

Poverty and Social Impact Analysis: *Lessons and Examples from Implementation*



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Increased attention to poverty reduction as the central goal of development has highlighted the need for an improved understanding of how policies affect the poor. With the advent of the Poverty Reduction Strategies (PRS)—vehicles through which countries articulate their strategic choices on policy and institutional reforms—many low income countries are struggling over the choice of public actions that will have the greatest impact on poverty. Reflecting the need for more evidence-based decision making, there has been a call for more systematic assessments of and dialogue over the impacts of policy reforms. Poverty and Social Impact Analysis (PSIA) is the analysis of the distributional impact of policy reforms on the welfare of different social groups, with a particular focus on poor and vulnerable groups. The analysis of winners and losers of policy reforms helps to inform the design and implementation of policies that promote shared growth as well as inclusive, evidence-based policy design and decision making.

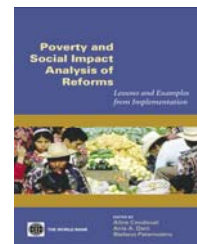
PSIA is challenging because of the complex nature of reforms and their consequences. The analysis of distributional impacts depends on many elements—the design of the reform itself, of course, but also the political economy of reform and the capacity of the implementing and regulatory agencies responsible for the reform program. The success of policy reforms thus depends heavily on the related institutional reforms and the political will to support these reform measures unstintingly. The process of implementing PSIA is an important determinant of the eventual use of the results for policy design.

The following ten analytical and operational lessons on preparing and using PSIA are drawn from a selection of case studies that illustrate the spectrum of sectors and policy reforms that can be informed by such analysis, including agriculture, energy, utilities, social sectors, taxation reform, as well as macro-economic modeling. They also illustrate the range of analytical tools and techniques that can be used for PSIA.

This short note is an extract from:

Poverty and Social Impact Analysis: Lessons and Examples from Implementation

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Poverty and Social Impact Analysis: Lessons and Examples from Implementation provides lessons and examples of implementation of Poverty and Social Impact Analysis (PSIA) of reforms. This book contains a selection of examples from the first cohorts of completed PSIAs. The case studies do not cover all the types of reforms analyzed, nor do they provide comprehensive coverage of all the tools and techniques that can be used to analyze policy impacts, but this cross-section of case studies is not atypical. The cases have been selected to illustrate the spectrum of sectors and policy reforms to which PSIA can be applied and to demonstrate the range of analytical tools and techniques that have been used for PSIA. The chapters largely deal with policy reforms in a single sector, such as agriculture (crop marketing boards in Malawi and Tanzania, cotton privatization in Tajikistan), energy (mining sector in Romania, oil subsidies in Ghana), utilities (power sector reform in Ghana, Rwanda and transition economies, water sector reform in Albania), social sectors (education reform in Mozambique, social welfare reform in Sri Lanka), and taxation reform (Nicaragua), but they also include macroeconomic modeling (Burkina Faso).

This publication can be ordered from the World Bank bookstore at www.worldbank.org/reference (type “Poverty and Social Impact Analysis”). A free electronic version can be downloaded from: www.worldbank.org/psia.

Five Analytical Lessons

Lesson 1: Negative and Positive Impacts

Broadening the analytical scope of PSIA to explore both positive and negative impacts across groups has made it more effective in considering alternative designs for policy reforms. Focusing PSIA exclusively on negative impacts would reduce PSIA to an instrument for designing mitigation measures, which might overlook possibilities to include the poor in the benefit stream of the reforms. Overall, a clear understanding of both positive and negative impacts on different groups can help identify impacts that need to be mitigated and formulate strategies for building consensus.

In designing reforms, taking the political economy of reforms into account is central to their success or failure. Although PSIA intends to protect vulnerable groups from negative impacts of policy reform, it recognizes the importance of identifying the likely impact of reforms on influential non-poor groups that may attempt to undermine reforms. Experience has shown that stakeholder interests and their influence shape institutions and incentive structures, and leads to support or opposition of reforms.

Lesson 2: Impacts on Different Social Groups

Distributional analysis can explore the impacts of reform on groups defined by income categories or other characteristics. Distributional impacts across different income groups typically use constructs such as income or consumption quintiles and deciles. For instance, the PSIA of Nicaragua's fiscal reform involved simulating the distributional impact of reforms on different quintiles to derive policy recommendations. These categories are very useful for understanding the effectiveness of targeting, comparing aggregate impacts of policy alternatives, and determining the optimal level of transfers.

However, such analysis does not lend itself to the examination of preferences and behavioral responses to policy change. Behavioral responses are often conditioned by other individual and household characteristics, including location, social or occupational characteristics, perceptions of benefits and risks, and the extent to which stakeholders feel they can influence outcomes. A review of PSIA conducted reveals that interests of stakeholders are also disaggregated along characteristics such as household size and composition, gender, ethnicity, locality and occupation. For example, the impacts of Mozambique's education sector reforms and Romania's mining sector reform were evaluated across spatially defined groups as well as gender groups.

In addition, by looking at the impacts on, and influence of, different stakeholder groups that have different interests

and degrees of influence on the reforms, PSIA is also able to analyze the political economy of reform. This provides insights into the likelihood of the reform being carried out as intended and into the likely responses of various groups, thereby deepening the understanding of reforms and their impacts.

Lesson 3: Short- and Long-Term Impacts

Most reforms have both direct impacts on selected groups, which often occur relatively rapidly, and indirect impacts, which can take longer to materialize. Assessing short-term impacts tends to be easier than assessing longer-term ones, in part because of their more direct nature. The same group of stakeholders can be affected positively in the short term and negatively in the longer term, and vice-versa. Providing a full picture of the net effects over time is critical to inform the debate around the reform options.

Very often, reforms are expected to have large indirect impacts through their effect on the fiscal balance or more generally their broader effects on the economy. Taking these indirect impacts into account is complex. In the case of the cotton reform in Burkina Faso, for example, these broad indirect effects are taken into account in the analysis of changes in cotton prices and volumes, and changes in agricultural production.

Lesson 4: Multiple Transmission Channels

Experience has also shown that it is critical for the analysis to consider multiple transmission channels for impacts, including such channels as prices and wages, employment, access to goods and services, assets, transfers and taxes, and authority. Indeed, selected groups of stakeholders might be affected positively through some channels and negatively through others. Neglecting some of these channels could therefore lead to erroneous conclusions in terms of the net impacts.

PSIAs can often help reveal transmission channels that may not have been considered previously. For example, although the studies on Malawi and Tanzania were initially approached primarily through the lens of income transfers, the analysis suggested that access to marketing services and changes in authority structures were also significant channels. Similarly, the analysis of utilities in Europe and Central Asia, as well as those in Ghana and Rwanda, suggested that in addition to concern for tariffs, access to utilities was an important consideration. The importance of access implies that subsidies for connection costs, in some instances, may be more helpful to the poor than recurring price subsidies.

Lesson 5: Choice of Research Methods & Tools

By and large, multidisciplinary approaches have proven to be invaluable for PSIA. Preliminary findings from one method are often tested and refined through complementary tools to add robustness through triangulation of results. More than half of the studies in this volume used multidisciplinary approaches. For instance, in the Romania mining study, the analysis of household survey data was compared with the results from the community study and the gender study to arrive at a more complete understanding of impacts.

A particular challenge of PSIA is the need to measure likely behavioral responses to policy reforms. Studies address this difficulty by relying partly on qualitative

techniques, including key informant interviews and focus groups, semi-structured questionnaires and purposive surveys, and qualitative research at the community level. PSIA also relies on quantitative methods to simulate behavioral responses, for instance by embedding dynamic demand or supply functions in models with micro-macro linkages; or by capturing likely behavioral responses of households to changes in price, quantity, quality or choice—for instance, changes in consumption patterns or changes in demand for education.

Political economy analysis of reforms can help to understand the interests of influential stakeholders. Political economy dimensions of reform can be studied through stakeholder analysis, institutional analysis, and risk analysis, in combination with analysis of secondary data.

PSIA in Ghana: Evaluating the Fiscal and Social Costs of Increases in Domestic Fuel Prices

The PSIA of the petroleum sector reforms in Ghana (summarized in chapter 11) emphasizes the need to identify the probable impact on the real incomes of the poorest households and alternative approaches to mitigate these effects. This study is a useful example of how household survey data and input-output data can be used together to evaluate the likely impact of reform, which in this case was an increase in domestic petroleum prices.

This PSIA evaluated the distributional implications of petroleum subsidies and first-order income effects of price changes to household real incomes. By simulating different scenarios using the national household survey and assessing the impacts of the different alternatives, the study found that the distribution of the benefits from energy subsidies across households involves substantial leakages of the benefits to higher-income households. The simulations showed clearly that targeted subsidies have high returns for protection to the poorest households and that maintaining lower kerosene prices is relatively inefficient. Thus, better-targeted programs could help reduce, or even eliminate, losses from subsidy leakage.

The results of this PSIA informed policy decisions in Ghana. In February 2005, shortly after the presentation of these PSIA findings, the government increased petroleum prices by, on average, 50 percent and emphasized its commitment to continuing sector reforms. It also introduced additional expenditure items in the 2005 budget intended to mitigate the adverse effects of the higher petroleum prices on low-income households. These programs included the elimination of school fees as well as investments in transport and an expansion of the rural electrification scheme.

While this example highlights the potential of PSIA, it also provides useful lessons about the PSIA process. In particular, the government's request for PSIA support came shortly before the budget discussions in which parliament would debate the reform. This time constraint limited the stakeholder consultation process, the breadth of policy alternatives considered, and the circulation of the findings prior to parliamentary debate. While such tradeoffs will always exist in practice, they should become less sharp as greater in-country capacity and planning for PSIA is developed.



Five Operational Lessons

The PSIA process, especially the extent of participation by stakeholders, has generated considerable debate. During the early years of PSIA, when there was some skepticism about its feasibility, more attention was given to its analytical and operational aspects. Now that the tools and methods have been developed and adopted, some bilateral partners and civil society organizations argue that the PSIA process needs more attention.

Lesson 1: Identification of Priority Reforms

The first operational lesson is that the need for PSIA should emerge from the PRS process. Since the elaboration of PRSs, or similar national development strategies, often involve extensive participatory processes, integrating consultations on PSIA priorities more systematically within future discussions of PRSs and country strategies is desirable. Selection of reforms for PSIA have usually been driven by the anticipation of large distributional impacts and/or perceived political sensitivity of the reform agenda. To the extent that countries have an inclusive process of strategic planning, other stakeholders are able to feed into that process.

The *PSIA User's Guide* recommends that four criteria be used to select priority reforms:

- the expected size and direction of the poverty and social impacts;
- the prominence of the issue in the government's policy agenda;
- the level of national debate surrounding the reform; and
- the timing and urgency of the underlying policy or reform.

Reforms of public utilities, agricultural markets, and mining are high on the governments' policy agendas, and all of them have generated a good bit of controversy. For instance, the reform of agricultural markets has been passionately debated for many years in Malawi. In the case of Sri Lanka, PSIA focused on a particular transfer program which was the most critical, both because of its size and because of the political economy surrounding it.



Lesson 2: Design of the PSIA

To be credible and useful, the analytical techniques and research methodologies employed should be transparent, and accessible to all stakeholders. Overall, it is important to

address the interest of the public by releasing information on the scope of work early and open a public discussion on the scope and design of PSIA before the analysis is undertaken.

This does not mean that all stakeholders should have an equal say in the technical design, where the application of established professional standards is of crucial importance. In practice, in some cases — where the policy reforms can affect influential stakeholders — a poorly-designed participatory research design process runs the risk of being undermined by powerful political economy interests.

For the majority of the studies in the book, the research questions for the PSIA were discussed with the government and key stakeholders before the PSIA was designed. The research design was prepared by the PSIA teams, in collaboration with in-country researchers, adapting economic and social analysis techniques from other contexts to these reforms.

Lesson 3: Analysis of the Reform

For the PSIA to be credible, the analytical work has to be technically sound and the basis for arriving at conclusions needs to be transparent and able to withstand public scrutiny by peers. This is the same standard that would apply to academic research. PSIA can be undertaken by government agencies, universities, research institutes, nongovernmental organizations, development agencies, or even private companies. In Nicaragua and Tanzania, for instance, the PSIA team comprised a mix of local academics, government analysts, and World Bank staff.

To promote the greater use of the PSIA process, in-country capacity for poverty and social analytical work is essential so that this sort of analysis can be carried out routinely within partner countries. In-country capacity remains a constraint in many borrower countries. In the examples provided in the book, client capacity building has tended to occur through on-the-job learning by in-country partners directly involved in the PSIA. The exception is the Burkina Faso study, where client capacity building was an explicit objective. In the long run, however, mainstreaming PSIA will require more deliberate, and significantly higher, investments in capacity building for PSIA.

Another lesson learned from experience in numerous countries is that the agencies responsible for implementing a reform, even though they might not be actually undertaking the analysis themselves, should be kept fully abreast of the analytical process. This permanent involvement is critical for ensuring that they understand the analytical findings and are able to both utilize the results and monitor reform impacts effectively. In the case of Nicaragua, the involvement of the tripartite committee

(representatives from government, civil society, and donors) responsible for the tax reform throughout the PSIA, proved critical to its influence on the policy designs.

Lesson 4: Policy Dialogue & Upstream Integration

PSIAs should be closely aligned with the ongoing policy dialogue. Embedding PSIA work institutionally within a country's planning processes makes it more likely that distributional impacts are systematically understood and PSIA results are relayed back into the policy dialogue. As PSIA is only one of the inputs into the policy dialogue around reform, establishing a parallel dialogue on the PSIA itself is neither practical nor useful. Rather, the key issue is to see analysis and policy dialogue as an iterative process with continuous cross-fertilization. This allows for the effective utilization of the PSIA results along with other factors such as the economic and financial returns of the reform, competing expenditure priorities, and the presence of political support for reform when debating policy options. Systematic upstream consideration of PSIA in designing programs enhances quality.

Although the PSIA has usually been conducted *ex ante*, it also has relevance during reform implementation and after a certain phase is completed. When reforms are already in the process of implementation, the PSIA can inform policy choice, allowing reform proponents to reconsider choice, design, pace, and sequence of policy and institutional reforms and identify or strengthen mitigation measures. Mozambique education and Sri Lanka social welfare PSIAs were conducted to help those governments reconsider their programs.

The dissemination of results from the analysis is critical to ensure it feeds into the broader policy dialogue. In practical terms, however, there is a tradeoff between early release of information and ensuring analytical rigor and peer scrutiny prior to dissemination of research results. There is no single solution to this tradeoff. In each case, a judgment needs to be made about the likely impact of disclosing information. Generally, it is good practice to release research results as

early as possible to increase their likely impact on the design of reforms.

Many of the studies have adopted creative solutions to share interim results with stakeholders. For instance, the Burkina Faso PSIA has been carried out directly with the government and local partners, giving them access to information throughout and involving them directly in the analysis. Similarly, the results from the Albania water and the Sri Lanka social welfare PSIAs were discussed with the government while the analytical work was ongoing. In Nicaragua and Tanzania, respective governments have been an integral part of the PSIA teams.

Lesson 5: Monitoring & Evaluating Reforms

One of the innovations of PSIA lies in its focus on *ex ante* analysis of reform impacts. This *ex ante* analysis means that the best PSIA includes several assumptions—about the macroeconomy, market trends, global market prices, investor behavior, behavioral responses by affected parties, political support for reform, the pace of parallel reforms, and institutional capacity. Changes in these assumptions are likely to occur, as the context of the reforms changes constantly. These changes affect the expected impacts of reforms, which might in turn call for changes and corrections to the design of some components of the reforms. The need to integrate the critical elements of the PSIA into monitoring and evaluating the reforms is therefore paramount. This is already happening in some cases—for instance, in the cases of the Romania mining and Sri Lanka welfare reforms—where governments are using the PSIA findings to refine their monitoring systems.

This integration is best done by integrating the monitoring of elements underlined by the PSIA within existing domestic monitoring systems — either PRS monitoring systems or sectoral monitoring systems. However, the PSIA might lead to a close monitoring of some elements that are not traditionally the focus of national systems. This may necessitate the contribution of other actors to the monitoring efforts, including local civil society organizations.

Looking Forward

As the collection of studies in the book illustrates, significant progress has been achieved in a relatively short period. Given requirements for the consideration of poverty and social consequences of reform for Development Policy Lending (OP 8.60) combined with a strong demand from donors and nongovernmental and civil society organizations, distributional analysis has established a firm foothold in World Bank analytical work. Despite this progress, truly mainstreaming PSIA within the Poverty Reduction Strategy process and policy formulation within client countries will require additional efforts.

Extending the application of PSIA and fostering evidence-based policy making will require greater country capacity in three dimensions. First, policy makers should be able to formulate their analytical needs and guide the analysis. Second, research and analytical capabilities among borrower countries will need to be strengthened to effectively analyze and monitor reforms. Third, PSIA approaches and findings need to be communicated in a manner that is accessible to all stakeholders.

Resources on the PSIA approach

Over the past few years, the World Bank has developed a broad array of guidance materials to stimulate and support PSIA. These resources are available on the PSIA website www.worldbank.org/psia

The first of these was *A User's Guide to Poverty and Social Impact Analysis* (World Bank 2003), which describes the methodological approach recommended for PSIA. The *User's Guide* presents key elements of good practice, highlights the operational principles and existing constraints on PSIA, and summarizes the key tools used by practitioners for PSIA of policy reforms.

The *User's Guide* has been supplemented by additional products focusing on tools and techniques. *The Impact of Economic Policies on Poverty and Income Distribution: Evaluation Techniques and Tools* is a compendium of tools and techniques relevant to PSIA, which range from incidence analysis to tools linking microeconomic distribution to macroeconomic frameworks or models (Bourguignon and da Silva 2003).

A second volume (forthcoming), *Evaluating the Impact of Macroeconomic Policies on Poverty and Income Distribution Using Micro-Macro Linkages Models*, will present five approaches through which macro-counterfactual experiments can be modeled and linked to microeconomic data.

The World Bank has also released a sourcebook of *Tools for Institutional, Political and Social Analysis (TIPS) of Policy Reforms*, produced in partnership with the U.K. Department for International Development (DFID) and the German Agency for Technical Cooperation (GTZ), which draws on a range of multidisciplinary tools to complement econometric analysis with what is generically called social analysis (World Bank 2007).

Two additional volumes—*Analyzing the Distributional Impact of Reforms: A Practitioner's Guide to Trade, Monetary and Exchange Rate Policy, Utility Provision, Agricultural Markets, Land Policy and Education* and its companion volume *Analyzing the Distributional Impact of Reforms: A Practitioner's Guide to Pension, Health, Labor Market, Public Sector Downsizing, Taxation, Decentralization and Macroeconomic Modeling*—present analytical guidance and an overview of the specific issues arising from the analysis of selected categories of policy and institutional reforms. These volumes offer guidance on the selection of economic tools and techniques for economic analysis of distributional impacts most appropriate to the reforms under scrutiny as well as examples of applications of these approaches.

The *Country Experience* page accessible from our PSIA website provides reports and summaries of completed PSIAs conducted in a wide variety of countries and sectors.

Learning tools on PSIA

PSIA e-course: The three module PSIA e-learning course introduces the PSIA approach, provides an overview of tools and methods, and looks at lessons learned from implementing PSIA. The e-course can be found under *Resources* on the PSIA website: www.worldbank.org/psia

TIPS e-course: This course provides an overview of the TIPS framework, tools and applications in regard to policy design and implementation. The course can be accessed at <http://www1.worldbank.org/prem/poverty/psia/training/2007/TIPS/index.html>

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