The World Bank and its Loans for Structural Adjustment:

A Review of Five Years of Experience

By Frank Vogl

Structural adjustment lending was introduced in 1980 as the World Bank's response to helping many developing countries carry out a difficult process of policy and institutional reform in an unfavorable international economic environment. At the time, numerous oil-importing developing countries were experiencing serious balance of payments problems as a result of petroleum price increases in the 1970s, which in turn helped produce adverse terms of trade, and of high rates of inflation not countered by exchange rate adjustments. Development programs were threatened. There was a need to reduce balance of payments deficits in relation to national economies, and simultaneously to ensure that domestic policies, programs and institutions were adapted to maintain, or restore, a reasonable pace of economic development. These adverse factors were later compounded by the international recession which reduced the demand for developing countries' exports and further depressed the terms of trade, and by increases in real interest rates. The need for adjustment became increasingly pressing, but the environment to support this adjustment became more difficult and resource constraints more binding.

As of December 31, 1984, the World Bank had approved 29 structural adjustment loans (SALs) in 16 countries, for a total of over $4.5 billion (see Table). The World Bank and the IMF have worked in close cooperation in formulating appropriate adjustment programs, and these have enabled countries to implement significant and often politically difficult reforms. SALs are characterized by their focus on policy and institutional reform, their comprehensive coverage of both macroeconomic and sectoral issues, and their detailed articulation of the policy modifications to be undertaken within specified time periods. If the adjustment process is to have a meaningful impact on the structure of the economy, initial reform measures have to be followed by other complementary policy and institutional changes. Thus, programs are typically formulated to accomplish needed reforms over a period of five to seven years, and in most cases the World Bank provides support through a series of SALs.

Frank Vogl, director of the Information and Public Affairs Dept. of the World Bank *(photo: World Bank)*

The World Bank, owned by 148 nations, with Japan ranking behind the United States as the second largest shareholder, is concerned with economic and social development in the Third World. It aims to help nations help themselves to move forward in the development process. At times of serious economic adjustment, the Bank has found that its relatively new SAL approaches have been most constructive.

To achieve the central objectives of structural adjustment lending—reducing the current account deficit to a sustainable level, and maintaining or restoring growth momentum—improvements have been sought in four interrelated areas: trade policy, mobilization of domestic and foreign resources; efficiency of domestic resource use, and institutional reform. Clearly, the precise blend of these reforms, the specific measures chosen to implement them, their timing, and the particular sector focus depend on several features, in particular a country's initial economic conditions, and the strengths and weaknesses of its institutions. There are no general solutions; adjustment programs have to be carefully tailored to meet the specific needs and policy objectives of individual borrowers.

Trade policy reform

In many developing countries, the development process itself and the balance of payments are adversely affected by inappropriate trade policies. Protective regimes favor production for domestic markets, and have often created an anti-export bias. The restricted competition inherent in such regimes has been exacerbated by regulations which impede the entry of new firms, and which favor established producers in the allocation of foreign exchange and other scarce resources. Such policies have often led to high investment and production costs, inadequate absorption of labor, sluggish expansion of exports, and may have simply generated excess profits for protected industries.

Such trade policies have an unfavorable effect on the growth of exports, and in turn, a negative impact on country creditworthiness and debt servicing capacity. Although trade policy reform,

Frank Vogl is the director, Information & Public Affairs of the World Bank. He was a journalist and had served as reporter and editor for Reuters Economic Services and later as European Business Correspondent for the Times of London based in Frankfurt and later as U S. Economics Correspondent based in Washington.

by encouraging export growth and efficient import substitution, is crucial for improvements in balance of payments and creditworthiness, it has frequently proven difficult because it impinges on established interests. Conversely, the domestic constituency for trade reform is often weak as potential beneficiaries—prospective entrepreneurs, workers, and consumers—cannot clearly perceive the potential benefits. Yet, efficient resource use for development and balance of payments improvement can only be achieved within a generally open and competitive environment with reasonable incentives for exports.

In nearly all countries, SAL programs include trade policy reforms as part of the adjustment package. The relative emphasis placed on initiatives such as quantitative restrictions, tariffs, investment licensing and specific measures to facilitate exports have depended on country circumstances. Phased elimination of quantitative restrictions is part of the SAL programs for Jamaica, Korea, the Ivory Coast, Turkey, and the Philippines. Tariff reforms, comprising increasing uniformity and decreasing average levels of tariffs, are part of the SAL programs for Kenya, Thailand, Turkey, the Philippines, and the Ivory Coast.

SAL programs also include other measures to promote exports including duty-free regimes for export industry, export processing zones, export guarantee and credit insurance schemes (the Philippines, Mauritius), streamlining of administrative procedures to reimburse exporters for taxes on imported inputs, reform of foreign exchange allocation systems (Turkey, Kenya), investment incentives for exporters (Turkey), and tax reforms to reduce the bias against exports (Thailand, the Philippines). Where misalignment of the exchange rate is seen to be an issue, the World Bank has relied on the government to take appropriate measures under an IMF-supported adjustment program, as in Turkey and Jamaica.

Structural Adjustment Loans (approved as of December 31, 1984)

Country	When Approved	Amount: $ million
Kenya I*	1980	55.0
Kenya II*	1982	130.9
Turkey I*	1980	275.0
Turkey II*	1981	300.0
Turkey III*	1982	304.5
Turkey IV*	1983	300.8
Turkey V	1984	376.0
Bolivia*	1980	50.0
Philippines I*	1980	200.0
Philippines II*	1983	302.3
Senegal	1980	60.0
Guyana*	1981	22.0
Mauritius I*	1981	15.0
Mauritius II	1983	40.0
Malawi I*	1981	45.0
Malawi II	1983	55.0
Ivory Coast I*	1981	150.0
Ivory Coast II*	1983	250.7
Korea I*	1981	250.0
Korea II*	1983	300.0
Thailand I*	1982	150.0
Thailand II*	1983	175.5
Jamaica I*	1982	76.2
Jamaica II*	1983	60.2
Jamaica III	1984	55.0
Pakistan*	1982	140.0
Togo*	1983	40.0
Yugoslavia	1983	275.0
Panama	1983	60.2
Total		4,514.3

*Fully disbursed as of October 31, 1984

Resource mobilization

All SAL programs include appropriate measures to improve resource mobilization. In Mauritius, interest rate ceilings were removed to stimulate private savings. In Korea, steps were agreed to increase taxes, and to achieve improvements in government savings as a proportion of GNP. In Thailand, a tax package was agreed to increase government revenues as a proportion of GDP. The program for Turkey sought to liberalize interest rates on deposits as part of a new Capital Market law, with measures to simplify banking regulations and otherwise improve the performance of capital markets.

For obvious reasons, debt management has come to be regarded as a key instrument for resource management. About two-thirds of all SALs have included measures to improve external debt management, ranging from improving central bank or treasury control over borrowing, to reforms of the mechanisms for debt planning and budgeting, data collection, and monitoring (Thailand, Turkey, Senegal, Malawi). Firmer controls over the foreign borrowing of public enterprises have been an important feature of SALs (notably in the Ivory Coast, Malawi, and Kenya), since such borrowing has been a frequent source of excessive indebtedness.

Public enterprises have become an increasingly important aspect of the financial operations of governments in developing countries. They cover such diverse fields as electric power, transportation, industry and agriculture. They depend on public resources to help meet their investment needs, and too often generate operating deficits which then have to be covered by the budget or by public borrowing. Realistic investment programs and efficient operations are therefore crucial to the financial health of the public sector. These issues have been addressed through reforms in public enterprise pricing systems, salaries, and management.

To reduce claims on the government budget and on the domestic credit system, and to improve public sector finances in the longer term also require managerial and technological assistance to these enterprises so they can compete effectively in a market-oriented society. More realistic prices for public utilities in power and transport are essential to limit growth in demand, to reduce or eliminate operating deficits, and to assure that these enterprises contribute an appropriate share of their future investments. For other enterprises, price autonomy is important but must be matched by increased competition to avoid simply passing high costs on to consumers. SALs for Turkey, the Ivory Coast, Togo, Malawi, and Thailand have included components to address these issues.

Efficient use of resources

A central theme of all SALs is improved efficiency in resource use in the public and private sectors (a concern which is also addressed in trade regime reforms). Particular emphasis has been placed on the size and quality of public investment programs.

Resource constraints in many countries have required a scaling-down of investment programs, and a reallocation of available resources among projects. The need is to avoid across-the-board cuts, and to protect implementation of projects which support required changes in the structure of production, which are quick-yielding, and which will help limit the current account deficit. The review of a large public investment program is a major task for a government and shifts in priorities can only be effected gradually. For some countries the World Bank has used the considerable expertise of its staff in sector and project related activities to help review public investment programs. These reviews have been useful in initial identification of high-priority projects which should be continued, and in helping governments to decide on the redesign, postponement or elimination of lower-priority operations.

The important long-term point is the need to institutionalize better programming of public resources by having governments agree on strengthened, more explicit project selection criteria, and to allocate staff capable of applying these criteria to the analysis of new projects and to the review of current ones. This would often involve intensive staff training, modification of administrative arrangements (in particular, strengthening links between public finance and planning agencies), and most importantly, acceptance by managers of the potential benefits of modern management tools.

Another important and often neglected aspect of improving the productivity of capital is operation and maintenance. Returns from expenditures on adequate operation and maintenance activities are frequently high, and actual allocations low, compared to investments in new capacity. SAL programs have emphasized (particularly in African countries) the need to allocate sufficient funds for operation and maintenance, and to generate resources from identified project beneficiaries to provide an increasing share of these funds.

One additional issue of major concern in many countries is the efficiency of resource use in public sector enterprises. There are often major inefficiencies resulting from poor management, inappropriate government intervention and the absence of adequate market and financial discipline. Many of the present SAL programs address these issues. For example, the program for the Ivory Coast aims to improve management of parastatal enterprises by setting up an effective monitoring system, rationalization of their relationships with the government, and implementation of reorganization plans for major enterprises. In Pakistan, a system of incentives to promote efficiency was devised which allows managers to identify appropriate production targets, and which establishes criteria to evaluate results.

There is strong evidence that distortions in productive sector incentives have lowered GDP growth rates for many countries. Complex and cumbersome systems of price controls and input subsidies have developed. Some countries may have succeeded for a while in stimulating production in particular sectors, and in insulating particular groups from increases in the prices of commodities. Over the longer run, as these become financially untenable, the tendency in a number of developing countries is to hold down output prices, to the detriment of production increases. This is particularly true of agricultural production despite long and ample evidence of its sensitivity to output prices. Remunerative producer prices help to increase production and the export base while allowing governments to reduce or eliminate subsidies on inputs. Examples of SAL countries with substantial reforms in these areas are Senegal, Malawi, the Ivory Coast, Jamaica, and Togo.

Institutional reform

Institutional reforms feature in all SAL programs and are always closely associated with reforms in other areas. Indeed, institutional change is intended to ensure the durability of policy reform.

Intended institutional changes are heavily concentrated on macro-economic and financial management (all 29 SALs to date); state enterprise reform (20); sectoral institutional reform—for industry (11), agriculture (18), and energy (8) —and trade policy and administrative institutions (12). More general improvements in public administration are also included in eight SALs.

The first objective in institutional reform programs has been to improve key economic management instruments, particularly those regarding debt, and to assure coordination between public investment and the budget. Second, reforms have been designed to strengthen government's capacity to implement policy changes. For example, measures have been taken to strengthen government agencies responsible for overseeing state enterprises (Pakistan, Turkey, Korea), so as to buttress policy adjustments in pricing, investment or subsidies toward the public enterprise sector; and, as in the case of Senegal, to design and implement new contractual arrangements between government and parastatal enterprises. In addition, reforms in sector institutions have ranged from improvements in energy planning capacity (Turkey, Pakistan, Korea, the Philippines) and liberalized price and incentive administration in industry and agriculture (Thailand, Jamaica, Guyana, the Philippines) to major sectoral reorganization (e.g., agricultural institutions in Senegal and Turkey). In trade, institutional change has focused on the simplification of administrative procedures.

Also, SAL programs begin to deal with systemic constraints to effective public sector management in the areas of policy-making, budgetary and financial systems, and the organization and efficiency of public administration. These long-term reforms are initiated under SAL auspices, with the recognition that program development and implementation would be pursued in the context of sector and project lending. For instance, in Jamaica and Thailand, they involve the introduction of program budgeting closely linked to planning, public investment management, and public sector accounting, and important reform initiatives in civil service structure, employment and incentives.

Finally, institutional programs have tended to branch out from macro-economic management of expenditure and borrowing toward more detailed sectoral and state enterprise programs, and to a lesser extent to in-depth reforms in public sector management.

Record of success

Through the design of SALs the World Bank aims to support a program of specific policy changes and institutional reform so as to achieve a more efficient use of resources and thereby contribute to a sustainable balance of payments in the medium- and long-term, while maintaining growth. A SAL is also designed to help a country meet the transitional costs of needed structural changes in industry, energy and agriculture by augmenting the supply of freely usable foreign exchange, and by acting as a catalyst for the inflow of other external capital to help ease the balance of payments situation.

The World Bank's headquarters in Washington, D.C.

In evaluating the success of this new form of Bank lending, it should be borne in mind that different countries embarked on the adjustment path at different points in time and that their problems have varied in scope and intensity. Moreover, it is not feasible to disentangle in the short-term the impact of changes in the domestic policy framework from further changes in the external environment, or from the effects of IMF-supported adjustment programs.

An interim evaluation, based on an assessment of what agreed actions countries have taken—or have failed to take—in the context of a SAL, and on the general shift of their policies toward a more efficient use of resources, suggests that the experience has been satisfactory. Most (but not all) countries that were among the earlier SAL recipients, and have therefore already utilized the loan proceeds, have now received additional SAL loans—a sign of their success with the earlier adjustment targets. Perhaps the most widespread frustration has been delays. Adjustment is almost always painful and has frequently proved more arduous than expected. The recent global recession—the worst in postwar history—certainly did not make a difficult task any easier for developing country governments. Let us hope that the brighter economic outlook for the mid-1980s will help governments accelerate the rate of economic recovery and the process of adjustment which is needed to sustain it. ●