The Political Economy of Sector Reform

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GTZ BBL

Political Economy of Sector Reform:
How can we promote Social Justice?

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Eschborn

SOcial Development Department
The World Bank
Political Economy of Reform – Key for Operations

What do we mean by...
- Political Economy: interactions b/w political processes & economic variables
- Political Economy of Reform: support and opposition to reform; capture of benefits by influential interests

Context:
- Initial reform focus was economic (e.g. utility privatization, market liberalization)
- Some operations stalled, delayed, or reversed, despite sound design
- Why? powerful interests sit on rents; capture future benefits -> lack of attention to political economy of reform

Reform Examples:

<table>
<thead>
<tr>
<th>Utilities:</th>
<th>Agricultural Marketing:</th>
<th>Decentralization:</th>
</tr>
</thead>
<tbody>
<tr>
<td>• inequitable pricing, subsidies&lt;br&gt;• willingness to pay/reluctance to charge&lt;br&gt;• public perception</td>
<td>• distorted production &amp; marketing chains;&lt;br&gt;• mix of public (regulatory) with private (marketing) functions</td>
<td>• loss of power by central gov’t;&lt;br&gt;• lack of implementation/enforcement of laws and regulations&lt;br&gt;• low capacity for new functions in local gov’t</td>
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Opportunity
Assess Equity of Policy Reforms and Operations

Poverty and Social Impact Analysis (PSIA)

- Over 160 PSIA in 70+ countries, 20+ sectors across Regions
- **Definition**: Analysis of the distributional impact of policy reforms on the welfare of different social groups, with a particular focus on poor and vulnerable groups

BUT... incentives, influential interests, capture of benefits not always considered, e.g.

- Powerful interests block change/gain from status quo; capture future benefits
- Less powerful/unorganized groups remain excluded from sharing benefits of growth (inequities remain)

Selected Examples of political economy consideration: Romania Mining, Bangladesh Port, Tanzania Crop Boards, Yemen Water, Albania Water, Tajikistan Land, etc
Institutional analysis: “rules of the game” - govern group behavior, interaction in political, economic and social spheres of life

Political analysis: power relations & entrenched stakeholder interests affecting decision-making & distributional outcomes

Social analysis: social relationships, governing interaction at different organizational levels (incl. households, communities, social groups)

Multi-disciplinary approach to policy change and operations
Challenge - Lack of understanding and managing of ‘political economy of reform’

- **Analysis:** Political economy literature not translated effectively into operations

- **Operations:** ‘Hidden expertise’ - ‘TTLs have tacit knowledge about political economy, but are unable to write about it due to ostensibly technical relationship with partner governments.’

- **More systematic** approach is needed
Political Economy of Reform Framework

- **Objective:**
  - unpack "black box" of political economy;
  - help illustrate "what works, why and how"
  (selected sectors: agricultural liberalization; public-private partnerships in water supply and sanitation)

- **Aim:**
  - More systematic approach for better understanding and managing of political economy of reforms/operations
  - Diagnostic and action frameworks to help practitioners enhance development effectiveness of reforms/operations

- **Approach:**
  - Collaboration with operational teams across sectors, regions
  - Inductively develop framework, grounded in operational experience - “from operations for operations”
## Political Economy of Reform – Issues and Implications for WB Lending *(FY08 ESW)*

<table>
<thead>
<tr>
<th>Country Case studies (elaborated)</th>
<th>Agricultural liberalization Budget Support</th>
<th>PPP in Water Supply and Sanitation Projects</th>
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</thead>
<tbody>
<tr>
<td>• Burkina Faso cotton sector</td>
<td>• Jordan, Amman water supply</td>
<td></td>
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<tr>
<td>• Senegal groundnut sector</td>
<td>• Albania, water sector reform</td>
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<tr>
<td>• Tanzania crop board reform</td>
<td>• Argentina, Water supply and sanitation services reform in Salta Province</td>
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<td>• Indonesia rice tariff reform</td>
<td>• Bolivia, La Paz and Cochabamba water supply.</td>
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<th>Country Case examples (brief)</th>
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<td>• Malawi ADMARC Reform</td>
<td>• Ghana urban sanitation</td>
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<td>• Chad Cotton Reform</td>
<td>• Ghana Water Sector Reform</td>
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<tr>
<td>• Mozambique Cashew nut sector reform</td>
<td>• Vietnam rural water supply</td>
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<td>• Mexico Agricultural Reform</td>
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SOCIAL DEVELOPMENT DEPARTMENT

DIAGNOSTIC FRAMEWORK

REFORM CONTEXT
- Economic, social, political and institutional context, at the sector and national level
- Scope of proposed policy reform (reform agenda)

REFORM ARENA
Stakeholders & Institutions
Economic Interests (rents, asset capture, etc.)
Political Interests (authority, clientelism, etc.)

REFORM PROCESS
Dialogue & Decision-Making
Champions & Opponents
Development Partner Influence

ACTION FRAMEWORK
Timing, Tailoring, Sequencing of reforms/operations
Lending Instruments
Analysis
Rigor, M&E
Transparency (Dissemination)
Realign
Accountability
Demand & Supply-Side
Partnership Strategy
- Decision Makers
  - Allies
Public Debate & Communication Strategy
  - Design & Implementation
Water Supply/Sanitation: selective Political Economy Challenges

- Reluctance of gov’ts to e.g. charge cost recovery tariffs, enforce collection (e.g. connected urban middle class-unconnected poor)
- Public perception/influence on operations & policy reforms=unclear
- 1990s: PSP seen as “solution”: expertise & investment for network rehabilitation and expansion
  - mainly int’l, multinational private operators
  - Public perception: profit maximization, lack of accountability, low willingness to pay
- 2000s: surge of local, regional private providers (estimated 160 mio HHs served by private providers in 2007 vs. estimated 96 mio HHs in 2000)
  - Also work on commercial basis, but higher accountability to customers and willingness to pay
  - Responsible behavior to local population, dialogue with LGs, ensuring local preferences are met
- WB emphasis for PPP: transparency, contract enforcement, accompanied by improved contractual and regulatory frameworks
  - Shift in incentives, performance enhancement of utilities: more accountable, commercially-oriented service provision, creditworthy, customer-focused
- Decentralization: important starting point for institutional change (e.g. central-local government relations)
Dramatic changes over last three decades:

- **Socio-Economic**: shift to a market economy from subsistence agriculture of North and command economy of South
- **Political**: New governance system after unification in 1990
  - Decentralization & Integration of traditional governance structures

- Formal legal system is not yet fully effective AND traditional conflict resolution system weakened - some tribal leaders act above law

- Inequitable distribution of assets, e.g. Land and Water
  - Access to land = access to water: increasing land concentration, privatization of communal land restricts water access, deep well irrigation individualizes water
  - poor groups have limited access to endowment land
  - tribal leaders are largest water consumers, but are charged with dispute resolution (incl. water disputes) – conflict of interest
Water Sector and Reform Context

- Yemen’s groundwater resources used up faster than replenished – poor worst affected
- Access to safe water & sanitation is low - poor worst served
- Urban WS lifeline benefits every connected HH – poor often excluded: unconnected, large families with above lifeline consumption
- Irrigation water use is sub-optimal
- Inefficient allocation of water investments
- Past reform efforts constrained by low implementation capacity of institutions, capture of benefits, reluctance to reform

2004: Nat. Water Sector Strategy & Investment Program (NWSSIP): pro-poor, demand-driven measures to address issues
  - New institutions: MWE, NWRA, GARWSP, NWSA
  - Reform Strategy AND Investment Program (vision and funds)
  - Participatory approach to reform: wide range of stakeholders
  - Past work to build upon (e.g. Energy PSIA, CWRAS, CSA, etc.)
BUT...Political economy of reform hampers NWSSIP Implementation

Full reform implementation remains constrained by

- Political economy of reform: Vested Interests, e.g. farmers exploit GW at expense of larger economy and urban/rural consumers; LG not proactive in preventing illegal drilling – receive fines after detection; some utility staff reluctant to increase revenues (incl. tariffs) as benefiting from public grants; and to adopt business model with cost recovery, service orientation and customer relations

- Institutional fragmentation in water sector (MWE, MAI)

- Incomplete decentralization (fiscal)

  - Agreement b/w Government, WB, GTZ to conduct PSIA to
    1. examine the progress of NWSSIP implementation
    2. analyze the equity of NWSSIP reform
    3. assess & address political economy constraints to reform in groundwater/irrigation, rural water supply/sanitation (2007); urban water supply/sanitation (2008 – GTZ funded, WB TA)

  - “Fit for purpose” PSIA (approach, methods, team) to inform policy debate and design of NWSSP update and operation
Political Economy of Reform Framework
- Linking Equity, Power Relations, Development Operations

Analysis

Policy Dialogue

combined with

...of NWSSIP
- Winners & losers (inclusion/exclusion)
- Supporters & opponents

...with broad range of stakeholders
- Build coalitions for change (equitable & sustainable development)
- Communicate effectively

Translate into design & implementation of

NWSSIP Update and Multi-donor SWAp

...for enhanced development effectiveness
PSIA Approach and Tools

- Participatory: PSIA is Yemeni exercise: (GoY/WB/GTZ/stakeholders)
  - Understand stakeholder interests, influence, support or opposition
  - Build coalition for change, enhance reform ownership

- Spatial and multi-sectoral perspective and team
  - Combine IWRM, socio-institutional analysis, political economy of reform, local context through case studies
  - Analyze Policies, Stakeholders, Institutions, Impacts, Risks & Dialogue

- Extensive consultations: 2007 PSIA: 3 workshops: Design (Dec ‘06), Consultation (March ’07, Sept ’07). 2008 PSIA: 2 workshops (April ’08, October ’08)
  1. stakeholders selected 2007 PSIA focus
  2. listen to stakeholders: understand/address reform support/opposition
    - Discussion how to address identified constraints
    - Matrix to operationalize PSIA via policy process & operation
  3. Stakeholders identified priority actions: SWAp & NWSSIP Update

- Finalization of report (reflecting stakeholder comments)

- Dissemination agreed to be done by GTZ YE (closer to stakeholders)
### Yemen Water Sector
**Power Mapping** (produced with stakeholders in 2nd workshop)

#### Support or Opposition for NWSSIP Implementation in Groundwater/Irrigation & Decentralization (D)

<table>
<thead>
<tr>
<th>High</th>
<th>Neutral</th>
<th>Opposition</th>
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<tbody>
<tr>
<td>Donors (W, A, D)</td>
<td>NWRA HQ (A, D)</td>
<td>Drillers (W, A, D)</td>
</tr>
<tr>
<td>MWE (W, D)</td>
<td>MAI (W, A)</td>
<td>MoF (A, D)</td>
</tr>
<tr>
<td>MoLA (W, D)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>NWRA Branches (W)</td>
<td></td>
<td>Large land owners, water well owners (W, A, D)</td>
</tr>
<tr>
<td>Local Admin: Governorate, LCs (W)</td>
<td>Parliament (W)</td>
<td></td>
</tr>
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<td>WUGs, WUAs, Consumers (urban) (W, D)</td>
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<tr>
<th>Willingness (W) and Ability (A) to influence NWSSIP Implementation</th>
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<tbody>
<tr>
<td>Low</td>
</tr>
<tr>
<td>Support +</td>
</tr>
<tr>
<td>Neutral 0</td>
</tr>
<tr>
<td>Opposition -</td>
</tr>
<tr>
<td>Farmers (poor) (A, D)</td>
</tr>
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Social Accountability: rights and responsibilities - Vision

Utilities: Service provider

1. Provide UWSS services
2. Pay bills for services received
3. More Revenues; Increased Incentives & ability to invest

Customer (every consumer is paying customer)

4. More satisfaction, and willingness to pay higher tariffs
Selected Key Findings

- **Vested interests still hamper reform**, e.g.
  - Large farmers capture benefits of water (public good) via access to land and tubewell drilling,
  - Urban network expansion and connection is most pro-poor strategy, BUT...
    - **Consumer, LG concern**: decentralization brings excessive tariff increases without visible service improvements
    - **MWE concern**: loss of sector control (incl. ability to guide utilities)
    - **MoF concern**: fiduciary responsibility for large investment, likely large future transfers of public funds to autonomous entities
    - **Utilities concern**: some internal resistance to change to business model, loss of subsidies/public grants
    - **Private sector concern**: impact of decentralization on its future role and profitability
Selected Key Findings (cont.)

- **Reform is not equitable**: water is saved, but at expense of rural economy, employment, income of the poor
  - Poor irrigating farmers, rural communities, landless hit hardest: cut of diesel price subsidy, higher water prices, lower consumption & incomes
  - Well-off cope better: diesel and water still affordable; alternatives

- **NWSSIP** is accepted reform strategy and investment program, but implementation is uneven
  - Best implemented as **reform package**
  - Efficiency & welfare gains possible, BUT need **change in incentive structure PLUS investment** in efficient irrigation, low-cost rural water supply, urban network expansion & connection of poor HH
  - Need substantial **extra effort** to achieve pro-poor outcomes, 'more income for less water', affordable access (urban)
    - = transformative process of **institutional development linked to investment**, esp. in rural/urban water supply and sanitation)
...but progress emerges on NWSSIP process

Ownership & momentum for enhanced reform dialogue, e.g.
- PSIA contributed to shift in GoY perception/interest to collaborate with all stakeholders on reform:
  - NWSSIP dialogue b/w MWE and MAI is promising
  - BUT...Ownership building needs to go beyond usual public agencies to further engage civil society, water user groups, Local Gov’ts
- Joint Annual Review (M&E of NWSSIP, 2007): Irrigation sector more involved; investment in irrigation improvement is visible
- Inter-Ministerial Steering Committee to lead NWSSIP Update
- Economic Incentives Study (incl. qat)
- Efforts for modern irrigation & demand management show results

2007 PSIA informed JAR; generated demand for UWSS analysis

Stakeholders agree to enhance NWSSIP equity and operationalize PSIA (2007, 2008) recommendations via
- Multi-donor Water Sector Support SWAp (Germany, UK, Netherlands, WB): funds some identified constraints and
- Update of NWSSIP: vision and investment
PSIA Uptake - Traction

- **PSIA Matrix** generated with stakeholders:
  - constraints identified to full sector reform implementation
  - clear policy actions
    - agreement on how to implement PSIA,
    - guided NWSSIP Update and SWAp preparation

- **NWSSIP Update**: enhanced focus on equity and power relations

- **Water Sector Support SWAp**: PSIA integrated into subsector activities and respective M&E framework: allows measurement of PSIA implementation as part of regular supervision, e.g.
  - Subsector Irrigation: inequities identified by PSIA addressed by two M&E indicators: 50% of support through SWp goes to smallholders
  - Subsector Urban: network expansion together with private sector to meet pro-poor demand
  - Subsector Groundwater: Water User Associations established as lowest level of resource management
PSIA: effective approach to understand & manage political economy
- identify and mitigate reform and operational risks

Effective engagement by development agencies
- Good political economy analysis, applied early in process
- Sustainable process of building coalitions for change: dialogue with wide range of stakeholders (incl. partner governments, donors, other development partners, and the public).
- Promoting transformative processes of institutional change, incl. empowerment and bottom-up accountability

Change of incentives, behavior, practice in development agencies
- Contextual understanding through analysis AND dialogue (distributional equity of reform outcomes, power relations, better access to reliable data)
- Broader range of interaction of development partners with wider range of stakeholders -not limited to MoF or line ministries-, (incl, sub-national gov’ts; parliament; private sector; civil society)
- Partnership approach, based on listening and learning
- More emphasis on participatory processes and communication; and valuing and using of local expertise