



european network on debt & development

## **Bail-out or blow-out?**

**IMF policy advice and conditions**

**for low-income countries at a time of crisis**

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- a specialist group with a reputation for producing accurate research and analysis on complex development finance policy issues;
- a clearing-house for synthesising and exchanging NGO and official information and intelligence;
- a facilitator of meetings and processes which improve concerted advocacy action by NGOs across Europe and in other regions.

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## About this briefing

This briefing is part of a series on IMF and World Bank economic policies and conditionality.

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Helpful suggestions on a draft of this briefing were provided by staff from the IMF, ILO and UN DESA.

Thanks are also due to:

Alex Wilks and Bodo Ellmers (EURODAD), Hetty Kovach (Oxfam GB), Bhumika Muchhala (Third World Network).

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This report was produced with the financial support of the European Commission. The views presented in this report do not necessarily represent the views of the Commission.



## Executive summary

At the London summit in early April, the leaders of the world's twenty richest countries decided that the International Monetary Fund (IMF) will be a major instrument to respond to the financial and economic crisis. They agreed to quadruple the Fund's resources from \$250 billion to \$1 trillion. But is the IMF fit for the purpose? Have some of these leaders forgotten how the IMF imposed harmful conditions in their own countries in the wake of the 1990s crisis which contributed to sink their countries further? What will be the outcome of the G20 decision for the tens of millions of people who are already suffering from the combination of the food, financial, economic and climate crises?

Eurodad's analysis of ten IMF agreements signed in the last six months shows that the IMF is still advising stringent fiscal and monetary policies to low income countries as well as controversial structural reforms. If the Fund is to provide funding to poor countries to meet the financial gaps created by the crisis it has to change and it has to do it soon. Reacting poorly and reacting late may mean death and starvation for millions of people in poor countries.

The \$1 trillion that the IMF will dispose of as a result of the G20 deal in London on 2<sup>nd</sup> April will certainly change the landscape of IMF lending to middle income countries. However, it is still uncertain what share is going to be channelled to low income countries, and on what terms. Impoverished countries are likely to receive around one fortieth of the one-trillion dollar deal – only \$20 billion. This money may be disbursed over a two to three year period and it may also be very expensive. Limited reforms to IMF conditionality and lending terms have also been announced, but these are slight shifts and have not dramatically changed the IMF's relations with recipient countries.

**Table 1: G20 financial package to revamp IMF resources**

Amount	Channel/ source	Details	New amount for low-income countries
\$250 billion	IMF Special Drawing Rights	Equivalent to printing money at international level.	\$19 billion.
\$500 billion	Contributions to the IMF for on-lending	\$250 billion now and another \$250 billion at the end of 2009. (\$100bn from Europe; \$100bn from Japan; \$40bn from China; the remaining \$250bn will be raised through New Arrangements to Borrow).	New Arrangements to Borrow funds are used, in principle, for non-concessional lending only. However, there is agreement to double the IMF's concessional resources to \$4 billion.
\$6 billion	IMF gold sales	To be agreed in the course of the next few months.	As discussion at the IMF Board stands now, only \$1 billion may go to LICs, and spread over the next 2-3 years

Source: Eurodad analysis of G20 Communiqué, London 2 April 2009.

The IMF estimates that, as a result of the crisis, thirty-eight of the world poorest countries could face a balance of payments shortfall of \$216 billion in 2009.<sup>1</sup> This is only the shortfall that low income countries will face in the budgets that were designed to meet their regular expenditures in "times of peace". It does not include the amounts that low income countries will need if they are to put in place the type of additional fiscal stimuli that Northern countries have announced to keep their economies afloat. According to the World Bank, this would require another extra \$41 billion in 2009, making a total of over \$250 billion for 2009.

<sup>1</sup> According to the IMF paper "The Implications of the Global financial Crisis for Low-Income Countries", March 2009, this figure "is computed by adding up the declines in several components of the balance of payments that may be considered exogenous in the short run: exports, FDI, remittances, donor grants, and the price effects on imports of the change in food and fuel prices" (page 57). <http://www.imf.org/external/pubs/ft/books/2009/globalfin/globalfin.pdf>

## Recent reforms at the IMF: not so fast

The renewed importance of the IMF and recent changes it has instituted mean less for low income countries than for middle income ones. In recent years when the institution was shedding middle income governments and deemed irrelevant from right and left, it maintained a strong influence in the world's poorest countries, providing both finance and policy advice.<sup>2</sup>

Terms of lending for poor countries may also remain largely unchanged, and therefore very unattractive to indebted governments. The new Flexible Credit Line (FCL), which is to provide precautionary credit with very low conditionality, will only be available for what the IMF calls "strong performers" - that is richer middle income or high income countries with policies judged adequate by the Fund. The Fund has also recently reformed some of the features of the Exogenous Shocks Facility (ESF) to ease low income countries' access to Fund's resources in the event of external shocks. More recently, in March 2009, the Fund also phased out Structural Performance Criteria, one type of condition attached to their loans.

**Table 2: IMF facilities and lending instruments**

Facility	Purpose
Exogenous Shocks Facility (ESF)	Provides financial assistance to low-income countries facing exogenous shocks. It is available to countries eligible for the Poverty Reduction and Growth Facility (PRGF) but that do not have a PRGF program in place. Financing terms are equivalent to a PRGF arrangement. The ESF has a Rapid Access Component (RAC) – which in principle does not have conditionality attached – and a High Access Component. The ESF can be used concurrently with a Policy support Instrument (PSI), Emergency Post Conflict Assistance (EPCA), Staff Monitored Programs (SMPs) or, in rare cases, an off-track PRGF. This facility was reformed in September 2008.
Flexible Credit Line (FCL)	New credit line introduced in 2009 for countries with very strong fundamentals, policies, and track records of policy implementation. The FCL is intended for crisis prevention purposes. FCL arrangements would be approved for countries meeting pre-set qualification criteria. Disbursements under the FCL would not be phased or conditioned to policy understandings as is the case under a traditional Fund-supported program.
Poverty Reduction and Growth Facility (PRGF)	The IMF's main instrument for financial assistance to low-income countries. It was introduced in 1999. Currently, 78 low-income countries are eligible for PRGF assistance. Eligibility is based principally on the IMF's assessment of a country's per capita income, drawing on the cutoff point for eligibility to World Bank concessional lending (currently 2007 per capita gross national income of \$1,095). Loans under the PRGF carry an annual interest rate of 0.5 percent, with repayments made semiannually, beginning 5.5 years and ending 10 years after the disbursement. Concessional lending under the PRGF is administered through the PRGF-ESF and PRGF-HIPC Trusts.
Policy Support Instrument (PSI)	Introduced in October 2005, this facility provides IMF advice to low-income countries without financial assistance. The PSI signal to donors, multilateral development banks, and markets the Fund's endorsement of a member's policies.
Stand-By Arrangement (SBA)	The bulk of Fund assistance is provided through SBAs. Intended to provide financial assistance to address short-term balance of payments problems. The length of a SBA is typically 12–24 months, and repayment is due within 3¼-5 years of disbursement. SBAs may be provided on a precautionary basis—where countries choose not to draw upon approved amounts but retain the option to do so if conditions deteriorate—both within the normal access limits and in cases of exceptional access. Non-concessional loans are provided mainly through Stand-By Arrangements (SBA) and the Flexible Credit Line (FCL) for members with very strong policies and policy frameworks. Except for the PRGF and the ESF, all facilities are subject to the IMF's market-related interest rate, known as the "rate of charge," and large loans carry a surcharge. The rate of charge is based on the SDR interest rate, which is revised weekly to take account of changes in short-term interest rates in major international money markets.

Source: IMF website, [www.imf.org](http://www.imf.org)

<sup>2</sup> "Critical Conditions: the IMF maintains its grip on low-income governments", Eurodad, April 2008: [www.eurodad.org/uploadedFiles/Whats\\_New/Reports/Critical\\_conditions.pdf](http://www.eurodad.org/uploadedFiles/Whats_New/Reports/Critical_conditions.pdf)

However, these changes are too little and too slow. The ESF still remains too expensive for low income countries.<sup>3</sup> Particularly in times of crisis large amounts of finance for these countries should be channelled at highly concessional terms to avoid new rounds of debt that may strangle these countries' fiscal space in the near future. The abolition of Structural Performance Criteria, although welcome, continues to leave unchanged other types of structural conditions as well as macroeconomic conditionality. These have been strongly criticised by some Southern country governments and independent researchers for obliging impoverished countries to adopt stringent fiscal and monetary policies. If this continues it will prevent increases in government expenditure to maintain economic activity at this time of crisis and safeguard pro-poor spending. As a Ministry of Education official in Sierra Leone stated, "IMF policies create and sustain poverty. IMF/World Bank policies are diametrically opposed as the former stymied the realisation of the latter".<sup>4</sup>

There are also concerns that reforms that formerly were pushed via conditionality may no longer come as binding conditions, but still feature in the IMF programme for the country. Although programmes are the outcome of the Fund and government negotiations, the Fund has a strong leverage in defining the features of the programmes because of its technical expertise and because it controls the purse strings. Countries are monitored and assessed on progress in areas defined in IMF programmes, even if these areas are not subject to strict conditionality.

This is the case in countries accessing the Rapid Access Component (RAC) of the ESF. Under the RAC, a country can access fairly quickly, up to 25 percent of its quota for each exogenous shock, with resources normally being provided in a single disbursement. While the RAC is formally conditionality-free and does not contain a conditionality matrix, the programme objectives are drawn from the IMF's analysis of that country's situation and recommendations by IMF staff, including through its Article IV and other assessments. Lifting formal conditionality does not necessarily lead to greater policy and fiscal space for countries to choose from a wider range of policy options if such options depart from IMF orthodoxy.

## **IMF conditions and advice at a time of crisis**

Restrictive IMF conditions and policy advice, which have already been problematic in times of economic growth and increasing aid flows, would be reckless in times of crisis. Poorer countries must be given the fiscal space necessary to pursue the kinds of counter-cyclical policies currently being used by rich countries, especially as the current financial and economic crises come on top of severe poverty and food price crises. UN Secretary General Ban Ki-moon warned G20 leaders before their summit in London that "at least \$1 trillion is needed to help developing countries get through the global financial crisis ... In providing this support you will bolster the global economy, help to underpin your own growth, and secure global stability."<sup>5</sup> This will obviously require that richer countries mobilise additional resources to help countries bridging the giant financing gaps they face and that these countries are allowed to implement policies which allow them to boost their economies.

The role of the IMF is paramount, not only as a lender but also as a gate-keeper for other incoming financial flows, as bond buyers and donors typically require that recipient countries are on-track with an IMF programme as a key "signal" to decide whether grants and loans continue flowing. The IMF has a strong role in determining what happens to incoming aid. In 2007 Sierra Leone's foreign aid suddenly dried up because of a negative IMF assessment. Countries such as Ethiopia continue to raise these concerns. In January 2009 the government of Ethiopia submitted to the IMF its request to be approved for the Fund's Exogenous Shocks Facility. It wrote that "several donors have been delaying disbursements because of concerns about Ethiopia's macroeconomic situation. ESF access would not

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<sup>3</sup> Civil Society letter on "The IMF response to exogenous shocks caused by the food and fuel crisis":

[www.ifwatchnet.org/sites/ifwatchnet.org/files/ESF%20Letter%20to%20IMF%20Executive%20Board%20August%202009.pdf](http://www.ifwatchnet.org/sites/ifwatchnet.org/files/ESF%20Letter%20to%20IMF%20Executive%20Board%20August%202009.pdf)

<sup>4</sup> Quoted in "Contradicting commitments: how the achievement of education for all is being undermined by the IMF", ActionAid, September 2005: [www.actionaid.org/assets/pdf/contradicting\\_commitments4.pdf](http://www.actionaid.org/assets/pdf/contradicting_commitments4.pdf)

<sup>5</sup> Press release by the UN Secretary General Ban Ki-moon, 26 March 2009:

[www.un.org/apps/news/story.asp?NewsID=30305&Cr=Financial+crisis&Cr1](http://www.un.org/apps/news/story.asp?NewsID=30305&Cr=Financial+crisis&Cr1)

only close the remaining financing gap in 2009, but also strengthen the credibility of Ethiopia's macroeconomic policy commitment".<sup>6</sup>

This briefing reviews ten IMF crisis loans for low income countries, including the four Exogenous Shock Facilities approved since the end of 2008, four Poverty Reduction and Growth Facilities (PRGF) approved in 2009, and two Stand-By Arrangements for Armenia and Mongolia.<sup>7</sup> It assesses whether, in times of crisis, IMF programmes allow for greater flexibility in these countries' fiscal and monetary policies, as well as in the structural reforms. The briefing reviews both IMF binding and non-binding conditions and programme objectives which are not subject to strict conditionality.

Eurodad findings show that **IMF programmes for low income countries are granting extremely limited additional flexibility in fiscal and monetary policies**. Limited flexibility is clearly granted on a very short-term and temporary basis, while emphasising the need to rapidly return to tighter fiscal and monetary objectives. Of the ten countries for which Eurodad has assessed the new IMF programme:

- five programmes push for wage bill freezes or cuts;
- five have to reduce their deficit, and
- all have to make spending cuts;
- five out of the ten programmes still prompt governments to pass on food and fuel rises to their citizens.
- None have flexibility to defer debt payments. Indeed for Senegal the Fund also requires as a binding condition that "any proceeds from asset sales be used for settlement of payment delays, and repaying nonconcessional debt".<sup>8</sup>

**Slightly greater flexibility compared to previous years is shown with regards to structural reforms.**<sup>9</sup> Privatisation and liberalisation related reforms are less frequent in the programmes reviewed. They tend not to be imposed any longer as binding conditions, but they still appear as an integral part of some Fund programmes. In some programmes, such as the ESF for Senegal, Malawi, and the Kyrgyz Republic, structural reforms are strongly focused on public financial management, with much less – or none – structural reforms in other areas. **However, all programmes without exception still foster structural reforms which may be deemed controversial, such as raising utility tariffs, tax reforms aimed at strengthening indirect taxation, financial and energy sector privatisation, or trade liberalisation.**

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<sup>6</sup> The Federal Democratic Republic of Ethiopia: Request for Disbursement Under the Rapid-Access Component of the Exogenous Shocks Facility, January 2009.

<sup>7</sup> See table in Annex 1.

<sup>8</sup> Senegal: Letter of Intent and Memorandum of Economic and Financial Policies, December 2008.

<sup>9</sup> "Critical Conditions: the IMF maintains its grip on low-income governments", Eurodad, April 2008: [www.eurodad.org/uploadedFiles/Whats\\_New/Reports/Critical\\_conditions.pdf](http://www.eurodad.org/uploadedFiles/Whats_New/Reports/Critical_conditions.pdf)

## Tightening fiscal and monetary policies: will impoverished countries sink further?

Fiscal and monetary policies determine the resources available to be spent either through government investment or recurrent expenditures. Fiscal policies determine the extent to which a country will be able to expand or cut its budget; how much new debt it will be able to contract; or how much money will be put aside to service debt repayments. Monetary policies determine how much money will be put into circulation; interest rates – and thus the ability of private sector and individuals to contract new debts; or the level of reserves, and thus the amount of available resources for government spending.

In recent months, richer countries have actively used monetary and fiscal tools in a desperate attempt to counter the effects of the crisis. US and European governments have reduced interest rates to close to 0% to provide incentives for private sector and personal borrowing. Richer countries and many emerging economies raced to provide fiscal stimulus – mostly in the form of increased government spending – to boost effective demand in their sinking economies. These measures have not only been applauded but also prompted by the IMF, in a sudden turn to Keynesianism. In December 2008, IMF chief economist Olivier Blanchard said: “What is needed is not only a fiscal stimulus now but a commitment by government that they will follow whatever policies it takes to avoid a repeat of a Great Depression scenario”.<sup>10</sup>

However, **Eurodad finds that this is not what the IMF has been advising, during the very same months, to the world’s poorest countries.** Virtually all countries we have assessed are required to follow tight fiscal and monetary policies, including by reducing their deficits; capping their ability to contract new debt and setting aside the necessary fund to service their debts; increasing their level of reserves; and lowering inflation, through higher interest rates. This is the rule in all IMF programmes approved in the last six months. Almost all programmes make clear that the overall objective is the “forceful implementation of the planned fiscal and monetary tightening.”<sup>11</sup> Similar statements are found throughout the programmes, including in Armenia, Ethiopia, the Kyrgyz Republic, Malawi and Mongolia. Although IMF staff consulted stressed that these programmes reflect the authorities’ choices, interestingly, the programme for Malawi states that “a tight budget for FY2008/09 has been approved despite significant political hurdles (and) ... an impasse in Parliament; it is fully in line with staff recommendations”.<sup>12</sup>

There are some exceptions where greater flexibility is being granted. But they are rare in numbers and limited in the extent to which they allow for alternative policies.

### Fiscal policy

In more than half of the countries assessed, the IMF programme intends to **reduce the deficit below 5% of GDP.** In Cote d’Ivoire, Ethiopia, the Kyrgyz Republic and Tajikistan targets are even more stringent, as the 2009 deficit is set below 2% of GDP. In countries such as Ethiopia where the annual shortfall of resources needed to reach the Millennium Development Goals (MDGs) was estimated at \$1.6 billion before the crisis,<sup>13</sup> further budget cuts will undoubtedly jeopardize the possibility of reaching the MDGs in 2015.

Ethiopia has been so far the only country that has benefited from the conditionality-free Rapid Access Component of the ESF. However, this has not translated into any departure from the IMF orthodoxy. The programme’s key measures include: “Significantly tightening fiscal policy and eliminating domestic borrowing... The general government deficit is projected to be reduced from 2.9 percent of GDP in 2007/8

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<sup>10</sup> “IMF spells out need for global fiscal stimulus: Interview with IMF Chief Economist Oliver Blanchard”, December 2008: [www.imf.org/external/pubs/ft/survey/so/2008/INT122908A.htm](http://www.imf.org/external/pubs/ft/survey/so/2008/INT122908A.htm)

<sup>11</sup> The Federal Democratic Republic of Ethiopia: Request for Disbursement Under the Rapid-Access Component of the Exogenous Shocks Facility, January 2009.

<sup>12</sup> Malawi: Request for a One-Year Exogenous Shocks Facility Arrangement, January 2009.

<sup>13</sup> UN Development Group: [www.undg.org/archive\\_docs/4447-Moving\\_the\\_MDGs\\_Agenda\\_forward\\_in\\_Ethiopia.doc](http://www.undg.org/archive_docs/4447-Moving_the_MDGs_Agenda_forward_in_Ethiopia.doc)

to 1.5 percent in 2008/9.” These objectives are said to have been set by national authorities; however, “the (IMF) staff viewed the policy response as appropriate and urged forceful implementation”.<sup>14</sup> IMF staff presumably made their views known at the time when the government was establishing its targets.

There is no doubt that long-term macroeconomic imbalances are bad for the poor. However, IMF programmes are not assessing the long term costs of cutting expenditures today. Only this year \$36 million would be needed to address the immediate needs of Ethiopian children. In the absence of this amount, “175,434 children under five are likely to need treatment for severe acute malnutrition in 2009”.<sup>15</sup> However, the IMF fails to account for the threat that fiscal tightening poses to the long term productive and human capacity were a whole generation of children to suffer from malnutrition as a result of the crisis.

On fiscal policy, the PRGF for the Republic of Congo aims at the apparently sensible objective of “achieving long-term fiscal sustainability to ensure that future generations benefit from Congo’s current oil wealth.” The staff estimates that this would occur when the basic non-oil primary deficit is in the range of 3 to 5% of non-oil GDP. However, the implication of this long term objective is an “annual deficit reduction of 3 to 4% over the next few years”, which for 2009 accounts for a 3% reduction of the non-oil deficit “based primarily on nominal cuts in non-priority spending, including a further decline in fuel subsidies.” Not surprisingly, Congolese authorities “express concern that the pace of fiscal adjustment may not allow for the flexibility needed to address immediate needs”.<sup>16</sup>

Some degree of flexibility is shown in some programmes, such as in Armenia, the Kyrgyz Republic, or Tajikistan, allowing budget deficits to increase. However, these countries came from very low budget deficits or even surplus – such as in Tajikistan. Deficit increases are generally as low as 1%, and none of these countries escapes some type of spending cuts. In Armenia, the Stand-By Arrangement approved on March 2009 allows the deficit to increase up to 2.8%. The programme also provides “room for additional infrastructure and investment spending as foreign financing materialises”. This is up from the objective to reduce the budget deficit to 1% 2009 in the PRGF agreement which was approved in October 2008, and which has now been cancelled and replaced by the Stand-By Arrangement (SBA). However, the deficit for 2009 is still down from the 3.5% which was projected for 2008 had the budget been fully executed.<sup>17</sup>

Greater flexibility in the Stand-By Arrangement for Armenia is consistent with the slightly greater flexibility shown in the PRGF approved in October 2008, where IMF conditions allowed for an exceptional agreement of \$50 million of new debt (partly on nonconcessional terms) from the World Bank and other international financial institutions.<sup>18</sup> These new resources were intended to finance several large infrastructure projects. Ironically, this amount coincided with the delayed disbursement of \$50 million committed by the Millennium Challenge Corporation for 2008. In Tajikistan, after years of surplus, the 2009 budget targets an overall deficit of 0.5% of GDP. However, given the needs for “additional social spending to alleviate the immediate impact of the global crisis on the population”, the deficit will be insufficient to meet Tajikistan’s financial needs so the government has therefore been forced to identify “expenditure cuts of 1.5% of GDP in current spending”.<sup>19</sup>

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<sup>14</sup> The Federal Democratic Republic of Ethiopia: Request for Disbursement Under the Rapid-Access Component of the Exogenous Shocks Facility, January 2009, page 7-8.

<sup>15</sup> UNICEF Humanitarian Action Update, March 2009:

[http://www.unicef.org/infobycountry/files/ETHIOPIA\\_UNICEF\\_HAU\\_12\\_March\\_2009.pdf](http://www.unicef.org/infobycountry/files/ETHIOPIA_UNICEF_HAU_12_March_2009.pdf)

<sup>16</sup> Republic of Congo: Staff Report for the 2008 Article IV Consultation, Requests for a Three/Year Arrangement Under the Poverty Reduction and Growth Facility, February 2008.

<sup>17</sup> The actual deficit in 2008 was finally limited to 1.9% of GDP “by saving revenue over-performance and curtailing non-priority spending.” Staff Report for the 2008 Article IV Consultation and Request for a Three-Year Arrangement under the Poverty Reduction and Growth Facility, October 2008.

<sup>18</sup> Republic of Armenia: 2008 Article IV Consultation and Request for a Three-year Arrangement Under the Poverty Reduction and Growth Facility, January 2009, page 12.

<sup>19</sup> Republic of Tajikistan: Memorandum of Economic and Financial Policies, March 2009.

**Table 3: Budget cuts**

COUNTRY	Deficit targets	Spending cuts	Some fiscal flexibility built into the programme
Armenia	Below 3% GDP		Yes
Congo (Republic of)	Surplus (mid-term target)		
Cote d'Ivoire	Below 3% GDP	Yes	
Ethiopia	Below 3% GDP	Yes	
Kyrgyz Republic	Below 3% GDP	Yes	Yes
Malawi		Yes	
Mongolia	Below 6% GDP	Yes	
Sao Tome	Below 5% GDP	Yes	
Senegal	Below 3% GDP		Yes
Tajikistan	Below 3% GDP	Yes	Yes

Source: Eurodad analysis of IMF programme documents December 2008 – May 2009.

In the Kyrgyz Republic a deficit increase is also foreseen in 2009 (up to 1.7% from a very low base);<sup>20</sup> however, such an increase is still accompanied by “sizable additional spending cuts”, including cuts in the **wage bill**.<sup>21</sup> Programmes for Mongolia and Sao Tome also foresee wage bill restraint. IMF Staff consulted to produce this study argued that the wage bill in Sao Tome absorbs nearly 40% of current public expenditure. Although proportions are high, once again the programme does not take into account the needs to access health services and workers of a country where almost one out of ten infants does not survive its first year of life.<sup>22</sup>

In Ethiopia, despite a general target to reduce the deficit from 2.9 to 1.5% of GDP in 2009, the IMF programme warns that “should expected revenue growth disappoint, the authorities stand ready to cut lower priority expenditure”, cutting investment spending and freezing the wage bill.<sup>23</sup> This may have devastating consequences in a country where per capita health annual expenditure stands at \$6, less than 20% of the minimum recommended by the World Health Organisation to cover basic health needs.<sup>24</sup>

<sup>20</sup> IMF Staff consulted pointed out that the Kyrgyz Republic will be allowed to incur into higher budget deficits (up to 6%) as a result of the last Staff Mission. They also pointed out that the next PSI review for Senegal will allow a budget increase of 1% with regards to the foreseen deficit for 2009 (from 3 to 4%). However, Eurodad has not had access yet to these documents.

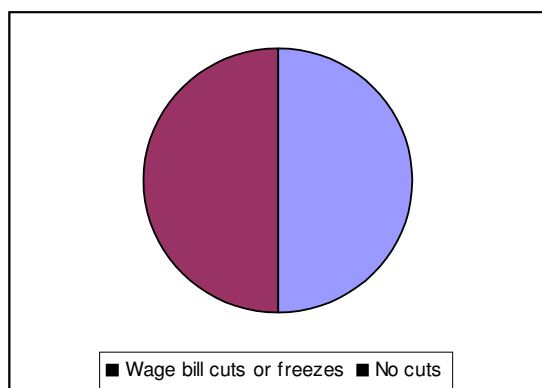
<sup>21</sup> Kyrgyz Republic: Staff Report, Request for a 18-Month Arrangement Under the Exogenous Shocks Facility, December 2008.

<sup>22</sup> Data source: Millennium Development Goals indicators: <http://mdgs.un.org/unsd/mdg>

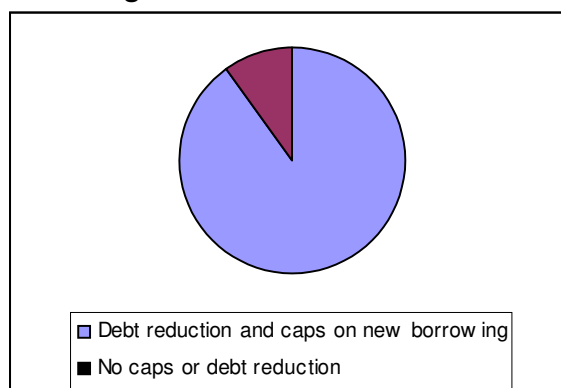
<sup>23</sup> The Federal Democratic Republic of Ethiopia: Request for Disbursement Under the Rapid-Access Component of the Exogenous Shocks Facility, January 2009.

<sup>24</sup> Source: The Global Fund: [www.theglobalfund.org](http://www.theglobalfund.org)

**Figure 1: Share of IMF programmes requiring wage bill cuts or freezes**



**Figure 2: Share of IMF programmes requiring debt reduction and caps on new borrowing**



Source: Eurodad analysis of IMF programme documents December 2008 – May 2009.

Nine of the ten countries are also required to **reduce their debt levels or cap new borrowing**. The programme in Ethiopia requires eliminating domestic borrowing, and in Malawi it aims at a 1.4% of GDP reduction of domestic borrowing. The Armenian Stand-By Agreement also “aims to restrict spending financed by domestic resources and instead rely on external financing to fund the increase in capital spending”.<sup>25</sup> This measure may boost domestic consumption, but no mention is made of the risks of excessive reliance on external financing flows.

Such risk is indeed acknowledged in Tajikistan. However, the programme still emphasises that the government must settle “external payment obligations ... in a timely fashion.”<sup>26</sup> Debt repayment also drains an important share of resources available to be spent in Senegal, where “any proceeds from asset sales will be used for settlement of payment delays, and repaying nonconcessional debt.”<sup>27</sup> Whereas paying arrears is fundamental to ensure access to finance, priorities should be carefully considered in a country where one in every hundred women still dies while giving birth because of lack of skilled assistance. UNCTAD Secretary General Supachai Panitchpakdi is among others who have called for a moratorium on debt payments to Low-Income Countries to enable them to maintain spending during this crisis which they did not cause.<sup>28</sup> He said: “In the current global crisis situation both debtor and creditor countries would probably be better served if scarcer foreign exchange earnings in the debtor economies were used for the purchase of imports rather than for debt servicing”. This view does not so far seem persuasive to the IMF.

## Monetary policy

Seven of the ten programmes reviewed by Eurodad aim at lowering inflation rates, of which four intend to keep **inflation below 5%** in 2009. This is the case in Armenia, Republic of Congo, Malawi and Cote d'Ivoire. In the medium term, the programmes of the Kyrgyz Republic and Sao Tome also aim at keeping inflation in single digits. And in the Kyrgyz Republic there is an explicit call to increase interest rates as a measure to control inflation. The programme of Armenia goes further and includes moving to full-fledged inflation targeting.

Lowering inflation often comes hand in hand with the objective to move to **more flexible exchange rate regimes** (this is the case in Armenia, Ethiopia, Malawi and Mongolia). Many countries are moving to flexible exchange rates to avoid having to drain their reserves defending a de facto fixed exchange rate –

<sup>25</sup> Republic of Armenia: Memorandum of Economic and Financial Policies, March 2009.

<sup>26</sup> Republic of Tajikistan: Memorandum of Economic and Financial Policies, March 2009.

<sup>27</sup> Senegal: Letter of Intent and Memorandum of Economic and Financial Policies, December 2008.

<sup>28</sup> Temporary debt moratorium needed for some poor nations, says UNCTAD Secretary-General, 30 April 2009. At: [www.unctad.org/Templates/Page.asp?intItemID=4819&lang=1](http://www.unctad.org/Templates/Page.asp?intItemID=4819&lang=1)

this was the case of Armenia which lost about \$600 million, close to half their reserves, in 2008. This comes after years of sticking to hard currency pegs in what has proved a vain attempt to improve confidence in the economy.

Policy decisions to reverse existing exchange rate regimes should take into account the importance to avoid “polarised exchange rate regimes” – that is, either “hard pegs” or totally flexible exchange rates. Some heterodox macroeconomists highlight the advantages of intermediate exchange rate regimes, as they can strike a balance between conflicting demands faced by developing country governments. Intermediate regimes would provide greater flexibility between hard pegs, which require strict fiscal and monetary discipline, and freely floating exchange rates regimes which can increase the costs of trade.<sup>29</sup> IMF programmes are to a large extent silent about nuanced policy options and a greater intervention in flexible exchange rate markets – including some form of capital account regulation.

Also a constant in almost all IMF programmes reviewed is the requirement to **increase the country’s international reserves position**, up to three or four months of imports.

The IMF is introducing some flexibility into programmes to respond to changing circumstances, but this is patchy and slow. IMF statements released at the conclusion of staff missions to Malawi (March 2009) and Senegal (April 2009) only partially address the lack of flexibility in the original programmes. Only Senegal is allowed to incur a “moderate and temporary rise of the fiscal deficit in 2009 to compensate for falling tax collections”.<sup>30</sup> In both cases IMF Staff claim to be building in flexibility in these programmes on an ongoing basis. In the case of Malawi, IMF Staff consulted while researching this briefing mentioned that the “strongly front-loaded, high-access ESF arrangement from December 2008 helped Malawi avoid a harsh adjustment path.” However, the programme still comes hand in hand with spending cuts and “continued tight monetary policy ... (including) increase in short-term interest rates (which) should over time help reduce credit growth to levels more consistent with the reserve situation.” Fiscal expansion, according to IMF staff, is only warranted “as long as it can be financed through higher domestic revenues or additional concessional financing (subject to a cap, given the precarious reserve situation).” Moreover, IMF staff considers that given the current growth rate in Malawi, “a policy stimulus does not seem warranted at this stage.”

Some of these measures, such as limiting contraction of new nonconcessional debt, may be necessary in some cases to avoid new rounds of high indebtedness for these countries. Securing a certain level of international reserves may also be necessary for poor countries, to provide some scope for countering sudden external shocks without having to resort immediately to expensive and burdensome emergency borrowing. In fact, this has been the strategy of several middle income countries in the last years to avoid the need to borrow from the IMF or other international financial institutions in times of economic downturn, and thus avoid conditions and policy advice which several Asian and Latin American countries were obliged to undertake in the wake of the 1990s crises.

## Too little, too late

The IMF has shown some limited sensitivity to maintain or increase pro-poor spending in virtually all programmes reviewed. This is welcome. However, building increased social spending into the programmes will not suffice in the context of the crisis if it does not come hand in hand with more expansionary fiscal and monetary policies which keep the economy afloat and ensure that jobs are retained and created.

More worrying is the fact that macroeconomic policies spelled out in IMF programmes are strikingly similar for all countries, leaving little scope for governments facing different circumstances to choose among different types of macroeconomic policies to secure stability with equitable growth and poverty reduction. It is also striking that the IMF programmes for low income countries continue supporting contractionary fiscal and monetary policies at a time of deep recession, when decision makers in rich and emerging economies have fully embraced the Keynesian credo and aggressive counter-cyclical spending.

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<sup>29</sup> Stiglitz, J., et al.: “Stability with Growth”, Oxford University Press, 2006, p. 119.

<sup>30</sup> Statement at the conclusion of an IMF Staff Mission to Senegal, April 2008:

<http://www.imf.org/external/np/sec/pr/2009/pr09113.htm>

The IMF argues that despite its willingness to accommodate fiscal stimulus in low-income countries,<sup>31</sup> “without indications of a scaling up of donor aid, and in the presence of limited liquidity in the regional financial market, there is just a natural limit of what can be accommodated if one wants to avoid the accumulation of arrears”.<sup>32</sup> Fortunately, such limits are not subject to the forces of nature. There is a range of policy decisions – such as a debt service moratorium, debt cancellation, or an increase in the concessionality of IFIs resources – that could be taken to increase fiscal space for developing countries. However, the IMF’s efforts to secure medium-term economic stability are still strongly biased towards cutting on the spending side of the budgets, and opening-up developing countries economies to the international markets.

The possibility of alternative approaches was recently demonstrated in Ukraine. In recent negotiations with Ukraine, IMF’s advice on spending cuts – including on pensions and social spending – was offset by proposals from the ILO to have a closer look at the revenue side of the budget, and increase government revenues from taxation by increasing and making more progressive the Ukraine’s flat income tax rate. This is an example of how the involvement of other international agencies, including UN agencies, could expand the breath of policy options available for developing countries to achieve macroeconomic stability without jeopardizing equitable growth and poverty reduction.

A shy departure from old-fashioned IMF policy recipes is just starting to be noticed in some of the programmes assessed. However, there is no signal to abandon restrained fiscal and monetary policies to more openly consider heterodox macroeconomic policies that would allow for a better policy mix, increasing resilience of low-income countries. The 2009 “Regional Economic Outlook” for Sub-Saharan Africa suggests that timid moves towards greater flexibility may only be temporary, rather than an indication of a rethink now that the former economic consensus has been largely discredited. While the joint Bank and Fund “Global Monitoring Report” warns that the crisis could last in developing countries until 2012 (or beyond), the IMF is already hoping for the fiscal balances to start recovering in 2010, from a very momentary “slippage” this year.

**Table 4: Budget deficits evolution in Sub-Saharan Africa: 2008 - 2010**

	2008	2009	2010
<b>Average African LICs</b>	-7.9	-8.6	-7.9
<b>Congo, Rep. of</b>	25.5	-2.5	18.2
<b>Cote d’Ivoire</b>	-2.3	-2.0	-2.6
<b>Ethiopia</b>	-7.2	-5.4	-4.3
<b>Malawi</b>	-15.9	-13.8	-12.3
<b>Sao Tome</b>	-14.4	-44.3	-24.2
<b>Senegal</b>	-6.6	-6.8	-6.3

Low income countries have less scope than richer ones to institute expansionary policies given their level of available internal and external resources. However, IMF programmes are largely blind to countries’ needs. The IMF programmes assess resources available and then prescribe spending cuts or structural reforms to limit government expenditures. The IMF is well aware of the budgetary needs of the country, however, it systematically fails to highlight funding shortfalls and send the international community a warning to mobilise additional external resources, or agree debt reductions. Likewise, fiscal reforms advised for domestic resource mobilisation fail to put on the table the type of taxation policies on the economic activities and the sectors that could provide a substantial increase in government income. Whereas the IMF may not be best placed to provide this type of advice,<sup>33</sup> it should at least refrain from systematically narrowing tax policy options.

<sup>31</sup> IMF Press Release, 31 March 2009: “IMF mission calls for fiscal stimulus in Tanzania”, <http://www.imf.org/external/np/sec/pr/2009/pr09103.htm> and IMF Press Release, 13 May 2009: “IMF mission calls for fiscal stimulus in Mozambique”, <http://www.imf.org/external/np/sec/pr/2009/pr09165.htm> .

<sup>32</sup> Excerpt from informal conversations held with IMF staff in the course of this research.

<sup>33</sup> Civil society organization have been calling for an upgrading of the UN Tax Committee, which would be better placed to provide pro-poor and pro-development tax advice to developing countries:

[www.un.org/esa/ffd/doha/hearings/civilsociety/KeyRecommendations.pdf](http://www.un.org/esa/ffd/doha/hearings/civilsociety/KeyRecommendations.pdf) The Doha Declaration on Financing for

## Some progress on structural reforms: much further to go

Structural reforms set out in IMF programmes are controversial as they technically fall outside the core mandate of the Fund.<sup>34</sup> An evaluation by the IMF's own Independent Evaluation Office (IEO), published in December 2007, found that during this decade the Fund had contravened its own conditionality streamlining policy and dramatically increased both the number of structural conditions and their intrusiveness in recipient countries. Previous Eurodad research has also confirmed this.<sup>35</sup> IMF conditionality has spread to areas such as tax rates, banking regulation, commodity prices and even institutional reform. It has also spread to areas which are considered to be outside the Fund's expertise, such as state-owned enterprise reform and privatisation, social policies. Following the IEO evaluation and strong civil society criticism, the Executive Board prompted IMF management and staff to continue efforts to streamline structural conditionality and limit these conditions to those that are strictly macro-critical.

Some progress has since been made in the way that the Fund attaches structural conditions and advises low income countries on structural reforms. In March 2009, the Fund's Executive Board decided to abolish one type of structural conditions, the Structural Performance Criteria. Also welcome is the fact that some of the Exogenous Shocks Facilities – Ethiopia and Malawi – do not have formal structural conditions attached. Others, such as the Exogenous Shocks Facility for Senegal, do not have structural conditions, but this type of conditions are actually part and parcel of the Policy Support Instrument (PSI) that the country has with the IMF – a programme which does not provide funding but comes with conditions attached. Although these are only small steps, they are ones in the right direction and civil society hopes this will be just the start of a complete overhaul of IMF policy conditionality.

### Sensitive privatisation and liberalisation related reforms

Privatisation and liberalisation related reforms, which have proved to be highly controversial and even harmful in many cases, in particular in the utilities and essential services sectors, **are less frequent in the programmes reviewed**. They tend not to be imposed any longer as binding conditions, but they still appear as an integral part of some Fund programmes. This is the case in the PRGF approved in 2009 for the Republic of Congo, which includes **trade liberalisation** as part of the programme, “including reduction of the maximum common external tariff and tariff rates”.<sup>36</sup> In Cote d'Ivoire, the programme states that “following the signing of an interim agreement with the EU at end-2007, the government will continue to support the signing of a regional Economic Partnership Agreement (EPA).” EPAs have been highly controversial for pushing trade and development policies which are negative to the interests of developing countries.<sup>37</sup>

Likewise, **privatisation of the energy sector and reform of public enterprises** are also part of the PRGF for Sao Tome and Principe and the ESF for the Kyrgyz Republic. In the Kyrgyz Republic the programme aims at privatising parts of the energy sector and at seeking private participation for large hydropower project Kamar-Ata. Local CSO activists have for years expressed their concerns: “for about a decade, civil society activists are trying to prevent next phases of energy assets privatization, the main reason being that the first phase – which was intended to create joint stock companies – was unsuccessful as it did not result in efficient management, accessibility of energy and safeguards from commercial losses.”

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Development agreed at the Doha Conference held in November 2008 also called for a strengthening of the UN Tax Committee: <http://daccessdds.un.org/doc/UNDOC/LTD/N08/630/55/PDF/N0863055.pdf?OpenElement>

<sup>34</sup> Faced with strong criticism for its expansive and erroneous use of conditionality, the IMF approved in 2002 a set of guidelines to inform their use of structural conditionality: <http://www.imf.org/External/np/pdr/cond/2002/eng/guid/092302.htm>

<sup>35</sup> “Critical Conditions: the IMF maintains its grip on low-income governments”, Eurodad, April 2008.

<sup>36</sup> Republic of Congo: Staff Report for the 2008 Article IV Consultation, Requests for a Three/Year Arrangement Under the Poverty Reduction and Growth Facility, February 2008, page 14.

<sup>37</sup> TWN-Africa Policy Brief: “The Ghana – EU Stepping Stone Economic Partnership Agreement”, April 2009, <http://documents.twnafrica.org/policybrief-ghana-iepa.rtf>

### Box 1: Privatising Basic Utilities in Sub-Saharan Africa: The MDG Impact

In their book *“Privatization and Alternative Public Sector Reform in Sub-Saharan Africa”*, Kate Bayliss and Terry McKinley analyse the effects of privatisation on the delivery of water and electricity in Sub-Saharan Africa. Their main conclusion is that privatisation in these areas has been a widespread failure, which has hampered progress on the MDGs for both water and sanitation, and on many other MDGs dependent on energy.

They maintain that privatisation has failed on several counts. Contrary to expectations, private investors have shied away from investing in such utilities in the region. So it has been costly for governments to motivate them to invest. Moreover, the focus of investors on cost recovery has not promoted social objectives, such as reducing poverty and promoting equity.

The initial hopes for privatisation were so high that donor spending on infrastructure fell in the expectation that the private sector would take up the slack. For example, World Bank lending for infrastructure investment declined by 50 per cent during 1993-2002. At the same time, the World Bank increased its support for private investment in utilities through its International Finance Corporation. While Bank lending to public electricity utilities dropped from about US\$ 2.9 billion in 1990 to only US\$ 824 million in 2001, its sector lending to private investors rose from US\$ 45 million to US\$ 687 million. Hence, African countries have been caught in a terrible bind. Not only has donor financing of public investment declined but also private investment has followed suit. Moreover, many governments have had to adopt fiscal austerity programmes, which have led to further declines in domestic public investment in utilities.

As a result of the failure of privatisation, many donors have had to rethink their reform models. In 2004, a World Bank report described the privatisation of infrastructure as ‘oversold and misunderstood’ and highlighted the need for a case-specific approach. Thus, the Bank puts now greater emphasis on laying the pre-conditions for successful privatisation. The authors state that “where privatisation does not work, the knee-jerk response is to strive even harder to make it succeed. A deep-seated ideological aversion to the public sector is probably a major explanatory factor.” Despite years of trying to privatise utilities, the state remains, by far, the dominant provider of water and electricity. Even in countries where there has been some private sector participation, a strong state has still been needed to monitor and regulate private firms. According to the authors, contrary to popular perception, private sector participation does not increase competition. Private investors are interested in risk-free rather than competitive environments. In practice, they often do not compete to win contracts so much as governments compete to attract their investment.

The authors conclude that “this kind of experience, repeated throughout the continent, suggests that instead of offering lucrative incentives to private firms, the policy priority should be to refocus on building state capacity since the public sector will certainly continue to dominate provision.”

Source: UNDP International Poverty Center Policy Brief *“Privatising Basic Utilities in Sub-Saharan Africa: The MDG Impact”* by Kate Bayliss and Terry McKinley, January 2007, <http://www.undp-povertycentre.org/pub/IPCPolicyResearchBrief3.pdf>

**Raising utility tariffs and phasing out subsidies** is also controversial, as this can restrict poorer people’s access to basic utilities, such as energy, if the appropriate targeted subsidy schemes are not introduced simultaneously. In the wake of the 2008 food and fuel price rises, the IMF insisted in their programmes that governments should pass through price increases to the consumers.<sup>38</sup> This is **still the case in half of the programmes reviewed** – Congo, Ethiopia, Sao Tome, Senegal, and Mongolia – where the Fund still requires phasing out fuel subsidies, increasing domestic energy prices, or adopting market-based pricing for the energy sector. With regards to food prices, some limited exceptions are granted to Ethiopia and Malawi, where the programme allows the government to allow wheat imports for poor families below the market prices in Ethiopia, and fixing maize prices in Malawi. However, the programmes also clearly state that these are only temporary measures that will need to be phased out at a later stage.

<sup>38</sup> “Quick fixes or real solutions? WB and IMF responses to the global food and fuel crisis”, ActionAid, Bank Information Center and Eurodad, December 2008: [www.eurodad.org/uploadedFiles/Whats\\_New/Reports/Quick%20Fixes%20or%20Real%20Solutions.pdf](http://www.eurodad.org/uploadedFiles/Whats_New/Reports/Quick%20Fixes%20or%20Real%20Solutions.pdf)

Six of the ten programmes reviewed still contain **structural reforms in the financial sector**, which are actual programme conditions in the case of Armenia, the Republic of Congo, and Sao Tome and Principe. In Kyrgyz Republic, the programme envisages the sale of the state-owned Ayul Bank.

## Pushing “the tax consensus”

**Tax reform** is recurrent in several programmes. It is envisaged six of the ten programmes, including in Armenia, Congo, Cote d’Ivoire, Ethiopia, Kyrgyz Republic and Sao Tome. Some of these financial sector and tax reforms respond to the needs highlighted by the crisis, including strengthening financial sector capitalisation, strengthening the capacity of governments to mobilise domestic resources, or granting tax reductions on basic foodstuffs to ease consumer access in the context of increased foodstuff prices.

However other **reforms in these sectors could be highly controversial** if they are not designed in a way that takes fully into account the impact on the poor, and measures are not taken to offset potentially negative distributional impacts. This could be the case with the envisaged privatisation of the state-owned Ayul Bank in the Kyrgyz Republic. Likewise, the approval of the financial sector strategy in the Republic of Congo (structural condition) aims at an expansion of private sector credit which could be controversial if it is not offset with appropriate targeted measures to ensure that the most vulnerable sectors of the population will also benefit from greater access to credit.

With regards to tax reforms, temporary Value Added Tax (VAT) exemptions on foodstuffs consumed by the poor are envisaged in the programmes for the Republic of Congo and the Kyrgyz Republic. However, in Senegal, the programme aims at removing all subsidies on food products and reinstating duties and taxes on food. The IMF has been generally advising to phase out temporary tax exemptions on foodstuffs consumed by the poor once food prices have started to decrease. One of the reasons put forward by the IMF is that tax exemptions were not well targeted to the poor, so they should be substituted for schemes which target better the poor. The main concern is that such schemes may not yet be in place and the poor may have to pay higher prices for basic foodstuff as a result of phased out exemptions at a moment when they are facing the worst effects of the financial crisis.

This context also casts doubt on the appropriateness of the widespread IMF advice on VAT implementation in developing countries. A recently published Christian Aid occasional paper on tax policy in sub-Saharan Africa states that “although indirect taxes are not inherently regressive, the distributional impact of indirect taxes (such as VAT) depends on tax administration, the extent of the informal economy, the consumption bundles of different social groups, and whether the poor act as both consumers and producers of the same good. ... when implemented (indirect taxes) have proved regressive, and appear to become more so as the economy develops”.<sup>39</sup> The findings of this report coincide with those of a Christian Aid occasional paper. The paper claims that during recent decades a tax consensus has emerged among multilateral donors with regards to their tax-policy recommendations to developing countries. The paper also finds strong support for the claim that “the IMF has promoted the tax consensus – often in spite of evidence that the implied policies are failing to meet their objectives.” Indeed, tax reforms envisaged in the IMF programmes Eurodad has reviewed strongly lean towards implementation of VAT; reduction the number of tax incentives; and significant structural overhauls to the tax administration.

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<sup>39</sup> Marshall, John: “One size fits all? IMF tax policy in sub-Saharan Africa”, Christian Aid, April 2009.

## Box 2: What is the “tax consensus”?

A recent paper by Christian Aid “Once size fits all? IMF tax policy in Sub-Saharan Africa”, states that during recent decades, a powerful consensus has developed which has included not only the structure of taxes, but also the level of tax rates... to refuse to subscribe to it would be imprudent as well as incurring disapproval from the IMF and World Bank. According to the paper, the tax consensus can be summarised as requiring that countries aim for tax neutrality and typically for revenues of the order of 15-20 per cent. “Tax neutrality” is the theoretical outcome in which the tax system does not change economic incentives (eg for efficient production, consumption, investment etc). In practice, tax neutrality implies a shift away from direct taxation (the taxation of income and profits) and from trade taxation, and towards consumption taxation. Any revenue losses should, in theory, be compensated for by increases in the tax base and the efficiency of collection. Redistribution will occur – if at all – through government expenditures, not via taxation.

More specifically, the consensus has:

- encouraged reductions in the rates of corporate and, to a lesser extent, personal income taxation
- supported trade liberalisation (reduction of both export and import taxation)
- encouraged the introduction or expansion of sales taxes (and a value added tax, VAT, in particular), often including an element of regional harmonisation
- emphasised, especially in recent years, the need to reduce the number of incentives and exemptions across the tax code
- proposed significant structural overhauls to the tax administration.

With regards to corporate tax incentives and reductions, the paper says that despite their goal of increasing international competition, their actual distributional impact may be regressive, and that other important investment incentives, such as the rule of law, are missing options. The paper acknowledges the merits of enhanced tax administration and indirect taxation. However, it also cautions that these are not easy tasks, and all too often the results deviate dramatically from the expectations. It concludes that “tax neutrality, strong revenue mobilisation and global competitiveness are highly attractive outcomes for any developing country. (However) this first-best scenario seldom occurs in developing countries where the underlying prerequisites fail to hold, and this makes such prescriptions sub-optimal. Effective tax policy must consider the complex structural and political realities that characterise individual countries.”

### IMF recommendations

Despite numerous international criticism, the IMF has continued to promote the so-called tax consensus. This consensus is reflected in revenue trends across the sample of 18 sub-Saharan African nations assessed by the Christian Aid paper. It has focused upon reducing corporate, personal and trade tax rates in favour of expanding the base of consumption taxes. Additionally, the increasing prevalence of VAT and particular forms of tax administration and base enhancement are widely observed in specific country papers.

This paper has found strong support for the claim that the IMF has promoted the tax consensus – often in spite of evidence that the implied policies are failing to meet their objectives. Looking at how little policy recommendations differ across time and country reveals that many of the central tenets of the tax consensus are uniformly promoted by the IMF regardless of important country-specific characteristics. Certainly, there does not appear to be the diversity or magnitude of characteristic-specific differences in recommendations that the theoretical and empirical tax literature would propose. Where differences do exist, they are almost equally split between theoretically sound and wrong-headed recommendations for developing countries. Consequently, many countries are failing to realise the critical economic, social and political benefits associated with effective and inclusive taxation.

The paper recommends that wider development community, including NGOs and donor countries, must ensure that the option of the IMF continuing to promote inappropriate policies on a uniform basis is not left open.

*Source: Christian Aid Occasion paper, by John Marshall: “One size fits all? IMF tax policy in Sub-Saharan Africa”, April 2009, <http://www.christianaid.org.uk/images/imfoccpaper.pdf>*

Several of the IMF programmes reviewed – Ethiopia, Mongolia, Sao Tome, and Senegal – include the strengthening or establishment of **safety nets to protect the most vulnerable** sectors of the population. While this new sensitivity of the Fund is welcome, the concern remains that the IMF may not be best placed to provide this type of advice. IMF programmes should mainstream the needs for pro-poor spending, as well as the need to raise domestic revenue through improved taxation systems, when assessing the countries’ macroeconomic frameworks. However, the Fund should refrain from taking action in advising structural reforms in these areas, as this is not part of its core mandate and it lacks the right expertise on this area.

## Conclusions and recommendations: turning a blind eye to the crisis?

While the research department of the IMF publishes alarming statistics on the balance of payments shock for low-income countries this year and has revised downwards from 6.4% to 4.3% its 2009<sup>40</sup> growth projections for these countries, the country departments of the Fund are continuing largely as before the crisis.

Assessment of the IMF programmes to low-income countries agreed or amended since December 2008 show that by and large the IMF has not still changed its preference for stringent and pro-cyclical fiscal and monetary policies. Despite the Fund's increasing acknowledgement of the virtues of counter-cyclical policies and the need to scale up a coordinated fiscal stimulus worldwide, almost all IMF programmes for low income countries rule out any possibility of fiscal stimulus for them. The few examples of greater flexibility – such as allowing Armenia and the Kyrgyz Republic to slightly expand their fiscal policy – are extremely timid and exceptional. The rule in Fund programmes and conditions continues to be stringent fiscal and monetary policy. Greater recognition of the need to maintain social and pro-poor spending is welcome. However, it is often hard to see how this priority spending will be maintained in the context of the further budget cuts, fiscal consolidation, and efforts to rebuild the international reserves position that the IMF continues to demand.

Further progress has been made in the area of structural reforms and conditions, but this needs to go much further. Several commentators and decision-makers have stated that as the current financial and economic crisis was not caused by developing countries they should not have to face external policy conditionalities on any money provided to cushion the effects of the crisis. Structural reforms and conditionality frameworks are lighter for some IMF programmes than in previous years, and focus mostly on public financial management. This is the case for Exogenous Shocks Facilities in Senegal, Malawi and the Kyrgyz Republic. Also welcome is the fact that lower access programmes under the ESF framework do not have additional conditions attached, as is the case of Ethiopia. However, this is just part of the picture. ESFs usually complement other Fund programmes which are already in place, such as PRGF or PSI, to provide additional resources in the event of an exogenous shock. This means that the country is already facing the burden of structural conditions under other existing Fund programmes. Moreover, structural reforms also come in the form of policy objectives embedded in the programme – rather than under the shape of binding conditionality.

In the wake of the fuel and food crises, the IMF advised tax cuts on basic foodstuff products and enhancing safety nets for the poor. However, the Fund has not extended this approach to government macroeconomic frameworks at this time of crisis. So far, Fund programmes have proven to be blind to low income countries' budgetary needs; they have rather taken the scarce available resources as a given. The Fund should also highlight the budgetary shortfalls facing low income countries and signal to the international community what additional external resources are needed.

Funding needs of low income countries have skyrocketed as a result of the crisis. According to the Fund's own estimations, an additional \$216 billion will be needed in 2009 on top of what was anyway required.

The Fund has a very chequered and controversial history and has played a part in encouraging and persuading governments to implement liberalisation policies that have left them vulnerable to the current financial and economic crisis. Many governments and organisations remain extremely sceptical about the IMF's ability to reform and therefore about whether the IMF should play any part in the current crisis response. As a matter of principle, resources to cover for the shocks suffered by poor countries as a result of a crisis that they have not created should come as a compensation for the harm created. This means that these resources should be channelled in grant terms through the most appropriate mechanisms or institutions.

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<sup>40</sup> "The Implications of the Global financial Crisis for Low-Income Countries", IMF, March 2009, p. 5.

It appears that the G20 is of a different mind, however, and wishes the Fund to channel resources for low income countries to meet some of the financing gaps resulting from the crisis. If this is the case the IMF should:

1. Grant rapid access for low income countries at highly concessional rates. Rates of concessionality should be much higher than the existing ones – including the reformed ESF – and similar to IDA terms of lending.
2. Refrain from attaching any additional policy conditions, along the lines envisaged for the new Flexible Credit Line available for richer countries;
3. Refrain from providing stringent fiscal and monetary policy advice. More crisis waivers should be considered and granted to widen the fiscal space available for poor countries;
4. Not work on the strict assumption that available resources are fixed; instead highlight the budgetary shortfalls facing low income countries and signal to the international community what additional external resources are needed.

## ANNEX 1: List of operations assessed

<b>Country</b>	<b>Programme</b>	<b>Approval date</b>
Armenia	Stand-By Arrangement	March 2009
Congo, Republic of	Poverty Reduction and Growth Facility	December 2008
Cote d'Ivoire	Poverty Reduction and Growth Facility	March 2009
Ethiopia	Exogenous Shocks Facility	January 2009
Kyrgyz Republic	Exogenous Shocks Facility	December 2008
Malawi	Exogenous Shocks Facility	December 2008
Mongolia	Stand-By Arrangement	April 2009
Sao Tome and Principe	Poverty Reduction and Growth Facility	March 2009
Senegal	Exogenous Shocks Facility	December 2008
Tajikistan	PRGF	March 2009

## ANNEX 2: Acronyms

ESF	Exogenous Shocks Facility
FCL	Flexible Credit Line
FDI	Foreign Direct Investment
GDP	Gross Domestic Product
IEO	Independent Evaluation Office
ILO	International Labour Organisation
LICs	Low-income countries
MICs	Middle-income countries
MDGs	Millennium Development Goals
PRGF	Poverty Reduction and Growth Facility
RAC	Rapid Access Component (of the ESF)
SBA	Stand-By Arrangement
SC	Structural Conditionality
SPC	Structural Performance Criteria
UNCTAD	United Nations Conference on Trade And Development