Human Development, Adjustment And Growth

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PREFACE

"Adjustment without growth and human development is unacceptable and counterproductive. It is possible, indeed mandatory, for national and international policy makers to design such policy packages as to make adjustment policies compatible with growth and human development."

This was the central message of the second session of the Roundtable on Human Development held in Salzburg on September 7-9, 1986. The Roundtable brought together about forty prominent development experts from academic and international institutions and high-level policy makers from national and international organizations for candid discussions on the impact of economic recession and adjustment on human development.

In the autumn of 1985, just prior to the annual joint World Bank-IMF meeting in Seoul, where U.S. Treasury Secretary James A. Baker proposed his now-famous plan to ensure some financial inflows into some of the debtor countries in order to avoid a collapse of the world financial system, North South Roundtable members met in Istanbul to discuss the human impact of the economic pressures of the 1980s on the developing countries. The main objective of the Istanbul Roundtable was to reassert the central importance of human well-being as the objective of all development efforts and to appeal to policy makers to redirect policy and planning toward human development, even when their budgets come under heavy pressures due to an unfavorable external environment. The volume Human Development: The Neglected Dimension, a record of the Istanbul Roundtable, immediately became an important addition to the professional thinking on the importance of human resource building in the development process.

The current volume, Human Development, Adjustment and Growth, is a product of the Salzburg Roundtable, which was organized by the North South Roundtable in collaboration with the UNDP Development Study Programme. The Salzburg Roundtable explored how different approaches can ensure adequate human development, especially among the most vulnerable groups, during adjustment periods without jeopardizing the growth process. Approaches at two levels were considered: first, in the design of macro adjustment and growth policies, and second, in sectoral and micro interventions.

The volume has been divided into four parts. Part I gives an overview of the discussions that took place in the Istanbul Roundtable and of the directions that the current deliberations should take in order to come up with some concrete policy proposals. The achievement of adjustment with growth and human development offers an intellectual and policy challenge in designing programs and policies which can combine adjustment measures with protecting levels of growth, employment and other social development sectors. To the intellectual community, the challenge is to do the analytical work in order to achieve a synthesis between adjustment with growth and human development; to national policy makers, it is to rationalize and prioritize their policies in order to protect the social sectors; and to the international institutions, it is to be sensitive and responsive to the economic and political realities of the I980s.

The chapters in Part II examine the range of macro economic policies that are used to correct payments imbalances. Starting from an analysis of conventional adjustment measures, the discussion goes on to suggest alternative policy proposals which could protect vulnerable groups. Mobilization of the rural population, mediumterm strategies and a greater emphasis on social sector policies are among the components for designing macro policies that combine adjustment with growth and human development.

Part III contains chapters dealing with sectoral policy issues associated with stabilization programs. The impacts of contractionary stabilization policies on social sectors such as health, education and employment are well researched and have been presented frankly by the authors in this volume. The authors analyze how education is being negatively affected by the realities of economic recession, how the worldwide employment situation has deteriorated, and how health budgets are being cut. One compelling chapter in this part deals with the impact of dietary deficiency on productivity. This paper, which is the result of an ongoing research project, warns that if nutrition is compromised by thee adjustment process, then this process is self-defeating and self-perpetuating.

Part IV presents experiences of a few developing countries in dealing with the above issues, The country papers clearly point out what has been happening in country after country following the years of economic adjustment and recession. Human development has been stalled over the last five to ten years in many of these countries. In Africa, there has been negative per capita growth in about two-thirds of the countries, and this is expected to continue for the rest of this decade. With the continuing deterioration of the international environment, per capita expenditures on health and education have fallen, real wages have deteriorated and malnutrition has risen. In Latin America, although economic conditions are better than in Africa, the collapse in oil prices, falling commodity prices and volatile interest rates diminished the conditions for growth, which needs foreign exchange and investment. It is clearly impossible to generate foreign exchange and savings when these countries are required to transfer these resources to banks in developed countries in order to service their debts.

What African countries need now is special financial support, such as IDA funds and conversion of their public debts into grants. Other countries in Latin America and Asia need more time for adjustment measures to bear fruit, more flexibility on the part of the international financial institutions in negotiations, and more resources from both public and private sources. Above all, both national governments and intemationalorganizations must pay extra attention to the protection of the human dimension in all their policy measures. The Salzburg Statement, appended to this volume, gives the policy recommendations of the Salzburg Roundtable.

We offer our grateful thanks to the government of Austria and the provincial government of Salzburg for the very gracious hospitality provided to the Roundtable. We thank all the participants for their valuable contributions to the meeting and to this volume. Our heartfelt thanks go to our two co-chairmen, Mr. Bradford Morse and Dr. Mahbub ul Haq, for providing their continuing leadership and direction to this Roundtable. The chairman of the North South Roundtable, Mr. Maurice F. Strong, deserves special thanks for always guiding and encouraging us to devote our best to the cause we all believe in.

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Khadija Haq
March 18, 1987 **Uner Kirdar**

PART I
AN OVERVIEW

CHAPTER 1

On the Nature of Ad justmen t Policies and Human Development

Louis Emmerij

Much has been said about adjustment, growth and human development. Of the three, it is adjustment and adjustment policies that have become the most controversial concept in recent times. But human resources, human capital and human development are all concepts that, although containing less apparent controversy, are not without ambivalence.

It may be useful, therefore, to attempt to unravel some of the obscurities and ambivalence surrounding the concept of adjustment and adjustment policies on the one hand, and of human resources and human development on the other.

On the Nature of Adjustment Policies

It's probably true to say that what one has come to call adjustment policies are the spillover into developing countries of the current financial and economic orthodoxy in OECD countries. This orthodoxy is distinctive in that it concentrates on increasing the efficiency of market signals as a guide to an improved allocation of resources. In practice, such a strategy is often introduced during a period of crisis, when economic stabilization and the adjustment of imbalances are of high priority. Consequently, measures to improve relative prices are usually accompanied by measures to control the rate of increase in the general level of prices. Emphasis is then placed on monetary and fiscal policies and on financial reforms.

Adjustment policies as defined in this more monetarist sense are not concerned only with short-run readjustment and restoration of the macroeeonomic balance, after which longer-tern policies can be resumed. The current orthodoxy is deeply concerned with microeconomic issues, with removing distortions and getting the right set of relative prices that will permit efficient long-run growth. In the developing countries, a major element of such a strategy is to allow the urban-based private business sector greater freedom. This sector then becomes the focus of development and takes on the role of the dynamic sector responsible for generating backward and forward linkages with the rest of the economy. The role of the state is minimal, being confined to providing an undisturbed, stable economic environment in which the private sector can flourish. That is, by using stabilization policy, the state attempts to reduce fluctuations of the economy to a minimum, thereby helping the private sector to make reliable forecasts. Policies to denationalize state-owned enterprises (to avoid a crowding out of the private sector) and legislation to reduce trade union power are also part of such a strategy. In the extreme case, this strategy approaches one of laissez faire.

The objectives of the adjustment policies are first, to stabilize the economy; second, to improve the allocation of resources, and thereby raise the level of output and income; and third, to achieve higher levels of savings and a more efficient use of capital in order to raise the rate of production growth. The policy is noninterventionist in spirit; in particular, measures to alter the market-determined distribution of income are opposed on the grounds that such interventions inevitably introduce distortions and inefficiency, which ultimately harm the poor.

This means that these policies are almost opposite to those designed to tackle the problem of poverty head-on by emphasizing the importance of creating more productive employment for the working poor; by giving top priority to satisfying the basic needs for food, clothing and shelter; by redirecting public expenditure in favor of human capital formation, notably toward elementary and secondary education, primary health care and nutrition programs; by decentralizing public administration and more fully exploiting opportunities for local resource mobilization; by promoting greater participation by the poor in the institutions that affect their wellbeing; and, in some cases, by redistributing productive assets, notably land.

Small wonder, therefore, that adjustment policies as just defined have been attacked as being short-term policies with negative longerterm implications. An earlier roundtable that resulted in the publication Human Development: The Neglected Dimension emphasized that theme. For example, the preface states:

The attention of national and international policymakers has shifted from long-term goals to short-term financial and adjustment concerns. The international community is more interested in ensuring the timely payment of debts and interest rates than in seeking to eradicate poverty and in strengthening the human dimension of development. Thus, anti-poverty and human development programs have been pushed aside. Poverty can wait, the banks cannot!'

A number of articles in the same volume, particularly those by Frances Stewart and Richard Jolly, stress the extreme nature of such policies. Jolly mentions that historians will view the first half of the I980s with awe because of the extreme rise of ideology and the fall in nutrition levels. He makes a forceful plea that the human consequences of adjustment policies must not be left as a by-product, but treated as an essential concern. "Neglecting human resources is an economic error of the most fundamental sort," he asserts.

It is often said that adjustment policies, with their heavy emphasis on the decreasing role of the state and on the consequent decreases in public expenditure, hit such items as education and health disproportionately hard. If it is true that the current financial and economic orthodoxy in the OECD countries is at the very base of the adjustment policies that are now more and more the rule in developing countries, we should be able to discover analogous patterns in terms of expenditures on education and health in both the OECD and the developing countries. Table I presents absolute figures in constant 1980 U.S, dollars for total public expenditure and outlays on education, health and public investments for all OECD countries taken together between 1975 and 1984. We note that total public expenditure has continued to increase, albeit much less quickly between 1980-84 as compared to the period 1975-80. However, when it comes to public expenditure on education, we note that after a continuous increase until 1980, it declined relatively rapidly after that, reaching a low point of less than $90 billion in 1984, as compared to $136 billion in 1980. The situation is less extreme for health expenditure. Here, also, 1980 is the turning point, when public outlays on health reached $265 billion. After that, a decline set in, but much more steadily and slowly than for education, with expenditure reaching $250 billion in 1984. It looks as if the medical lobby is much more forceful in OECD countries than the educational lobby! At any rate, for the OECD countries, the hypothesis is true that the education and health sectors have been hit hard by the current financial and economic orthodoxy.

TABLE 1

OECD Countries, 1975-

	Total Public	Education	Health	Public Investment
1975	1,708,280	117,380	213,070	52,820
1980	2,216,700	136,650	264,080	52,250
1981	2,260,900	131,950	262,660	53,400
1982	2,340,200	120,427	272,340	49,810
1983	2,402,90	95,216	258,160	40,685
1984	2,506,665	89,703	250,370	33,520

SOURCE: OECD Development Centre, Paris.

But the question must be asked whether only the so-called "soft sectors" have been hurt. That is why table 1 also shows a column on public investment. These are investments not in human but in physical resources. The table makes it abundantly clear that public investments did not increase between 1975 and 1980, contrary to education and health expenditures, but stagnated. Since then, they have also decreased rapidly, as much in relative terms as expenditure on education and much more than expenditure on health.

Table 2 gives the relative figures for the same items. It presents public expenditure as a percentage of GDP. We note that public expenditure continued to increase from 26 to 30 per cent of GDP. As a percentage of total public expenditure, expenditure on education fell from close to 7 per cent in 1975 to 3.6 per cent in 1984. So already, between 1975 and 1980, a relative decline set in, in spite of an increase in the absolute figures. The same is true for health expenditure, which peaked in 1975 at 12.5 per cent of total public expenditure and fell gradually to 10 per cent in 1984. Public investment as a percentage of total public expenditure declined from over 3 per cent in 1975 to 1.3 per cent in 1984.

Table 3 presents relative figures for the same sectors, namely, education, health and public investment, for four selected developing countries - Brazil, Mexico, Venezuela and South Korea - covering the same period, 1975-84. The three Latin American countries show a similar trend in expenditure on education as the GELD countries: strong declines for Brazil and Mexico and less of a decline, but a decline nevertheless, for Venezuela. The exception is South Korea, which continued to increase its educational expenditure as a percentage of total public expenditure from 14 percent in 1975 to more than 20 per cent in 1983, when a decline set in and the figure fell to 19 percent in 1984. This is yet another confirmation of the fact that development achievements have been very different during the I980s in Asia and in Latin America.

TABLE 2

Public Expenditure, Education, Health and Public Investment in

OECD Countries, 1975-84

(Percentage)

	Public Expenditure as % of GDP	Education as % of Public Expenditure	Health as % of Public Expenditure	Public Investmint as % of Public Expenditure
1975	26.2	6.9	12.5	3.1
1980	28.8	6.2	11.9	2.4
1981	29.0	5.8	11.6	2.4
1982	30.0	5.1	11.6	2.1
1983	30.1	4.0	10.7	2.0
1984	30.0	3.6	10.0	1.3

Source: OECD Development Centre, Paris.

Turning now to public expenditure on health, a similar but more subtle picture emerges as for the OECD countries. Health expenditure has not declined, or has declined less than educational expenditure. This is true for Brazil and for Venezuela, but not for Mexico, where the decline has been very significant indeed. South Korea, once again; was an exception until 1983, when the decline also occurred there.

The evolution of public investment in these countries is similar to the OECD trend: a heavy decline in Brazil, Mexico and Venezuela, and much less of a decrease in South Korea, although this time the turning point is 1982.

TABLE 3

Public Expenditure on Education, Health and Investment as Percentage of Total Public Expenditure in Selected Developing Countries, 1975-84

Educational Expenditure

	1975	1980	1981	1982	1983	1984
Brazil	7.1	3.4	3.8	4.2	3.7	...
Mexico	17.9	18.0	18.2	13.1	11.0	...
Venezuela	16.5	20.1	16.2	15.7	15.1	15.7
South Korea	14.1	17.1	17.9	19.5	20.5	19.0

Health Expenditure

Brazil	6.5	6.5	7.4	7.8	7.3	...
Mexico	4.3	2.4	1.9	1.3	1.2	...

Venezuela	9.1	8.8	7.6	7.6	8.0	7.6
South Korea	1.0	1.2	1.3	1.4	1.6	1.4
	Public Investment					
Brazil	10.9	5.5	6.9	6.7	2.6	...

SOURCE: OECD Development Centre, Paris.

The overall conclusion must be :

a) OECD policies since the end of the 1970s have had the same effects in industrialized countries, relatively speaking, as the adjustment policies in many developing countries, particularly in Latin America.

b) However, this impact is more subtle than is often made out.

c) It is heavy on education.

d) It is less important for health.

e) It is significant on public investment.

f) It follows that not only the so-called "soft sectors," important for human resource development, have been hit, but also the hard sectors, where physical investments are important.

In this case, therefore, the OECD countries are practicing at home what they preach abroad. It remains an open question whether the particular development strategy inherent in the current OECD orthodoxy makes sense for the developing countries. Does it apply to all of them at all times, in all circumstances? Clearly, there is a need for comparative research on alternative development strategies. This research should benefit from an historical as well as an analytical dimension.

On Human Resources, Human Capital and Human Development

On a previous occasion, I tried to define the human factor in three different fashions.' First, the traditional definition of human resource development which emerged some twenty-five years ago focused primarily on education and secondarily on health. Skill formation was seen as an investment in human capital that had to be undertaken parallel with investments in physical capital. Second, a broader definition of human resource development is possible by making a distinction between (i) the creation of human resources, (ii) their deployment and (iii) the setting up of an incentive structure with which to realize such a desirable deployment. Thus, not only certain types of education and training, but also employable skills, including those of management, must be provided. Furthermore, what purpose does a highly educated population serve if it may not participate in the decision-making process? The World Bank Report 1980 comes close to defining human development along such lines by including education and training, better health, nutrition, fertility reduction, entrepreneurial and administrative abilities, and research and technology. All this would mean a quite different policy package in the field of human resource development than has so far been pursued.

Third, and finally, the question of human resources can also be interpreted much more broadly than in the two previous definitions. This would lead to the question of the human factor in development, touching upon such questions as innate ability, motivation and achievement, and even more importantly, upon the question of whether systematic differences in these factors occur. This is clearly an extremely delicate matter. The most difficult situation that a government has to face is to break through a Malthusian low per capita income equilibrium. And this is not only an economic problem. A fundamental overall social change is necessary to set in motion a process of economic development. Subsequently, it has been realized that lack of organizational ability prevents the realization of development plans even more than the lack of capital.

This brings us back to fads and fashions which, despite obvious interrelationships, assert that some one factor is more important than all the others. We know by now that if one succeeds is breaking one bottleneck, the result is usually that another one comes into prominence. We must be careful here not to get into a circular argument: when trying to be comprehensive, one loses operational qualities, and therefore, analytical and policy handles. Attempting to identify one or two crucial factors may lead to partial analysis because of neglect of all the others!

A balanced human resource development policy - balanced with respect to other factors that are important for economic, social and cultural development - would have to look carefully at the human factor at the micro level, i.e., at the level of organizations and firms. It would ensure that the labor force is well educated and well trained. It would be sensitive to the needs of good and comprehensive management at all levels, especially at the middle level. It would introduce a judicious incentive structure which would include both monetary and nonmonetary incentives.

But there is another and perhaps even more important problem, namely, how does one introduce motivation at all levels? How does one get people to agree with the objectives of the organization or firm in which they work? How can one ensure that people give the best of themselves at all times? Is not the real secret of why certain firms or countries do better than others the simple fact that their employees work harder because they believe in what they are doing, and/or because they enjoy their work?

Such reasoning leads naturally to a consideration of the relationship between Harvey Leibenstein's X-efficiency theory and human development.° X-efficiency measures the degree of effectiveness or ineffectiveness in the utilization of inputs that are easily quantifiable. X-efficiency theory is concerned with the different ways in which traditional inputs of capital and labor can be used to different advantage in firms. Changes in X-efficiency involve changes in productivity.

X-efficiency depends not only on techniques of management; it also depends on the organizational life of the firm. The actual activities that employees carry out will depend to some degree on their own choices and those of others with whom they work. The fact that these choices are very much constrained does not rule out the possibility that some degree of choice or discretion is indeed involved. Most, if not all, jobs are presumed to require interpretation. These interpretations imply that the employee in some sense chooses the activities that he carries out, the pace at which he will carry them out, the quality at which they are carried out and the time sequence of activities.

The notion of job interpretation implies that, at least to some extent, individuals are free to choose the effort levels at which they work. These effort levels in turn determine the value of the output that individuals contribute to the firm. Thus, productivity depends not only on the amount of labor and capital, but also on the nature of the job interpretation made by workers and employees. In Harvey Leibenstein's words:

Motivation may be viewed as an input, but it is important to bear in mind that it is not an input that u purchased in the market. Rather it is a consequence of the interactions between individuals within the firm and a system of payments, promotions and sanctions which the formal management attempts to impose. However, the formally determined motivational system is only a part of the actual motivational system, and furthermore, the formal system very frequently may not operate the way the management anticipates.'

What has all this to do with human resources, human capital, human development and the human factor? The answer is simple and complex at the same time. X-efficiency theory puts emphasis not only on the quality of the traditional input capital and labor, and therefore on the education, training and skill aspects of the labor force, but also on motivation, job interpretation, the organizational life within the units which compose an economy, techniques of management, peer group interactions, approval and disapproval mechanisms, systems of payment and promotion, sanctions, and so on. It stresses the fact that motivation is an input that is not purchased in the market but is precisely a result of interaction between individuals within the firm and the system of incentives and disincentives imposed by management.

Instinctively, one would be inclined to believe that it is only in exceptional circumstances that people will give the best of themselves for their firm or their country. But surely the art of management, and of policy making for that matter, is to create an environment in which people will always work at their highest possible levels of productivity. For that to happen, the "human factor" must move to center stage in management and policy making.

Conclusion

It is obvious that adjustment policies as they have been defined hitherto are not the best way, to put it euphemistically, to motivate people in the developing countries at any level of decision making. They are in fact practically the worst way to get people to give the best of themselves. The assumption inherent in much of the current financial and economic orthodoxy is that short-run defationary adjustment measures consisting of cutting public sector deficits and spending are the best way to achieve more rapid economic growth in the long run. And so we observe cuts in educational expenditure, health expenditure, and even in outlays on public investment. Such a short-term policy produces negative incentives all around and hence is bad economics.

It seems as if at least the IMF is now learning from past experience, judging from the recent agreement reached with Mexico. This agreement puts heavier emphasis on the objectives for growth and long-term structural adjustment than on the usual targets for tighter monetary and fiscal policies. It even goes so far as to concede that an increase in public spending may be needed in 1987 if the economic growth of Mexico is still flagging. Gradually, it is coming to be recognized that deflationary measures may not only threaten political stability in important parts of the developing

world, but also impose heavy costs on the OECD economies.
One last point: it should be clear that talking about the human factor in development is not the same thing as talking about the cultural factor in development. Sometimes, one gets the impression that the cultural factor is being stressed in order to find yet another rationalization not to stress economic factors, and more particularly, the need for capital transfers from the developed to the developing countries. One lesson to be learned from events of the past decade is that a balanced approach to development is essential: the balance between investments in physical and in human resources; the balance between the role of the state and the role of the market; the balance between central planning and private initiatives; the balance between stress on growth factors and emphasis on distributive measures. It is when policies move from one extreme to another and lose sight of the delicate balances that should exist in an economy and in a society that its people are in trouble.

Notes

I. Khadija Haq and liner Kirdar, eds., Human Development The Neglected Dimension (Islamabad: North South Roundtable, 1986), pp. xv-x.
2. Ridurd Jolly, "Adjustment with a Human Face," in Human Development, p. 388.
3. The next three paragraphs summarize a discussion presented in full in Louis Emmerij, The Human Factor in Development," in Human Development, pp. I3-27.
4. Harvey Leibenstein has vn,uen quite a lot about X-efficiency over the past demde. A slim volume of his would be as good as anything else to refresh one's memory. See Harvey Leibenstein, Inflation. Income Distribution and X-Efficiency Theory (London and New York: 1980).
5. Ibid., p. 30.

CHAPTER 2
From Dialogue to Action

Mahbub ul Haq

The development dialogue has gone through many cycles in the past. In the I970s, it was dominated by the concern about absolute and relative poverty and policy actions to alleviate poverty. In the I980s, we have been tormented by the discussion on adjustment policies, to a point where the words "adjustment" and "development" are beginning to become uncomfortably interchangeable. The so-called "poverty decade" has been succeeded by the ever-insistent "adjustment decade." And yet all this is an illusion, or at most, a passing fashion; for the basic nature of the development problem has not changed in the developing countries. What is needed is a restoration of our perspective on the adjustment debate and a timely descent from dialogue to action.
The real dilemma we confront today is: Can we manage adjustment policies while engineering high rates of growth and high levels of output and employment, while protecting expenditures on education and health and enhancing human development? The issue can be addressed on at least at three levels: first, at the conceptual and intellectual level; second, regarding policy options at the national level; and third, regarding international choices.

The Conceptual Challenge

On the conceptual level, it seems somewhat strange that while the presumed conflict between adjustment policies and growth with human development has dominated international discussion now for the last few years, there has not been as much intellectual investment in this issue as it really deserves. There is a school of thought that believes that adjustment policies and growth with human development are really antithetical and cannot be combined in a national policy framework or in international policies. It argues that adjustment policies require short-term demand management, while growth policies require long-term supply expansion. It argues, as Louis Emmerij has argued in his excellent paper, that adjustment policies require correction of price distortions, a greater role for the market mechanism and less government intervention - a conscious withdrawal of government presence from the economy - while human development policies require more government interventions and greater presence of the government, particularly in the education and health sectors.
We need to examine this thesis very carefully, because the presumed conflict between adjustment policies and growth and development may be more apparent than real. In fact, the present resource allocations are not perfect in most developing countries; and if there is better demand management, if there are corrections of price distortions, if there is reduction in unnecessary public intervention in

many industries, and if there are fewer inefficient and corrupt economic and administrative controls, then these measures often release much-needed and extremely precious resources for both growth and human development.

My experience as the Planning Minister of Pakistan for the past five years has shown that correct adjustment policies can release resources to achieve both higher growth levels and better allocations for education, health and human resource development. Over the past six years, from 1980 to 1986, Pakistan has not reduced its expenditures on education and health, but increased them from 8.6 percent of the total government expenditure in 1980 to 14.2 percent in 1986. And this has been done neither at the cost of growth - because GDP growth rates during this period have been around 6.5 percent per annum - nor at any other expense. Instead, it has been accomplished through a series of structural policy changes which simultaneously achieved badly delayed adjustment as well as growth with human development. For instance, during this period, many public industries which had been nationalized in the I970s and were running inefficiently were returned to private control. Economic controls were reduced, the system was deregulated, price distortions and subsidies were reduced. Contrary to popular belief, many subsidies which persist in the developing countries are distorted in favor of the rich and the powerful, and generally, the urban elite. As such, the reduction often enables these countries to pursue programs which are more populist or which benefit a large majority. During 1980-86, 25 percent of Pakistan's total government budgetary resources were released through various adjustments which were carried out, and these allowed for greater investment in energy development, health, education and other human resource development programs.

So, far from being antithetical, the achievement of adjustment with growth and human development offers an intellectual and policy challenge in designing programs and policies which can combine much-needed adjustments with protecting levels of growth, employment and human development.

The conceptual challenge of combining these two concerns is like a similar challenge faced in the early 1970s of combining the conflicting viewpoints of the growth school and the distribution school. At that time, one school of thought contended that developing countries must pursue GNP growth above all else, because otherwise, they could only redistribute poverty. Another school of thought argued just as vehemently that if GNP growth were the only god that was worshipped, this would lead to serious concentrations of income and wealth, and the quality of human life would diminish even as the national production increased. There was thus an intellectual challenge: Could growth and distribution policies be combined in the national planning framework?

The academic community and the intellectuals who got together to address this challenge made a concerted effort in various institutions. Finally, a group working for about two years at the Sussex Institute in Britain, financed largely by the World Bank (under Robert McNamara at that time), led by Hollis Chenery and bringing together brains like Hans Singer, Richard Jolly and others, to which I made a marginal contribution, produced a fresh analysis on this subject. The breakthrough was simple, as most truths are. Yes, increased productivity is necessary; but let us ask the question, increased productivity of whom, and for whom? Can this also be increased productivity of the majority of the population, of the poor? Thus, increasing the productivity of the poor became a way of combining growth and distribution policies. As such, the redistribution of assets and public services also demanded attention. With that intellectual breakthrough, national policy makers focused on recasting their development planning strategy. The measurement of poverty profiles the and delineation of policy action to increase the productivity of the poor became as much of a planning staple as GNP growth measurement and policies to increase national production. Internationally, Robert S. McNamara, with his vision and dynamism, took up the banner of increasing the productivity of the poor and bent all the policies and lending programs of the World Bank toward this concern. Through his persistent and persuasive advocacy, he managed to influence the policies of all the other international institutions, as well as the thinking of the world at large.

We must now generate a similar intellectual ferment around the concerns of adjustment with growth and human development. Let some institutions step forward - WIDER, the OECD Development Centre, the ODC and others - and let some analytical work be undertaken to achieve a synthesis between these concerns, which are essentially compatible. And let the World Bank and the IMF provide a financial umbrella for this work so that the end product can also command their immediate attention and worldwide discussion.

Rationalizing National Priorities

The second challenge is to pursue this concern at the national policy level. It does little credit to the developing countries to externalize all their internal problems and to t'md constant alibis in the deteriorating international environment for a lack of action on issues that are essentially structural in nature, and which only national planners and policy makers can address. Some time back, then Tanzanian President Julius Nyerere asked in legitimate despair: "Must we starve our children to pay our debts?" It is at least equally legitimate to ask: Must we starve our children to increase our defense expenditure? For the sad reality is that expenditure on education and health as a proportion of central government expenditures declined from 21 percent in 1972 to 9 percent in 1982 in low-income developing countries, while at the same time and during the same period, the defense expenditures of all developing countries increased from 7 billion dollars to over 100 billion dollars. Is it therefore impertinent to ask: When our children cry for milk in the middle of the night, shall we give them guns instead?

Defense expenditures are not the only source or evidence of irrationality in domestic resource allocations in the developing countries. The margins of public inefficiency and corruption often exceed 20 percent of the public budgets in many developing countries. Yet we quibble endlessly about small reductions in foreign assistance, when fighter economic management could release sub-stanfally more resources for legitimate growth and human development needs.

When Pakistan confronted the necessity for an immunization program for our children, what did it take? Immunization coverage- for Pakistani children was 5 percent five years ago; it is 75 percent today. It has been one of the most dramatic stories of increasing child survival, and by now, 100,000 infant deaths are prevented every year. And what did it take? More assistance from abroad? Or did it take reducing our growth rates? No. What it took was postponing the decision to build an expensive urban hospital for five years. That, by itself, totally financed the entire expenditure on the immunization campaign.

When it came to the question of spreading public services and infrastructure to the rural areas, containing 70 percent of the population, what did it take? Only 10 percent of the total public expenditure was going to the rural areas while 90 percent was going to the urban areas, because even the rural elite live in the urban areas. And this is a pattern not atypical of most developing countries. Yet Pakistan has been able to electrify half its villages over the past six years by suffering one or two hours of load-shedding of electricity in the cities from time to time.

These are very difficult political choices; but just by shifting internal priorities, much can be accomplished. Similarly, economic deregulation, lowering subsidies, reducing public expenditures on inefficient industries and other shifts in internal priorities enabled Pakistan to increase both growth and human development. Nonetheless, there is still considerable scope for improving Pakistan's economic management and diverting more resources toward growth and human resource development. Those who postulate a basic conflict between these goals often assume, incorrectly, that an ideal or optimum allocation of resources already exists in these countries.

These are choices no one can make for us but ourselves. These are structural problems rooted in our domestic power structures and alliances which only national planners and decision makers can resolve. While we can legitimately argue that the international environment should not make these choices more difficult than they already are, it is undeniable that national planners have to address these issues directly and courageously if adjustment policies are to be r combined with both growth and human development. Otherwise, irrespective of how much improvement takes place in the international environment, the domestic choices may well be distorted against both growth and human development. It is my belief that over 90 percent of these issues are national in character; and to pretend otherwise would be dishonest.

Responsible International Action

Let me come to the third theme to be discussed here: international choices. What is the extent of international responsibility in this?

First, the international community must try to ensure open markets, less regulation and fewer controls, because it is becoming somewhat ironic for the developing countries to be repeatedly advised to reduce controls, price distortions and subsidies, to deregulate, to follow the logic of the marketplace, only to find that the same principles and advice are being ignored at the international level. The most pressing issue at present is the next round of trade talks, which must start with as comprehensive an agenda as possible and then strive to strike some initial bargains which benefit most nations and generate a sense of momentum toward a freer international trading system.

Second, while much can be said about capital transfers, and many proposals have been made for additional transfers, the heart of the issue at the moment is that adjustment policies in the developing countries cannot be smooth if these countries simultaneously have to transfer resources to the rich nations. The very least we can expect and demand is that there should be no reverse transfer of resources to the developed countries, which is totally against the letter and spirit of the Bretton

Woods arrangements. How,over the past four or five years, have we come to accept the negative resource transfer of over $50 billion a year from poor nations to rich nations? Obviously, this makes the task of developing countries in combining adjustment with growth and human development extremely difficult.

Third, we must revive the international institution responsible for monitoring and managing adjustment in the developing countries. It is unfortunate that adjustment policies have ended up being the province of the wrong institution, the IMF. The IMF has its own role, which it should continue to play. But during the last five years, there has been a quiet withdrawal of the World Bank from leadership at a time that was tailored for World Bank expansion, when the Bank could have managed adjustment policies consistent with growth and human development. If adjustment policies are to be combined with growth and human development, it is absolutely essential that the World Bank's role be greatly strengthened.

In conclusion, the present discussion must address the conceptual challenge of combining adjustment with growth and human development; the rationalization of national priorities; and the resumption of international responsibility. We should discuss these choices in a spirit of enquiry, a spirit of honesty; because we are not here representing anyone or anything except the search for truth.

CHAPTER 3

Adjustment and Growth with Human Development: A Review

Uner Kirdar

The objective of development is people. Yet an analysis of the development process over the last four decades will show that one of the major obstacles to economic, social and political progress in many developing countries is the insufficient attention given to the human dimension of development. This neglect has been further aggravated by recent economic pressures and difficulties. Following the repercussions of the oil, food, financial and debt crises, growing budget deficits and, more recently, falling oil prices, the 1980s witnessed successive economic adjustments which caused a shift in the orientation of national and international policy makers from long-term goals of poverty eradication and strengthening the human dimension of development to short-term concerns, such as the timely payment of debts and interests rates and the reduction of budget deficits.

Since the beginning of this decade, serious cuts in human resource development investments have resulted from the austerity, or so-called "stabilization," programs worked out in most developing countries with the assistance of international financial agencies and from the adjustment policies adopted by several developed countries to enhance the necessary adjustment at the implementation level. There is now clear evidence that, in country after country in both the developing and the developed world, expenditures for education, health, nutrition and many other forms of human capital formation have been heavily curtailed.

A survey of recent stabilization programs reveals first, that they have been unrealistically short-term and that adequate attention has not been given to a most important element of the development process, namely, human development. The conditionality measures embodied in these programs have generally inhibited the process of human capital formation in the countries concerned, and consequently have damaged growth and prevented the emergence of a self-reliant capacity for further development.

Second, the success of these programs largely depends upon whether they are properly designed by the country itself, with conviction and commitment, and not imposed upon it by an outside financial institution. However, most of the developing countries - especially the least-developed African and small Latin American countries - do not possess the required expertise to work out such programs by themselves.

In the light of experience gained from this process, it may be concluded that while all these belt-tightening measures involved major human and social costs, they still have not brought about the expected economic recovery. On the contrary, In several countries of sub-Saharan Africa and in Latin America, they have caused serious loss of output, depressed employment and rising poverty levels. It is projected that in the sub-Saharan region, GNP will continue to fall for the rest of this decade and that in 1995, 65 to 80 per cent of the population will still be living below the poverty line.'

Recently, there has been increasing international concern for growth-oriented adjustment because of the unpredictable political implications of the prevailing situation. Within this context, it is promising to note that, finally, there is also a growing recognition of the vital role of the human element in the resumption of sustained and balanced growth.

The Impact of Adjustment : Recent Trends

during the 1970x, economic growth was more or less steady in both developed and developing countries. An average rate of growth of about 3 to 4 percent per year was ensured in the former and above 6 percent in the latter. After the second sharp rise in oil prices, a major, widespread recession began in 1981, especially in industrialized countries. This also had a serious impact on developing countries. In the OECD member countries, the increase in output was only 0.5 percent in 1982, and more than 30 million people were unemployed.

In developing countries, as a result of the oil shock, which was followed first by the financial crisis and later by the debt crisis, severe austerity measures were taken to adjust both external as well as internal imbalances. The rate of growth of the real gross domestic product (GDP) has declined in the past half-decade to an average of less than 2 percent per annum. In early 1986, the non-oil commodity price of major exports of these countries was, in dollar terms, some 20 percent lower than in the early 1980s. In a sample of 83 developing countries for which preliminary information was available in 1985, no less than 49 had zero or negative GDP rates of growth per capita.'

In Latin America, per capita GNP fell by 4.9 percent in 1982, by 4.5 percent in 1983, and increased by barely 1.5 percent on average in 1984 and 1985. By the end of 1985, the average GDP per capita in Latin America and the Caribbean had fallen to the level of 1976.

In Africa, especially sub-Saharan Africa, the situation started to deteriorate in the late 1970s. By 1984, the per capita income was estimated to be not higher than the I960s level. In 1983, the servicing of external debt payments absorbed 30 percent of Africa's export earnings, and the total debt was estimated at nearly 60 percent of the GDP. For instance, one of the worst-affected countries is the Sudan, where the external debt is currently estimated at seven times its export earnings.

In human terms, about a quarter of the total population of developing countries experienced an actual fall in per capita real income in the first half of this decade, while real income remained at about the 1980 level for a further quarter of the population.

TABLE 1

Population and GNP Per Capita, 1980, and Growth Rates, 1965-83

Country Group	1980 GNP (Billions of Dollars)	1980 Population (Millions)	1980 GNP Per Capita (Dollars)	Average Annual Growth of GNP Per Capita (Percent)				
				1965-73	1973-80	1981	1982	1983
Developing countries	2,064	3,124	660	4.1	3.2	1.0	-0.7	0.0
Low-income countries	550	2,102	260	3.0	2.7	3.0	3.2	6.1
Asia	497	1,900	260	3.3	3.0	3.5	3.7	6.9
China	287	978	290	5.0	3.8	3.5	6.1	8.8
India	162	687	240	1.6	1.8	3.5	0.5	5.1
Africa	53	202	260	1.2	0.1	-1.3	-2.4	-2.7
Middle-income oil importers	693	580	1,660	4.6	3.1	-0.8	-2.0	-1.6
East Asia and Pacific	212	162	1,310	5.7	5.7	3.9	1.8	4.7
Middle East and North Africa	25	31	820	3.5	4.2	-1.9	4.4	0.3
Sub-Saharan Africa	26	33	780	2.0	0.5	3.8	.-5.0	-5.5
Southern Europe	213	91	2,340	5.4	2.9	0.2	0.0	-0.9
Latin America and Caribbean	411	234	1,760	4.5	2.9	-4.2	-4.9	-4.5
Middle-income oil exporters	551	441	1,250	4.6	3.4	1.5	-2.8	-4.4

SOURCE: World Bank, World Development Report 1986, p. 154.

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TABLE 2

GDP in Selected African and Latin American Countries
Average Annual Growth Rate (Percent)

	1965-73.	1973-84
Argentina	4.3	0.4
Brazil	9.8	4.4
Costa Rica	7.1	2.8
El Salvador	4.4	-0.3
Ghana	3.4	-0.9
Ethiopia	4.1	2.3
Liberia	5.5	0.2
Nicaragua	3.9	-1.1
Nigeria	9.7	0.7
Jamaica	5.4	-1.4
Sierra Leone	3.7	1.8
Tanzania	5.0	2.6
Togo	5.3	2.3
Uganda	3.6	-1.3
Venezuela	7.5	2.7
Zaire	3.9	-1.0
Zambia	2.4	0.4
Zimbabwe	9.4	1.7

SOURCE: World Bank, World Development Report 1986, pp. 182-3

TABLE 3

Per Capita GNP of Selected African and Latin American Countries
Average Annual Growth Rate (Percent)

Argentina	0.3
Bolivia	-0.2
Central African Republic	-0.1
Chile	-0.1
El Salvador	-0.6
Ethiopia	0.4
Ghana	-1.9
Madagascar	-1.6
Mali	1.1
Nicaragua	-1.5
Niger	-1.3
Jamaica	-0.4
Peru	-0.1

Senegal	-0.5
Sudan	1.2
Zambia	-1.3

SOURCE: World Bank, World Development Report 1985, pp. 180-1.

Adjustment in Developing Countries

In its literal sense, the tern adjustment means adaptation to changing circumstances. In economic terms, it refers to the restoration of the macroeconomic balance in a national economy. However, in the early 1980s, the implementation of prototype stabilization programs became synonymous with:
a) Devaluation of the currency of a country. b) Severe curtailment of imports.
c) Stringent measures to compress internal demand.
d) Radical curtailment of government expenditures, particularly in the areas of human resource building ahd social development, such as investments in health and education, subsidies for nutrition, etc:
e) Freezes or cuts in wages and salaries in the public sector.
'Thus, the way in which the adjustment of the world economy has taken place in the past few years has had strong negative effects on the economies of most African and Latin American countries. The adjustment policies brought about a worsening of the existing structural economic problems, which were al.eady affecting the well-being of the people of these countries. Investments have dropped sharply and are approximately 30 percent lower than in the 1970s. The long-standing unemployment problem has been compounded by a high level of open unemployment, with a particularly severe impact on the lives of youth. Poverty has increased in certain segments of the population, and the problems of the lowest-income groups have worsened.
Overall, the adjustment policies of the I980s have had considerable short- and long-term effects on the income, nutrition, health, education and housing conditions in developing countries and have particularly affected women and children, who constitute the majority of the population. Social and political tensions have increased in several developing countries because of this.
However, despite the recent efforts of several intergovernmental and riongovernmental organizations and private individuals to assess the negative impact of adjustment policies of the 1980s on human development, it is not easy to give precise quantification for developing countries in toto. First of all, research in this area is hampered by the analytical complexity of the subject. Second, either the lack of appropriate statistical indicators, especially for the least-developed countries, or differences in coverage and comparability of data further complicate the task. Nevertheless, information available on the situation in certain developing countries, as well as statistics on central government expenditures on education, health, social amenities, etc., do shed some light on the human costs of adjustment.

Education

According to the World Bank's World Development Reports for 1985 and 1986, central government expenditures for education in low-income developingg countries declined from 15.2 percent in 1972 to 4.7 percent in 1983. Similar declining proportions are also recorded for all other categories of developing countries.
In many African countries, the education sector expanded after independence. A study by the World Bank concerning the adjustment process in sub-Saharan Africa shows that the education sector is now suffering from a reversal both in the quality and the quantity of services provided.'
In twelve sub-Saharan African countries, primary enrollment ratios declined during 1980-83. In some countries, such as Somalia, Togo an Mozambique, this decline was around 10 percent or more. In Nigeria, school enrollment dropped from 90 to 60 percent in an eighteen-month period ending in 1984.4

TABLE 4
Central Government Expenditures for Education in Selected Developing Countries
(As Percentage of Total Expenditures)

	1972	1983
Argentina	8.8	7.6
Brazil	6.8	3.7
Bolivia	30.6	26.9
Chile	14.3	13.7

El Salvador	21.4	16.6
Ghana	20.1	18.7
Mexico	16.4	11.0
Lesotho	19.5	17.4
Panama	20.7	11.0
Peru	22.7	18.5
Sri Lanka	13.0	7.1
Sudan	9.3	6.1
Turkey	18.2	12.5

SOURCE: World Bank, World Devebpment Report 1986, pp. 222.5.

Similar trends also emerge for the more developed of the developing countries in Latin America. In Mexico, as compared to 1978 prices, the cost of education increased by 30.8 percent in 1981, 80.6 percent in 1982 and 97.1 percent in 1983.' Experience proves that in times of economic difficulty, the children of the poorer segments of the population tend to drop out in relatively large numbers, either because parents cannot afford the cost of their attendance or because the children are needed to supplement the family income. According to government figures in Brazil, one-third of all children between the ages of 7 and 14 - some 8 million - at present do not attend school.'

The dropout rate from schools caused by the high cost of attendance also perpetuates social divisions in developing societies, particularly since girls are more likely to drop out than boys. Thus many of the longer-term beneficial effects of primary education on nutrition, health, infant mortality, family planning, etc., are lost.

Health

The I980s have seen a decline, not an improvement, in the health services of most African and Latin American countries. Health expenditures, too, are often vulnerable to cuts during periods of fiscal austerity. Public expenditures in the health sector have been curtailed in quite a number of developing countries - particularly in Africa - and the higher cost of imports has also often reduced the real value of appropriations for the health sector.'

According to the World Development Reports for 1985 and 1986, central government expenditures for health in low-income developing countries declined from 6.1 percent in 1972 to 2.7 percent in 1983.

In many countries, this has resulted in a lower overall standard of health care being provided to the public. For example, immunization levels have dropped in recent years in the most hard-hit countries, such as Zambia, Tanzania and Ghana.

TABLE 5

Central Government Expenditure for Health in Selected Developing Countries

(A4 Percentage of Total Expenditure)

	1972	1983
Argentina	2.9	1.4
Bolivia	8.6	3.1
Chile	8.2	6.0
El Salvador	10.9	8.4
Ghana	6.3	5.9
Mexico	5.1	1.2
Morocco	4.8	2.9
Lesotho	8.0	7.2
Sri Lanka	6.4	5.1
Sudan	5.4	1.3
Turkey	3.3	1.8
Uganda	5.3	4.6
Venezuela	11.7	8.6

SOURCE: World Bank, World Development Report 1986, pp. 222.3.

Food and Nutrition

Available data suggest that more than 700 million people in the developing world lack the food necessary for an active, healthy life. Malnutrition, particularly among young children, handicaps their ability to learn, to work and to grow. Of these 700 million, it is estimated that 340 million will not receive the necessary minimum calorie intake to prevent serious health risks and stunted growths

Problems of malnutrition do not result only from inadequate food supplies, as is widely believed; they also arise from a lack of purchasing power. It is estimated that absolute poverty in rural Africa increased from 82 percent in t974 to 91 percent in 1982. Some ISO million people suffer from malnutrition. Both the calorie supply and the supply of protein have been falling. In 1983, the high rate of malnutrition in the Sahelian region affected 20 to 30 percent of preschool children and 60 percent of pregnant women, who now suffer from serious marasmus and nutritional anemia."

The proportion of malnourished children reached a peak of 53 percent in Ghana in 1983, while in Ethiopia at present, 40 to 60 percent of the children aged 1 to 3 years are below the standard weight for their age. In Mozambique in 1984, four out of every ten children below the age of 5 years perished from a shortage of food and water, compounded by deteriorating sanitary conditions.' °

In Latin America, about 40 percent of families are poor, in the sense that their food intake does not meet basic requirements. A comparison of infant mortality in Bolivia between 1973 and 1983 shows a dramatic increase in infant deaths related to malnutrition. The same is valid for Brazil; 36 million under the age of IS -about 60 percent of the total - are in need. More than half the children under 6 years of age are malnourished.' '

No problem of underdevelopment is more serious than the human development crisis, nor does any other issue have such important implications for the self-sustained, long-tern growth of the developing countries.

Employment

The economic slowdown caused by external indebtedness and the austerity measures adopted by governments in Africa and Latin America in conformity with adjustment programs have sharply increased recorded unemployment. In many of these countries, the situation has been further aggravated by a substantial decline in real wages. Asymetrically, price increases reached unprecedented levels because of high inflation rates. In Africa, where the large majority of the population live and work in rural areas, the deteriorating employment situation mainly took the form of increased unemployment or underemployment. According to the 1986 report of the ILO Director-General, open unemployment in urban areas in Latin America averaged 5.8 percent in the early I980s. Subsequently it rose to 8.1 percent - an increase of 40 percent. lithe urban labor force is taken into account, the number of unemployed has grown by 67 percent. Between 1980 and 1984, urban unemployment more than doubled in Uruguay and Venezuela. Similarly, in recent years, at least 20 percent of young people were unemployed in Colombia, Ghana, Kenya, Mexico, Nigeria, Sierra Leone, Tanzania and Zaire."

A typical stabilization program foresees a curtailment in government spending accompanied by policies to control increases in wages and salaries. Normally, it is the poorest segment of the population which suffers most from the implementation of the combination of these two sets of policies. These measures are also always coupled with successive devaluations of national currencies. As wage and salary increases are normally kept below the rate of inflation, both blue-collar and white-collar workers become poorer, and their shares in national incomes are reduced. For instance, in Mexico during 1983 alone, a notable deterioration of income distribution occurred, since the purchasing power of minimum wages fell by 23 percent. At the beginning of this year, civil servants were informed that there might be no salary increases in 1986 because of government austerity measures. With 63 percent inflation in 1985, this meant that they had taken a two-thirds cut in their pay."

Adjustment In Developed Countries

The increase in poverty levels due to the adjustment process is not confined only to developing countries. In several industrialized countries, investments in human development have been curtailed substantially during the period under review on account of adjustment measures taken by governments because of economic recession, growing budget deficits and/or prevailing economic philosophies.

Unemployment

The impact of recession and economic difficulties on industrialized countries was usually marked, as mentioned earlier, by a significant rise in unemployment. This took place at a time when a considerable number of young people in both North America and Europe were trying to join the labor force. The first signs of a rapid rise in unemployment were seen during the recession of 1975. There has been a continuous increase In unemployment each year since 1980, peaking at 9 percent in 1983 - almost three times higher than a decade earlier. By 1984, unemployment was estimated at 20 percent in Spain, 15.2 percent in Belgium, 14 percent in the Netherlands, 13.2 percent in the United Kingdom, 11.3 percent in Canada, 8.4 percent in the Federal Republic of Germany, 8.7 percent in France and 7.5 percent in the. United States.'

Health

According to WHO research, it is clear that there have been considerable reductions in industrialized countries in the rate of growth of expenditure for health services in relation to GDP during the I980s. In some of these countries, health expenditures have been reduced in real terms over the past two years."

Education

In several developed countries for which statistics are available, there have been considerable decreases in central government expenditures in the area of education.

TABLE 6

Cenual Government Expenditures for Education in Selected Developed Countries
(As Percentage of Total Expenditures)

	1972	1983
United States	3.2	1.9
Federal Republic of Germany	1.5	0.8
Belgium	15.5	13.9
Italy	16.1	8.6
New Zealand	16.9	11.9
Spain	8.3	6.0

SOURCE: World Bank, World DevelopmentReport 1986, p.225.

In developed countries, the part of the population hardest hit by the recent economic difficulties has probably been the youth. Interrelated social, economic and political factors are creating a vast new class of poor youth, less educated and likely to give birth sooner than earlier generations of the poor. The reasons are many and complex and are tied to certain government policies and deep social changes. In the United States, for instance, according to recent studies, some 14 million, or 22 percent, of Americans under the age of 18 are at present living below the poverty level - up from 14.3 percent in the I970s. According to some estimates, 30 percent of the U.S. federal budget involves spending for older Americans, while only 3 to 5 percent is spent on children.'

In a recently published book, Family and Nation, U.S. Senator Daniel Patrick Moynihan writes that the number of single-parent families has doubled: more than 40 percent of black families are now headed by a woman, as against 25 percent in the late I960s. More than 50 percent of these families live in poverty. He also notes that the illegitimate birth rate has.doubled since the late 1960s. Last year, within the overall unemployment rate in the United States of around 7.5 percent, the range for all youth aged 16 to 19 was 17.8 percent, and for the black teenager, 38.2 percent)

The growing mass of politically silent poor youth in affluent nations is a social revolution with unpredictable ramifications. Thus, the neglect of the human dimension during adjustment has not only increased the levels of poverty, but has also generated a lack of opportunity for the younger generation in particular. It is unfortunate that the adjustment policies of the I980s lacked the vision to rescue the most valuable patrimony of each country from misery' and offer instead the chance to develop their skills, capabilities, ingenuity and creativity.

Positive Developments:

An International Awakening Fortunately, there is an ever-increasing recognition of the shortcomings and dangerous impact of the adjustment policies of the I980s and an emerging concern for growth-oriented adjustment, especially after the presentation of the Baker Plan. It is now being argued that adjustment should become synonymous not with policies of austerity, lower growth or economic retrogression, but with policies aimed at resuming sustainable growth with prosperity and human development.

The North South Roundtable

The North South Roundtable should be congratulated for its avant garde role in bring the human development issue to international attention.

The first session of the Roundtable on Money and Finance in Istanbul in September 1983 declared that "solutions which do not take the human dimension and human resources building into account will fail to provide an enduing answer to the world's financial and monetary crisis. Until human resources needed for substantial economic growth are developed, real development will remain a dream." The view was also expressed that in the last analysis, the success of all adjustment processes, all policy options and institutional alternatives should be judged by the same yardstick: the impact they have on human welfare.'" ° In Santiago in March 1984, the second session of this roundtable argued that "human resource development should not he cacrifired for chnrt-lived oacoe ,n material production." The third session, in Vienna in September 1984, advocated that the developing countries needed to rethink their development strategies so as to give a higher priority to human resources development." It recommended the "preparation of an annual comprehensive study on the state of the human condition, to focus national and international attention on people-oriented strategies"' °

The first session of the Roundtable on Development: The Human Dimension in September 1985 dealt in depth with the impact of the adjustment policies of the I980s on the developing countries and their negative ramifications for human development. These roundtables have greatly contributed to a recognition that the adjustment policies and conditionality packages of the 19808 in their present form are inhibiting the process of human capital formation in the developing countries and thus damaging growth and preventing the emergence of a self-reliant capacity for further development. Successive roundtables have demonstrated the urgent necessity for reversing these trends by adopting growthoriented adjustment with a human dimension.

During the past year, there has also been an accelerating interest both at the intergovernmental and at the U.N. secretariat levels in the subject of human resource development and the negative effects of adjustment.

ILO

The International Labor Organization is one of the main specialized agencies of the U.N. system concerned with the subject of human resource development and employment. In 1983, the International Labor Conference adopted a resolution calling for the convening of a tripartite meeting, with the participation of relevant international financial agencies, to discuss the negative effects of current stabilization policies and programs on employment and real incomes. The ILO Director-Generalwill report to the next conference on the convening of this meeting.

WHO

The World Health Assembly in 1985 adopted a resolution requesting the WHO Director-Geperal to prepare a report on the effects of the widespread economic crisis on health. This report shows that the world economic situation and stabilization programs have had a very bad effect on many states in the developing world; certain measures for health and well-being have suffered setbacks; and health conditions have substantially worsened.

UNDP

The UNDP Development Study Programme has been an active partner of the North South Roundtable in organizing the roundtables and bringing their conclusions to the attention of the international community. At the governmental level, the June 1986 session of the UNDP Governing Council had a high-level policy discussion on human resource development and development cooperation in the I980s. To assist this review, the UNDP Administrator had prepared a report on Human Resources Development: Issues and Implications (DPI 1986/10). The report underlined that human resource development must be a long-term commitment, and the necessary investments must be considered investments in the future. It stressed the need to find ways to ensuree that the pressures of economic stabilization programs do not violate the very purpose of development, namely, the enhancement of the human condition.

UNICEF
UNICEF has recently embarked on in-depth studies on the impact of adjustment policies on children and become the main advocate of a broader approach to adjustment policies with the motto "Adjustment with a Human Face.

Special Session of the UN General Assembly for Africa

The special session of the General Assembly, which met last Jane to discuss African economic recovery and development 198690, adopted a Program of Action. The analysis of Africa's critical economic situation which became an annex to that program clearly recognized that the persistent economic crisis in Africa has been aggravated by a combination of factors, including insufficient managerial/administrative capacities and inadequate human resources. Therefore, it included a special section on human resource developmeat, planning and utilization at a total estimated cost of USS 7 billion.

Economic and Social Council

At its July 1986 session, the Economic and Social Council considered the report of the Director-General for Development and International Economic Cooperation on Policy Review of Operational Activities for Development (A/41 /350). The report took note of the repercussions of the global economic crisis and stressed the need to enhance cooperation between international financial institutions and those organizations addressing social issues in assisting developing countries, particularly with regard to external debt management, adjustment measures and containment of their social cost.
Taking into account the increasing importance of U.N, activities in the development of human resources, the Council adopted a resolution by which it reaffirmed the need for an integrated and multidisciplinary approach to all aspects of the development of human resources in the program of work of the U.N. system and requested the Secretary-General to prepare an in-depth report on this area with recommendations for consideration by the 42nd General Assembly session in 1987.

ACC

The U.N. system has also taken some joint action at the level of the Administrative Committee on Coordination (ACC). At the request of the ACC, the Task Force on Long-term Development Approaches carried out a study on the economic and social implications of growth strategies and the impact of adjustment policies and measures. Similarly, in 1986,' the ACC Special Committee on Nutrition held a symposium on "Economic Recession, Adjustment Policies and Nutrition" in Tokyo. It has also been decided thaj the topic for the joint meetings of ACC and the Committee for Program and Coordination of the Economic and Social Council in 1987 should be the coordination of the activities of the U.N. system in human resource development and its contribution to meeting the economic and social objectives of the developing countries.
The World Bank, as a major financing institution for the development of developing countries, has recently concentrated its activities at both the research and operational levels on offsetting the negative impact of the adjustment policies of the I980s.
As the main architect of the adjustment and stabilization programs of the I980s, the International Monetary Fund has come under severe criticism. Because of the negative impacts of these programs on economic, social and especially human conditions, this criticism has been advanced both at the national and international levels, in the North as well as the South."
The U.S. Congress even amended that country's "Bretton Woods Act" to read that the United States' representatives to the IMF should recommend decisions that would provide that the United States' repesentatives to the IMF should recommend decisions that would provide that

in approving any economic adjustment programme, IMP shall take into account the effect such a programme will have on jobs, investments, real per capita income, a gap in wealth between the rich and the poor, and social programmes such as health, housing and education, in order to seek too minimize the adverse impact of those adjustment programmes on basic human needs.
As this recommendation was not implemented by the U.S. Executive Directors to the IMF, this amendment unfortunately has remained a dead letter. It is, however, encouraging to see that the validity of the concept conveyed by this amendment has recently been recognized by the management-level leadership of the Fund.

In the early I980s, the Managing Director of the IMF, referring to the adjustment policies of the Fund, stated that such policies "will no doubt involve difficult social choices regarding education, housing, health and even public employment, but these choices have to be made."r a In July 1986, in his address to the Economic and Social Council, Mr. de Larosiere expressed, however, a much more positive point of view. He emphasized that

programmes of adjustment cannot be effective unless they command the support of governments and of public opinion. Yet this support will be progressively harder to maintain the longer adjustment continues without some payoff in terms of growth and while human conditions are deteriorating. Likewise, it is hard to visualize how a viable external position can be achieved if large segments of the work force lack the vocational skills - or even worse, the basic nutritional and health standards - to produce goods that are competitive in world markets Human capital is after all the most important factor of production in developing and industrial countries alike. Adjustment that pays attention to the health, nutritional, and educational requirements of the most vulnerable groups is going to protect the human condition better than adjustment that ignores them.

Conclusion

All the initiatives, studies and pronouncements described above are promising developments. However, in concrete terms, they must now be translated into specific operational measures to render future adjustment policies and programs more conducive to growth and to achieve the required sustained development of human capital.

The most obvious negative impact of present adjustment policies is the burden, in the short term, of heavy human costs and suffering. The second impact, also negative, is more fundamental. There will be a tremendous long-term loss of productivity caused by present policies. The existing human capital situation will deteriorate and lead to a decrease in skill formation, less quality improvement, and reduced creation of the physical facilities and infrastructure necessary for the running of a sound economy.

Thus, many developing countries may lose their present capacity to produce, to trade, to engage in exchange. In turn, there may be a switch from the current demand constraint imposed on them by the existing unfavorable international conditions to a situation of supply constraint caused by the lack of available human skill. This may generate a long period of further economic stagnation.

Taking into account past experience, it is essential to remember that the human element is vital for the resumption of sustained, balanced growth. Physical capital and natural resources cannot substitute for it. Both at the national and international levels, careful policy measures must be designed to ensure long-term economic viability by relying on the human element. In this process, it should be remembered that in balanced, sustained development, efficiency and equity, growth and social justice, frequently go together. Therefore, new adjustment policies and measures should be perceived as growth strategies which also bring about structural changes for social progress and the adequate protection of the most vulnerable segments of society.

Notes

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PART II
MACRO POLICY ISSUES

CHAPTER 4

Stabilization and Adjustment Programs and Policies

Lalth Jayawardena

A recent research project' conducted by the World Institute for Development Economics Research (WIDER) focused on eighteen countries with two major objectives. The first was to see what alternative economic policies to those actually adopted might have been negotiable within the currently available range of International Monetary Fund/World Bank facilities in order to be able to reach desirable adjustment objectives, but at a possibly lower social cost. This exercise was envisaged as a factual piece of counterreseareh, and the authors were at liberty to develop an appropriate economic model in terms of which the analysis could be done. The second was to see how much better countries might have done had a "better" range of facilities been on offer from the international financial institutions. An alternative way of posing the question is to ask how far, different domestic policies apart, the adjustment process itself might have been facilitated by a desirable and feasible reform of the international financial institutions. This paper focuses on the second set of questions, namely, what reforms of the international financial institutions seem desirable in the light of the findings of the WIDER project?

A major area of reform long urged upon the international financial institutions has been for them to develop a long-term facility for providing program financing involving substantial resources at a relatively low level of conditionality. The argument for this has been developed in two places. The first was in a study by Sidney Dell and Roger Lawrence' on the balance-of-payments adjustment process; their findings were based on a similar series of country studies of stabilization and adjustment policies. The second venue for the argument was in the first Brands Commission report,' specifically in the case made out for a World Development Fund. The Brands report identified a number of gaps in the international financial system, two of which - long-term program lending and debt reorganization finance - were analogous to the purposes intended to be served by the Dell/Lawrence facility within the IMF.

Although the Brands Commission did not explicitly go into the nature of the conditionality to be attached to World Development Fund lending in general, the fact of arguing for a new institiution carried with it the clear implication that conditionality would be far less onerous.

Since then, a process of evolution has indeed occurred within the international financial institutions. Within the Fund, less reliance is now placed on the Extended Fund Facility introduced in the middle

I970s, where the traditional three-to-five-year lending period was replaced by an eight-to-ten-year period under tighter-than-normal conditionality. Instead, multi-year standby arrangements have tended to become the rule, especially after the developing country debt problem began to loom large. Within the Bank, a new structural adjustment facility has been introduced where program lending is made available in support of "planning" objectives, e.g., longer-term resource allocation priorities concerning particular economic sectors and fiscal policy changes. While demand management policies, in response to either internal or external shocks, have continued to remain the province of the Fund, the Bank has thus moved away from purely project-oriented activity with its program lending linked to an additional set of Bank conditionalities. Typically, also, a country cannot qualify for a Bank structural adjustment loan until it has secured its Fund seal of good housekeeping with a standby. A few developing countries have, in addition, been engaged in a continuing dialogue with both financial institutions under the aegis of an aid consortium or a consultative group which provides external resource funding on an annual basis.
The decision making process in such consortia is, of course, influenced by country assessments made by Fund and Bank staff and presented to these annual meetings.
This impressionistic account of current practice merely indicates the distance still to be traveled in regard to the objectives which the Dell/Lawrence and the Brands Commission studies had in mind, namely, relatively substantial flows of long-term program lending at substantially lower levels of conditionality than is presently the case. It is therefore important to restate the argument for such a facility, drawing both on general macroeconomic considerations and the experience of the WIDER country studies.

Conditionality; The Need for New Terms

The argument following from general macroeconomic reasoning is straightforwardly stated. This is that the international adjustment process works in an asymmetrical way. Countries in current account balance-of-payments surplus, such as, for example, Japan and Germany, are under no obligation to revalue their exchange rates. On the other hand, countries in balance-of-payments deficit have no option but to devalue when their reserves run out or when their international indebtedness reaches a point, as in the case of the United States today, where corrective action has to be voluntarily taken or forced upon it by market forces affecting confidence. Since arithmetically, for the world economy as a whole, current account surpluses are the counterpart of deficits elsewhere in the system, this asymmetry introduces a profoundly defationary bias into the world economy.
In other words, countries in deficit experience limits to growth which do not apply to countries in surplus. For if surpluses were corrected sooner, counterpart deficits would be smaller and more readily financeable.
While it is true that the major surpluses and deficits affect the developed economies, the aggregate deficits of the developing countries are not insubstantial. As the system works today, the latter are the particular victims of its defationary bias, and the inadequacy of the mechanisms for recycling surpluses to developing countries means that they are compelled to run lower deficits than would otherwise be the case. It is this which provides the basis for the argument that they ought to be placed in a position where they can command access to additional unconditional resources through the international financial institutions. In other words, in a rationally ordered world, these additional resources would come to them in the normal way, without conditions, either through better recycling of surpluses or through an avoidance of defationary bias. It is therefore incumbent upon the international system to find a way of redressing the disadvantageous position in which developing countries find themselves on these two counts.
The inadequacy of current recycling mechanisms has formed the thrust of a recent WIDER Study Group report.° The Economist cited this work as containing "the firmest ideas on how to recycle Japan's cash." According to the Economist, the Study Group "de-tided that two sorts of incentive would be needed to induce Japan's private sector to invest in the Third World. One was some form of guarantee by an international institution such as the World Bank. The second was for the Japanese government to top up returns by subsidising interest rates on loans or giving grants or collateral to investors."'
Such schemes have still to be implemented, and if that were to happen, not only would the developing countries be able to run larger deficits, but they would also be able to release other resources for program financing for their unconditional use.
The guarantee by an international institution could also serve to attract funds from Japan for a new kind of terms-of-trade facility offered on a basis of low conditionality.

Adjustment: The Cost to Developing Countries

When one looks at the country studies, one of the points which emerges with clarity is the degree of economic loss suffered by many developing countries as a result of a lack of adequate amounts of external finance.

Take, for example, Sri Lanka. Along with other countries of the Indian subcontinent, Sri Lanka has had perhaps the ideal international framework for handling its external relationships, namely, a consultative group going back to 1964. The actions of this group, supported by the Fund and the Bank, have been favorably influenced in the long run by Sri Lanka's success in managing to reach high levels of quality of life at a relatively low per capita income. Our adjustment experience in recent years, as indicated in the country study on Sri Lanka,e has also had many textbook elements, such as an excess demand problem induced through the electoral cycle,, which required an import surplus to be run if inflation was to be dampened.

Apart from the standard package of devaluation and credit restraint, the quid pro quo in the Sri Lankan negotiations in 1977 was the phasing out of a food subsidy in order to promote the shift of resources from consumption to investment. The external support for this package of measures comprised a standby, an Extended Fund Facility drawing from the Fund, and major project support under Bank and consultative group auspices for a river valley development scheme.

One result of the program, namely, getting relative prices right, but only in the context of major public investment in irrigation during a previous period, was therapidachievement of self-sufficiency in rice production. Yet by 1984, the import saving on this score had been largely offset by adverse movements in Sri Lanka's terms of trade. By 1984, the merchandise trade deficit at 1978 prices of both imports and exports would have been a fraction of the deficit that was actually registered in current prices.

Or take the case of Brazil Dias Carneiro' cites a study by Bacha,s who has calculated that from 1979 to 1981, domestic policy actions to control the current account were practically compensated by the intensity of internal shocks, and that in 1982 and 1983, the effects of domestic policies were overridden by external shocks.

The international community has still to find a satisfactory way of insulating a developing country engaged in a relatively successful adjustment effort from the disruptive consequences of international price movements that are entirely beyond the control of that country. The absence of a satisfactory facility to deal with this problem simply complicates the political economy of the adjustment process, at least in a Third World democracy. It is not too difficult for an incoming government to call upon its electorate to support austerity measures and restraints in real wages if it can hold out and achieve a credible prospect of rapid growth and increased employment over the medium term. In the Sri Lankan case, it was certainly this prospect which made the initial food subsidy cut politically feasible. However, it is a very different thing for a country to be called upon to make repeated adjustment efforts and experience repeated cuts in living standards simply because the terms of trade turn against it for reasons not of the country's own making.

More than anything else, it is the failure of the international system to provide adequate compensation for terms-of-trade losses that has cast the Fund and the Bank into a role more resembling the awkward policemen of the system than Sidney Dell's kindly grandmother.° According to Dell, Fund conditionahty as it is practiced today is actually a latter-day graft. This is not to say that conditionality per se is undesirable. What is undersirable is the need to administer repeated doses of conditionality simply because the international system has not so far developed the means to control an external economic environment that is beyond the control of any particular developing country. It is this prospect, and the relatively short-tern nature of Fund adjustment programs, which involve repeated bouts of austerity, which has inspired the Baker Plan for growth-oriented conditionality as a way of providing a more durable approach to the debt problem.

The Case for a Dual Exchange Rate

There is a second area of Fund policy as it emerges from the country studies on Tanzania and Sri Lanka. Insistence on a substantial and politically infeasible devaluation may exacerbate a balanceof-payments disequilibrium that might have been corrected on the basis of a more flexible approach to exchange rate management. Paul Streeten said at WIDER's recent Hunger and Poverty Conference in Helsinki' ° that what was worse than getting prices right was to get key prices absolutely wrong for a long enough period. The principal price he had in mind was of course the exchange rate, and the notion that if it were allowed to get out of line for too long, not only would eventual correction be

unnecessarily painful, but also avoidable economic costs would be incurred in the meantime.
Now, the political economy of getting an exchange rate right has invariably to be country-specific. For example, if a sharp devaluation results in a compression of real wages unacceptable to the country's trade union movement, then the result is a wage/price spiral that can rapidly negate the export incentive effects of the devaluation. Such was perhaps the experience of Britain after her 1949 devaluation, or so Nicholas Kaldor" has argued. His own suggested remedy for this is a dual exchange rate system.
This is a system where a relatively appreciated rate, in terms of (for example) Sri Lankan rupees per dollar, applies to essential wage goods imports and to price-inelastic traditional exports such as tea. A more depreciated second rate would apply to imports that are deemed inessential and to exports the country wishes to promote, such as manufactures, textiles, and light engineering products, all of which are relatively price-elastic. A dual exchange rate system can be so devised as to provide adequate import substitution domestically for imported wage goods such as rice and to prevent arbitrage between the two exchange markets.
A dual exchange rate system was in operation in Sri Lanka from 1966 to 1977 and underpinned a long period of basic needs achievement in the country. The protection to wage goods and living costs it provided was complemented by the fiscal discipline that characterized budget making for much of this period. The balance-of-payments problems of the country were, for the most part, externally induced and the result of adverse terms-of-trade movements.
When this exchange rate regime was first negotiated, the Fund's position was that it was the wrong step in the right direction; but it was the peculiar sensitivity of that 1966 Fund negotiating team to Sri Lanka's political matrix that made the deal possible.
Contrast this approach with that of the Fund to Tanzania in recent years. The key problem in Tanzania has been the long-term concern of the authorities with the implications of a devaluation on the price of sembe, the basic staple in Tanzania. The program proposed by the Fund in 1952 for Tanzania would have had the effect of raising the price of sembe very substantially, to the point where it would have sparked off major social unrest. Had consideration been given to a dual exchange rate regime, it might have been possible to negotiate a program with a fair balance between an increase in the price of a staple and the other manifest advantages of getting the exchange rate right. The question, therefore, is why is the Fund today not willing to encourage the kind of wrong step in the right direction to which it reluctantly conceded in Sri Lanka in 1966? The evidence of the Tanzanian experience, dealt with very comprehensively by Benno J. Ndulu,' 2 shows that a failure to come to terms with the Fund has cost that country a great deal in terms of output foregone, which a different, more flexible approach on the part of the Fund might have prevented.

Merger of Bank and Fund?

A final issue at the level of the general reform of the international financial institutions relates to the resources that the Fund alone can provide.
When the IMF was set up, the sum of its quotas, which represented its lending power, were around 15 percent of world trade. This figure is now down to around 2 percent, and there is evidence to suggest that much of the tightening up of Fund conditionality over the years has occurred in an attempt to ration out this reduced availability of resources among a variety of competing countries.
One of the questions that arises is whether the case for an increase in the resources available to the international lending institulions could be more fully met by their merger into a single institution. The argument in favor of this move is powerful. We have today repeated instances of cross-conditionality, that is, of conditions imposed by the Fund being either reinforced or negated by those imposed by the Bank. The rule of thumb that is evidently now practiced is that a standby with the Fund is a necessary prerequisite for a structural adjustment loan from the Bank. While this corresponds to the demand management and planning roles into which these two institutions have been respectively cast, one can only divide their institutional responsibilities in this way at the cost of much logical untidiness. In the case of most developing countries, the adjustment problem (formally the problem of the Fund) and the development problem (formally the problem of the Bank) are telescoped together.
One of the arguments against substantial exchange rate devaluation of the conventional kind is that the structural rigidities of developing countries prevent the necessary resource shifts needed to improve their balance of payments from occurring automatically. In the case of the typical developed country, there is enough domestic capacity to support a switch from the domestic to the external market by the relative price effect of an exchange rate devaluation. In the typical developing country, such relative price changes have to be accompanied by major investments, some in the public sector,

which take time for their balance-of-payments benefits to be realized. In a developing country, therefore, exchange rate revisions ought to be approached in a spirit of gradualism rather than through major jumps.

The argument for merging the Bank and the Fund rests essentially on the notion that a coherent understanding of the development process in a country is best achieved through an understanding of its adjustment/development program as a whole, which today, for many of us, defies institutional separation.

It must be recognized that there are powerful counterarguments to this proposal which certainly carry weight with the developing countries. Ass things are today, the existence of two institutions is held by many to widen the options available to the developing countries in their negotiations. This freedom will be absent, presumably, in the case of a single monolithic institution.

If, however, a single institution is presumed to have an overall advantage in approaching the adjustment/development question in a country as a whole, then there are ways in which these advantages can be preserved consistent with maintaining a legitimate concern for developing country interests in decision making. One line of approach, already canvassed in the Commonwealth report on the Bretton Woods system," is simply to leave decisions on country programs to the level of staff assessments, without requiring a board decision on matters where more political approaches may tend to predominate. An alternative approach, mentioned by Dragoslav Avramovic,14 is for debtor countries to "obtain a fair share in relation to paid-up capital proportion, of the key policy making and management posts in the institutions. These posts will still have to be filled by staff of first-rate professional quality. But the approach proposed here would assure that the 'mind-set' now dominating the leading institutions would be modified to accommodate different theories of economic policy." Clearly, therefore, the case for a single institution rests on having' the right kind of institution in place, and detailed work in this area would need to be done.

The last major recasting of the present international institutions came in the wake of postwar idealism in search of a better world. One would hope that a similar major reconstruction need not have to wait upon yet another international crisis.

Notes

I. This paper makes frequent reference to work presented at the WIDER Conference on Stabilization and Adjustment Programs and Policies held in Helsinki on August 19.21,1986, referred m hereinafter as the WIDER Smblization Conference.

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CHAPTER 5

Alternative Macro Policies, Meso Policies and Vulnerable Groups

Frances Stewart

Macro policies are those policies directed at the macro aggregates in the economy. They include, for example, the money supply, the budget surplus/deficit, the level of government expenditure - in fact, all the variables that form part of most IMF adjustment packages. Analysis of the impact of recession and adjustment policies on vulnerable groups has shown how important macro policies are in influencing the conditions of vulnerable groups in both the short and the medium term. Consequently, an essential element in any strategy for adjustment with a human face is to ensure that, at the very least, the macro policies do not, through their negative effects on vulnerable groups, undermine other human-face policies being introduced and, at best, contribute directly to the improvement of the conditions of vulnerable groups.

Tfus paper considers how protection of the vulnerable will affect the design of macro policies. It should be emphasized that the aim is to develop organizing principles, not detailed programs, because the latter must depend on the specific circumstances prevailing when a country program is designed.

Macro policies have both an immediate direct impact on vulnerable groups (e.g., by altering the level of employment and/or food prices) and also a longer-term effect as a result of the impact on the pattern and rate of growth of the economy.

There are three major ways in which vulnerable groups may be affected by macro policies:

a) Through the impact on incomes of low-income households by affecting wage and employment trends in the formal sector and, more indirectly, income-earning opportunities in the informal sector. Macro policies affect rural incomes primarily through their effects on the terns of trade of the agricultural sector.

This paper coma from work by UNICEF on these questions, to be published as Adjustment With a Human Face: Protecting the Vulnerable and Promoting Growth (forthcoming).

b) By affecting the availability and price of major items of consumption allow-income households, especially food.

c) Through the impact on levels of government expenditure relating to vulnerable groups, especially in the social sectors.

Analysis of the impact of conventional policy packages on vulnerable groups has shown that in the short run, these have often been associated with negative impacts on each of the three elements, although causal responsibility as between the economic difficulties which necessitated the adjustment and the adjustment policies themselves is not clean Real incomes and employment, especially in urban areas, have typically been depressed during the adjustment process; food prices have risen; and government expenditure on the social services has often been cut. However, in some cases, rural incomes have risen, at least relatively, as agricultural prices were raised. Moreover, many countries with conventional adjustment packages have continued to experience declining incomes.

It is because of such negative impacts that it is necessary to introduce explicit policies to protect vulnerable groups during adjustment. In addition to specific micro policies, adjustment with a human face requires alternative macro and mesa policies which

xplicilly recognize the need to sustain the living standards of the most vulnerable in society.

Growth-oriented Adjustment

The objective of protecting vulnerable groups during adjustment implies protecting the vulnerable immediately, when the policies are introduced, not waiting until general economic growth is resumed. But such protection is unlikely to be sustainable in the face of prolonged decline in per capita incomes - of the dimension, for example, that is likely in sub-Saharan Africa for the rest of this decade. The experience of Jamaica in the 1970s showed how economic decline eventually undermined strong commitments to protect the vulnerable. Consequently, a critical element in adjustment with a human dimension is halting the decline in per capita income, For countries where conditions of the most vulnerable are very deficient - for example, in Ghana, where only 30 percent of the population have any access to health services, where sanitation and water facilities cover less than half the population, and where incomes of poor households are grossly inadequate to meet minimum food needs - bringing the conditions of the poor up to tolerable levels will be possible only

if economic growth is restored.
Economic growth may improve the conditions of the vulnerable through the three mechanisms described above.
First, improving employment and wage levels in the formal sector indirectly expands earning opportunities in the informal sector, which provides intermediate goods and services for use by the formal sector and supplies consumer goods and services to wage earners in the formal sector. Economic growth can also increase peasant incomes.
Second, improving supplies of food to the vulnerable is indispensable. Economic growth is generally associated with improved supplies of food and other basic wage goods and less rapid rises in their prices. In countries with a large agricultural sector, growth in domestic food production is likely to form an important aspect of achieving aggregate growth. Where countries rely heavily on food imports, improved economic growth will increase the capacity to import food.
Third, economic growth increases taxable capacity and, consequently, governments' ability to provide basic health and educational services.
Unless offsetting measures are taken, deteriorating per capita incomes tend to have adverse effects on all three mechanisms. Consequently, adjustment with growth is an important aspect of adjustment with a human face. The recent advocacy of growthoriented adjustment initiated by U.S. Treasury Secretary James Baker and now being explored by the major financial institutions is therefore a very important aspect of achieving adjustment with a human face.
However, it is apparent from examining the mechanisms connecting economic growth with the welfare of vulnerable groups that while growth is conducive to improved welfare of the poorest, this improvement in welfare does not automatically follow from accelerated growth. Capital-intensive patterns of growth in the industrial sector associated with slow employment growth and deteriorating urban income distribution, or agricultural growth which is based on inappropriate mechanization and associated with deteriorating rural income distribution, leads to growth with minimal trickle-down and little or no improvement in the condition of the poor. Agricultural growth consisting of expanding nonfood cash crops (as in the recent history of Brazil) may mean that growth is accompanied by falling food supplies and rising food prices. Expanding tax capacity may be accompanied by little change in expenditure on basic services to the poor. Consequently, while growth-oriented adjustment is, typically, a necessary condition for achieving adjustment with a human dimension, it is not sufficient. Even with a broadly appropriate pattern of growth, it may be necessary to take explicit action tp ensure that growth is equitable and that the vulnerable participate, not only in terms of employment and household incomes, but also in terms of their access to social services. Therefore, policies need to be designed both to achieve growth-oriented adjustment and to include specific actions directed toward human needs. Sectoral policies and specific measures focused on the poor will be needed.

External Finance

It is obvious that in general, a higher level of external finance would make it easier for countries to secure these objectives. More external finance reduces the need for short-Arm disabsorption, permitting structural adjustment to take place over the medium term without increasing short-term unemployment. More external finance also eases the need for downward adjustment of investment, government expenditure and consumption.
The acute economic and social problems of the 1980s have arisen in part because of the collapse of international lending. In both Africa and Latin America, the large amount of net lending in the 19705 was replaced by a net outflow of funds in the I980s.

TABLE 1
Net Transfer of Funds to Africa and Latin America
1977-78 and 1984-85
(USS Billions per Year)

	1977-78	1984-85
Africa	+8.6	- 5.4
Latin America	+4.9	-59.0

NOTE: Calculated as curacnt account balance less interest payments. SOURCE; IMF, World Economic Outlook (April 1986), table 55.
To achieve our objective in a comprehensive (i.e., across many countries) and sustained way will certainly be more attainable with, and may require, a reversal of this fmancial squeeze. In some poor

countries, resumed growth may not be possible without substantially more external finance to pay for essential intermediate inputs. Analysis of the recent experience of both Tanzania and Zambia suggests this to be the case in these countries.

As the Baker Plan recognized, extra finance is an essential element in securing growth-oriented adjustment. The need to protect vulnerable groups provides a further urgent reason for more finance.

However, while extra finance is highly desirable - especially to secure growth - this does not mean that countries can do nothing to achieve adjustment with a human face until there is a major change in the financial commitments of developed countries. Countries can

a) By their own actions affect their own financial situtation. b) Within given financial limitations, greatly improve their achievements by the policies they adopt.

Country Policy toward Financial Flows

The net transfer of external finance received by a country consists in the following net balance:

Positive	Negative
+ Gross lending (private and public)	- Amortization
+ Gross grant aid	- Interest payments

Governments have some control over each of these items – a control which varies with the particular circumstances of the country.For example, a country with a good credit rating may choose to increase its gross borrowing. This was the policy adopted by Brazil in the I970s, permitting investments in large import substitution projects, which resulted in improving the trade balance in the 1980s.Similarly, South Korea chose to borrow both in the 1970s andI980s, which allowed adjustment to take place with less deflation and unemployment than in the absence of borrowing. In the 1970s some countries borrowed in order to avoid making necessary adjustments. This may protect vulnerable groups in the shortt run, but unless the adverse shock is rapidly reversed, it leads to more problems in the medium term, since countries are then faced with two problems: the initial adjustment problem, and a debt problem arising from the borrowing. This is in fact what happened to some countries in the 1970s. This strategy, obviously, is not being advocated here. Rather, the objective is to borrow to permit adjustment to take place more slowly and less painfully, with less deflation and unemployment than in the absence of borrowing. Such slower adjustment makes it easier to protect the vulnerable during adjustment and also promotes medium-term growth, since levels of investment can be maintained. The choice of greater external borrowing and less deflation is an option only for those countries which have not seen their credit ratings reduced to near zero following the accumulation of debts combined with ineffective adjustment.

Countries which have accumulated a large amount of debt have some choice over rates of amortization and interest, which they may exercise unilaterally (e.g., the recent experience of Peru) or by negotiation (the recent experience of Mexico). Rescheduling of amortization in particular offers a changing time profile of net financial flows which potentially extends to most of the seriously affected countries. Especially if combined with >ome debt relief, it could considerably improve countries' access to external resources. For example, a major rescheduling would greatly improve Ghana's medium-term prospects, while without such rescheduling, debt service obligations may reach over 60 per cent of export earnings. To some extent, the debt rescheduling option depends on agreement from creditor countries. However, farsighted creditors should be prepared to accept a rescheduling which offers a high probability of restoring economic viability, and therefore, long-term repayment capacity. More generally, international mechanisms should be adopted relating debt relief to country needs - with special attention paid to the relationship between debt repayment schedules and the health and nutrition of vulnerable groups. Former Tanzanian President lulus Nyrere asked, "Must we starve our children to pay our debt?" The aim - at a country level and an international one - must be to devise policies which avoid this.

Aid flows are likely to be greater if a country shows its determination to adopt policies which protect vulnerable groups. A UNICEF study of Ghana suggestedd an additional annual cost of $65 million per annum for a more human-oriented adjustment program. It seems likely that donors would finance some of this extra cost for the human, economic and political advantages that would follow. In Botswana, aid donors have met 50 per cent of the costs of drought relief measures.

For these reasons, it seems that the finance limitation should not be treated asimmutable, either from the perspective of individual countries or from that of international aggregates.

Alternative Macro Policies

The assumption of a given external fmagcial constraint in the short term makes the options more limited. But reallocation of resources and incomes within a given total can improve the fulfillment of priority targets and may even, in certain circumstances, ensure better achievement than with more resources, but less attempt to direct resources to priority areas. This was indicated, for example, by--- the successful achievements - on basic needs as well as in the war effort - in Britain during the World War II. Consequently, in times of strict resource constraints, macro policies must be designed to ensure that the major priorities for protecting vulnerable groups and promoting growth are met despite the resource limitation.

Broadly, there are two categories of priorities - those related to achieving growth, and those related to protecting vulnerable groups. For each, the precise activities included will vary according to the circumstances, but some generalizations are possible.

In the growth priority, investment is the most obvious item, including investment in infrastructure, in "productive" sectors and in human capital. Not all investment is equally productive, and some investments are actually unproductive. So the growth priority includes only those investments with positive social rates of return. Intermediate inputs are also essential for growth.

The human dimension priority covers all expenditures related to the income-earning capacity of very poor households, to the basic health, education and sanitation services they receive, and to their nutritional status.

The precise dividing line between priorities is bound to be a bit arbitrary and subject to much political debate. But the extremes will usually be easy to determine. Even though it is unlikely that any country will come to universal consensus on priorities or be able to execute any agreement on priorities comprehensively and without exceptions, the attempt to plan according to priorities will improve resource allocation from the perspective of protecting the human dimension compared with normal decision making.

Macro policy packages generally take the form of target values for selected priority instruments - e.g., exchange rate, tax x levels, budget deficit, credit creation. Adjustment with a human face has implications for the selection of instruments, targets and performance criteria. Moreover, these macro variables can be associated with a variety of sectoral or micro implications - e.g., the same tax burden expressed as a proportion of GDP may fall on direct or indirect taxes, on the rich or poor, or on industry or agriculture. These will be called "meso" implications, to distinguish them from macro aggregates or micro projects. Generally, conventional adjustment packages take a broadly neutral view of meso implications, allowing them to occur as determined by the normal workings of the system. Adjustment which combines growth and the human dimension, in contrast, is predominantly concerned with the meso implications in order to ensure that these objectives are met to the maximum possible extent in the context of any macro policy package.

There are, then, three types of policy interventions which help to achieve the objective of growth-oriented adjustment with a human dimension

a) Policies determining the levels of macro variables, which are directed at influencing macro aggregates in the economy. These include levels of taxation and government expenditure, of credit creation, the exchange rate, etc. They are intended to influence the level of national income, the rate of inflation, the external balance. These are the variables normally defined as forming part of the macro policy package.

b) Meso policies, or policies that influence the allocation of income and resources within a given macro policy package. These concern the distributional and allocational impact of particular macro variables (e.g., the distribution of government expenditure, or of taxation).

c) Policy reforms and institutional changes which are likely to improve the performance of given macro and meso policies (e.g., by increasing female participation).

Macro Policy Variables

The choice of instruments, the targets chosen and performance criteria need to be selected taking both growth and human objectives and priorities into account. The appropriate policy package will vary according to country circumstances and therefore cannot be laid down here. However, some general points need to be made.

Deflation

Adjustment with a human face would try to minimize deflationary adjustment - i.e., adjustment achieved by compressing domestic expenditures more than the amount likely to be absorbed by the production of additional exports. The approach would aim to minimize this type of deflation, because it is a significant source of adverse developments for vulnerable groups and for growth (through rising unemployment, reduced incomes, reduced government expenditures and depressed investment).

Deflation of domestic expenditure is typically designed to achieve three objectives. The first is to reduce domestic absorption so that more resources may be devoted to exports and/or import substitutes, which is essential to improve the external trade balance. For large changes in the trade balance, such domestic disabsorption is essential. Where an improved balance may be achieved by increasing supply instead of depressing demand, it is clearly preferable. However, additional supply usually requires investment in new capacity and is therefore possible only in the medium term. In economies with much unused capacity, this can be a short-term policy which does not require deflation. However, typically, there may not be much excess capacity of a dnd which can immediately be used to produce extra exports or import, substitutes. Hence, disabsorption may be necessary to release resources for improving the external balance. But in many countries there is little short-term flexibility in domestic resource use. In the short run, resources cannot be transferred, for example, from producingmaize for domestic consumption to producing coffee for export, or from building clinics to exporting textiles. Rapid and low-cost resource switching on a large scale is possible only for countries with highly flexible economies, which generally means economies with well-developed manufacturing sectors. For others, investment, and therefore time, is necessary. It follows that the short-runn potential of using domestic disabsorption or deflation to achieve the resource switch and improved external balance is limited in many economies.

The second objective of deflation is to depress domestic consumption and investment so as to reduce imports. This can be very effective in improving the external balance quickly. It has occurred in Jamaica since 1983, for example, and in Botswana in 1980-81. But it is costly, since it typically hurts vulnerable groups and depresses investment. Moreover, it produces only a temporary improvement in the external balance, which will be reversed once the deflation stops. However, in the absence of sufficient bridging finance, it may be necessary to attain temporary improvement while more mediumterm measures to improve the capacity to produce exports and/or import substitutes have time to take effect. But great care is needed to ensure that short-term deflation does not impede the mediumterm efforts by reducing human and physical capital.

The third objective of deflationary policies is to reduce the inflation rate. In some cases, controls on credit creation have been advocated even where the external balance is satisfactory in order to achieve inflation control. On balance, adjustment with a human face would put 19ss weight on inflation control as an objective in its own right and give it substantial importance only where the inflation itself is clearly threatening the vulnerable.

It follows from this discussion that domestic disabsorption (or deflation) may have a role to play, but our approach would aim to minimize that role and seek bridging finance in order to do so. Typically, then, macro policies to protect the vulnerable might be associated with higher budget deficits (or slower reduction in deficits) than is the case in the more orthodox packages.

While limitation of external resources may necessitate some deflation in the short run, countries have succeeded in combining adjustment with economic growth - with only short periods of rising unemployment - showing that appropriate policies can reduce this deflationary element. The experiences of Brazil and South Korea both illustrate the possibilities. By adopting import substitution policies in major sectors, by expanding sectors (e.g., construction) with low import coefficients, and by promoting exports, improvement in the trade balance was achieved without massive underemployment of domestic resources. It will be more difficult to achieve this in countries with more rigid structures, and especially in those highly dependent on primary exports, but even in these contexts there is normally some possibility of changing the structure of output so as to reduce the necessity for deflation.

Taxation

Adjustment with a human face requires that the impact on vulnerable groups be explicitly considered for each policy instrument. This would be likely to mean higher levels of government expenditure (and taxes) where these are essential for vulnerable groups. The level of taxation (and government expenditure) may vary considerably, consistent with any particular target budget balance. Some priorities are almost invariably in the public sector (e.g., primary health care, primary education, sanitation, economic infrastructure); some are of a type which is generally in the private sector (small-scale farming and industry); andd some may be in either sector (e.g., drug production, transport). For quintessentially public sector activities, priority achievement may require a higher level of expenditure (by central, regional or local government) accompanied by higher levels of taxation or by charges to finance it. Higher taxation is normally necessary where taxation and public expenditure have fallen to very low levels both absolutely and as a proportion of GOP, as in Ghana in 1983, when government expenditure had fallen to less than 5 percent of GDP. There is great variation across countries in the proportion of GDP accounted for by taxation and other sources of government revenue. Among developing countries, Ghana's low of 5 percent represents the bottom of the range, while ratios of around 30 percent are found in a few countries (e.g., Egypt,.Yugoslavia, Trinidad and Tobago).

Policies towards privatization and a reduced role for the public sector should, inter alia, take into account the impact on vulnerable groups. Decisions on exchange rate changes should also explicitly take this perspective. This would often mean a more gradual change in order to avoid sudden, large distributional changes. In general, explicit consideration of the implications for vulnerable groups would be likely to alter the chosen policy mix and the pace of adjustment.

Compensatory Action

Where policy instruments can be shown seriously to hurt vulnerable groups, they should be introduced only if accompanied by compensatory action. These compensatory measures should be regarded as an intrinsic part of the policy package and their costs included as costs of the package. For example, devaluation and raised producer prices for the agricultural sector often lead to higher food prices and reduced real incomes for low-income urban households and for agricultural laborers. Where -such changes seriously hurt vulnerable groups, they should be introduced only if accompanied by compensatory changes in incomes or food subsidies for low-income households. Where such compensation is not possible, alternative policies, e.g, export subsidies, import taxes or multiple exchange rates, should be considered.

Monitoring

Program monitoring and performance criteria should include the welfare of vulnerable groups (e.g, as measured by nutritional indicators and the real incomes of those below the poverty line) and also growth-related indicators (e.g., levels of investment and growth in GDP).

Meso Policies: Priorities and Selectivity

These macro aggregates themselves have direct implications for the achievement of our objectives. But any given macro aggregates - e.g, budgetary balance or GNP level - may be associated with many different levels of achievement with respect to the two priority areas, as shown by the fact that some low-income economies manage to attain higher levels of basic services for the most vulnerable than some high-income societies. The normal adjustment package has targets for macro variables but is not concerned with the allocation of these items to priority and nonpriority areas. In the human-face approach, the effect on resource and income distribution as between priority and nonpriority areas is critical.

Consequently, whatever the policy package, the macro policies must be married with their consequences for distribution of resources between prioritiess and meso policies must be designed so that the two together (the macro policies and the meso consequences) protect vulnerable groups during adjustment.

To illustrate the position, macro targets may be thought of as dictating the speed of a wheel (rotations per second). The consequences of this rotation for the rest of the system will depend on the size and number of cogs on that wheel and other wheels linked to it. While timing the speed of rotation may be broadly determined by external finance, the meso consequences can be greatly altered by altering the dimension and number of associated cogs and wheels. The approach may be summarized as combining macro instruments with selectivity.

In practical terns, this approach means that all expenditures/ incomes affected by macro policies and relevant to the achievement of growth and the human dimension can be divided into priority and nonpriority elements. A threefold classification is suggested :

Priority I : Activities/resources/expenditures/incomes essential for the achievement of growth and the protection of the human needs of low-incomegroups.

Priority II: Intermediate items.

Priority III : Activities, etc., definitely not related to the above.

The precise dividing line between categories 1, II and 111 is bound to be arbitary. This is one reason

why an intermediate category (II) has been proposed- this category would include all "ambiguous" items. The aim would be to include as many category II items possible.
Despite the problems of categorization, it is nevertheless possible to divide incomes, expenditures, etc., into three rough categories. Some types of expenditure or income are obviously not of top priority for meeting the needs of vulnerable groups (e.g., luxury consumption items), while others would certainly be somewhere in the top priority (e.g., vaccines). A completely watertight and acceptable categorization of all items will never be possible. However, a rough ordering can greatly improve achievement of the objective in a resource-constrained setting.
The aim of any strategy devoted to achieving growth and protecting the vulnerable would be to achieve 100 percent of the priority 1 activities; as many of the priority II as possible; and, until all land 11 are achieved, as few of priority III as possible. Each policy instrument would be used to achieve this objective. Economies vary in the instruments they have, and therefore, in how this approach would be interpreted in practice. However, all governments have some instruments influencing the allocation of activities and the achievement of priorities. In a human-face approach, these instruments would be used explicitly to achieve the objectives of protecting the vulnerable and promoting growth. How this would operate will become clearer in a brief consideration of particular policies.

Meso Policies

Each meso policy is concerned with improving the impact of a given macro variable on the allocation of resources and/or the distribution of income so as to better achieve the priorities. Some policies achieve this primarily by affecting the availability (supply) of goods and services, and some more indirectly, by affecting income distribution and consequently, demand.
Supply variables include decisions on the allocationn of public expenditure, of aid and the distribution of credit. Policies affecting demand include policies toward taxation and subsidies and toward incomes. Price controls and policies toward import tariffs may affect both supply and demand.
The actual range of policy instruments varies with the country. For example, controls (e.g., over imports or investment) are used in some economies, but not elsewhere, and the same is true for price control. There are an abundance of policy instruments - more instruments than objectives. Even economies with minimal direct controls exercise direct control over allocation of public expenditure and (together with aid donors) aid. Together; these often account for over half of all investment. Every economy uses direct and indirect taxes, and most have some subsidies, which together help achieve priorities in consumption. The human-face approach requires that, collectively, the available policy instruments be used to secure the stated priorities. Generally, this would be attainable with full use of existing policy instruments and would not require additional ones.
The same priorities may be achieved by different policy instruments (e.g., use of the price system or allocation by controls). In a particular case, the preferred instruments must depend on which instruments are available, how effective they are likely to be, and political preferences and constraints.
A brief discussion of individual policies will help to explain how they may promote the achievement of the selected priorities.

Policies to Influence Supply

Public Expenditure

Every government has direct control over allocation of public expenditure. In principle, prioritizing public expenditure - permitting all priority I and a minimum of priority III - is straightforward. Selectivity in public expenditure may involve bath intersectoral and intrasectoral allocations. In the former category, for example, defense spending may be reduced and social 'ector expenditure or food subsidies increased; or within a sector, expenditure on tertiary education may be cut while expenditure on primary education is expanded. A good deal of social sector expenditure and food subsidies are of a nonpriority nature - i.e., they go toward nonpriority types of expenditure, consumed mainly by middle-income groups (e.g., some hospitals). Consequently, reallocating between sectors may not help achieve priorities unless the intrasectoral allocations are also improved. The prime focus must be on meeting the specific needs of vulnerable groups (e.g., expansion of primary health care). Reallocation toward meeting these needs could be achieved by reallocation toward basic health care from within the health sector, from other parts of the public sector or from

private expenditures.
In practice, of course, there will be bureaucratic and political obstacles to complete rationalization of priorities along these lines. These may limit, but are unlikely entirely to prevetit, improved allocation.

Aid-Finance

Like public expenditure (with which it typically overlaps), discretionary project-by-project decisions are the rule in aid, giving rise to opportunities to be selective. Selectivity needs the active cooperation of aid donors, as well as initiative by the government. Moreover, the political and bureaccratic problems are likely to be at least as great as with public expenditure. Past decisions - already incorporated in half-built roads or hospitals, for example - are particularly difficult to change and may account for a large proportion of current aid flows. However, the potential for achieving priorities by reallocation within aid can be great. For example, an ILO mission in Tanzania found that additional finance for priority imports equivalent to 10 percent of imports could be secured by cutting back on nonpriority aid projects and switching half the amount served to general import finance.'
The choice of priorities to promote growth and the human dimension is likely to accord with the objectives of many aid donors. Together, aid finance and the public sector usually account for over half of investment decisions, and often for over three-quarters - so that the administrative tool for exercising priorities over much of investment exists even in nonplanned economies.

Private Sector Supply

Private sector supply may be affected by credit policy, producer price policies and other controls (e.g., over import allocation or investment decisions), where these exist.
Credit policy: The government can require that credit be allocated only to priority areas. This was an important feature of Killick's proposed alternative package for Kenya.' In Zimbabwe, an increasing proportion of agricultural credit has been given to small farmers. Credit for small-scale industry is an essential aspect of schemes to promote small-scale industrial activities. However, the availability of foreign finance can bypass domestic allocations, so that the policy would need to be supplemented with a review of the allocation of foreign finance to ensure consistency with priorities.
Producer prices: Many governments offer floor (and/or ceiling) producer prices for major agricultural commodities. Assuming that conditions exist to make these prices effective (i.e., absence of a black market, prompt payment of producers by the marketing authorities, availability of consumer and producer goods for purchase by agricultural producers at reasonable prices), producer prices are a powerful mechanism for influencing the agricultural terms of trade and the relative incentive to produce food as against other cash crops. Producer prices affect priority objectives by helping to determine the incomes of rural producers and the availability of food. They may simultaneously help rural vulnerables (unless they are subsistence producers or landless laborers) and hurt urban vulnerables (as food consumers). Careful analysis is therefore needed to determine appropriate policies. Rising food prices contribute to the long-term food supply objective and also to maintaining the incomes of small farmers while hurting low-income urban households and landless laborers. In the short term, special measures will be needed (e.g., food stamps) to protect these groups when raising producer prices of food.

Policies to Influence Demand and Real Incomes

Taxation

As discussed earlier, the protection of vulnerable groups would normally be helped by higher levels of taxationo and expenditure. Within any total, the tax incidence may be used to further the objective. Direct taxes influence the distribution of disposable income, with progressive taxation reducing the disposable income of upper-income groups, aa priority III item. But the extent of this effect is normally limited by administrative and political constraints. Indirect taxes and subsidies offer more potential: indirect taxes on luxury consumption items may reduce the disposable income of upper-income groups and consumption of low-priority goods and services, while subsidies on basic goods and services consumed by the poor increase the real incomes of the vulnerable and encourage a switch in consumption to priority items.

Consumer Price Controls

Some economies have a full array of price controls, but these are often ineffective when there are large imbalances between demand at official prices and supply, as is typical during economic crises. In such a context, therefore, consumer price controls may not be effective in achieving priority objectives. But where price controls are supported by adequate supplies, they may be used to ensure stable prices of basic commodities for low-income urban households. The conventional adjustment package often requires dismantling of some or all price controls. The approach suggested here would be to reduce the number of controls to a few on key basic commodities and to support control on these key prices by policies to generate adequate supplies. In fact, price control policies might better be considered as supply policies for key basic commodities, with any price increment being a symptom of failure of supply. The key commodities should normally include (i) a basic staple food, (ii) a basic fuel, (iii) soap and (iv) basic drugs.

Import Controls and and Tariffs

Import controls and tariffs can affect patterns of demand and supply. The lowest-priority items should be subject to very high tariffs or banned, while controls and tariffs should be reduced on priority items. As far as intermediate products are concerned (viz., parts, raw materials, etc.), the priority to be attached to the item depends on the priority of the final product. In economic crisis, this may involve reducing or even eliminating supplies to some industries.

Wages and Employment Policy

Wages and employment policy directly influence the incomes of employees. Adjustment packages often reduce real wages and employment in the public sector. Such policies generally contribute to the stabilization objective by simultaneously improving the public sector balance (through reducing government expenditure) and reducing incomes and consumption, and therefore, imports. Whether some adjustment of this type is necessary depends on the macro balances in the economy. The effects of such policies on vulnerable groups depend on whether the government sector is relatively a high-wage or low-wage employer and how the policies are administered. Real wages can be reduced selectively so as to protect those on the minimum. If the incomes of vulnerable groups would be seriously affected by reduced government employment, then reduction, if essential, should be phased in gradually and compensatory employment provided as far as possible in the form of public works and the promotion of small-scale enterprises.

This brief (and incomplete) review of meso policies shows that governments have many instruments which could be used to attain the priorities that form an intrinsic part of protecting the human dimension and promoting growth in a resource-constrained context. These policy instruments are not new but are already in use, generally without systematic regard for their consequences for vulnerable groups and for growth. To some extent, this is a consequence of the politics of decision making, especially in crisis. But to some extent, it is due to lack of a systematic approach to attaining priorities.

Policy Reforms and Institutional Changes

These are changes designed to improve the design of adjustment policies from a human-dimension perspective and to make any given set of policies more effective in reaching vulnerable groups. They involve changes in national mechanisms associated with developing adjustment packages and increased empowerment and participation of vulnerable groups.

National Mechanisms

Traditionally, £mane ministries have taken the lead in the formation of adjustment policies and in negotiations with international institutions. Inevitably, this gives major priority to the stabilization aspects of the package, since these are the priority concerns of finance ministries. Extending the objective beyond stabilization to growth protecting the welfare of vulnerable groups requires that those parts of government concerned with these issues (development or planning ministries and the social sector ministries) form an integral part of the team which develops adjustment policies.

Thus requires that they be brought into the process of policy formation and consultation with international institutions at the initial stages and not at a late stage, when most decisions have been made. The precise mechanism for achieving this will vary according to country circumstances: interministerial committees or task forces reporting to the president or prime minister offer possible mechanisms. Similarly, international institutions concerned with development and the human dimension need to be incorporated into decision making on adjustment.

Empowerment and Participation

The empowerment and participation of vulnerable groups - especially women - is essential to secure the political commitment to get policies introduced and effectively implemented; to improve the design of policies so that they correspond to the needs and conditions of the people to whom they are directed; and to improve the efficiency of the policies in terms of their objectives. It has been established, for example, that public works schemes are more efficient
and have better distributional effect when local people are involved in their design.
Changes which assist in this empowerment and particpation include:
a) Developing institutions to assist in organization of the landless, women's groups, the urban poor, etc. (The Grameen Bank is an example.)
b) Providing financial support to community efforts.
c) Building requirements for consultation and participation into project design.

Conclusion

Giving clear priority to the protection of vulnerable groups in both the short and medium run has important implications for the design of adjustment policies. In general, it requires a less deflationary approach to adjustment and more access to finance, secured either by borrowing more or by deferring payments on existing debts. In choosing macro policies, the implication of each policy for vulnerable groups should be explicitly considered, and the effects on vulnerable groups should be systematically incorporated into the process of monitoring achievements. In order to maximize achievements where the use of resources is constrained, expenditures and incomes should be grouped into priorities and all policy instruments aimed at achieving the chosen priorities within a given resource constraint.
This approach to adjustment has implications for national mechanisms to develop policy packages. Those whose first concern is with vulnerable groups and with growth must be integrally incorporated into the process of policy formation. It also requires measures to increase the empowerment and participation of vulnerable groups.

Notes

1. ILOfJASPA, Basic Needs in Danger A Bade Need, Oriented Development Strategy fop TaneanW (Addu Ababa, 1982).
2. Tony Kil ick et al., The Quest for Stabilkatbn: The IMP and the Third World (London: Hein<msn Eduatio at Book,, 1984).

CHAPTER 6

Social Policy Making During Adjustment

Giovarmi Andrea Comic

This paper discusses some general principles that might be of assistance in the formulation of social policies during periods of adjustment. Indeed, a comprehensive discussion of these policies and of their articulation provides a thorough understanding of the main thrust of an alternative approach to social sector policy making during periods of adjustment.
A few clarifications are necessary to clear the ground of possible misunderstanding.
First, in order to provide a consistent perspective for the various types of measures described in this paper, it is necessary to examine the role the state and other social institutions should play during periods of recession and adjustment. The main objective of public policy during adjustment periods should consist in enhancing the redistributive role of the state, compensating not only for structural inequalities in the distribution of assets, incomes and opportunities, but also for the unequal

distribution of the burden of adjustment. One way to enhance such a role consists in expanding the supply to the poor of basic goods and services during a period of general contraction of the economy. The provision of goods and services in the areas of health, education and nutrition in particular has been shown to have positive redistributive effects.' A converging approach consists in the creation of buffering mechanisms, protecting the poor from the hardships provoked by the recession and the implementation of severe stabilization measures. Under such circumstances, special provisions need to be made, such as instituting labor-intensive public works schemes, subsidizing certain items, suspending the payment of given charges, etc. - often only for limited periods of time.

This paper has been dawn from a chapter of the book AQiustment With a Human Fare: Protecting the Vulnerable and Promoting Growth (UNICEF, forthcoming) and makes reference to numerous studies included in it. The sections of this paper on the topics of community liwndng and targeting were facpamd by Frances stexart.

Second, the relation between economic and social sector policies during periods of adjustment should receive closer scrutiny, in many, if not most, cases these two sets of policies are regarded as independent from one another. Economic policies receive the lion's share in terms of overall priority and resource allocation. In addition, the formulation of social policy generally takes place within a preestabiished macroeconomic framework which pays very little attention to distributive and welfare issues. This situation is often responsible for the failure of adjustment policies to generate adequate social support.

This situation clearly requires important modifications. To start with, the separation between economic and social policies should be rejected. Economic policies do influence human welfare, and that of children in particular. In food-importing countries, for instance, devaluation negatively affects the food consumptionn and nutritional levels of net food buyers. Social policies also influence economic performance. Reduction in health care expenditure and in nutritional support for the poor, for instance, represent a typical case of disinvestment in human resources with adverse effects on both nutritional levels and short- and long-term production prospects.

Social policy making should not be seen, therefore, as an appendix to but as an integral part of the overall process of policy making during adjustment. In this regard, it is necessary that macro-economic decisions concerning resource allocation, pricing, expenditure cuts, etc., be seen in terms of their potential effects on human ecology. So far, this has not often occurred, in Brazil, for instance, the substitution of oil imports with alcohol extracted from sugar cane had a negative impact on average calorie intake. To produce 50 liters of alcohol for car engines, one ton of sugar cane is needed, which in turn requires land equivalent to the amount needed to grow food for 200 people. The expansion of agricultural land used for growing sugar cane or export crops forced a drop in the cultivation of basic foods for domestic consumption, leading to growing shortfalls in calorie intake.' Equally, decisions concerning the social sector must be considered in terms of their support for restoring and sustaining growth. In other words, there is a need to formulate these two sets of policies in an integrated fashion.

The need for integration between social and economic policies becomes even more evident when considering the timedags with which various types of policies produce their effects. While macro-economic demand restraint policies have an immediate depressive effect on output, employment and incomes, supply expansion policies, part of the same adjustment package, require at least a few years before they start producing increases in output. Many households may therefore face long periods of deprivation, possibly with irreversible effects on small children and other vulnerable groups. There is a need, therefore, to bridge this gap. Appropriate social policies - such as instituting income-generating schemes and nutritional support - do have positive immediate effects that can offset the immediate negative effect of demand restraint policies.

Third, the articulation of social sector policies themselves should be discussed. Two points deserve particular attention. First, while some social policies aim at the whole population, specific socioeconomic, age and sex groups are affected by recession and adjustment far more severely than average. As such, they should be the aim of specific policy support. Social group analysis should thus be the basis for policy formulation. Besides allowing identification of those in need, such an approach is fundamental for the design of appropriate targeting. Second, social policy should not be limited to the provision of health and education services. As experience has shown, interventions in these two sectors alone cannot guarantee acceptable standards of living for poor children and their households. Food subsidies, income transfers, income generation, support to small-scale productive activities were in fact applied - if temporarily - in countries as different as Zimbabwe, Botswana, Peru, South Korea and Chile. In particular, the need for increased interventions in the area of food and nutrition was recognized in the majority of the countries analyzed. During periods of recession and adjustment, the scope of social policy must be widened.

Directly or indirectly, all policies toward the social sectors have implications in terms of efficiency, equity and level of resources. Broadly speaking, they can be grouped in two categories, i.e., those aiming at sustaining the flow of resources to the social sector, and those aiming at improving the efficiency of use of such resources.

Sustaining the Flow of Resources in the Social Sector

This section examines the available policy options for maintaining, and when feasible expanding, the flow of resources to the social sector during periods of adjustment.

Sustaining Budgetary Allocations to the Social Sector

Budgetary resources are known to be limited in most developing countries. In the early I980s, total government expenditure has been declining in about half of the developing countries for which information is available. However, except in cases like that of Ghana, where the decline in GDP, tax base, government revenue and total expenditure was so pronounced as to make any attempt to sustain any particular kind of outlay illusory, there almost invariably is scope for maintaining real levels of social sector expenditure. Whether the latter will decline or increase is largely a matter of political choice. In Sri Lanka, for instance, in 1985 food subsidies received an allocation of Rs. 1,700 million, while it was reckoned that the minimum needed to reach all the eligible was on the order of Rs. 2,5003,000 million. It was argued that the lack of resources did not permit a rise in the allocation to the required level. During the same year, however, the national airline received a subsidy of Rs. 1,000 million.
There are also examples where social expenditure has increased during general recession and adjustment. Jolly and Cornia,3 for instance, provide evidence of how real social expenditures were increased in South Korea during the 1979-81 recession. In Burkina Faso real per capita expenditure on health was increased between 1980 and 1983 by 3.6 per cent a year despite a sharp drop in GDP per capita and total government expenditure per capita. On the occasion of the budget speech in January 1986, the President of Indonesia announced that despite- a 50 percent cut in the overall development budget owing to sharp declines in oil and gas revenue, none of the child survival development activities (oral rehydration, immunization, support for breast-feeding, nutritional surveillance and education, vitamin A and iron supplementation, and family planning) would suffer any reduction, while the funds allocated to immunization were actually increased.' For many countries there is also evidence that in the second half of the 1970s' and between 1979 and 1983 the social sector was "relatively protected" from budgetary cuts as social expenditure declined more slowly than total expenditure.
In a number of cases, the flow of budgetary resources to the social sector has been sustained through the imposition of ad hoc taxes, the revenue of which was specifically to be used for social objectives. In Brazil, for instance, one of the federal government's responses to crisis was the creation in May 1982 of the Fund for Social Investment (Finsocial). Finsocial was fed by an additional .5 per cent tax on sales and a 5 percent surcharge on corporate income tax. It was designed to finance programs in the areas of food and nutrition, housing for the poor, health, education and support to small farming. In 1982, Finsocial collected resources for approximately US$ 300 million, while in 1984 the level reached almost US$ 1 billion. While the sales tax feeding Finsocial is likely to be regressive, the degree of progessivity of the expenditure has not yet been evaluated. Whatever its shortcomings, the Finsocial experience proves that considerable resources for the social sector can be mobilized in a relatively short period of time. More thorough utilization of the fiscal instrument (both indirect and indirect taxation) could generate important resources for sustaining priority expenditure in the social sector. This is true even in low-income economies. Increases in taxes on beer and cigarettes would allow many countries in Africa to rmance a good part of the local cost of primary health care.
There is a clear case, therefore, for arguing for a sustained flow of public resources to the social sector. The degree of persuasiveness of the argument could be greatly increased in particular cases if the request for funds were accompanied by specific indications as to their use. There is a also a case for arguing for a selective application of budgetary cuts when total government expenditure declines. As the examples wen above indicate, these cuts should be targeted so as to avoid impinging on basic services to the most vulnerable.

Introducing or Increasing User Charges

User charges were found to account for between 10 and 15 percent of total government health expenditure for the 17 countries for which information foryears between 1977 and 1983 was compiled by the World Bank." Researchers reckon that even under the most optimistic assumptions, such a share is not likely to surpass 20-25 percent of total government expenditure over the next five to ten years. At the same time, the share of private health expenditure in total health expenditure, including water expenditure, averages around 50 percent, with peaks of 80 percent and over. Thus, households already devote a substantial amount of their resources to health care and other services, with only a small fraction of this private expenditure going to the public sector, normally to pay health workers and buy drugs. A similar picture would emerge with respect to user charges in education, water and other social sectors.

During recent years there has been an increasing tendency to present user charges as a possible way of alleviating the resource constraint provoked by the economic decline of the 19805,' and there is currently evidence of rising charges in sectors such as health, water, education, etc., in many countries.

However, the potentially regressive nature of user charges should be emphasized, as in many developing countries the need for health care, education, etc., rarely coincides with the ability to pay for it. Raising charges in these sectors will have an adverse effect on vulnerable groups in three ways. First, it may lead to lesser use of services by vulnerable people. In the state of Bendel in southern Nigeria, for instance, after the reintroduction of school fees, primary school enrollment dropped from 90 to 60 percent during an eighteen month period ending in 1984.° Second, experience in the health sector shows that the introduction of fees tends to discourage the utilization of preventive services in particular (prenatal care, immunization, etc.), for which patients may not see an immediate relevance. Preventive services,_ however, have been shown to be much more cost-efficient than curative methods, and also to have the capacity of preventing in childhood specific adult health problems.' By reducing the utilization of preventive services, greater economic costs (for curative services) or welfare losses (death, illness, etc.) will be borne in the future. Third, for those who continue to use the service, the introduction of a charge will have a negative income effect which may adversely affect a household's ability to meet other basic needs (e.g., to purchase food). Raising charges during a period of economic recession has an even more regessive effect as households' incomes decline and their ability to rely on privatee health, sanitation, education and other social services is substantially eroded. For instance, in 198485 there was in the Philippines, a sharp increase in attendance at public clinics as the soaring cost of private care and declines in incomes made private services no longer accessible to many lowincome households.

The various social sectors, however, comprise different types of services, some clearly geared to the needs of the poor, others catering to the needs of the middle and upper class. While primary education, disease control programs and basic curative services are part of a basic needs basket and are therefore not well suited to the introduction of charges, the same cannot be said about university education and elective cosmetic surgery (which could be designated as highincome services). For the latter group of services, some form of cost recovery would be advisable in most developing countries. A report from the World Bank,' ° for instance, suggests that for most countries it would be efficient and equitable to shift a greater share of the cost of higher education to those who benefit from it. There is also a third category of intermediate services, including most curative health services, secondary education and others. For them, selective cost recovery based on an income criterion might be desirable.

It is also important to distinguish between nominal and substantial user charges. The former are principally intended to deter unnecessary utilization of services and aree not expected to generate large revenues. Their main purpose is to promote a more efficient use of resources. In the case of health services, for instance, too little time is often spent on essential services because valuable staff and supplies are overburdened with treating lower-priority cases. Substantial charges, on the contrary, aim at recouping a much larger part of the cost borne by the public administration and to generate important flows of revenues.

In conclusion, while a case-by-case approach is warranted, the preceding discussion suggests that

a) Cost recovery is not generally to be recommended (either for the poor or for the rich) for that group of public services that meet basic needs, including primary education, public health and preventive health measures, installation of public water points, sanitation, etc.

b) User charges should be introduced selectively (according to an income criterion) for the group of intermediate services comprising, for instance, secondary education, several curative and health services, piped water, etc. Low-income people should either be exempted or charged only nominal charges.

c) Finally, for high-income services, a large portion of the full economic cost should be recovered from all income groups.

Community Financing

Community financing presents an alternative to user charges or national taxation as a method of financing local services. Community financing has. been used for the construction of schools, clinics and sanitation projects and to meet recurrent costs.

A survey of over 100 self-financing health sector schemes" found nine principal methods of financing, including fees for services and drug sales, financing by contributions from production cooperatives, the use of voluntary labor, exchange of services, special incomegenerating activities and ad hoc fund-raising. The most common objective of the projects was to meet drug costs, followed closely by compensation for health workers. The schemes rarely met hospital costs, nor did they usually defray the costs of management or evaluation.

The effects of community-financed schemes on vulnerable groups vary according to whether the schemes are a substitute for or addition to nationally financed health services, the wealth of the community, and precisely how the schemes are organized.

Community-financed schemes have developed mainly in the rural areas, which are typically poorer than the urban areas. "Community financing ... places a significant burden on persons who have little ability to pay.... It does nothing to reduce disparities between town and country or among geographic regions; and as health services develop it may accentuate disparities."" In very poor communities, the vulnerable groups themselves bear the main cost of the schemes. However, insofar as the schemes supply additional services to those provided nationally (or prevent cuts that would otherwise occur), they may protect the most vulnerable (children, lactating and pregnant women, the sick) during the adjustment process.

The diverse methods of community financing have different implications for the protection of the most vulnerable.

a) Schemes relying on sales of drugs or payments for services are in way a form of "decentralized" user charges and suffer, therefore, from the shortcomings discussed above - i.e., they are regressive and discourage the utilization of services, particularly preventive services. However, a number of such schemes provide sliding scales or exemptions. For example, village health committees in Iampung, Thailand, issue fee exemption cards for the indigent. In some cases, it has been found desirable to let a committee determine exemptions, because health workers were pressured by relatives, etc. Sliding scales and exemptions have been rare for drug sales.

b) Community labor provided during the slack agricultural season has been widely used in construction and maintenance. In this way, even poor regions and communities may generate resources to meet their needs. For example, communities in one part of Ethiopia fenced and cleared 3,000 springs, built nearly 38,000 latrines and dug over 3,000 refuse pits. In most parts of West Africa, while governments finance the teachers' salaries, rural communities take care of the construction of primary schools. Community labor has also been used for productive enterprises which generate cash used in part to support social services. For example, the Eastern Clinic in Sierra Leone developed an oil palm plantation with a press and soap factory as a way of making money.

e) Fund-raising activities such as raffles, lotteries, ere., are another way of generating funds. In Carrizal, Costa Rica, a health committee raised $11,000 to buy land and materials for a health post.

In conclusion, community-financed projects can provide a valuable mechanism for helping to provide basic services provided that (i) the projects are additional to national supplies, not substitutes; (ii) the method of financing adopted allows the most vulnerable (low-income, children, etc.) to benefit from the services with low or zero charges; (iii) the schemes have adequate leadership, design and management; (iv) the finance generated by the local community is matched by outside support to provide essential inputs which are not available from local sources. This is particularly the case for teachers' and health workers' salaries and most purchased imports.

It is worth emphasizing the desirability of providing external support for local community projects. First, without some outside resources, the projects may not be viable at all, especially in very poor communities which can contribute labor, food and local materials but not enough finance to purchase inputs from outside the area. Second, external agencies (the central government, regional government, NGOs or official aid donors) may be able to help in design and management, which tends td be weak at the community level. Third, the known availability of some external source of finance to support local efforts may provide a powerful incentive to local initiatives. In an unsual experience in South Korea, 35,000 villages were supplied with cement and steel reinforcing rods to support village improvement projects in roads, bridges, wells and sanitation facilities. Each village was rated according to its accomplishments; those doing well received further, though modest, support, while those doing poorly received nothing. The Saemaul movement has transformed the appearance of South Korean villages, fostered the completion of a large variety of cooperative self-help projects, and promoted more effective working relationships both among farmers and between farmers and local officials.

Mobilizing International Resources

Besides its overall level, the effectiveness of external assistance is influenced by specific policies regulating its use. One such policy concerns counterpart funds and recurrent costs. A temporary relaxation in the rules regulating external assistance could result in increased (and more relevant) financing for the social sector.

At present, most projects require that local and recurrent costs be financed by the recipient country, while external assistance takes charge of the capital costs of the project. In periods of recession and adjustment, government budgetary resources are generally squeezed, and it is not uncommon that counterpart funds, usually intended to finance recurrent costs, are sharply curtailed. This leads to a decline in the utilization of projects already initiated, and newly allocated aid money frequently cannot be disbursed for lack of counterpart funds. Ironically, in this way, the negative effects of economic decline are compounded by the norms regulating aid utilization. As a result, clinics, schools and water systems (often built with external assistance) fall into disrepair, with almost no drugs or books or spare parts, and with absentee staff who may not have been paid for several months.

The refusal to meet local and recurrent costs has not only biased decisions toward capital-intensive and import-intensive projects but also reduced the rate of utilization of existing projects and the total disbursement of foreign assistance. As mentioned earlier, this vicious circle becomes particularly evident during adjustment periods, when both budgetary resources and foreign exchange decline.

This situation is now widely recognized, and it is increasingly accepted that new projects should not be launched until existing ones have been restored to fuller use. This implies the willingness, one way or another, to finance recurrent costs. The question at issue, therefore, is not whether or not to finance recurrent costs, but how and when.

A policy on local and recurrent costs could be articulated as follows

a) To start with, it is necessary to verify that there is a real local commitment to the project under consideration, and that after a few years the project can become self-sustaining. This means that under normal conditions, local counterpart funds should cover at least, say, 30-40 percent of the total costs of the project, and that local funds should be able to finance total recurrent costs after a few years. However, in order to avoid the capital- and import-intensive bias mentioned above, the choice (whether capital or recurrent) of what costs to finance with foreign assistance in the short run should be left to the recipient countries. Often, for instance, what is needed is not new projects, but revitalization of old ones. This requires funds for repair and maintenance and for recurrent costs rather than new capital investment.

b) The exceptional situation of countries either in deep recession or undergoing severe adjustment must be recognized. Their budgetary and foreign exchange situation must be thoroughly assessed before applying the above criteria. A degree of country differentiation appears to be necessary at this point. While middle-tohigh-income developing countries - with relatively well developed health, sanitation and school systems - may not require any change in recurrent and local cost policies, low-income developing countries of Africa and Asia ought to be treated differently. First, labor and other contributions in kind (construction material, current inputs, food, etc.) should be counted both as counterpart funds and recurrent inputs. Second, for a limited amount of time, recurrent costs both for ongoing projects and new projects could be met by donors. For instance, recurrent costs might be met for, say, three years, or on a sliding scale for, say, five years. The figures are only indicative and should be adapted on a case-by-case basis. Barring exceptional circumstances, after this "grace period" the project should become self-sustaining.

If these changes are accepted, one should expect an increase in the resources for adjustment in the social sector in low-income developing countries as foreign assistance previously blocked by the lack of counterpart funds is released for funding of both recurrent and capital costs of ongoing and new projects. Such changes would also result in an increase in the rate of utilization of existing projects and in a greater increase in the output of the social sector than when external assistance is used exclusively for new capital investment.

Improving Efficiency in the Use of Social Sector Resources

The measures described here aim at increasing the level of output and at improving its distribution for any given level of resources available to the social sector. The measures proposed broadly aim at maximizing collective welfare by increases in efficiency and equity and changes in the organizational make-up of the social sector.

Promotion of Self-help at the Household Level

At least 75 percent of all health care is estimated to take place at the family or individual level," with women having the greatest responsibility for promoting family health and nutrition. The degree of self-provisioning is lower in other social sectors - education, for instance. It is important to note, however, that in many societies there is scope for decentralizing many activities in health, nutrition, child care, sanitation and other services at the family (or community) level. This decentralization is not costless. Important efforts have to be made to mobilize public opinion and to create awareness of the need for the adoption of certain health, nutrition and child-rearing practices Governments, community leaders and foreign donors must often join forces to organize and sustain massive public education campaigns. Social communication aimed at the mother is the key element of this strategy. The current UNICEF approach to the treatment of diarrhea (the number one infant killer in the world) through home-based oral rehydration is an appropriate example. While until recently diarrhea was treated at considerable cost in health posts or hospitals by means of intravenous rehydration, the new strategy emphasizes home-based treatment consisting of two teaspoons of sugar and one teaspoon of common salt diluted in a liter of boiled water. All the ingredients of the oral solutions are generally available even to very poor families, while prepackaged mixtures of salt and sugar are produced industrially and sold commercially in many developing countries at extremely low cost (US 6-10 cents per packet). While such an approach may increase time cost for women to an extent," it places extremely modest monetary costs on the households and leads to substantial savings in the public sector, where a considerable proportion of beds, staff time and current inputs are absorbed by the care of diarrhea) disease.,Other areas where this approach can be applied include breast-feeding and weaning and growth monitoring.

Improving the Efficiency of Government Social Expenditure

Despite the conspicuous and growing shortage of budgetary and human resources, the social sector seldom utilizes them in an efficient way. Indeed, in many developing countries, the provision of social services is affected by a long series of biases in favor of expensive, urban-based, capital- and skill-intensive activities often modeled on those of the industrialized countries. As seen earlier, the capital intensiveness of such services is often influenced by donors' preference for financing capital costs and by the practice of tied aid. For these and other reasons, educational, health, sanitation and other services often cater to a relatively small, mostly urban, upper and middle class while bearing little relevance to the satisfaction of the most elementary health, nutritional and educational needs of the population.

In many countries, therefore, substantial scope exists for improvement in the efficiency of government recurrent and capital expenditure. For ease of exposition, such improvements are grouped into five categories.

a) As far as capital expenditure is concerned, there is the need to proceed to the selective rehabilitation of the social service infrastructure. Output increases obtained by rehabilitating existing infrastructure are generally substantially cheaper than those obtained through new investment. It is important to underline, however, that this rehabilitation should be selective in nature, i.e., starting from those facilities with the highest potential coverage and the greatest unfulfilled needs. Selective rehabilitation should also represent an occasion for restructuring social services away from expensive, high-tech solutions and toward low-cost and high-efficiency measures. In Ghana, for instance, in view of the expensive nature of hospitalbased care, the government should consider putting a stop to new hospital construction and to major extensions of existing capital. The resources so freed should be used for the rehabilitation of health posts and health centers.

b) Within each sector there is a need to restructure social expenditure toward the satisfaction of the needs of the poor majority. In the Philippines, for example, there was a serious misallocation of resources within the health sector, with total subsidies extended to five specialized health institutions catering to the upper class amounting to 229 million pesos, while government funds for primary health care totaled only 45 million pesos. Although not always so extreme, the problem of an excessive allocation of health resources to the hospital sector is to be found in many other countries. In Malawi in 1983, hospitals received over 60 percent of government health funds," while in the Senegal (1981-82) and Tanzania (1980), hospitals absorbed respectively 51 and 58 percent of the government health budgets.' 6 Intrasectoral misallocation of resources is typical not only of the health sector. In Burkina Faso, for instance, between 1980 and 1984 secondary and university education received on average a share of the education budget twice as large as primary education, although the latter covered a ten times larger school population," while according to a World Bank study, "in Francophone Africa two percent of each cohort in the population attain higher education and receive 40 percent of the public resources devoted to education."

Correcting such glaring misallocations is not simple. For technical and social reasons, capital and labor resources are only partially mobile. A large hospital cannot be fractioned into fifty primary health care posts. Neither is it easy to provide sufficient incentives to secondary school teachers from urban areas to take up service in a primary school in a remote rural area. Moreover, reallocation is easier at the margin during periods of overall growth of resources. Despite these difficulties, there is both a need and the possibility to redirect government social expenditure in favor of primary education, primary health care, the installation of communal fountains, etc. Such restructuring has happened in a number of countries. In Zimbabwe, for instance, the share of preventive health services doubled between 1979-80 and 1985-86. A similar shift in favor of primary education was noted in Zimbabwe during the same period. A study on the provision of education in Commonwealth countries" showed that attainment of the universal primary education target could be substantially accelerated by reducing unit costs in secondary and higher education and by shifting the resources thus saved to primary education.

c) The adoption of low-cost, high-efficiency measures for the satisfaction of the basic health, sanitation, water, education and shelter needs of the poor will substantially contribute to more efficient use of social sector resources. In the past, expensive techniques were used to deal with common problems. Several low-cost, high-efficiency interventions have been developed recently thanks to technological and scientific advances. Water pumps have become sturdier, cheaper and simpler to operate and maintain; vaccines are cheaper, more resistant to heat (thus facilitating their transport) and more potent; and supplemehts to correct vitamin A, iodine and iron deficiencies can now be made available at negligible cost. The low cost of such measures, furthermore, permits their application on a mass scale, which further reduces costs as a result of economies of scale. For instance, one study showed that in Indonesia between 1979 and 1982, the yearly out-of-pocket cost of an integrated child survival package (UPGK) comprising growth monitoring, oral rehydration, breast-feeding, immunization, distribution of vitamin A capsules and nutrition education covering 8.9 million children in 1982 averaged US$ 6-7 per under-five, or about US$ 1 per head of population.' ° There is also ample evidence" that, ceteris paribus, the cost of programs tends to decline with the scale of the service delivered. In this way, a "virtuous circle" is created between the low cost of an intervention (which allows for increased coverage at any given level of resources) and economies of scale which, by gradually reducing unit costs per capita, further stimulate the expansion of coverage.

d) The adoption of a less skill-intensive and more communitybased approach to the delivery of social services will increase service coverage. Although highly qualified staff (trained teachers, water engineers, doctors, certified nurses, nutritionists, etc.) are scarce in most developing countries, their precious time is often absorbed by relatively simple problems which could easily be delegated to lowerlevel staff and to community workers. For the health sector, for instance, the Alma Ata declaration explicitly recommends the institution of a three-tier primary health care system in which the first and second tiers are manned by village health volunteers and paraprofessionals with the ability to treat common ailments, while more complicated cases are referred to the higher tiers. In this way, substantial savings on personnel costs and a more rational allocation of highly qualified staff become possible. The introduction of village health volunteers, although not without problems, has further strengthened this approach to cost-saving and rapid increase in service coverage. In Indonesia, for instance, the monetary cost per under-five of the UPGK program could be reduced by around 30 percent by the unremunerated work of village health volunteers." While the use of volunteers requires considerable training, the results they produce often go beyond all expectation.

e) Increasing the overall efficiency of the social sector includes a series of heterogeneous measures which can contribute to cost-saving and increased efficiency. Among them, appropriate procurement policies play a particularly important role. For instance, in many countries, governments should consider establishing a basic drug list, as advised by WHO. Importing basic drugs under the WHO/ UNICEF Drugs Procurement Facility allows cost savings of up to 40 to 50 percent. Besides keeping costs down through centralized bulk procurement, the establishment of an essential drugs list could generate substantial financial and foreign exchange savings by explicitly banning drugs which have been proven to have no or negative effects This is particularly the case for drugs supposedly treating diarrhea (such as clioquinol, neomycyin, septrin, lomotil, etc.) which, although widely used, have no therapeutic value.

Overall efficiency can also be improved by attempts to reduce wastage. An evaluation of a measles immunization campaign in Cameroon" reports that out of 100 doses of vaccine, 83 were wasted, as they had either lost potency or were given to children who were too young, too old or already immune. While insufficient or inappropriate investment is at times responsible for these high levels of wastage, increased expenditure on supervision can substantially increase the efficiency of the overall delivery system.

Targeting

Targeting is a further powerful way of reducing program costs and increasing the efficiency of social expenditure during the process of adjustment. In principle, achieving effective targeting should form an important aspect of sectoral policies to protect the vulnerable during adjustment. But to achieve this requires very careful design of targeting. The discussion here uses food interventions to illustrate the general issues.

a) Defining the target population is an essential prerequisite for targeting. Such definition is not easy, since it requires facts, which are typically scanty or nonexistent, and norms, which have to be chosen, the target group being those who fall below the selected minimum standards

There are further problems in the selection of standards, the first being the choice of the reference dimension, i.e., the dimension against which the target group is to be defined. For example, in nutrition, the target group could be defined with reference to anthropometric data, or to caloric intake, or to household income levels. Choice of a reference dimension is partly dictated by the availability of data. It also depends on the administrative mechanism and target group being considered. For example, if children are the main target and health clinics the administrative mechanism, then some anthropometric dimension is appropriate. An income reference dimension is more suitable for income-support schemes. Second, how is the cutoff point to be selected? In general, for most needs, including nutrition, there is no scientific justification for any particular cutoff point, so some arbitrariness enters the determination of norms. But the fact that no precise cutoff point is scientifically based does not mean that no cutoff point is necessary - i.e., malnutrition exists, even though nutrition experts disagree on precisely when this occurs. Third, the target group should be differentiated with respect to the extent of inadequacy - e.g, distinguishing the severely malnourished from the mildly malnourished. This is important, because failure to meet the needs of the most severely deprived (ultra-deficient) is more serious than failing to reach the rest of the target population.

b) Two types of mistakes can occur when targeting. Assume the target population, T, has been identified and that it is divided into the deficient (DT) and the ultra-deficient (UT). Designing targeting interventions then aims to ensure that all T is covered by the intervention, but no one outside the target group. It follows that the targeting may be subject to two types of mistake.

Mistake E is excessive coverage, i.e., some interventions go to those outside the target group. This may be represented by E. The greater E, the higher the cost of any scheme; or, put in another way, the size of the program to each member of the target group could be increased if E-type mistakes were all eliminated.

The major criticism of untargeted interventions (e.g., across-the-board subsidies) is that E-type mistakes are very large, so that total costs are high. For example, in Morocco, it was estimated that 80 percent of the budgetary costs in the rural areas and 70 percent in the urban areas "increased the consumption of the already well-nourished."" This means that E was approximately 3, or the costs could have been reduced to one-third by eliminating E-mistakes. It should be noted that E-mistakes raise incomes of the nontarget group. In principle, these could be recouped by taxes (e.g, income tax or indirect taxes).

Mistake F is failure to cover all the target group, Suppose F represents the proportion of the target group who is not covered; then FT people's needs are not met. From the perspective of protecting vulnerable groups, F-type mistakes represent a serious failure which cannot be compensated for in the way E-type mistakes can. Fmistakes are particularly serious if they consist in failures to reach the ultra-deficient group.

Even apparently "universal" subsidies can involve some F-mistakes - e.g, where the subsidies do not cover inferior goods or subsistence farmers, Increased F-mistakes are a normal consequence of moving from a universal to a targeted approach and may be offset by good design of targeting.

In designing schemes; there tends-to be a tradeoff between E- and F-mistakes: the more narrow the focus on target groups, the less the E-mistakes and the greater the F-mistakes. In general, the aim should be to try and reduce both types of mistakes; but insofar as there is a tradeoff, the emphasis - from the perspective of protecting the vulnerable during adjustment - must be placed on reaching all the target group, and especially the ultra-deficient, even if this is at the cost of including some

outside the larger group.
c) Types of targeting. Schemes may be targeted by income (e.g., ration shops, or coupons provided to those falling below a certain income), as in the recent Sri lankan food stamp scheme; by needs as identified, by health workers, with coupons or free or subsidized foods provided to the needy, as in schemes in Botswana and Indonesia, where food is delivered to children who are identified as most deficient using anthropometric measures; by commodity, subsidizing only basic or "inferior" foods; by geography, locating subsidized ration schemes in areas where a high proportion of the target population live; by age, providing subsidies for all those below (or above) a certain age (this can be extended to pregnant or lactat-g ing women); through employment in food-for-work schemes; and by season, providing free or subsidized foods at certain times of the year. Particular schemes may combine elements - e.g, providing food to children of low-income households at certain times of the year.
The first two approaches differ from the remainder in being somewhat discretionary, in that the administrators of the scheme decide many particular case whether the person qualifies. This discretionary aspect can lead to abuse (e.g., through corruption); and people who are needy may be left out because they do not come forward. This seems to occur particularly among the ultra-deficient, who generally have other characteristics (e.g., low levels of education, remote location) which make it less likely that they will come forward. The remaining schemes are nondiscretionary - and therefore sometimes described as "self-targeting" - being universally available within a restricted category. How far they generate the two mistakes will depend on the nature of the target group in comparison with the nontarget population. For example, if all and only the target group lives in one remote region, then providing subsides for everyone in this region would achieve perfect targeting, avoiding both mistakes.
In order to assess how far particular schemes are likely to generate E- and F-mistakes in any context, it is helpful to draw up a matrix describing the characteristics of the target population (divided into deficient and ultra-deficient) and comparing these with the nontarget groups.

FIGURE 1
Matrix of Characteristics

	(1) Targeu Deficient		(2) TargeUltra-deficient		(3) Non.taiget	
Characteristics	Absolute No,.	%of Group	Absotute No,.	%of Group	Absolute No,.	%of Group
1. Age and sex Undm5 FM 5.15 F M 15-60 F,M 60+ Pregnant & lactating						
IL Location Urban Rural						

FIGURE l -- Continued

	(I) Target-. Deficient		(2) Target: Ino-adeficient		(s) Non-target	
Characteristics	Absolute Nos.	% of Group	Absolute Nos.	% of Group	Absolute Nos.	% of Group
III. Region "North'						
IV.Consumption Of staple' as % income Of staple 2 as % income						
V. Occupation Formal sector, wage Informal sector Landless agricultural worker Subsistence farmer small cash farmer						
VI. Seas on Jan-March April-June July-se Pt. Oct: Dec.						
Vll.Other relevant characteristics						

Where there is a high proportion of the target group included in any category (high percentage in columns I and 2), then a subsidy based on that characteristic will achieve high coverage of the target group (low F-mistakes). If there is a low proportion of the nontarget group with the same characteristic (low percentage in column 3), then there will be low E-mistakes.
Schemes which combine characteristics may achieve improved targeting. For example, in Brazil, common foods are subsidized in shops in certain poor areas (combing commodity and location).
d) Other considerations in designing targeting schemes are: (i) Administrative cost, which depends in part on the existing situation. For example, in India and Pakistan, ration shops have already been

established, but elsewhere they would need to be set up. Administrative costs tend to be higher for special schemes (e.g., food-for-work and feeding schemes). Discretionary schemes have high administrative costs because they require identification of the target population on an individual basis. (ii) Potential for corruption and perversion. (iii) Liability to pressure from private interest groups "that want to divert program funds from the target groups."r' (iv) Effects on work incentives. (v) Effects on local food production incentives. Food-for-work schemes supported by food aid can have negative effects on local production incentives. So can price controls on foods, but they need not, if accompanied by producer subsidies (as in Sri Lanka in the I960s and I970s). Feeding programs using locally purchased foods have positive effects on producer incentives. (vi) Effects on consumption patterns and tastes. Subsidies on foods which are not produced locally, or which are produced locally at high cost, may have undesirable effects on tastes. Subsidies on weaning foods or nutritionally superior foods can have positive effects.

In conclusion, targeting cam help in sustaining minimum levels of nutrition and health of the whole population during periods of declining resources by concentrating the provision of benefits on the group facing the most severe deprivation. In several countries there is scope, for instance, for redirecting subsidies from generalized to targeted schemes. This would allow either substantial savings of budgetary resources or a higher benefit for the population in need. The problems encountered in the design of targeting indicate that there is frequently a tradeoff between E- and F-mistakes. Whenever the aim of reducing both mistakes cannot reasonably be attained, priority should be attached to reaching all those parts of the target group, even if this entails the cost of including some outside the target group.

Targeting also has limitations. In Chile, for instance, a very efficient targeting of stagnant and/or slightly declining overall resources on the groups most at risk (severely malnourished children, under-lives, pregnant women, etc.), while contributing to the decline of infant and child mortality until 1983, could not prevent a broader deterioration in health status indicators, such as the incidence of infectious and waterborne disease. The efficiency of declining resources, in other words, cannot be stretched beyond a certain limit.

Conclusion

The foregoing analysis shows that substantial scope exists for protecting the poor and the vulnerable during periods of rapid economic decline and rigorous adjustment. To achieve this objective, the role and scope of social sector policies must be substantially enlarged, as economic trends and adjustment policies, however, efficient, tend to put enormous burdens - at least for a few years - on the fragile shoulders of low-income households During such periods, their autonomous capacity to satisfy the most elementary nutrition, education, health, sanitation and shelter needs declines dangerously. Evidence shows that although the middle and upper classes have also been severely affected by declines in standards of living, this has generally not been reflected in serious nutritional and health hazards. The purpose of social policies during adjustment, therefore, should be to expand the supply of basic goods and services, particularly to the poorest segments of society.

In the course of the discussion, three main avenues were identified for achieving these objectives. They are the mobilization of additional resources for the social sector, the improvement in the efficiency in the use of such resources, and an increasing emphasis on equity in the distribution of these benefits. While the potential of the first option might be limited in a number of countries, greater equity and efficiency are viable propositions for all countries facing severe economic decline.

Better targeting and restructuring of social expenditure in particular can substantially contribute to sustaining minimum standards of living of the poor during periods of economic hardship. In most sectors, new technological breakthroughs and the increased self-help and participation of thee communities now make possible the adoption of low-cost, high-efficiency approaches substantially benefiting the poor and their children. Their low cost and high efficiency also make them attractive from a political point of view.

Notes

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CHAPTER 7

Macro Policies, Adjustment and the Human Dimension

Gustav Ranis

We are all keenly aware of several incontrovertible facts: (i) that much of the adjustment process which developing countries have experienced over the past few years has been painful; (ii) that, in spite of the sacrifices incurred to date, there seems to be no end in sight; (iii) that the international community continues to show a decided preference for mounting short-term rescue operations rather than coming up with long-term solutions; (iv) that any hope that overall global recovery would "refloat all ships" - probably misplaced at any time -looks exceedingly forlorn today, when even the only major locomotive, the U.S, seems to be showing signs of slackening.

If there is agreement onn this somber state of affairs, it also behooves us, more than at any other time, to raise the question of how the international community is going to extract itself from the corner into which it seems to have painted itself - short of a disruptive repudiation of debt on the one hand, isolationist/protectionist retreats on the other, or both. Central to both the problem and to its solution is the human element. It is the human element, especially the most exposed or vulnerable segments of LDC populations, which has suffered most of the pain over the past few years, and without the visible benefits which might have provided a convincing argument that the "medicine" was necessary to cure the patient; and it is the human element, if properly deployed, which is also likely to be an essential part of the solution.

This paper will proceed by presenting some general propositions on what has happened and what might happen differently in the future if we are to turn matters around, illustrating with reference to the specific case of the Philippines.

There are some basic propositions which are fundamental to a proper assessment of what has transpired in the past and, as a direct consequence, what needs to be addressed if we are to place the LDC adjustment process on a viable and nonconfrontational track.

Proposition 1: In most LDCs, the unavoidable adjustment which was required of their systems during the last three or four years has been borne by a reduction in imports, investment and incomes, with consumption, both public and private, generally stagnating, certainly on a per capita basis.

Proposition 2: While there has been a generally remarkable willingness to put up with declining per capita incomes in situations in which the population had been accustomed to 3 or 4 percent rates of growth in per capita income over extended periods of time, there are also ample signs that patience is wearing thin. With people still at low levels of consumption and without clear prospects for resumed growth, it would be foolhardy to assume that further adjustments requiring further stagnation of consumption amid reduced levels of investment would be politically and socially feasible in all but the most repressive societies.

Proposition 3: The original response of the international community to the crisis was to ask LDCs to adjust by tightening their belts by a few notches and generating the required exports through structural adjustment reform packages administered mainly by the International Monetary Fund and increasingly, of late, with the participation of the World Bank, usually with a one- or two-year time horizon and with little concern for the impact on various exposed or vulnerable groups within the debtor countries.

Proposition 4: More recently, there has been a greater awareness of the human dimension of the adjustment problem on the part of the international community. This has manifested itself in some softening of the IMF's hard-line views of precisely what an ideal package must consist of and a greater flexibility in seeking an expansion of the available resources, as in the Baker Plan and other proposals.

Assuming these propositions are accepted, there are some serious problems to be considered. For one, the new, if somewhat grudging, flexibility witnessed today really extends more to 'adjustment with growth" than to the equitable nature of that growth. And this in turn is based on the mistaken assumption, if often only implicitly stated, that the protection of vulnerable groups is necessarily in conflict with efficient growth, i.e., that it must be defended on humanitarian grounds rather than as the necessary, rational protection of essential and easily depleted human resources.

Relatively little thought has been given to date to the question of the role of policy-based lending in relation to the specific protection of vulnerable groups, either in the sense of providing direct support through the provision of additional foreign capital or of inducing the government - via the structural adjustment loan or IMF conditionality mechanism - to take appropriate direct action. This seems to be largely based on the inadequacy of the current wisdom with respect to how the goal of "adjustment with equitable growth" can best be induced, i.e., by what combination of domestic and international actions. In fact, most of the current discussion revolves around the amounts of additional rsoutces that need to be transferred; the new interest rates or margins over LIHOR which can be negotiated; how the commercial banks can be induced to participate with additional "voluntary" lending; how (for instance, in the case of Mexico) LDCs might be insured against a further drop in the price of oil - with others presumably symmetrically insured against a rise in the price of oil. But there has been very little discussion on how new international modalities might be deployed so that there results no further substantial injury to the most vulnerable groups in the developing countries in the course of the adjustment process.

Improving the System

There are several ways in which the system might be improved both at the national and international levels so that we can begin to work ourselves out of the present difficulties. These suggestions will undoubtedly be controversial.

Expanding the Time Frame

The time frame for negotiations between the debtor countries and the international community must be expanded. All protestations and labelling to the contrary, the one- or two-year time frame which typically applies to current IMF standbys (in spite of the fact that they are, of course, routinely rolled over), as well as to the typical

A policy on local and recurrent costs could be articulated as follows:
a) To start with, it is necessary to verify that there is a real local commitment to the project under consideration, and that after a few years the project can become self-sustaining. This means that under normal conditions, local counterpart funds should cover at least, say, 30-40 percent of the total costs of the project, and that local funds should be able to finance total recurrent costs after a few years. However, in order to avoid the capital- and import-intensive bias mentioned above, the choice (whether capital or recurrent) of what costs to finance with foreign assistance in the short run should be left to the recipient countries. Often, for instance, what is needed is not new projects, but revitalization of old ones. This requires funds for repair and maintenance and for recurrent costs rather than new capital investment.
b) The exceptional situation of countries either in deep recession or undergoing severe adjustment must be recognized. Their budgetary and foreign exchange situation must be thoroughly assessed before applying the above criteria. A degree of country differentiation appears to be necessary at this point. While middle-tohigh-income developing countries - with relatively well developed health, sanitation and school systems - may not require any change in recurrent and local cost policies, low-income developing countries of Africa and Asia ought to be treated differently. First, labor and other contributions in kind (construction material, current inputs, food, etc.) should be counted both as counterpart funds and recurrent inputs. Second, for a limited amount of time, recurrent costs both for ongoing projects and new projects could be met by donors. For instance, recurrent costs might be met for, say, three years, or on a sliding scale for, say, five years. The figures are only indicative and should be adapted on a case-by-case basis. Barring exceptional circumstances, after this "grace period" the project should become self-sustaining.
If these changes are accepted, one should expect an increase in the resources for adjustment in the social sector in low-income developing countries as foreign assistance previously blocked by the lack of counterpart funds is released for funding of both recurrent and capital costs of ongoing and new projects. Such changes would also result in an increase in the rate of utilization of existing projects and in a greater increase in the output of the social sector than when external assistance is used exclusively for new capital investment.

Improving Efficiency in the Use of Social Sector Resources

The measures described here aim at increasing the level of output and at improving its distribution for any given level of resources available to the social sector. The measures proposed broadly aim at maximizing collective welfare by increases in efficiency and equity and changes in the organizational make-up of the social sector.

Promotion of Self-help at the Household Level

At least 75 percent of all health care is estimated to take place at the family or individual level," with women having the greatest responsibility for promoting family health and nutrition. The degree of self-provisioning is lower in other social sectors - education, for instance. It is important to note, however, that in many societies there is scope for decentralizing many activities in health, nutrition, child care, sanitation and other services at the family (or community) level. This decentralization is not costless. Important efforts have to be made to mobilize public opinion and to create awareness of the need for the adoption of certain health, nutrition and child-rearing practices. Governments, community leaders and foreign donors must often join forces to organize and sustain massive public education campaigns. Social communication aimed at the mother is the key element of this strategy. The current UNICEF approach to the treatment of diarrhea (the number one infant killer in the world) through home-based oral rehydration is an appropriate example. While until recently diarrhea was treated at considerable cost in health posts or hospitals by means of intravenous rehydration, the new strategy emphasizes home-based treatment consisting of two teaspoons of sugar and one teaspoon of common salt diluted in a liter of boiled water. All the ingredients of the oral solutions are generally available even to very poor families, while prepackaged mixtures of salt and sugar are produced industrially and sold commercially in many developing countries at extremely tow cost (US 6-10 cents per packet). While such an approach may increase time cost for women to an extent," it places extremely modest monetary costs on the households and leads to substantial savings in the public sector, where a considerable proportion of beds, staff time and current inputs are absorbed by the care of diarrhea! disease.,Other areas where this approach can be applied include breast-feeding and weaning and growth monitoring.
Improving the Efficiency of Government Social Expenditure

Despite the conspicuous and growing shortage of budgetary and human resources, the social sector seldom utilizes them in an efficient way. Indeed, in many developing countries, the provision of social services is affected by a long series of biases in favor of expensive, urban-based, capital- and skill-intensive activities often modeled on those of the industrialized countries. As seen earlier, the capital intensiveness of such services is often influenced by donors' preference for financing capital costs and by the practice of tied aid. For these and other reasons, educational, health, sanitation and other services often cater to a relatively small, mostly urban, upper and middle class while bearing little relevance to the satisfaction of the most elementary health, nutritional and educational needs of the population.

In many countries, therefore, substantial scope exists for improvement in the efficiency of government recurrent and capital expenditure. For ease of exposition, such improvements are grouped into five categories.

a) As far as capital expenditure is concerned, there is the need to proceed to the selective rehabilitation of the social service infrastructure. Output increases obtained by rehabilitating existing infrastructure are generally substantially cheaper than those obtained through new investment. It is important to underline, however, that this rehabilitation should be selective in nature, i.e., starting from those facilities with the highest potential coverage and the greatest unfulfilled needs. Selective rehabilitation should also represent an occasion for restructuring social services away from expensive, high-tech solutions and toward low-cost and high-efficiency measures. In Ghana, for instance, in view of the expensive nature of hospitalbased care, the government should consider putting a stop to new hospital construction and to major extensions of existing capital. The resources so freed should be used for the rehabilitation of health posts and health centers.

b) Within each sector there is a need to restructure social expenditure toward the satisfaction of the needs of the poor majority. In the Philippines, for example, there was a serious misallocation

of resources within the health sector, with total subsidies extended to five specialized health institutions catering to the upper class amounting to 229 million pesos, while government funds for primary health care totaled only 45 million pesos. Although not always so extreme, the problem of an excessive allocation of health resources to the hospital sector is to be found in many other countries. In Malawi in 1983, hospitals received over 60 percent of government health funds," while in the Senegal (1981-82) and Tanzania (1980), hospitals absorbed respectively 51 and 58 percent of the government health budgets.'s Intrasectoral mjsallocation of resources is typical not only of the health sector- In Burkina Faso, for instance, between 1980 and 1984 secondary and university education received on average a share of the education budget twice as large as primary education, although the latter covered a ten times larger school population," while according to a World Bank study, "in Francophone Africa two percent of each cohort in the population attain higher education and receive 40 percent of the public resources devoted to education."

Correcting such glaring misallocations is not simple. For technical and social reasons, capital and labor resources are only partially mobile. A large hospital cannot be fractioned into fifty primary health care posts. Neither is it easy to provide sufficient incentives to secondary school teachers from urban areas to take up service in a primary school in a remote rural area. Moreover, reallocation is easier at the margin during periods of overall growth of resources. Despite these difficulties, there is both a need and the possibility to redirect government social expenditure in favor of primary education, primary health care, the installation of communal fountains, etc. Such restructuring has happened in a number of countries. In Zimbabwe, for instance, the share of preventive health services doubled between 1979-80 and 1985-86. A similar shift in favor of primary education was noted in Zimbabwe during the same period. A study on the provision of education in Commonwealth countries" showed that attainment of the universal primary education target could be substantially accelerated by reducing unit costs in secondary and higher education and by shifting the resources thus saved to primary education.

c) The adoption of low-cost, high-efficiency measures for the satisfaction of the basic health, sanitation, water, education and shelter needs of the poor will substantially contribute to more efficient use of social sector resources. In the past, expensive techniques were used to deal with common problems. Several low-cost, high-efficiency interventions have been developed recently thanks to technological and scientific advances. Water pumps have become sturdier, cheaper and simpler to operate and maintain; vaccines are cheaper, more resistant to heat

(thus facilitating their transport) and more potent; and supplements to correct vitamin A, iodine and iron deficiencies can now be made available at negligible cost. The low cost of such measures, furthermore, permits their application on a mass scale, which further reduces costs as a result of economies of scale. For instance, one study showed that in Indonesia between
1979 and 1982, the yearly out-of-pocket cost of an integrated child survival package (UPGK) comprising growth monitoring, oral rehydration, breast-feeding, immunization, distribution of vitamin A capsules and nutrition education covering 8.9 million children in 1982 averaged US$ 6-7 per under-five, or about US$ 1 per head of population.' ^ There is also ample evidence" that, ceteris paribus, the cost of programs tends to decline with the scale of the service delivered. In this way, a "virtuous circle" is created between the low cost of an intervention (which allows for increased coverage at any given level of resources) and economies of scale which, by gradually reducing unit costs per capita, further stimulate the expansion of coveragee
d) The adoption of a less skill-intensive and more communitybased approach to the delivery of social services will increase service coverage. Although highly qualified staff (trained teachers, water engineers, doctors, certified nurses, nutritionists, etc.) are scarce in most developing countries, their precious time is often absorbed by relatively simple problems which could easily be delegated to lowerlevel staff and to community workers. For the health sector, for instance, the Alma Ata declaration explicitly recommends the institution of a three-tier primary health care system in which the first and second tiers are manned by village health volunteers and paraprofessionals with the ability to treat common ailments, while more complicated cases are referred to the higher tiers. In this way, substantial savings on personnel costs and a more rational allocation of highly qualified staff become possible. The introduction of village health volunteers, although not without problems, has further strengthened this approach to cost-saving and rapid increase in service coverage. In Indonesia, for instance, the monetary cost per under-five of the UPGK program could be reduced by around 30 per cent by the unremunerated work of village health volunteers." While the use of volunteers requires considerable training, the results they produce often go beyond all expectation.
e) Increasing the overall efficiency of the social sector includes a series of heterogeneous measures which can contribute to cost-saving and increased efficiency. Among them, appropriate procurement policies play a particularly important role. For instance, in many countries, governments should consider establishing a basic drug list, as advised by WHO. Importing basic drugs under the WHO/ UNICEF Drugs Procurement Facility allows cost savings of up to 40 to 50 percent. Besides keeping costs down through centralized bulk procurement, the establishment of an essential drugs list could generate substantial financial and foreign exchange savings by explicitly banning drugs which have been proven to have no or negative effects. This is particularly the case for drugs supposedly treating diarrhea (such as choquinol, neomycyin, septrin, lomotil, etc.) which, although widely used, have no therapeutic value.
Overall efficiency can also be improved by attempts to reduce wastage. An evaluation of a measles immunization campaign in Cameroun" reports that out of 100 doses oC vaccine, 83 were wasted, as they had either lost potency or were given to children who were too young, too old or already immune. While insufficient or inappropriate investment is at times responsible for these high levels of wastage, increased expenditure on supervision can substantially increase the efficiency of the overall delivery system.

Targeting

Targeting is a further powerful way of reducing program costs and increasing the efficiency of social expenditure during the process of adjustment. In principle, achieving effective targeting should form an important aspect of sectoral policies to protect the vulnerable during adjustment. But to achieve this requires very careful design of targeting. The discussion here uses food interventions to illustrate the general issues.
a) Defining the target population is an essential prerequisite for targeting. Such definition is not easy, since it requires facts, which are typically scanty or nonexistent, and norms, which have to be chosen, the target group being those who fail below the selected minimum standards.

There are further problems in the selection of standards, the first being the choice of the reference dimension, i.e., the dimension against which the target group is to be defined. For example, in nutrition, the target group could be defined with reference to anthropometric data, or to caloric intake, or to household income levels. Choice of a reference dimension is partly dictated by the availability of data. It also depends on the administrative mechanism and target group being considered. For example, if children are the main target and health clinics the administrative mechanism, then some anthropometric dimension is appropriate. An income reference dimension is more suitable for income-support schemes. Second, how is the cutoff point to be selected? In general, for most needs, including nutrition, there is no scientific justification for any particular cutoff point, so some arbitrariness enters the determination of norms. But the fact that no precise cutoff point is scientifically based does not mean that no cutoff point is necessary - i.e., malnutrition exists, even though nutrition experts disagree on precisely when this occurs. Third, the target group should be differentiated with respect to the extent of inadequacy - e.g., distinguishing the severely malnourished from the mildly malnourished. This is important, because failure to meet the needs of the most severely deprived (ultra-deficient) is more serious thann failing to reach the rest of the target population.

b) Two types of mistakes can occur when targeting. Assume the target population, T, has been identified and that it is divided into the deficient (DT) and the ultra-deficient (UT). Designing targeting interventions then aims to ensure that all T is covered by the intervention, but no one outside the target group. It follows that the targeting may be subject to two types of mistake.

Mistake E is excessive coverage, i.e., some interventions go to those outside the target group. This may be represented by E. The greater E, the higher the cost of any scheme; or, put in another way, the size of the program to each member of the target group could be increased if E-type mistakes were alt eliminated.

The major criticism of untargeted interventions (e.g., across-the-board subsidies) is that E-type mistakes are very large, so that total costs are high. For example, in Morocco, it was estimated that 80 percent of the budgetary costs in the rural areas and 70 percent in the urban areas "increased the consumption of the already well-nourished."" This means that E was approximately 3, or the costs could have been reduced to one-third by eliminating E-mistakes.

It should be noted that E-mistakes raise incomes of the nontarget group. In principle, these could be recouped by taxes (e.g., income tax or indirect taxes).

Mistake F is failure to cover all the target group. Suppose F represents the proportion of the target group who is not covered; then FT people's needs are not met. From the perspective of protecting vulnerable groups, F-type mistakes represent a serious failure which cannot be compensated for in the way E-type mistakes can. Fmistakes are particularly serious if they consist in failures to reach the ultra-deficient group.

Even apparently "universal" subsidies can involve some F-mistakes - e.g., where the subsidies do not cover inferior goods or subsistence farmers. Increased F-mistakes are a normal consequence of moving from a universal to a targeted approach and may be offset by good design of targeting.

In designing schemes, there tends to be a tradeoff between E- and F-mistakes: the more narrow the focus on target groups, the less the E-mistakes and the greater the F-mistakes. In general, the aim should be to try and reduce both types of mistakes; but insofar as there is a tradeoff, the emphasis - from the perspective of protecting the vulnerable during adjustment - must be placed on reaching all the target group, and especially the ultra-deficient, even if this is at the cost of including some outside the targer group.

c) Types of targeting. Schemes may be targeted by income (e.g., ration shops, or coupons provided to those falling below a certain income), as in the recent Sri Lankan food stamp scheme; by needs as identified, by health workers, with coupons or free or subsidized foods provided to the needy, as in schemes in Botswana and Indonesia, where food is delivered to children who are identified as most deficient using anthropometric measures; by commodity, subsidizing only basic or "inferior" foods; by geography, locating subsidized ration schemes in areas where a high proportion of the target population live: by age, providing subsidies for all those below (or above) a certain age (this can be extended to pregnant or lactating women); through employment in food-for-work schemes; and by season, providing free or subsidized foods at certain times of the year. Particular schemes may combine elements - e.g., providing food to children of low-income households at certain times of the year.

The first two approaches differ from the remainder in being somewhat discretionary, in that the administrators of the scheme decide in, any particular case whether the person qualifies. This discretionary aspect can lead to abuse (e.g., through corruption); and people who are needy may be left out because they do not come forward. This seems to occur particularly among the ultra-deficient, who generally have other characteristics (e.g., low levels of education, remote location) which make it less likely that they will come forward- The remaining schemes are nondiscretionary - and therefore sometimes described as "self-targeting" - being universally available within a restricted category. How far they generate the two mistakes will depend on the nature of the target group in comparison with the nontarget population. For example, if all and only the target group lives in one remote region, then providing subsides for everyone in this region would achieve perfect targeting, avoiding both mistakes.

In order to assess how far particular schemes are likely to generate E- and F-mistakes in any context, it is helpful to draw up a matrix describing the characteristics of the target population (divided into deficient and ultra-deficient) and comparing these with the nontarget groups.

FIGURE 1

Matrix of Characteristics

(1) (R) (5)

Target: Deficient Target Ultradenuent Non-target

characteristics Absolute %of Absolute %of Absolute %of

No,. Group Nos. Group No.. Group

I. Age and sex Under-5 F ,M 5-15 FM 1560 FM 60 + Pregnant &
lactating

II. Location Urban

FIGURE I -Continued

- _(I) (2) (S)

Target Deficient Target: Ultra-deficient Non-target

Characteristics Absolute %of Absolute %of Absolute %of

Nos. Group Nos. Croup No.. Group

IILRegion "North' "South"

IV.Consumption Of staple'
as % income Of staple 2
as % income

V. Occupation
Formal sector, wage Informal sector Landless agricultural
worker
Subsistence farmer Small casts farmer

VI. Seas on Jan.-March April June July-Sept.

VII.Other relevant characteristics

Where there is a high proportion of the target group included in any category (high percentage in columns 1 and 2), then a subsidy based on that characteristic will achieve high coverage of the target group (low F-mistakes). If there is a low proportion of the nontarget group with the same characteristic (low percentage in column 3), then there will be low E-mistakes.

Schemes which combine characteristics may achieve improved targeting. For example, in Brazil, common foods are subsidized in shops in certain poor areas (combing commodity and location).

d) Other considerations in designing targeting schemes are: (i) Administrative cost, which depends in part on the existing situation. For example, in India and Pakistan, ration shops have already been established, but elsewhere they would need to be set up. Administrative costs tend to be higher for special schemes (e.g., food-for-work and feeding schemes). Discretionary schemes have high administrative costs because they require identification of the target population on an individual basis. (ii) Potential for corruption and perversion. (iii) Liability to pressure from private interest groups "that want to divert program funds from the target groups."2 ` (iv) Effects on work incentives. (v) Effects on local food production incentives. Food-for-work schemes supported by food aid can have negative effects on local production incentives. So can price controls on foods, but they need not, if accompanied by producer subsidies (as in Sri Lanka in the i960s and 1970s). Feeding programs using locally purchased foods have positive effects on producer incentives. (vi) Effects on consumption patterns and tastes. Subsidies on foods which are not produced locally, or which are produced locally at high cost, may have undesirable effects on tastes. Subsidies on weaning foods or nutritionally superior foods can have positive effects.

In conclusion, targeting cam help in sustaining minimum levels of nutrition and health of the whole population during periods of declining resources by concentrating the provision of benefits on the group facing the most severe deprivation. In several countries there is scope, for instance, for redirecting subsidies from generalized to targeted schemes. This would allow either substantial savings of budgetary resources or a higher benefit for the population in need. The problems encountered in the design of targeting indicate that there is frequently a tradeoff between F- and F-mistakes. Whenever the aim of reducing both mistakes cannot reasonably be attained, priority should be attached to reaching all those parts of the target group, even if this entails the cost of including some outside the target group.

Targeting also has limitations. In Chile, for instance, a very efficient targeting of stagnant and/or slightly declining overall resources on the groups most at risk (severely malnourished children, under-lives, pregnant women, etc.), while contributing to the decline of infant and child mortality until 1983, could not prevent a broader deterioration in health status indicators, such as the incidence of infectious and waterborne disease. The efficiency of declining resources, in other words, cannot be stretched beyond a certain limit.

Conclusion

The foregoing analysis shows that substantial scope exists for protecting the poor and the vulnerable during periods of rapid economic decline and rigorous adjustment. To achieve this objective, the role and scope of social sector policies must be substantially enlarged, as economic trends and adjustment policies, however, efficient, tend to put enormous burdens - at least for a few years - on the fragile shoulders of low-income households. During such periods, their autonomous capacity to satisfy the most elementary nutrition, education, health, sanitation' and shelter needs declines dangerously. Evidence shows that although the middle and upper classes have also been severely affected by declines in standards of living, this has generally not been reflected in serious nutritional and health hazards. The purpose of social policies during adjustment, therefore, should be to expand the supply of basic goods and services, particularly to the poorest segments of society.

In the course of the discussion, three main avenues were identified for achieving these objectives. They are the mobilization of additional resources for the social sector, the improvement in the efficiency in the use of such resources, and an increasing emphasis on equity in the distribution of these benefits. While the potential of the first option might be limited in a number of countries, greater equity and efficiency are viable propositions for all countries facing severe economic decline.

Better targeting and restructuring of social expenditure in particular can substantially contribute to sustaining minimum standards of living of the poor during periods of economic hardship. In most sectors, new technological breakthroughs and the increased self-help and participation of thee communities now make possible the adoption of low-cost, high-efficiency approaches substantially benefiting the poor and their children. Their low cost and high efficiency also make them attractive from a political point of view.

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CHAPTER 7

Macro Policies, Adjustment and the Human Dimension

Gustav RaMs

We are all keenly aware of several incontrovertible facts: (i) that much of the adjustment process which developing countries have experienced over the past few years has been painful; (ii) that, in spite of the sacrifices incurred to date, there seems to be no end in sight; (iii) that the international community continues to show a decided preference for mounting short-term rescue operations rather than coming up with long-term solutions; (iv) that any hope that overall global recovery would "refoat all ships" - probably misplaced at any time-looks exceedingly forlorn today, when even the only major locomotive, the U.S., seems to be showing signs of slackening.

If there is agreement on this somber state of affairs, it also behooves us, more than at any other time, to raise the question of how the international community is going to extract itself from the comer into which it seems to have painted itself - short of a disruptive repudiation of debt on the one hand, isolationist/protectionist retreats on the other, or both. Central to both the problem and to its solution is the human element. It is the human element, especially the most exposed or vulnerable segments of LDC populations, which has suffered most of the pain over the past few years, and without the visible benefits which might have provided a convincing argument that the "medicine" was necessary to cure the patient; and it is the human element, if properly deployed, which is also likely to be an essential part of the solution.

This paper will proceed by presenting some general propositions on what has happened and what might happen differently in the future if we are to turn matters around, illustrating with reference to the specific case of the Philippines.

Some Propositions

There are some basic propositions which are fundamental to a proper assessment of what has transpired in the past and, as a direct consequence, what needs to be addressed if we are to place the LDC adjustment process on a viable and nonconfrontational track.

Proposition 1: In most LDCs, the unavoidable adjustment which was required of their systems during the last three or four years has been borne by a reduction in imports, investment and incomes, with consumption, both public and private, generally stagnating, certainly on a per capita basis.

Proposition 2: While there has been a generally remarkable willingness to put up with declining per capita incomes in situations in which the population had been accustomed to 3 or 4 percent rates of growth in per capita income over extended periods of time, there are also ample signs that patience is wearing thin. With people still at low levels of consumption and without clear prospects for resumed growth, it would be foolhardy to assume that further adjustments requiring further stagnation of consumption amid reduced levels of investment would be politically and socially feasible in all but the most repressive societies.

Proposition 3: The original response of the international community to the crisis was to ask LDCs to adjust by tightening their belts by a few notches and generating the required exports through structural adjustment reform packages administered mainly by the International Monetary Fund and increasingly, of late, with the participation of the World Bank, usually with a one-or two-year time horizon and with little concern for the impact on various exposed or vulnerable groups within the debtpr countries.

Proposition 4: More recently, there has been a greater awareness of the human dimension of the adjustment problem on the part of the international community. This has manifested itself in some softening of the IMFs hard-line views of precisely what an ideal package must consist of and a greater flexibility in seeking an expansion of the available resources, as in the Baker Plan and other proposals.

Assuming these propositions are accepted, there are some serious problems to be considered. For one, the new, if somewhat grudging, flexibility witnessed today really extends more to "adjustment with growth" than to the equitable nature of that growth. And this in turn is based on the mistaken assumption, if often only implicitly stated, that the protection of vulnerable groups is necessarily in conflict with efficient growth, i.e., that it must be defended on humanitarian grounds rather than as the necessary, rational protection of essential and easily depleted human resources.

Relatively little thought has been given to date to the question of the role of policy-based lending in relation to the specific protection of vulnerable groups, either in the sense of providing direct support through the provision of additional foreign capital or of inducing the government - via the structural adjustment loan or IMF conditionality mechanism - to take appropriate direct action. This seems to be largely based on the inadequacy of the current wisdom with respect to how the goal of "adjustment with equitable growth" can best be induced, i.e., by what combination of domestic and international actions. In fact, most of the current discussion revolves around the amounts of additional rsoutces that need to be transferred; the new interest rates or margins over LIHOR which can be negotiated; how the commercial banks can be induced to participate with additional "voluntary" lending; how (for instance, in the case of Mexico) LDCs might be insured against a further drop in the price of oil - with others presumably symmetrically insured against a rise in the price of oil. But there has been very little discussion on how new international modalities might be deployed so that there results no further substantial injury to the most vulnerable groups in the developing countries in the course of the adjustment process.

Improving the System

There are several ways in which the system might be improved both at the national and international levels so that we can begin to work ourselves out of the present difficulties. These suggestions will undoubtedly be controversial.

Expanding the Time Frame

The time frame for negotiations between the debtor countries and the international community must be expanded. All protestations and labelling to the contrary, the one- or two-year time frame which typically applies to current IMF standbys (in spite of the fact that they are, of course, routinely rolled over), as well as to the typical structural adjustment loans of the World Bank, is wholly inadequate. LDCs, and especially their more vulnerable populations, have no assurance under the present system that the additional resources to be made available will not be cut back after one or two years, even though the structural policy changes under negotiation usually carry with them a longer-term impact and longer-term risks. A three- to five-year time dimension is crucial if we are to be sure that debtors have a chance to restructure their economies dependably, i.e., to switch expenditure patterns through policy change rather than simply to reduce expenditures.
The argument is often quite forcefully made that donors and international agencies face legislative restrictions on their ability to commit future resources; but such creditor country structural adjustments should be subject to discussion, as are the structural adjustments being asked of the debtors. The fear that a three- to five-year perspective almost inevitably reduces the pressure for policy change is not justified if commitments on domestic policy change or, preferably, the self-imposed conditionality package is hammered out at the outset.

Macro Policy Changes

Macroeconomic policy changes continue to be vital to the achievement of an adjustment process which protects and indeed enhances the human dimension. There is a tendency in some quarters to conclude from the fact that macroeconomic adjustment has led to an unequal sharing of the burden over the recent past - quite aside from not restarting growth that one should return to the direct action or project mode of the 1970s. In those days, the language was indeed different, i.e., to try to ensure that foreign aid reaches poverty target groups (the "new directions" of 1973, as far as the U.S. aid lexicon is concerned). But it would be a serious mistake to assume that macroeconomic reforms are certain to injure particular groups at the lower end of the scale. Such groups are admittedly vulnerable, but this does not mean that reforms tending to diminish interventionist distortions are necessarily inimical to their interests. Instead, the lessons of the 1970s perhaps tell us that chasing down target groups with particular basic needs, poverty or income distribution-oriented projects while leaving the macro policy dialogue to one side is utter foolishness and cannot serve the purposes for which it is intended. In other words, a direct action program can be just as wide of the mark as an exclusive focusing of macro policies on short-term balance-ofpayments adjustment in the absence of adequate attention to restarting "growth with equity." Heavy reliance must indeed be placed on macroeconomic fiscal, monetary and exchange rate policies while making sure that the attendant risks for particularly vulnerable groups during the transition are adequately addressed.

The typical adjustment package includes some import liberalization and a devaluation, along with more restrictive fiscal and monetary policies. Does this package have to have an inhuman face? Not lithe market mechanism toward which one is trying to move is a truly competitive market rather than the kind of oligopolistic structure often faced in developing countries. The fact that devaluation don't stick, or that they hurt vulnerable groups disproportionately, often results from the fact that entrepreneurs do not fit the textbook definition of competitive actors but are in fact noncompetitive rent-seekers. This means the benefits of, for example, devaluation are not passed on to the producers of exports, while the desired negative effect for importers, producers for the domestic market and the elite organized labor force are cushioned by the noncompetitive features of the private market, as well as by government interventions. While trade liberalization represents the best anti-oligopoly policy, domestic licenses, permits, price controls, etc, often permeate the market and cannot be ignored.

There exists, of course, a large and growing literature on the relationship between liberalization and devaluation under different conditions, e.g., import and export elasticities and, more recently, the possibly perverse workings of the capital market. These analyses usually do not sufficiently emphasize the importance of market structure and government interventions on the outcome of a given structural adjustment package: i.e., if devaluation do not work as predicted, it is as likely to be due to price controls, parallel markets and oligopoly as to the Marshall-Lerner conditions. The substitution effect of a devaluation as between various affected parties may, of course, also be swamped by an income effect reducing growth and thus hurting the groups which have stood to benefit from the substitution effect. It is for this precise reason, i.e, to avoid the possible net negative total effect, that foreign capital ballooning may be needed in the transition to make the requisite structural changes feasible and relatively painless

There is, of course, the danger that any such ballooning of foreign capital, if not properly negotiated in relation to structural policy changes, can have just the opposite effect by relieving the pressure and thus make real adjustment less likely. All too often, additional foreign capital inflows, just like natural resource bonanzas, have been used (or misused) in that way. Thus, what is essential is a longer-term (three- to five-year) bargain between the international community and the debtor country which is not just acquiesced to by the latter but actually initiated and fully supported by it as both technically appropriate and politically acceptable.

The basic notion here is that the achievement of adjustment with equitable growth is best assured via an employment-oriented, rurally based development strategy. Of course, this does not just happen as a consequence of appropriate macroeconomic policies. It is also very much dependent on a reallocation of government infrastructure, including irrigation, electricity, roads, etc., toward the rural areas. In the absence of an employment-oriented development program encouraging balanced growth in the rural areas, development will continue to exhibit some of the blemishes of the I970s. To chase down poverty-oriented projects while ignoring macro policies is like putting hot compresses on an open wound, this time defined as "cushioning adjustment," but probably yielding neither growth nor adjustment, and most likely not even reaching the target groups.

We must, of course, be careful to recognize that there are public goods which need to be allocated by the public authorities, i.e., health, education, potable water, which make up a

substantial proportion of the typical requirements of the vulnerable groups during the transition process. This is also true for science and technology-related research expenditures, for the relative emphasis within education (higher relative to primary), within health (curative relative to preventive), within irrigation (maxi relative to mini), etc. In most of these areas, direct action by the local government is required, with or without persuasion from the outside. Usually, this means the maintenance or improvement of the levels of consumption of such public goods by the rural poor which can be achieved without increasing the total level of public goods consumption, but simply by reallocation of resources away from favored elite urban groups. It is difficult to measure the imputed value of government expenditures for various groups in a society, including any particularly vulnerable subset, but the evidence seems to indicate a loose associ-ation between the customary distribution of money income and the distribution of public goods due to the well-known relationship between political and economic power. While this is clearly an empirical matter, in most developing country situations there exists a very substantial potential for reallocation among such public goods expenditures currently providing large rents to the upper income groups.

In attempting to reach the most vulnerable groups with public goods, we often encounter the risk of spillage, the "leaky bucket" or the "hijacking by the middle class." This problem can be minimized by focusing on particularly poor regions of a developing country and/or by including only appropriate goods of the kind that are not readily consumed by the middle-income group. Moreover, we should be willing to live with some leakages. Occasionally "throwing" some explicit subsidies at the poor may be preferable to continuing with implicit subsidies for the rich,

The Philippine Example

The Philippine economy has indeed suffered from a severe decline in per capita income during the recent crisis, i,e., by 16 percent during 1984-85. In fact, per capita income is now back to the 1975 level, while there is evidence that nutrition as well as literacy rates have been falling recently. With specific reference to vulnerable groups, there is evidence that income distribution, always unfavorable, has been getting slightly worse; the ruralJurban average income gap declined from ,75 in 1975 to .48 in 1983 and has fallen still further since 1983. Even the World Bank admits that between 40 and 50 percent of the population now resides below the poverty line - given all the difficulties attached to that concept. If we accept the notion that the bottom 30 percent of the population of the Philippines is "poor," 81 percent of those poor are agricultural families. The reduction in literacy and nutrition levels clearly has its heaviest impact on the most vulnerable groups, e.g., on the sugar workers in Negros. While public expenditures on education have been further reduced from a low 2 percent to less than 1,8 percent of GNP, even more troubling is the fact that the percentage of public expenditures devoted to higher education rose from 6.7 percent in 1972 to more than 20 percent in 1981.

The Philippine economy has deep structural problems of long standing. The crisis of 1984 only rendered the underlying problem more severe, in contrast to the situation of some other developing countries, e.g., in East Asia. The Philippines, by failing in the I960s to restructure its economy toward labor-intensive industrial exports on the one hand and to fully mobilize its rural economy on the other, was ill prepared for the deterioration of the external environment in the early I980s. As long as natural resources could carry the day in the I960s and/or foreign capital could be had for the asking in the 1970s, the basic structural problem could he masked by reasonably good growth rates. But once the international environment deteriorated after 1981, the underlying structural problems became evident. It is less clear, however, whether the sacrifices of the last three years have measurably contributed to addressing these deepseated structural problems.

Thus, while the present Philippine crisis does have deep roots, this has not yet been fully recognized in the negotiations on adjustmcnl and resumed growth which have taken place to date. Certainly, until the coming into power of the Aquino government, it has been difficult to see any sustained effort to correct the fundamental structural imbalances in the economy.

The new government is currently engaged in a series of negotiations with the IMF, the World Bank-chaired Consultative Group and other donors. There is every indication that, given the severe pain which has been suffered over the last several years, especially by people at the lower end of the scale, the IMF is going to be more flexible with respect to the new program to be negotiated than it was in the last years of the Marcus regime - in terms, for example, of the deficit as a percent of GNP target. On the other hand, the government is likely to maintain the objective of retaining a realistic floating exchange rate and a moderate expansion of the money supply, in rddition to more specific objectives, such as the removal of price controls on agricultural goods, the continuation of the import iberalization program (reversed during the crisis), and other com~onents of a gradual decontrol policy in various markets. Recently, >olicy agenda reports were presented to the Philippine cabinet both m general macro policies and on specific rural sector policies by ;roups at the UP/Dilliman and UP/Los Banos. Both reports emphasize hat growth achieved through the mobilization of rural areas can 'field an improvement in the incomes of people at the lower end of The Philippine economy has deep structural problems of long standing. The crisis of 1984 only rendered the underlying problem more severe, in contrast to the situation of some other developing countries, e.g., in East Asia. The Philippines, by failing in the I960s to restructure its economy toward labor-intensive industrial exports on the one hand and to fully mobilize its rural economy on the other, was ill prepared for the deterioration of the external environment in the early I980s. As long as natural resources could carry the day in the I960s and/or foreign capital could be had for the asking in the 1970s, the basic structural problem could he masked by reasonably good growth rates. But once the international environment deteriorated after 1981, the underlying structural problems became evident. It is less clear, however, whether the sacrifices of the last three years have measurably contributed to addressing these deepseated structural problems.

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the distribution scale without conflicting with overall growth objectives. The key to that, as has been shown in other countries, is that as agricultural productivity increases, and as labor-intensive opportunities in new agricultural crops as well as in rural nonagricufture become available, rapid overall growth becomes consistent with an improvement in income distribution and a reduction of poverty. There is no doubt that a participatory, employment-oriented growth path can be generated in a labor-surplus country like the Philippines with the help of the appropriate macroeconomic policies, and that it would simultaneously generate faster growth, an improved distribution of income and the gradual elimination of poverty.

Thus, the current policy agenda as presented to the cabinet and endorsed in principle by that body seems to be right on the mark. We must recognize, however, that the determination of the new government and its capacity not only to accept this macroeconomic package but to implement it has still to be proved. It is still an open question whether the Aquino government will be a truly reformist government, in the sense that it is willing to step on the toes of some of the entrenched interest groups for the sake of the structural adjustment which it has rhetorically ag-eed is required. While it is, of course, much too early to be pessimistic - and one should recall that this government did not have a transition period and has been in office for only a few months at the time of this writing- there are some clouds in the sky. For one, while the private sector is being viewed as the main engine of growth in most of the pronouncements, one sometimes has the uneasy feeling that what is really meant is a return to the private sector environment of the late 1970s - monopoly capitalism, satisfactory to a small elite group, public and private, rather than the kind of market mechanism which could, with the help of some direct government action, yield complementarily between growth and employment and the protection of vulnerable groups. Such a truly participatory version of the engine of growth in a mixed economy can be utilized only if some of the direct controls, licensing systems and other interventions - including Hoard of Investment fiscal incentives, which are available only to large-scale enterprises - are eliminated over time.

What Frances Stewart has called the "primary payments system"' has to be relied upon as the first line of defense to ease the conflict between growth and distribution. This can be accomplished only with the pursuit of an efficiently labor-intensive, rural-focused growth path. The "patching up" through direct interventions and poverty redressal programs alone is not likely to work, even if the intentions are honorable (which often they are not).

But there is more to the achievement of adjustment with equitable growth than the pursuit of the appropriate macro policies as they have been and will continue to be negotiated in the Philippines. Much can and should be accomplished through the reallocation of public expenditures as between elite and mass clientele. In the course of the recent crisis, the IMF insisted on a reduction of expenditures to bring the budget defciet down from, say, five percent of the GNP to two percent, but without concerning itself too much with the precise allocation process. As a consequence, the maintenance of irrigation infrastructure turned out to be one of the casualties - a method of budget pruning later objected to by the World Bank.

Both the allocation of overheads as between rural and urban areas and the method of project identification within each category are at stake here and extremely crucial. In this respect, a much greater reliance on a decentralized decision-making process, permitting local governments to identify the priorities among competing public works projects, would correct the pervasive and persistent overcentralization of decision making of the past. tot present, at best, regional-level proposals are massaged in Manila, while centtal government line ministries are ultimately empowered to set their own priorities, with the precise allocation decisions often politically tinged. The essential task of eliminating bottlenecks in the way of the balanced rural growth which could become a possibility once the appropriate macroeconomic framework is in place requires much more activity at the provincial and municipal levels. Such decision making would be able to rely on the so-called "goldfish bowl" concept to ensure both better project identification and the minimization of the misallocation of funds in project execution - both of which have been the bane of public works projects in the Philippines, as in many other developing countries. There is little doubt that the identification of productive infrastructural investments by people on the scene and their knowledge of how much money has been allocated by a block grant from the center are critical to the removal of the bottlenecks currently inhibiting more vigorous balanced growth in the rural areas. All this requires, of course, not only a viable local government, but also the willingness to let some fiscal powers de-volve onto local governments, which would generate resources in addition to the block grants initially provided by the center.

Any effort to move a mixed developing economy along a balanced growth path with maximal, efficient participation of its underemployed workers requires such decentralized decision making with respect to both the physical and the organizational infrastructure. Yet even today, a dim view continues to be taken in Manila of the existence of the necessary entrepreneurial and technical capabilities among would-be medium- and small-scale rural industrialists, as well as among local government officials at the municipio and barrio levels. Consequently, any devolution of fiscal or project identification functions to the local level would have to overcome this rather formidable perceptual hurdle.

In a similar vein, the Philippine National Science and Technology Board structure, complete with specialized institutes, is, as in so many other developing countries, focused more on the frontiers of science and technology than on mobilizing and diffusing appropriate technology and market information. The agricultural sector still remains the best bet for furthc growth in the Philippines, as is indicated by the fact that even during the last two crisis years, agriculture has managed to maintain some modest growth (.8 percent in 1984, 1.3 percent in 1985), in spite of negative protection, terms of trade deterioration, fiscal disincentives, etc. The colonial habit of favoring traditional exports with respect to research and other facilities has been maintained in a relative sense, but the import substitution policies in toto have continued to relegate all of agriculture to the role of much cow to help create "under-the-table" rents for the new urban industrial elite.

The system, though professing under the new government to want to become more useful to the development effort, is still replete with heart centers instead of malaria control, kidney foundations instead of dysentery centers, and the usual preference for research 'n cash crops as opposed to food crops. These science and technology networks typically have substantial budgets and command substantial human resources. Modifying their budgetary systems so that the subsidy component is gradually reduced over time, thus forcing them to obtain contracts from the private economy, plus changing some of the internal personnel rules to provide individual incentives for work at the adaptive end of the spectrum, would constitute important dimensions of the needed reallocation of scarce infrastructural resources.

Finally, there is the question of land reform as a necessary (or at least helpful) component of a policy which will guarantee adjustment with equitable growth. As is well known, the land reforms propagated during the Marcus regime were restricted to rice and corn, and their implementation left something to be desired. Land under rice and corn covers only 20 percent of the total crop area, and tenancy actually increased from 18 to 25 percent between 1971 and 1980, all of which does not count the evasions under the legislation by parcelling out land to relatives, etc. Moreover, the most vulnerable of all agricultural groups, the,landless, were not handled appropriately, partly because of a lack of alternative employment opportunities outside the basic food crops. Increased underemployment among agricultural workers and the working poor in the rural areas usually results if land reform is not accompanied by the appearance of new labor-absorbing activities in these areas. Cleaning up the reforms in rice and corn and extending them to sugar and coconuts in the years ahead would undoubtedly make a substantial contribution to the achievement of equitable growth. But whether immediately extending reforms beyond rice and corn represents an essential ingredient of success is a matter which is less clear. The land ownership Gini in the Philippines is approximately .5, not at the extreme end of the spectrum for LDCs. And there are limits to what the fledgling Aquino government can attempt over the next couple of years.

But the fundamental questions remain: how committed is the new Philippine government to putting together a sequential policy package which would shift the economy to an alternative track, and how willing is the international community to support such an effort, including the protection of vulnerable groups in the transition? The abundance of natural resources and good terms of trade in the I960s and the easy availability of foreign capital in the I970s clearly made it possible for the Philippines to maintain an inequitable and biased growth path. The more generous mother nature, and the more generous one's creditors, the more tempting it is to postpone any potentially unpleasant changes in economic structure. Once the international environment deteriorated in the early I980s, however, the poverty of shortsighted policies became evident. Moreover, the current difficult adjustment period has not yet brought the Philippine polity to the point where it is ready to decide whether it simply wants to try to recreate the situation of the 1970s, with the help of the international community, or whether it indeed recognizes the need for more fundamental structural change which will withdraw rents from import-substituting industrialists, civil servants and the elite laboring class.

Conclusions

Every developing society is constrained by its initial conditions, but it also has at its disposal institutional, organizational and economic policy choices over time, yielding different capacities to adjust to external shocks with or without growth, and with or without equitable growth. The basic question before us is clear: can the more seriously affected debtor countries work their way out of the current crisis, i.e., can they adjust successfully without inflicting additional human costs on the most vulnerable portions of their populations? My response is in the affirmative. It is technically feasible to devise structural adjustment programs which, if given enough time, can put these countries on a sustained growth path and, with the proper use of additional resources from outside, avoid further reductions in consumption, especially at the lower end of the income distribution scale. This belief is based on the assessment that there exists no inevitable conflict between an improvement in the distribution of income and the resumption of growth, but that the inhibiting problems are likely to be of the political economy type in terns of both the required domestic and international action.

With respect to domestic action, the roots of the conflict between growth and a more extensive sharing of that growth are embedded in the structure of LDC economies. This structure has evolved during the past three decades, not just in recent years. Taking the Philippines as a case in point, the problem in many LDCs has been that the narrow basis of the development efforts pursued over the past three decades left most of the small- and medium-scale producers, agricultural and nonagricultural, out of the game. With virtually four-fifths of the population thus economically disenfranchised, economic growth was fuelled by ample natural resources early on, later supplemented by generous inflows of foreign capital. It is this structure which needs to be addressed if the current problem is to be solved. And this, in turn, depends heavily on all systems' willingness to effect real changes in macro and sectoral policies with the purpose of achieving balanced growth as between agricultural and nonagricultural activities in the rural areas while simultaneously enhancing the capacity to export industrial products, initially laborintensive and later more capital- and technology-intensive, on a competitive basis. While this is not the appropriate place to go into details of a proposed strategy of policy change for countries like the Philippines, it should be clear that the adjustment process as experienced in recent years cannot be amended without a full understanding of the underlying cumulative effects of monopoly power and domestic government interventionism which constitute the rest of the iceberg. A strategy of "adjustment with equitable growth" requires policies which ensure that more profits accrue to the small, competitive enterprise than to the large, protected oligopoly, to small, owner-operated farms instead of rural industrial estates, absentee landlords, etc. Domestic policies which encourage the efficient utilization of unskilled labor via rural mobilization or sustained nonagricultural export activity constitute the key; and the obstacle resides largely in inadequate domestic policies, to which the structural adjustment program must be addressed - on the assumption, of course, that the debtor country's own technicians fully agree with the diagnosis.

Improving the primary payments system through policy change would not necessarily take care of everyone at the lower end of the scale, including some unemployables and other poverty groups, which would have to be addressed separately by direct government action. But from the technical point of view, major increases in output and employment are possible without major additional adjustment costs, resulting in a simultaneous improvement in the distribution of income, respectable growth and the generation of sufficient exports to service debt.

The problems to be overcome, therefore, are not technical problems but problems of political economy. In many contemporary LDCs, the decision-making process seems to be adversely affected by the presence of plentiful natural resources and/or foreign capital. While additional resources should theoretically make a country more capable of making the necessary adjustments, they apparently also make it less willing to do so. This phenomenon has been evident in affecting the choice of the growth path followed by many LDCs in the 1950-80 period; it is true as well during the current crisis. It continues to be "human" for governments to avoid unpleasant decisions if some ready-made alternative is at hand. To mobilize the rural sector in a balanced, consistent and sustained fashion, and to permit the nonagricultural sector to turn outward consistently and make its increasingly diversified contribution to the financing of its own future growth,requiresa package of policy changes. Its adoption requires overcoming deeply ingrained habits of three decades of protectionism and an even longer period of paternalism and centralization in both the public and private sectors.

Recognizing the problem in its entirety is only the first step. Moving on it, given normal governmental myopia, is another. The secret of any successful adjustment policy is that the diagnosis be fully accepted, and that self-imposed conditionality be put in place and maintained. This means agreement on sequential policy changes liberalizing various markets in a persistent and logical fashion. It means not overstraining the administrative capacities of the government, yet keeping in mind the need for the packaging of related policies to provide minimal consistency. And it includes the willingness to step on some important toes, even if only for a short while.

But the successful outcome of negotiations between individual debtor countries and the international community also requires that the latter make an effort to overcome its own political economy constraints. Both parties need to get away from "under the gun' emergency meetings, reschedulings and other types of quick transfusions while conditions for one or two years of "good behavior" are imposed. We need instead to move toward a more independent and multilateral framework for reaching agreement on a country's current situation and its potential for achieving a fundamental restructuring with the help of additional foreign resources.

Such additional foreign resources may, of course, also be used for specific assistance to the most vulnerable groups while agreement on the changes in policy which may temporarily put these particular groups at risk are implemented. For example, there is no reason why some portion of a structural adjustment loan could not be specifically related to the short-term hurt inflicted on certain groups by the policy changes tied to other portions of the same package.

The initiation of such a medium-term reform program must rest squarely on the shoulders of the debtor country. The only way to render the ensuing negotiations credible, as well as acceptable, is to put the argument not in terms of more liquidity versus more conditionality, but in terms of how, with the help of more liquidity, policies can be restructured without politically unsustainable and economically wasteful additional pain for the system's human resources. But the donors must be just as willing to think in three- to five-year terms and to render the whole package credible with agreed-on resources alongside the agreed-on policy commitments.

Overcoming the rich countries' political economy problems also means the ability to render such resource ballooning fiscally possible. There is no reason to accept the fact that Gramm-Rudman and other parliamentary constraints on budget-weary developed countries must inhibit the international community's ability to provide capital ballooning on a country-by-country basis. Once the qualitative aspects of each bargain are understood and adhered to, the advantage of working for successful programs of "adjustment with equitable growth" over the not-so-attractive alternatives staring us in the face are self-evident. Realistically, no one expects huge additional NorthSouth capital flows to materialize in the near future; but the possible ballooning of resources over a three- to five-year period for the handful of countries each year who take the initiative is eminently reasonable. Once these new modalities do succeed in achieving adjustment with equitable growth in a creditable fashion, it may, moreover, be not too optimistic to assume that this will also loosen future purse-strings - not only with respect to official support from developed country governments, but also with respect to the resumption of truly voluntary commercial bank lending.

The alternative is a much greater likelihood of global recession in the presence of a stagnant Third World, not to speak of the threat of "conciliatory" or not-so-conciliatory default and its effects on national and international financial stability. It is clearly in the enlightened self-interest of both rich and poor nations to ensure that the necessary organizational and policy changes are put in place which would permit the LDCs to resume a sustainable development path, and not at the cost of the most vulnerable segments of their populations.

Notes

I. "Inequality, Technology and Payments Systems;' World Development 6:8 (1978).

CHAPTER 8

Poverty, Adjustment and the IMF

Tony Killick, Tony Addison and Lionel Demery

In a topic riddled with controversy, what is agreed on all sides is that, if they have any effect at all, IMF stabilization programs affect the distribution of income and are liable to impinge upon the interests of the poor. The controversies are about the nature of the effects, i.e., whether they tend to worsen or improve the poverty inequality situation or, indeed, whether it is possible to generalize on such a matter.

Earlier work at the Overseas Development Institute in London suggested that the evidence available at that time did not permit any generalizations on this subject, and that it was not a controversy that could be settled on an a priori basis. The ODI therefore embarked on a follow-up study' to examine the impact of macroeconomic adjustment on the distribution of income. The study includes five country studies - India, Jamaica, Kenya, Sri Lanka and Zimbabwe - and is now nearing completion. When finished, the study will include assessments of IMF and World Hank conditionality and will set out a case for programs of "adjustment with equity." Associated with this project, ODI has also collaborated with various international agencies, including UNICEF, the ILO, the World Bank, UNCTAD and the Group of 24, in the preparation of specific papers dealing with aspects of the subject at hand. It is currently finalizing plans for further work in this area: on the operation and effects of monetary policy in primary producing LDCs; on the impact of adjustment programs on agriculture; and on the integration of adjustment and poverty alleviation programs.

This paper borrows heavily from various papers prepared in the course of our work and also from the work of others who are being increasingly drawn into this previously neglected area of study. This paper falls into four principal sections. The first explores the relationships between balance-of-payments adjustment and poverty; the second examines the position of the IMF in these matters, including a statement and assessment of its policies; the third asks whether it is possible for stabilization/adjustment programs to protect the poor within the framework of existing arrangements and policies; and a summary outlines the content of a possible program of "adjustment with equity."

Adjustment and Poverty

One problem in assessing adjustment's poverty impact is that of separating out the effect of the policies per se from the poverty changes which would have occurred in the absence of the chosen measures. Given that real incomes are often falling prior to the adoption of adjustment measures, how much of their change after the program's implementation can be attributed to the new policies? The IMF has emphasized this problem in its reluctance to evaluate the poverty impact of Fund-supported programs.

This is an important question, but one which has no easy answer. However, from the viewpoint of poverty alleviation, it 'snot necessary to have a complete specification of the channels through which adjustment impacts on the poor. A rough identification of the main channels is often sufficient to indicate who is at risk and what measures should be taken to assist them. While it is useful to know whether increasing poverty is due to world recession or government policies in order to apportion blame, it is largely immaterial to the poor themselves what is the exact cause of their destitution. Although the impact of adjustment on poverty remains imperfectly understood, knowledge is sufficient to indicate the following impor tant mechanisms.

Demand Management Policies

Changing the fiscal and monetary "stance" affects poverty through its effect on the level of demand within an economy and thence the level and composition of output. Cutting government expenditures will reduce the government's demand for output from the rest of the economy and will generally lead to reductions in output, employment and incomes within the private sector. Tighter credit policies will have similar effects.

The exact nature of these effects is much disputed, and their impact on income distribution is still more complex. Much depends on the economy's basic structure, with the poor being more vulnerable to demand effects in the more developed countries. In Chile, the severe fiscal squeeze applied over 1975-76 (partly to correct a previously overexpansionary policy) achieved some success in curbing hyperinflation, but at the cost of substantial falls in real incomes and employment. With much of Chile's poor concentrated in the informal sector and dependent on the ebb and flow of urban incomes, poverty correspondingly increased. The ranks of the existing poor were then swelled by the unemployed "new" poor. Similarly, in Jamaica, where poverty is largely urban, the public expenditure and employment reductions of the 19805 have increased urban poverty. In contrast, in Africa, where most of the poorest are dependent on subsistence agriculture, the demand management measures taken after both the 1973 and 1979 oil price shocks seem to have had the greatest impact on urban wage-earners, with the rural poor afforded some protection from the demand effects by their lack of integration in monetized activity. Rural poverty groups have been more affected by the direct effects of fiscal cutbacks on rural clinics and schools, as well as the decline in government programs aimed at boosting their productivity.

In support of fiscal stringency, governments have to choose which expenditure items to cut and which taxes to raise. These choices have different effects on different social groups, depending on their consumption of government services and the incidence of taxes and benefits.

Cuts in social service programs are frequently implemented during the course of fiscal adjustment; the real value of existing programs is often allowed to decline, and new programs are shelved. For example, in Zimbabwe, the 198485 budget reduced allocations to social. service ministries by over 19 percent. In addition, when savings have to be made, it is usually easier to cut back future investment rather than seek greater economies in recurrent budgets; and within the latter, it is easier to maintain employment but allow reduced provision of items such as drugs and school materials.

Reductions in health budgets can have severe effects on the poor and will usually intensify existing inequalities in health care. For example, priority is often given to maintaining urban hospitals as against protecting the expansion of rural health services, where the poor have the greatest access. In Sao Paulo state of Brazil in 1982, a cut in the expanded immunization program contributed to an outbreak of deadly communicable diseases among children.' In Ghana, cuts in primary health expenditure during 1984-85 contributed to a rapid increase in the incidence of infectious diseases and related mortality. Increased health charges will impact particularly severely on the poor.

Likewise, cuts in education budgets can reduce the ability of the poor to develop their "human capital" and therefore raise their incomes. Increasing cost recovery may be a necessary budgetary measure, but introducing or raising charges for education usually reduces educational access by poor children. In Nigeria, state governments have imposed fees on both primary and secondary education and made parents responsible for the entire cost of school books without offering compensatory protection for poor families. Consequently, the letter's enrollment rate has fallen drastically. In contrast, university education (which mainly benefits wealthier families) remains largely free.

The reduction of poverty alleviation projects is common in adjustment programs. In Chile, a child-feeding program was cancelled in the 1983 budget, and this was correlated with increased malnutrition among children under five years of age (which then subsequently fell upon the program's reintroduction).

Price Measures

The prices paid to producers for their crops are commonly government-controlled in LDCs. Raising food prices to restore production incentives is often essential to assist the recovery and expansion of food output and to reduce the balance-of-payments burden of food imports. In the absence of consumer subsidies, an income transfer from consumers to producers will result. In countries wherb small-holder production predominates, food price increases will benefit low-income farmers who are able to sell food surpluses but will adversely affect urban poverty groups and food-deficit producers. Similar effects will be observed in LDCs with higher concentrations of land ownership, but additionally, the real incomes of landless rural laborers may fall unless the increase in labor demand by farm owners provides sufficient compensation (and where rural unemployment is high, the offsetting wage increase will be small).

Reduction of food subsidies without compensatory measures can increase poverty. Although food subsidies are generally an inefficient way of benefiting the poor (since higher income groups also benefit), their removal can quickly increase malnutrition. For example, in Sri Lanka, there is some evidence that the reduction of food subsidies beginning in 1977 was correlated with an increase in malnutrition. In Zambia, the price of maize meal (the main consumer staple) was raised in one step by 50 percent in 1985 as the first stage in removing the subsidy, with adverse effects on the urban poor. However, in Tanzania, the removal of the maize meal subsidy in 1984 had less than the expected effect on nutrition, because a high proportion of the commodity was being traded on parallel markets at "free" market prices. If price controls are not operating effectively, then their removal, although publicly dramatic, will not have significantly adverse poverty effects. Since the poor spend, on average, a higher share of their budget on food, at least in the towns, the negative real income effect of food price increases is more severe for them than for higher-income groups.

Increases in domestic export prices will have mixed effects. While most LDCs have little influence over the world prices of their exports, they can increase producer incentives by raising the domestic prices of their "exportables" either through reduced taxation (where producer prices are controlled at below world market equivalents) or through devaluation.

If the poor are employed or self-employed in activities producing "exportables," then beneficial effects on their incomes can result. In parts of Africa, many of the poor are engaged in producing export crops, although the largest gains will go to better-off small holders with greater access to land and capital. Even if export agriculture is dominated by plantation production (as in Central America, the Philippines and Sri Lanka), the poor may benefit through increases in rural employment. But there are doubts about the effectiveness of price changes per se in reducing poverty. Many of the poor are located in areas ill served by rural infrastructure, input and capital availability, and marketing facilities. Increases in output prices may not be of much benefit to such groups if their capacity to increase output remains severely restricted. Shortages of imported wage and intermediate goods may also make it difficult for them to translate higher cash incomes into improved living standards.

Over the longer term, correcting exchange rate overvaluation can have beneficial employment effects by encouraging greater substitution of labor for capital in both industry and agriculture. Overvalued exchange rates encourage the use of imported capital relative to local labor. However, increasing the prices of exportables also has some adverse poverty effects. Increasing the domestic price of exportables can harm poor groups where such commodities are staple foods, as in the case of rice in Thailand or beef in Argentina. In addition, devaluation, through raising the domestic price of imports, can have severe poverty effects. In Jamaica, which has a high food import dependency, the devaluation of 1984 onwards generated large food price increases. Similarly, the 1986 devaluation in Guinea is said to have quadrupled the price of imported rice. In Sri Lanka, an average of 35 percent of the consumption needs of lowincome families are met through imports, which makes them particularly vulnerable to the price effects of devaluation.

Real Wage Cuts

Real wage cuts are often a deliberate policy measure, particularly in the public sector, to support government expenditure controls. Real wage falls also occur in response to austerity itself and are often falling prior to adjustment. In Africa in the 1980s, wage controls have been increasingly used alongside producer price increases to shift the rural-urban income differential in favor of agriculture and away from urban employment. For example, in Tanzania during 1980-84, the World Bank' estimated an increase in real farm incomes of 5 percent, while urban wage earners faced a real income fall of 50 percent. In Ghana, farm incomes stagnated (but are now increasing) while urban real incomes fell by 40 percent over the same period.

In Latin America, real industrial wages fell by 2.6 percent in 1982 and by a further 6.6

percent in 1983. While those in jobs are often the relatively better off in LDCs, real wage falls of the magnitude of 17 percent in Peru and 16 percent in Argentina in 1985 have certainly swollen the ranks of the poor. Similarly, in Mexico, by the end of 1985 urban minimum wages in real terms were 72 percent of their 1980 level, with further falls expected as adjustments to the loss of oil revenues are undertaken. Open urban unemployment in 1985 was 17 percent in Chile and about 16 percent in Peru, although the region's unemployment level is down from its 1984 peak.'

The overall impact of adjustment will therefore depend on the measures chosen, the time horizon over which they are applied, the structure of production and asset ownership, and the survival strategies applied by the poor. It is probable that stabilization measures over short time horizons have the severest impact on poverty, given the type of government programs which are usually reduced most severely. Structural adjustment measures with longer time horizons give greater opportunities to incorporate the poor into the restructuring of production. In addition, gradual adjustment programs give the poor more time to adapt than under "sharp shock" stabilizations.

However, much depends on the base from which adjustment begins. In situations characterized by hyperinflation, chronic shortage of basic goods and collapsing government services, the poverty impact of rapid stabilization will almost certainly be less than continuing with existing policies. However, this caveat provides no reason for abandoning the search for stabilization measures which give better protection to the poor.

IMP Conditionallty and Distribution

The Fund's official position on distributional issues can be gleaned from a number of sources, including speeches by its managing director (usually reprinted in IMF Survey) and special papers and pamphlets produced in its defense, such as that of Nowzad? Among the most useful recent statements are a pamphlet by the Fund's current managing director, Jacques de Larosiere, entitled Does the Fund Impose Austerity?' which was produced in response to a resurgence in criticism by LDCs pursuing Fund-supported programs, and a recent speech to the U.N.'

The pamphlet defines austerity as reduced output and per capita incomes as well as increased unemployment and presents six reasons why the managing director believes that accusations against the Fund are misconceived. These can be summarized as follows:

a) Economic adjustment via the standard IMF policy measures is inescapable, and many countries have aggravated their difficulties by postponing adjustment to recent external economic shocks. Thee alternative of import restrictions and expansionary fiscal and monetary policy has a worse outcome for output and employment than adjustment through IMF measures.

b) Fund-supported adjustment is not synonymous with lower growth in the long run. Indeed, the Fund's policy conditionality will, through improving the efficiency of resource allocation, raise the growth rate over the longer term.

c) While these programs do entail austerity in the short term, this is less than the costs of not adjusting, since the Fund is able to provide both its own finance and to act as a catalyst for additional international official and commercial lending to ease the adjustment process.

d) Fund programs designed for the short to medium term are usually associated with, and supported by, World Bank project and program lending for longer-term development purposes, and this supplies the necessary "supply side" support. However, increased finance of the activities of both multilateral agencies is desirable to further improve the effectiveness of their cooperation.

Turning specifically to the distributional impact, the pamphlet makes-the following two points :

e) The Fund and the country's policy makers together assess the macroeconomic constraints operating on the country. These, in association with the available external financial resources (including the finance the Fund agrees to provide), determine that certain measures must be taken withsegard to the level of domestic absorption, the division of national income between consumption and investment, and the division of national output between traded and nontraded goods. This, in turn, implies policy targets for such variables as the public sector deficit, the rate of domestic monetary expansion and the exchange rate.

The government must then make its choices as to how the required adjustment effort is to be distributed within society and on the items of public expenditure which must be reduced. The impact of the Fund-supported program on the poorest groups is determined by the policy choice of the government concerned and not by the Fund.

f) Finally, the effects of specific policy measures such as exchange rate adjustment may, in any case, have benefits for the poorest groups, particularly in countries dependent on export agriculture and where small holders are disadvantaged by overvaluation, which in turn protects urban groups.

In summary, the Fund holds to the position that its assistance is requested by the government concerned and that it does not impose conditions but merely assists, with finance and policy advice, those responsible for implementing the stabilization program.

Responsibility for adjustment costs must be attributed to the underlying economic situation that produces the need, in the first place, for corrective action rather than to those who assist, to whatever degree, in the formulation of these policies.'

While Fund missions have often noted sources of economic disequilibria with underlying distributional causes, and while Fund programs often include policy measures with explicit distributional ramifications, the IMF has nevertheless remained reluctant to monitor the distributional consequences of implementing its programs. This is reflected in the small volupw of past Fund research back-up on the issue of stabilization and distribution which could be of value to its country missions. The only published item of Fund research directly concerned with the distributional consequences of stabilization is Johnson and Salop,' ° which works almost entirely with the functional distribution of income between labor and capital. While this framework may provide some initial guide to the effects, its relevance in relation to low-income countries reliant on small-holder agriculture is limited." Papers by research staff on stabilization in general have touched on some of the distributional issues," and research on specific policies - for example, food subsidies -has considered their impact on the poor. However, given the policy importance of this subject and the consequent amount of criticism directed at the Fund, it is surprising that the Fund has neglected stabilization and distribution as a research issue. However, it is known that the IMF's Fiscal Affairs Department has now completed a study on stabilization and distribution for internal dissemination," and a new publication has been in production for some time.

The Fund has four principal reasons why its country missions cannot involve themselves extensively with the distributional consequences of their programs. Two of these stem from the Fund's mandate, while the remainder arise from the Fund's view of the difficulties of monitoring changes in poverty.

a) The mandate of the IMF directs country missions to tasks of restoring balance-of-payments viability as the overriding objective of its financial support.

b) The choice of the distributional objective by government is largely an internal political matter and therefore outside the scope of an international organization.

c) If Fund programs are to be evaluated, then their distributional outcomes must be compared to some feasible alternative policy set. Identifying such a counterfactual is conceptually and empirically too difficult to have practical application on Fund missions.

d) The quality and quantity of data on employment and incomes, as well as poverty and inequality measures in LDCs, is not such as to allow an adequate comparison of welfare both before and after the programs' inception or continuous and close monitoring of the programs' effects.

We take each of these points in turn.

The IMF's mandate, in particular Article l, is well known. That mandate has been interpreted as limiting the Fund to providing short-term balance-of-payments support to restore balance-of-payments viability as its priority objective.' • Table l, which details the objectives of Fund standby arrangements, shows that balance-ofpayments and inflation targets predominate. Protection of the poor against possible adversee effects is found as an explicit objective in only one standby program, and that was during the 19606 A similar survey for the 1980s is not available, but given the tightening of conditionality after 1982, it is unlikely thatt country programs have generated any increased concern with the poverty impact.

TABLE I

Objectives of Standby Arrangements as Identified by IMF

Number of Observations

1964.69 1970-75 197479

A: General				
1. Balance of payments:				
a) Quantified target		7	8	10
b) Nonquantified objective		3	2	-
2.Infationtarget	2	3	7	
9.Quantified economic growth target		4	8	9
B:Specific (selected items)				
4.Raise/sustain level of investment		2	8	4
3.Raise/sustain domestic saving	1	3	6	
6 Raise capacity utilization		5	-	5
'7 Promote import substitution	5	6	2	
8.Promote exports		5	9	7
9.Reduced subsidies/increased taxation on consumer goods	3	-	7	
10. Restrain growth of money wages		2	2	4
11. Protect poor agaimt possible adverse effects of program	1	-	-	
12. Pridngpoedes	5	4	8	
IS. Refon4improvement of tax system	8	7	6	
14. Interest rate policy		1	3	4

NOTE: For each entry, the maximum number of observations is 10.
SOURCE: NE, special survey conducted by ON in 1981. See T. Rillick, ed, The Quest for Economic Smbilsttion: The IMP and the Third World (London: Gower end ODI, 1984).

Concerning the choice of distributional objective, the Fund has consistently maintained that focusing programs on broad macro instruments such as the rate of domestic credit expansion and the exchange rate allows government a wide range of policy choice within the basic macroeconomic constraints of the program. It is argued that if a government-wishes to protect poor groups, then it can do so through a change in budget priorities from items such military expenditures and social expenditures directed to wealthier income groups toward allocating greater resources to specific poverty groups. The tax system can be altered to broaden the base of personal income tax; export duties which fall on small farmers can be removed; graduated property taxes can be introduced; and the indirect tax structure can be altered to switch a proportion of revenues from basic to luxury items. More controversially, it argues that the removal of food subsidies will redistribute income from urban consumers to rural small holders who may make up the bulk of the low-income group, and poor groups could be both compensated and better targeted through specific poverty programs.

The Fund maintains that all these measures have been frequently proposed by its country missions but rejected by the authorities for political reasons. The Fund argues that although governments may have distributional objectives, these are not necessarily directed toward reducing poverty and that, in fact, the implicit objective of many governments is to redistribute incomes in favor of middle- and high-income groups, particularly toward state employees and the government's political supporters. Thus government health, education and employment programs are often biased toward those groups who are the most politically vocal; taxes and low producer prices are used both to maintain public salaries and for transfers to cover losses in inefficient public enterprises; and monopoly positions in trade and industry are granted to those winning political favor. Fund missions have ar:ued that, ironically, the most controversial aspects of their recommendations are those measures of price and public sector reform which redistribute incomes back to the poorer groups and which are opposed precisely because the reforms will reduce the incomes of those benefiting the most from existing policies. IMF officials further maintain that if a government requests country missions to evaluate alternative policy approaches to meeting distributional objectives, then the Fund is prepared to do so.

The managing director's recent speech, while expressing great concern with the deterioration of the human condition in many LDCs, retains a very cautious stance on the role it might play in poverty alleviation measures:

The Fund has neither the mandate nor the staff and the technical capacity to design health, nutritional, or educational programs.... This does not mean that the Fund cannot do its part to help developing countries protect basic human needs. Over the past two years, we have, in fact, expanded our contracts with some of these "specialized" agencies in order to advance our mutual understanding of hbw the most vulnerable groups might best be protected during the adjustment process. In addition, when requested by a member country, Fund missions may consider with the authorities the implications of alternative approaches to adjustment for the distribution of income [emphasis added]."

However, although the Fund has indicated a willingness to respond to requests, its staff has not been optimistic about whether they would yield useful results. The report of the Fiscal Affairs Department (cited earlier) concludes that satisfactory empirical analysis is impossible.' ° This brings us to the counterfactual problem and the data problem which form the basis of the Fund's research pessimism.

The distribution of income in a country seeking Fund support will almost certainly not be sustainable, since the country's state of payments disequilibrium will require some policy action whether or not a Fund program is implemented. The Fund consequently takes the position that a simple comparison between the pre-program and post-program distribution is not useful in evaluating the impact of its policies." Given this problem, further methodological difficulties are raised:' °

a) Should the comparison be made with the distribution which would arise in the absence of a program and as economic disequilibrium increases, or against an alternative policy set (either may be termed a counterfactual)?

b) If the latter is chosen, can an alternative policy set be A. identified, taking both the prevailing availability of concessionary and commercial finance and the current world economic environment as given? The consensus among Fund staff is that for most LDCs, an alternative and adequate set of stabilization policies is difficult to identify, given the time horizon imposed by the current availability of external finance. In support of this view, they argue that most LDCs do not themselves identify an adequate program before approaching the Fund, or they propose a program which requires, financing at levels which are not currently available from the Fund, commercial sources or aid donors_

c) Even if the above difficulties are met, the Fund takes the position that economic analysis is currently not such as to allow an accurate comparison between the Fund program and the counterfactual. Two difficulties are raised: first, the absence for most LDCs of general equilibrium models that allow simulations of alternative policy sets, and second, the absence of adequate cross-section and time series data by which to evaluate the effects of different policies.

This brings us to the impediments to research arising from data problems. Fund staff have raised the standard problems concerning both the choice of variable to measure welfare and the actual availability of country data on the chosen variables. It is argued that as a minimum, a detailed income and expenditure survey is required close to the point in time at which the program is implemented." In addition, data would be required on the consumption of public services by income group, as well as the distribution of public sector employees by income group. These, and difficulties concerning the underreporting of income (particularly of low-income budgets), application of different measures of poverty and employment, and obtaining time series data are cited as substantial obstacles to re-search.

In summary, therefore, the Fund's position is that its mandate directs its country missions to concentrate on the balance-of-payments target as the primary objective and that distributional aspects are the concern of the government, although a mission if requested "may" offer advice on the distributional effects of alternative adjustment programs. However, in the IMF's view, the methodological and data problems are of such a degree that in almost all LDCs a close monitoring of a program's distributional or poverty impact is impossible.

An Assessment

We turn now to the adequacy of the Fund's reasons for not involving itself in distributional questions. In the first instance, how convincing are the arguments that the IMF's governing mandate precludes the inclusion of income distribution issues in the formulalion of its stabilization programs? While it cannot be denied that the principal objective of its mandate is to secure restoration of balance-of-payments viability, there are two chief reasons why greater consideration of distribution by the Fund would lead to the more effective discharge of its responsibilities under its mandate.

First, balance-of-payments difficulties can originate from distributional conflicts and objectives originating in the domestic economy. Simple monetary prescriptions, though they provide a measure of stabilization in the short run, will do little to remove the underlying forces giving rise to the disequilibrium. Treating the payments problem in an LDC as a purely monetary phenomenon cannot restore equilibrium over the longer term, where such a solution requires changes in the "real economy."' ° Second, stabilization policies generally influence the balance of payments through effecting changes in the structure of production, consumption and incomes, as (for example) in the case of devaluation. For devaluation to improve a country's payments position and to move the structure of output away from the production of nontraded to traded goods, a change in the structure of incentives in favor of traded goods must take place, and this can only be mediated through a change in the structure of incomes. In other words, the process through which a devaluation works involves significant income distribution changes. Khan and Knight express this succinctly :

In general ... as long as the devaluation succeeds in temporarily altering the real exchange rate by raising product prices in domestic currency relative to factor incomes, one would expect it to have an initial stimulative impact on aggregate real supply.... Second, since no supply-side effects would appear if all factor incomes were perfectly indexed, the stimulative effects of devaluation depend onthe degree to which it reduces the real income of one or more factors of production [emphasis addedl."

Even when stabilization requires only disabsorption through the reduction of the fiscal deficit, the composition of the fiscal adjustment (and therefore its distributional consequences) is not entirely unrelated to the balance-of-payments outcome. Some components of government expenditure have greater import content than others, and their adjustment will therefore have greater impact on the balance of payments. Similarly, insofar as disabsorption involves private expenditures, the import intensities of which will vary, the choice of which components to cut will have implications for the effectiveness of the policy. It should not therefore be a matter of indifference to the Fund, and not simply a domestic political issue, as to which components of expenditure are reduced during dis-absorption. In summary, there are technical grounds for a greater concern by the Fund over distributional questions.

However, there are broader egalitarian and humanitarian grounds in favor of a more active concern by the IMF over distributional issues. If stabilization policies are causing hardship among those groups least able to cope, there is a strong case for changing the IMPS governing mandate to give country missions an explicit responsibility to devise policies which either protect these groups or at least minimize stabilization's impact upon them. The World Bank, for example, studies the distributional impact of its Structural Adjustment Loans (SALs), and this may point the way. There has been an increased dialogue between the Fund and other international agencies concerned with equity issues (e.g., ILO and UNICEF), but the evidence so far does not suggest that these exchanges are likely to have much opgrational impact on Fund-supported programs. Moreover, it is difficult for the Fund to sustain a position of distributional neutrality, since, as Killick observes,

... by remaining aloof from such questions [of income distributions the Fund tacitly accepts the distributional policies of the government in power, whether it likes them or not. This, more often than not, implies a de facto alignment with forces opposed to reduced inequalities ... the politics are inescapable."

It must be recognized that while a more active role for the Fund in this context would be desirable, it is nevertheless a reality that some governments would not wish to entertain equity-based stabilization programs which would have an adverse effect on the relatively wealthy.

However, while these distributional issues are a sensitive area for the Fund, sensitivity of subject matter has not deterred the Fund from other policy controversies - for example, on the respective roles of the public and private sectors. If the Fund were to see its role as that of assisting least-cost adjustment, it would be essential to take a view of the likely impact of program design on poverty groups. To do so may also have a crucial bearing on the likelihood that an agreed program will be executed and sustained, as past difficulties over the reduction of subsidies have demonstrated (although we admit that this consideration will not necessarily point to protecting the poorest).

Moreover, while it is true that there will be practical difficulties for the Fund both in implementing an assessment of the distributional impact of its policies and in monitoring the effects on specific groups, it has overemphasized the problems of conducting such an exercise. Although specification of a counterfactual to Fund policies does have a number of difficulties, these are problems which apply not just to the distribution question. Rather, the problem is encountered in evaluating the impact of IMF policies compared to possible alternatives on a whole range of variables, including the balance of payments, inflation and growth. The Fund's argument that it is very difficult to specify an adequate alternative set of policies to form the basis of a counterfactual is not strong. Alternative policy packages, such as that of the "real economy" approach, which focuses greater attention on the structure of the supply side, have been proposed," while the recommendations of the "structuralist" critique, particularly with regard to lengthening the period of adjustment, should be borne in mind." It is possible to derive a counterfactual by modifying the IMF policies themselves - for instance, specifying a devaluation of equal size to that recommended by the Fund, but increasing the time period over which it would be implemented. Deriving alternative programs by modifying the size of required policy changes is particularly important, since LDC disagreement with the Fund often concerns not the question of whether a policy change should be implemented or not, but the size of the required change." IMF staff have already undertaken simulations in which trade and capital liberalization are pursued at different speeds and in different sequences, and significant variations in adjustment costs in terms of output and employment are shown to exist depend ing on the policy mix and timing.'

On the question of data by which to monitor the programs' effects, it is true that data paucity. presents problems to conducting this exercise. However, a monitoring exercise does not necessarily require complex absolute or relative poverty measures on a country-wide basis. Rather, a careful selection of a sample of poverty groups from both regions and activities and the collection.of data at regular intervals could generate sufficient information to monitor the effects of the policy changes. In that regard, each sample group would provide information on price changes over time in their basket of consumption goods, changes in their consumption of health and education services, alterations in their employment patterns, and specific information on nutrition and child mortality. It is in this respect that if the Fund were to broaden its concerns, then a closer relationship between the IMF and organizations such as UNICEF, which have specific expertise in monitoring the status of vulnerable groups, would be of benefit."

There are two further topics of particular current interest. The first relates to the magnitude and direction of the net flow of resources from or to the Fund. It is not an entirely simple matter to obtain regional information on net flows, but it appears to be the case that there was a small net return flow from Africa to the IMF in 1985, that there is likely to be a much larger return flow in 1986, and that this feature may continue in 1987, depending on the extent of use of the Structural Adjustment Facility.' e There will be corresponding increases in the share of IMF credits to major debtor countries in Latin America and elsewhere. This marks a reversal of the situation in the preceding decade, when there was a considerable increase in the absolute value add share of Fund resources going to Africa.

Associated with this are the well-known difficulties which some african countries have been experiencing in meeting their repurchase obligations to the Fund as they become due - both providing the Fund with a motive for wanting to reduce its exposure in Africa and drawing attention to the danger that it will be actually worsening Africa's financing problems in the near term. Indeed, one interpretation of the initiatives by U.S. Treasury Secretary James Baker to secure more funds for Africa-via the Structural Adjustment Facility and the eighth replenishment of IDA - is to ensure that African countries will be able to meet their obligations to the IMF.

The relevance of the above to the theme of this paper, of course, is that a large proportion of all those living in poverty are Africans, and that Africa is the continent which holds by far the worst record for long-term economic decline. Although we are far from assuming any one-to-one relationship between Fund credit and the welfare of the poor, it would nevertheless be difficult to reconcile an adequate Fund response to the problem of poverty with a substantial and sustained net withdrawal of resources from Africa, particularly from those countries with the most severe economic problems.

The second additional topic that may be taken up here relates to the operational interpretation that iss to be given to the new insistence that Fund programs should become more "growth-oriented." Traditionally, the Fund has always given priority in the design of its programs to the restoration of "viable" balance of payments to the borrowing country. "Targets" with respect to such variables as the rates of economic growth and inflation have always been strictly subordinate to the payments objective.' ° We may now ask, does the new stress on growth mean that henceforth, the achievement of some minimum growth target will be treated as a constraint in the design of Fund programs? The answer of the Fund's management appears to be negative on thins ° and although the new agreement with Mexico has interesting provisions for the protection of growth, these reportedly do not involve the resources of the IMF. But if growth is not to be accepted as a•constraint, it night be asked, what is the operational significance of the "new" policy?

In a similar vein, it can be asked whether the Fund will henceforth be taking a less exclusively negative view of the role of domestic credit in its programs. Within the monetarist framework, credit is viewed as weakening the balance of payments and increasing aggregate demand, but it can also be viewed as contributing to capital formation and the possibilities of structural adjustment. A related question arises concerning the composition of government expenditures in Fund-assisted programs. The experience in the past has been that governments faced with the necessity of restraining their spending have often found it easier or more expedient to cut back on capital formation than on the recurrent budget. At an earlier date, the Fund gave consideration to the question of whether in its programs it should seek to safeguard against this danger, but decided against it. It is a question that now arises with more force - for governments as well as the Fund - in the content of growth-oriented programs, and it would be valuable to know the Fund's current thinking on this subject.

Can Present Arrangements Protect the Poor?

Quite apart from the specifics of Fund programs, there are some larger, more systemic questions about the extent to which the present policies of those governments which have a controlling say in the policies of the international agencies are consistent with attempts to protect the interests of the poor in the adjustment process.

Perhaps the most fundamental point is one that will be thoroughly familiar and hence needs no elaboration - the retreat, at least until very recently, from the notion of adjustment as an international process involving surplus as well as deficit countries. Leaving aside the special situation of the United States, the effect of this, of course, is to thrust a disproportionately heavy burden on policies and levels of economic activity in deficit countries, which include many of the poorest countries in the world. This basic fact of life in international monetary arrangements - the de facto rejection of effective surveillance of surplus country policies - is one which is bound to set limits on what can be achieved by specific measures to protect the interests of the poor.

Related to this is the question of the overall adequacy of financial flows to low-income countries, within which the efforts of the IMF must be viewed. The prospects on this do not seem good. Much emphasis is now placed by donor nations on the importance of private flows, but the overwhelming evidence on this is (i) that the volume of such flows - as regards both commercial bank lending and direct investment - has been declining in recent years (to a spectacular extent in the case of net commercial bank lending); and (ii) that such flows aree in any case concentrated on the relatively advanced developing countries. There is fairly general recognition, in fact, that the poorer LDCs require more concessional finance, but real aid levels have been fat recently, and the OECD does not think that a real overall growth rata in excess of 2 percent per annum is likely to be forthcoming in the foreseeable future."

While it is probably true that a larger proportion of available aid flows will be directed to poor countries in sub-Saharan Africa, there is, even so, likely to be a substantial shortfall from the estimated needs of that continent. A recent World Bank study" shows an unfilled financing gap of $1.5 billion, implying a 30 percent increase over the actual aid level of 1984 and a 20 percent rise over currently projected levels.

There are, in any case, problems with the present concentration on the financing needs of the (mostly Latin American) major debtor countries and of Africa, in that populous and poor countries of Asia and elsewhere are in danger of being left out. This issue arises most acutely as it relates to China and India - countries which will take no advantage of the new Fund Structural Adjustment Facility and which will experience real reductions in IDA loans under the eighth replenishment, the second successive cut in the case of India. However, it is also an issue for other low-income Asian countries, such as Burma and Sri Lanka. There appears to be a major risk that present policies will result in a neglect of the undoubted needs of countries containing very large numbers of people living in acute poverty. This too is part of the global context in which the efforts of the Fund should be set.

It should also be borne in mind that even for the countries of Africa which are currently receiving the special attention of aid donors, aspirations are exceedingly modest. The World Bank estimates of financing needs referred to above are based on the objective of merely halting the decline in per capita consumption by 1990 and of achieving some growth thereafter. On the Bank's own estmates, this would leave consumption standards in Africa well below the levels achieved in the 1960s, Even so, as already mentioned, this very modest target leaves a financing gap that appears unlikely to be filled.

The question, then, is whether the global economic environment within which the IMF seeks to assist developing countries is such as to permit a process of adjustment which could effectively protect the living standards of those in poverty. Given that its principal task is in the balance-of-payments arena, and given the small size of its own resources, there is a strict limit to what the Fund could achieve even if it were to adopt a more active antipoverty stance.

Toward the Design of Adjustment with Equity

Devising adjustment-with-equity strategies does not require any radical breakthrough in knowledge. Rather, it involves marrying adjustment policies to cost-effective poverty measures. Consequently, it can draw on the already existing development strategies of redistribution with growth, employment generation and basic needs. While the latter strategies point to no panaceas, they do provide a basis for the formulation of "poverty-oriented" adjustment. In addition, there have been breakthroughs in the delivery of cost-effective health care. UNICEF" has developed the most comprehensive set of recommendations, but World Banks SALs are often supported by poverty projects, although in the 1980s the Bank has given more priority to adjustment per se and less to poverty concerns compared to the "McNamara years."

The following policies have been suggested by the advocates of adjustment with equity.

Restructuring Government Expendttures

Poverty-oriented adjustment would attempt to balance the maintenance of public expenditures necessary to support adjustment (e.g., infrastructure) with the protection of expenditures serving the poor. While this impliess some tradeoff in expenditure decisions between the needs of adjustment and poverty alleviation, this tradeoff can be reduced by improving the efficiency of all public expenditures.

Social expenditures could be given priority before defense and "prestige" urban projects. The Indonesian adjustment program initiated in 1983, while restraining public expenditure growth, has increased the share of the social sectors in the development budget, with more resources devoted to child immunization and family nutrition. However, this is now threatened by the increased stabilization effort needed to respond to the 1986 fall in oil revenues. In 1985, Brazil initiated a social priorities program emphasizing the poor which is now receiving increased World Bank project support However, protecting social expenditures is only part of the story, and both UNICEF and the World Bank have advocated restructuring social service expenditures to raise the efficiency with which they discriminate in favor of target poverty groups. Investment in social services has the additional advantage that they are generally more labor-intensive and less import-dependent than other activities.

Before reducing food subsidies, other subsidies could be cut first (e.g., those on energy, or those directed to public enterprise industries, such as national airlines). More importantly, food subsidies can often be redesigned to increase their benefits to the poor and to assist fiscal restraint. The largest subsidies are often applied to foods mainly consumed by middle- and higher-income families; e.g., in the Philippines, only 16 percent of the beef subsidy benefits the lowincome group. Better targeting requires identification of those needing nutritional support and of the type of food required. For example, in Brazil, subsidizing legumes would transfer about 39 percent of the benefit to the low-income group compared with 18 percent for the bread subsidy?' Targeting can be further refined by restricting the sale of subsidized foods to areas where purchases by better-off groups are unlikely, e.g., to remote and poor rural areas, or through shops in poorer urban communities.

Alternatively, food stamps can be issued to target groups for exchange in shops, although these schemes have had mixed success. Jamaica introduced a food stamp scheme in 1984 to offset the nutritional impact of food price increases resulting from the stabilization program. This scheme currently covers some 9 percent of the population, although its value would have to be dot bled to guarantee an adequate nutritional intake.

The resources spent on food subsidies can often be better applied thrpugh direct feeding schemes, e.g., via health clinics or schools. Jamaica now has a school feeding scheme (supported by food aid) which provides a free lunch to some 500,000 children, and clinics distribute food supplements to mothers and preschool children.. Where resources are very stretched, weight monitoring can be used to screen children for admission to supplementary feeding - as in the World Bank-assisted program in Tamil Nadu, India. In Zimbabwe, a supplementary feeding program was conducted in 1980-83, eventually covering 270,000 children. Although the program was primarily a response to the drought, it was also partly contemporaneous with a stabilization program launched in 1982. There is no reason why such schemes cannot be directed to protecting nutrition during adjustment as a primary objective.

Similar considerations apply to other welfare measures; e.g., drug subsidies can be restricted to essential medicines and applied only to drugs bought at clinics in poor areas. In general, increasing the targeting of welfare interventions eventually comes up against the limit of administrative cost. Consequently, some agencies (particularly the World Bank) and governments have increasingly emphasized the role of the market as against that of the state in providing social services. This is very controversial, but while poor regions are often ill served by any sweeping privatization of services, there may be some benefit in allowing the market to provide a larger share of the services consumed by middle- and higher-income families in order to allow increased state resources to be directed to the poor."

Raising Public Revenues

The type of adjustment measures undertaken will largely determine the extent to which poverty alleviation can be built into the reorganization of revenue instruments. In IMF programs involving major reductions in the public sector deficit, or where the external position is such as to require rapid stabilization, the revenue objective will be dominated by the need to increase revenues rapidly. In such cases, mom for incorporating poverty concerns will be less than in IMP programs with less severe fiscal targets, or in structural adjustment programs with longer time horizons. Moreover, raising taxes which are regressive (such as the sales taxes on basic goods or poll taxes) are often the easiest revenue sources. From the equity viewpoint, raising revenues from proportional taxes on income

and property, as well as selective consumption taxes on "luxury" items, are to be preferred - although limited administrative resources may constrain their implementation.
Increasing user charges provides one means of raising revenues, and increasess can sometimes be imposed which minimize the increase on low-income groups. In Jamaica, when electricity and water tariffs were raised, a smaller increase was imposed for minimum consumption levels to allow the poor continued access to a basic level of service..

Increasing the Incomes of the Poor
Insofar ass the income of the poor can be raised, there is less need to support them through transfers which can then be concentrated on the most disadvantaged. This can assist fiscal restraint and, if the poor can be. drawn further into export and import substituting activities, will also support structural adjustment.Income is derived from a variety of productive assets, including land, inanimate capital and human capital embodying skills. Consequently, incomes can be increased by raising the return to the assets held by the poor - through increasing the price of the commodity produced (hence the importance of producer price policy in agriculture), by reducing the costs of their inputs, or through raising their productivity.
Measures can also be taken to increase the access of the poor to productive assets. Landlessness or limited access to land is a critical determinant of rural poverty in much of South Asia and Latin America as well as parts of Africa (e.g., Kenya). Land reform can be an effective means of reducihg rural poverty (although it is not a sufficient condition). However, there can be a tradeoff between the needs of poverty alleviation and those of growth and adjustment where the productivity of large farms exceeds that of smaller fauns. This is mainly the case in areas where the modernization of agriculture is relatively advanced, and where larger farms have a competitive edge through their better access to new technologies. But even in such cases, there are often large tracts of underutilized land which can be distributedd to the poor. In areas where traditional agriculture predominates, small farms generally have higher productivity than large farms because thee former use their labor more intensively. In such cases, land reform, by raising productivity, can contribute to growth and structural adjustment. In northeast Thailand, the government is allocating land to poor femilies as a measure of compensation for recent increases in the rice price."
Measures can also be undertaken to increase employment, and specifically, to enhance the occupational and geographical mobility of the poor. Adjustment incorporates incentives to move from the production of nontraded to traded goods. This can be supported by, for example, assisting the urban poor to move into agricultural activities, or the absorption of redundant public employees into the private sector. Both Brazil and Ghana have undertaken such measures.
Alternatively, labor-intensive public works can provide employment. Many governments (particularly in South Asia) have experimented with such schemes, mainly to cope with seasonal employment shortages. But these projects can also provide some of the infrastructure necessary to support adjustment - e.g., roads, irrigation schemes and storage facilities. However, the fiscal cost of such schemes can bee high, since they largely create assets which do not generate government revenue, so their implementation may be limited by the objectives of stablization. In addition, such schemes generally pay very low wages in order to discourage people other than the poor; and unless they create assets or skills for the poor, they are inferior to measures directly attacking the root causes of poverty. However, as an immediate measure to alleviate the consequences of stabilization, they may be essential. For example, Chile's emergency employment schemes were providing jobs to nearly 14 percent of the labor force in 1983 (the peak unemployment year).

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CHAPTER 9
Human Implications of Strategic Adjustment Programs
Mihaly Simai

Adjustment basically means the process of restoring correct relationships. In the vocabulary of international economics in the past decades, the concept of adjustment was closely related to external imbalances, indebtedness and the conditionalities established by the IMF and the World Bank.

Adjustment also refers to a set of policy measures taken in cases where the difficulties are of internal origin. Rapid growth of government expenditure may result in a budgetary deficit, leading to domestic cost and price increases. inflation, declining competitiveness and eventually, balance-of-payments difficulties. The restoration of the national balance of supply and demand often requires drastic stabilization measures, even without pressure from international organizations. Technological change also requires far-reaching adjustment measures. In order to survive, countries have to adjust.

In the framework of the OECD, the concept of "positive adjustment" describes policies which facilitate shifts from declining to expanding sectors, and from less efficient branches of the economy more efficient ones. According to this definition, adjustment policies are also regarded as positive if they are directed toward achieving such other governmental objectives as improving the social and physical environment, the distribution of income or the fair sharing of burdens. Adjustment is an integral and necessary phase of the echononi.L growth process. In a flexible economic system, adjustment is not an alien element; it is more or less a permanent requirement in economic policy making. Since the domestic and external environ ment is changing constantly, economic policies have to accommodate these changes sooner or later. Depending on the intensity and the nature of the changes, adjustment requirements may greatly differ.

In this paper, I define strategic adjustment as a comprehensivd set of policy measures taking place in a macroeconomic framework and including not only external measures, but also internal changes in development policies and priorities and structural shifts in output and consumption. Adjustment may influence the role of a given country in the international division of labor. Short-term adjustment to external shocks may contain the beginnings of strategic adjustment. The interrelationship between short-tern adjustment measures and strategic changes may be especially strong in cases where the factors requiring adjustment are of major importance and of a lasting nature. In those cases, short-term steps must be followed by longer-term policies.This is especially true in the contemporary world economy, where an ongoing technological revolution, long-term imbalances in international finance, and structural changes in world output and trade indicate that short-term imbalances reflect long-term development problems. Therefore, adjustment policies must be implemented with a longer-term view and with a new time horizon. In the increasingly hierarchical structure of the world economy, global distributive mechanisms and pressures are reproducing acid strengthening inequalities, while there is no clear sign of an increase in international economic solidarity.Technological progress renders the achievements of earlier industrialization increasingly obsolete in the global division of labor. Some sectors of the world economy are in a condition of deep structural crisis.

The failures and partial successes of short-term adjustment policies have proved the necessity of planning the adjustment process in a longer-term framework. Due to the complex nature of the process, the human implications even of short-term adjustment policies and measures must also be considered in a longer-term context.

Keeping in mind the recent national and international debate on medium-term adjustment and the problems encountered in practice, this paper will consider the following economic policy issues :

a) Which are the best ways to minimize the costs of adjust ment, especially the human costs?
b) How can the adjustment capacity of individual countries be improved?
c) How can the efficiency of public administration, especially the branch responsible for the elaboration and implementation of adjustment programs, be increased?
d) What are the best ways to provide international institutional support for national adjustment policies?
All these issues have important human implications.
While adjustment policies are necessary in every country, their different external and domestic conditions may require completely different measures, and their demands for international support may vary greatly. There are enormous differences in the capabilities of countries to adjust to change. The potential and actual costs and benefits of the adjustment process may depend on factors which can be controlled more by one country than by another, depending on its economic and political power, the structure of its economy, its achieved level of economic and social development, etc. There are important systemic factors influencing the concrete policies of adjustment. In the centrally planned economies, the problems of output, consumption and trade are now receiving greater attention.
In spite of the great differences among countries, there are also important similarities in the tasks they face, in the causes of success and failure, in the factors determining costs, and also in social conditions and consequences. The similarities are especially strong among the developing countries. This paper will concentrate on their experiences while also taking into account some of the lessons of the centrally planned economies and of industrial western countries.
Who is Covering the Costs?
Adjustment in a national economy becomes necessary when the country is faced with difficulties. These difficulties may be limited to one country or to a group of countries, or they may be of a general, global nature. When only a few countries are facing serious problems requiring major adjustment measures, the external environment can be more supportive than in the case of widespread and long-term difficulties. For many countries in the latter position, the "world economy" may represent a hostile environment. External forces may undermine or destabilize the national economic structure or force a country to sacrifice its social priorities and change the dominating system of values. The weaker the country and the more restricted the role of international assistance, the greater the shocks will be.
During the Great Depression, the "beggar-my-neighbor" concept characterized policies by which different countries attempted to shift the burden of adjustment onto their partners. The main burden was thrown on the debtor countries. Adjustment, according to the formulation of Keynes, pushed thesecountries "in the direction most disruptive of social order, and [threw] the burden on the countries least able to support it, making the poor poorer."' The experiences of the past decade have not been dissimilar to the process characterized by Keynes. The economic and social costs of adjustment were high in most countries, especially the developing countries. The poorer and more dependent the country, the higher the costs and the more serious its domestic problems. In the developed market economies, both policies and practice emphasize that adjustment presupposes the alleviation of the burden of those directly affected by compensation payments, unemployment benefits, training programs, etc. Such facilities are seldom available in the developing countries, where the costs of adjustment are thus relatively higher. The acceleration of inflation has reduced real wages, sometimes by as much 30-40 percent. Import restrictions and declining demand resulted in major losses in output and employment. Underemployment has also increased, and the informal sector has grown rapidly. There has been a general deterioration of social conditions as public expenditure for the extension and maintenance of social infrastructure declined sharply. Health and education expenditures were cut in real terms in many countries, sometimes by 50-60 percent. Few countries were able to "defend" their social programs, in spite of strong efforts to do so.
According to the estimates of the author, calculating the differences between the actual and potential output during 1975-85 and taking into account the losses in terms of trade and the

higher interest rates, the combined total loss of the developing countries was equal to their entire 1980 GNP. This was, of course, not the cost of adjustment programs alone, but the result of cumulative losses suffered by these countries. Part of the loss, however, was connected with adjustment policies.

Minimizing the Cost ofAdjustment

Experience has shown that it is difficult to develop a cost minimizing adjustment strategy, especially for a single country alone. Costs are often not even calculated by the countries. Some lessons, however, can still be learned from the experiences of the past decade.
a) Adjustment policies became especially costly for these counties in an international environment dominated by the neo conservative economic policies of the larger western industrial countries. The idea of "global belt-tightening" emphasized the ideal of economic policy autonomy in an interdependent world. The developing countries were not able to build efficient defense lines against the burden-switching effects of these policies.
b) It is correct to state that among countries where prices and exchange rates were greatly distorted, those which adopted import-substituting policies of low efficiency, borrowed too much and exported too little in relation to their external obligations had a very difficult time with adjustment. Adjustment policies in outwardoriented economies worked better. As for costs and benefits, the difference between success and failure depends not on world market orientation, but on a country's ability to develop and implement correct and comprehensive policy packages. Changes in development strategies (such as a shift from import substitution to export orientation) go beyond a short- or even a medium-term horizon, due to the different structural, skill, managerial and marketing requirements of such policies in comparison to earlier strategies. The transition from one strategy to another demands coordinated macro and microeconomic changes, different marketing orientation, etc.
c) There are great differences among small countries as far as their external position and internal structure is concerned. It is difficult to generalize; however, since smaller countries are more exposed to external shocks as a result of high trade intensity from a structurally weak position in the world economy, it is better to plan for prevention of the worst problems by exposing the country to external changes and organizing the growth process in a more flexible way. When shocks occur in small, highly protected countries, it is much more difficult to act. Economic adjustment in small countries is much more difficult amid major international socioeconomjc problems, stagnation and tension. In small countries specializing in only one or two products, adjustment without proper international support can cause disastrous domestic consequences.
d) When external shocks or inappropriate domestic measures create disequilibrium, the necessary corrective actions should be taken as quickly as possible. External financial sources should be used to speed up adjustment, not to postpone it.
It is of course true that certain economies cannot respond rapidly to sudden changes in policies or regulations. Usually it is the more developed and flexible economies which can adjust to rapid policy shifts more easily. As for the political implications, there is a strong case to be made for rapid adjustment. The sacrifices are brief, there is less time for the build-up of opposition against the programs, and if they yield quick results, they can even generate considerable support; and the social impact of the adjustment program is more manageable. Gradualism, in principle, facilitates greater flexibility in the implementation of programs and in the distribution o£ the burden. It may create, however, a long period of austerity with very little concrete change, diminishing popular support and increasing discontent.
e) Since the ability of any given country to develop and implement adjustment programs which minimize the costs, mitigate the burdens of adjustment and avert political tension depends to a great extent on the efficiency of the public administration, to strengthen its capacity is a major long-term undertaking. There must, of course, be strong executive leadership, and the staff of the economic or development administration must be highly motivated. The economic and social goals of the adjustment process must also be well and clearly defined. Priorities in the adjustment process should be properly selected. In government agencies, there must be clear responsibilities for specific areas of adjustment. The tasks must be well coordinated, with a minimum of overlapping. The issue of

"centralization or decentralization" during the adjustment process must be treated flexibly and pragmatically.

Adjustment tasks and their implementation can cause tension within the administration. Such issues as budget cuts and the reallocation of resources exacerbate the situation, and the weaknesses and inconsistencies of the administrative structure may become more conspicuous. Administrative reform may become indispensable. While it is not easy to implement administrative reforms during the adjustment process, in certain cases it may be a fundamental condition for success.

In difficult periods, it is even more important than under normal circumstances to achieve a popular consensus and ensure the participation of the population in the development dialogue, and not only in the implementation of policies. The stability of a society depends not only on the economic successes or adverse consequences of the adjustment process, but also on broad popular participation. If priorities are correctly selected and the political structure facilitates participation, even difficulties are better tolerated.

f) The proper choice of partners in economic relations can be a vitally important asset in the adjustment process. The complementarity of economic structures, the character and norms of relations, the mutuality of advantages, the partners' reliability and readiness to provide assistance if necessary, are all especially relevant. Due to the fact that the main partners of any country are determined by historical, economic, political and structural factors, the freedom of a small country to make sudden shifts is very limited in the short term. Sudden shifts are possible only among marginal partners. There are of course exceptions, when a larger country is ready to help a smaller partner through deliberate actions and by providing special facilities in the market. This practice, which is not completely unknown in the world economy, usually has strong political motivations.

g) Developing countries are especially interested in forms of multilateral cooperation which could strengthen their economic position by collective measures, taking into account the interests of all partners involved and in which the partners share responsibilities. The present international institutions, such as the IMF, the IBRD or regional bodies, even though positive changes have taken place in the past decade, have not been able to fulfill the functions of a growthoriented collective economic adjustment-supporting system.

Human Implications of Sectoml Adjustment Efforts

From the point of view of direct human implications, sectoral adjustment problems represent an especially important issue. They also reveal the limitations of many developing countries in this respect.

The task of adjustment emerges in most cases as a structural problem: to change the role and place of the given sectors in the economy, or to introduce adjustment measures within the given sectors, e.g., to increase exports in order to achieve the required increase in import capacity, or to increase domestic demand, improve supplies to the domestic market and increase employment. In this paper we look at three major sectors.

Agriculture

Adjustment tasks in agriculture differ in the developing countries. In certain cases, due to a declining capacity to import food, adjustment aims at an increase in domestic production. In other cases.traditional export products are replaced by new, more competitive goods. For the two aims, different incentives are introduced. While such measures in principle should have a moderately favorable impact on the agricultural sector, in practice, it is sometimes neutralized by the declining prices of traditional agricultural export products.

Agricultural incomes in general are not increasing, and even in the case of larger farms, the purchase of tractors and other agricultural machinery is deferred because of the relatively high cost. Forms of medium-term adjustment assistance such as institutionalized credits tend to help larger farms and estates over small farmers and landless agricultural workers, who are facing great difficulties. Agricultural poverty is on the increase, and the shrinking purchasing power of the agricultural population is adversely influencing other sectors as well.

The agricultural sectors of many developing countries have major long-term structural problems, such as the form of land ownership, low levels of technology, and a lack of institutional infrastructure for marketing, financing, etc. All these problems limit the possibilities of efficient adjustment. The solution, however, goes beyond adjustment tasks to require major agricultural reforms.

Mining

In the mining sector (other than fuel), the long-term impact of world economic changes requires major steps in adjustment to reduced demand and decliningprices by reducing output, introducing processing and diversifying the production of the extractive industries add of the economy in general. Another target of adjustment is rationalization. Even if prices rise due to a stronger and more widespread economic recovery, it will be necessary to consolidate and rationalize existing operations, to increase the efficiency of investments, to rely more on smaller activities, and to increase the value added by expanding vertical integration. It is also important to find areas where the mining sector could efficiently increase its relations with the domestic economy through different inputs. Since the mining sector is often the most important source of external earnings and nonagricultural employment, the success of adjustment measures influences the general economic situation in many countries and regions. If deterioration continues, the already adverse effects on incomes and public expenditure will be increasingly felt.

Problems within the mining sector, as well as the potential success or failure of adjustment policies, raise another important issue - the possibility of price stabilization. The price explosion of the I970s and the decline of raw material prices in the I980s proved that price changes, if they are allowed to fluctuate to the extent which characterized the last fifteen years, cause major economic instability. Relatively stable prices are more conducive to global welfare than unstable ones. Price stabilization provides a net gain to ptoducers and consumers alike if it is done correctly and allows sufficient flexibility.

Industry

Due to the dim outlook in the agriculture and mining sectors, the problems and tasks of adjustment in manufacturing are especially important for the majority of developing countries.

The manufacturing sector was affected by world economic problems and their domestic consequences in many ways. Production capacities developed earlier became obsolete as a result of postponed investments. The upgradingof machinery and equipment was deferred, and technology imports were reduced. Industrial infrastructural projects were postponed or completely abandoned. Expenditures on domestic research and development and on technical education were reduced. Industrial infrastructural projects were postponed or completely abandoned. Industrial unemployment increased in many countries.

Adjustment measures include increasing productivity and efficiency and changing the structure of qutput in order to promote international competitiveness and increase exports. There are new efforts to strengthen import substitution and make it more efficient, especially in the field of capital goods. The human implications of these tasks include such important issues as the availability of skills and managerial capabilities at a scale and structure which is required. While there is an oversupply of certain skills, it is generally a shortage of highly qualified persons which hinders change.

Export promotion activities are often combined with efforts to reexamine the possible role of foreign investment and the different ways to attract more foreign capital. The encouragement of private sector activities is often accompanied by reductions in the size and role of public enterprises in manufacturing, often disregarding the. social role of the public sector in certain important areas, such as creating jobs or developing skills.

The harmonization of the above strategies with exchange rate and trade policies is also part of the adjustment process. It is fundamental from a human point of view that planned adjustment measures must be instrumental in recouping the severe reductions in real wages and the deterioration in the distribution of income which has taken place in the last several years. It seems more or less inevitable that real wages, especially of unskilled labor, will continue to be low due to high unemployment and underemployment. Under these conditions, increased social pressure can be expected, since a disproportionately large share of the cost of adjustment falls to the low-income and unemployed segments of the population.

There is another very important human problem connected with adjustment tasks. Since it is highly unlikely, under present conditions of technological development and investment constraints, that the autonomous job-generating capacity of industrial development will be sufficient, it will be necessary to develop special jobgenerating strategies, especially in certain highly urbanized regions of the Third World.

Employment problems are going to increase due to continuing rapid urbanization in the developing world. According to U.N. estimates, in addition to the 840 million urban population, by the turn of the century another 1.0 - 1.2 billion people will have to be absorbed by the cities of the Third World. Most of them will be poor and unskilled. About 50 percent of them come as a consequence of population growth; the rest will migrate from the agricultural regions. Adjustment measures must therefore include job-creating programs at low capital investment costs. Projects which are both labor-intensive and also justified on economic terms must be developed in the industrial sector. Most of the manufacturing opportunities which can satisfy these needs are concentrated in the smallscale industrial sector. (Such opportunities also exist, of course, in urban services).

As in the case of agriculture, the adjustment process in manufacturing is also adversely influenced by external protectionist measures employed in a discriminatory manner, in particular against the developing countries. Protectionism is especially strong in those areas where the developing countries have a comparative advantage, or where there are structural adjustment problems in the developed market economics.

The Role of TNCs

The role, and especially the potential role, of transnational corporations (TNCs) in the strategic adjustment process is often discussed by experts. It also has important human implications. The contributions TNCs may make include

a) Bringing in, reallocating and investing capital, thus helping to alleviate the debt problem.

b) Innovating, adopting, perfecting and transferring technology, which can help in upgrading technological capabilities.

c) Bringing in new and useful knowledge about organization and management, which are important for domestic structural changes.

d) Facilitating international marketing.

e) Providing new job facilities for the local labor force.

f) Educating and upgrading workers, professionals and managerial staff.

g) Through the international vertical organizations, promoting a more effective progression of goods from one stage to another outside the free market, which can lead to greater stability of export earnings.

h) To an extent, stimulating local services and output.There are, of course, great differences between the actual and potential roles of TNCs, since their activities are guided not by altruism or the public interest, but by the profit motive.

The above potentials may aid adjustment efforts, especially by increasing exports. However, the subordination of large segments of the national economy to international strategies or interests may hamper such aims of the adjustment process as :

a) Increasing export surplus and saving imports.

b) Maximizing external earning potentials.

c) Creating new jobs for the masses through labor-intensive operations.

d) Increasing international competitiveness in those areas which are not in the interest of the given TNCs.

The outflow of resources through the price mechanism in the form of profit remittances, royalties, etc., is often excessively high. TNCs also encourage the outflow of highly skilled professionals (the brain drain). Experience has also shown that during periods of adjustment, TNCs often reduce their operations or completely cease their activities. There are of course, exceptions, as well as cases where reduced real wages, devalued currencies and different direct incentives provided especially favorable conditions for TNCs to operate.

The Politics of Adjustment: Human Implications

Adjustment programs, especially strategic adjustment programs, require strong involvement of the state. Even in the developed industrial countries, proper government policies are the basic condition for the success of any major adjustment program. National or international market forces alone cannot be expected to correct imbalances rapidly without disastrous social consequences and high economic costs. Adjustment is a complex process which calls for the most efficient mobilization of national resources through state intervention and planning harmonized with market forces, with the participation of both the public and the private sector. The process requires both good entrepreneurs and well-trained, efficient civil servants.

Corrupt public administration, inefficient bureaucracy, and governments which are weak and politically divided are unable to develop and implement successful adjustment programs.

The characteristics of the economic policy formation and implementation process in every country are a major factor in adjustment programs. Not only can national successes and failures be largely explained by individual countries' different political capabilities and influences, but the nature of adjustment measures is also closely tied to political decisions.

a) Decisions made on the government economic policy level reflect prevailing political preferences.

b) Policies implemented in a given social environment reflect the nature and degree of compromises in the given power structure.

c) Economic considerations are subordinated to the political value judgments of the decision makers of a given country. These judgments influence such important issues as timing and impact incidence of the costs of adjustment on different social groups.

d) The domestic consequences of the adjustment process often cause major political tensions, leading to political changes. The readiness of the masses to accept costs and make sacrifices reflects the degree of political cohesion and confidence in a given regime, and also the ability of its leadership to develop and implement successful adjustment programs without sparking off unrest and tension.

e) It is not just domestic political life which has a strong, often decisive, influence on the adjustment process, but also international politics. It is a well-known fact that in a politically divided world, there are always countries which are held in disfavor by the major centers of economic and political power, and the use of economic instruments can hamper their economic adjustment and lead to political destabilization. Much less attention is devoted, however, to the different political philosophies which can adversely influence the position of the weaker countries by denying them the necessary international institutional support and/or completely disregarding the socioeconomic implications of adjustment by maximizing expectations concerning the role of market forces, In this scenario, the developing countries "have very little scope of action to resist economic and political domination. The prevailing pattern of consumption would continue to spread to the social groups that have adequate incomes ... It seems inevitable that this scenario would produce more inequalities and imbalances among the countries of the Third World and within each country, among sectors incorporated in the world market and those left outside it.'"

The international distribution of adjustment burdens is an important international political issue, considering that the changes demanding adjustments from a developing country are often caused by the policies of the developed industrial countries. The lack of symmetry in sharing the costs of adjustment, and the fact that the poorer countries have to carry a disproportionately high cost, has especially serious consequences for these countries in the world economy.

Conclusions

a) Strategic adjustment is a special phase of economic growth. Every adjustment measure involves economic and social costs and benefits. These costs have been distributed in an extremely unequal way during the past ten to fifteen years. The human costs of adjustment have been too high, and their long-term consequences may be extremely harmful.

b) The development of adjustment programs with lower costs is not possible inmost countries due to the character of the problem, the prevailing economic philosophy, the weakness of the world economy and the lack of economic and political expertise in decisionmaking bodies and/or institutions.

c) The accumulated experiences of adjustment policies proved the strategic importance of prevention, of fast action (shock treatment) whenever it is feasible, and of comprehensive (package) programs. These programs have been more successful than isolated measures. The transition from one development strategy to another is a more complex task and goes beyond the framework of mediumterm adjustment.

d) The sectoral consequences of adjustment are especially important. The effects on employment, incomes, exports and capital movements are very significant. Different sectors experience specific problems. Where international interrelations are very strong, they may influence the outcome of adjustment efforts adversely,

e) Adjustment should take place in such a way that it challenges the given structure of the international division of labor. It should not weaken the bargaining position of a given country in the world economy or create internal anarchy or a political straitjacket.

f) Stabilizationn measures, rescheduling and other efforts to increase external earnings should be well coordinated and harmonized with domestic requirements, especially with the satisfaction of the most elementary needs of the population in nutrition, health and education.

g) The distributive effects of adjustment programs should be analyzed in advance in order to achieve a more symmetrical sharing of the inevitable burden.

h) The marginalization of people and the further growth of unemployment, underemployment and the further expansion of the informal sectorshould be avoided. Therefore, together with structural changes, special social programs should be developed.

i) Unavoidable cuts in health, education or cultural expenditures should be made with extreme caution and within a long-term policy framework, since losses in these areas cannot be easily recouped, and since the long-term damages of even shorter-term measures may be excessively high.

It was not the task of this paper to discuss the role of external support in assisting the adjustment policies of individual countries. The economic and social consequences of past adjustment strategies raised several issues - for example, about the role of stabilization assistance, structural adjustment loans, etc. The consequences of conditionality are an especially important issue, at the center of which is the question whether the solution of one economic problem by the creation of others, both economic and social, is a feasible approach.

Another broadly shared perception relates to the necessity of making the burden of national adjustment more sustainable through well-conceived common efforts promoting economic growth and trade. All countries could gain if the goal of strengthening national and global economic security were taken as the major guideline for the policies of the international agencies in connection with adjustment, and if all parties would accept the responsibility for guaranteeing global economic stability and act accordingly.

Note

1.Donald Moggidge, eel., The Collected Writings of John Maynard Keynes (Macmillan, 1980), voL 25, p. 29.

2. Francois le Guay, 'The International Crisis and Latin American Development: Objectives and Instruments' CEPAL Review no. 26 (1985): 130.

PART III
SECTORAL POLICY ISSUES

CHAPTER 10
The Role of Human Resources in a Civilization of Knowledge

Mahdi Elmendjra

The word "change" has been overused and often abused. We tend, therefore, to overlook the meaning and implications of its content, and we rarely take the trouble to project into the future the consequences change may entail, particularly with respect to learning. This is due first of all to our learning systems, which are geared toward maintenance and pattern reproduction and are not therefore at ease with dynamic processes.

The world is changing. This has been so ever since the beginning of humanity. What is new, however, is the swift rate of this change, which has greatly reduced the time allowed for adaptation. We could almost say that the very concept of change has itself changed due to an acceleration of history.

What are some of the striking changes which need to be recalled to permit us to sketch out very broadly a few of the new learning needs? These changes are of a quantitative as well as a qualitative nature, although often the distinction between these two aspects U blurred and becomes almost a formal one.

Change and Knowledge

For the first time in the history of mankind, man is capable of eradicating his own species, not to speak of all other forms of life. The meaning of "survival" has thus radically changed. This has faraeaching implications for our learning systems.

The growth of the world population, and the world's inability to cope with its socioeconomic consequences, has brought about new problems of natlonal'and planetary management.

iRemarkable breakthroughs in science and technology have led to a higher complexity and created a new "problematique" – to use an expression dear to the Club of Rome - that is an intermeshing of a large number of sectoral problems, none of which can be properly handled on a purely sectoral basis.

A real explosion of knowledge has ensued from these breakthroughs and has contributed to an overflow of information.' It is estimated that the total knowledge of mankind doubles now every seven or eight years. Over 2,000 titles of new books are published daily. It is not only the amount of information which has grown. The speed of its processing (1.2 billion operations per second in a Cray 2 computer), the stocking capacity (the equivalent of 275,000 pages on a small, compact laser disk which fits into a pocket) and the ease and rapidity of access through telematics have totally transformed the servicing of knowledge.

The information revolution and developments in the other high technologies, such as artificial intelligence, biotechnology, new materials and space technologies, have come about and flourished because of one main ingredient: knowledge, with much less emphasis on natural resources or even capital. This transformation of society from a civilization based on raw materials, capital and production to one based on human resources and knowledge is only just beginning and does not yet affect all parts of the globe with the same intensity. It is, however, an irreversible development with enormous consequences for our learning systems.

One of the economic indicators that help to measure these changes is the increased weight of "services" in national economies and in international economic relations. In international trade, services amounted to $30 billion in 1970; in 1985, this figure rose to $400 billion.

Change has also affected the ethical norms of the international system, but not always for the better, because our societal learning processes did not enable it to capitalize on the positive aspects of these transformations. Maintenance learning has prevailed in spite of the political decolonization of the 1950s and 1960s. Although the planet has become a village, Inequities have been reinforced and social justice underplayed, to the point where we may even speak of the development of an international feudalism. The compound NorthSouth inequality ratio is of the order of 1 to 20 and may reach 1 to 50 by the year 2000.

Things have changed and are changing, but not In the same way and the same pace for every one. Hence the emergence of a cornpletely new paradigm of social justice and human rights, and the need to learn how to reverse the increasing gap between the "two humanities" and to reduce the schism between the "two cultures." Over one-third of humanity is living below the poverty line, and famine is still the lot of tens of millions of people, not to speak of the devastation of ignorance and disease suffered by millions of others.

On the eve of the twenty-first century, almost one out of four inhabitants of the globe is still illiterate. Over 400 million people are underemployed or unemployed at a time when human resources have become the key factor in development. With 20 percent of the world population, the industrialized countries account for 85 percent of the world expenditure on education and 95 percent of expenditure on research. These disproportion are further accentuated when one takes into account the fact that over one-third of the world's population is under 15 years of age, and that 90 percent of these young people live in the Third World.

Obstacles to Rational Use of the Human Potential

One could go on with a long list of positive and negative changes which affect our lives, but this paper is not about change per se, but rather about the learning needs which are mandated by these changes. One problem is that the development models which have made these changes possible have tended to exclude man from the equation. It is only in recent years that we have begun to hear, in developmental circles, about the role of the "human element." In the early 1960s, the World Bank (IDA) made its first soft loans to education as a social sector rather than as a "productive" one. Not until 1985 did the Bank articulate a formal and official stance on the importance of human resources for development. The report of the executive director of UNICEF for this year highlights more clearly than ever before the place of the "human factor" in socioeconomic development. The UNDP, co-sponsor of this Roundtable, has also come a long way from the stand it took twenty years ago about the finance big of literacy projects; the letter of invitation sent to Roundtable participants says that "the time has come for bold new ideas to improve the use of the human factor in development and to formulate practical plans for practical action." Another change, and a welcome one. But there are at least five important things which have not yet seriously changed and which constitute major obstacles to the assessment and satisfaction of the new learning needs.

a) Development models - especially those of Third World countries, which are the product of an almost blind imitation, either voluntary or imposed by external exper tise.

b) Learning systems of the North and South alike.

c) The mental structures which these models and systems produce and maintain.

d) The insufficient weight given to soclocultural values in the elaboration of educational systems and the programming of their content.

e) A resistance and/or an incapacity to analyze and seek solutions within a long-term perspective, i.e., an absence of vision due to the shortsightedness of politicians, govern ment officials and most decision makers, who are usually more preoccupied by short-term considerations.

These are also the major causes of what we have called, in a report to the Club of Rome,' the "human gap." The human gap is the distance which separates the level of our attainment in the areas of knowledge and resources from our capacity to master and solve the problems engendered by this knowledge. Th1s gap can also be seen as a learning failure. For Aurello Peccel, the founder of the Club of Rome, one of the major problems of society is the peat gap - if not divorce between man as creator and man as manager.

The above constraints must be taken Into account whatever measures are envisaged at the learning level. One of the first needs of learning is how to overcome them. In my view, this cannot be done only through adjustments, mild reforms, Increasing financial resources or adaptation. What is needed is an overhauling and transformation of learning systems so as to make them socioculturally relevant and capable of facing the challenges which change has brought about.

In the above-mentioned report to the pub of Rome, the authors present a relatively simple thesis: the present learning,rystems, like all those which preceded them, have one basic historical fLnctlon - maintenance, the reproduction of norms and values from one generation to another. In the put, change, was slow enough to allow then systems to evolve and adipt. This is no longer pouible; ' hence the need for "Innovative learning" instead of "maintenance learning." Innovative learning demands two prerequisites: participation (solidarity in space), and anticipation (solidarity in time).

The issue in question here is of a universal nature; we should at all costss avoid polarizing it into a North versus a South perspective. The problems of both learning systems are similar,

especially if we bear it in mind that the learning systems of the South are very poor photocopies of northern ones. The qualitative needs are the same, and so are the challenges ahead, even if quantitatively the problems of the South are enormous in scope.
We are, of course, speaking here about the purpose and objectives of systems of learning, not about their specific content. Let me sketch out a brief list of issues which should be considered in any exercise aiming at the reassessment of learning needs and the optimalization of human resources in a changing world.

Issues in Reassessing Learning Needs

The greatest element of waste in our contemporary society is to be found in the area of human resources. We are obsessed by the concept of productivity and efficiency when it comes to land, mines, machines, products, industrial processes and management. At the same time, the world contains about one billion illiterates - not a very rational use of the human potential, or even of those who have received an education. According to some specialists, we do not, as individuals, use even 10 percent of our learning potential. We have a fairly exact inventory of the natural resources of the planet, and we are now surveying the composition of the universe, but we do not seem to be sufficiently preoccupied by the untapped human resources which could greatly improve the quality of life and enhance creativity.
In spite of great strides in science and technology, including artificial intelligence, neurophysiology and psycho-pedagogy, we still know very little about how our learning process functions. Some of the very little knowledge we have acquired is not available to the scientific community at large, but is locked up in the laboratories of the military and the pharmaceutical industry.
The main characteristic of a society of knowledge is the increasing proportion of resources devoted to research. In the advanced technologies, industry spends between 7 and 11 percent of its turnover on research and development. In the area of learning, the amount spent on R&D is not only infinitesimal, but it is almost impossible to identify and measure. We do not even have international norms and standards to collect comparable statistics. Statistics on R&D in the educational sector are not available in any international yearbook. So not only do we know very little about the learning process, we know even less about what we are doing to find out more about it.
The role of sociocultural values in the learning process, and the role of the learning process in value orientation, is vastly underestimated. Learning is in essence a process of internalization, which necessitates endogenous models of development and does not successfully lend itself to excessive imitation or nonimaginative borrowing. Its main ingredients are innovation and creativity. At the risk of being totally misunderstood and misinterpreted, let me say that learning is the area of international cooperation in the truest sense of the tern; it is also the least suited for massive flows of external technical assistance or financial aid. The key part of the learning process and of national educational policies is self-reliance. You cannot build up self-reliance through dependency. There is not a country in the world today that does not have the local ways and means to eradicate illiteracy and to develop its human potential. What most countries lack is the political will and the courage to do so - in spite of, or because of, the great sociopolitical transformations which education brings about.
Because of an acceleration of history, learning has become, more than ever before, a long-term process. Any reform of learning systems ought to be worked out in terms of generations to be able to achieve a thorough change from preschool education to postgraduate studies, including the training of teachers and the production of new teaching materials. A period of fifteen to twenty years is the minimum time required to transform an educational system.
The unemployment crisis in the world has introduced new preoccupations which have distorted the relationship between education and employment. A fair proportion of unemployment is due to the structural causes of change and a lack of foresight and long-term planning, and not to the basic functions of education, which go beyond the mere provision of a work force for the economy. For over half of the types of employment which will be needed by the year 2000, there are today no suitable courses offered by the '

universities and higher training institutes throughout the world.

Some Learning Needs of a Society of Knowledge

What are some of the learning needs of the society of knowledge which is in the making, and which will sooner or later engulf all parts of the world?
a) A recentering of development models around man and his creative capacities.
b) National programs for the eradication of illiteracy within the shortest time possible and at the highest priority, with very little or no reliance on external financial assistance.
c) A reshaping of the learning systems so as to favor innovation, participation and anticipation in order to facilitate the tackling of the growing complexity which a society of knowledge entails.
d) A greater emphasis on R&D, particularly in areas which have a direct bearing on the understanding of the teaming process.
e) A concentration on the high technologies, especially in the case of the less-developed countries, leaving aside what has been euphemistically called "appropriate" or "adapted" technology.
f) The development of new criteria and parameters, as well as statistical norms and standards, to monitor achievements in the fields of education and teaming.'
g) The building up of national, regional and international information networks on teaming.
h) The launching of an international multidisciplinary research project on the learning process involving both industrialized and developing countries.
i) A greater integration of science and technology in the national development plans of Third World countries so as to facilitate the integration of national-qualified manpower and to reduce the brain drain phenomenon! Third-level university students from the developing countries represented about 40 percent of the world total in 1985 and will exceed 50 percent in the year 2000. India atone had 2.5 million scientists and technologists in 1983. The brain drain problem needs to be tackled in a more imaginative manner through the building up of policies, facilities and an environment conducive to the constructive use of qualified manpower in Third World countries.'
j) Special attention needs to be paid to the rural world, bearing in mind the fact that no developmental policy of any kind is capable of stopping the process of urbanization in the developing countries. About 40 percent of the working population of the world in the year 2000 will still bee in the agricultural sector, and this is where illiteracy is concentrated.
k) Learning systems still have to learn how to make the best use of the advanced technologies, such as Informatics, robotics and telecommunication sciences, which present a great potential for the enhancement of knowledge and its application to the solution of contemporary problems.
l) A new understanding of the concept of "work" is needed, and a more intimate connection between employment, learning and leisure is required.
m) A novel approach to equity and social justice is needed to provide equal learning opportunities within and between countries (learning justice), as well as full respect for cultural values (cultural justice).

Notes

1. According to an MIT study of 1989, the number of words distributed by the media in the United Settee inaemed, within a few years, by around 9 percent annually, whereas the number of words absorbed by the Ametim public incensed by len than $ percent annually (see the Economist, 20.26Ju1y 1985).
2. J. Botkjn, M. Elmandjm and M. Maama, No Limps to Learning, a report to the Cub of Rome (Pergamon Prers, 1979).
3. In March 1986, the French Ministry of Education announced the session of a "Centre de prospective et devaluation" which will elaborate new "efficiency indicators" to measure the retina of the investments and activities within the sector of education (Le Monde, 9 March 1986).
4. In 1985, 51 percent of the engineer, with a Ph.D. degree who entered the U.S. labor

market were non.Ameriuns (1,226 out of a total of 2,591). A Zahian, "The Brain Drain," mmreogtaphed (London, September 1985).
5. In 1977 the UNDP launched a program known as "TOKTEN" (transfer of knowledge through expatriate nationals), over l,ooo assignment, were made under this program, and it may be useful to learn from the UNDP what lessons they have drawn from thh experience.
the land, or an increase in either open unemployment or underemployment.'

CHAPTER 11

The Impact of Recession and Adjustment on EducationSylvain Lourie

The background note to this meeting recalls that the "human element is at the core of all development efforts." While one cannot find room for disagreement with such a statement, which is essentially of a rhetorical nature, let us not forget that political decisions made by any government are founded on a power process of negotiation and decision which is marked by the paramount purpose of preserving and developing the state which that government serves. The foundation of that preservation and development is predicated on a variety of value-laden considerations and preferences: for some, social mobility and justice for the many come before economic growth led by an entrepreneurial group, while for others, production necessarily precedes redistribution, and thus growth is the inevitable first step toward development. Experience, however, has regrettably taught us that while most governments pay lip-service to the "human element," their simultaneous obligation to meet military, production, trade and financial objectives leads them to take actions which do not necessarily reflect social and cultural imperatives. Although the latter are unquestionably linked to growth and development in the long term, they are too often neglected for the benefit of solutions to short term crises. As in most human endeavors, what is "urgent" weighs more than what is "important."

It is from this concrete context that one must pragmatically ask how a case can be made for giving greater priority to human development within existing constraints, illusions and ideologies.
The following pages will attempt to show how one segment of human resource development, education, is being negatively affected by the realities of economic recession and the consequent adjustment policies. It will conclude with some thoughts on possible attitudes or measures that may help to limit the societal damage caused by this

deterioration without demanding spectacular policy overhauls.

Turning our attention specifically to education, let us recall the synergy of three isolated factors which characterized the educational scene of the 1960s - a high rate of economic growth, an expansion of the demand for school places by all age groups in industrialized and developing nations, and the birth and spread of the theory of economics of education in non-centrally planned economies. The latter identified the "residual factor" (human element) to explain productivity and therefore economic growth.

Thus the 1960s witnessed relatively high rates of growth (national income expanded at a rate of 5.1 percent per annum between 1965 and 1970 on the average for all developing countries), while at the same time in those countries, public expenditure for education grew at a pace of 8.7 percent per annum.

This situation led the international agencies concerned with technical assistance and financial aid to move into the field of education. Thus the UNDP gave considerable support to UNESCO for literacy programs, for the establishment of teacher training institutions throughout Africa, for the development of educational planning in all developing countries, and for a vast fellowship program to train educational leaders and teachers of the Third World. These were also the years when the World Bank gradually moved into the field of education (1965), starting by participating in the expansion of institutions offering vocational and higher education. These moves were indeed influenced by the combination of the three factors suggested above.

Taking a long jump to twenty-five years later, we note that economic growth has slackened considerably and even decreased in developing countries; that the rate of enrollment expansion has essentially slowed down for primary education; and the theory which previously justified investments in education has been reduced to "rate-of-return" analyses which justify outlays for education in terms of optimum earnings for a given level of educational attainment. We shall now attempt to assess both the impact of the recession on formal school education, measured by indicators such as public expenditure and enrollment, and subsequently, the consequences of adjustment policies on education.

Recession and Education

The measure of the national effort in favor of education is shown by the share of GNP spent on public education. Its evolution between 1960 and 1982 (see table 1) reveals a general upward trend, which would suggest that education continues to receive a high degree of priority despite the economic crisis which began in the 1970s. Although developing countries spend somewhat less than developed countries in relation to GNP, their growth rate (82 percent) was higher between the beginning and the end of the period than that of the developed countries (62 percent). Naturally, the situation varies from one region to another. For example, Africa doubled its share of GNP for public education.

Looking now at the annual growth rate of public spending for education expressed in constant prices (see table 2) for five historical periods (1960-65, 1965-70, 1970-75, 1975-80 and 1980-82), two aspects reveal more subtle differences - a slowing down of the growth rate of public expenditure on education between the periods studied, and the existence of parallel patterns of expenditure between the different regions *prior to* the economic crisis in the mid-I 970s, as opposed to the diversity of regional behavior patterns *subsequent to* that period. Developed countries slowed down their expenditure more than the developing countries; witness the sharp drop between 1975 and 1980, followed by a more spectacular one still between 1980 and 1982.

TABLE 1

Percentage Share of GNP for Public Education (1960-82)

	Years						
	1960	1965	1970	1974	1976	1980	1982
Developed countries	3.47	4.30	4.86	5.24	5.45	5.55	5.64
Developing countries	2.55	3.13	3.63	3.69	4.13	4.35	4.65
Latin America and Caribbean	2.75	3.32	4.09	4.29	4.56	4.77	4.91
Asia and Pacific	2.46	3.00	3.32	2.93	3.49	3.54	3.94
Africa	2.50	3.11	3.56	3.86	4.35	4.70	5.03
Anglophone Africa	2.40	3.69	3.73	4.13	4.53	4.93	5.48
Francophone Africa	2.31	2.94	3.57	3.70	4.04	**4.48**	4.60
Arab countries	3.01	3.39	3.93	3.59	4.20	4.28	4.71

SOURCE: J. C. Eicher, *L'evolution des system's d'enseignement dans le monde de 1960 a no fours: Aspects economiques et financiers* (Paris: UNESCO, 1985)

TABLE 2

Mean Annual Growth Rate of Public Spending on Education (In Constant Prices)

	1960-	1965-70	1970-75	1975-80	1980-
Developing countries	10.5	8.7	7.7	7.2	7.0
Africa	9.6	8.9	8.6	6.6	6.8
Asia	9.3	8.6	8.3	8.3	10.3
Latin America and the Caribbean	12.1	8.7	5.9	6.8	4.3
Industrial market-economy countries	10.7	8.0	6.8	3.6	1.2
Oil-producing countries	13.7	9.9	11.8	7.8	6.2

SOURCE: J.C. Eicher, L'evolution des system's d'enseignement dons le monde de 1960 a nos fours: Aspects economiques et financiers (Paris:

UNESCO, 1985).

A superficial analysis might suggest, therefore, that in spite of the economic crisis, educational expenditures have not suffered much due to recession. A closer look should quickly dispel such a misleading conclusion.

To proceed with such an examination we propose to look at the case of several countries selected on the basis of their exceptional rate of indebtedness. By comparing the rates of growth of their GNP, indebtedness and expenditures for education with those of school enrollment at the primary, secondary and higher education levels a new picture emerges (table 3).

This table shows that while countries have experienced acute drops in GNP growth rates between 1965-73 and 1973-83 together with a spectacular multiplication of their external public debt, their overall growth rates of the share of educational expenditure in GNP have been positive, with the exception of Argentina, Nigeria and the Philippines. Given, however, the extraordinary decrease in the GNP growth rate, the ratio simply suggests that at best, total educational expenditures in absolute terms have stagnated, and at the worst, have actually decreased. Comparing expenditure growth rates with enrollment growth rates reveals the spectacular distortion which reflects the impact of the economic crisis on education. The case of Brazil may serve as a useful illustration. In the period 1970-83, the country increased its outlay for education by 10 percent while primary school enrollment grew by 42 percent, secondary school enrollment by 80 percent and higher educational enrollment more than doubled! The extreme case of Nigeria shows that in the same period, it simultaneously suffered a drop of over 50 percent in its educational outlay related to GNP and witnessed a growth of almost three times in primary school enrollment, four tunes in secondary school enrollment and ten times in higher educational enrollment. This table, which illustrates some of the more acute cases, shows unambiguously that

far from benefiting from an increase of resources, education has in fact suffered a spectacular drop in terms of resources actually available per student.

TABLE 3

Comparative Growth Rates for Selected Countries of GNP, External Debt, Public Expenditures for Education and School Enrollment by Levels

	GNP (1965-73) – (1973-83)	External Public Debt (1970-83)	Total Educational Expenditure (1970-83)	Enrollment (1970-83)		
				Primary	Secondary	Higher
	(%)	(%)	(%)	(%)	(%)	(%)
Argentina	−91	12.3	− 33 (82)	+ 27	+ 50	+ 330
Brazil	−51	18.2	+ 10	+ 42	+ 80	+ 234
Costa Rica	−62	33.0	+ 12	0	+ 101	+ 367
Mexico	−29	20.1	+ 13	+ 66	+ 283	+ 333
Ivory Coast	−34	18.5	+ 56 (80)	+ 126	+ 207	+ 325
Madagascar	−91	16.7	+ 152 (80)	+ 40	—	+ 472
Niger	—	21.0	+ 115 (80)	+ 163	+ 510	+ 400
Nigeria	−88	23.6	− 51	+ 292	+ 412	+ 1,103
Philippines	0	17.3	− 23	+ 23	+ 80	+ 105

SOURCE: Compiled by author on the basis of *World Development Report* (World Bank, 1985), tables 2, 16; and *UNESCO Statistical Yearbook 1985*, tables 3.4, 3.7, 3.11 and 4.1.

One detailed study' shows that five out of eleven African countries witnessed a drop in their expenditures per primary school student from 25 to 50 percent. In Asia, three countries out of five witnessed a drop from 30 to 60 percent per student, while in Latin America, three countries out of six have witnessed an expenditure decrease per student from 12 to 20 percent.

One more indicator should be mentioned. The pupil/teacher and student/professor ratios have also fallen in this period. This means that enrollment growth was accompanied by parallel or even faster recruitment of teachers. In other words, as the number of students grew and the cost per student dropped, the number of teachers and professors kept on growing parallel with enrollment. The consequence is clear: as available resources expressed in constant prices were reduced and as recruitment of teachers went unabated, the purchasing power of teachers was correspondingly affected. One may say that the momentum of enrollment growth took place at the expense of the take-home pay of teachers. Although in Africa and Latin America, a teacher's annual remuneration expressed in terms of GNP per capita is higher than in the OECD countries, it has tended to drop alarmingly.

If one assumes that the greater the number of "contact hours" of teachers in their classrooms, the higher the quality of teaching, then the drop in real wages of teachers has had a negative impact on the quality of education. This is so since poorly paid teachers need to supplement their limited income by teaching in more than one school or privately, or by driving taxis or running a private business, with negative repercussions on their classroom performance.

As many governments often need to mobilize all available resources to meet pressure from teachers unions to preserve a relatively low pupil/teacher ratio and thus maintain recruitment momentum, fewer, if any, financial means are available to meet other recurring expenditures, such as textbooks, notebooks, pencils, etc. In fourteen countries of Africa, no country spent more than 3.6 percent on recurring expenditures outside wages in primary education budgets, and more than half spent less than 2 percent.'

The first impression, therefore, needs to be corrected: things are not going well for education as a result of the economic crisis. A clear deterioration of educational systems has been taking place, particularly in heavy-debtor countries.

To complete this depressing picture, it is necessary to recall that while the economic crisis has affected both the human and financial *inputs* into education and the learning process, it also has had adverse effects on the *output* of the educational system, given the unemployment characteristics of most developing countries. Among these, the most obvious and well known is the outflow of educated manpower - the brain drain. Lesser known but no less dramatic is the qualification escalation for jobs without significant skill requirements, which are increasingly filled by overqualified people. This in turn hastens the race toward more diplomas and thus accelerates further the expansion of school systems.

Impact of Adjustment on Education

One consequence of the economic crisis is that education - considered by economic planners as part of the "soft" social sector - faces demands for domestic austerity and competes with higher priority items such as export promotion and military spending, notwithstanding demands made on education by the production and infrastructure sectors. The social sector (education, health, housing, social security, etc.) is usually the first to be hit by austerity, while debt servicing and military expenditures are considered irreducible. One possible consequence of this may be a dwindling of the role of the state in the field of education and a corresponding boost for the private sector.[3] Such a trend is contrary to the historically accepted role of the state in providing for public education, which rests on three assumptions worth recalling: (i) social and economic needs for education are greater than private demand; (ii) the external effects of education extend considerably beyond an individual and his family; and (iii) poverty must not bar an individual's access to education.

While privatization may represent the extreme alternative to public education as we know it, other consequences of adjustment measures essentially leading to a stagnation or decrease of resources for education must be identified.[4]

a) Structural changes are likely to take place in the internal distribution of resources in the education budget. Less funds will be made available for investment in the short term as pressures to meet recurring expenditures (essentially wages) predominate. Furthermore, no lobbies will fight for recurring expenditures other than teachers' wages. "Because most expenditure is in salaries ... there is reason to believe that provision of materials and supplies will fall more than overall budgets and cause greater damage. These effects may well outlast the resolution of the current debt problems."[5]

b) Allocations by level and sectors within the educational system are likely to favor secondary and higher education. The "chimney suction" effect of the formal school system implies that the end purpose of primary education is admission to secondary education, which in turn is justified by entrance into higher education. Thus graduates of one level are automatically attracted to the next. This has very serious financial implications as unit cost per student rises very rapidly indeed from one level to the next. Thus, primary education unit cost in Africa in 1981 was 59 current dollars, while for the same year, secondary education cost $409 and higher education cost almost $3,500. Equivalent figures for Latin America were $212 for primary education, $301 for secondary and $1,720 for higher education.'

As graduates of one level of schooling move on to the next, the cost of their study rises dramatically (sixty times in Africa as a primary school pupil becomes a university student). This naturally leads to a shift of expenditures in favor of the system's upper levels and further increases social imbalance as rural-based, primary school age children are neglected in favor of upper-level students who are essentially urban-based and represent an articulate and vocal constituency close to the centers of political power. The present trend moves resources away from primary education and potential beneficiaries from the low-income group and toward higher-income groups whose children often benefit from both tuition exemptions and high living allowances.

c) To counter the above trend, efforts are sometimes made by governments and at least one lending agency' to implement cost recovery measures. "Many systems levy official and unofficial school fees on students to support facilities in schools, increasing the direct costs to parents even in those systems where education is nominally free."" Examples abound, from primary education in Chile to secondary education in Tanzania. Although this may reduce the pressure on government budgets, it has damaging implications for equity. It is worth recalling in this connection that a 2 to 3 percent decline in average income in Africa means quintupling such a drop for the poorest.[9]

d) As resources for outlay other than wages are almost unavailable, research, experimentation and innovations which in certain cases can spell the solution to an apparently hopeless situation (for example, in Mali, 15 percent of government expenditures pay for 30 percent primary school enrollment, while another 15 percent goes to enroll less than 10 percent of the secondary school age group and less than 5 percent of the higher level age group youths) are simply not taking place at the initiative and cost of most developing countries, and in Africa in particular. This absence of a search for alternatives is often made up by donor agencies, to be sure, but this further serves to increase dependency on outside software and alien socio cultural models.

A Challenge to the International Community

We noted earlier how the decrease in new resources for education is affecting teachers' presence in the classroom and the availability of learning aids. Later, we listed four negative consequences of adjustment policies, all of them tending to accentuate social imbalance and jeopardize the achievement of the fundamental equity objectives of education. We also warned that we should not fall into the trap of wishful utopian ideologies as we grope for redress to the growing injustices inevitably taking place in a world of human imperfection.

This does not mean, however, that the international community must choose between desperate inaction or sterile rhetoric. Between the two are several viable alternatives, worthy of attention, including:

a) Providing governments with detailed, systematic analysis of the deterioration of education and its implications for future generations. Existing studies and surveys need to be published and disseminated. Educational planners must learn to produce and utilize the financial and economic tools necessary for negotiations with overall planning, financing and monetary decision makers in order to prove and not simply to state - (i) that cuts in educational outlays are harmful to the nation in the long term, and (ii) that better management of available resources (school location, staffing and in-service training) are conducive to savings.

b) Mobilizing resources for producing school materials, which will also serve to develop national entrepreneurial and marketing capabilities.

c) Resisting the transfer of resources away from deprived target groups and attempting to establish cost recovery from higher income groups. Transfers to private sources should be tempered by intermediary measures, such as government-guaranteed student bank loans. These are necessary in order to "avoid adverse effects on equity if education is rationed according to personal resources."[10]

The push for increased and improved schooling for the poor through a system of education which offers them access to it and opportunities for promotion within it are objectives that few countries will challenge in formal statements. Yet adjustment measures designed to conserve scarce resources are likely to push the neediest out of the system. This may well be the brutal reality which is imposed on all governments faced with the desperate need for economic survival. However, such choices will have long-term counter-productive consequences. The development of a privileged urban class at the expense of the rural and urban poor may ultimately spell the inability of these countries to mobilize the intellectual and creative resources of tomorrow.

While the intention of giving importance to the human element is unquestionably of a noble nature, it must not be forgotten that the internal mechanics of the decision-making process in governments relate more to power structures than to generous and praiseworthy motives. Thus, whenever initiatives are taken by individual governments to ensure greater social justice through a redistribution of educational opportunities, the international community should extend its full financial support. Economic growth is a condition of development, but it cannot be allowed to take place with international support if at the same time it negates the values of social mobility and justice, which are indispensable factors for avoiding future domestic and international strife and violence.

CHAPTER 12

The Impact of Present Adjustment Policies on Employment

S. K. Jain

Adjustment is an ongoing process, whatever the state of the world economy *as* incomes rise, tastes change and the location of production shifts. However, adjustment should be easier and less painful to accommodate in times of fast world growth; furthermore, at any point in time, some countries will be seen to adjust faster than others. In the developed world, some countries have traditionally been more successful than others in changing their production structure while preserving employment levels, although the great labor shake-outs of 1980-81 changed the general impression as to which countries were most successful in this respect. For the developed countries, successful adjustment has clearly required predictable government policies, relatively farsighted enterprise management, reliable and present sources of enterprise financing, and an appropriate labor relations framework that stressed collaboration rather than confrontation in wage bargaining and labor-management relations.

The changes in the international trade and financial system since the 1970s have given the concept. of adjustment a much more narrow focus, shifting the emphasis from adjusting to long-term secular trends in employment and productivity in various sectors of the economy to 'coping more directly with decreased export possibilities.

Since the debt crisis broke first in Latin America and then in Africa, the form of adjustment which has been forced on developing countries has required them to (i) lower imports in order to free resources for debt servicing, (ii) raise exports so that foreign exchange Carr be earned for growth to take place and (iii) pursue development paths which allow poorer countries to export those products for which demand in industrialized and semi-industrialized countries is still increasing, and so to rely less on growth in the developed countries automatically trickling down to them (i.e., to adjust to a situation of depressed primary commodity prices and reduced flows of outside finance).

Achieving these three aims has been associated with generally concretionary policies of stabilization and the management of internal demand; devaluation to boost the production of trade able goods and services; liberalization to eliminate any bias against exporting which may be caused by excessive domestic protection; and increased attention to resource mobilization, often including higher interest rates, in order to raise domestic savings. Merely to list these policies is to suggest that a country forced to implement all of them will be likely to run into severe problems of timing and sequence, if not indeed contradiction, given the very uncertain time frame in which they may take effect. In addition, the sum of the effects of these policies may well differ from the expected effects of each taken individually.

It is also, of course, frequently pointed out that different countries have differing abilities to adjust precisely because some are more able to change their structure of production, and to change it more quickly than others. Energy-rich developing countries may have particular problems in this respect, since reliance on one principal and profitable export has made diversification difficult, and more traditional exports may have been abandoned. However, what gives countries that ability to adjust, and what role labor markets play in adjustment - both within the enterprise and in general - is a subject for discussion. There is common agreement that what is required is "flexibility," although there is far less agreement on whether that flexibility will be achieved by a withdrawal of state intervention, market regulation and investment guidance and by a reduction in budget deficits, or by continuing prudent intervention, protecting acquired labor rights, and fostering social consensus to support necessary policy decisions.

How the package of policy measures called "adjustment" can be expected to affect employment will vary according to (i) what are viewed as the most desirable characteristics of employment and how attainable they are, (ii) the nature of the labor market, especially the extent of dualism, whether or not this is intensified, and (iii) the precise policies which are thought necessary to achieve adjustment (stabilization and structural adjustment policies), the sequence of their implementation, and their overall impact on GNP growth. The first two points perhaps need some explanation.

There are certain characteristics of employment which are recognized as desirable. Employment should be productive; it should be freely chosen; it should provide an adequate income, security and the opportunity for skill acquisition and advancement. The employed are not solely wage-earners. The self-employed also have their targets - for reasonable access to raw materials, markets and credit and for opportunities to raise their productivity. In times of austerity and adjustment, what seems the minimum to stipulate as desirable characteristics of employment is that (i) excessive falls in income levels should be avoided, as must be prolonged rates of high open unemployment, because of the social harm they bring; (ii) if enterprises collapse, the workers must have fair warning - and an opportunity to help save their jobs, which requires a degree of information-sharing and dialogue with employers; and (iii) the framework for training must be laid so that the self-employed and small-scale entrepreneurs have the opportunity to help themselves.

A further view of labor markets in developing countries is that they exhibit various degrees of "dualism," which might be summarized as the existence of widely varying levels of pay and conditions of work in return for the same input of effort. It does not follow that either the more or the less dualistic labor market is likely to demonstrate the desirable employment characteristics mentioned in the previous paragraph. Highly dualistic markets are likely 'to provide some workers with a reasonable degree of labor protection, which may be associated with a more than reasonable degree of trade protection and privileged access to finance for some enterprises. Some of those who plead for greater flexibility in developing economies see this element of dualism as a handicap to adjustment. In less dualistic labor markets, which are to some extent associated with more export-oriented economies, and perhaps with economies with a greater degree of rural inter household income equality, there may well be widespread flexibility in hiring, firing and wage setting with very little worker-management dialogue. However, it is likely that the extent of dualism will strongly affect the impact of output growth on labor market behavior. Output growth within the context of a dualistic labor market (or perhaps it would be better to refer to dualistic labor and product markets) may lead to productivity increases in the already high-productivity segment of the economy and to a slow rate of net labor transfer from low to high productivity occupations. In other words, underemployment in informal sector activities may continue to predominate in large parts of the economy. In less dualistic markets, output growth should lead to the turning point at which the real wages of unskilled labor begin to rise faster than the rate of output growth as, finally, even this type of labor becomes scarce.

Stabilization Policies

In respect of the nature and sequence of policies within the adjustment package, the first policies to discuss are those bringing about some contraction in demand in order to reduce imports to a level which can be financed by reliable foreign exchange earnings and inflows.

Monetary restraint and credit policy are usually important aspects of stabilization policies. Since in most developing countries a large part of available credit is provided by the banking system to the central government, credit restrictions often also involve trimming the public sector deficit and are thus closely connected to fiscal policies. Money wage restraint, especially with inflation, will also result in demand contraction. Since, over time, inflation has usually resulted in an increase in the effective exchange rate, devaluation is often recommended as an accompanying measure in order to restore an earlier effective exchange rate. This gives an upward push to domestic prices, but as the demand for import able decreases and that for export able increases, the initial effect of higher prices should be compensated by higher growth in real GDP if supply factors are favorable. Furthermore, by making imports more expensive and by providing exporters with higher returns, at least in domestic currencies, a shift also takes place in net incomes to producers of trade able goods (even in the absence of increased production) from those producing non tradable (including the government administration).

These represent the type of policies which have been introduced widely in Africa. Although balance-of-payments deficits have been reduced, the turnaround in economic activity and the pick-up in employment have yet to come. Real wages in non agriculture, for example (see table 1), have dropped considerably; furthermore, the growth of nonagricultural employment has been lower than that of the population, suggesting a greater concentration of population on

TABLE 1
Development of Reel Wages Between 1980 and the Most Recent Year Available

Country	1980	Latest Available Year	Index
Kenya	100	1984	87
Zambia	I00	1984	67
Tanzania	100	1983	60
Malawi	100	1982	90
Maudtim	100	1984	98
Swnlland	100	1983	95
Zimbabwe	100	1983	97

SOURCE: Unpublished 1W data

One reason why the situation in Africa has not improved, and why stabilization has failed to lead to a sustainable balance-of-payments position, is that the structure of African economies makes ordinary stabilization policies less effective, and even in certain cases countereffective.

Most countries still have a dualistic agricultural sector with a considerable subsistence share, a very weak industrial base and a young bureaucracy. Above all, more time and more new investment are needed than most stabilization programs provide for. The main elements of stabilization policies in Africa are common, and a major one is a reduction in the public sector deficit. Since the tax base usually cannot be expandedd as income from trade-related taxes has usually fallen, this leads to a decrease in public activities in general.

Public sector deficits have often increased precisely due to external causes. Lower imports and exports mean less revenue from import and export taxes (often a considerable source of revenue), while also because of the recession, increased claims are put on the government to cushion effects of the downturn by price subsidies, writing off losses of public enterprises, and providing alternative employment. Another factor is the continuous pressure for recurrent expenditure associated with development projects financed with bilateral or multilateral aid. In the absence of sizeable domestic capital markets, most borrowing is directly from the banking system, generating an inflationary impact. However, as imports are usually rationed and already considerably restricted, the inflationary impact translates itself not directly into increased imports but into excess liquidity in the domestic market, which finds its way into urban and rural informal activities and into black markets for foreign exchange, where rates are pushed up by the great pressure to transfer wealth out of the country at almost any cost.'

Devaluation is likely to be an essential step in promoting the export sector in Africa, although it is questionable whether the reaction of producers to devaluation will be as expected without measures to improve infrastructure and to supply incentive goods. However, what happens in the urban environment is equally important. Real wages have already dropped considerably, and continuous devaluation and increases in food prices (often not the consequence only of increased producer prices, but also of abolishing subsidies) Will continue to worsen urban living standards. Poverty in Africa is becoming increasingly not only a rural but also an urban phenomenon as the gap between rural and urban incomes naaows. Although this may mark a reversal of earlier and unwanted trends, some aspects of it worry many African countries. Real wages have decreased largely because of sizeable increases in the price of the staple food (either because subsidies were abolished or through the combined effects of adjusting producer prices to border prices at a time of currency devaluation). The price of the staple food traditionally plays an important psychological role in African societies, and although price increases may have been warranted, their extent has often met with strong reactions.

Inevitably, African experience suggests that income distribution and social factors were not given appropriate consideration in deciding on the measures to be included in stabilization programs. Large decreases in real wages and reduced expenditure on essential services for education and health will not only have unfortunate social effects, but will also negatively affect labor productivity. If wages drop fast, the worker's morale falls, productivity is low, and activities develop rapidly outside the official job in order to complement falling incomes. This sets into motion a downward spiral of lower wages, lower productivity, lower wages, etc. If it is not possible to maintain wages at an acceptable level, some industries and public services could offer either such traditional compensatory measures as increased social security or worker participation in the enterprise, or, perhaps less traditionally, the allocation of plots of land to workers to grow their own foodstuffs, with set times of the day or week to cultivate these plots, thus avoiding high degrees of absenteeism during the working week.

In most Latin American countries, stabilization policies have also been successful in reducing the external balance; but this had its costs. Adjustment was reached through a large contraction of imports, which by 1985 were about 40 percent below their 1980 level. Real per capita GNP fell by 9 percent between 1980 and 1984. Such internal contraction resulted in increases in unemployment; open unemployment went up from 7 percent to a probably underestimated I 1 percent in 1984. However, not only did unemployment increase, but real wages often fell by large amounts, as shown in the following table.

TABLE 2
Cumulative Change in Real Industrial Wages in Selected Countries from 1980
(Percent)

Country	**1981**	**1982**	**1983**	**1984**
Argentina	-10.7	-21.2	8.1	28.9
Brazil	6.5	13.9	3.8	-2.9

Chile	11.7	8.8	-2.4	-3.1
Colombia	0.4	4.3	7.9	16.8
Mexico	3.1	1.7	-23.4	-35.5
Peru	-1.9	-1.0	-22.2	-22.2
Venezuela	-3.0	0.0	-3.1	-10.0

SOURCE: ILO, Report of the Director-General to the 12th Conference of American States Members of the International Labour Organisation (Montreal, 1986).

Almost all stabilization policies carried out in Latin America relate to urban and formal sector activities and comprise a reduction in the government deficit, devaluation and wage restraint. Reduction of the government deficit through spending cuts (to the extent that taxation could not rise) has obvious contractionary effects; devaluation is supposed to have initial contractionary effects, but longerterm expansionary effects; a decrease in real wages is aimed at increasing employment (assuming a high elasticity of substitution of labor for capital), at regaining international competitiveness, and at lowering production costs, and consequently, inflation.

In order to boost the production of tradeables, devaluation has been common; however, the international recession and mounting protectionism have reduced the benefits which might earlier have been expected. Imports mainly consist of intermediate products and capital goods and, with some exceptions, hardly of consumer goods. The former categories are much less sensitive to price changes than are consumer goods, so that devaluation on the demand side in effect results in increased production costs, which are absorbed either by increasing the prices of the final products or by decreasing other production costs, often wages. To tackle these problems, either production and productivity have to be increased, or production must be shifted to more profitable activities. This, however, requires much more time than is allowed in normal stabilization programs.3

Real wages are often the cost category par excellence to be reduced in order to compensate for other cost increases. However, since the production structure is fixed in the short term, such decreases in wages will not quickly lead to increased employment. It has indeed been suggested that after stabilization policies have been implemented, the wage share in national income has usually fallen.

The impact of contractionary policies on employment is thus generally negative. Wages fall, and employers are likely to make strong attempts at reducing wage and nonwage costs. Larger enterprises are likely to be more resilient than small ones or are more likely to be helped out by the government, so that dualism may well increase. Some of these negative effects, but not all, may be inevitable. There is, for example, no reason for traditions of trade union recognition and worker-management dialogue to be rejected during recessions. Indeed, it can be argued that they are more necessary than before. However, we now turn to a discussion of the employment impact of the type of policies of deregulation and liberalization associated with structural reform.

Structural Adjustment

Structural adjustment can be interpreted as the implementation of policies which change the current allocation of resources in order to foster long-term growth. It could thus include virtually any spectrum of policies. However, given the problems most countries have in obtaining foreign exchange to pay for a critical mass of imports of consumer and intermediate goods, as well as the capital goods needed in order to diversify the structure of production, and given that the internal markets of many developing countries are too small for economies of scale to be reached, most structural adjustment policies rather drastically emphasize improving the country's ability to export. In that respect, many countries are being urged to adopt policies which involve a greater reliance on market-determined prices and withdrawal of government intervention in directing the pattern of investment. It is usually claimed that such policies will benefit labor as a whole, although one may doubt whether such a process will be in any sense automatic, or without substantial costs. If such policies lead to increased growth, then of course employment should benefit. However, some problem areas for employment are those connected with the transition and the implementation of structural reform, including job losses in previously protected industries or in slimmed-down public enterprises, and with the role of government in industry. Another issue is the risk of neglecting small-scale urban and rural activities which may appear to operate at low productivity levels. Indeed, the relation of deregulation and trade liberalization to rural development is rarely made clear. In addition, the extent to which the lower real wage levels in the public sector often associated with such policies will not only lower morale but alsoo decrease efficiency through stepping up civil servants' secondary and tertiary activities should be a matter of continuing concern.

Certainly in many countries restrictive trade policies have created industries which are protected from effective competition, have a high cost structure, and often use unnecessarily capitalintensive techniques, thus reducing employment opportunities. Dualistic labor markets have thus been encouraged. Most structural adjustment programs, therefore, contain policies for trade liberalization. Although the theoretical gains from trade liberalization are well known, and the abundant factors of production which should benefit in most developing countries include labor, recent literature and the analysis of specific country situations indicate that the issue can be complex.' Trade liberalization can have unpredictable results when it takes place in an economic environment where distortions apply in virtually all markets.

A further question is that of timing: if capital cannot be transferred rapidly to new industries (or is anyway absent because of low domestic savings or capital flight) and capacity utilization cannot be increased, one result may be to lower real wages without increasing employment. If there are such problems with mobilizing domestic capital, liberalization policies are likely to be associated with a greater use of foreign savings, or with direct foreign investment. Transitional problems may arise when the new employment generated benefits different labor force groups from those who lost jobs earlier. Further problems may arise if the foreign investment does not develop links with local enterprises.

Trade liberalization is also expected to stimulate enterprise efficiency through competition. Enterprises must, of course, be able to withstand competition if they are to survive, and the certain threat of competition is a powerful force. However, greater efficiency can also be achieved through better management, better labormanagement relations, anticipatory investment in more up-to-date technologies, etc. One of the problems of transition to a more open economy is to convince entrepreneurs that liberalization will stick, and then to assist them in making these internal changes - which may be easier if they have access to foreign capital in advance of trade liberalization.

It may be useful to review some country experiences. Thus, for example, in the Southern Cone countries in Latin American in the second half of the I970s, a number of liberalization measures were enacted. At different times and in a different sequence, Argentina, Chile and Uruguay undertook trade liberalization, moving toward a common tariff level which was lower than previously, domestic financial deregulation and freeing capital movements. In the first part of the period, stabilization programs aimed at reducing government deficit spending were also in place. Especially in Chile, where the government budget deficit as a share of GDP had been very high in the early 1970x, the initial deflationary impact of stabilization policies was severe.

By the mid-1970s unemployment had risen inn all three countries, and real wages had fallen. Subsequently, unemployment fell gradually in Chile until 1981, as it did in Argentina, although the fall came later in Uruguay. Given the essentially modem nature of these three economies, with a predominance of wage labor, and given the apparent absence of any policies aimed at raising levels of productivity in small-holder agriculture (in Chile, the rate of decline of the agricultural labor force accelerated throughout the period 1960-80), then employment growth will largely depend on the investment patterns of private firms and the rate of growth of the creation of new enterprises. So far as the former is concerned, it would appear that private dinvestment, which at least in Chile and Uruguay was particularly depressed in the early 1970s, recovered well toward the end of the 1970s. The general picture is one of a rise in productive investment during the liberalization period which nevertheless did not necessarily compensate for the fall in levels of government deficit-financed activity in the earlier period. This no doubt was a major reason for the large jump in Chile's unemployment rate in 1974-75.

Many observers have nonetheless pointed out that one of the unexpected effects of liberalization was that enterprises began to devote more attention to making profits on financial transactions than through the production of goods. This was also a consequence of domestic financial deregulation, which raised interest rates, and of freer access to foreign funds. One result of liberalization was the destruction of certain enterprises and increased concentration among producers.° The remaining enterprises by all accounts became considerably more productive, and large increases in labor productivity were recorded as many firms began to have access to imported technologies. Quality increased in the face of foreign competition. However, enterprises in some product lines apparently switched from production to the distribution of the competing imported product.

Another example is that of the Philippines, where in the late 1970s the argument gained ground that trade policy had inhibited the development of the country's comparative advantage in laborintensive exports. One result was the establishment of an export processing zone, but the employment results were disappointing. The incentive system for industrial production in fact continued to favor many relatively capital-intensive sectors, and manufacturing's share of total employment fell gradually during the 1970x. In 1980 the government adopted a structural adjustment program for the industrial-commercial sector with a World Bank structural adjustment loan. A major element of this was a three-stage process of trade liberalization to be carried out until 1985.

Comparing employment data for 1980 and 1981, there is no doubt that the introduction of the liberalization program reduced employment, especially in textiles, and in most sectors as imports rose (consumer goods imports more than tripled from 1975 to 1981). However, comparing employment indices for end-1981 and 1983, overall manufacturing employment was some five percentage points down but textiles and garments were four or five points up, while the intermediate goods-producing sectors, which had been overprotected - chemicals, paints, plastics, cement, glass, etc. - lost significant amounts of employment. It seems likely, therefore, that the program was working in the direction of shaking out the more capital-intensive industries and promoting the labor-intensive ones, although clearly with net negative effects on employment.°

These remarks suggest a number of conclusions. One is that both the timing and the sequence of changing policies are very important. In the Southern Cone countries, especially Chile, trade liberalization of a fairly thorough kind followed a period of socially painful stabilization, and the results for employment and incomes were severe. Output increased, but not very quickly, and the political strain generated was intense. Furthermore, whatever economic benefits were generated were substantially weakened by the inconsistency of later financial and commercial policies, which suggests that such ambitious attempts at liberalization need extremely careful direction. Chile's experience also points to the possibility of a number of perverse reactions by enterprises which can further reduce employment and possibly increase labor market segmentation as the concentration of enterprises increases. This conflicts with the picture of trade liberalization as drawing more and more semiskilled workers into producing for the export industry.

In the last respect, structural reforms in the Philippines might finally change the pattern of industrial production toward greater labor intensity, with beneficial effects on labor absorption in manufacturing. But the Philippines' experience in general also suggests that, as in many developing countries, the positive effects on rural incomes of developments in the manufacturing sector (and these effects were certainly negative at one point) are probably minor and slow to appear. Thus structural reforms need to apply as much to rural development as to trade and industrial policy if the bulk of the labor force is to benefit.

The discussion suggests that the beneficial effects of liberalization on employment may come in two main ways, namely, via the possibility of expanding exports (where so much depends on the market situation in the main importing countries) and via the likelihood of reducing the prices of intermediate products, especially those used in agricultural production which had been overprotected earlier.

What, then, can we say about the impact of adjustment on employment, bearing in mind the impact on (i) growth of output, (ii) dualism in labor (and product) markets, and (iii) attainment of desirable characteristics of employment? Some points seem simple: contractionary policies designed to reduce domestic consumption and investment and hence improve the balance of payments will, as such, reduce output growth rates. "Import strangulation" may easily result in factory closure and, if it extends, for example, to the production of farm inputs, lowers rural incomes also. Cutting government deficits can also lead to postponing investment expenditure, thereby making the employment prospects of casual construction labor worse than usual. It also contributes to the deterioration of existing infrastructure, which will raise transport costs and lower overall productivity. Public sector wages will usually be frozen and recruitment halted. How long such effects continue will depend on where the new growth impetus comes from.

Contractionary policies aside, most elements of adjustment policy are aimed at (i) ensuring that developing countries wilt be in a position to respond to whatever growth impulses come from outside (e.g., by establishing a reasonable exchange rate, or increasing enterprise efficiency and awareness of foreign markets), and (ii) domestic deregulation, in the hope that internal stimuli to growth will emerge. However, as we have seen, contractionary policies cannot be set aside from other adjustment policies. For example, even in Chile, when the policies were implemented in sequence, the overhang of contractionary policies in terms of unemployment made the acceptability of liberalization much more difficult. In other countries, e.g. in Mexico over the last two or three years, there has been an attempt to implement all facets of adjustment at once - unsuccessfully. In many African countries there is an increasing belief that, whatever the merits of recommended adjustment policies, there is a threshold level of imports which is necessary for their success and which has not been reached. Furthermore, while the pattern of agricultural prices which would probably follow liberalization would be helpful in promoting agricultural exports, pricing policy alone is insufficient to promote output growth.

Many advocates for liberalizing and deregulating policies of structural reform like to contrast highly distorted economic systems with outward-oriented and usually more successful economies in terms of growth and labor absorption. It is not difficult to demonstrate the general superiority of the latter, even if certain desirable employment characteristics are not present. However, it is not generally spelled out how economies should move from one state to the other, nor how the inevitable costs can be minimized, nor, indeed, why governments should always consider it in their interests to do so. It is also not clear why countries should adopt what is often to them a wholly new approach to development because of the problem of foreign exchange scarcity experienced at one point in time. Furthermore, it is difficult to substantiate the claim often made that governments in faster-growing countries generally played a smaller role in direct production and in guiding investment decisions. Thus, one issue is not whether there should be government intervention or not, but what form it should take.

Some observers claim that one major difference between the more outward-looking Southeast Asian countries and most Latin American countries is the greater weight given to agricultural interests in the former's economic decision-making process. These countries generally prefer an open trading environment; in contrast, countries with highly protected industry and a large service sector are usually against changing the trade regime. Liberalizing governments in much of Latin America will therefore face considerable difficulty in implementing reform, since the constituency which would favor it is either small in size, e.g., agriculture, or yet to be created, e.g., producers of manufactured and processed exports based on the country's comparative advantage in labor productivity. Furthermore, the protectionist policies of the industrialized countries are preventing this latter pressure group from growing. In such circumstances, the process of liberalization can easily be reversed. In addition, in such countries the state has been directly involved in creating a certain production structure, which has been run in conjunction with the private sector. If that structure is to be demolished, it is unlikely that the private sector alone can create another.

What are the consequences for employment? It can be speculated that countries which really do pass from a distorted to a liberal regime might end up with a less dualistic labor market. However, the process could be lengthy and easily frustrated, and the expected result might never be reached.

A further point is that since adjustment policies are becoming all-embracing, it is of major importance that whatever policies are applied should be consistent and well coordinated with other longterm policies. One important policy area in this respect is that of human resource development. In this area, policies must not only be integrated with whatever structural adjustment policies are being undertaken, but must also take into account the devastating consequences of the present economic crisis on human resources. A target group approach to human resource development would seem to hold the most promise.

For workers in the low-productivity agricultural and the urban informal sector, human resource development can best take the form of increasing production and productivity by means of providing both more income-earning assets and improved techniques. However, since most of these labor force groups live on the fringe of poverty, training and skill upgrading cannot be undertaken in time spent away from production. It has rather to take place during actual production, which calls for nontraditional approaches to skill formation and upgrading.

Another group is that of the openly unemployed. Their characteristics differ among the various regions of the world, for the very reason that in the poorest countries, nobody can afford to be really unemployed. Relying on informal support from family or friends usually implies being partially involved in their economic activities. Thus, we need to distinguish between the "fully unemployed" and those involved in fringe activities. For the latter group, it will be necessary to decide whether in the future they will continue to be engaged in such activities, albeit with higher productivity, or whether they will move or return to more formal activities. (This last point is an important but often overlooked facet of informal activities, namely, the extent to which activities are undertaken because of an individual's belief that they will yield a fair income, or are seen as a second-best option. This has obvious consequences for future human resource development policies in many low-income countries.)

Human resource development for those who have become openly unemployed would be in first instance guided by the need to prevent a person's losing his ability to work, and secondly by anticipating future demands for specific skills. Although this issue is too complex to be discussed in a few pages, a gross oversimplificaton would be that for the first objective, emergency employment schemes could be the best solution, and for the second, retraining schemes are ideal.

Returning to the need for human resource development to be closely related to the structural adjustment policies being undertaken, a few points can be mentioned.

Industries will certainly shift their production processes and their products in the wake of structural adjustment policies, and some industries may become obsolete. For the labor force, this would imply an ability first, to be able to upgrade existing skills, and second, to develop new skills for new industries. The first of these might be easier to accomplish than the second, and a lot depends also on the general level of education and training of the labor force, as well as its age structure. It is important for any structural adjustment program to take these characteristics into account. A special but related aspect o£ structural adjustment and its relation to human resource development is that of new technologies, especially in the middle-income and other developing countries with a large industrial base. In some of these countries, the percentage of students in higher education is rapidly increasing, and workers to cooperate with these new technologies will not be lacking. Some structural adjustment programs may well emphasize the development of modem technologies, and this may widen the distance in skills and income between modern sector workers and those engaged in low-income activities. This in turn may strain the political system.

The final conclusion of these thoughts can perhaps be best phrased as a caution against applying standard solutions in the process of adjustment to the present shortage of foreign exchange. Future policies depend very much on the structure of the country involved and its ability to cope with change. Unwanted solutions will usually be short-lived. In that respect, it is important for any society, in close consultation with the various social classes, including organized labor, to formulate its own direction for the future.

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CHAPTER 13
Adjustment Policies that Increase Poverty

Nevis S. Scrimshaw

We live in a world in which chronic lack of adequate food is the daily lot of a substantial portion of the populations of most developing countries. Superimposed on this widespread condition are periodic crises of increased hunger occasioned by drought, civil disturbances or wars, and the inept policies of governments. In the present decade, poverty has increased, and the nutritional status of large populations has deteriorated further in many countries,` especially in sub-Saharan Africa and Latin America, where per capita incomes and public expenditures on health, education, and other basic social services have been sharply reduced by an additional factor. The effect on the poor of some economic adjustment policies urged or imposed on governments in order to qualify for international loans is a new and very real threat. Already burdened by huge debts and inadequate resources to service them, some countries are extremely vulnerable to further erosion of basic social services and an increase in poverty.

While economic adjustment actions are necessary and can be designed to help the poor, they commonly are not. Measures to restore foreign exchange balances that give little or no consideration to the potential deterioration of the nutritional and health conditions within a country can worsen the already unfavorable nutritional and health status of the poor, who make up the bulk of the populations of these countries. Their well-being has been increasingly sacrificed for short-term balance-of-payments gains. It is not the purpose of this paper to review or discuss these adjustment policies or responsi bility for them, but rather to analyze the significance for individuals and societies when such policies exacerbate poverty and malnutrition.

The much-publicized crises of famine and acute hunger of the current decade are an unnecessary disgrace to our global society and serious in their political, economic and human consequences. How ever, even more damaging in the long mn is the chronic under-nutrition that afflicts such a large proportion of the populations of developing countries.' When caloric intakes of many developing a countries are compared with the FAO/WHO' estimates of requirements, the evidence suggests that at least 800 million people are calorie-deficient'

For some populations, dietary calorie intakes average 10 to 20 percent lower than "requirement" estimates suggest. They are undernourished because they cannot afford enough food to allow a desirable level of physical activity.' For many, the hidden hungers of iron deficiency, avitaminosis A and iodine deficiency disorders are more common and significant than simple lack of food.

If undemutrition were an acute episode of limited duration met by prompt refeeding and rehabilitation, as occurred in Holland at the end of World War II, the effects would be minimal .6 This is not the case in developing countries with chronic undemutrition and longstanding nutrient deficiencies. Anything exacerbating these deficiencies increases their adverse functional consequences and elevates mortality from infectious diseases.

Despite the chronic undernuMtion, these populations are not wasting away and dying of starvation. Therefore, some compensatory mechanism must be involved that enables them to survive on apparently inadequate caloric intakes. The critical question is whether or not this adaptation has serious individual, social and economic costs. Sukhatme' has suggested that the adaptation may be one of increased efficiency of metabolism, but careful research studies indicate that, at most, I S percent of the adaptation could be accounted for by this mechanism, and probably much less.° Moreover, there is good evidence that most of this adaptation comes about through reduced physical activity.'

When the adaptation required is too great, or when the individual is forced to maintain activity despite reduced food intake, weight loss must occur. Because survival requires that work activity be sustained as much as possible, most of the reduction occurs in discretionary activities that are essential for family improvement and community organization, and on which development plans depend. And, of course, if the caloric deficiency is sufficiently severe, work activity will be affected as well.' °

An example of the effects on work activity is that in much of Central America, plantation workers are paid by the task rather than by the hour because there is so much variation in the amount of work that a poorly nourished laborer can complete in an hour. Viteri and Torun" observed that male workers on a plantation in Guatemala worked hard for the hours necessary to complete their tasks and then remained sedentary for the rest of the day and slept long hours in the afternoon and at night. When they were given food ad libitum for lunch, caloric intake and discretionary activity markedly increased."

A study of road workers in Kenya reported an increase of 12.5 I percent in daily productivity after an average of 53 days of caloric supplementation." Such observations are not confined to developing countries. It was reported in 1946 that the productivity of one group of calorie-restricted German industrial workers in World War Il increased by 47 per cent when caloric intake was increased by 500 calories per day."

The activity of children is similarly affected by caloric restriction. Viteri and Torun" observed in detail for one month the activity patterns and growth of children in a home for the recuperation of malnourished children in Guatemala. They then carried out the same observations when the caloric intake was reduced by 10 percent and later, 20 percent for similar one-month periods with protein and other nutrient intakes unchanged. With the first food intake reduction there was a notable decrease in play activity, but growth was not affected, and zero energy balance was achieved. With a 20 percent decrease in dietary energy, a further reduction in physical activity was not enough to compensate, and growth was also affected.

No comparable studies have been carried out with women. Since in peasant societies they must keep working from early morning until night, the adaptation must lie in the rate and efficiency of their work. Moreover, in some societies they are observed to lose weight during the hungry season." While physiological adaptation to calorie deficits may be complete in the sense that energy balance is achieved, the behavioral consequences are clearly of social significance. For women, the consequences extend not only to their household activities and child care, but also to the birth weight of their infants. This is particularly significant, because low birth weight due to undemutrition during pregnancy is associated with higher _ infant morbidity and mortality and poorer growth.

For young children, such a reduction in physical activity also means that the interaction with their environment that is essential for normal cognitive development is reduced, with long-term consequences for learning and behavior. When the energy deficit is more severe, their growth will be permanently stunted and future work capacity reduced, as discussed below.

Effects of Severe Calorie Restriction

The discussion thus far has considered degrees of enforced caloric restriction to which populations can adapt by reduced physical activity, sustained or seasonal weight loss, or impaired child growth. However, in many populations the impact of adjustment policies is even greater: many experience some degree of starvation with progressive weight loss and a marked loss of strength and endurance. When the weight loss is only 10 to IS percent, such changes as slowed heart rate, reduced ability to concentrate, and increased tiredness are apparent. The most complete review of the effects of marginal undernutrition is by Keys et al." With weight losses of IS to 20 percent, individuals become depressed, apathetic and weak and reduce their activity to a minimum.' s

Long-term Consequences of Growth Retardation

There is no question but that smaller adults require less food, since calorie requirements at any level of activity are a direct function of body weight. A decrease in metabolically active tissue decreases total metabolism. The problem with weight loss as an adaptation to adverse environmental circumstances is similar to that for adaptation by reduced activity.Significant individual and societal costs are incurred that tend to perpetuate

underdevelopment and poverty.
While it is apparent that people who have been stunted in childhood and survive to adulthood can work very hard and develop endurance, they are still at a disadvantage in the performance of manual labor. Many studies confirm this observation. In Guatemala, the physical capacity of plantation workers has been found to be less for stunted individuals as judged by treadmill measurements and field observations of capacity to cut sugar cane.' ° Similar findings have been reported from Brazil' ° and India."
The same relationship has been described for Colombian," Brazilian" and Indian" school-age boys. Desai et x1.99 showed that stunted adolescent males had a reduced physical capacity as measured by work at a heart rate of 170 beats per minute, which was one-third lower. The same significant relationship has been reported for Ethiopian1O and Indiana' adult males. Gopalan has warned of the fallacy of considering that "small is beautiful" when referring to the stunting that occurs with chronic malnutrition in childhood.'
Adaptation to low food intakes, beyond reduced physical activity, requires stabilization of weight at a lower level than that associated with good ad libitum nutrition. Adults in the low-income groups in developing countries are typically thin and obviously undernourished. If higher energy intake is required and caloric intake is not sufficient for energy balance, weight loss occurs and semistarvation results, with the further consequences described. The individual literally consumes muscle tissue to protect the essential visceral organs, including the liver, pancreas and intestines. The heart muscle shares in the loss, with a reduction in cardiac capacity.

Relationship of Hunger and Malnutrition to Infection

Reference has already been made to the strong association between malnutrition and infection. The relationship is synergistic. Any infection, no matter how mild, worsens nutritional status, and most nutritional deficiencies increase susceptibility to infection. The result is more serious than could be predicted from the effects of either alone.
Infections, even as mild as immunizations with attenuated virus strains, cause measurable anorexia and increased metabolic losses of nitrogen, vitamin A, ascorbic acid and other vitamins, minerals and electrolytes." These catabolic effects are compounded by the diversion of amino acids and other.nutrients essential for the synthesis of immunoglobulins and a variety of other metabolites associated with the response to infection. If the gastrointestinal tract is affected by the infection, absorption of nutrients may also be impaired.
These biological effects of infection on nutritional status are often compounded by behavioral ones. In many societies, individuals with fever and other symptoms of infectious disease receive starchy gruels instead of solid food. This practice is particularly hazardous for young children. The combined result of all of these effects is that the infection may precipitate acute clinical manifestations of nutritional deficiency disease if the individual already has a borderline status for a specific nutrient.
In populations where diarrhea! and other infections are frequent, new infectious episodes occur before nutritional recovery from the effects of the previous one. This explains the appearance of nutritional disease after an infection that seems to be no more serious than many previous ones. When death occurs in poorly nourished children, it is usually due to the synergism of malnutrition and infection, regardless of the apparent specific terminal cause.
An example of a nutritional disease usually precipitated in malnourished subjects by recurrent infections is kwashiorkor, the nutritional cause of which is protein deficiency relative to calories. Also in this category are xerophthalmia and keratomalacia due to vitamin A deficiency, and the vitamin deficiency diseases of ban-ban, pellagra and scurry. Moreover, iron deficiency, whose consequences are discussed later, is frequently due primarily to the effects of hookworm disease, schistosomiasis or malaria.
There is also extensive evidence for the role of malnutrition in reducing resistance to infection, so that both morbidity and mortality from infectious diseases are increased even in marginally malnourished populations.' ° The mechanisms include interference with cellular immunity, including Tell function, impaired phagocytic capacity, reduced, delayed cutaneous hypersensitivity, and defects in complement formation. With more severe malnutrition, the results are reduced antibody formation and alterations in epithelial integrity.' 1 The net result is that malnutrition and infection are mutually

reinforcing and often lead to a vicious cycle that ends in death.

Effects of Specific Nutrient Deficiencies

In addition to inadequate calories, there are three widespread -specific nutritional deficiencies with significant functional consequences both for individuals and for societies as a whole. These are deficiencies of iron, vitamin A and iodine. Fortunately, the other potential nutritional disorders are no longer of public health and social significance.

Iron Deficiency

Iron deficiency is the most common single nutrient deficiency in the world today. Iron deficiency anemia is found in about onethird of the population of many developing countries, and another third can be identified biochemically as iron-deficient, even though they do not manifest anemia. The significance of iron deficiency lies in the increasing evidence that both cognitive performance and resistance to infection are reduced even when the disorder is only mild to moderate in degree and not accompanied by anemia." As would be 'expected, these functions are still more affected when the iron status is poor enough to cause anemia. This pattern of iron deficiency effects also appears to hold true for work capacity and productivity.

The evidence for the effect on cognitive performance comes mainly from observations in the United States, Guatemala, Egypt and Indonesia. These studies show that infants, preschool children and school children who are iron-deficient have impaired performance on a series of appropriate behavioral tests. When they are then given either an iron supplement or a placebo on a double-blind basis, test performance becomes normal in those receiving the iron if the deficiency is mild to moderate. It is unchanged in those receiving the placebo.

This was the finding in studies of preschool children in Cambridge, Massachusetts," in Guatemala" and in Egypt.3 If the iron depletion is severe, however, as in some preschool children in the studies in Guatemala and Egypt, full recovery of test performance is not seen within the supplementation period of two months.'" In Indonesia," complete recovery of the hemoglobin concentration of anemic school children after three months of supplementation with 10 mg/kg/day of ferrous sulfate (figure I) is accompanied by improvement, but not complete recovery. No changes were seen in the placebo group. Similar studies have not yet been conducted with adults, but there is no reason to believe that the results would be different.

FIGURE 1

Cognitive Performance of Indonesian School Children

Before and After Iron Supplementation

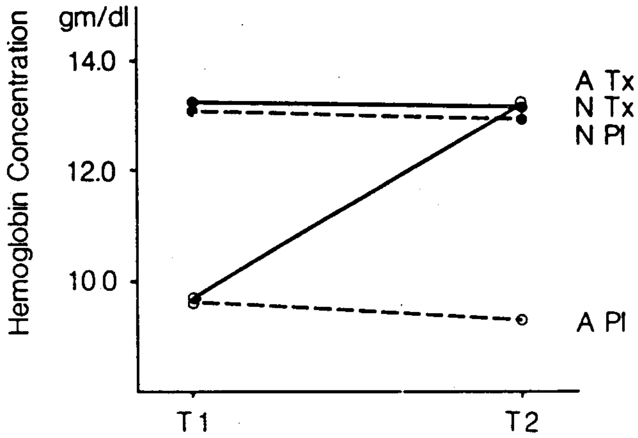


FIGURE 1A: Henfoglobin concentration at pre- (T1) and posttreatment (T2).
NOTE: A Pl: anemic placebo, A Tx: anemic iron–treated, N Pl: nonanemic placebo, N Tx: nonanemic iron-treated.

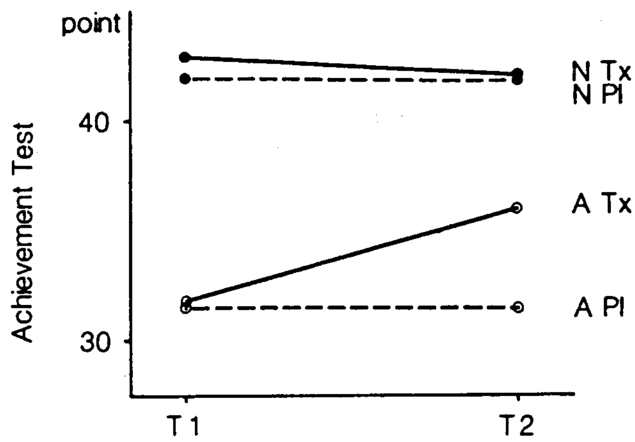
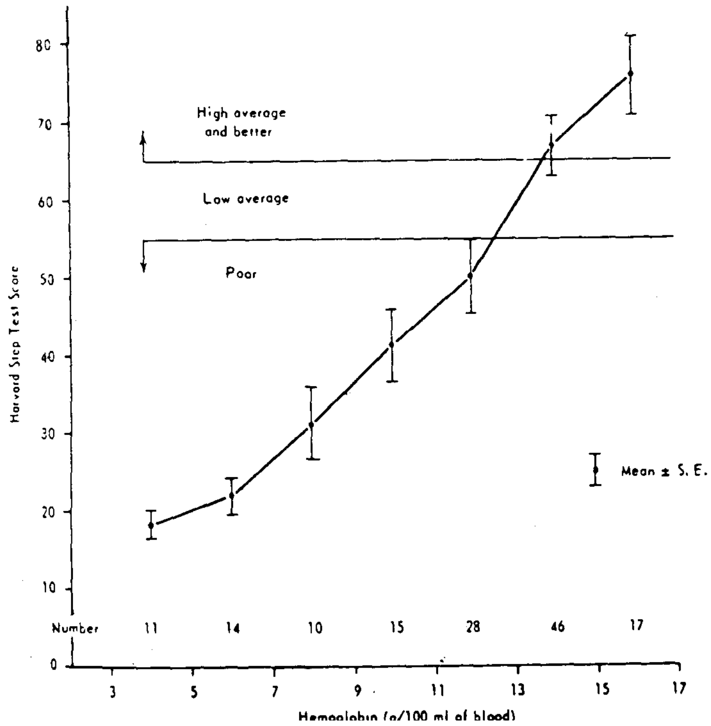


FIGURE 1B: Achievement test score at pre- (TI) and post treatment (T2).

NOTE: A Pl: anemic placebo. A TX: anemic iron-treated, N P1: no anemic placebo, N TX: no anemic iron-treated.
SOURCE: **A. G.** Semantic, E. Pollitt and I. Kim, "Iron Deficiency Anemia and Educational Achievement," *American Journal of Clinical Nutrition* 42 (1985): 1221-8.

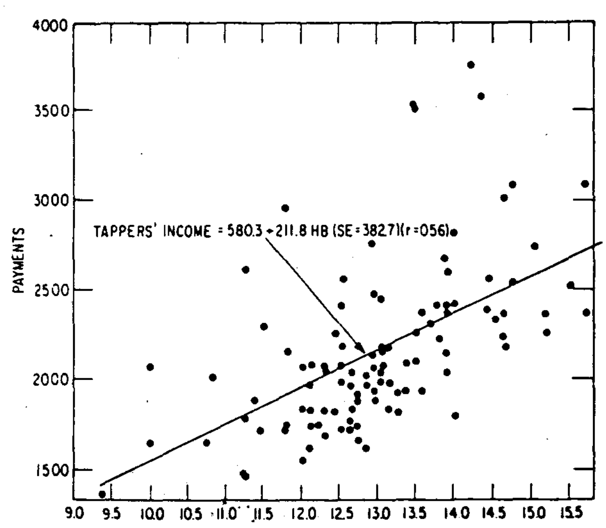
To study the effects of iron deficiency on physical fitness, Viteri and coworkers measured Harvard step-test performances on a Guatemalan plantation .[3 8] As figure 2 shows, scores were linearly related to hemoglobin levels, and the performance of most of the anemic workers improved strikingly with iron supplementation, while for most a placebo had no effect. Figure 3 shows the relationship between the take-home pay of Indonesian rubber tapers paid by the amount collected as a function of their hemoglobin level.3 9 When they were given an iron supplement for 60 days, their collections and pay increased by 36 percent. Similar relationships between hemoglobin and treadmill performance and productivity have been described for tea plantation workers in Sri Lanka" ° and Indonesia. [1]

FIGURE 2
Physical Fitness in Relation to Hemoglobin Concentration
in Guatemalan Agricultural Workers



SOURCE: A. G. Soemantri, E. Pollitt and I. Kim, "Iron Deficiency Anemia and Educational Achievement," *American Journal of Clinical Nutrition* 42 (1985): 1221-8.

FIGURE 3
Hemoglobin versus Taper's Income (Preintervention
Program on an Indonesian Rushers Plantation)



SOURCE: S. Baste, Soekirman, D. rkaryadi and N. S. Scrimshaw, "Iron Deficiency Anemia and the Productivity of Adult Males in Indonesia," American Journal of Clinical Nutrition 32 (1979): 916-25.

Equally significant is the relationship between iron deficiency and an increased frequency and severity of diarrheal and respiratory infections observed in studies in Alaska, Indonesia and a number of other countries." [z] Iron deficiency lowers the activity of the iron dependent enzymes that are needed in phagocytic cells to kill ingested bacteria, with the proliferation of the T-cells that are important for effective phagocyte function. It also affects the kind of delayed coetaneous hypersensitivity that is exemplified by the tuberculin reaction and that is an indicator of resistance. The hemoglobin iron of meat is the most readily absorbed, but iron deficiency can be inexpensively prevented through the consumption of leafy vegetables, the fortification of staple foods with suitable iron compounds, or the similar fortification of sugar or salt.

Iodine Deficiency Disorders

Endemic goiter is global in distribution wherever food supplies are produced locally on iodine-poor soil. The latter includes regionsthat have been glaciated, mountainous areas and areas with heavy rainfall. Goiter is still prevalent along the Andean chain of mountains, across central Africa and the Asian subcontinent, and along the entire length of the Himalayan chain, with large pockets of severe disease in China, Burma, Vietnam and New Guinea"Until recently, iodine deficiency was identified only with a compensatory swelling of the thyroid gland known as endemic goiter and with cretinism, a manifestation in the child of severe iodine deficiency during the mother's pregnancy. The typical cretin has profound mental deficiency, a characteristic appearance, a shuffling gait, shortened stature and a spastic dysplegia. The subject is usually deaf and mute, and usually dies unless given good care.

It is now recognized that even when cases of cretinism are small in number in a population, their presence indicates a much larger number of persons who do not have any of the classic features of cretinism, but whose linear growth, intellectual capacity and neurological functions are compromised to varying degrees.' ° Thus the burden to the community due to iodine deficiency lies in the widespread functional impairment in the population. The tragedy is that these conditions are all readily preventable through the iodination of salt or the administration of iodinated oil to women of childbearing age.

Vitamin A Deficiency

Severe vitamin A deficiency results in xerophthalmia, or dry cornea, and in a softening of the cornea - keratomalacia. The deficiency can progress to eventual prolapse of the iris and loss of the lens and a scarred, blind eye. This kind of lesion is most often seen in children with severe protein-calorie malnutrition or as an aftermath of diarrhea, measles or other communicable diseases of childhood in children already of borderline nutritional status with respect to the vitamin. Vitamin A deficiency also exacerbates iron deficiency` ° and is associated with increased susceptibility to infections.

Almost any society has green leaves available, if necessary wild ones, as well as green and yellow vegetables that, if consumed, would effectively eliminate avitaminosis A.

Cumulative Social and Economic Consequences

Greene° a has used a biocultural model to show that the range of iodine deficiency diseases, including mild mental and physical impairments, was accepted by an Ecuadorian community as normal and lowered their cultural expectations for human performance. These were adjusted downward to include the considerable number of mildly to moderately affected individuals. The same phenomenon has been noted by Chavez and Martinet in Mexico.° ° Parents assumed that passive, unresponsive children were normal and became distressed when the children became active and noisy after a supplementary feeding program was instituted. It seems likely that whole societies have adapted culturally to chronically limited food intakes. How they would respond to increased availability of food is unknown.

The realization that the majority of the population, both adults and children, in some struggling developing countries are being adversely affected by hunger and malnutrition and their synergistic interaction with infection can be viewed only with concern and alarm. The prospect of these conditions being worsened by the policies of international lending agencies that do not take such possibilities into account cannot be tolerated. There is an urgent need to draw attention to the magnitude of this problem and to take effective action to address the nutritional and health consequences of national economic crises and of adjustment policies to meet them.

The Prevention of Hunger

The world is quite capable of producing all of the food that is required for the foreseeable future, including anticipated population growth. Moreover, food continues to be produced to meet effective demand, that is, food that someone will pay for. The problem is that much of the world's population lacks the resources to pay for the food they need or the means to produce it. Even during most of the historical famines, food has been available and even exported, but the starving had no way of purchasing it.

No kind of assistance to governments, whatever their political orientation, will succeed in eliminating hunger unless the governments act with concern for the welfare of their populations; and such assistance may actually postpone the need for policy changes or have adverse effects on local food production. In such circumstances, assistance tied to specific policies or projects can still be beneficial for the people and may promote a favorable evolution of government policy. Where government policies have shifted in favor of the rural sector and food production, as in India in the I960s, the results have often been spectacular.

Less dramatic and less publicized than the emergency famine and refugee situations, but far more significant for the developing world, is the ineffectiveness, and often the indifference, of governments when confronted with chronic hunger in their populations, Given this, it is not surprising that in their dealings with international monetary authorities, they are not effective defenders of the poor. Under these circumstances, it is not sufficient for the lending agencies to say that the effects of their policy suggestions are the responsibility of the country concerned to determine and accept or reject.

There are enough successful examples to demonstrate that, for most developing countries, the conquest of hunger is a matter of policy, and not of resource limitations. If hunger and malnutrition are to be abolished in this century, there must be a far better understanding among policy makers in the international system, including those of the lending agencies, as well as of the individuals responsible for national government policies, that seriously adverse consequences for individuals translate into serious impediments to economic and social development. Thus, assistance of any kind that does not take into account the real human consequences will in the long run be self-defeating.

International meetings to discuss world hunger problems tend to recommend actions that have already proved impractical or inadequate. Moreover, while they have often stressed the role of the FAO and WFP, they have tended to ignore the actual or potential influence of the IHRD, the IMP and regional development banks. The true solution must be sought in a comprehensive process of social, economic and political development that is ecologically sound and that directly attacks both rural and urban poverty. Unless adjustment policies are designed to take this into account, improved balance-of-payments and debt management can come at the human cost of increased morbidity and mortality from malnutrition and infectious disease and perpetuation of the cycle of poverty and W health.

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CHAPTER 14
The Impact of Recession and Adjustment on Health in Developing Countries

Hakan Hellberg

The widespread economic crisis has resulted in a fall in living standards in the western hemisphere of over 9 percent (1981-83). In sub-Saharan Africa, they have fallen to 1970 levels. Food production in the African countries, seriously affected by drought, dropped by 15 percent between 1981 and 1983. Living standards also fell in some of the poorest countries of Asia. What follows is an analysis of the effects in tents of poverty, unemployment, hunger, ill health, and expenditure on health and health services.

The economic crisis has resulted in serious unemployment, currency devaluation and formidable austerity policies in response to the high cost of fuel, the heavy burden of interest payments, and unfavorable terms of trade in Africa and Latin America. While some countries have succeeded in protecting their health services from public expenditure cuts, many others have made substantial cuts in their health budgets. Import restrictions have severely reduced supplies of drugs and medical equipment to a number of countries, particularly in Africa. The effect of the crisis in some countries has been a virtual disintegration of rural health services.

Poverty increased as a result of unemployment, inflation and unfavorable terms of trade. Food subsidies have in many cases been abolished, and in drought-stricken Africa, food of any kind has been in short supply. The cumulative effects on health of increased poverty, unemployment, underemployment and famine, and the reduced capacity of health services to respond to health problems, cannot only be inferred, but documented with facts for a number of countries in Latin America and Africa. Malnutrition has increased. Reductions in infant mortality have been checked or reversed. Rates of well over 200 deaths per 1,000 live births have been reported within a number of countries of southern Africa.

The Economic Crisis

A major and widespread recession began in 1981 after the second sharp rise in oil prices It followed a period (1977-81) during which economic growth had been steady and considerable - at an average rate of about 3 percent per year. The increase in output fell to only 0.5 percent in 1982. There was a recovery in 1983 to a growth rate of about 2.5 percent, rising to over 4 percent in 1984.

The position of sub-Saharan Africa started to deteriorate in the 1970s. Between 1970 and 1980, GDP grew at an average rate of about 3.5 percent; then it started to fall. With population rising by over 3 percent per year, per capita income was estimated by 1983 to be about 4 percent below its 1970 level.

In Latin America and the Caribbean, GDP per head rose by 0.2 percent in 1984 - the first positive increase since 1981. But in twelve countries, including the largest, overall GDP per head fell for yet another year. In nine countries, GDP per person was lower in 1984 than in 1970, and in the worst case it fell back to the 1960 level. In sub-Saharan Africa, per capita GDP fell by 4 percent in 1981, 3.3 percent in 1982 and an estimated 3.8 percent in 1983. The most drastic fall in average living standards was suffered by the oil-exporting countries of sub-Saharan Africa: GDP per head fell by 6.7 percent in 1981, 4.7 percent in 1982 and an estimated 7.3 percent in 1983. The low-income countries suffered a total fall in average living standards of nearly 5 percent over these three years.

The Drought in Africa

The worst drought in fifteen years hit large parts of sub-Saharan Africa in 1982, extended its range in 1983 and continued in 1984. Food production in the twenty-four most seriously affected countries declined by 15 percent between 1981 and 1983. Export crops of coffee, cocoa and oil were seriously affected. Cattle losses were substantial in Botswana, Mauritania and Zimbabwe. Four to five years of good rainfall are estimated to be needed to restore cattle herds.

The devastating drought brought to a head the longer-term adverse trends in food production in this area, which has the highest population growth in the world. In the twenty-four countries most seriously affected by drought, per capita grain production has been falling by 2 percent per year since 1970. If this fifteen-year trend continues, per capita production for 1988 will be the same as in the drought-ravaged year of 1984, even if 1988 has normal weather. Cereal imports to sub-Saharan Africa totalled 9.25 million metric tons in 1982; this implies that one person in five (the equivalent of the region's entire urban population) was being fed from imports. Even in 1980, Africa as a whole was meeting only 86 percent of its 5 food requirements. Between 1981 and 1983, food imports increased from US$ 2,400 million to USS 5,800 million.

Debt and the Balance of Payments

The initial sharp rise in oil prices which triggered the crisis led to acute balance-of-payments problems for oil-importing countries. For example, the cost of fuel imports rose to 40 percent of Ghana's export earnings. On top of this, there was a 45 percent appreciation in the value of the United States dollar by 1984 compared with 1979, which contributed to a fail in commodity prices and a 20 percent deterioration in the terms of trade of developing countries with OECD countries between 1980 and 1984. Finally, world interest rates rose substantially, with high interest rates in the US.. caused by its substantial fiscal deficit. For example, interest payments in Senegal were multiplied threefold between 1980 and 1983.

Devaluation and Austerity

The balance-of-payments problems of the Latin American countries led to a series of devaluation of national currencies and formidable austerity policies which were reflected in negative growth rates and cuts in imports. In the extreme case of five countries, imports per head in 1983-84 were half or less than half the rates of 1980. The policies were successful in improving the overall balance of trade.

Africa was not in a position to make similar dramatic changes in its balance of payments. In 1984, nearly half its overall fiscal deficit was being externally financed - over 3 percent of GDP. First, it was a net food importer; for example, in a recent year, Nigeria imported food to the value of US$ 2,000 million. Second, there was slow growth in world demand for primary products.

Although a reverse in the balance of payments was virtually unachievable, retrenchment became necessary in nearly every African country. At least seventeen countries devalued their currencies. Everywhere, budget deficits were curtailed by severe cuts affecting growth in public expenditure. New public investments and subsidy payments were sharply reduced. At least seven countries raised interest rates. Many governments introduced new taxes, particularly on imports and travel.

Poverty and Health Consequences

Growing unemployment has led to increased poverty in a number of developed countries. Hardships are particularly severe in some of the recently industrialized developing countries, which have not yet created elaborate social security and social welfare systems and in which it is common to find families with only one breadwinner. Unemployment causes a sense of alienation, despair and apathy in the young and psychological and physical stress in older people, leading, for example, to increases in alcoholism and violence. Evidence is accumulating of the different ways in which unemployment can damage health. The relation is complex and involves multiple causes.

Austerity policies adopted by governments in Africa and Latin America and by some governments in Asia have increased recorded unemployment. However, in developing countries, a much smaller proportion of those in the labor force depend for their income on full-time employment in a single job in the official sector. A large proportion of people may depend on a single income. Between 1980 and 1984, estimated urban unemployment more than doubled in both Uruguay and Venezuela. No country in Latin America or the Caribbean has unemployment insurance such as that available in more developed countries. Moreover, the unemployed lose the right to use health services financed by social security and thus add to the demands on the overstrained government health services. Estimates that at least 20 percent of young people are unemployed have been reported for Colombia, Ghana, Kenya, Mexico, Nigeria, Sierra Leone, Tanzania and Zaire in recent years.

Africa

Poverty increased sharply in rural Africa, particularly as a result of the deterioration in terms of trade. The proportion of the rural population living in absolute poverty is estimated to have increased from 82 percent in 19741o91 percent in 1982. It must have increased still further by 1984. Some 150 million people suffer from food shortages and, in some cases, famine. Both the calorie supply and the supply of protein have been falling. The position of the poor was made still worse in at least seven countries by the reduction of consumer subsidies.

It was estimated after the 1984 rainy season that the number of African countries likely to face food emergencies in 1985 was about twenty-one, of which thirteen belong to the category "least developed." While the principal health consequences of drought are malnutrition and the infections it fosters, the situation has been further complicated by epidemics of cholera and acute diarrhea] diseases. The concentration of populations around a few water points and on the edges of towns is conducive to the outbreak of epidemics and the spread of communicable diseases. Certain countries in Africa have in addition suffered outbreaks of yellow fever and cerebrospinal meningitis. Massive displacements of refugees have exacerbated the situation.

The major contributory cause of death of children in the countries affected by drought are protein-energy malnutrition (PEW, low birth weight (LBW), malaria, diarrhea, infectious diseases, respiratory infections and neonatal infections, notably tetanus. The most prevalent diseases among the drought-affected population are those of the eyes, upper respiratory tract and gastrointestinal tract, diarrhea] diseases being highly prevalent among children. In the Sahelian region, which has only one crop per year, more than 70 percent of food intake comes from cereals, mainly sorghum and pearl millet. The average Sahelian diet thus does not satisfy individual energy and protein requirements, particularly for mothers and preschool children. In 1983, the high rate of PEM in the Sahehan region affected 20 to 30 percent of preschool children and led to peak child morbidity and mortality rates in the preharvest period. Estimates are that 40 percent of preschool children and 60 percent of pregnant women suffer from serious marasmus and nutritional anemia. These deficiencies, poor environmental hygiene and lack of potable water all contribute to a high incidence of infectious diseases and high morbidity and mortality rates.

According to UNICEF, "at least five million are estimated to have died from hunger, malnutrition and related causes during 1984 - about a quarter more than would have died under `normal' circumstances - and millions more have suffered physical and mental disability due to prolonged malnutrition." In six of Mozambique's nine provinces, the infant mortality rate exceeded 200 per 1000 live births and probably exceeded 250 per 1,000 in the three worstaffected provinces. When conditions were at their worst, between December 1983 and March 1984, it is estimated that four out of every ten children below the age of five perished. In the Sudan, 20,000 more children died every month in mid-1985 compared with earlier years. In both Burkina Faso and Chad, infant mortality has risen to above 210 per 1,000. One out of every three Angolan children under the age of five is said to have died during the food scarcity. In Ghana, the infant mortality rate, which had been declining to around 100 per 1,000, now appears to have increased to about 120 to 130 per 1,000, with a rate as high as 250 per 1,000 in some northern and upper regions of the country.

The Americas

The concentration on production for export, the increase in the cost of imports, inflation, high housing costs, high levels of unemployment and underemployment, and the suspension of food subsidies have substantially increased poverty in the region of the Americas. The last element is of particular importance for health, insofar as it leads to increased malnutrition in pregnant women with the risk of higher infant mortality. In the 1970s, about 40 percent of Latin American families were poor, in the sense that their food did not meet basic requirements. It is mainly a rural problem - 62 percent of rural families are affected, as against 26 percent of urban families. Poverty indicators have risen in both absolute and relative terms. Surveys in six Latin American countries have indicated that income differences are widening. Comparison of infant mortality rates in Bolivia in 1973 and 1983 shows a dramatic increase in deaths due to diarrhea) disease and a sharp rise in the proportion of all infant deaths related to malnutrition.

Southeast Asia, the Eastern Mediterranean and the Western Pacific

In the Eastern Mediterranean, it is estimated that half the population lives in poverty. Despite the high growth rate for Asia as a whole, the recession dealt particularly harsh blows to the struggling economies of this area's least-developed countries. In a few cases, low per capita income suffered further decline.

Poverty is increasing in Southeast Asia. In the three largest countries, 400 million people are estimated to be living in absolute poverty - the greatest number in any region. In the

Western Pacific region, the growth of poverty has been greater in the rural than in the urban areas. The potential labor force continues to increase faster than the capacity of the economies to provide employment.

In general, it can be said that in each region, the recession has had its main impact on those least able to bear it - simply because they have neither the political power to prevent it nor the economic ease to absorb it. Children have almost certainly suffered most of all in terms of low birth weight, malnutrition, frequency of illness, and poor mental and physical growth.

National Resources for Health

The austerity policies adopted by many developing countries in response to the severe economic recession and unfavorable terms of trade - when revenue depends heavily on taxes levied on exports - have often included reductions in public expenditure. Such reductions have often been required as a condition for obtaining short-term loans during periods of "adjustment" or "realignment." Not only has total expenditure often been reduced, but allowance has had to be made for the higher cost of debt servicing at increased rates of interest. In addition, a number of developing countries have been spending more on defense: the total number of persons in the armed forces of developing countries rose steadily between 1919 and 1981. For all these reasons, public expenditure in the health sector has been reduced in quite a number of developing countries, particularly in Africa. Moreover, the higher cost of imports due to poor terms of trade has often reduced the real value of appropriations for the health sector.

In view of the failing living standards in the African region as a whole and the difficulty of increasing taxation as a percentage of GDP in view of the weak demand for exports, per capita public expenditure on health has been falling in real terms in the majority of African countries. Nutrition, water, sanitation and preventive programs have suffered. Lack of equipment and supplies has been paralyzing services. Health personnel have suffered a loss of purchasing power, which has led to low morale, poor attendance and a general loss of effectiveness and efficiency. Increases in health budgets have been overtaken by the rise in the cost of materials and commodities. Financial resources and manpower have had to be reallocated to meet the emergency health needs of millions of people in the areas affected by drought. The economic crisis and the drought have limited the resources of governments and thus reduced the collective effort for health. The same factors have left too little foreign exchange to pay for imported building materials, laundry and medical equipment for hospitals, and facilities for transport. There are insufficient resources to cover the recurrent costs of activities required to achieve health for all. There are chronic shortages of essential drugs, and water supply systems break down because of shortages of spare parts and fuel.

In general, the shortage of funds to pay for imported drugs-and equipment has seriously disrupted services in many African countries. In the words of the Chairman of the OECD Development Assistance Committee, fiscal retrenchment and inflation have led to "the disintegration of rural health cervices."'

Statistical reports to international agencies on expenditure are less likely to be made by the poorest countries. While Africa and the Americas were the worst affected by recession, cuts in health service spending have also been made in some countries in Asia. For example, there was no growth in the health budget for Indonesia for two successive years, despite the growth of the population.

External Cooperation

Have the developed countries and multinational agencies made more development assistance available for the health sector in view of the effects of the economic recession? The OECD countries have faced their own problems of public expenditure - in particular, the need to accommodate the high cost of supporting large numbers of unemployed. Nevertheless, total OECD development assistance has been increasing. On the other hand, the lower price of oil in recent years has led to a reduction in development assistance from OPEC countries. Official development assistance for all purposes reached its peak in 1980, fell in 1981, and then remained at the same real level up to 1984. The available evidence suggests that there was little change in the real level of development assistance for the health sector over the period 1980 to 1983. About 4 percent of bilateral assistance from the

OECD countries is devoted to the health sector. The share of such assistance going to health, social infrastructure and welfare changed little between 1975-76 and 1982-83. However, there was a 13 percent decline in aid specifically directed to health between 1983 and 1984 in current prices.

Assistance, whether in the form of grants or loans, is more readily provided for capital expenditure than for current costs. Occasionally, recurrent costs are funded, but usually only for the duration of a specific project. Thus, countries receiving assistance are later faced with the problem of finding from their own resources the running costs arising out of development. This has become a critical problem in a period in which budgets have often been suddenly reduced owing to changes in the world economic situation.

Prospects for the Future

It is well known that economic growth does not necessarily help the poorest section of the population, whose health is most at risk. But it does increase the capacity of governments to promote socioeconomic development deliberately aimed at the poorest, including development of the health sector, and to do so with the full participation of the target communities.

Economic decline reduces the capacity of governments to make this response. It adds to the number of the poor. It makes the poor still poorer when employment in the informal sector has to be shared out among more people, when terms of trade turn against agricultural producers, when the prices of staple foods rise disproportionately because land is used to produce for the export market. Sharp and sudden economic decline has been the fate of Latin America during the recession. If the annual decline in living standards in Africa has been less sharp, it is the more serious, as it is part of a longer-term trend - at least for sub-Saharan Africa. Moreover, Africa is a region where least-developed countries are heavily concentrated, where food has to be imported even in years with normal rainfall, and where drought has coincided with poor terms of trade as a result of the recession. Stalled economic growth and economic decline place the health of the most vulnerable at gave risk.

The effects of the world recession on health are poorly docu mented. Hard evidence is very limited. The full effects of more and greater poverty on morbidity and mortality can only be inferred, and they cannot be distinguished from the consequences of protracted droughts in large parts of Africa. But the evidence is accumulating via statistics on malnutrition and rising infant mortality.

Despite the pressures on national budgets, particularly the cost of debt servicing, certain countries in all regions of the world have managed to allocate a higher proportion of public expenditure to health and health services. They have striven to maintain or even expand their social programs despite formidable difficulties. But these are the exceptions. Central governments in a number of developing countries have sharply cut expenditure per head. In Africa, import restrictions are hampering health delivery in a number of countries. The effects have probably been most serious for the rural and urban poor, who cannot afford to buy from the private sector what public services are no longer able to provide. For all these reasons, the effects of the economic crisis have been most serious for the poorest, and those whose health is most vulnerable. In countries most seriously affected, progress toward health for all has already been halted or reversed.

The economic situation in Latin America is at last improving, though progress is uneven. One effect of the economic crisis has been to reduce funding for public hospitals, thereby making it possible to put extra funds into primary health care. In many countries, substantial progress could be made by improving the efficiency with which current health resources are used and by rationalizing or improving the coordination of services. The challenge is to ensure that resources are used so as to give priority to the less favored and to the major health problems which face each country.

The basic economic problems of Africa are more deep-rooted. Many African countries are still faced, if not with drought, then at least with the consequences of past droughts, such as the resettlement of populations. Clean and sufficient water supplies are of major importance for the prevention of disease and the maintenance of basic sanitary conditions.

Drought now appears to be a quasi-permanent feature of the African continent. It is clear that Africa will need substantial help from the international community for many years to come. This reinforces the need for each country to establish its priorities for the health sector, as for other sectors, after the serious setback of the past years. The aim, as in other regions, is to concentrate efforts where they will be most effective in promoting equity in health. Strengthening the health sector of the developing countries contributes to their economic development.

Notes

I. UNICEF, Within Human Reach (1985),pp. 10.11.
2. Organization for Economic Cooperation end rvelopment, Development Cooperation Renew (Paris, 1984), p. 39.

CHAPTER I5

The Role of NGOs in Adjustment

John Clark

The Increased Role of NGOs

Non Gove mental agencies have an increasingly important but increasingly complex role to play. Until recently seen as a character part on the world stage - well

loved, but not taken too seriously - the *NGO* community has now achieved an increased prominence. This change has come about for at least three reasons.

Climate of Poverty

The famine in Africa in recent years made clear not only that a relief effort was necessary, but also that traditional approaches to development were not adequate to arrest the growing gap between rich and poor.

The polarization of wealth has led to a world in which an increasing number of people live precariously balanced on the edge of hunger. *No* one is comfortable with this.

Calculations from the *World Development Report* 1986 show that the poorest thirty-six countries with 51 percent of the world's population account forjust 5 percent of the world's *GNP.* In contrast, the seven leading industrialized countries command 58 percent of *GNP* with just 13 percent of the world's population. There is, of course, a similar inequality within developing countries themselves. In Kenya, for example, the poorest 40 percent of the population received only 10 percent of total income (1976).

Statistics such as this may be familiar ones, but it is perhaps important for all in the development field to remember them from time to time so as to recall what the motivation for development should be. Hunger and famine are as much the symptoms of the maldistribution of the world's resources as of drought and war. Official

Most of this paper is drawn from a book to be published by Oxfam later this year.

aid agencies recognize this. Many also recognize that, with resources that look increasingly slender on the scale of international economics, to make a dent on poverty requires a more skillfully targeted approach than has been the case in the past.

In the words of the World Bank (Poverty and Hunger, 1986) this might mean "shifting *resources from large farms to small farms, from export crops to food crops, from industry to agriculture and from capital intensive to labor intensive activities." The U.K. Aid Minister, similarly, has talked of the need "to look much more closely at what can be done to revitalize peasant agriculture." But experience shows that to reach the poor effectively involves working closely with the poor. This is often difficult for official aid agencies to achieve, whereas many NGOs have a good track record in this respect.*

NGOs therefore have become an important conduit for official development assistance; and, where local governments are supportive of such efforts, NGOs are becoming increasingly important partners in designing and implementing poverty-focused schemes.

Size

NGOs are on a rapid growth curve. By 1984, NGO aid amounted to $3.6 billion, of which $1.3 billion was contributed from official aid sources and $2.3 billion from public support.

The voluntary component was about the same size as net IDA disbursements in 1983, and total NGO grants accounted for about an eighth of alt OECD aid in 1984. It is small, but it is not insignificant.

It should also be remembered that NGO aid is virtually all on grant terms, and that the figures do not include the value of services provided by volunteers. Moreover, the distribution of NGO aid is much more heavily weighted to the poorest countries than is the case with official development assistance. NGO aid constitutes a considerable proportion of development investment in countries such as Burkina Faso.

Public Opinion

In western countries, the public view of world poverty has changed dramatically. It is no longer a concern only of the middle-aged and middle-class. Today a much wider spectrum of society is demonstrating its anxiety to help fight poverty. The foundation for concern is the traditional motivation of pity for the starving, but reinforced now by the emotion of anger - anger that our world's leaders are not using the power at their fingertips to abolish hunger forever.

Politicians are responding to this new public mood. Not in decades have there been so many debates in Westminster on Third World issues, nor such cross-party concern about the aid record of western governments.

The British government has responded by stepping up famine relief aid and aid for post-famine reconstruction in Ethiopia and elsewhere. On the whole, the response - paying Paul - has been made possible by robbing Peter. Virtually no new aid funds have been allocated by the British government, in spite of the wave of public compassion. Aid to the Indian subcontinent has taken a nosedive to accommodate the new high levels of U.K. aid to Africa; famine relief has been at the expense of long-tern development in the government's aid program.

An Analysis of NGOs

NGOs are alive to the need to adjust their programs to take into account the economic forces that fuel poverty. This may involve close contact not just with other nongovernmental organizations, but also with official aid agencies, and sometimes government departments, in a new collaborative approach to development. At least *they* must learn to understand what those official institutions are doing and the effect of these actions on the poor. Macro and micro ways of working must meet.

Aware of the sea of changes that surrounds them, voluntary organizations like Oxfam are also searching for new *ways* of working. How can they be content with working in a few scattered communities, helping create a few islands of prosperity, when all around them conditions of poverty are getting worse and worse? They may be powerless to do anything that stops the slide directly, but they are realizing that they cannot ignore it.

It is easier to acknowledge the need for change than to determine what direction the new departure should take. Some people within NGOs argue for a much fuller partinership with the official agencies - that this opportunity is being offered at present and should be seized. Others doubt this. They say that a meaningful partnership would not be possible, because the two parties have such totally different definitions of what "development" means: two people can only share a taxi if they are going in the same direction. If the kinds of projects that official development assistance supports are not consistent with the NGOs' perception of the interests of the poorest 40 percent, then the two parties must agree to differ.

Resolution of these differences is not made easier by a distortion of the situation by official aid donors. It has become fashionable among the official agencies to blame the policies of African governments for the woeful record of African development in the last twenty years. NGOs share in making criticisms of past mistakes, but these are only a small part of the truth. Dumping on African governments all the blame for the sorry record of the past is as cheap and easy as it is unhistorical and irresponsible.

NGOs on the whole believe it is the policies of western governments that have predisposed African governments to make many of the mistakes for which they are now condemned (such as debt management, domestic agricultural policies, protectionistt trade policies, commercialization of aid).

Besides the distortion, NGOs believe there is a policy manipulation practiced by western governments and their financial institutions and aid agencies. In the name of "efficiency" and "good housekeeping," the policy prescriptions are always pro-private enterprise, liberalizing markets and anti-parastatals, whatever the local context.

Oxfam - itself a private agency with no love for government bureaucracies - believes that in some African countries there are no immediate alternatives to parastatals, nor are there particular reasons to search for them. In a country such as Zimbabwe, the basic food distribution parastatals do get the food marketed and distributed, and do so relatively efficiently. To seek to replace this system with the "free market" would be ideologically, not practically, motivated.

In Zambia, where the parastatals have been disenfranchised, private enterprise is serving many farmers - perhaps the majority - very well; but Oxfam is already concerned that the entrepreneurs are offering much lower prices to farmers in the remoter areas, or are not even prepared to buy there.

In short, the question that NGOs are trying to grapple with is: Do they believe in the official agencies' objectives of structural adjustment, or will they be satisfied with nothing less than structural change?

The analysis described here is necessarily superficial. But it summarizes the thinking and concerns not just of many northern NGOs, but also of the major African NGOs, as expressed in their submission to the U.N. Special Session on Africa.

Oxfam Field Experience

The following are some examples of the evidence gained from its field work which gives

Oxfam its perspective on recession, adjustment and how these are felt by the poor. Such evidence tends to be anecdotal. Oxfam works at present in about 3,000 communities (a tiny fraction of the Third World), and it is from these communities that the evidence is drawn. This evidence, however, concerns the lives of "real people" - all too often a missing component in macro economic analysis. The examples below attempt to put a human face on the adjustment processes at work today and to show how an NGO such as Oxfam has had to change its approach in the light of external economic factors. The micro and macro worlds have met, and NGOs are increasingly pitting their "micro solutions" against "macro problems."

Bolivia

Since the collapse of the International Tin Council in October 1985 and the economic difficulties this has caused Bolivia (40 percent of whose exports derive from tin), Oxfam has been working with poor families in the mining communities. Oxfam has witnessed a sharp increase in malnutrition in this period and has recently made a considerable grant to a group of mining families to help them set up a food-buying cooperative - buying in bulk so as to get basic food at cheaper prices.

Ecuador

The major export crop has been bananas, but now Ecuador is trying to diversify into palm oil. Forty thousand hectares of oil palm have now been planted (77,000 tons per year output). The plan is to increase this area tenfold. The project is funded by British aid via the Commonwealth Development Corporation and by other aid agencies.

Oxfam's staff in Ecuador are concerned about the social and environmental costs. Ten thousand indigenous Indians have already been displaced or seriously affected, and Oxfam is working closely with those people and with the groups who support them. In addition are the environmental costs (destruction of forests and environmental pollution resulting from the wastes of palm oil processing). Oxfam is also doubtful about the economic wisdom of the scheme. There is a trend toward a world glut in vegetable oils (Malaysia already has a "lake" of palm oil it cannot sell); prices have already fallen sharply (50 percent from April to October 1985); and the EEC is poised to promote expanded oil production within Europe. Ecuador could destroy its forests and indigenous cultures to produce a product that no one wants.

Dominican Republic

Oxfam is helping poor coffee growers to get more for the crops they grow. As the economic situation has worsened, the power and monopoly of the middlemen have increased. Oxfam has funded a network of producer groups to help them break into direct exporting, thereby earning considerably more. (Note: in Uganda, until about a year ago, producers received only 1 9 percent of the export price of coffee.)

Brazil

a) In the Ilheus region of northeast Brazil, a former Oxfam country representative has described the clearing of peasants from land which has been taken over (by powerful landowners and ranchers) for cocoa production. This process has been gradual and steady over many *years.* In the state of Bahia as a whole, the number of cocoa trees has increased by 40 percent in ten years. Oxfam is funding the legal costs of the displaced families in pursuing their cases against encroaching landlords.

b) In the Amazonian region of Acre, Oxfam works with the local people who tap rubber and gather Brazil nuts for their livelihood. They live in ecological harmony with the rain forests. This is changing rapidly now, however, as wealthy ranchers from the south and multinational companies move in. After clearing the forests, there is much profit to be made in beef ranching and selling the meat for export.

The rubber tappets have tried to defend their forests and their traditional way of life, but the juggernaut of progress seems unstoppable. They decided that the only hope was to band together with rubber rappers from other parts of Brazil. Helped by funding from Oxfam, 120 people from different parts of Brazil came together for the first-ever national meeting of rubber rappers in October 1985 in the capital city, Brasilia. For some, the journey was immense. Oxfam's country representative describes how one woman traveled for thirteen days by canoe and then seven days in buses and boats to take part. The meeting was not just a chance to exchange experiences and plans. It also enabled the rubber rappers to meet with government representatives and explain their problems directly. It is too early to tell what the outcome will be.

c) An Oxfam survey in 1983 showed that 40 percent of children in the state of Ceara were malnourished.

Bangladesh

a) Oxfam is working with poor peasants who were encouraged to grow jute in the early 1980s, when prices were reasonable, and who are now finding that they are having to sell their produce at a loss. Oxfam is helping them to diversify their agriculture.

b) In a worsening economic environment, credit becomes harder to obtain and interest rates rise. Traditional moneylenders are frequently charging 10-12 percent interest *per month.* Oxfam is funding many village banks and credit schemes, with a special emphasis on lending to women.

Philippines

Oxfam's work in a number of countries has been influenced by the difficulties of Third World sugar producers. For instance, the collapse of the sugar industry in the island of Negros in the Philippines has brought widespread unemployment and malnutrition.

Oxfam has provided grants to pay for feeding centers for the hungry and to help the unemployed sugar workers to grow rice, maize and vegetables on the uncultivated sugar land.

Zambia

The situation in Zambia clearly demonstrates the heed for organizations like Oxfam to adjust their work in the light of global economic forces.

Zambia's debt stands at $3.8 billion. Payments on its debts are scheduled to consume over 70 percent of its export earnings for the rest of the decade. But its exports are tumbling. The real price of copper fell by 60 percent from 1974 to 1984, and copper traditionally accounts for about 90 percent of Zambia's exports. As a result, Zambia is trying to diversify from copper by rushing into export crop production. Oxfam's country representative describes Zambia as "probably the only country in the world trying to move from an industrial to an agricultural base."

In order to remain solvent, Zambia has had to borrow heavily through the IMF, and in exchange, to implement a sweeping program of "economic reforms" and austerity which, in Oxfam's view, ate bound to result in greater poverty, with a widening of the gap between rich and poor, Spending cuts have put the health service under great strain. The Ministry of Health has been allocated only one-seventh of the budget it needs for importing essential drugs. A consequence of dramatic devaluation of the kwachu has been the doubling of fertilizer and fuel prices, and the price of maize meal has gone up 80 percent in two months, hitting the urban poor in particular.

In such situations, the importance of Oxfam's work is to seed new ideas and new ways of working that are being pioneered by the poor themselves. On the scale of need, the resources of voluntary agencies are a drop in the ocean. But, well targeted, that drop could have a major impact. Government *services* are obliged to adjust rapidly to much-reduced budgets. They can learn from the example of community groups how to stretch their slender resources a long, long way. It is hoped that the health projects supported by Oxfam in Zambia will inject into the official service methods for providing effective but cheap primary health care to poor people. It is hoped that the community mobilization work Oxfam supports will catalyze a new approach to the organization of local government. It is hoped that the work with groups of poor peasants in vulnerable areas will encourage local agricultural officers to evolve a pattern of agriculture more suitable for the poor.

Jamaica

Although a small country, Jamaica's debts (around $3.2 billion) are enormous - considerably more per person than the debt of either Brazil or Mexico. An Oxfam report published in 1985 described how 40 percent of Jamaica's export earnings are spent servicing the debt, and how, as a result of five IMF negotiations since 1977, the government has introduced a series of austerity measures which hurt the poor.

The economic deterioration and escalating unemployment (up to 30 percent in 1984) has been fuelled by the collapse in the market for bauxite, Jamaica's principal export. Price controls and subsidies have been removed, wage restraint has been introduced, and there have been savage cuts in public spending, particularly hitting the health and education services. Basic food prices rose 61 percent in 1984, while a third of the labor force now earns less than £5 per week. There has been a sharp increase in both rural and urban malnutrition, with 28 percent of under-four year olds now malnourished.

The cuts have led the government to turn some of the agriculture, marketing and even health services over to the private sector. Several health care projects have been referred to Oxfam. In one poor suburb of the capital, Kingston, Oxfam was asked to help fund a primary health care center. The number of health workers had been reduced from 200 to 25, and health care was suffering as a result. In one area, the incidence of anemia in pregnant women had increased from 23 percent in 1981 to 42 percent in 1983.

Development Education

Many NGOs have also made major adjustments in the style of work in their home country. They have become alive to the need to describe their experiences and achievements not in isolation, but in the context of the international economic and political environment in which they work. NGOs are not normally inhibited - nor modest - in describing their achievements. Now they are learning to "tell it like it is," that is, to contrast their success stories (important as they are for the millions of people helped each year by NGOs) with the downward slide toward greater poverty that is the fate of hundreds of millions of nennle in the Third World today.

In Britain, Oxfam, alongside the World Development Movement and other NGOs, aims in its publicity work to show the public how the problem of western recession is filtering down, being magnified and being borne by the very poorest people on earth. Besides Live Aid and Sports Aid, which had an immense public impact but which were largely fund-raising in nature, 1984.86 has seen an immense increase in campaigning activity on development issues. The major event was a mass lobby of Parliament at which 20,000 people - an all-time record in Britain - met with their Members of Parliament in a single day, Foreign Secretary Sir Geoffrey Howe recognized that the lobby "demonstrated the high degree of public concern in this area" and that Britain has experienced "an unprecedented increase in the level of public and parliamentary interest" in aid and development issues.

This upturn in public interest appears to have been more significant in the U.K. than elsewhere, perhaps because of fuller media coverage (especially TV.) of the famine in Africa; perhaps because Live Aid, Band Aid and Sports Aid were "home grown"; and perhaps because British NGOs were better prepared for a popular campaign on the causes of hunger and famine than in other countries,

Hundreds of thousands of people have taken part in marches or vigils, written to M.P.'s, supported petitions, taken part in symbolic fasts, or joined in one of the myriad activities around Britain under the slogan "We're Hungry for Change." The unprecedented frequency of parliamentary debate on aid and development has reflected this mood, and the government has felt obliged to respond to the pressure with some policy shifts.

Individually, these shifts are not startling. Taken together, they amount to a significant, though still insufficient, change of *govern*ment emphasis. The British government took a lead in orchestrating a sizeable EEC emergency *food* aid plan in December 1984. It eventually agreed to restart development aid to Ethiopia along the lines of an Oxfam proposal (£3 million was contributed to famine rehabilitation aid). The overall aid budget was increased slightly (£l7 million) after six years of cuts. *More* aid has been committed for "peasant agriculture" and *for* research into crops suitable for drought-prone areas. The Aid Ministry has forged an arrangement with India, reserving a proportion of U.K. aid for poverty-focused projects. And the British Aid Minister has launched a bid to reform EEC food aid. These are some of the major shifts in aid policy that have followed public lobbying. On non-aid issues, there is less news. The government has now announced a lifting of import quotas on shirts from Bangladesh following a campaign organized by the World Development Movement and has given some support to efforts to curb the marketing of pharmaceuticals.

NGOs are more committed than ever to development education and campaigning. They see this activity - in their home country - as an objective equal in importance to direct development work overseas. Oxfam, for example, allocates 6 percent of its general income (i.e., all income other than that donated for special appeals) to its Education and Campaign Program.

This shift toward speaking out about the international root causes of famine has been strongly welcomed by southern NGOs. For example, the African NGOs' presentation to the U.N. Special Session on Africa welcomed the campaigning of northern NGOs on issues such as debt and trade and called for more of this. Their message was that the best thing that northern NGOs could do to help Africa's poor would be to get the North off Africa's back.

Northern NGOs are pleased to receive such encouragement but are sanguine about the difficulties. To some extent, aid is a "soft issue." If you push it, it moves (though not necessarily very far). Issues such as the debt crisis and terms of trade are the opposite. Being so inextricably bound up in international economic systems, they are extremely "hard." Lobbying efforts are likely to be rewarded with little change. Furthermore, the issues involved are so much more complex and apparently impersonal than aid.

For NGOs, it is tempting to stick to the issues - such as aid and baby milk - in which they know they can campaign effectively. But to ignore the bigger issues of adjustment (the need for adjustment in the economies of North as well as South) is to admit defeat. Aid alone is bound to fail, given its small part in overall resource transfers. The elimination of absolute poverty necessitates, first, the elimination of the international economic pressures which create national poverty. Once that is realized, NGOs have no choice - though they may have considerable trepidation - in mounting public campaigns on the broad theme of putting a human face to adjustment. In the words of one NGO, they must "be realistic and demand the impossible."

PART IV
COUNTRY EXPERIENCES

CHAPTER 16

Social Progress and Adjustment in Mexico

David Ibana

It is now commonplace to assert that Mexico's economic crisis is the most profound, protracted and generalized since World War II. The crisis is far from being over. Thus, it is dangerous to assume that financial imbalances are vanishing. By and large, both the government and the country are in 1986 in a weaker position to deal with national economic problems than they were in 1982.

Product per capita decreased by over 10 percent between 1981 and 1985. Its level today is similar to that attained eight or nine years ago. National income is even more depressed (12 percent), to judge from the deterioration in the terms of trade (16.5 percent) and the increase in external debt servicing. There are social groups within the country that might have lost between one-fourth and two-fifths of their former income.

In terms of internal discipline, the effort to adjust to a harsh external environment has been enormous. In order to fight inflation and service the debt, growth, private consumption, government spending and imports have been drastically cut. A case iq point: the current account deficit in the balance of payments reached $14.1 billion in 1981, $3.7 billion surplus in 1984, and was in equilibrium in 1985; likewise, the trade balance shifted from a $4.6 billion deficit to a $14 billion and $9 billion surplus in 1984 and 1985 respectively. However, such remarkable results were due not to an increase in exports - which fell by 4 percent, in spite of a 45 percent rise in volume - but to a sharp, recessive decline in imports (44 percent), that is, to a large extent, in purchases needed to supply strategic inputs or to sustain capital formation.

By the same token, net flows of foreign savings (i.e., net credits plus net external investment minus interest and profit payments) reversed their sign: instead o£ making a positive contribution of some $13.8 billion to internal investment, as in 1981, they represented an outfowin excess of $9 billion in 1985.' Therefore, it is not surprising to observe a decline of more than 7 points in the investment cu efficient (from 1980 to 1985) and, as a consequence, a lower capacity to attain growth or to undertake essential structural changes (for instance, the transformation of the traditional export sector).

During the same period (1981-85), Mexico's external debt rose from $74.9 to $97.8 billion,' not so much because of fresh inflows of resources, but rather as a result of capitalized interests agreed upon de facto in the renegotiation process. The debt service in 1985 is equivalent to 47 percent of total exports of goods and services and represents the main source of fiscal deficits.

Despite the easing of world inflationary pressures and the implementation of the IMPS restrictive adjustment policies, far from receding, inflation seems to be gathering strength as time goes by. Between 1979 and 1981, inflation rose at an annual average rate of 26 percent, but in 1983, it climbed to 99 percent, decreasing to 59 percent in 1984 only to climb again in 1985 and reaching an annual equivalent of 100 percent during the first six months of 1986. Cost_ push pressures and widespread social dissatisfaction regarding the distributional effects of the adjustment process are changing inflation into a phenomeflolt that cannot simply be corrected by demand management. Moreover, the sharp decline in oil prices during 1986 has nullified the efforts made thus far, making new sacrifices unavoid able.

Economic Costs of Adjustment

The assumption that the debt crisis is grounded in past policy mistakes on the part of either borrowing governments or lenders is perhaps too simplistic and misses the true nature of the problem. Underlying structural changes in the world economy are behind the new economic cleavages opened between North and South - changes that also explain the diminished capacity of the industrial centers to foster growth in the developing world through financial assistance or, better yet, through liberal access to their commodity markets.'

Thus, it is worthwhile to emphasize some important functional links among finance, trade and growth. Without net capital inflows, when the rate of expansion of a given economy is below the rate of interest, the external debt service can be satisfied only by decreasing domestic consumption. On the other hand, under the same assumption, when the growth rate of export earnings is lower than the rate of interest, the capacity to service the debt can only be strengthened by diminishing purchases abroad.[4] Therefore, when both consumption (12 percent) and imports (44 percent) have been drastically reduced for half a decade in the midst of still high demographic pressures, it is only natural to encounter mounting frustrations and resistance to further adjustment measures.

Historically, governments overwhelmed by short-term economic dislocations are rarely able to take the necessary steps to transform the economy and society in the proper direction. One explanation for this is the fading political legitimacy associated with contracting income and employment levels for extended periods.

The recent Latin American experience clearly demonstrates that there are strong asymmetries associated with the distribution of adjustment costs. Not only does the type of adjustment sponsored by the international financial institutions have a built-in bias, but acute disparities in political power among the different social strata are also present. In addition, from a pragmatic standpoint, governments are inclined to cut wages rather than profits in the belief that the latter will play a key role in any future attempt to revive economic growth.

Although these trends are descriptive of the Mexican case, there are important singularities that should be spelled out. First, labor is organized into a national federation of unions (one of the three sectoral constituencies within the main political party, PRI) that has traditionally cooperated with the government in exchange for either economic gains or power and open participation in the domestic political interplay.

Given the encompassing organizational nature - in the Olson' sense - of the union's federation (CTM) and its mediating role vis-a-vis the state, it is logical to expect labor to prefer salary cuts to increased unemployment as its contribution to the adjustment process decided upon by the national authorities.`

Second, the previous Mexican administration took drastic steps in 1982, enacting exchange controls and nationalizing the private commercial banks, thus breaking away from the traditional liberal financial policy followed by the Mexican government.' Even if these measures were technically sound, they had side effects that generated new social cleavages between business and government. The history of economic policy after 1982 is to a large degree an ... account of governmental efforts to fully restore business confidence while taking steps to accommodate the economy to rather unfavorable circumstances.

Third, the conservative economic paradigm prevailing both abroad and at home had the effect of intensifying in depth and shortening in time the macroeconomic adjustment on demand. Banks and foreign governments up to now have refused to accept a share of the debt burden, and the Mexican authorities, for their part, have been in no position or have been unwilling to take a strong international stand on the debt issue. Therefore, the brunt of adjustment has been borne domestically, mostly by breaking the social compact that used to protect the wage earners' and employees' shares in the national income.

Fourth, the Mexican record demonstrates the prevalence o. a pronounced temporal asymmetry between adjustment on the aggregate demand and adjustment on the supply side. Accommodating public and private expenditure to external payments restrictions, while not easy, is proving to be a task that could be accomplished fairly rapidly. Unfortunately, the crux of the debt quandary lies elsewhere. To find appropriate solutions, Mexico needs to modernize its productive and export activities, as well as to democratize the design and implementation of its economic policy. However, such an endeavor will require time, significant switching in the allocation of resources, political reform and a favorable world environment. Unfortunately, these preconditions are well beyond the scope of short-term demand management policies

Because of the above-mentioned factors, it is our contention that declining growth is determining unprecedented regressive shifts in income distribution patterns through which, once again, the human ingredient in development is undermined. The logic of restoring business confidence as *a key* component in beginning a fresh process of capital formation led to the attempt to protect profits and laid the costs of adjustment primarily on the workers and the public sector.

In practice, however, private firms are subject to an uneven process of profit squeeze. Restrictive monetary policies and the priority given to the financing of public sector deficits are crowding out business demands for loan able funds from the banking system. By the same token, the sharp decline in wages and salaries is reducing the level and changing the composition of aggregate demand. The consequences are higher coefficients of excess capacity and the misalignment of supply and demand structures, all of which reinforce inflationary cost pressures and produce downward spirals in economic activity. The detrimental effects are not spread evenly; rather, they are concentrated on small and medium-sized enterprises and on firms closely linked to capital formation (construction and capital goods industries) - that is to say, on activities with the highest employment potential or the highest capacity to sustain autonomous growth in the long term.

Summing up, after five years of adjustment efforts and significant losses in human welfare, the Mexican economy is far from the path of growth and stability. For the first time in almost half a century of steady progress, there is neither economic growth nor social advancement, while the endurance of the political system is increasingly taxed.

Social Indicators

From the I940s to the end of the 1970s, Mexico attained high rates of sustained growth (gross domestic product increased eleven fold in real terms). The pace of industrialization was also impressive (8-9 percent per year), as was that of urbanization (by 1980, urban dwellers accounted for more than 53 percent of the population, compared to 35 percent in 1940). As a result, national institutions and basic economic structures underwent dramatic transformations. By and large, social progress raised the population's standard of living and, in spite of serious shortcomings still prevalent, there was wide-spread confidence in the possibility of narrowing the poverty gap.

From 1950 to 1980, illiteracy fell from 44 to 17 percent. As indicated in tables 1 and 2, total school enrollment rose at an annual rate of 6 percent, and that of intermediate and university education reached an impressive growth rate of more than 12 percent a year. Likewise, health programs and facilities were greatly expanded. Membership in the different social security systems increased from 1 to almost 31 million persons between 1950 and 1980. During the same period, infant mortality went down 60 percent while between 1940 and 1980, life expectancy at birth rose from 41 to 65 years (tables 3 and 4).

TABLE 1
Educational Enrollment
(Thousands of Students Enrolled)

	Total	Primary	Intermediate	University
1950	3,051.9	2,867.3	106.9	29.8
1980	20,973.3	14,666.3	4,299.6	937.9
1985	22,400.1	15,1 24.2	*6,076.7*	1,199.2
Rate of growth				
1950-80	6.6	6.0	13.1	12.2
1980.85	1.3	0.6	7.2	5.0

SOURCE: Institute Nacional de EssadIstiq Geogafia a Informatica, *Esradisticus historicas de* Mexico (Mexico, 1985), and for 1985, Seeretaria de Education Publics, Sub. secewu de Planeacion Edu®tiva, INr'ecdon General de Progamacion.

TABLE 2
Social Security System

Thousands of Bedsv | Millions of Members

1950 - 1.1 1960 4.0 1965 14.8 8.6 1970 40.2 12.2 1880 56.4 30.8 1881 55.0 34.0 1983 52.4 33.8

SOURCE: Institute National de Estadlstica, Geografsa a Informatics, *Estadisticm hts-tnricasdeMexico* (Mexico, 1985).

vindudea social security institutions and public hospitals.

TABLE 3
Infant Mortality

Per Thousand Live Births

1950 96.2 1960 74,2 1969 66.7 1980 38.8 1982 33.0

SOURCE: Imtituto National de Esmdutisa, Geogafia a Informatica, *Esmdisticas his-* toiles, *deMexico* (Mexico, 1985).

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TABLE 4
Life Expectancy at Birth

	Years
1940	41.5
1950	49.7
1960	58.9

1970	61.9
1980	64.9

SOURCE: Inttimto National de Estadutica, Geografia a Infornutiea, Estadlsticas hlstoricas de Mexico (Mexico, 1985).

The structure and level of employment changed significantly. In the three decades prior to 1980, the labor force expanded 2.5 times, while the share of employment in primary activities decreased by half.

Structural change and rapid economic growth used to be the basic formulas used to reconcile rising social demands with a rather uneven income distribution (partially justified. by the need to foster capital accumulation). The estimated Gini coefficient for Mexico is high, fluctuating around 0.5 since the 1950s.° Both private and public investment growth, for their part, have usually been around 7 percent per year, as the record of the past three or four decades indicates.

Fiscal policy has played a key role in the growth process. Public expenditure has been used extensively to subsidize and to create external economies for the benefit of private business activities; by the same token, it has been instrumental in fostering political stability by alieviating income inequalities through the expansion of social services and welfare subsidies.' ° This is the locus of the forces behind the extremely robust growth in public expenditure, which rose from 8 percent to 42 percent of the gross domestic product

between 1950 and 1980 (table 5).

SABLE s
Public Sector: Income and Expenditure

	Income		Expenditure	
	Billions of	Percentage of	Billions of	Percentage of
	Pesos	GDP	Pesos	GDP
1950	8.64	8.6	9.46	8.2
1960	19.46	12.2	20.15	12.6
1970	109.06	24.5	109.26	24.6
1980	2,050.98	47.9	178.00	41.6

SOURCE: BancodeMexico, Informennual.various numbers.

Successful socioeconomic growth patterns take a long time to change. The progressive Mexican model began to falter in the early I970s and has reached a dangerous standstill in the I980s. Most of the key domestic and external economic variables have lost their dynamic ability to foster growth: because of its change in structure, public expenditure is no longer able to play its eailier developmental role; import substitution is at least partially exhausted; traditional export revenues, including oil, are facing depressed markets and prices; inflows of capital from abroad are no longer available; and capital flight and debt servicing *are* depleting domestic savings.

Yet there have been few departures from traditional policy strategies, and none of them are duly consolidated after five years of negative economic growth. So far, the crisis has been weathered simply by placing the cost of adjustment on the shoulders of the weaker social groups. However, to the surprise of many observers, national political institutions have shown a remarkable resilience in shielding the workings of Mexican society from serious disruptions. Admittedly, tensions are mounting as the regressive distributional effects of the adjustment process gather strength, causing a further deterioration in both living standards and the government's legitimacy.

It is difficult to assess how much longer such an evolutionary process can be accommodated politically without causing irretrievable damage to the social fabric. In any case, the human cost o£ the crisis has been high, and the end is still not in sight."

Economic Indicators

Data on the distribution of the burden of the economic crisis are scanty. Nonetheless, the available figures are enough to integrate an aggregate picture of the effects of the adjustment process over the 1981-1984/85 period.

The wage share in gross domestic product is falling at a dramatic pace. In 1981, the workers' share was estimated at 37.4 percent of gross domestic product and only at 27.7 percent, for 1984. Real minimum wages declined by 32 percent from 1981 to 1985. In only two years, the average real salaries paid by the government decreased by 40 percent (see tables 6, 7 and 8).

TABLE 6
Income Distribution
(Percentages)

	1981	1982	198$	1984
Gross domestic product	100.0	100.0	100.0	100.0
Wage income	57.4	55.5	28.8	27.7
Nonwage income	54.5	54.5	60.9	62.4
Indirect taxes minus subddies	8.1	9.9	109	9.9

SOURCE: Institute National de Estadstica, Geografia c Informatics, SIstema *de* Cuentas Naeiona/es, *1980.1982 y 1980-1984*)Mexico, 1985 and 1985).

TABLE 7
Government Salaries

Average Annual	Consumer Price Deflected Salaries
Salary per Person	Index (Thousands of
(Thousand Pesos)	(1981 = 100.0) 1981 Pesos)
1981 202.8 100.0 202.8 1982 904.5 198.8 155.1 1985	419.1 959.4 116.6

SOURCE: Institute National de Estadistica, Geagrafia a Informatics, *Sistema de* Cuentas Nacfonales: Cuentas *de production del* sector publico, 19751983 and Banco de Mexico, *Inform anus?,* various numbers.

TABLE 8 Wage Indicators (Percentages)					
1981	1982	1985	1984	1985	
Real minimum wages	100.0	95.8	75.7	69.0 67.8 (1981 100.0)	
Mean real wage paid	100.0	97.6	71.8	68.5 (1981 = 100.0)	
Real salaries from 100.0	77.5	62.5	65.4 national accounts*		
(1981 = 100.0)					

SOURCE: CEPAL, *Noras pam* el estudio *economico de America farina y e! Car/be. 1985, Mexico* (LC/MEX/L 55) and Institute Natonal de Estadistica Geografia a Informatics, Slsrerm *de Cuentas* Nacfonales de Mexico. *1982-1984.* (Mexico, 1985). * Nominal salaries deflected by the National Consumer *Price* Index.

Defensive strategies implemented by the National Federation of Workers (CTM) - the acceptance of lower real wages as a tradeoff for higher employment, the ability of the informal economy to

absorb displaced wage earners from modem activities in low-productivity jobs, and greater emigration - explain why unemployment figures have been rising rather slowly in spite of the acute economic crisis. However, there are indications that during 1986, the layoff rate of previously employed workers has worsened to a degree that can hardly be offset by the so-called "job absorption flexibility" of informal economic activities.

Open unemployment rates for the main urban centers rose slightly from 1981 to 1983, followed an opposite trend for the next two years and started to climb once more in 1986 (table 9). Unemployment is not distributed evenly throughout all economic activities. Employment in primary production, as well as in community and personal services, increased from 1981 up to 1984, mainly reflecting the slack demand for labor in the modern sector of the Mexican economy rather than genuine job expansion in those activities. In fact, employment in manufactures declined by 12 percent in the 1981-86 period (table 10) and in the construction industry by more than 20 percent during the same years.

Since employment fell less than income and production, productivity is contracting rapidly (21 percent between 1981 and 1984 - see table 11), and it is becoming both a source of cost-push inflation and a hindrance to export efforts.

TABLE 9
Open Unemployment Rates
(Percentages)

	1981	1982	1989	1984	1985	1986'
Mexico City	6.9	4.0	6.9	5.8	4.9	4.9
Guadalajara	5.8	5.0	7.4	6.1	8.4	2.6

Monterrey	4.2	4.9	9.8	7.5	5.8	5.0

SOURCE: [nstituto National de Estadistica, Geografa a Intormatica, *Cuaderno de into maobn oportuno,* various number:

* January.March.

TABLE 10
Employment Index in Manufacturing Activities
(1981 s 100.0)

1981	100.0
1982	97.5
1983	88.2
1984	87.5
1985	89.2
1986	87.9

SOURCE: Institute National de Estadinica, Geogmfia a Informatics, *Cuaderrm de infornm.* don oportuna, various numbers.

a As of January.

TABLE II
Labor Force Productivity
(1981 • 100.0)

	1981	1982	1985	1954
Total	100	94	81	79
Primary sector	100	98	100	100
Industrial sector	100	94	85	85
Services sector	100	98	93	92

NOTE: Productivity is defined as gross value added per worker.

SOURCE: Estimated with data taken from Insdmto National de Estadutica, Geografla e Informatics, *Estadhtkas* hutoriros de Mexico (Mexico, 1985).

The burden of the adjustment process is not due only to depressed real wages and creeping unemployment. A wide array of other factors is also eroding the living standard of most social groups. Since 1981, government expenditure on welfare has consistently declined; indirect taxes and the prices of public services have been revised upwards; inflation connected to some wage goods is well above the consumer price index. Finally, debt servicing and movements in the terms of trade are withdrawing a large proportion of the gross domestic product from internal use.

Government expenditure in social development diminished by 23.5 percent in real terms during the 1981-84 period. In particular, budgetary outlays for educational services declined by 29 percent, for health services by 20 percent andd for social security services by 24 percent (tables 12 and 13).

TABLE 12
Public ExpenditmrStrucure
(Percentage,)

	1975	1984
Total	100,0	100.0
8odaiDevelopment	21.1	18.2
Economic Deveopment	61.3	34.2
Industry	8.6	4.6
A1Nculture	*1.3*	*5.5*
Commerce	7.3	5.2
Energy	25.4	18.8
Communicators	8.4	5.0
Tourism	0.3	0.1
Adndnittntion and defense*	17.6	52.6

SOURCE: Jnfomudegobiemo.vasiou*numbers. *Indudes service of the public debt.

TABLE 13
Social Development Outlays
(Billions of 1970 Pesos)

Social	Total	Education	Health	Security
1981	70,7	23.0	3.5	28.1
1982	73.2	23.8	3.8	27.2
1983	52.6	15.2	2.7	22.1
1984	54.1	16.4	2.8	21.5
Rate, of Growth				
1981-84	-23.5	-28.7	-20.0	-24.2

SO77ECE: Non Imtig, "Economic Crisis and living Standards in Mexico' mimeographed

(E1 Cole io de M^e^xi^c^o, 1986).

Fortunately, up to now, budgetary restrictions have not been fully translated into a quantitative or qualitative deterioration in governmental welfare functions. A cushion has been provided by cost cuts, either through the reduction in real salaries paid to public employees or through measures aimed at increasing efficiency and reducing expenses. At the same time, lower levels of public investment have been accepted to liberate resources to finance current expenditures while keeping budgetary deficits within specified limits. Gross fixed public investment, which used to represent more than 10 percent of gross domestic product, barely reached 6 percent last year and is estimated to be 3 percent at the end of 1986 (table 14). In fact, the margins of economic maneuvering are vanishing. The country is on the verge of damaging both the human and the material capital formation processes, with lasting effects on future growth.

The impact of adjustment on economic equality has followed different paths, most of them of a regressive character. From 1982 to May 1986, the prices of basic food products (tortillas, bread, beans, rice, eggs, meat, milk) rose at rates that easily overshadow those of wages and salaries." In addition, fiscal revenue expansion is derived mostly from higher indirect tax collection or higher prices of public services (energy, water, transportation, etc.), both of which have a greater relative effect on the budgets of low-income social groups.

Indirect tax contribution to total tax revenues increased from 37 percent in 1981 to 54 percent in 1985, in part as a result of a 50 percent increase in the mean *rate* of the Value Added Tax (table 15). At the same time, subsidies for urban transportation and on the consumption of tortillas and bread are in the process of disappearing" after representing public expenditures of more than 200 billion pesos in 1984.

Finally, servicing of the foreign debt, coupled with an unusual drop in the terms of trade (24 percent from 1980 to 1985), *are* entailing huge transfers of resources abroad, further depressing domestic markets and incomes, Table 16 shows that, in the present decade, such financial movements have expanded substantially, from 3 to more than 8 percent of gross domestic product.[19] Incorporating in the same picture the recent collapse of oil prices and the monetary outflows related to debt amortization and to capital flight, it would be fair to assert that resources of no less than 10 to 15 percent of gross domestic product are systematically removed from internal use, greatly impairing growth performance and prospects.

TABLE 16

Income Tmnsfen Abroad (aillioesof 2980 Dollar,)

	1980	1981	1982	1988	1984	1985
Net factor payment	6.209	8.817 1	1.405	8.868	9.118	7.858
Tents of trade effect	0.135	6.000	8.257	8.279		8.355
Total current transfer 16.208	6.209	8.952	17.405	17.125	27.!25	
Total as percentage of CDP	3.3	4.5	8.7	9.0	8.B	8.0

SOURCE: Eatimeuons butd upon ECIAC data.

Conclusions

a) The need for adjustment in the Mexican economy arises from two different sets of contemporary and interrelated problems. On the one hand, there is a cumulative misalignment in national exports with respect to world market trends, greatly amplified by the effects of the debt crisis. On the other hand, the diminished dynamic responses of the import substitution process, as well as the highly expansive policies of the I970s, clearly called for changes in economic policy,

b) Granted the need for adjustment, the strategies chosen proved to be inefficient on several counts. From an economic standpoint, government policy emphasized short-tens repressive demand measures of the IMF type, setting aside and even precluding complementary structural shifts on the productive side. Without solving basic supply imbalances, recessive policies must be maintained for increasingly longer periods, with mounting human costs. Therefore, adjustment has been socially inefficient, not only because of the allocation of income losses to the weaker population groups, but also becausee by eroding the framework for employment and growth, recession is extended in time. Finally, as far as the ongoing accommodations entail the weakening of both human development and the capital formation process, as well as that of political solidarity,, dynamic growth losses will inevitably arise as one of the end products.

c) Since 1982, the central objective of economic policy has been stated in terms of abolishing inflation. However, given the nominal wage and salaries' downward inflexibility, differential leeway for movements in factor prices have been the chief mechanism for allocating the adjustment burden Thus, paradoxically, instead of being adversaries, inflation and adjustment were functional partners for altering income shares in the needed proportions, albeit with little economic fairness.

d) As for remedies, it is hard to be optimistic, given the prevailing mood in the international economic environment. In the Latin American case, lessening the human cost of the crisis will require a truly international cooperative effort through which the governments of developed and developing nations must make strong political commitments and grant each other meaningful concessions. Mexico badly needs access to world commodity and financial mar-

kets, less protectionism and faster redeployment by the industrial nations, as well as less rigid conditionality to allow for properly synchronized adjustment movements on both the demand and supply sides.

e) Domestic efforts seem to be equally stringent. Traditional import substitution policies should be greatly modified in order to (i) increase productivity, competititon and technical change, (II) create dynamic export capabilities, and (iii) reduce fiscal and monetary imbalances. At the same time, it is imperative to rebuild the political consensus between the state and the civil society which was broken by economic disorder. Thus, democratization in the design and implementation of economic policy is a precondition both for minimizing the social costs of the adjustment process and for enhancing domestic solidarity to the degree needed for the solution of the growth impasse.

Note.

1. ECLAC, *Notes pare d esmdlo* de America Latin *y el Carib.,* various number, (Mexico).

2. Benco de Mexico, Inform. anal, various number, (Mex.c).

5. D. mar,a "Note sobre el fi:ancumiento dal Dessrtollo Latinomericano," mimeographed (Mexico, 1986).

4. D. Ibam, Msis. *Debt and* Adjustment in *Latin America,* Proceedings of the Standing Senate Committee on Foreign Affaha, no. 8 (Ottawa, 1986).

5. M. Ol.on, The Rise and Decline *of Nations* (New Haven: Yale University Press, 1982),

6. Additionally, there are no unemployment insurance benefits.Pensions are low and are not keeping pact with the inflation rate.

7. D. Ibarra, "Comments on the Mexican Financial System," mimeographed (Tokyo: UNU-ECLAC Workshop on Pinandal Liberaaratlon,1985).

8. D. IMxra, "Crlale y Sector Extemo en America Latina," mimeographed (Santiago: Inter-Amedan Dialogue, forthcoming).

9, Salvador KaEfa, "La Distribution dal Inge.o en Mexico," mimeographed (Mexico, 1982); and E. Hei ands Laos and j. Cordoba, La Distribucon *dal Ingrem en Mexico* (Mexico: Cenero de Investlpdone. pea Is lntegeacfon Social, 1982).

10, o,Garcia-Albaandj.Sera,CauusyEfecrosdeli Crisis EconomiadeMexico (Mexico: El Colegio de Mexico, 1985).

11, 1. Boa and N. L sty, "Stabilization and Adjustment in Mexico: 1982-1985," mimeographed (Mexico: UNU/WIDER Project, 1986).

12, N, Lu.tig, "Economic Crists and Living Standard. in Mexico: 1962.85," mimeographed (Mexico: El Cnlegio de Mexico, 1986).

15, The price of tortillas more than doubled a the first seven month, of 1986, and subway fares in Mexico City lnaeued by 20 time a August of the sate *year.*

14. Before 1982, foreign inflows of capital and reedit. outvndghad debt service payments pie capital aan.fers abroad.

CHAPTER 17

Bolivia: Change, Crisis and Adjustment

Gustavo Fernandez-Saavedra

Bolivia is a country his transition. During the last thirty years, starting with the national revolution of 1952, it has experienced a slow, conflicting and painful process of social integration, regional articulation and diversification of its productive base. After the initial revolutionary phase and the subsequent military dictatorships, the aim has been to restore and consolidate a democratic system of government in order to ensure the basic institutional stability required for development.

The crisis which began in the early 1980s - originating in external circumstances and further exacerbated by internal factors - has interrupted and frustrated the transition process. The stabilization and structural adjustment measures taken so far have met with heavy popular resistance, which has intensified internal instability, and thus, external vulnerability. Nevertheless, Bolivia is not condemned to take this option for development. Another concept of structural adjustment which could consolidate and accelerate the process of transformation of the last thirty years should be sought. Such a program would allow Bolivia to adapt better to the main tendencies of the world economy. This paper will attempt to describe the background of the current crisis and propose some alternative rescue and reorientation measures for the Bolivian economy based on the country's resource potential.

The Reform Process

At the beginning of 1950, Bolivia was the least developed country of South America. It was 98 percent dependent on its mineral exports; per capita income was less than $80; the 80 percent rural population of a total population of three million lived under a virtually feudal regime. Although it had lost more than one million

square kilometers in successive dismembering following the wars of the Pacific, of Acre and o£ the Chaco, the state had been unable to integrate the various regions of the country into a single political, economic and social unit.

It was a country *ripe* for revolution. In April *1952,* the citizens and miners of La Paz overthrew the army of the oligarchy and began the difficult process of transforming Bolivian society and the economy.

Social Integration

The Agrarian *Reform* Law of August *1953* decreed the elimination of unproductive latifundia, handed *over* land to the peasants and *freed* them from feudal bondage. The following years witnessed a decrease in illiteracy, greater urbanization and an increasing participation of the peasants in the control of internal production and marketing circuits, as well as their more active and independent political presence.

Literacy and rural education campaigns carried out by the peasants themselves and supported by the central government reduced the illiteracy rate from *75* to *30* percent between *1952* and *1982.* The process of distribution and division of land produced minifundia (that is, individual ownership *of very* small plots of land), which in turn spufred the emigration of landless peasants to neighboring towns and to the eastern regions, mainly to Santa Cruz, where they earned wages growing sugar cane, cotton, soya or corn. More recently, these migratory currents have shifted toward Cochabamba and the Bend for the growing and marketing of coca leaves. The result of this exodus has been the growth of the urban population and the expansion of the eastern region.'

The participation of the peasants in Bolivia's economy, together with their growing control over the production and distribution of foodstuffs, gave them a new economic power. They were able to put pressure on the price-setting mechanisms for agricultural products and, through the production, collection, transport, storage and marketing of food, to control the food supply in the main urban centers. Parallel to this, the peasant world, perceived until recently as a homogeneous culture, began to differentiate itself into social classes with contradictory interests. On the one hand is the germ of a new rural bourgeoisie, who act as a link between city and country,

who manage their resources outside the banking and financial systems, and who account for one of the highest rates of accumulation and reinvestment in the national economy. On the other hand is the poor peasant, settled in the least productive outlying regions, organized in syndicates linked to workers' unions, surviving with difficulty as a wage earner in the service of other peasants or joining the migratory currents headed east.

The political presence of the peasant population is related to their increasing literacy, migration and economic participation. Soon after the revolution, universal voting was manipulated in elections; "zero democracy" (with all votes going to the government and none to the opposition) became the symbol of this manipulation. But things have begun to change on this front as well. Although peasants still follow the voting orientation of the nearest urban center, their political participation is more and more independent and less manipulated, as is evident from the results of the last three or four elections.

Thus the agrarian reform was a decisive factor in the still unfinished process of integrating the peasants into Bolivian society. This integration may be measured in relation either to the level of total marginality of the indigenous population prior to the agrarian reform, or to peasant integration in the more advanced Latin American countries. By the first measure, progress has been enormous; but by the second, the process has only just begun.

Exhaustion of the Mining Cycle

Bolivia has always been a mining country. Its economic activity has always moved with the rhythm and direction imposed by the market for silver and, later, tin. In the mid-

1970s, the growth of petroleum exports and of nontraditional agricultural exports such as sugar and cotton gave a brief impression that the country could diversify its productive structure as well as its foreign trade. This hope did not last long. Mining collapsed, modern agriculture failed to evolve, and Bolivia continued to depend on its natural gas and cocaine exports, whose significance grew disproportionately in the scenario of a blind-alley economy.

The recent collapse of the international tin market has accelerated thus process, but the decline of mining from its predominant position had already started years earlier. The contribution of mining who manage their resources outside the banking and financial systems, and who account for one of the highest rates of accumulation and reinvestment in the national economy. On the other hand is the poor peasant, settled in the least productive outlying regions, organized in syndicates linked to workers' unions, surviving with difficulty as a wage earner in the service of other peasants or joining the migratory currents headed east.

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The recent collapse of the international tin market has accelerated this process, but the decline of mining from its predominant position had already started years earlier. The contribution of mining

to the GDP decreased from 12 to 8 percent between 1970 and 1983.[2] Between 1948 and 1983, sales of minerals decreased from 98.3 to 44 percent of total exports. And in 1985, the sales of hydrocarbons surpassed, for the first time, those of minerals.

The end of the dominance of tin has had dramatic consequences. In 1909, 36,000 tons of tin were extracted from Bolivian mineral deposits; in 1985 the figure was only 15,750. Bolivia plunged from second to fifth position in world tin production, and its participation in world exports fell from 16 percent in 1970 to 9 percent in 1985.'

International factors, such as the decline by 11 percent in world tin consumption between 1970 and 1985, sales in the international market of the United States' strategic tin reserves, the presence of new producers such as China and Brazil, the slump in demand, substitution by other products and price instability all seriously influenced the decline of Bolivian mining, but internal circumstances accelerated the process. Among these may be mentioned severe deficiencies in management by COMIBOL, an inappropriate tax system, high financial costs resulting from a heavy foreign debt, technological backwardness of production and management methods, dependency on marketing channels controlled by transnational enterprises, and serious distortions in the exchange rate. The resources generated by nationalized mining financed the process of revolutionary -transformation during the 1950x. Then a political decision to disinvest in the mining sector sparked a progressive decline in Bolivia's international competitive position, a decline which was also caused by the exhaustion of Andean deposits and a persistently decreasing tin content in the ore.

Thanks to good world price levels in the 1970s and to a better capacity for action by the state, exports of some nontraditional agricultural products from the eastern region - sugar, cotton, coffee, soya and wood - increased significantly. However, the increase in the production and export of hydrocarbons was much more important. In 1973, during the world oil price hike, Bolovia began to export small volumes of petroleum (nearly 30,000 barrels per day). This phenomenon did not last long, but it fostered the illusion of a still nonexistent prosperity and encouraged the government of the time to contract loans which would prove impossible to repay. At the end of the 1970x, the production of liquid hydrocarbons fell precipitously, and exports were stopped.

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TABLE 4
Life Expectancy at Birth

Years	
1940	41.5
1950	49.7
1960	58.9
1970	61.9
1980	64.9

SOURCE: Inttimto National de Estadutica, Geografia a Infornutiea, Estadlsticas hlstoricas de Mexico (Mexico, 1985).

The structure and level of employment changed significantly. In the three decades prior to 1980, the labor force expanded 2.5 times, while the share of employment in primary activities decreased by half.

Structural change and rapid economic growth used to be the basic formulas used to reconcile rising social demands with a rather uneven income distribution (partially justified. by the need to foster capital accumulation). The estimated Gini coefficient for Mexico is high, fluctuating around 0.5 since the 1950s.° Both private and public investment growth, for their part, have usually been around 7 percent per year, as the record of the past three or four decades indicates.

Fiscal policy has played a key role in the growth process. Public expenditure has been used extensively to subsidize and to create external economies for the benefit of private business activities; by the same token, it has been instrumental in fostering political stability by alleviating income inequalities through the expansion of social services and welfare subsidies.' ° This is the locus of the forces behind the extremely robust growth in public expenditure, which rose from 8 percent to 42 percent of the gross domestic product

between 1950 and 1980 (table 5).

SABLE s
Public Sector: Income and Expenditure

Income	Expenditure

Billions of		Percentage of	Billions of	Percentage of
Pesos		GDP	Pesos	GOP
1950	8.64	8.6	9.46	8.2
1960 19.46 12.2 20.15 12.6 1970 109.06 24.5 109.26 24.6 1980 2,050.98 47.9 178.00 41.6				
SOURCE: BancodeMexico, Informennual.various numbers.				

The national revolution of 1952 accelerated the march toward the east. As Salvador Romero remembers, "It accentuated and brought into practice the plan of building a unitary and centralized State which would tend to standardize, in a model of abstract community and homogeneous culture, the particular elements of society."' The Cochabamba-Santa Cruz highway, the first paved road in Bolivia, was built with the intention of better exploiting the region's agricultural and mining potential. To the hydrocarbon and gas potential must be added the tin and gold wealth of the so-called Brazilian Escudo, a region located in the Amazon basin in the departments of Santa Cruz, Beni and Pando, and the potential of capitalist agriculture in the eastern regions, mainly in sugar, coffee, cotton, soya, corn - and cocaine. This last product calls for some special reflections, to be explored later.

It is interesting to note that the process of strengthening the Platense region of Bolivia coincided with the swift development of Brazil, although Brazilian effects on Bolivian internal transformation were less significant than the impact of national change. It is also noteworthy that the decline of the dominant power of the Andean region in the Bolivian economy runs parallel with a slowdown in the rhythm of development of its neighbors in the Pacific, affected, like Bolivia, by the instability of mineral prices and markets.

The process of regional articulation is still limited to the growing participation in the national economy of Santa Cruz and, in smaller measure, of Sucre and Tarija. However, it is already possible to perceive the risks and opportunities which this process implies for Bolivia. On the one hand, the incorporation of the new centers of activity into the old structure of national power will generate tensions and difficulties which will have to be dealt with carefully. On the other hand, it will open vast horizons of expansion and progress for Bolivian society.

Illicit Cocaine Trade

Drug production is a powerful factor altering Bolivia's economic and social fabric. Until recently only sensationalist news in the press, cocaine trafficking has escalated and become a source of deep national worry.

Although statistics on the production and distribution of cocaine are not trustworthy due to its illegal nature, some estimates

give an idea of its magnitude. World cocaine production, calculated between 100,000 and 150,000 tons in 1984, is concentrated in Peru, Bolivia and Colombia, with a smaller participation by *Ecuador,* Brazil and Argentina. Production increased by 70 percent with respect to the level reached in 1982, thus provoking a notable price decrease at the consumer level.

The marketing of the drug in the United States market is controlled by Colombian suppliers. Bolivia increased its participation from 10 to 15 percent, while *Peru* reduced its participation from 10 to 5 percents

The total value of the drug trade in the United States in 1985 was estimated at between US$ 60 and 100 billion.' At an approximate price of US$ 150 per gram[s] and a volume of approximately 200,000 tons per annum, the cocaine business, with a value of US$ 15 billion, would represent between 15 and 25 percent of the total drug traffic in the most important world market.

Bolivia cultivated approximately 60,000 hectares of coca° and produced between 42,000 and 63,000 tons of cocaine in 1984)[0] It is thought that around *40,000* peasant families are occupied with the growing of coca and with the processing of cocaine paste, which means that nearly 300,000 persons depend on this product.

Calculations on the value of Bolivian cocaine exports vary between US$ 1 or 2 billion." However, the different estimates agree on the figure of US$ 600 million per annum which must return to or be maintained in the Bolivian economy.' [2] This *figure* is equivalent to that of the total legal exports in 1985 and 50 percent higher than the total legal exports of 1986.

During recent years the cocaine trade has served as an escape valve *for* the Bolivian economy and may explain how the recession provoked by the world crisis did not push the country into uncontrolled social violence. In practice, a large part of the Bolivian import trade is financed by foreign exchange earned from narcotics trafficking, since resources earned through legal exports, mainly gas, *barely* cover the obligations and purchases of the public sector." Finance Minister Juan Careaga calculates that the underground economy, especially in narcotics, supplies two-thirds of the daily demand for three million dollars in currency. The remaining one third is sold by the Central Bank.' ` The Bolivian economy itself has thus become addicted to the currency provided by the cocaine trade. A temporary reduction in drug traffic following an operation called

"burning the furnaces," made with United States' direct intervention, disrupted the currency market and put severe pressure on the exchange rate, which may oblige the present government to modify its plans for what it calls the new economic policy." It is noteworthy that the effect of cocaine exports on the Bolivian economy is much more accentuated than in the cases of Peru and Colombia, where the magnitude of domestic production and of legal exports are much higher than in Bolivia.

Nevertheless, even with its apparent advantages - high rentability," a very small investment and intensive use of manual labor - coca culture *for* the production of cocaine has all the known disadvantages of the exploitation of any commodity. It depends upon few markets; it incorporates scarce aggregated value; its technological contribution is *very* low; price instability is very high, and so are the probabilities of substitution. As with other commodities, the producers' share in the financial benefits of the trade is very low. The price of one gram of cocaine in Colombia is US$ 15,[16] while the same gram is New York sells for $150. The transport costs and marketing commissions account for 90 *percent* of the final cost. The Peruvian or Bolivian farmer receives only 3 to 7 percent of the final price of cocaine.

The *Financial Times* notes, correctly, that "until recently, the problem has been seen in national rather than international terms. Producer country governments generally turned a blind eye, and the western consumer countries tended to attack only the policing problem (by pursuing the dealers) and the health problem (by treating addicts)." ' Today, it is an admitted truth that the nature and ramifications of drug trafficking call for concerted international action and that the nerve center of the problem is in the purchasing countries, for the simple and irrefutable reason that "cocaine production is a function of its demand." [e] A specialized conference of the United Nations has been called to examine the subject and its multiple economic, juridical, police, political and health ramifications."

Not much progress has been made, however, in the selection of adequate instruments to fight narcotics trafficking, defined as a "crime against humankind." Recent actions have continued to be eminently repressive, ignoring the fact that the peasants subsisting on the cultivation of coca and on cocaine processing were pushed into these activities by poverty and marginalization. Today, thousands of unemployed mine workers are emigrating to the coca-producing regions, reinforcing the contingent of city dwellers led by the tin crisis to Cochabamba, Santa Cruz and the Beni. *A development* answer must be found which will offer real survival alternatives to a population sadly dragged into this occupation by circumstances beyond their control.

The rehabilitation of the coca-producing countries in proportion to their evident structural weaknesses is a process that should be tended as carefully as the detoxification of drug addicts. If this is not done, the consequences could be extremely serious. Indiscriminate and imprudent police action against peasants could create the conditions necessary for the beginning of armed conflict, which up to now has been avoided by the Bolivian people all through the interminable years of political turbulence and economic crisis.

The Impact of Recession and Bolivian Adjustment

Bolivia suffered as few other countries did the harsh impact of the world economic crisis and the consequences of stabilization programs. The world recession of the early I980s brusquely curtailed hopes for the diversification of Bolivia's productive and export structure. Tin prices fell, frustrating the tardy attempts to rehabilitate mining. The fall of prices and the contraction of demand for commodities interrupted the promising export expansion of the agricultural products of eastern Bolivia. The debt crisis severely limited Brazilian financial capacity and was one of the factors which led to a postponement of the bilateral agreement for the purchase and sale of natural gas to Brazil.

In successive waves, the world recession, the debt crisis, droughts and foods, the collapse of tin prices, hyperinflation and shock treatments subjected the political and social fabric of the country to extreme tensions whose consequences have still not been adequately measured.

The Debt Crisis

During the 1970x, as has been the case with many other countries in Latin America during the tenure of authoritarian regimes, Bolivia financed with foreign credits the expansion of imports (especially of luxury goods) and public works, particularly the in frastructure for transport and communication. Bolivia's total foreign debt grew from US$ 551 million in 1970 to 3,041 million in 1980, 3,849 million in 1983,[20] and 5,214 million in 1985."

The Bolivian experience does not differ much from that of other Latin American countries regarding the efficient use of these resources: a very significant part returns to creditor countries as investment in real estate, tourism expenses and the simple and direct transfer of capital.

In the context of world recession and with the sudden increase in the cost of money, it was evident that Bolivia would not be able to honor its commitments to its creditors. Simple arithmetic may help to save comment and explanations. Exports in 1985 *were* valued at US$ 580 million, while the amount the country had to pay as capital and interest on foreign debts totaled US$ 774 million in 1984 - that is, 133 percent of exports." The servicing of interest alone, worth US$ 190 million, absorbed 32 percent of foreign sales.

In May 1984, Dr. Siles Suazo's government announced that it was obliged to suspend temporarily the payment o£ interest on public foreign debt to international private banks and to limit to 25 percent of exports the servicing of public debt to governments and multilateral financing institutions due to the impossibility of honoring Bolivian obligations under the conditions originally agreed upon.

There was no formal rupture of negotiations with the banks, nor were there public retaliation measures against Bolivia, notwithstanding the climate of recrimination and menace following the decision to enforce a partial moratorium. But the facts prove that a heavy curtain of silence fell over the "Bolivian case," and that flows of foreign financial resources were limited to a minimum, except for credits from the IDB, the Andean Reserve Fund and the Andean Development Corporation.

The decision to isolate Bolivia was taken. It was only a matter of time before this situation would oblige Bolivians to retrace their steps. With virtually paralyzed foreign financing and with severely diminished export earnings (due to the collapse of tin sales and to Argentina's difficulties in paying punctually for its natural gas imports), the economy went out of control: inflation reached around 15,000 percent per year. The particular fragility of the Bolivian economy and the lack of internal political consensus aggravated the situation to such an extent that in November 1984, President Siles decided to shorten his presidential mandate and called for general

elections the following May, In August 1985, President Paz Estenssoro took over. One of his first acts was to resume links with the International Monetary Fund and the banks. The moratorium was over, but the drama continued.

The Tin Crisis

On 23 October 1985, the London Metal Exchange closed its tin operations. The price of the metal, which had reached US$ 7.62 per pound in 1980, dropped on that day to US$ 5.42, to $3.44 in November 1985 and to $2.47 in July 1986.

The effect of the collapse of the international tin market *was* catastrophic for Bolivia. The loss of export gains of around 42 percent between 1978 and 1985 was almost fully explained by the fall in tin prices and exports. The accumulated losses are estimated at US$ 1 billion. With production costs of over £10,000 per ton[29] and prices in the range of £3,700 per ton in August 1986,' very few mines will be able to continue working.

lithe tin price is stabilized at around US$ 3.20 per pound, production will fall to approximately 7,600 tons per year,[3] S which represents only half the 1985 production of 15,750 tons and only one-fourth of the production during ihel960s. In this case, nearly 70 percent of operating mines would close by October 1986. Over 50 percent of employed labor in the mining sector, or 39,000 workers, would have to be discharged.'" According to the most optimistic scenario, at a price of around US$ 4.20 per pound, one-third of the labor force, or around 22,500 workers, would be out of work.

The combined effect of the debt crisis and the collapse of the tin market provoked a depression of unprecedented proportions. The GNP decreased by 21.4 percent and the product per capita by 31.4 percent during 1982-85, which brought incomes down to 1960 levels. Urban unemployment doubled from 6 to 12.6 percent, domestic investment fell from 17 to 7 percent, and between 1978 and 1985, exports fell by 42 percent and imports by 57 percent.

The Adjustment Plan

On 29 August 1985, Dr. Paz Estenssoro's government established an orthodox plan of monetary stabilization under the designation "new economic policy." The main objective was to stabilize the economy and to control hyperinflation. The following measures were taken

a) Reduction of the fiscal deficit.

b) A flexible exchange policy, arrived at by a combination of

directed flotation and mini-devaluations, c) Free prices.

d) Salary freeze.

e) Rebate of customs tariffs to a general level of 10 percent, in some cases reaching 20 percent over the value of imported merchandise.

I) Restructuring of public enterprise.

One year later, the government had *achieved* control over hyperinflation, holding it to a "manageable" level of 60 percent from January to June 1986.

The reduction of real salaries is the nucleus of the new policy, whose original purpose was improving international export competitiveness by compressing the labor component of the price of a given product. In a memorandum of 2 June 1986, consultant J. Sacks peremptorily stated, "It cannot be expected that workers will recover the real salary levels of 1985 or before," and "Within the government, it should be understood that there are no resources for a higher increase of salaries.""

However, although salaries lost nearly two-thirds of their acquisitive power, the exercise did not yield the results expected, as exports fell *even* lower in 1986, a year in which it is estimated that mineral sales will not surpass US$ 56 million and that total exports will remain at around US$ 400 million.' °

The consolidation of the economic program, as noted by Mr. Sacks, "depends on significant reductions in the personnel of COMIBOL, YPFB and the central administration."" The same consultant estimates that 13,000 worker; (of a total of 22,000) should be discharged from COMIBOL and nearly 2,000 employees from the state oil enterprise.

The elimination of tariff protection caused ravages within the weak industrial sector.[30] Cuts in state investment did probably irreparable damage to education and public health. Negative redistribution of income concentrated wealth in the higher-income sectors. The collapse of the tin market drowned expectations of *recovery* from exports, and the exchange *rate* proved for the hundredth time to be an insufficient instrument to develop exports in a backward country with so many serious problems on the supply side, in transport and in marketing. International financial cooperation proved to be as miserly as ever. International banks would not even consider fresh loans to Bolivia, and the IMF continued to insist on its never-ending list of requirements, requests and conditions before disbursing, one month ago, the first US$ 50 million of its support program.

Now that the first period of the monetary stabilization program has come to an end, its limitations as a development instrument are becoming evident. Its theoretical basis cannot be reconciled with the intrinsic conditions in a backward, dependent and marginal country.

On the one hand, opening the foreign sector aggravates the situation for national industry without an adequate counterpart increase in exports due to the very bad condition of commodity markets, especially that of minerals. On the other hand, the debt problem continues to throw a constant and ominous shadow over Bolivian development plans, while no political solutions of a Latin American character have been found in which the government appears interested at the moment.

The hope of direct foreign investment is another optimistic thesis of the plan which will probably never crystallize?' Several factors combine against this possibility: the stagnation of demand and the fall of tin prices, the weakness of the commodity market, the scarce infrastructure of services,. and the small and primitive industrial structure.

Finally, the responsibility which the plan has placed on the shoulders of the Bolivian private sector is disproportionately large. Without calling into question its patriotism and vocation for service, one cannot but remember the structural frailty of national private enterprise, its extremely low level of capitalization, and the very wide technological and management gap in relation to levels found in neighboring countries. Private sector exports represent barely one sixth of total sales abroad. The limited role of the industrial sector in a country with such a small and dispersed market is well known; and no further analysis is needed regarding the backward agricultural sector, which includes the so-called modem agriculture of the eastern region.

The folly of applying neocapitalist solutions to a country with Bolivia's structure and development level is so obvious that the zeal with which the new truth is preached and the rigor with which programs are put into practice can be explained only by the need to maintain rationality and coherence in the face of the industrialized countries' determination to consolidate and expand their control of the world economy. On the global scene, the final result of the Bolivian program is of no major importance. Suffice it to say that its voice does not ring flat in the chorus.

Structural Adjustment - Meaning and Content

The "new economic policy" closely follows the model of adjustment policies recommended by industrialized countries and the International Monetary Fund. As already seen, it tries to *(1) reduce* aggregated demand, with a consequent diminution of the level of imports, control of monetary issue and balancing of the budget; (ii) restructure the economy and produce more exportable goods; and (iii) apply a new outward-oriented development strategy, with a reduced role for the state and more privatization of economic activities.

The need to reestablish equilibrium in, and control of, the Bolivian economy cannot be disputed, especially considering the current balance-of-payments situation after a nearly surrealistic period of hyperinflation. But it may be questioned whether the price of monetary stability should be, in the short term, as high as has been described. Beyond ethical or moral considerations, the economic logic of these measures should be carefully examined in the perspective of a longer-term development strategy. To begin with, the meaning of the expression "structural adjustment" should be discussed, as it is used ambiguously and ambivalently by different political and economic schools.

The need to "restructure" the economy of developing countries is a clear consequence of changes in the international economy. The risks and opportunities which these transformations imply for so-called Third World nations are also evident. The situation of the commodity market and the state of technological change are of particular relevance to Latin America.

Commodities

In relation to the commodity market and its influence on Latin American development, the following facts should be kept in mind:

a) The importance of commodities in the world market has diminished from 31.6 percent of global exports in 1966 to 17 percent in 1983.

b) The relative proportion of the participation of industrialized and developing countries within the commodity market has also altered. Between 1966 and 1983, the industrialized countries increased their share from 54 to 63 percent of the total, while the share of developing countries fell from 33.6 to 29.3 percent during the same period. The fraction claimed by Latin America remained stable at around 13 percent of the developing countries' total.

c) Due to the falling share for developing countries in commodity trade, Latin America's share of total world exports diminished from 11.6 percent in 1950 to 6 percent in 1981." This drop may be explained by the fact that the region continues to depend on commodity sales for 80 percent of its exports.

d) World prices fell in 1985 to their lowest levels since 1948. Between 1980 and April 1986, the prices of commodities decreased by 30 percent in dollar figures.

e) Lower prices caused an accumulated loss of export earnings of approximately USS 36,000 million for Latin American and Caribbean countries during 1978-83, excluding petroleum.

These events may be explained both by the contraction of demand for commodities and by the increase in supply. On the one hand, the consumption of commodities was limited by slow growth and recovery in the industrialized countries, the use of new materials and substitutes, and reduction of the use of energy and other commodities per unit of production as a consequence of technological change. On the other hand, shielded by their subsidies policy and their control of world transport and marketing mechanisms, the industrialized countries increased their supply and their participation in the global exchange of these goods. Developing countries, in turn, found themselves obliged to raise their own export levels, hoping to try to maintain markets in order to meet their colossal financial and debt servicing obligations.

To be precise, in the midst of over all economic uncertainty and due to the instability of the commodities market, the only safe forecast is for a continuing loss of the importance of commodities in world production and trade.

Technological Change

The structure of production and demand in industrialized countries is undergoing a profound transformation as a consequence of the development of new technologies, especially in semiconductors, computing and communications. A recent study by the *Econo*mist states that "the country dominating the three most crucial of all technologies [mentioned above I will surely head the most powerful motor of development of the twentieth century."[3]J Technological change is the most dynamic factor In the transformation of the world economy and projects its influence into the sphere of political and strategic interests, altering the precarious balance among the super powers and shaking the relationships among the western industrialized countries. The "space shield" project of the Reagan *administration,* the *modernization* of the Soviet economy and the Eureka Plan" of the European countries are manifestations of the same need to adapt to the requirements of this contemporary revolution (or of consolidating its control, in the case of the United States),

The consequences of technological change will also *condition* the nature and characteristics of the development prices in developing countries. In the long term, comparative advantages based on the availability of labor or natural resources will not be the main deter*mining* factors of world competitivity.[11] In the next twenty-five years, in nearly the whole world, cheap or expensive semlipecialized labor will quickly give way to "smart' machinery as the key element in competitively, Energy costs are irrelevant, typically only 3 to 4 percent of industrial costs. The same may be said of the labor force, which represents only S to 15 percent of the total costs,'°

The introduction of technological changes will also reduce the volume and value of commodities incorporated into final products and the amount of commodities that enterprises will have to keep in their *inventories,* On the other hand, substitution within the commodities sector, and substitution of commodities for industrial products, has been one of the factors most responsible for the depression of several commodity markets" In its diverse forms, the effects of technological change on the demand for commodities will be felt more and more strongly in the near future.

However, new technology also offers crucial opportunities to spur the development process in developing countries at a lower cost, in less time and more efficiently than traditional' methods," For countries such as Bolivia, the problem is not one of access to new technological knowledge or the production of high-technology goods, but of the possibility of using this knowledge and these goods to solve the traditional problems of its backwardness.

Undoubtedly, the application of new technologies may improve the levels of nutrition, education and health of the Bolivian population. The production costs of export commodities could be *reduced* if better methods and equipment were placed within the reach of countries with small consumer markets through the introduction of flexible manufacturing plants which could operate twenty-four hours a day, producing hundreds of different products instead of concentrating on only a single product line."

Whatever happens - whether technological change condemns countries like Bolivia to definitive marginality or enables them to remove the obstacles hindering their development - is essentially a political issue, It *depends* on the character of the chosen development model, on the nature of the structural adjustment program *adopted* and on the attitude taken toward international cooperation.

The character of the tendencies described leaves little doubt as to the orientation of structural adjustment programs: they must be guided by the aim of progressively reorienting the economies of developing countries away from the commodities sector, whose future is every day more compromised and difficult, toward the more dynamic sectors of world production and trade - manufactures and services,

But the criteria guiding present-day adjustment plane are quite different, and one cannot but express doubts as to the effects that programs structured by the industrialized countries, the IMF and the World Bank will probably have. Their determination to leave the economies of developing countries open to the so-called free play of offer and demand, and their interest in maintaining the productive specialization of those nations in the primary sector, is in open contradiction to the main present day economic tendencies of stagnation and decline in the commodity market. The systematic elimination of all forms of protection - both good and bad - from the domestic production of manufactures destroys the basis of industrial development. The brutal reduction of public investment in

education, health, nutrition and public services damages, probably irremediably, the possibilities of structuring an adequate policy of human resource development at the precise moment when the world economy has begun to rotate around man as the axis of the development process.

The opening of the weakened economies of the developing countries after a decade of successive crises leaves them more exposed and vulnerable than ever before to the mutations of a volatile, disordered and unpredictable world economic system. These constant shock treatments unchain a process of social and political agitation which on the one hand, neutralizes or obliterates the desired stabilizing effect of economic measures, and on the other, destabilizes fragile domestic political systems, as Bolivia's experience has dramatically demonstrated.

The Bolivia of the I980s is *very* different from the Bolivia of the 1950s. It now has a growing peasant presence in its domestic economy and politics. The tin cycle is coming to a close, and a tottering and unstable process of building a new productive base is under way with the twofold purpose of occupying the place left by mining and of eliminating the country's dependence on the illicit cocaine trade. Bolivia has progressed a few steps in the internal direction of regional articulation, but the full occupation of its own territory is a yet distant objective. Although after heavy sacrifice the country has managed to reestablish democratic institutions, it still has a long road to travel before they are definitively consolidated.

Without falling into rhetorical excess, it may be stated that Bolivia's fate will follow the fate of this transformation process. That is *why* the orientation and results of stabilization and adjustment programs are of utmost importance. If the mechanical and simplistic grafting of solutions created for different societies and economies persists, the risk of tension and domestic conflict will be very high, not only aggravating the crisis which *they* intend to heal, but menacing the very basis of the social contract on which the republic is based.

The new adjustment strategy should be based on several requisites. To start, it should be able to count on the participation and support of a significant portion of the population and be based on a minimum internal consensus. It cannot be imposed by the simple expedient of force. Repression has often been used by authoritarian governments as an instrument of economic policy, with well known results, and it would not make sense to have democratic governments committing the same error.

In the Bolivian case, and owing to the force of circumstances, the adjustment program should have a modest start. Diversification and widening of the bases of production and the export of commodities are clearly within reach, considering the potential and resources of Bolivia. These measures will help to compensate for losses provoked by the tin collapse and to eliminate the perverse consequences of the illicit cocaine trade. In this scenario, the export of natural gas becomes an immediate development option. Studies of quantities of reserves and cost analyses have been satisfactorily completed, and negotiations to reinitiate agreements with Brazil have been resumed. The satisfactory conclusion of these agreements will offer the necessary breath of air which will enable Bolivia to restart the expansion of agriculture and to rehabilitate gold, lithium and even tin mining.

The new development strategy will have to reorient the national economy, concentrating state action and support in those activities designed to satisfy, in a growing and self-sustained way, the population's basic needs for food, health and education. This implies concentrating a good part of the effort to restructure and dynamite the economy in the internal market! ° particularly in the expansion of agriculture and of small- and medium-scale industry. Parallel to this, instead of withdrawing its assistance, the state must maintain and rationalize its support to the health and education sectors with the aim of improving the formation of human resources and of avoiding the institutionalization of the unfair and dangerous principle that access to health and education is a privilege of the higher-income sectors.

The financing of this development program will depend, more than ever, on Internal savings, as there is not much hope for a change of attitude by the industrialized countries or for an acceleration in external financial flows, whether public or private. But the introduction of tax reforms will not be enough, nor will an Increase in the efficiency of tax collection mechanisms. One requisite will be to ensure that the first and foremost beneficiary of the sacrifices imposed by the adjustment process shall be the Bolivian people. The servicing of debt and financing a new start for the growth process are not mutually exclusive. This means that internal savings will have to be retained in the country to finance its development, and that

the export of part of these savings in the form of interest payments and amortization will have to diminish substantially. Different procedures may be used to reach this objective, and it seems prefer able to establish them in consultation with creditors. But the possibility of unilateral action cannot be excluded if creditors maintain a position which is not only unfair, but also unlawful and against their own interests.

Within the frame of this rehabilitation program - based on internal political consensus, with the diversification of exports, with priority given to meeting the basic needs of the population, to agriculture and to small• and medium-scale industry, and with the expansion and retention of domestic savings - Bolivia may recover a certain economic balance and modestly *improve* its possibilities *for* growth. But Its fundamental condition of being a dependent and marginal country will not be altered, nor will its structural problems of internal development be resolved, *For* Bolivia and other small and medium-steed nations of Latin America, the structural changes required to incorporate themselves into the world economy's more dynamic currents should be faced with a serious effort toward continental integration.

Note

1, The urban population grew from 750,000 In 1960 *to more* then three million in 1988 The eunmmoat dry of 8uta Cxua, which had 40,0001nhabltanta M 1980, now hen 400,000,

1. *TIN InraMatlonal* (February 1986). 8.Ibid.

4, to 1974, wiehln Ut. framework of. group of bWtuel eoowraeon graementy a comaNtment w sea 400 m1Non wblc leer pet day of natmet ps to 6tua wen made. It hen net yet been fulfilled.

S. klndor aamero pltW, "DeacentrWUdan, demo tS y podn lust," *mama* Hong (La Fu), 11 June 1966, p.6.

6. NattonM Nucetlm Intelligence Comumen Committee, *N.Md* blbune, 19 Augut 1986,

7. PYnanck(T(mn, 9 Aueurt 1966.

8, Nemld Ttlbune, 11 August 1966, *9. Fmanckl Tlmn,* 19 AuNat 1986, *10. HmtW Twbum,* 11 Aupu 1986.

SL FmnncW Ttmu. 19 August 1966. At a price of 916 per r, the use of

63,000 mm would represent V88 00 million.

12. *Faanolal* Timer. 19 Augwt 1986; Robert,, Jordan Panda, "Coca, Cocaine and Narw-traffic," *PnrencO.* 10 Much 1986; *Lr NOnvel Observateur,* 28 Augurs 1986, p. 48.

18. Gar sale, to Argentina account for a figure near U6$ 880 million, After the latest fall In price,, around UB$ 100 million of this amount Is retained by Argentina.. payment of the Bolivian debt m that country. Vlae•President5. Garrets noted in a speech to Congress on 6 Augwt 1986 that the amount the state ha. available for imports I_s U5$ 300 million.

14. FInanelai T/mss. 19 August 1986.

18. It Is estimated that coca leaf production per hectare hat a value of UB$ 10,000 per annum. RentabWty of a hectare in the pampa burned, (wet flatland,) Is approximately Us. 1,000 to $1,809 per annum.

16. *Herald* Tribune. 22 August 1986.

17. *Financial Tlmes,* 9August 1986.

10. Speech of MlnlsterGnstao Femandee2uvedra to the UN. General Assembly,

2 October 1984.

19. The initiative for convening this conference war originally submitted *by Ba*livla during the 1982 and 1984 sessions of the General Assembly.

20. World Bank, World *Development Report 198$*

21, Report of the Mlnbtry of Finance of Bout, quoted in an BFB agency able, 11 Augurs 1986. According to the *CEPAL* Economic *Report 1985,* the relasionahip of BolMa's debts m its exports, on the order of 880 percent, b the highest in Latin America - higher than that of Peru (370 percent), Argentina (483 percent), Brazil (868 percent) and Mexico (822 percent),

22. The situation I, equally bad in 1886. According to declarations of the Minister for Planning, debt serriclng will require almost UB$ 1,600 million this year, while exports will earn less than $400 million - a debt.export relation of 400 proem, BFB cable, a 1 Augwt 1986.

28. The Bruilan costs are under £ 4,000 per ton.

24. P7nancai *Times,* 16 August 1986,

26, Nvaro Uplde, "L al,la dal mane;" Foro Economlco (L Pu), January

1986, p. 17.

26. Ibld.

27. Memorandum of J. Bach,, *Roy* (L Pa), 14 August 1986, p,$. 20, June Ganetq menage to Congress, 6 August 1986. 29. J. Bath,.

80, According to the President of the Chamber of Industries, the approval of the new Will regime "comtltutu a real 'coup de grace' to Industry" and "very shortly It will produce a massive derma of factories with the consequent dismissal of worker,," Javier Wye Gamma, *Ray* (L Pa), 22 August 1986.

31. "Ihe Industrialised countries constantly repeat to developing countries In general -and a the Latin American couMa in particular- that they have to learn to rely an their own sources of a,4np for the internal process of capital accumulation. Foreign apical, In the farm of direct investment, .41i arrive *ajar* the recovery of the growth proton and Inumuch a monetary, institutional and salary policies proposed by developed countries will have been

comely designed and executed in developing countries." V. Ventura-This and G, Femandes-0ovedra, *America Latlna y Ia eronank* mundlal (CBPAL, 1986), p.6.

82. 1MP, *Supplement of Tad.* Satlalw (1902), pp. 118.21.

B3. "Survey on High Technology," *Sconomhq* 23 August 1886,

54. The Eureka Plan Implica the execution of 62 joint development projects, mainly In the area, of computer., semlwndumora and telecommunication,, at a con of USE 2,100 million. Financial Thnes, 1 July 1986.

55. Venture.DlaeendFeenande..Suvedm,AmerlcaLatlna,p.25. 58. "Nigh Technology.'

57. "Technological Change and iu Implication, for Some Latin American Export

Cummodltlea," mimeographed (UNCTAD/ECLAC/UNDP project RLA/82/012 , p.4. 88. Venttua.Dia, and Fernandea.8uvedra,Amer/ca *Latlna,* pp. 21 ff. 59. "HIgh Technology."

40. *NntlonalF/anforRehabilitation andDevelopment. 1984/987* (La *Paz).*

CHAPTER 18
The Social Cost of Crisis and Adjustment in Latin America and the Caribbean

Neville O. Beharie

The early 1980s witnessed the onset of the worst decline in economic performance and social well-being in the Latin American region since the depression of the 1930x. The impressive economic growth and improvements in economic and social infrastructure achieved during the post-World War II period up to 1980 have been seriously impaired, and the social and political fabric of the region has come under severe strain. Nor is any substantial alleviation of this situation envisaged for the medium term, given the projected debt burden, the outlook for commodity prices, international market conditions generally, and the time required before national responses to the crisis actually affect economic performance. Such responses, at the minimum, will have to include a reworking of internal policies geared to increasing productivity in traditional export sectors, to expanding competitive nontraditional exports, and to stimulating efficient import substitution activities and the production of nontradeables.

Achievements Prior to the Crisis of the I980s

During the period 1960-80, Latin America achieved a rate of economic growth significantly higher than that of developing countries as a group. Real GDP increased at an *average* annual rate of 5.8 percent, while population growth decelerated over the period to an average of 2.5 percent per year. Gross domestic product per capita thus increased at an average annual rate of 3.3 percent - again, higher than that of the rest of the developing world, excluding the petroleum-exporting countries (table 1). This relatively high growth rate of the Latin American economy is evident in a narrowing of the income gap vis-a-via the industrialized countries, with the ratio of Latin America's GDP per capita to that of the OECD countries rising from 14.1 percent in 1970 to 15.8 percent in 1980 (table 2).

TABLE 1

Growth in GDP Per Capita
(Percent)

Period	1960.70	1970-80	1980.85	Averages	
Argentina 3.7	2.8			0.7	-
Bahamas	n.a	3.6}	-0.5		
Barbados	5.9	0,7	-1.5		
Bolivia	2.4	1.8	-6.5		
Brazil	2.9	5.9	-0.7		
Colombia	2.2	9.7	0.8		
Costa Rica	9.2	9.1	-2.1		
Chile	2.1	1.1	-1.8		
Ecuador	1.8	5.8			
E1 Salvador	2.7	0.8	-3.4		
Guatemala	2.6	2.7	-9.9		
Guyana	1.9	0.9	-3.7		
Daid	-0.8	9.0	-2.9		
Nonduraa	1.8	1.6	-2.3		
Jamaica	4.5	-2.1	-1.2		
Mexico	3.6	9.6	-1.2		
Nicaragua	4.1	-2.4	-2.4		
Panama	5.4	3.1	0.4		
Paraguay	2.1*	5.9	-0.7		
Peru	2.6	0.9	-2.9		
Dominican Republic	3.1	4.3	-0.8		
Surinamc		0.5}	-1.8		
Trinidad and Tobago	2.9	3.4	-2.1		
Uruguay	1.0	2.5			
Venezuela	2.6	1.1	-4.2		
Total	2.9	9.4	-1.6		

" 1963-70 for Paraguay.

} 1976-80 for Bahamas and Surinamc.

SOURCE: 1DB Data Bank, based on official statistics.

The pattern of development in most of the countries of the region up to 1980 was characterized by an intense process of invest ment, which resulted in a transformation of the production structure and of technology. The consequent diversification and expansion of the region's productive capacity allowed it to reach to a high level of self-sufficiency with respect to consumer goods while at the same time making significant inroads into the production of intermediate and capital goods. Partly as a result of this process, the region suc

ceeded - since the I960s - in substantially diversifying its exports, with a significant proportion of these consisting of intermediate and manufactured products directed mainly to the regional market. At the same time, increased integration and sectorsl interdependence was achieved among the national economies of the region, facilitated by the expansion of productive infrastructure, especially in the energy, transportation and communications sectors.

The strong rate of growth and increased diversification of production and exports up to 1980 afforded a steady increase in productive employment in most countries (table 3). For nine selected countries` taken together, employment in the formal urban sector expanded at an average annual rate of 3.6 percent in 1950-60, 3.8 percent in 1960-70, and 4.1 percent during the period 1970-80. Moreover, the growth rate of employment in eight of the nine countries exceeded that of the working age population, with the result that unemployment rates were maintained at fairly moderate levels.

TABLE 3
Latin America: Employment Growth in the Formal Sector
(Average Annual Growth Rates)

	1950-60	1960-70	1970-80	1950-80
Economically active population	2.1	2.5	8.0	2.5
Working age population	2.6	2.9	2.9	2.8
Urban population	3.6	3.6	4.2	3.3
Foniial employment	3.6	5.8	4.1	8.9
Working age population				
Argentina	1.9	1.7	1,5	1.7
Brazil	2,9	3.1	2.9	8,0
Colombia	2.6	5.2	5.0	2.9
Costa Rica	3.2	5.9	8.7	3.6
Chile	2.2	2.4	2.3	2.3
Mexico	2,7	3.8	3.4	5.1
Peru	2.2	2.7	8.1	2.8
Uruguay	1.2	1.1	0.4	0.9
Venezuela	3.4	4.0	4.1	8.8
Formal employment				
Argentina	2.7	1.7	1.3	1.9
Brawl 3.7 4.8 4.5 4.3				
Colombia	3.6	6.4	42	4.7
Costa Rica	4.5	5.8	6.0	5.4
Cite	2.3	5.2	2.8	2.8

Mexico	6.5	3.3	5.2	5.0
Peru	3.4	4.2	46	4.1
Uruguay	1.3	1.2	0.1	0.9
Venezuela	5.3	4.4	7.0	5.6
SOURCE: PREALC, CEPALandCELADE.				

At the same time, substantial gains were achieved by the region in general social conditions, with the result that life expectancy at birth rose from about 56 years in 1960 to 64 years toward the end of the 1970s; access to potable water rose from under 40 percent to over two-thirds of the growing population; and school enrollment rates at the primary level reached close to 100 percent in most countries.' In addition, improvements in the coverage and quality of health delivery systems and in general nutritional standards brought about impressive declines in infant mortality rates, though with considerable variation across countries.

TABLE 5
Retrogression in Real GDP Per Capita (1984 US6) - 1985 *Levels* Compared with Pre Criss Performance

Comparable		Number of Years
Countries	Year	Retmgrased
Nicaragua	1960	25
El Salvador, Venezuela	1964	21
Bolivia, Guyana, Jamaica, Peru	1965	20
Argentina	1967	18
Guatemala	1972	13
Surname*	1975	10
Costa Rica, Uruguay	1976	9
Barbados, Honduras, Trinidad and Tobago	1977	8
Chile, Ecuador, Haiti	1978	7
Bahamas, Brazil, Mexico, Paraguay, Dominican Republic	1979	6
Panama	1981	4
Colombia	1985	0
All countries	1977	8

Data available only for period beginning in 1975. SOURCE: IDB.

TABLE 6
Real Wage Indices for Selected Countries, 1985 (1980= 100)

Average Real	
Avenge Real	Real Minimum Wages in
Remuneration	Urban Wage Construction

Argentina 114.5 127.5 109.0 Brazil 113.1 88,2 82.8 Colombia 114.0 110.0 106.1 Costa Rica 922 112.2 79.6* Chile 93.0 76.1 61,4 Dominian Republic 82.2 n.a. Ecuador	n.a.	59.7	n.a.
E1 Salvador		66.4	n'a.
Guatemala	n.a.	99.1*	109.5}
Haiti	na.	87.1	
Honduras		89.0	87.1
Mexico	73.1	71.7	70,6
Nicaragua	n.a.	65.6"	96.3+
Panama		86.0+	n.a.
Paraguay		99,1	89,3+
Pen.	59.7	55.3	61,6
Uruguay	88.0	94.1	70.4
Venezuela	n.a.	65.8+	ace.
1984. 1983			
SOURCE: CEPAL, Crisis *Economics y Pout* fear de Ad/eats, *EsmbNzaclon y* Crecimiento			
(1986), tables 16,17 and 18.			

Unemployment and Underemployment

The median urban unemployment rate increased from about 7 percent in 1970 to almost 13 percent in 1984, the highest since the end of the 1960s (table 7), increasing continuously during 1979-84. In some countries, the unemployment rates reached in 1984 were 24 tunes higher than they had been fifteen-years earlier. In addition, while in 1970 only two countries had unemployment rates equal to or higher than 10 percent, and in 1980 only three were in this situation, eight of the thirteen countries for which data are available fell into this category in 1984.

Impact of the Crisis on Key Indicators

The severe recession of the early 1980s had a major impact on the income gap between Latin America and the industrialized countries, on real incomes, and on employment and social conditions.

The ratio of the region's GDP per capita to that of the OECD countries fell to 13.6 percent by 1984, somewhat below the 1970 level. For the 1981.85 period as a whole, real GDP per capita declined by 8 percent, with the result that income levels in most countries of the region fell to levels attained years (sometimes decades) before.

Output and Income

The impact of the crisis on the economy of the region is dramatically reflected in the path followed by the region's GDP per capita compared with performance in the previous two decades (table 4).

The severity of these declines in output is evidenced by the fact that the region's 1985 real GDP per capita level fell to a figure comparable to that for 1977, with a wide dispersion among countries (table 5). Moreover, although the evidence is scattered, there are strong reasons to suggest that the declines in income affected low-income families more severely, as most countries appear to have experienced steeper reductions in real minimum wages and in wages in the construction sector compared to overall average wage levels (table 6).

During this same time, however, natural gas sales to Argentina had already started, and these would advantageously replace the lost oil incomes and come to occupy first place among the country's legal exports.° In *1983,* with a bill of *USS 351.3* million, gas sales accounted for *53* percent of total Bolivian exports. In *1985,* with the same volume, they accounted for *68* percent of exports due to the collapse in the production of minerals.

Regional Articulation

Throughout most of Bolivia's history, the center of economic and political power has been located in the Altiplano and the valleys of the Andes, where nearly all the population lived during the Inca, colonial and early republican periods. Following the colonial development pattern in Latin America, the main urban agglomerations and the agricultural centers rotated around the silver and tin mining nuclei or followed the route of their export channels. This was how Sucre and Cochabamba developed to supply Potosi and Oruro, and how La Paz and Tarija grew in importance as transit points on the roads to Lima and Buenos Aires. At the end of the nineteenth century, the exploitation of natural rubber in the Beni and Panda opened the possibility of establishing a development pole far from the Andean axis, in the heart of the Amazon. The experiment ended with the fall of rubber prices in the international market and with the Acre war.

For centuries, the supremacy of the Andean region was unquestioned. But the rest of the country did not really exist. Vast empty spaces in the Amazon and Platense regions constantly invited the attention of neighboring countries.

The discovery of petroleum and the Chaco war during the *1930s* changed Bolivia's perception of the occupation of its own territory. Political leaders and thousands of fighting forces that had descended the Andes discovered the strategic value and economic potential of the eastern region. Brazil and Argentina also perceived the abundance of natural resources in Santa Cruz - hydrocarbons, iron, cattle, agricultural produce - and started economic cooperation programs aimed at strengthening their presence in the zone. The Santa Cruz-Corumba and Santa Cruz-Yacuiba railway lines are evidence of their plans.

Rising unemployment rates were accompanied by changes in the structure of the underutilized labor force in a manner that seriously reduced family income, as the unemployment rate within the 25-44 age group increased substantially, thereby affecting the incomes of heads of households. This substantial and sustained increase in the open unemployment rate represented a break from the preceding decades, which were characterized by shorter and less intense cyclical variations. Moreover, there is some evidence to suggest that the unemployment rate among the highly educated has been on the rise, a situation which could accelerate the loss of talent and skills by the region.

The increase in visible unemployment was accompanied by a decline in participation rate (the "discouraged worker" syndrome) as marginal portions of the work force (mainly women and youth) abandoned the search for employment in the face of declining prospects of finding any, suggesting that measured open unemployment underestimates the degree of the problem. This is made even worse by the apparent increase in visible underemployment through a reduction in hours worked resulting from a weakened demand for labor, a situation which has been significant in several countries, including Argentina, Chile, Peru and Costa Rica.

The increase in invisible underemployment, which is reflected in the rapid growth of the informal sector, is characterized by low levels of productivity and income and a high degree of instability in the duration of employment. With such activity amounting to an estimated 30 percent of the employed urban labor force, the implications for income distribution and the degree of poverty become quite clear.

The rising unemployment and underemployment rates of recent years have been the result of several factors: the combined impact on the regional economy of an unfavorable external economic environment and internal policy adjustments which had a concretionary effect on output, income, and consumption; the cumulative and continuing effect of a declining share of agricultural employment coupled with rural-urban migration; and the inability of the modern urban sector to generate employment at a rate equal to the rate of growth of the urban labor force, despite the fact that employment in the industrial sector grew at an average annual rate of about 4 percent. Indeed, with the urban population in the region having

increased from about 50 percent in 1960 to an estimated 70 percent

by 1985, the employment problem during recessionary times has become critical. In the past, "the social impact of economic crises was hidden as it was scattered over a large number of small towns or disseminated into the rural areas. In the latter, the possibility of resorting to subsistence agriculture worked as a buffer mechanism that alleviated the impact of a crisis. "a

Public Expenditure on Social Services

The effects of the crisis on low-income segments of the *popula*tion were further aggravated by the inability of the public sector to function as an ant cyclical counterforce, mainly because of the dramatic decline in its own revenues and the consequent need to implement fiscal austerity measures. Social outlays in most countries of the region declined substantially in real per capita terms at a time when needs, especially among low-income persons, were growing

TABLE 9
Central Government Expenditures in Soda1 Services, 1970, 1975, 1980.84
(Percentage of Total Expenditure)

	1970	1975	1980	1981	1982	1983	1984
Argentine	40.8	940	54.0	31.0	26.6	25.9	33.4
Bahamas	42.5	43.7	41.6	35.6	97.0	39.2	44.5
Barbados	59.0	51.7	52.8	50.8	46.2	47.4	49.4
Bolivia	42.4	38.5	41.4	35.0	16.8	-	-
Brazil	47.0	49.9	49.6	46.1	48.3	-	-
Ozile	28.6	45.5	49.5	54.2	58.5	61.5	38.0
Colombia	39.1	45.2	46.7	45.1	41.8		-
Costa Bin	49.7	48.1	47.1	47.4	45.7	49.9	44.2
Dominican Republic	325	40.0	990	96.7	24.5'	220	25.1

Ecuador	25.4	31.7	49.1	40.2	98.5	98.2	95.1
El Salvador	-	52.5	49.1	49.8	39.4	38.5	55.6
Guatemala		46.9	42.1	34.4	40.1	24.2	27.2
Guyana	22.6	17.6	16.7	17.9	12.0	14.6	10.2
Haiti	23.6	27.8	592	99.4	45.5	440	-
Honduras	92.2	94.0	30.4	29.7	52.7	29.8	27.6
Jamaica	57.4	92.5	95.8	35.4	54.2	90.0	29.9
Mexico	23.4	24.7	20.0			-	-
Nicaragua	34.1	42.9	32.8	99.9	26.7	18.1	-
Panama	90.2	26.8	29.6	28.5	28.0	922	
Paraguay	19.1	38.5	58.7	37.6	41.5	46.0	46.0
Penn		26.3	15.4	17.9	-	26.0	26.4
Sudnune	921	58.9	25.6	40.5	41.9	90.0	
Trinidad and Tobago	-	49.8	54.0	52.8	51.4	53.1	50.1
Uvguay		49.9	51.2	49.8	54.4	50.5	-
Venrxuela	32.2	28.7	953	903	92.2	35.4	-

SOURCE: 1DB, based on official figures.

rapidly. This is indirectly reflected in the fact that, *although* overall public sector expenditures declined in most countries, the proportions allocated to social services also declined in 1984 compared with 1980 levels (table 9).

In the face of continued growth in the population, increasing unemployment and underemployment, and declining *real* incomes, the pressures on available social services severely restricted accessibility and quality. Recent studies for five countries of the region,[4] focusing mainly on urban areas, indicate that declines in public social outlays imply a deterioration in the distribution of income in every case and a significant increase in the percentage of the population under the poverty line.

General Social Conditions

The combined impact of rising unemployment and underemployment, declining real income and deterioration in its distribution, and reductions in the level and quality of public social services on general social conditions - especially on the poor - are only now becoming apparent. While the social effects of the crisis, in contrast with the financial and economic effects, have been slow in emerging, the damages inflicted are more difficult to reverse, and the consequences are likely to be felt far into the future. The evidence, though sketchy, is compelling. There has been a serious deterioration of physical infrastructure in the education, health/sanitation and housing sectors: erosion of teacher salaries, increased student/teacher ratios and overcrowding of facilities, shortages of books and materials, increasing incidence of nutrition-related ailments, fewer facilities providing health/nutrition services to pregnant women and nursing mothers, scattered evidence of lower birth weights, and increased child abandonment and youth delinquency.

While it would be imprudent to be alarmist about these apparent trends, it would be equally unwise to ignore them, since their generalization within the region would have serious implications for medium and long-term productivity and for the region's capacity and resilience to respond to the accelerating technological and competitive challenges which lie ahead. Moreover, they are concerns *which* should trouble not only the national policy makers of the region, but also external creditor banks, bilateral agencies and multilateral financial institutions.

Conclusions

Even if the population growth rate continues to decelerate for the rest of the century, the growth rate of the labor force will remain relatively high, since it is determined largely by the past rate of population growth, with something on the order of a fifteen-year lag. The crucial imperative for the medium term will therefore have to be a search for development strategies that are employment-intensive in order to stop the erosion in standards of living that has been under way in the region since 1980. A continuation of this erosion could intensify social and political instability, which would in turn render the implementation of development programs even more difficult.

This will involve a rethinking of the short-tern emergency measures which were initiated by governments of the region in an effort to counter the adverse effects of the economic crisis on employment, with a view to seeking the structural changes necessary to expand employment at a more acceptable rate. While this will require a recovery in overall investment levels - which declined by about 30 percent in real terms between 1980 and 1984- a conscious effort will need to be made to emphasize activities with high employment effects. Indeed, even under optimistic conditions, anticipated growth rates in output are likely to be inadequate to generate the levels of employment necessary to keep up with the growth of the labor force, unless higher employment/output elasticity's can be achieved through careful project identification and design. In this connection, some sacrifice might have to be made on labor productivity, especially with regard to nontradeables, in order to expand employment. Continuation of the 3 percent per year growth in labor productivity which was achieved in Latin America during 1960-80 (equal to that in the OECD countries) would require a (3DP growth rate of 6 percent - a difficult target in itself - but would leave unemployment rates at their already dangerously high levels.

While strong efforts will have to be made to intensify the process of employment generation, mainly in the private sector, in order to improve the standard of living of large segments of the population in the medium to long run, there will still be an important *role* for the public sector: first, to ensure that the policy environment is appropriate to induce the desired employment expansion; and second, to continue to take measures to improve conditions for segments of the low-income population which cannot participate in the work force, or for whom employment opportunities are slow in coming. Indeed, since the current tight fiscal situation can be expected to continue for some time, a deliberate effort will have to be made to channel efficiently the limited resources which will be available for public social outlays to the most needy social groups. This will invariably require fundamental changes in the structure of existing social programs - changes which could be facilitated by new financing mechanisms by multilateral institutions. In particular, multilateral institutions can help to finance the transition toward more targeted social services and to fee structures that guarantee access to the poor but avoid unnecessary subsidies.

In the end, the region's capacity to service its debt in the longer run while stopping the erosion of social conditions will be possible only if strong economic growth is resumed. This will require a restructuring of much of the region's current stock of external debt to permit the needed recovery in the levels of producer imports and of investment. At the same time, the productive use of imported capital and intermediate goods and the efficient allocation of investment will necessitate continued improvements in internal policy environments and increased market access in the industrialized countries. Obviously, these are difficult conditions to achieve, but their attainment would clearly benefit all parties concerned.

Notes

l. Argentina, Brazil, Colombia, Costa Rica, Chile, Mexico, Pens, Uruguay end Venezuela.

2. IBRD, *Poverty in Latin America: The Impact of Depression* (1986), p.2.

5. UNICEF, Impact of World Recession on Children (1984).

4. See mB/ECIEL, "El Gazto Publim Social en America Latina y ma Effectors Distributives" for Argentina, Chile, Costa Rica, Dominican Republic and Uruguay, mimeo graphed (1985).

CHAPTER 19

The Human Costs of Adjustment in Zambia

B. R. Kabwe

Human development has been the centerpiece of Zambian policy since independence. At the same time, Zambia has been negatively affected by an inordinately large number of adverse forces which have both retarded human development and prevented the full utilization of the human resources at hand. This paper will discuss these forces, as well as Zambia's continued and serious efforts to adjust, a fact acknowledged by all commentators. Zambia may even prove to be a textbook case of the harsh choices involved in the adjustment process.

Setbacks to Economic Growth

The economy of Zambia since independence (1964) has been affected by a number of forces which have prevented growth on a continuous basis. Zambia has had to adjust to a long series of shocks involving a number of interrelated factors.

The first major shock came within a year of independence after Rhodesia's (now Zimbabwe's) unilateral declaration of independence (UDI). Zambia, as a landlocked country, was heavily dependent on Rhodesia not only for transport mutes but also for manufactured goods. The UDI imposed enormous costs on Zambia, thereby deflecting many development efforts. Although the world copper market was buoyant, the high cost of transportation by road and air absorbed foreign exchange which could have gone for human development.

The Zambian economy has suffered a prolonged period of contraction since 1975. Various factors have contributed to this situation, including heavy reliance on a single commodity export, i.e., copper, for more than 90 percent of foreign exchange earnings; the heavy import dependency of the existing economic structure; and a sharp deterioration in Zambia's terms of trade (70 percent

during the decade), which has greatly reduced Zambia's import capacity and resulted in underutilization of existing capacities in the economy. Hence, in 1982 the country was forced to suspend external debt service payments through the Paris Club debt rescheduling system.

The interaction of the various factors outlined above has contributed to Zambia's current economic crisis. These movements, of course, have been reflected in the balance of payments, where a surplus in current accounts in 1970 has been replaced by a series of deficits which amounted to several hundred million kwacha in 1984. Partial adjustment was achieved through a reduction of imports, which averaged an 8 percent decline from 1973 to 1984. Borrowing, of course,, was a second consequence. External public debt increased fourfold from 1970 to 1984. As a share of GDP, this debt rose from 36 percent to 114 percent. Similarly, debt service as a share of exports has increased and is projected to be 82 percent in 1986.

Related to the above is the world recession in industrialized countries and high interest rates in the early I980s. Although the world economy has experienced a weak recovery in the last few years, the demand for Zambian copper has been restrained by restrictive monetary and fiscal policies in Europe and Japan and by the United States' attempts to deal with its own balance-of-payments problem.

Population Growth and Unemployment

Zambia is also struggling with a severe population problem. The rate of population growth is estimated at 3.3 percent per annum, while the total fertility rate is 7.2. The labor force is growing at an average annual rate of 3.8 percent. The implications for the development of human resources are serious: a declining resource base must be distributed among a growing number o£ Zambians.

Since 1980, the growth in employment opportunities in Zambia has lagged behind growth in population. In fact, formal sector employment declined from 381,490 in 1980 to 365,260 in 1984. This represents a reduction in total employment of 4 percent over this period. The unemployment situation in the country has worsened due to the high rate of increase in the labor force on the one hand and the decrease in formal employment on the other.

Zambia has already had more than its share of obstacles to overcome. Nonetheless, it may be that the worst is yet to come. Being landlocked continues to expose Zambia to political shocks in southern Africa, now largely created by South Africa. In August 1986, South Africa, placed restrictions on goods shipped to Zambia, which, among other things, could cut off Zambia's supply of mining equipment. Although there is sea access through Tanzania, increased use of that route would be costly. Furthermore, given the depressed conditions of the Zambian economy, the consequences could be far more serious than the unilateral declaration of independence noted above.

Human Resource Implications

The Zambian government has long recognized human resources to be one of the most important instruments of development. Man is the reason and agent for development, and therefore, the hub of all economic activity. Thus Zambia aims to create an egalitarian society in which there is equal opportunity for self-development for all. Problems of human resource planning, development and utilization constitute a very important element in the overall socioeconomic development of Zambia. With independence, the government initiated an ambitious program of institutional and human development, both of which had been sorely neglected. For example, in 1964, the country had barely 100 university graduates, 1,000 school certificate holders and a few technicians. The country was thus faced with very serious manpower problems at independence. Urgent political decisions were taken to correct this situation. The first was to provide free education to all, from primary to university level. The next was to provide free medical services in order to ensure the physical and mental fitness of all citizens. These two policy decisions have helped to change the situation for the better.

Zambia's progress in the field of education has been impressive since independence. Compared to 1964, enrollment in primary, secondary and technical education had increased by 155, 520 and 336 percent respectively by 1978. Primary and secondary school teacher training had increased by 140 and 2,248 percent respectively. The University of Zambia, which opened in 1966, had more than 3,000 students in 1978. By 1978, about 97 percent of children aged

7 years were estimated to be in grade one, and the total enrollment in primary education was about 84 percent of the relevant age group.

In spite of the progress noted, economic conditions of the late 1970s and early 1980s seriously hindered Zambia's emphasis on educational development. For the planning period 1980-84, it was necessary to sharply curtail planned expenditure. In comparison to projected outlays, only 16.1 percent was authorized, while actual expenditure was further reduced to 14.6 percent of initial projections. This austerity led to a deterioration in the quality of education. For example, in primary education, the number of pupils per class increased from 40.4 to 43. Moreover, instruction was hampered by shortages of textbooks and teaching materials. A declining quality at the primary and secondary levels clearly limits further academic, technical and professional education. This, in combination with limited facilities for higher education, has led to an influx of school leavers into the labor market with unmet aspirations.

Although Zambia has invested heavily in the expansion of education at all levels, there are still gaps between the output from education and training institutions and the requirements for differential skills in various sectors of the economy. This problem may be attributed to the fact that in the past, the educational system in Zambia did not emphasize mathematics and science, which are critical in the development of most professional and technical skills, e.g., engineering, medicine, accountancy, etc. The government is now taking steps to strengthen the teaching of mathematics and science in both primary and secondary schools in order to overcome this particular problem.

Despite these achievements, Zambia still suffers serious limitations with regard to human resource development and utilization. The first major handicap for Zambia is historical. Lack of adequate

educational facilities for Africans during the colonial era posed a serious manpower constraint during the post-independence era. For instance, in 1968, the Zambia Industrial and Mining Corporation (ZIMCO), which constitutes a major part of the government economic sector, inherited Zambian manpower, which was concentrated . mainly in the unskilled occupations. In the companies which were taken over, most of the expatriate manpower opted to leave, thereby creating a performance gap. As a result, a number of Zambians moved into jobs for which they did not have the required skills and training.

In the management field, about 66 percent of positions were occupied by Zambians. The report of the Zambia Managerial Manpower and Training Needs Survey of the Private and Prostates Sectors (1977) noted in its conclusions that "a very high percentage of non-Zambians (34 percent overall) occupy the 27,000 management and supervisory positions estimated as existing in Zambian industry. This expatriate figure is even higher (69 to 81 percent) for specific senior management posts such as General Manager, Deputy and Assistant General Manager, Company Secretary, Production Manager, Works Manager and Financial Manager." Although strides have been made in ZIMCO since 1968 toward training Zambians to fill key positions, there still exists a need to intensify training in the fields of engineering, accountancy, management and agriculture, which are still problem areas. ZIMCO has, therefore, adopted a development and training system for its manpower through the introduction of a Corporate Planning and Job Evaluation Department at the head office level.

Regional and International Cooperation

The shortage of appropriate skills for various sectors of the economy is a national problem. Thus, manpower development in terms of education and training programs can *only* be meaningful if such programs are tailored to specific pectoral manpower requirements. This inevitably requires huge investments in human capital. Given the current economic crisis, it is not possible for Zambia to resolve her problems regarding human resource development single-handedly. The government of Zambia can hardly afford these financial outlays. For this reason, Zambia is an active member of the Southern African Development Coordinating Conference (SADCC) Manpower Council, the Eastern and Southern Africa Management Institute (ESAMI) in Arusha, Tanzania, and other African institutes. This coordinated approach to human resource development at the sub regional and regional levels should ensure effective utilization of limited resources for common purposes.

Zambia has also been receiving generous financial and material support from the international community for human resource development. Donors include the World Bank, the African Development Bank (ADS), SUM, CIDA, FINNIDA, USAID, NORAD, the

British Council, the Republic of Ireland, UNDP, UNFPA and ILO. The full list would be much longer. These organizations have invested directly in infrastructural development, provision of teachers, and funding of scholarships and fellowships.

Country Initiatives

The government has set up institutions and administrative procedures to facilitate the progress of human resource development and utilization at the national and sectoral levels. Manpower development at the national level is coordinated by the National Commission for Development Planning through its Manpower Planning and Research Department, which is also responsible for population matters. The role of the department is to provide regular labor market information, to prepare national manpower planning and training strategies, and to carry out research into labor market issues.

The government has decided to establish a manpower council under NCDP in order to improve coordination between sectors of the economy. The council will be a tripartite body representing the government, employers and trade unions. The Department of Manpower Planning and Research will act as secretariat to the council. These measures are expected to improve efficiency in the formulation of policy. For example, coordinating information and research among the agencies dealing with various facets of manpower will maximize the benefits of research. Moreover, sound policy conclusions will lead to better utilization of human resources. Noticeable progress has already been made.

Such are the achievements and limitations of human resource development and utilization in the Zambian context, and the continuing efforts Zambia is making to resolve its problems. Success will not be achieved overnight. It will require major country efforts, including the effective implementation of the policy initiatives outlined above. Zambians are under no illusions about the sacrifices involved and the political will required to face them. Success will also require continued, appropriate and timely assistance from donor agencies. A final necessary condition will be an international environment within which the combined efforts of Zambia and foreign donors can bear fruit.

CHAPTER 20

Adjustment and Recession The Human Impact in Africa

Before discussing the impact of adjustment and recession on human development in Africa, it is useful *to recall* the three major objectives of adjustment policies in sub-Saharan Africa :

a) Reestablishment of a viable balance-of-payments position. b) Reduction of the inflation rate.

c) Creation of favorable conditions for sustained economic

growth.

The balance-of-payments objective, which is the most crucial, is the reduction of a sustained deficit in current transactions which can be financed by long-term capital without too much disturbance of debt servicing,

Consequently, adjustment programs in sub-Saharan Africa generally foresee a reduction of current deficit in public finances, calculated as a percentage of the GDP. For example, if the deficit is 10 percent and the target is 4 percent, then a three-year adjustment program would aim for an annual reduction of the deficit by 2 percent.

Since IMF resources are limited and have a relative aspect, the IMP cannot reasonably support an adjustment program without sound assurance that the major objective of restoring the balance of payments will be reached, A simultaneous reduction of the inflation rate is obligatory to reinforce the external position of the given country.

The main actions taken by each sub-Saharan country differ from one country to another, but generally, we can classify these actions into two categories :

a) If the target is to reduce or even suppress imbalances *which* derive from an excess of internal demand compared to a shortage of available financial resources, the action will consist of reinforcing the management of internal demand,

b) If the target is to reduce imbalances related to structural problems, then the action will aim at suppressing the structural weaknesses.

As a matter of fact, most sub-Saharan countries opt for managing domestic demand. This domestic demand management policy leads to certain classical measures, such as containing the money and credit rate of expansion, a restrictive budgetary policy, and a sound credit policy.

These being the main features of adjustment policies in sub-Saharan Africa, what is the impact of adjustment on human development in this area of the world? Two major questions emerge:

a) How vulnerable are sub-Saharan African economies to external shocks?

b) What type of adjustment is really suitable for these countries?

Vulnerability

The world economy during the last few years has been characterized by sharp increases in energy costs, inflationary tendencies, high rates of interest, a very broad range of exchange rates, and a fall in the demand for raw materials such as those exported by sub-Saharan countries. These factors were a result of recession in the industrialized countries, but they constituted serious obstacles to accelerated growth in Africa.

For some years, the structural weaknesses of African economies have been evident, and most countries have moved toward adjustment. Many African countries have requested IMF technical assistance in setting up and implementing adjustment programs. Adjustment has become compulsory, since no country can survive for long with serious economic imbalances.

But the process of generating growth is nothing more than planning and implementing efficient and value-added actions which aim at increasing the national productive capacity. Therefore, a viable growth policy involves an adjustment policy aspect which can be implemented with or without the IMF, or with or without the "package deal."

Adjustment Alternatives

If sub-Saharan African countries hesitated for a long time before undertaking vigorous adjustment efforts, it is because adjustment programs were not conceived to solve their structural difficulties. Besides obstacles to growth presented by the international economic environment, these countries also had to face very hard climatic conditions, such as drought, which seriously affected agricultural and livestock production. Their economic stmcture, based mainly on agricultural production, broadly depends on water supply. As a consequence, it becomes obvious that all these weaknesses cannot be corrected exclusively by means of classical adjustment measures.

From the African governments' point of view, development can never be dissociated from adjustment policies, provided internal economic policies are better defined. Domestic demand management is intimately connected with production policy. The question is: in a poor country, shall we request a hungry man to further reduce the level of his daily consumption, or shall we give him the means to increase his production? This is the dramatic choice we are facing in sub-Saharan Africa. Unfortunately, this reality is not always ac*knowledged* by our foreign partners. However, we must recognize that investment policy in the public sector has not always been rational. The adjustment process should lead African decision makers to a better allocation of financial resources and to a meaningful increase in directly productive investments.

In sub-Saharan Africa, which is one of the poorest regions in the world, the average income level is *very* low. Thus an adjustment policy which results in cutting down buying power over a long period is not well adapted to the situation of countries in which people cannot even satisfy their basic needs.

If we recognize that adjustment is linked to development, we cannot afford to neglect its social and human implications.

In fact, there is a limit to any country's capacity to adjust its internal policies to world economic conditions - in other words, to the industrialized countries' economies. Any review of internal economic policies should be carried out together with a review of the nature of the economic and financial relationship between the industrialized and the developing countries. Adjustment and development are undoubtedly complementary, but international cooperation is also necessary to ensure a more equitable direction of world economic growth in favor of the raw material-exporting countries.

No attempt to design an adjustment regimen suitable for sub-Saharan countries can fail to address the question of financial resource planning. The capability of families, enterprises and the public sector to generate domestic savings remains weak in these countries, despite some incentives set up to mobilize savings. Thus, savings levels are low, and export income suffers from great instability. Moreover, adjustment program financing comes mostly from overseas, at high rates of interest and on inflexible conditions for reimbursement. Consequently, a sub-Saharan African country has little chance of successfully carrying out an adjustment program if it cannot rely on stable and even soft terms of assistance, with the leeway to plan its allocations over the long term.

All these considerations do not imply that African governments are looking for easy solutions when they discuss adjustment programs. They do not want to take refuge in arguments aimed at demonstrating the weaknesses of the present approach to adjustment. Their sincere wish is that the international community will help them to find pragmatic and appropriate solutions which will make adjustment not a death sentence, but a means of recovery.

One example of the dramatic social implications of adjustment comes from Tunisia, which two years ago suffered a social revolt which became known as the "bread revolt." This explosion was the unpredictable consequence of a decision taken by the Tunisian government to cut subsidies on bread. So far, about twenty sub-Saharan countries have initiated adjustment programs with IMF assistance. It would be unfortunate if the results resembled the Tunisian case.

Sound internal economic policies are compulsory for African recovery, but the leading role must be played by international cooperation.

The Human Dimension in Benin

For many years the government of Benin has been fully conscious of the importance of the human dimension in economic planning. Concrete and decisive actions have been taken in two main sectors: education and health. The educational system in Benin is ruled by Law No. 75-30,

dated 23 June 1975. Under the provisions of the law, the guidelines

for national education are as follows:

a) The goal is the full integration of education into society. b) Education is compulsory and free of charge.

c) Students must gear their studies toward a practical profession.

d) Academic instruction is intimately associated with national production.

e) The government will do its best to guarantee employment for graduates.

It is clear from these guidelines that academic education in Benin is coordinated with employment and economic growth. The implementation of this law has resulted in a sharp increase in school attendance all over the country. From 1970 to 1983, the number of children attending primary schools increased from 155,225 to 428,185. In secondary schools, the number grew from 17,243 in 1970 to 132,395 in 1983.

University training is mainly oriented toward science and technology in order to provide the national economy with manpower in the appropriate quantity and quality. But the unemployment problem in Benin, as in other sub-Saharan countries, remains critical. In view of this, a policy to support small-scale industries and micro realization is being implemented with international financial assistance. Moreover, in 1985 the government set up a National Commission of Human Resources chaired by the Ministry of National Planning. The main task of this commission is to relate training to employment.

The second sector in which the Benin government has clearly demonstrated to its international partners its full commitment to the human dimension of development is the health sector. The health sector in Benin follows WHO guidelines for "Health for All by the Yea: 2000." To meet this objective, a comprehensive health program has been set up with the following guidelines:

a) Top priority is given to preventive medicine, especially in

rural areas.

b) Health coverage is being increased throughout the country, with appropriate infrastructure being set up in big cities as well as in small towns.

c)Sanitary infrastructure is being maintained and expanded.

d) Adequate supplies of medical equipment and medicines are ensured.

The main problem in the health sector is the financing of running costs. Due to the present critical public financial situation,

Benin requested some time ago that the EDF assist the government in financing part of the running costs. This request has been granted, and the agreement is now being implemented by stages.

In March 1983, the Benin government began its efforts to mobilize external financing for the Second Five-Year Plan. In this connection, the UNDP supported North South Roundtables have been particularly helpful to Benin. Unlike the World Bank Consultative Groups, roundtables are generally attended by a very broad range of donors, most of whom act in areas in which the major international institutions usually do not move, particularly the U.N. specialized agencies and NGOs.

The Benin government has now started preliminary discussions with the IMF and the World Bank. Our sincere wish is to convince these institutions that adjustment must have a human face. Toward the achievement of this end, a broad debate under North South Roundtable auspices on global economic interdependence would benefit the countries of sub-Saharan Africa and other developing nations.

CHAPTER 21

The Role of the Human Element in the Development of Korea

Ahn Seung-Chat

The impressive growth of the Korean economy over the past two decades is by now well known. From the poverty and strife of the years immediately following the Korean War, Korea has brought itself economically to the forefront of the newly industrialized countries. Its progress was built on real GNP growth rates that averaged 9.5 percent from 1965 to 1975 and 7.4 percent between 1975 and 1985. These economic strides and a falling population growth rate made it possible for per capita GNP, only US$ 105 in 1965, to soar in two decades to a respectable $2,032.

This remarkable success raises a number of important policy questions. First, what were the major sources of past economic growth in Korea, and specifically, what was the relative contribution of the human element in the economic development process? Second, can the economy sustain its high growth rates in the changed future environment, and what will be the role of Korea's human capital in that search for growth?

Before addressing the questions listed above, a brief summary of the government's role in Korea's recent development will provide a useful background to the discussion of the state's policies for fostering the growth of human capital. A distinctive feature of Korean economic development strategy, as compared with that of many other nations, has been the government's choice during the past quarter-century to allow a series of five-year economic plans to play a leading role in economic growth. The first five-year plan was announced in 1962, when the industrial base of the economy was very weak.' Under the rather primitive industrial structure, the market system could not function effectively; this necessitated government orchestration of the development strategy.

Initially, the government's economic development, strategy focused on expanding the size of the economy. Serious supply-side

pressures. in the Korean labor market made this emphasis necessary. These pressures stemmed not only from a continuously growing population, but also from a persistent movement of the labor force from the rural to the urban sectors.' The emphasis of economic policies, therefore, had to be placed on enhancing the economy's ability to absorb the increasing labor force into the modernized industrial sectors.

Successful economic growth during the first four development plan periods spurred progress toward important economic goals, such as reducing the number of those in absolute poverty and expanding employment opportunities. Concurrently, policy makers paid little attention to social welfare issues until the end of the Fourth FiveYear Plan; the government has therefore made substantial investments in social development programs since the early 1980s. Two central policy issues in the upcoming Sixth Five-Year Plan (1987-91) are industrial structural adjustment and the promotion of social welfare. In short, while quantitative expansion of the economy has been the central policy goal of the past, improvement of the quality of life will receive greater attention in the future.

Labor Input into Korean Economic Growth

The adoption of outward-looking development strategies initiated an era of very rapid economic growth for Korea. As shown in table 1, between 1965 and 1985, GNPgrew by 8.3 percent annually in real terms,, far exceeding the average growth rate of less than 4 percent among developed nations for the same period. Real GNP in 1985 had risen to five times that of 1965. During that period, the population size increased by only one and a half times (a 1.5 percent annual increase), while the employment size tripled (a 1.8 percent annual increase). Per capita GNP in current U.S. dollars increased by 16 percent per year.

TARLE t

Performance of the Korean Economy

-1965-85					
Annual Average Growth					
1965		1975	1985	Rate	
(A)		(B)	(C)	(%)	CIA
GNP				`	
1980 prices: trillion wan	10,6	26.1	52.6	8.8	5.0
(Current prices: billions)	(9.0)	(20.9)	(s9.1)		
Population	28.7	35.3	41.6	1.9	L5
(minion)					
Employment	8.2	11.8	14.9	9.0	1.8
(million)					
Per Capita GNP	105	591	2032	,15.0	19.4
(cunentprices, $)					

SOURCE; Korean Economic Indicators, Economic Planning Board, June 1986.

If Korean and foreign policy makers are to learn from Korea's past growth, they must be able to assess the relative importance of the various factors contributing to economic advancement. The estimated sources of Korean economic growth during the past two decades are reported in table 2, along with comparable figures for some developed nations! As indicated in the table, the standardized growth rate of Korea from 1963 to 1982 is estimated at 8.1 percent - slightly lower than that of Japan during its high-growth period (8.8 percent), but substantially higher than the rates for most other developed nations. For the case of the Korean economy, the relative contribution rate of labor input to economic growth turned out to be substantially higher than the rates for capital and other factors. By breaking down labor input into several subcomponents, we find that the three most important factors *were* employment, hours of *work* and education. The relative contribution rate of labor input was 40.7 percent, more than twice the contribution of capital (19.4 percent). Other important factors that helped drive high economic growth were economies of scale and advances in knowledge.*]*

TABLE 2
An International Comparison of Sources of Growth of
Standardized Growth Rate of National Income
(In Percentage Points)

West				
Korea		Japan	France	Gemany
Item	196382	1953-71	1950-62	1950-62
Standardized growth rate	8.13	8.81	4.70	6.27
(100.0)		(190.0)	(100.0)	(100.0)
Labor	3.31	1.85	0.45	1.57
(40.7)		(21.0)	(9.6)	(21.9)
(Employment)	2.18	1.74	0.08	1.49
(26.8)		(12.9)	(1.7)	(23.8)
(Hours of work)	0.45	0.21	-0.02	-0.27
(5.9)		(2.4)	(-0.4)	(-4.3)
(Education)	0.39	0.94	0.29	0.11
(4.8)		(3.9)	(6.2)	(1.8)
Capital	1.58	210	0.79	1.41
	(19.4)	(29.8)	(16.8)	(22.5)
Advances in knowledge	1.09	1.97	1.51	0,87
	(13.4)	(22.4)	(32.1)	(19.9)
Improved resource allocation	0.66	0.95	0.95	1.01
(8.1)		(10.8)	(20.2)	(16.1)
Economies of sole	1.49	1.94	1.00	1.61
(18.3)		(220)	(21.3)	(25.7)

NOTE: Numbers in parentheses represent relative contribution rates (in percent). SOURCES:

Kim Kwangeuk and Park Joon-kyuag, Sources of Economic Growth in Korea: 79537982 (Korea Development institute, 1985); Edward F Denison, Accounting for Slower Economic Growth: The United Stares in the] 970s (Brookings Institution, 1979).

International comparisons yield several interesting observations. First, the relative contribution rate of labor input was much lower for other nations than for Korea. Second, except in Korea and Japan, the number of hours worked has been negatively correlated with economic growth, reflecting a recent decline in working hours in most developed nations.[4]

Third, it is interesting to find that the relative contribution rate of capital was approximately equal in all nations studied, ranging between 19 and 24 percent. This result probably reflects the relatively high mobility of capital in international markets as compared to that of other factor inputs, such as labor and technology. Finally, the role of knowledge advances in economic growth was lower for Korea and West Germany than for other nations.

Both in absolute and relative terms, Korea achieved its high economic growth mainly through the contribution of labor input. , Table 3 traces the changes in the components of labor input over the past two decades. Total employment increased most rapidly, reinforcing the earlier finding that labor force growth contributed more heavily than other factors to economic growth. Average weekly hours worked and labor quality changes due to education rose more slowly than employment. Regarding hours worked and quality changes, the increase in the index is primarily attributable to higher values of the index among new labor market entrants rather than to an overall increase in the index value of the existing labor force. For example, average hours worked have increased slightly over time, but the main reason for the increase in the hour index is the composition change: a higher proportion of new entrants than of those already working have found full-time jobs. By the same logic, for the case of educational attainment, new entrants have acquired substantially higher levels of education, which consequently increases the overall index average.

TABLE 3
Indices or labor Input in the Korean Economy
(Nonresidential Business Only)
(1972.100)

Labor					Efficiency	
Quality					Gain Due to	
Average			Agc•Sea	Change	Reduction	Total
Total		Weekly	Composition	from	in Weekly	Labor
Year	Employment	Hours	of Workers	Eduation	Houn	Input*
	(I)	(2)	(3)	(4)	(5)	(6)

1963	75.5	98.4	100.1	95.6	99.8	64.1
1966	80.8	93.7	100.5	96.4	100.1	75.1
1969	89.3	99.2	101.8	97.9	100.9	89.1
1972	100.0	100.0	100.0	100.0	100.0	100.0
1975	112.0	104.9	100.6	102.5	100.1	121.9
1979	128.5	107.6	102.1	105.9	100.2	149.9
1982	134.8	107.4	102.5	107.3	100.8	160.5
Average annual rate of increase:						
1965-72	5.5	0.8	0.0	*0.7*	*0.0*	5.1
197282	9.0	0.7	0.3	0.7	0.1	4.9

Obtained by multiplying the first five elements.

SOURCE: Kim Kwang.suk and Park Joon-kyung, Sources *of Economic Growth in Korea: 1963-1 982* (Korea Development Institute, 1985).

Manpower Development Policies

In the late I980s and I990s, Korea will face an economic environment very different from that in which it prospered over the last two decades. The slow pace of structural adjustment in the developed countries has fed protectionist sentiments there, tightening the market for Korean exports. Rising domestic wages have also raised unit labor costs in some traditionally important export sectors. In response, and as the next stage of its development, the Korean economy must undergo its own process of adjustment. Moving into high-technology industries and entering the information age will mean facing direct competition with the advanced economies. To do this successfully, Korea will require a new, technologically literate labor force. A review of recent education, manpower training and welfare programs draws on the lessons of past experience to suggest policies for the future.

Educational Expansion

School enrollment has increased dramatically over the past two decades. In Korea, compulsory education covers only six years in primary school, but there has been a heartening change in the entrance rate to middle school. In 1965, only 54 percent of the graduates of primary school entered middle schools, but by 1985, 99 percent did so. The entrance rate to high school also increased considerably, so that 90 percent of 1985 middle school graduates advanced to high school. Finally, the government's decision to increase the college enrollment quota in 1981 by about a third has expanded the number of university students. In 1985, about 36 percent of high school graduates entered colleges; the comparable figure for Japan in 1983 was 30 percent. In fact, Korea's college entrance ratio may now be the second highest in the world, next to that of the U.S.

The continued expansion of educational opportunities has contributed to a vast improvement in the educational background of the labor force. The ratio of employment of college graduates to total employment increased from 2.4 percent in 1960 to 8.9 percent in 1980; a 1985 population *survey* estimated that the ratio already exceeded 10 percent. The figure for high school graduates also increased sharply, from 7.4 percent in 1960 to 26.7 percent in 1980.

The rapid expansion of the student population at all levels of schooling was made possible in part by the continued growth of government expenditure in education. On the other hand, it should be noted that the private sector has also been integral to educational expansion. The share of private schools in Korea's secondary and higher education is fairly high - 65 percent for high schools and 75 percent for colleges. For these private institutions, student tuition constitutes the major source of revenue.

The strong demand for higher education observed in Korea has a twofold explanation. First, the social value of education is traditionally high in Korea. Social prestige is often directly correlated with educational attainment. The country's lower status in educational achievement during the early 1960s was due mainly to an underdeveloped system of formal education rather than to low educational desire. A second answer, somewhat related to the first, is the economic explanation. The wage differential between high school and college graduates is quite large in Korea, probably much larger than in most European nations. The main cause for this gap is that the number of college graduates was quite small in absolute terms until the mid-! 960s and scarcity drove their average wages up. This gap has persisted, fostering aspirations for college education.

Manpower Training Programs

For some time after the adoption of an outward-looking development strategy in the mid-1960x, labor absorption in the Korean economy took place mostly in the labor-intensive industries in which the skill level required of laborers was minimal. There was, therefore, no shortage of skilled manpower in the early years of industrial expansion. As the industrial structure deepened in recent years, however, special attention was given to expanding the capacity and improving the quality of vocational education and training both within and outside the system of formal education.

Technical high schools and junior technical colleges, as well as four-year engineering colleges, began to increase their enrollment at government initiation. Within this group, the technical high schools are the most important in terms of absolute numbers of students. Specialized technical high schools produce technicians for special fields such as precision machinery, electronics and steel, while general technical schools provide a broader spectrum of skills. At present, 101 technical high schools produce 60,000 to 70,000 skilled workers each year.

The government has also established public vocational training centers throughout the country. Besides producing skilled workers, these centers have the added objective of providing training opportunities for workers from low-income families, thus raising their qualifications and enhancing their long-term career possibilities. Currently, twenty-five such training institutes recruit primarily middle school graduates for one to three years of vocational training. In recent years, however, the increase in high school entrance rates has made the recruitment of trainees more difficult. New directions for public vocational training are thus being explored.

The expansion of technical high schools and public vocational training centers has clearly helped industries to secure skilled workers. To encourage industries to make their own efforts to develop the needed manpower, however, the government adopted a training levy system in the 1970s. Under this program, a fixed tax is collected from those firms in specified industries that do not provide their own in-plant training. In large firms, in-plant training has served as a major source of skilled manpower. On the other hand, because such training programs are seen as a heavy burden for many smaller firms, the latter tend to look to the open labor market and public school graduates for their prospective workers.

Policy makers have continually tried to adapt the vocational education and training system to changes in the economic environment. To a large extent, they have succeeded. Manpower development efforts over the past twenty years have been integral to ensuring an adequate supply of skilled workers for Korea's economic development.

Social Welfare Policies

The government's recognition of the long-teen complementarily between economic growth and improved social welfare is reflected in the steady increase in government expenditures on welfare over the past decade. Table 4 shows that welfare spending's share of overall government outlays rose from 21 percent in 1974 to about 30 percent in 1955. As a percentage of GNP, welfare expenditures almost doubled over the same period, from 3.4 percent in 1974 to 6.1 percent in 1935[6]

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TABLE 4
Trends in Government Social Welfare Expenditures
(Percentage)

	1974	1978	1982	1985
As a percentage of government Expenditures	21.4	21,7	50.7	50,0
Education	12.9	19.7	17.0	16.9

Health	1.1	1.5	1.2	1.5
Social security	5.1	4.5	8,5	5.5
Housing	1.5	1.2	5.5	5.2
Others	0.9	0.4	0.7	1.0
As a percentage of GNP	5.4	5.9	6.9	6.1
Education	2.1	2.5	5.8	5.4
Health	0.2	0.8	0.5	0.5
Social security	0.8	0.8	1.9	1.1
Housing	0.2	0.2	0.7	1.1
Others	0.1	0.2	0.2	0.2
SOURCE: Budget Bureau. Economic Planning Board.				

Much of the increase in welfare spending during the past decade has been in education, which has a direct impact on productivity, and in housing, which is closely linked with organizational concerns. Between 1974 and 1975, the shares of education and housing in total government expenditure rose from 12.9 percent to 16.9 percent and 1.3 percent to 5.2 percent respectively. In comparison, the increase in spending on health and social security, the major components of social welfare in the narrow sense, has been minimal. Health expenditure as a percentage of total government outlays in 1985 was 1.5 percent, only 0.4 percent higher than in 1974. Likewise, social security spending increased negligibly, from 5.1 percent of government expenditures in 1974 to 5.3 percent in 1985. In the next few years, however, the government plans to introduce a national pension system and to increase the coverage rate of the medical insurance system quite substantially. Methods of financing these welfare schemes are being studied.

Concluding Remarks

An examination of the sources of Korean economic growth and development strategies over the past two decades reveals that the contribution of labor input to rapid economic growth was highly significant both in absolute and relative terms. In the past, the social and economic issues that the Korean economy faced were primarily quantitative; that is, the major objective of economic growth was the elimination of absolute poverty. Policy makers thus put their faith in quantitative means, relying on the large numbers of the growing labor force to propel economic growth. In the early stages of industrialization, the required level of skill was low, and thus the role of the education and training system was merely to produce a large work force with minimal skills.

Since the industrial structure began to deepen in the late 1970s, improving the quality of manpower has become an important policy issue. The need is particularly great in high-tech industries, which are expected to lead future economic growth. Highly trained scientists and technicians will play a decisive role in the development of these industries, making an effective manpower training system and an efficient educational system essential for further development.

For a country with scarce natural endowments, the importance of the human element in economic growth cannot be *over*emphasized. Proof may be found in labor's contribution to the Korean economy's past high-growth performance. The issue for the near future is whether Korea will be able to produce the necessary skilled scientists and technicians and to improve the overall quality of the work force.

Certain basic policy steps will greatly tmprove the chances of success. First, Korea should develop a manpower supply system that produces trainees who have the characteristics and skills sought by industry. Such a supply system would prevent situations like the present one, which suffers a surplus of college graduates with liberal arts backgrounds but a shortage of those with technical knowledge

i and experience. Second, since education has such extensive social effects, the relatively high proportion of private schools raises issues of balance between private and social costs and benefits. In Korea, private schools tend to supply work force mainly in areas where the private costs of education are cheaper. In this regard, the government

v should delineate separate roles for public and private education. Third, the government must enact policies to change the public belief that income should be determined primarily by educational credentials rather than by contribution to productivity. In other words, the quality of education and its social ramifications should *receive* greater attention.

The need to address these issues will be Korea's greatest chat leas in the near future. Perhaps the most important lesson that can be drawn from the Korean experience is that human capital should not be neglected. In retrospect, it seems clear that low domestic savings rates made foreign borrowing inevitable for the attainment of rapid economic growth. Furthermore, there is much evidence that foreign capital has contributed greatly to Korea's economic development. Nevertheless, Korea's high rate of economic growth could not have been achieved through the import of foreign capital had there not also been an abundance of well-trained manpower.

Because educational and welfare investments have a longer gestation period than physical investments, there is always the temptation for government not to invest in human capital during periods of economic recession or budgetary *stringency.* This is a temptation that must be resisted. Skilled and healthy human resources are essential for long-term economic and social development.

Notes

I. Agricultural production constituted about 40 percent of GDP, versus only

about 15 percent of GDP for manufacturing production. *Major Statistics of the Korean Economy.* Economic Planning Board, Korea (1985).

2. Population grew by 2.5 percent annually during the 1960, (as compared to l.5 percent in the 1980s), and the share of farm employment in total employment was 56 percent in 1965 (versus only 25 percent in 1985). Revised Fifth *Fbe.Yeat* Economic and *Social Deve7opmextPkn.: 1984.7986,* Government of the Republic of Korea (1985).

S. The estimation method b explained in detail in Edward F. Denlson, Why

Growth Rates Differ Poster Experience In Nine Western Counvkt (arookings lmdtudon,

1916). The standardized growth rates in the table are adjusted to factor out the estimated contribution of each convoy's special and ine€War factors.

4. in Korea's case, the number of hours worked has even increased silly in recent years: the average hours worked per month, 217 in 1975, inasased to 226 by 1985. *Year Rook o/ Us or Statistics* (Korean Ministry of Labor, 1985).

5. The source of educational statistics in this section is the *Year Book* of *Educm dorsal Statistics* (Korean Misdntry of Education, 1985).

6. Despite the increased emphasis on social development policy in recent years, government

spending on welfare is still considerably lower than In developed nations. in the U.S., for example, 50 percent of government expenditures go toward social welfare; in Swedrn, 60 percent.

APPENDICES

THE SALZBURG STATEMENT

Following the fall in commodity prices, thrrising debt service burden and a decline in real capital flows, a large part of the developing world - especially in Africa and Latin America- has experienced almost perpetual economic difficulties and crises during the 1980s. Consequently, many countries have had to undertake stringent adjustment programs. About two-thrds of the countries in Africa and Latin America have experienced sharp declines in income per head. There have been dramatic falls in employment and real wages, and widespread cuts in expenditure in the social sectors. The incidence of malnutrition among children is rising in a large number of developing countries.

The economic and social costs of the adjustment process of the I980s are under no circumstances justifiable or acceptable, even on the pretext of promoting growth. There have been substantial cuts in investment in most countries affected, while reductions in social sector expenditures, together with diminishing standards of nutrition, continue to undermine human capacities - the most important resource a country possesses, as well as the most basic objective of development. Moreover, these policies have not even been successful in establishing a viable external payments position, partly because of continued adverse external developments - including sluggish world trade, rising protectionism, falling commodity prices and high real interest rates - and partly because of inadequate domestic policies.

Furthermore, present trends are not encouraging. Indeed, in some ways, further deterioration is occurring. In spite of creditor complacency, which exhibits itself in a willingness to put together emergency rescue packages while waiting for world recovery, the recovery has been slow and halting and accompanied by further declines in raw material prices.

Aid pessimism is widespread and deepening; serious new protectionist pressures are being felt in many *large* industrial countries. The IMF and the World Bank, which have provided net resources to developing countries over the past ten years, are under present conditions likely to be net recipients of resources over the next five years. For most developing countries, this means there is no hope that the situation will improve. Meanwhile, the political and social tolerance for a further worsening of conditions - after years of austerity - is

sharply deteriorating. The social fabric of many countries accustomed to substantial *growth* in the I960s and I970s has held up surprisingly well to date, but such tolerance cannot be counted on indefinitely.

Human-Focused Adjustment

The human costs of current adjustment measures are unacceptable from a humanitarian perspective. *Nor* can they be accepted from an economic perspective. Fortunately, in most cases, the two perspectives are complementary and not competitive.

The health, nutrition, education and participation of the majority of the population are essential for economic growth. Reductions in social sector expenditures - and the waste of human potential and capacity associated with unemployment - will have long-term negative, perhaps irreversible, effects on the productive potential of the affected economies. The few historical examples of highly successful development and adjustment efforts demonstrate, above all, the. critical importance to development of investment in human resources. It is essential, therefore, to redefine the objectives and policies of adjustment programs. The objeeti.e of adjustment programs must be to achieve economic growth while protecting and promoting human development and pursuing equity-oriented policies.

The elements of this objective are mutually supportive and not in conflict, as is sometimes suggested. Medium-term external stability requires an expansion of exports and of import substitutes. Both demand a flexible, educated and employed work force. Policies promoting small-scale production - especially in agriculture and industry in rural areas - will generally help to promote growth, save on imports and also raise the incomes of the poorer sections of the population. Deflationary stabilization - typically achieved at the expense of the most vulnerable human beings - can bring only short-term balanee•of-payments relief -while undermining mediumterm prospects and political and social support for the program.

National governments and international institutions should immediately and publicly acknowledge, that successful adjustment can be achieved only by pursuing growth-oriented policies and safeguarding the human dimension as an integral part of the adjustment process. Pubiic acceptance of this objective is an essential first step toward identifying and introducing the changes necessary to achieve it.

There is no necessary conflict between the closely related goals of balance-of-payments adjustment, the resumption of growth and the protection and promotion of human development. Just because the burden of macroeconomic adjustment in the past has often been shared unequally, it does not follow that in well-orchestrated, internationally supported country programs this should be so.

If individual debtor countries take the initiative to adopt the required policy changes over a three- to five-year period with additional foreign resource commitments over the same period, growth can be encouraged while protecting and promoting the welfare of people at the lower end of the income distribution spectrum. The precise contours of such packages will differ from country to country. They will not be easy to formulate, nor to put into effect. The problem is not one of a technical conflict among competing objectives, but of the political will to take the necessary actions within the developing countries themselves and within the international community.

In order to facilitate policy change and help protect vulnerable groups, there must be a reorientation of domestic policy strategies, together with some expansion of external resources. For some countries, the development strategy must be shifted toward employment-oriented, rural-based development; for others, toward the productive integration of the urban informal sector, together with the diversification and expansion of industrial capacity and exports. These changes are possible. The obstacles lie with inadequate national and international policies.

Both North and South have a mutual interest in the attainment of growth-oriented adjustment. Growth-oriented adjustment among developing countries will expand markets for products from the industrialized countries, easing their intractable employment problems. With successful adjustment, debt servicing will be assured and international finical stability will increase. At the same time, the protection of human conditions and the achievement of economic growth *are* likely to increase world political stability.

National Policy Action

The precise policy package for adjustment with growth and human development will differ for each country according to paretic-ajar conditions, needs and opportunities. Several important elements are likely to play a part in most countries.

1) Adjustment packages should be as *expansionary* as conditions permit, with the objective of securing internal and external balance in the medium term. Current packages, in contrast, often have a very short time horizon and consequently contain major deflationary elements.

2) The generation of productive employment opportunities is a major means of protecting the incomes of the poor while promoting economic growth. In economies where the rural areas provide a livelihood for a very large section of the population - often accounting for the majority of the poor - this requires the efficient mobilization of the rural sector, both in agricultural and nonagricultural activities, with special efforts to promote the productivity of small farmers and small enterprises. In other economies, where urban poverty is very extensive, it is essential to focus on improving urban employment opportunities by extending resources and technology to the urban informal sector and by promoting the expansion of efficient industrial activities.

In addition to macro policies which do not discriminate against the agricultural sector, small-scale producers and labor intensive activities, programs require a willingness to decentralize public expenditure decisions and to support small-scale producers - small farmers and industrialists. Policies may include land reform, redirection of credit and the provision of infrastructure.

3) Because of the extreme scarcity of resources during adjustment, it is necessary to establish priorities so as to ensure that resources are devoted to those uses which are essential for adjustment, the protection of the vulnerable and the promotion of growth, in preference to uses of lesser priority. The systematic use of policy instruments - including taxation, credit, public expenditure and aid - will contribute to the achievement of the agreed priorities.

4) Essential services are inexpensive and may be extended to poor groups even during expenditure cutbacks by redirecting expenditures between and within sectors and by reducing waste. In the health sector, for example, a full immunization campaign in one country was paid for by postponing expenditure on an urban hospital for five years.

Most countries could effect major internal adjustments, thereby contributing to meeting priorities, by reducing the substantial

levels of inefficiency, opportunism and outright misallocation of resources in the economy. Through such means, it is believed, as much as a quarter of some national budgets could be reallocated. This potential is in addition to the major savings to be gained from a substantial reduction in defense expenditure.

5) The effectiveness of domestic markets would be much enhanced by reexamining and phasing out various government interventions likely to create private monopoly power and public corruption, e.g., license permits, exclusive market shares, price controls, and inefficient subsidies favoring privileged groups. One major explanation for the frequent failure of expenditure-switching policies on the supply side is the imperfect character of private markets.

6) Special measures may be necessary to protect the welfare of low-income groups during the adjustment period, before longer-term policies have time to take effect. These measures may include nutrition interventions to prevent intolerable levels of malnutrition, which have permanent effects on mental and physical capacities, and public works schemes to provide temporary employment and incomes to the unemployed while helping to rehabilitate and construct social and economic infrastructure.

7) It is important for developing countries to take the initiative in formulating and putting forward such programs when negotiating with the international community, making sure that these programs are fully understood, agreed upon and politically accepted,

International Action

Domestic policy change is essential, but without a change in the international environment, it will be difficult for developing countries to achieve adjustment with equitable growth. Several changes are needed.

1) There should be coordination among developed countries to secure sustained growth in world trade and output through interest rate reductions and reflection, especially in the surplus countries.

2) Additional mobilization of resources is needed for adjustment and development. This requires increasing both public and private financial flows. Policies include replenishment of the international institutions; measures to facilitate recycling of the surpluses

of rich countries; and the participation of commercial banks in country programs through new voluntary lending. For heavily indebted countries, it may be necessary to undertake substantial debt restructuring so as to reduce significantly their current debt servicing obligations.

3) Current General Agreement on Tariffs and Trade (GATT) negotiations must guarantee, at the minimum, a halt to new protectionist measures and should ultimately aim to roll back the formidable forces of neoprotectionism in the European Economic Community, the United States and Japan. The developing countries are being asked to restructure their economies, yet the developed country markets are gradually closing for imported industrial and agricultural goods. There is also increasing intervention by the industrialized countries to give artificial support to their exports of primary products and other goods. These forms of protectionism are making it extremely difficult (in some cases, impossible) for developing countries to earn their way out of the crisis.

4) The time frame for negotiating programs for adjustment with equitable growth must be extended to at least a three- to five-year perspective. In some cases, mostly among African countries, a longer time period is needed. Developing countries cannot reasonably be asked to make structural policy changes, the effects of which are painful and long-term, while the additional outside resources to ameliorate the pain are assured only over an eighteen-month period. It is not acceptable to ask debtor countries to overcome their domestic political economy problems at considerable risk while taking the position that nothing can be done about the donors' current political inability or unwillingness to make long-term resource commitments.

5) The increased flexibility being exhibited by the IMF in current negotiations with debtor countries is commendable. Particularly noteworthy is the inclusion in the current Mexican standby of provisions which include flexibility in response to unexpected external shocks, specifically due to fluctuations in the price of oil; which permit the exclusion of interest on the domestic debt from budgetary deficit calculations; and, most interestingly, which provide for additional external funding if, in the case of full compliance with the agreed terms of conditionality, the growth rate falls below 3-1 /2 percent. Similar efforts should be made within future agreements to buffer least-developed countries (LDCs) against exogenous shocks and focus conditionality on matters which are indeed within the

control of a developing country, while defining a minimum acceptable level of growth.

6) When packages are negotiated, policy actions by governments and international commitments should be directed toward the comprehensive objective of protecting the human dimension and promoting growth with human development. The components of policy discussion, conditionality and program monitoring should take all these conditions fully into account. Negotiations on adjustment should not be the sole province of finance ministries, but should also include those ministries concerned with the social sectors and economic development. On the international side, not only agencies associated with finance and economic development, but also those involved with the human dimension, should be associated with the formulation and

implementation of adjustment packages.

7) There is a need for special financial support for sub-Saharan. Africa and other small, low-income economies where the problems are most severe. The major share of the shrinking International Development Association (IDA) funds should be earmarked for those countries. Bilateral donors should convert their aid to such countries to no project aid on a grant basis and should forgive accumulated public debt.

Conclusions

The Salzburg Roundtable reached a clear consensus in three central themes:

I) Adjustment without growth and human development is both unacceptable and counterproductive. It is possible, indeed mandatory, for national and international policy makers to design such policy packages as will make adjustment policies compatible with growth and human development. The objective of adjustment programs must be to achieve economic growth while protecting and promoting human development and pursuing equity-oriented policies.
2) At the national level, this objective can be accomplished through a reorientation of domestic policies aimed at both the rural and the urban poor. New development strategies may be based on increasing the productivity of small farmers; expansion and diversifi cation of exports; reallocation of national budget expenditures toward basic education, primary health care and nutrition programs; the institution of low-cost programs in many sectors; reducing economic controls and increasing market efficiency; promoting small enterprises and providing trained manpower with productive employment; and creating an environment which will encourage people to realize their full potential.

3) At the international level, this objective can be achieved through additional resource transfers (particularly by reversing the present negative resource transfer from South to North); through modified conditionality, including the protection of growth and human resource development levels and a more medium-term perspective; by the maintenance of an open international trading system and the reflection of world demand; by providing additional resources for multilateral financial institutions; through the cancellation of public debts and the provision of long-term concesslonal assistance for low-income countries (notably in Africa); and through other measurers to provide debt relief so that savings may be allocated to investment, and not only to debt repayment.

The strenuous efforts of the world community over the past several years to overcome a series of crises - energy, food, debt - must not be succeeded in the future by a far more fundamental crisis: the crisis of human *development.* Though often tempting, short-term solutions should not be bought at the cost of creating less obvious long-term problems, including those of human environment. If that were to happen, the future of development efforts would have been mortgaged to the indirect effects of short-term adjustment policies in many parts of the Third World. Then, national and international decision makers would have failed to combine policy objectives which are essentially compatible, and to recognize that the fundamental objective-of all economic activity is the enrichment of human lives.

APPENDIX B
PARTICIPANTS AND CONTRIBUTORS

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APPENDIX C
NORTH SOUTH ROUNDTABLE

The North South Roundtable, established in 1978 under the auspices of the Society for International Development, is an independent intellectual forum in which academics, researchers and policy makers from around the world come together to discuss global development issues. The Roundtable brings together experts from every continent in many fields, all sharing a commitment to orderly progress in human affairs, for the advancement of a constructive dialogue between North and South, developed and developing, rich and poor nations, in search of a more just and stable world order. In its various sessions the North South Roundtable seeks to identify and analyze the most significant issues and to develop policy proposals in the mutual interest of North and South. The ideas evolved in the Roundtable process are disseminated to the general public, national decision makers and other international organizations through Roundtable publications and through direct briefings.

NSRT activities are funded by governments, international organizations and foundations; its policies are determined by a Steering Committee.

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UNDP DEVELOPMENT STUDY PROGRAMME

The Development Study Programme of the United Nations Development Programme (UNDP) was established by the Governing Council of the UNDP in 1981 in order to promote a greater understanding of the issues, strengthen public and governmental support, and generate new ideas and innovative solutions to the problems of development and technical cooperation. The activities of the UNDP Development Study Programme take different forms, such as seminars, lectures and informal discussion groups. Participants at the various events held under the auspices of the Programme are drawn from among high-level national policy makers, government representatives, senior officials of the United Nations Development System, leaders of public and private enterprises, representatives of the media and academics.

The UNDP Development Study Programme is financed by voluntary contributions from governments, international public and private institutions and foundations. Contributions include the provision of hosting facilities and collaboration in organizing joint seminars and meetings.

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APPENDIX D

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