate of the actual or potential resources which are linked to possession of a durable network of more or less institutionalised relationships of mutual acquaintance and recognition – or in other words, to membership in a group – which provides each of its members with the backing of the collectively-owned capital, a 'credential' which entitles them to credit, in the various senses of the word."

This definition suggests that social capital can be decomposed into two elements:

- the social relationships that allow individuals to access resources owned by their associates; and
- the amount and quality of those relationships.

In the subsequent proliferation of research work, however, social capital has been defined variously as norms of behaviour, trust, density of social networks, favours, social cohesion, and a number of other related terms. As a result, the concept arguably has begun to lose any distinct meaning.

Any attempt to restore the usefulness of the concept must confront three dilemmas:

**1. Definitional circularity.** A central problem in defining social capital is the apparent circularity of the term. This arises when a definition incorporates both the mechanisms that generate social capital (e.g. reciprocity, expectations and group enforcement of norms), and some of the consequences of social capital (e.g. better information). Equating social capital with the resources acquired through it leads to tautological – or circular – statements.

**2. Positive vs negative benefits.** Early research appeared to assume that social capital has only

"Notwithstanding a weak theoretical framework, and the lack of a widely accepted definition, social capital has a place in public policy analysis"

“Communities with high levels of interpersonal trust may be more willing to pool health-care risks”

positive effects. However, a range of disbenefits is also possible. One obvious example is the existence of organised crime, such as the Mafia, which – it can be argued – is also a form of social capital, in the sense that it possesses a high level of internal trust and provides its members with access to collectively-owned resources. Several recent authors have begun to redress this imbalance by taking account of negative impacts. By

implication, however, the optimum level of social capital in a given situation is not necessarily the maximum available.

### 3. Horizontal vs vertical networks.

Social capital tends to be defined, and measured, only in terms of horizontal social networks, with positive value added when these are heterogeneous in membership. Intuitively, however, social capital can exist vertically – for example, through public trust in government institutions. This issue has been addressed only partially in the recent literature – through the ideas of ‘bonding’ and ‘bridging’ social capital – and it is indicative of the challenges still facing the development of a convincing theory of social capital.

Perhaps the most useful idea – also introduced by Coleman – is that of ‘closure’ within social networks. It is argued that networks:

- facilitate the development of co-operation (by increasing the levels of inter-personal trust);
- allow reputations to develop (thus enabling individuals to establish who they can trust); and
- facilitate the emergence of behavioural norms that make social sanctions effective – an important practical condition for encouraging individuals to enter informal contracts.

## Social capital and the analysis of risk in economic development

Some of these ideas have already been addressed in the development economics literature, where there is a substantial body of work that analyses risk – and the responses to risk – in low-income countries. Systems that facilitate savings, credit and private transfers are all considered as playing an insurance function, and the literature stresses the importance of information flows for the maintenance of such systems. As noted, most attention has been given to ROSCAs.

“If informal risk-sharing contracts are to succeed, social mechanisms are needed to regulate behaviour”

There have been two strands to this literature. Economists have tended to focus on the internal dynamics of institutions such as ROSCAs. Substantial

work has also been done by economists on the Grameen Bank – a similar type of institution that also relies on peer monitoring. In contrast, writers on social capital have focused on the necessary conditions for ROSCAs to emerge, highlighting the presence of trust or other forms of institutionalised relationships within a community. Both strands stress that, if informal contracts are to succeed,

social mechanisms are needed to regulate behaviour. However, the social capital literature talks of ‘social norms’, while the economics literature uses terms such as ‘reputational and social collateral’: mechanisms – such as repeated games – that allow for the development of reputation are used by economists to explain how a similar environment to that described by network closure may be created.

The social capital approach indirectly draws attention to the problem of ‘crowding-out’, namely the displacement of informal risk-sharing networks by large-scale public safety-net programmes. The ways in which formal and informal risk-sharing institutions interact with each other have been examined. Most evidence confirms that formal mechanisms – in particular, freely available safety-net programmes – do crowd-out informal risk-sharing arrangements.

## More sustainable health services?

The ideas highlighted by the social capital approach raise the possibility that communities with high levels of interpersonal trust may be more willing to pool risks in the health-care field, for example, through participation in health insurance schemes. However, it may be important to distinguish between formal and informal risk-sharing schemes. Evidence of the development of informal risk-sharing networks within communities is strong, but whether more formal risk-sharing arrangements would be equally attractive is unclear. No studies to date have considered the impact of a voluntary health insurance scheme promoted – and possibly subsidised – by government (as in Vietnam), and for which a premium must be paid. It is at least conceivable that local populations may prefer more informal arrangements, particularly where government officials are perceived to be corrupt.

Many other questions also remain. For example, how can social capital be reliably identified, and then harnessed by policy-makers? How can insurance institutions combine the benefits of large schemes for risk-sharing with local management and monitoring to contain moral-hazard problems? Such issues offer a rich agenda for future research.

## Conclusion

Social capital has not yet become the widely used concept that many expected. The principal reason is the weakness of its theoretical framework, and the lack of a widely accepted definition. Nevertheless, there remains a feeling that the idea has something to offer public policy analysis in low-income countries, particularly in the increasingly important arena of health economics. Perhaps social capital’s greatest potential lies in enriching current thinking by prompting the use of theoretical frameworks drawn from sociological and political science approaches, as well as from the development economics literature.

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## E-GOVERNMENT: NEW TOOLS FOR PUBLIC ACCOUNTABILITY

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*The easy availability of a wide range of user-friendly software, the robustness and rapidly falling cost of hardware, and the growing world-wide familiarity with the use of computers, all combine to create opportunities for using information and communications technology (ICT) to improve the efficiency of public agencies. But, according to Pierre Landell-Mills, case-study evidence reveals that relatively simple ICT tools can be used also for improving public accountability, especially in pro-poor directions. Despite many obstacles, these may prove – over time – to have a significant impact on governance, especially in countries where corruption is pervasive. However, further research is needed to assist policy-makers in taking greater advantage of such tools.*

### Government and governance: efficiency vs accountability

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Despite improvements in development policies and programmes, weak governance – especially pervasive corruption – is increasingly seen as the central obstacle to improving livelihoods in developing countries. Inappropriate incentives, and the nature of the political process, lead public officials to pursue their own, rather than the public, interest.

The World Bank has defined ‘governance’ as ‘the manner in which power is exercised in the management of a country’s economic and social resources for development’. However, this definition does not distinguish sufficiently between the ‘efficiency’ and ‘accountability’ of public officials, who may abuse their powers. Efficiency (part of ‘good government’), and its impact on the intended beneficiaries of public services, is crucially linked to the degree of public accountability (‘good governance’). Insufficient attention to governance (in this sense) helps explain why attempted reforms often fail.

The adverse consequences of poor governance are severe. Official corruption undermines efficiency and opens government to capture by criminal elements, who can demoralise the public service. In the worst cases, as in Zaire (and possibly Argentina), it may lead to the collapse of the state.

### Benefits and challenges of e-government

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Wherever public officials exercise power over citizens, opportunities for bribery and extortion will arise. Therefore, effective reforms must remove, or limit, officials’ discretion. The introduction of e-government processes can significantly increase transparency, formalise transactions, and alter the interface between public officials and citizens by reducing the opportunities for rent-seeking and making bribery and extortion more risky.

e-Government processes may include:

- computerised records (of land titles, birth and marriage certificates, etc), accessible via the internet or conveniently located information ‘kiosks’;

- electronic financial transactions (e.g. payments for permits, bills, fees, duties and taxes);
- e-procurement and computerised service-delivery processes that reduce bureaucratic discretion;
- electronic tracking (e.g. with bar codes) of government stores and other inventories; and
- posting of public budgets, accounts and audits, as well as laws and regulations, on official web-sites.

Such measures can lead both to improved efficiency in service delivery and increased transparency and public accountability. However, a fundamental problem is that the officials implementing corrective actions are also those who benefit from governance abuses. Thus, effective reform depends on building sufficient political pressures to generate the managerial will and capacity to impose changes.

### Learning from global experience

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e-Government has grown steadily over the past decade in both rich and developing countries. Case-study evidence on the possibilities and limitations of e-government demonstrates that ICT tools can be powerful instruments for enhancing public accountability, but cautions against excessive expectations. There have been a few notable successes, even in very poor environments not noted for government efficiency (see Box). The weight of evidence suggests that, given a supportive institutional environment, the backing of key stakeholders and co-ordination with other projects, the inclusion of ICT applications in reform efforts can have a dramatic impact on the quality and accountability of government services both locally and nationally. But there have also been many costly setbacks, mostly resulting from a failure (a) to harness the enthusiasm of ICT specialists appropriately for the intended users and beneficiaries, and (b) to ensure that the applications remained simple.

**“Weak governance is the central obstacle to improving livelihoods in developing countries”**

In the successful cases, ways were found to raise productivity and improve service quality by adapting modern ICT solutions to local circumstances. ‘Formalising’ public management systems through computerisation strengthened information flows, both inter-agency and between the public and government. Increased transparency and reduced official discretion offered fewer opportunities for bribery and corruption.

### Public procurement

Among the main sources of ‘grand’ corruption are public procurement – the letting of contracts for major public works – and sales of public assets, sometimes resulting in personal gains of millions of dollars. ICT processes can reduce such opportunities dramatically by depersonalising transactions and increasing transparency. In Chile, Mexico

and Brazil, for example, electronic bid submissions have helped overcome the problem of bidders employing hoodlums – sometimes with the connivance of the police and officials – to prevent competitors from delivering their tenders to designated offices.

### Stock security

Losses from pilferage and theft of public stores and property can be combated by use of bar codes to track inventories. For example, vast sums are involved in illegal logging, and experiments with bar codes – which enable the origin and legitimacy of log consignments to be checked anywhere along the marketing chain – have shown that, given effective commitment by the relevant officials, illegal logs can be confiscated. This provides a strong incentive to all traders to be honest and to insist that those upstream respect the requirements for sustainable forest management.

### Financial accountability

Public financial accountability lies at the core of honest government. However, few developing countries have robust public spending accounting systems. Too often,

budgeting systems lack transparency, public accounts are seriously delayed and highly flawed, reported deficiencies in public audits routinely ignored, and parliamentary scrutiny cursory or non-existent. Officials responsible for missing or misused funds are rarely sanctioned, except where politically convenient, in which case they may be unfairly victimised. In these circumstances, transparency can become a powerful tool to foster reform and increase accountability. To this end, a few countries, including very small ones (e.g. Guatemala), have begun posting their official budgets, accounts and audits on a web-site for public scrutiny.

### Risks and limitations

Although the failure rate in e-government initiatives is worryingly high, the lessons correlate with those from the broader public-management literature about managing change. Failures can occur when:

- projects are driven by ‘technies’ who do not understand the objectives and needs of the exercises or make them too complicated;
- managers or staff are given insufficient incentives to adopt the changes, or insufficient reassurance when they feel threatened by them;

- powerful key stakeholders would be deprived of illicit benefits from the existing arrangements.

The gaps between conception and reality are usefully summarised by the acronym ITPOSMO: information, technology, process, objectives (including values and motivations), staffing and skills, management, and other resources. As the public management literature would predict, attempting to ram through changes without keeping the techniques subservient to the reform objectives, and without understanding (though not

necessarily giving in to) the concerns of all the stakeholders, is counterproductive.

### Stakeholder resistance

Although most e-government reforms have both efficiency and accountability goals – which are thus intertwined – stakeholder resistance to increased accountability is much greater. Consequently, a successful reform strategy requires a thorough stakeholder analysis. It is necessary to identify and nurture the ‘drivers of change’ – those decision-makers within the public bureaucracy and civil society who, for various reasons, are strongly motivated to ‘clean up’ corruption. But mechanisms must also be found to overcome or bypass the resistance from those who will suffer losses of benefits, privileges, status or power.

Informal realities – whose existence is well-known to officials, but often not readily acknowledged – must be included. For example, tax collectors or customs officials may be accustomed to reaping substantial private benefits from ‘negotiations’ with taxpayers or importers. Posting the tax codes on a web-site, permitting self-assessed returns and payments to be made electronically, and backing up the process with rigorous spot audits, will substantially reduce the scale of such abuse. Control efforts and resources can then focus on preventing corrupt audits. However, resistance to such reforms can be vicious (and effective): customs officers in Bangladesh responded by destroying their newly introduced computers!

### Sustainability challenges

Sustainability of the reform process is crucial. ICT innovations that bring about system changes that cannot be easily reversed – for example, when accounts and land registries are computerised – should be promoted first. Also valuable are low-level innovations that can subtly render transactions more transparent. Successful e-governance reforms also require an ‘ICT-friendly’ context, including support for the development of:

- the ICT skills base;
- an information culture, including local language web-sites;
- equitable business and civil society access to ICT-based government services;
- an open, well-regulated and competitive ICT sector;
- business use of internet e-commerce, through regulatory and judicial reform, including privacy encryption issues; and
- community information centres, internet infrastructures and start-up firms.

Finally, in this fast-moving area, governments should facilitate – not compete with – private-sector exploitation of ICT.

### A research agenda

The argument that e-government offers potential for improving e-governance – especially by making public bureaucracies in developing countries more accountable – suggests a research programme with four main themes:

1. **Conceptual framework.** There is need for a stronger

“e-government processes can significantly increase transparency by reducing opportunities for rent-seeking”

“Mechanisms must be found to overcome resistance from stakeholders who suffer losses”

theoretical framework to guide analysis, evaluation and measurement of e-governance issues, especially their impact on the poor.

**2. Good-practice observatories.** Promising innovations and good practices need to be identified, analysed and disseminated, and their potential for adaptation to different country conditions assessed.

**3. Effectiveness of applications.** The effectiveness of ICT applications in improving public-resource management and accountability and pro-poor service delivery requires assessment. This includes applications in finance and administration, and those – including ‘smart cards’ and web-based score cards – intended to target public benefits, disseminate public information, and reduce face-to-face contact with government officials.

**4. Bridging the ‘digital divide’.** Assessment is also needed of the effectiveness of ICT in promoting ‘citizen voice’ and reducing the transactions costs – especially for the poor – of doing business with the government.

## Conclusion

e-Governance tools offer an impressive array of new opportunities to improve public accountability and poor-country livelihoods by modifying the incentives and institutions (rules of the game) governing transactions between government officials and the public. As yet, this potential is largely unexploited. Success depends on the legislative, judicial and executive organs of the state acting as responsive and accountable agents for their citizens. Research is needed to assist policy-makers in taking greater advantage of ICT tools to achieve better governance, with special attention to the impact on the poor.

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### E-GOVERNMENT IN PRACTICE

The Indian state of Andhra Pradesh (AP) has enthusiastically embraced e-government, by creating a networked information-based society, benchmarked against global standards.

Computerised registration of land deeds, transfers and property valuations, and imaging of documents, is replacing the previous archaic and corruption-infested manual system. There are already 239 networked sites – serving 11,200 of the 19,499 panchyats – where citizens can complete registration formalities in less than an hour, and obtain certified copies of documents within 10 minutes, compared to 1-3 days under the old system. Over 80 per cent of all transactions are now done electronically.

Under a pilot network covering 30 departments, AP citizens will be able to make bribery-free electronic payments for utility bills and documentary and license

fees, with public information continuously available.

AP’s innovations are being keenly watched by other Indian states. Karnataka, among others, has already successfully replicated the land-registration scheme. In Calcutta, the municipal government has computerised records and payment systems for 15 different services, including waste collection and water supply, budgeting/accounting, mapping, property valuation, building plans, appeal hearings, and births and deaths. In the case of waste collection by private contractors, the weight of each lorry entering and leaving landfill sites is recorded electronically, and end-of-month payments are generated automatically. With no opportunity for operators to ‘negotiate’ payments, there has been a 30 per cent saving in garbage-collection costs. Some of the benefits have been shared equitably with the operators, thereby providing legitimate rewards for good performance.

## THE IMF: STABILISATION VS POVERTY ALLEVIATION?

*The role played by the International Monetary Fund (IMF) in the ‘international financial architecture’ has been subject to re-evaluation in recent years for two broad reasons. First, its mandate to defend economic stability has required re-interpretation in the context of increasingly large and volatile international capital flows. Second, the perceived connections between widespread poverty and economic instability in low-income countries have induced the Fund to develop policies that address the challenges of poverty alleviation and social development. Alan Roe suggests that, although these two elements of the policy agenda raise*

*significantly different questions, they can in principle be connected.*

### Re-interpreting the IMF’s mandate

In the immediate post-War world of tight currency and capital restrictions, the Fund’s mandate for promoting global economic stability had a simple interpretation: it was largely co-terminous with the objective of reasonable stability of exchange rates in the context of gradually increasing current-account convertibility. However, as

underlined by the sequence of recent financial crises – including Mexico, East Asia, Russia, Brazil and, most recently, Argentina – in the modern globalised economy, ‘stability’ needs a broader interpretation. Efforts to build a more stable global financial system, less prone to periodic crises, must address financial-sector behaviour more generally. Since early 1998, this new reality has motivated extension of the Fund’s mission, embracing two elements:

- new measures to reduce the likelihood of future financial crises; and
- more controversially, a re-think of the measures for dealing with crises when they arise.

Increasingly, however, it has also been recognised that financial instability is likely to be most damaging to low-income and vulnerable families. Consequently, protection of the poor, as opposed to international capital, should have greater emphasis as a reason for wanting ‘stability’. Traditionally, this possibility received little formal reflection in the Fund’s work, thus attracting – with some validity – the familiar radical criticism that the IMF’s standard monetary and fiscal policy requirements are anti-poor. Since 1999, however, there has been a growing – and much more explicit – emphasis on poverty reduction and social development in the IMF’s stabilisation agenda.

### Financial crisis prevention

Work here is increasingly oriented around multi-agency efforts to understand Fund members’ vulnerability to crisis and induce them to conform to a range of stability-enhancing financial standards. In 1999, the G-7 Financial Stability Forum (FSF) was convened, World Bank teams initiated a limited series of vulnerability studies, and the Bank and Fund jointly agreed to produce Financial Sector Assessment Papers (FSAPs) assessing countries’ vulnerability across a wide range of macro policy, banking and regulation issues. The intention is that each country’s FSAP position should be reviewed within a regular Article 4-style cycle. This possibility evokes criticism on the grounds that the potential determinants of a country’s vulnerability are not susceptible to such routine procedures. Equally, crises have a nasty habit of appearing at inconvenient times unrelated to a pre-determined pattern of review.

### Standards compliance debate

The FSF programme has focused on achieving greater compliance with a range of international financial standards. The Forum has compiled a Compendium of International Standards covering 12 broad subject areas (‘modules’), including monetary and fiscal policy transparency, data dissemination, corporate governance, accounting and auditing, market integrity, and banking and financial supervision and regulation. The number of module ‘reports on the observance of codes and standards’ (ROSCs) is growing rapidly, although publication is voluntary and some countries have withheld permission.

The standards programme has met with some resistance and criticism:

- the Group of 24 developing countries has objected to the whole process (Communiqué of September 2000);
- others have criticised aspects of the process, including the possibility of standards being incorporated as formal conditions in World Bank adjustment loans;
- the limited competence of Fund staff in many subject areas points to the need to enlist inputs from a range of specialised agencies, although this may create tensions with the Fund’s own predilection for confidentiality;
- the Fund’s inclination towards a ‘one size fits all’ approach may be incompatible with the existing diversity of standards, for example between the EU and the US;
- the starting point for different countries is radically different (e.g. Russia versus Mexico) and it is likely to be a long time before there is enough compliance to make a significant impact on the likelihood or scale of prospective crises in vulnerable countries; and
- some IMF insiders have expressed doubts about whether even a high level of formal compliance would be sufficient to head off future crises.

Thus far, there has been little interest in any cost-benefit analysis: how much extra cost in terms of standards and codes compliance is needed to avoid one future crisis? However, research into the attitudes of selected developing and transition countries towards the initiative and other aspects of the new international financial architecture has begun.

### Financial crisis management

The Fund was much criticised for its handling of the Mexican, East Asian and Russian crises. Some argued too much accommodation was given to some countries for too little genuine adjustment; and it was widely asserted that, in some instances, taxpayers money was used to provide almost costless bail-outs to private speculative investment. Part of the current reform agenda constitutes the response to those criticisms. However, there is no strong consensus about the right way forward.

### Pre-qualification?

The Meltzer Committee, set up by the US Congress in 1998 as one of the conditions for new IMF funding, argued that IMF support should be concentrated on countries with fundamentally sound policies and temporary financial difficulties. Ideally, such countries should be identified in advance. Chronically mismanaged countries should get little or no help. A related proposal is that poorly managed countries requesting support from the Fund should be accommodated, if at all, only at high interest rates and for very short periods. The logic is that such countries would either be deterred from borrowing by the high cost, or would need to make even bigger adjustments in order to recoup the cost.

These ideas – dubbed ‘romantic’ by Barry Eichengreen – have gained little support. The idea that countries might pre-qualify for Fund assistance is fraught with moral-hazard problems. How would the Fund know how to place a country on the right side of the eligibility line? How could such classification avoid sending damaging signals to

“Protection of the poor, as opposed to international capital, should have greater emphasis as a reason for wanting ‘stability’ ”

markets if the country's policies deteriorate? Could disqualification itself trigger a crisis? Equally, the East Asian experience showed that even the best economic performers are not immune from crisis. If a pre-qualifying country enters a crisis and the Fund fails to change its classification, how does it deal with its own responsibilities (to say nothing of its loan exposure)? Thus, proposals to eliminate Fund discretion by pre-categorising all members as either 'good' or 'bad' appear seriously flawed.

The Fund's Contingent Credit Line (CCL), established after the Asian crisis, provides partial support for this conclusion. Designed to help countries pursuing strong economic policies avoid contagion from others' crises, it has basic design flaws: applying for CCL support might be construed as signalling future problems where none currently exist; and losing CCL access might prove worse than never having had the facility. Perhaps unsurprisingly, to date no country has been persuaded to apply.

### Practical crisis management

However, there is some common ground about the Fund's crisis management role. Criticisms notwithstanding, it remains widely agreed that the world still needs a lender of last resort and that the IMF is the institution best placed to take the lead role. Disagreements on matters of detail include the terms of crisis support; the mechanisms for distinguishing country-specific from systemic or contagion-driven crises; and the pros and cons of pre-qualifying well-managed countries for support. Ensuring greater participation and burden-sharing in rescue packages by private lenders and bond-holders – e.g. automatic private-debt standstills – is particularly important. Bond debt issued under US procedures, where there is little basis for collective bond-holder action, raises particular problems. The addition of collective action clauses (CACs) to bond covenants would give the Fund and the country a sounder basis for negotiating private-debt standstills.

The emerging architecture also involves strong support for the Supplemental Reserve Facility (SRF), introduced in 1997 to augment EFF and Standby facilities in the event of sudden and disruptive losses of market confidence. However, suggestions that SRFs and CCLs be merged to create a single new supplemental Crisis facility lack support. In any event, such variants will be needed less if – as seems likely – exchange-rate regimes become less pegged. But fears that poor-performing countries will be excluded from access to IMF help are unfounded: no alternative rescue route is available to them and the IMF cannot stand idly by and allow any member's economy to slip into chronic recession, thereby damaging the country's prospects for social cohesion and poverty alleviation.

### Poverty and social development agenda

This second component of the IMF's re-defined role sits less comfortably with its traditional mandate. The Fund will always fall back on the proposition that in the long run financial mismanagement and instability help nobody – rich or poor. Although true, this ignores two points:

- some Fund programmes fail to achieve stability – or take an excessive time to do so – while imposing high social costs; and
- even in successful stabilisations, the transition costs are

particularly damaging for poorer families because of their smaller capacity to absorb downside developments.

### 'Enhanced' structural adjustment

Prior to 1999, these issues were reflected largely in the Fund's easier accommodation terms – through its Enhanced Structural Adjustment Facility (ESAF) – for a pre-defined group of low-income countries with deep-seated economic problems. This approach had weaknesses: it was focused on poor countries, and not on poor people; and, apart from low interest rates and extended loan maturities, it offered few real concessions to address particular dimensions of poverty. Although assistance did flow to countries accounting for some 3 billion of the world's poorest people, there was great diversity in the income gains/losses achieved by different groups in the beneficiary countries. ESAFs were also criticised for the relatively limited ownership /inclusiveness achieved in the process of preparing the Policy Framework Papers (PFPs) that underpinned the programmes, despite the involvement of both the recipient country and the World Bank.

“The argument that the IMF should be restricted to a very narrow mandate is naïve”

### Poverty-reducing growth

In 1999, the ESAF was replaced by the Poverty Reduction and Growth Facility (PRGF), operated jointly with the World Bank. The PRGF also provides the programmatic basis for IMF debt relief through the revised HIPC ('highly indebted poor country') initiative. In all cases, PRGF-HIPC access requires prior preparation of a Poverty Reduction Strategy Paper (PRSP). The PRSP process is explicitly led by the recipient country, with Fund/Bank staff playing a mainly supportive role. Thus, greater inclusiveness is actively sought, but in many beneficiary countries the analytical resources available are limited. Hence, there is a persistent danger that the views of the international financial institutions may retain disproportionate weight. Foreign advisers have also been heavily involved in drafting some PRSPs.

Early PRGF evaluations pointed to several lessons:

- **Ownership.** The rush to obtain debt relief can shoulder aside solutions that rely more on local ideas and consensus.
- **Internal consistency.** Problems can arise in integrating the macroeconomic and poverty-specific elements of proposed strategies.
- **Quality of growth.** Emphasis on the pre-eminence of faster growth is accompanied by inadequate assessment of the meaning of 'pro-poor' growth.
- **Consultation vs participation.** Consultation levels appear high, but evidence of true participation – especially shared decision-making by parliaments – is harder to find.
- **'Social impact' of adjustment.** This is taken seriously in ex ante strategy design and rhetoric, but in-depth evaluation of the possible social downside of macroeconomic adjustment is lacking.
- **Time inconsistencies.** Despite some recent adjustments to the process, the urgency of preparing PRSPs for debt-relief purposes remains inconsistent with the time needed for preparing a genuine anti-poverty strategy (possibly 5 years).
- **External constraints.** More recognition is needed of the

relevance of the external environment – particularly the impact of HIV/AIDS and accelerating trade reforms – in formulating a viable poverty strategy.

Evidence supporting these propositions confirms many external critics in their view that the Fund's involvement in structural – including social – areas should be limited. They consider that longer-term lending facilities – including ESAFs and the PRGF – have drawn the Fund into technical areas of conditionality, for which it possesses neither the requisite specialist skills nor the institutional commitment,

and which are more appropriately dealt with by the World Bank. For its part, the Fund regards these programmes as evidence of its commitment to pro-poor development. Moreover, the PRGF provides the basis for IMF debt relief through the HIPC initiative, and external evaluations of the ESAF programme offer compelling evidence that aid (including presumably debt-relief) is effective only in satisfactory macroeconomic policy environments – and no one seriously disputes the Fund's primacy in this area. Since there is validity in both these arguments, a fair conclusion is that the present partnership deal between the Bank, the Fund and its member countries should be allowed more time to bed down, provided the lessons intimated above are seriously addressed by all concerned.

**“The present partnership deal between the IMF and the World Bank should be allowed more time to bed down”**

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### **Connecting stabilisation and the social agenda**

The Fund clearly recognises the need to engage increasingly with the broader political and social – as well as the economic – sustainability of its programmes. The short shelf-life of many trade and structural reform efforts demonstrates that even technically sound policies forced on unwilling governments, in return for adjustment lending or HIPC relief, often precipitate both a political backlash and policy reversals. The backlash may be slow to show up in autocratic countries; in democracies, however,

sustainable policies must carry a reasonable degree of popular support and avoid unfair distributions of the cost burden. This implies more in-depth analysis of policy impacts and much more real consultation – requirements that, in turn, make the IMF's task more difficult.

Can the IMF's traditional operating style – somewhat inflexible, mechanically technocratic, and constructed around a narrow economics agenda – really adapt to embrace greater respect for democratic consultation, an extended agenda, concern for minorities, and genuine participation? The 'romantics' argue that it should not even be asked to do so, but should be restricted to a very narrow mandate. But this is a naïve view. If the developing world is truly to be characterised by greater democracy, policy ownership and citizen participation, the Fund must either be a part of that paradigm or leave the stage. To date, the Fund's outward face has adapted to these matters – but substance has lagged behind.

Part of the answer lies in the Fund contracting out a significant proportion of the technical work – including the design of financial codes and poverty strategies – associated with the enlarged social agenda. However, it is an open question how far that process should go. But the Fund also has to build the capacity to live with the sub-contractors' work and with the results of more participatory processes. This includes a willingness to accept greater diversity of policy solutions, as well as modification of some elements of the Fund's standard menu of policy prescriptions.

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