Pro-Poor Macroeconomic Policies Require Poverty and Social Impact Analysis

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The IMF's PRGF is supposed to provide policy flexibility based on a PSIA of the targets it imposes. In practice, PRGF programmes have failed to incorporate this objective. Increasingly, this is leading to public embarrassment for the Fund such as that which followed revelations about limits on teacher recruitment and retention in Zambia and Honduras. This article argues that the IMF continues to use a rigid economic model that fails to recognise the existence of different macroeconomic policy options. Considerable work is going on outside the IMF on developing techniques for such analysis. Unless the IMF takes more concrete steps to ensure policy flexibility and adopt PSIAs, its commitment to poverty reduction will become rapidly discredited.

1   Introduction

In September 1999, the International Monetary Fund and the World Bank endorsed a new framework for their efforts to support low-income countries. The new framework – embodied in Poverty Reduction Strategy Papers (PRSPs) – was supposed to form the basis for their concessional lending and for debt relief under the enhanced Heavily Indebted Poor Country (HIPC) Initiative. At the same time, the Fund renamed its Enhanced Structural Adjustment Facility the Poverty Reduction and Growth Facility (PRGF), reflecting the new commitment of the IMF to poverty reduction.

This article begins with a review of the main features and constraints of the Fund's monetary model on which most of its policy recommendations are based. Drawing on the work of several respected economists, it argues that the PRGF's macroeconomic framework is neither sufficiently flexible nor proactive enough to reduce poverty. In particular, it fails to utilise in its methodology the lessons learnt regarding economic exclusion. The article shows that spaces for flexibility exist in economic terms and should be maximised. It then examines the ongoing efforts in assessing the impact of macroeconomic policies and the Fund's overall refusal to carry out such assessments of its policy recommendations.

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2   Challenging the IMF model

2.1 The monetary model used by the IMF since the 1950s

The centrepiece of the IMF's macroeconomic policy framework is a model which has remained more or less unchanged since the early 1950s. The model was originally designed by Jacques J. Polak, former Head of Research at the IMF, when the Fund's core activity was to provide short-term lending to countries experiencing a balance-of-payments deficit. It is used to determine the causes of a country's deficit and the impact of corrective macroeconomic policies. Upon adoption of the Fund's policy suggestions, the IMF then provides short-term adjustment lending. According to Polak (1997: 17), '[s]ince the early 1950s, it [the model] has been the centerpiece of the analysis leading to IMF conditionality – the policy actions that a borrowing country must take to have access to IMF credit'.

The model belongs to the monetarist school of thought, whereby governments constrain their intervention in the economy in order to limit the supply of money and credit, which then limits current account deficits. Doing so is expected to subdue inflation, promote exports, and encourage savings and investment without actually directing financing into particular sectors, which is instead seen as the role of the private sector. To further depoliticise the economy and to avoid business cycles due to elections, governments are encouraged to hand final authority over interest rates to the central bank.

Structural conditions attached to IMF lending increased drastically in the 1980s and 1990s, and the model was obliged to adapt. More countries liberalised their exchange rates; there were unprecedented increases in capital flows; corporate finance became extremely complex; and the debt of low-income countries continued to soar. Though various attempts have been made to extend the model,[1] the Fund found itself increasingly concerned that new structural requisites for growth and stability could not be introduced into the model's methodology and, thus, IMF analysts began to 'base [lending] conditionality on a set of ad-hoc instruments that seemed plausible under the circumstances' (Polak, 1997: 17). Structural policy specifications such as privatisation, pensions reform, and labour-market reform – previously under the tutelage of the World Bank – entered the macroeconomic framework, effectively as heuristic crutches to lend the monetary model some realism. The reliability of this method of determining appropriate policies is said to lie in its scientific rigour, eschewing value judgments and approximating qualitative issues as much as possible for comparison. However, because the model remains ad hoc and partial, it is unable to assess the impact of policies on the poor objectively.

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1. According to Polak (1997), the core changes were: (i) the credit creation variable was split into two: credit for government (discouraged), and credit for the private sector (encouraged); (ii) an exchange-rate variable was added, in order to monitor not only the balance of payments more effectively, *but also the country's productive capacity*; (iii) sub-models were introduced to design optimal tax policies and some social expenditures such as safety nets; and (iv) growth was formally taken to mean the change in GDP and the growth in productive capacity, though the latter has traditionally been neglected.

2.2 The meaning of 'pro-poor' in 'pro-poor macroeconomic policies'

Policies which are good for the economy as a whole are not necessarily the same policies that are good for eradicating poverty; this much has been acknowledged by Eduardo Aninat (2002), the Fund's Deputy Managing Director. The PRGF's objectives of growth and stability are considered to be necessary for poverty reduction, but they are far from being sufficient. Other pre-requisites are macroeconomic policies that promote economic inclusion, empowerment and social investment. For a start, the first prism or set of assumptions in any model to be used for PSIAs must reflect the very real particularities of poverty in an economy.

The principal market feature distinguishing poor countries from industrial economies is the informal economy, which presents substantial structural challenges for poverty reduction.[2] It implies that there are informal ways for the poor to acquire the mechanisms, foresight and confidence that are required to engage productively in a market-based society. The existence of the informal economy, with its historical roots, irregularities and dependencies, suggests that, without due emphasis on pro-actively integrating the activities and realities of the poor, macroeconomic policy in support of formal markets will fail to reduce poverty. Among Southern economists and practitioners speaking at a recent EURODAD conference, this was a point of consensus (EURODAD, 2002).

PRGFs marginalise these issues, and the all too frequent reply from Fund economists to the challenge of social particularities is that they are political issues, to be left to politicians. Instead, the Fund intends to stick to its core expertise, which it considers to be 'objective' and apolitical macroeconomic policies. This is, of course, a false division. PRGF prescriptions are political; they determine, *a priori*, substantial allocative decisions, in many cases with a strong bias towards the formal market, which tends to exclude the poor.[3]

3   The macroeconomic framework

The PRGF's macroeconomic framework has two main goals: growth and stability. From these, poverty reduction is predicted to follow. In relation to these two goals, the

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2. See International Labour Organisation (2002), according to which the informal economy has grown to the point where it accounts for 80% of non-agricultural employment, and 90% of all employment created during the past ten years in Africa. The report also finds that increased regulatory flexibility for corporations has contributed to this trend.

3. Many PRGFs have attempted to facilitate some political enablement with a view to taking on board these realities. Most PRGFs endorse streamlining and rationalising public institutions, and institutional training and transparency are also promoted, particularly in new institutions for financial oversight. The approach remains highly template-driven, however, and the training provided to governments is so exogenous and 'authoritative' that it often fails to capture cultural particularities or ensure administrative continuity; see Malaluan and Guttal (2002). Decentralisation has been advanced as a solution to local particularities, but it remains largely limited to budget implementation and tax administration. Local authorities are allocated authority to implement pre-formulated budget allocations, without due representation in policy formulation; mechanisms for decentralised, bottom-up policy-making are practically non-existent, notwithstanding growing instances of local budgeting. Decentralisation can be extremely counter-productive where it is inefficient or irregular, by reinforcing local elites. For this reason, the Fund's efforts to stem corruption (chiefly by promoting transparency) are welcome.

IMF has two key targets: GDP growth and low inflation. The following paragraphs discuss firstly growth and then stability. Examples demonstrate that there is a clear debate and potential for flexibility in both areas. They even represent lessons that have thus far been ignored by the Fund.

3.1 Growth

Problems with GDP as a measurement of progress

Despite the increasing rhetoric surrounding poverty reduction, growth in GDP remains the most recognised success indicator for PRGFs. While growth is an important requirement for poverty reduction, there are a number of issues around the way growth is measured. In particular, GDP can be very misleading as an indicator of progress in poor economies.[4] Non-monetary contributions and informal market production – for example, self-sufficient agricultural systems, welfare co-operatives, and unpaid household labour such as travelling for water, activities which absorb up to 80% of economic activity in some countries – are largely underestimated or neglected in the calculation of GDP. By contrast, increases in illness, resource depletion, and state repression show up as positive contributions because they entail payment of health-care fees, corporate investment, or security expenditure. Even corporate profits that are instantly repatriated from the host country count as increases in GDP. In Georgia, the apparently impressive growth rate of 5% is made up largely of scrap metal exports as the country gradually dismantles its industrial base. With all the sophisticated accounting techniques used globally by corporations and others, the continued reliance of the IMF on such a crude measure is surprising. Various actors have developed alternative indicators that could be tools for the PRGFs' policy matrix.

The *Genuine Progress Indicator* developed by Redefining Progress,[5] for example, includes non-market transactions and subtracts for underemployment, environmental damage, and other anti-poor contributions. Research shows the GPI to have declined significantly vis-à-vis GDP since the early 1980s.[6] Other growth indicators put the household, rather than the firm, at the core of accounting; corporate investments, however profitable, are measured by the effects they have on household income, a community's labour supply and resources, and local government's tax revenues. Kakwani (2001) has also suggested the use of a poverty equivalent growth rate, intended to disaggregate growth as a policy tool for poverty eradication. These are ways to begin to internalise poverty in PRGF growth projections and responses. While there is clear evidence that measuring progress through GDP is highly inadequate for low-income countries, the IMF has yet to explore any of the alternatives in its programming, even on an experimental basis.

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4. For an overview see Cavanagh et al. (2002: Chap. 6, Section 5).
5. Redefining Progress, a US-based public policy institute working on sustainable economics, developed the GPI in 1994 to address the inadequacies of GDP as a guide for public policy (www.redefiningprogress.org).
6. See Redefining Progress (available at http://www.rprogress.org/projects/gpi/updates/gpi1999.html).

Mainstreaming monetary policy

The informal economy can significantly undermine the effectiveness of the PRGF's monetary policies to benefit the poor. If ultimately governments are to rely on the creation of domestic credit to regulate growth and stability, then clearly the estimated savings and investment rate, the interest rate, and the rate of growth of the money supply must be mainstreamed and credible. In structurally poor economies, the majority of savings, often non-monetary, are outside the banking system, many capital investments do not pass through registered companies, and values rely much less on the money supply than on immediate need. Credit creation in poor economies takes place predominantly through moneylenders in fragmented credit markets; their interest rates are not only uncompetitive but also largely un-related to the central bank's rates. This suggests that policy-makers often rely on unrepresentative data for policy formulation, which leads to implementing policies with biased effects, and finally reporting inaccurate outcomes.

Monetary policy needs to harness the productive capacity of the poor proactively; it is by far the policy area that most fails to internalise realities of poverty in the macro-framework. There is little initiative on the part of policy-makers to use the experience of micro-credit agencies, for example, to foster productive investment by the poor. These highly successful enterprises, among them the Grameen Bank and Banco Sol, have rigorously demonstrated the creditworthiness of poor rural producers – particularly women – and the financial viability of micro-credit enterprises based on group lending.

As Sobhan (2002: 7) argues, 'there is, today, no reason why such organisations, of the maturity of the Grameen Bank, should not graduate into the macro-finance system by accessing the deposits of the public and even marketing their assets at the global level, through such financial instruments as securitisation, which are in widespread use in more advanced financial systems'. New monetary policy instruments that link the financial activities of the poor to the corporate sector could be used not only to ameliorate credit rates, but also to increase and mainstream the savings rate of the poor. The Grameen Bank has created a mutual fund which invests a small fraction of its $187 million worth of savings in the corporate sector; if facilitated by monetary and financial policies, this type of initiative could, according to Sobhan (2002: 8), 'move the poor out of the village economy and into the more dynamic corporate sector, to a stage where a significant share of corporate wealth could be owned by the poor. The savings of the poor can not only augment the savings base but also broaden the investment capacity of the economy, while transforming the poorest rural household into stakeholders in the process of national economic growth.'

Common credit-market failures such as adverse selection and uncompetitive interest rates can be mitigated by peer-group lending (see Armendariz de Aghion and Collier, 1996), a common feature of micro-credit, which is one reason why monetary policy should facilitate commercial participation in this sector. Even IMF-promoted research has shown that measured state intervention, for example to promote rural branch expansion by corporate banks, can have high benefits for the poor (see Burgess and Pande, 2002). If credit creation is going to be a government's principal tool for encouraging growth, then finding new ways to include the poor in the credit market is a paramount task for the PRGF. Despite the clear opportunities for broad, meaningful poverty impact of monetary policy, none of the PRGF programmes surveyed by

EURODAD made any attempt to address this issue, while a number included structural conditions involving privatising state banks, which is likely to lead to a reduction in credit available to the poor.

Mainstreaming gender

Gender patterns – such as differential incomes, consumption preferences, and intensities of labour in the unpaid versus paid economies – are well-known brakes on economic growth. Beyond growth, they are also integral to any attempt to tackle poverty; the majority of the world's poor are women. Yet there are no analytical or policy provisions in PRGFs to integrate a gendered analysis. The key lesson from gendered economic analysis is that neo-classical assumptions about the adjustment costs implicated in market transition (measured by changes in consumption) have an inherent male bias (see Elson, 1995). In part, this is because in reality households are not equitable or unitary. Women are typically responsible for their families' domestic needs (for example, food, water, attendance at health clinics etc.), and the share of household income they receive from males in the household is not responsive to market price fluctuations. Gendered responsibilities have meant, for example, that public service user fees often represent *de facto* fiscal transfers to the public purse from women, who have to pay for them, despite being already among the poorest actors in poor countries. Declines in the real income of women leave households worse-off, particularly in terms of forgone education and health, even if they are matched by increases in male income.

Trade-related macroeconomic policies have also had a potentially negative effect on gender equity and poverty reduction at the household level; shifts to cash-crop agriculture, promotion of the textile industry, and currency devaluation to promote exports, often had overall disproportionate costs for women.[7] In the majority of cases, women have been forced to increase their labour in the paid economy – particularly agriculture – without decreasing their work in the unpaid economy. And wage differentials between men and women *within* the paid economy – not touched on by the type of labour-market de-regulation in the PRGF – are inefficient, particularly in sectors such as textiles where women make up the majority of the labour force. Designing compensatory measures is not at all straightforward, which is why it requires a consultative approach. Certainly the macro-adjustment frameworks promoted by the IMF cannot be genuinely pro-poor unless they consider gender issues.

3.2 Stability

According to Polak (1997), controlling inflation has become the main priority of the Fund's macroeconomic recommendations, even more than maintaining a stable balance of payments. High inflation undoubtedly hurts the poor, but there remains a great deal of debate as to how high inflation may go before it becomes anti-poor or stunts growth in poor countries. Arguably, Fund-supported programmes maintain a reliance on inflation control, which is less appropriate in poor economies than it might be in wealthy ones. A recent IMF staff paper by Khan and Senhadji (2000: 1) concluded that 'the threshold level of inflation above which inflation significantly slows growth is

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7. See various reports of the 'International Gender and Trade Network' (available at http://www. genderandtrade.org).

estimated at 1-3% for industrial countries and 11-12% for developing countries'. Furthermore, as Gunter (2002: 28) has pointed out, a number of studies have also challenged how Fund programmes attempt to stabilise inflation: by neglecting local business cycles, and acting too aggressively and with inappropriate instruments.

Most PRGFs have an inflation target under 5%, precluding fiscal and monetary policies that might promote the type of 'real' stability that poor people require – job security and physical well-being. In Bolivia, Mali and Tanzania, for example, where inflation remains well under control (under 5%), governments have been allowed little or no flexibility to promote employment, initiate local growth strategies, or increase social spending where they see fit. It is by no means clear – and it is beholden on the Fund to clarify this – that individual low-income countries with single-digit inflation could not easily sacrifice some inflation points for additional public investment. This flexibility – properly administered under consultation with all stakeholders – could induce the stability required, whilst enabling domestic investment and productive capacity development by the poor.

The Fund also needs to demonstrate explicitly how inflation is measured in PRGF-supported programmes. This issue is vital in order to analyse the correct place of inflation control on a list of priorities for poverty reduction. Do the goods and services tracked by inflation indices reflect consumption and production patterns of the poor? Much as GDP aggregates all values regardless of whether they benefit or hurt the poor, so inflation indices are biased where demand is sufficiently weak for the products tracked to make their price levels statistically insignificant for poverty reduction. Given the emphasis put on inflation control, analysts need to consider how accurately formal (particularly urban) market prices portray production and consumption rates and their impact on poverty.

3.3 Policy options and impact analysis

As Sobhan (2002: 2) describes, a genuine pro-poor macroeconomic framework 'serve[s] to transform the poor from being the incidental beneficiaries of economic growth to becoming one of its prime movers'. Thus far, macroeconomic frameworks have sought to sustain poor people at the margin, through fiscal social-sector policies that constitute *de facto* 'relief' programmes. Instead, the macroeconomic framework of a PRGF must have the social and political realities of poverty at its core and equitably mainstream poor people's economic activities; designing safety nets is not enough. The above section gives just a few examples of the scope there is for debate on the key fundamentals of stability and growth, and some of the changes required if the reality of poverty is to be systematically integrated.

Ultimately the social challenges to macroeconomics are not resolved only through flexibility to determine ceilings on fiscal expenditure. Policy flexibility must enable governments to consider the economic particularities of the country concerned, and the proper means to create markets in that context. One clear way to begin to address these issues is for the IMF to ensure that there is a clear assessment of the poverty and social impact of all major macro-adjustments.

4   PSIA of macroeconomic frameworks

A lot of work is going on around the world looking at the impacts on poor women and men of different macroeconomic policies and what this means in terms of optimal policy design. A number of different actors are involved and different methods are being employed. Concerns and criticisms increase, and progress particularly needs to be made on beginning to agree on standards, methodologies and tools. However, substantial progress is being achieved. Despite playing the pivotal role in designing macroeconomic policies in low-income countries, the IMF has had little involvement in this work to date. This is unacceptable from the point of view of the Fund's goal to reduce poverty. While there are constraints, it is obvious that the Fund can do much more to participate actively in the development of macroeconomic PSIAs and their systematic implementation in its programmes, particularly as this is one of the key features of PRGF-supported programmes.

This section begins by outlining what could be done immediately as basic first steps, and then goes on to describe some of the initiatives being carried out globally and their success in modelling the impact of macro policies. It then looks at some of the criticisms and continuing problems, though it concludes that the Fund should play a leadership role in working to address these problems and build on progress to date. There is no reason why PSIAs of macroeconomic options should not be systematically a part of all PRGF-supported programmes.

4.1 What is a PSIA?

A recent IMF paper, Inchauste (2002), states that the IMF gives two definitions of what it considers a PSIA to be. The first definition is broad, describing a PSIA as any reference to the social consequences of policies. The second definition is more specific, defining a PSIA as instances where analysis is supported by rigorous analytical studies. The study found that even when a PSIA was defined as a simple reference to social impacts, PSIAs were undertaken for less than half of all reforms that had potentially negative social effects. When the definition was tightened to cover only rigorous analytical studies, it found that, although macroeconomic reforms were undertaken in 94% of all PRGFs, none of the documents presented a rigorous study analysing the impact of these reforms. In addition, although privatisation was a structural reform in 83% of programmes, only 14% of documents contained some form of PSIA. This lack of PSIAs is further supported by a recent EURODAD (2003) analysis, which found that, of the 11 PRGFs analysed in March 2003, only one, Malawi, made reference to a PSIA and this was simply in the form of a one-page box where the IMF outlined its rationale for the reforms in the programme.

According to Lawson (2003), civil society organisations stress the importance of *ex-ante* PSIA, hence, an analysis that is carried out in advance of a reform, that looks at alternative policy options, and is based on broad country ownership of the analysis.[8] The

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8. This focus on options and ownership echoes two of the other key features of the PRGF, the need to provide 'appropriate flexibility with fiscal targets' and 'broad participation and greater ownership'. It shows how the three key features are clearly linked, and as the other EURODAD papers in this section have shown, there has also been little progress on either of these two key features.

IMF apparently shares this view, as Inchauste (2002: 6) writes that PSIAs should enable 'countries to weigh trade-offs of reforms and to take ownership of the policies to be implemented'. On these criteria it is evident that no PRGF has yet carried out anything that could be described as a PSIA of either macroeconomic or structural reforms. The move towards any discussion of the social consequences of a programme by the IMF is welcome, and represents a significant departure from the previous ESAF arrangements. However, we remain a long way from the full integration of country-owned PSIAs for all macroeconomic frameworks and key structural reforms.[9]

4.2 Macroeconomic PSIAs – feasible first steps

A basic first step towards macroeconomic PSIAs should be a clear discussion of the rationale behind a proposed quantitative macroeconomic framework. Assumptions underlying a programme can then be clearly outlined and discussed. For example, in the run-up to the agreement of a new Fund programme, or as part of an annual review, a series of debates should be held with a broad range of stakeholders prior to its agreement. At these debates the IMF should outline why it feels the quantitative framework proposed is the ideal one for optimising progress towards PRSP goals and/or the Millennium Development Goals for the country concerned. It should also outline what other scenarios or approaches were considered and why they were rejected. Feedback and input should be taken from stakeholders. If the Fund is convinced of a certain set of targets, it is beholden to win this argument in the public domain, and particularly if it wants to increase the political will towards actually achieving its targets. For example, IMF macroeconomic targets on the total public sector wage bill have led to ceilings on recruitment of teachers in Zambia and in Honduras, hugely emotive and political issues, particularly in the context of both countries' commitment to reaching the MDG of primary education for all. Yet in both cases the IMF failed to win support for these targets or carry out any analysis of their impact.

These debates over options often go on behind the scenes to some extent anyway, and in many ways this would be more an exercise in greater transparency and openness than a fundamental change in ways of working. Some recent PRGF documents have made small attempts to address this with one-page sections in final staff reports entitled 'PSIA', which are a welcome if cursory step in the right direction.[10] However, as they are available only after the programme has been agreed, they do little to increase ownership or options. In advance of an agreement, missions increasingly do meet with different stakeholders, but there is rarely a clear specification of what the new programme targets are likely to be and why. However, at the same time the IMF is pressurising governments to open up their budget formulation to public debate. As such, a few simple first steps to outline the programme and its assumptions would be easy to take, and would make a substantial difference.

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9. Since this article was first written the IMF has bowed to considerable pressure and set up a small 4-member unit to work on PSIA in July 2004, by contracting out and also carrying out its own studies. This first step has been broadly welcomed, and civil society is keen to see, via this unit, a rapid scaling up of country-owned macroeconomic PSIAs over the next year.
10. For example, see the IMF Staff Reports for Gambia, Mali, Senegal and Malawi (available on the IMF website).

4.3 Macroeconomic PSIAs – considerable ongoing initiatives globally

There are a number of different actors globally looking at the impact on the poor of different macroeconomic frameworks. These are both qualitative and quantitative approaches, and seek to include a broader range of poverty-related factors in the analysis.

Qualitative approaches

Qualitative data have received much greater acceptance in recent years, and as an important alternative and complementary source of information on poverty and the impacts of policies on the poor. They give greater depth and understanding of impacts and poverty dynamics, and can be particularly good in uncovering the second-round impacts of policy reforms. They are inherently contextual in that they seek to embed an analysis of policy within its broader social, economic and cultural context (Booth et al., 1998).

On the qualitative side, three initiatives/examples are of particular note. The first was the Structural Adjustment Participatory Review Initiative (SAPRI). This was a joint World Bank/civil society initiative in 1997 that involved a global network of 250 organisations reviewing the impact of adjustment lending in seven countries. It looked at a broad range of economic and structural issues including privatisation, trade liberalisation and social expenditure, and found, for example, that declining public expenditure on social services under structural adjustment had a negative effect on the poor, in particular women (SAPRIN, 2002).

The second major qualitative multi-country study was the World Bank's *Voices of the Poor* study, which was carried out in 23 countries during 1999. It sought to use participatory and qualitative methods to analyse the perceptions of the poor themselves regarding their poverty and its solutions, and was designed to contribute to the *World Development Report 2000/2001: Attacking Poverty*. Again looking at it retrospectively, it nevertheless covered the impact of the considerable economic reforms experienced globally in all low-income countries during the 1980s and '90s. Overall it found that the majority feel that they are worse-off and more insecure than in the past (see Narayan et al., 2000).

The third important qualitative initiative is the Uganda Participatory Poverty Assessment. Although participatory poverty assessments have been carried out in a large number of countries, the Ugandan example is noteworthy because of its scale and the degree to which it was incorporated in the government's programme and in the policy-making system. Originally, the first round was focused mainly on developing a clearer understanding of poverty dynamics, but this inevitably had macro-policy implications. For example, in the first round, the negative impact of the tax on bicycle parts was highlighted and this led to its removal. Equally, the tremendous success of the removal of health user fees is clearly demonstrated in the results of the second round of assessments.

Quantitative techniques

On the quantitative side, initiatives range from simple surveys looking at who benefits from a reform to more complex economic models. Economic models fit together a series of variables and seek to simulate the impact of policy changes. They can be either partial and involve only a set number of variables, or more ambitious and attempt to model a whole economy.

Within the World Bank, there has been a lot of work in recent years on developing analysis and economic models from different sections of the Bank and varying in their complexity. One example is the 123PRSP model. For a given set of macroeconomic policies, the 123PRSP model generates a set of wages, sector-specific profits and relative prices that are mutually consistent. The link with poverty analysis is constructed when the model's projected changes in prices, wages and profits are plugged into the available household data on wages, profits and commodity demands for different groups. According to Bourguignon and Pereira da Silva (2003: 19), the 123PRSP framework is probably the simplest CGE model of a complete economy that allows 'for a forecast of welfare measures and poverty outcomes consistent with a set of macroeconomic policies and their effect on key macroeconomic variables such as the real exchange rate or the sectoral allocation of employment'.

Outside the World Bank, there are a number of other initiatives looking at quantitative modelling. One good example is the Micro Impacts of Macroeconomic and Adjustment Policies (MIMAP). This programme seeks to assist developing countries in building up the ability to analyse poverty and the impacts of policy on it. It has built up a network of developing country researchers, policy officials, NGOs and international experts, and includes more than 40 research teams from Asia, Africa and Canada.[11]

There are also a small but increasing number of initiatives being developed to model quantitatively the impact of policy in low-income countries. One of particular note is the Distributive Effects of Economic Policy (DEEP) model developed by the Integrated Social Development Centre (ISODEC), a Ghanaian NGO. This model consists of three different modules that respectively track macroeconomic dynamics, the effects of pro-poor government spending, and detailed effects on income distribution.

4.4 Introducing increased realism and complexity using PSIA

As these different techniques and approaches are developed, the analysis of macro-policy impact is gaining more depth and becoming increasingly nuanced to include a number of variables crucial to a poverty focus. The IMF has started to use simple models to assess the impact of HIV/AIDS on growth predictions in Zambia, a variable that is integral to any successful poverty reduction strategy. Similarly in other countries in the past the World Bank has estimated the cost of corruption in terms of lost GDP.

On the side of civil society, one particularly interesting initiative has been taken by the Economic Development Research Centre (EDRC) (2002), an Armenian NGO made up of young economists. Concern about dramatically increasing inequality in their country and its negative impact on growth and development led them to develop an alternative model that focuses not just on growth but also on equity. It uses data about

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11. For further information, see the MIMAP website (http://www.mimap.org/).

the Gini co-efficient to model the impact of different growth rates and composition on achieving greater equity, and sets targets for equity as well as growth. This stands in stark contrast to the IMF's PRGF programming; of the eleven PRGFs reviewed by EURODAD, only one, Nicaragua, made any reference to equity.

Another area of particular interest within PSIAs is to analyse the impact of macroeconomic policies on gender, and particularly the impact of different growth strategies as described in the previous section. The impact of policy on gender is increasingly being modelled quantitatively as well as being a key part of participatory work. Analysis has shown that macro-modelling undertaken without considering gender is seriously flawed (see, for example, Catagay, 1998). At the same time others have begun trying to factor in longer-term environmental concerns and their impact on growth and poverty reduction in the medium term (for example the impact of electricity privatisation on fuel wood consumption).[12]

One final area that remains very poorly considered in macroeconomic policy development is the role of global trends and their impact on policy. A clear example of this is the push for large numbers of low-income countries to specialise in one commodity, which leads to price collapse.[13] Another is the pressure from the IMF for countries to liberalise their trade barriers, despite the continuing massive protectionism in developed countries, meaning that this is unlikely to benefit them. It is beholden on the IMF to consider the impact of its advice to poor countries on the external market as a whole, and at the same time to consider the impact of that same economic reality on the policies it prescribes.

4.5 Macroeconomic PSIAs: criticisms and space for improvement

The above section gives only a small flavour of the work being done on macro PSIAs, and a lot more is going on elsewhere. In addition, however, there are also continuing criticisms of what is being done, while at the same time major gaps remain. In terms of criticisms, both quantitative and qualitative techniques used to predict the impact of policies are questioned. Qualitative techniques are identified as intriguing and interesting, but they remain by design highly contextual, and as such any comparison between results or extrapolation beyond context is spurious in many ways. At the same time, quantitative models are only as good as the data and the assumptions on which they are based. Full data sets required for elaborate economic models are lacking or extremely unreliable in most low-income countries, although in recent years this has begun to improve. At the same time, assumptions underlying models can radically alter conclusions. To illustrate this, a recent study showed that when a structuralist and a neoclassical model were both applied in South Africa, the neoclassical model fully supported a set of 'Washington Consensus' policies, while the other recommended a far more heterodox set (Gibson and Van Seventer, 2000).

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12. See, for example, the website of the Macro Economics for Sustainable Development Office of the World Wildlife Fund (http://www.panda.org/resources/programmes/mpo/).
13. One good example of this is coffee, where prices have collapsed in recent years.

4.6 Macro-PSIAs: next steps and the role of the IMF

There are indeed legitimate criticisms to be made, and a lot more work needs to be done. Of utmost importance is the need to develop a broad set of agreed standards; development economists globally need to agree on some standards for the development of quantitative tools, for example. This will require leadership, and as one key analysis concludes, 'a concerted international effort by all interested parties is critical' (Gunter, 2002). The IMF could and should play a key role in facilitating this process.

The second important point is not to believe that full agreement will ever be possible; people have different assumptions, in many cases because they have different ideological perspectives, and these are often not based extensively on evidence. This is not to say that evidence-based macroeconomic policies are impossible, or that we should not aim towards these at all times. It is simply to point out that, even before agreement is reached, macro PSIAs based on ownership and options have a key role to play.

5   Conclusion

Despite a new agenda of 'pro-poor growth' making headway, the macroeconomic policies set out in PRGF-supported programmes and PRSPs remain very tenuously linked to the realities of poverty. For decades, the IMF has relied on a highly uniform model in macroeconomic policy design for low-income countires, which does not accommodate the diversity of local economic conditions and poverty incidence, nor adequately forecast the poverty impact of policy recommendations. Two key normative features of the PRGF are policy flexibility and 'social impact analysis of major macro-adjustments and structural reforms'.[14] The methodology and indicators used in the PRGF, however, preclude a large share of policy options, particularly those which emphasise the pro-active integration of informal production by the poor. Similarly, while there have been repeated commitments to increase efforts to carry out PSIAs since the inception of the PRGF in 1999,[15] it is clear that PSIAs remain the exception.

It is evident that, despite some limited progress, the IMF is essentially failing to deliver on both policy flexibility and PSIAs. There are two main reasons for this lack of progress, both stemming from minimal change in the organisational approach and mindset of the institution, despite considerable changes in rhetoric. One reason lies in the continuing perception of many staff that there is only one appropriate set of macroeconomic policies for low-income countries and one set of structural reforms that can support this macroeconomic framework. This set of policies is seen as a technical and objective given, rather than one among a number of policy options within the overall aim of broad macroeconomic stability for poverty reduction. Given this

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14. The relevant key features are (i) increased flexibility in fiscal targeting, (ii) social impact analysis of major macro-adjustment and structural reforms, and (iii) greater country ownership. In relation to ownership, the Fund asserts that 'Governments must be given more space to determine the timing and content of policies, in accordance with their priorities and assessment of what is feasible' (see IMF, 2000).

15. See, for example, IMF (2002), which highlighted the need to be 'using Poverty and Social Impact Analysis more systematically, and building country capacity in this area'.

continuing perception, it is not very surprising that flexibility and the analysis of different options have not been particularly forthcoming.

The second reason arguably stems from the belief in the IMF that poverty reduction is not its area of expertise. This belief is a legitimate one in many ways, as the majority of Fund staff are macroeconomists[16] with minimal understanding of structural poverty dynamics. This has meant that the stock response of IMF staff to questions on PSIA is that it is the responsibility of the World Bank.[17] In addition, many in the IMF also concur with the Bank's view that PSIA of macroeconomic frameworks is particularly difficult to do, and that there is minimal expertise or agreement on how this can be undertaken.

While this is true, there is already a great deal of learning which has yet to be implemented, and embedding PSIA in the PRGF is a means of reconciling the current constraints by, first, informing the debate on the appropriateness of different policy options and, secondly, generating benchmarks with which to measure the ability of PRGF programmes to make a difference in poverty reduction. Instead of having only one set of policies that are deemed to be appropriate in any one situation, there is in fact considerable debate over what constitutes the appropriate mix of macroeconomic policies, particularly in relation to core features of lower-income country economies such as economic exclusion, which PRGF largely neglects. This is the case even for countries with considerable macro-instability and certainly for those low-income countries now characterised as being in many ways 'post-stabilisation'.[18]

Although much work still needs to be done on PSIA of macroeconomic reforms, there is already a lot of positive learning on modelling poverty impacts. The IMF could do much more to take a lead in this work and implement existing learning, given its pivotal role in the macro-frameworks of all low-income countries. It is hoped that the establishment of a 4-person PSIA unit in the Fund will be a first small step in this direction. If the IMF is truly committed to poverty reduction and the Millennium Development Goals, it could ensure that PSIAs of all major macro-adjustments are systematically carried out in all its programmes, and that this analysis is built on broad ownership and debate about a number of different policy options. Unless the IMF takes clear steps to ensure this policy flexibility and the carrying out of PSIAs, the much hailed poverty commitment of the IMF to poverty reduction and the Millennium Development Goals will become largely discredited.

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16. The IMF employs only two social development advisers for all its programmes.
17. Indeed, this was the response of the IMF Managing Director to questions on PSIA raised when he gave evidence to the UK House of Commons Treasury Select Committee on 4 July 2002.
18. For a characterisation of 'post-stabilisation' see Adam and Bevan (2001). Essentially these are countries that have achieved a stable balance of payments and single-digit inflation, have expenditure under control and have built up foreign reserves.

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