

# GOOD PRACTICE NOTES FOR DEVELOPMENT POLICY LENDING

1.  
Designing Development Policy Operations

2.  
Using Poverty and Social Impact Analysis  
to Support Development Policy Operations

3.  
Financial Management Issues  
in Development Policy Lending

4.  
Environmental and Natural Resource Aspects  
of Development Policy Lending

5.  
Supporting Participation  
in Development Policy Operations

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## **GOOD PRACTICE NOTES FOR DEVELOPMENT POLICY LENDING**

Foreword.....	iv
1. Designing Development Policy Operations.....	1
2. Using Poverty and Social Impact Analysis to Support Development Policy Operations.....	31
3. Financial Management Issues in Development Policy Lending.....	53
4. Environmental and Natural Resource Aspects of Development Policy Lending.....	67
5. Supporting Participation in Development Policy Operations.....	87

### **ACRONYMS AND ABBREVIATIONS**

CAS	Country Assistance Strategy
CEA	Country environmental analysis
CFAA	Country Financial Accountability Assessment
ECA	Europe and Central Asia Region
ESW	Economic and sector work
EU	European Union
FMS	Financial management specialist
GDP	Gross domestic product
IBRD	International Bank for Reconstruction and Development
IDA	International Development Association
IMF	International Monetary Fund
M&E	Monitoring and evaluation
MNA	Middle East and North Africa Region
NGO	Nongovernmental organization
OP	Operational Policy
PER	Public Expenditure Reviews
PFM	Public financial management
PRGF	Poverty Reduction and Grant Facility
PRSC	Poverty reduction support credit
PRSP	Poverty Reduction Strategy Paper
PSIA	Poverty and social impact analysis
SEA	Strategic environmental assessment
SSEP	Social Sectors Expenditures Program

## FOREWORD

These Good Practice Notes are being issued in conjunction with the update of Operational Policy/Bank Procedure (OP/BP) 8.60, *Development Policy Lending*. Good Practice Notes 1 through 5 are intended to provide guidance to staff in the preparation of development policy operations and are not mandatory policy documents. Their contents will be updated periodically to reflect the lessons of experience. For further updates and other good practice notes, please check the Operations Policy and Country Services (OPCS) website under development policy lending or contact the Country Economics Unit in the OPCS Vice Presidency.

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**GOOD PRACTICE NOTE 2—  
USING POVERTY AND SOCIAL IMPACT ANALYSIS  
TO SUPPORT DEVELOPMENT POLICY OPERATIONS**

**CONTENTS**

I.	Embedding PSIA in Country Work .....	34
II.	Selecting Reforms for PSIA.....	36
III.	Good Practices and Integrating the Findings in Operations .....	38
<b>Annexes</b>		
	Annex 2.A. Key Questions to be Addressed by PSIA: A Summary Matrix .....	43
	Annex 2.B. Ten Key Elements of the PSIA Approach.....	47
	Annex 2.C. Resources Available to Task Teams.....	51
<b>Boxes</b>		
Box 2.1.	What is PSIA?.....	33
Box 2.2.	The PSIA Process for Development Policy Lending.....	35
Box 2.3.	Suggested Criteria for Selecting Reforms for PSIA .....	37



## **GOOD PRACTICE NOTE 2— USING POVERTY AND SOCIAL IMPACT ANALYSIS TO SUPPORT DEVELOPMENT POLICY OPERATIONS**

1. Good Practice Note 2 provides advice to World Bank staff and their government counterparts on promoting poverty and social impact analysis (PSIA) in-country and integrating it within development policy operations.<sup>1</sup> This note focuses on good practices in setting priorities for policy reforms and policy actions for analysis, designing the analytic work and the PSIA process, and integrating the findings in the design and implementation of operations. Development policy operations vary considerably by country context and reform program. Given the difficulty in analyzing the distributional impacts of a wide range of policy reforms, PSIA cannot be based on rigid rules. See Box 2.1 for a fuller description of PSIA.
2. The PSIA design, including the choice of tools—and the depth of the analysis—will depend on the nature of the reform, the timeframe for the analysis, the information base, and the resources (including domestic capacity).<sup>2</sup> Where information is sparse and time short, the core issues may have to be addressed on the basis of knowledge of the country and international experience of similar reforms. (In these cases, it is advisable to include a plan for improving the information base.) Where countries are better placed in terms of the information base, time, and resources, these assets should be taken into account when deciding the extent of the analysis.
3. This note provides a framework to help staff and governments acquire information on the possible distributional impact of planned reforms—to improve policy design, outcomes, and sustainability of the reform program. It covers three main topics: (a) embedding PSIA in country work, (b) selecting reforms for PSIA, and (c) following good practices in the PSIA process.

### **Box 2.1. What is PSIA?**

Poverty and social impact analysis refers to analysis of the distributional impact of policy reforms on the well-being or welfare of different stakeholder groups, with a particular focus on the poor and vulnerable. PSIA also addresses sustainability and the risks to policy reform and help to monitor poverty and social outcomes and impacts of policy changes.

The World Bank assists clients in analyzing the poverty and social impacts of reforms of country policies and institutions as part of its core mandate. It has an important role—with other development partners—in helping countries undertake PSIA to inform their national poverty reduction strategies, specific reform programs, and the Bank operations that support them.

For the Bank, PSIA is neither a new product nor a fiduciary requirement. It is a systematic approach to integrating analysis of potential distributional impacts of policy reforms in the Bank's operational work.

<sup>1</sup> Development policy operations may involve IBRD loans; IDA credits, including IDA poverty reduction support credits (PRSCs); or IDA grants.

<sup>2</sup> See *User's Guide for Poverty and Social Impact Analysis* (PRMPR/SDV, The World Bank, June 2003). Also see <http://www.worldbank.org/psia>.

## I. EMBEDDING PSIA IN COUNTRY WORK

4. The adoption of the Poverty Reduction Strategy Paper (PRSP) approach and of the Millennium Development Goals framework has increased the need for more systematic analysis of the poverty and social implications of reforms. Poverty reduction responds to changes either in growth or in distribution. Because poverty reduction has become the main goal of development, a debate has emerged over the distributional implications of many of the policies implemented within the framework of pro-growth strategies. By paying more systematic attention to distributional consequences of policy reforms, PSIA also informs that debate. PSIA is primarily the responsibility of borrower governments. But the Bank and other development partners have a major role in building local capacity for PSIA, and in helping countries fill analytical gaps and use PSIA to inform their national strategies and policy design. The Bank also needs to ensure that sound analysis underpins the reforms it supports.

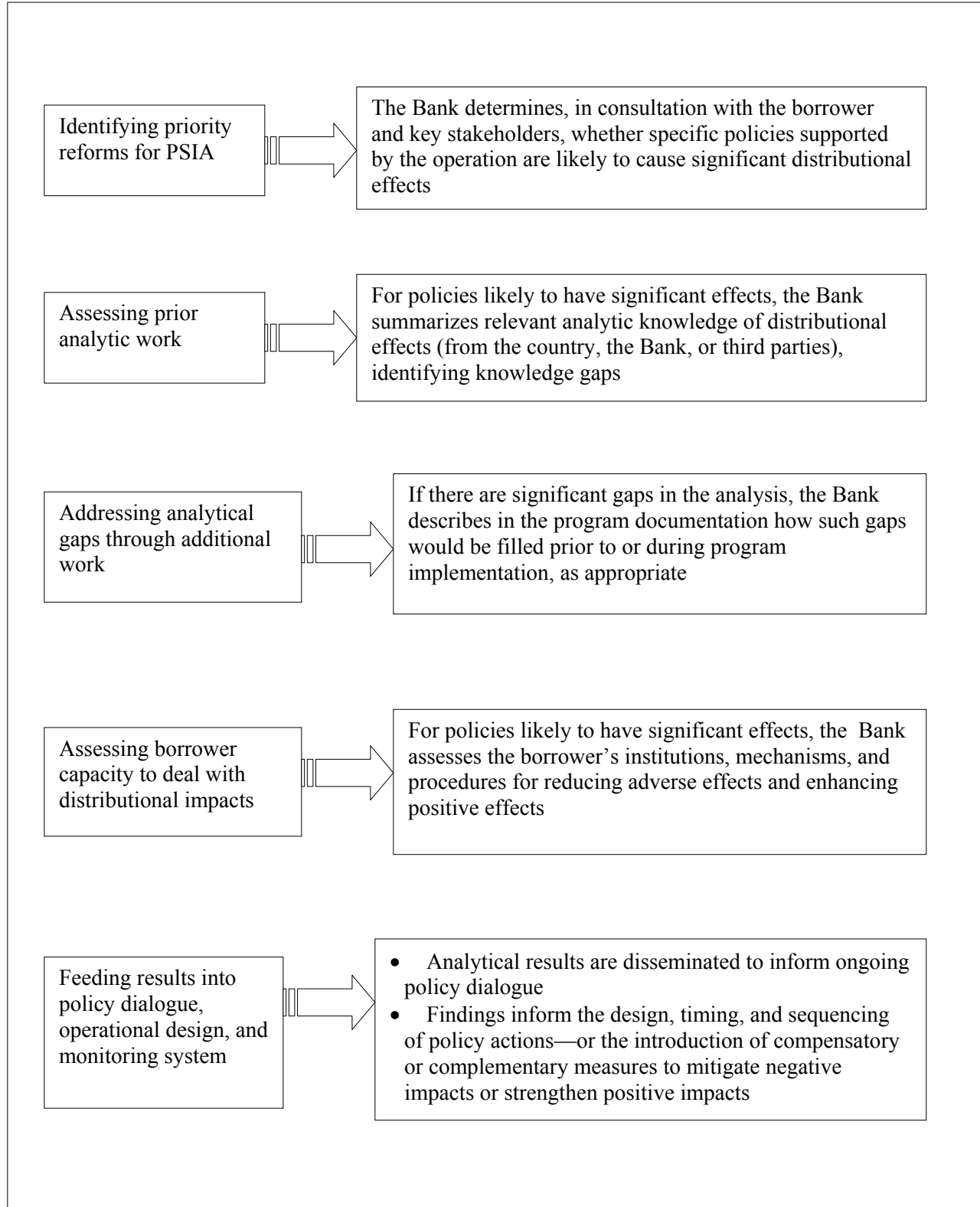
5. ***A Multiyear Programmatic Framework.*** Development policy lending is expected to support reform efforts by borrowing countries. In IDA countries the policy reforms are likely to emerge from the PRSP process. Since most policy and institutional reforms are long-term processes, it is likely that many operations will build on earlier phases of a government's reform efforts.<sup>3</sup> So these reforms normally have a gestation period long enough to do relevant analytic work before preparing a lending operation. A multiyear programmatic framework makes PSIA feasible

6. ***Integrating PSIA Within ESW.*** Reform programs and the operations that support them can be designed in detail only when there is enough analysis of the problems to be solved and enough clarity on the likely impact of the proposed interventions. For the Bank, planning for PSIA should take place within the standard cycle of economic and sector work (ESW). This is important because good analysis requires long lead times. PSIA of broad structural or macroeconomic reforms is normally carried out in conjunction with country-level ESW, such as Poverty Assessments, Public Expenditure Reviews, and Country Economic Memoranda—if the reforms and policy actions are sufficiently clear for their possible impacts to be assessed adequately when the ESW is carried out. PSIA may also be carried out through specialized sector work, as is often done for sectoral reforms. PSIA is a natural extension of the analysis underpinning a reform agenda with a potentially significant distributional impact.

7. In considering PSIA for a lending operation, Bank staff will draw on PSIA conducted upstream within the standard ESW cycle. It is highly desirable to carry out PSIA work upstream, prior to the preparation of the development policy operation. Where the country or other development partners have undertaken adequate analysis (say, through the PRSP process), the Bank can substitute this for its own analytic efforts. If there are analytical gaps, Bank staff can identify additional analysis that may be needed, taking into account the views of the government and other stakeholders. If upstream analytic work is not available and the country team or borrowing government feels the need to assess poverty and social impacts of a particular reform, further work to support the operation may also be undertaken within the constraints of data, time, and resources—to be part of the program documents or a self-standing document.

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<sup>3</sup> See *Good Practice Note 1— Designing Development Policy Support Operations*.

**Box 2.2. The PSIA Process for Development Policy Lending**

8. Under the revised policy for poverty reduction (OP 1.00, which replaced OP 4.15), the Country Assistance Strategy (CAS) will summarize existing knowledge on poverty, identify analytical gaps, and present the work program by the Bank and others to fill these gaps. Bank assistance for PSIA will be described—and budgeted for—in the CAS. Typically, the CAS

would set out key policy reform areas, identifying those for which PSIA will be undertaken and laying out the plan for integrating PSIA within existing Bank instruments. If reforms are to be supported in the outer years of the CAS and their details are not fully known during CAS preparation, the need for analytic work may be identified subsequently. Development policy support operations summarize the results of PSIA associated with specific reforms—except when the borrower or the country team feels that disclosure may compromise the success of the operation.<sup>4</sup>

9. ***PSIA in Development Policy Operations Supported by the Bank.*** Operational Policy (OP) 8.60, *Development Policy Lending*) requires Program Documents for development policy operations to specify which policies supported by the operation may have significant distributional consequences. For those policies, the Program Document summarizes the analytic knowledge (based on work by the country, the Bank, donors, or other agencies), and the country's ability to minimize adverse impacts and enhance positive impacts. If PSIA is carried out in the context of a specific policy-based lending operation, (a) the analysis may be conducted by the Bank or other partners before the operation goes to the Board or (b) the operation may proceed to the Board with an action plan (including a timeline) for the PSIA, describing how the analytical gaps will be filled prior to or during implementation.

10. PSIA may not be possible in emergencies or crises where there is no time for analysis. In such cases, teams are advised to state their assumptions about the expected impacts and monitor actual impacts so that the policy design and implementation can be modified as necessary.

11. ***Promoting Evidence-Based Decisionmaking by Building an In-Country PSIA Constituency.*** Countries may require substantial support from the Bank and other development partners to carry out PSIA. Building an in-country constituency and capacity for PSIA will strengthen country ownership and increase the prospects for mainstreaming PSIA work. Good practice involves three levels of capacity building:

- Strengthening the capacity of research organizations and government agencies to undertake PSIA data collection and analysis. This implies that the tools and methods used should be realistic, understandable, and replicable.
- Enhancing the ability of government policymakers to review the results and recommendations and consider policy alternatives based on the findings. This implies that the findings have to be shared with policymakers in a transparent and credible manner, easy to understand and communicate.
- Providing key stakeholders and opinion makers with evidence to consider during their internal policy debates and to build ownership for the reform.

## II. SELECTING REFORMS FOR PSIA

12. Selectivity is essential in the choice of reforms to be analyzed. It is not possible to meaningfully undertake PSIA for overall PRSP or Poverty Reduction and Grant Facility (PRGF) programs. Two constraints limit the ability to analyze impacts of entire programs. First, many

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<sup>4</sup> In some cases, such as the PSIA of a market-sensitive reform (such as an exchange rate devaluation), a fully open process might jeopardize the effectiveness of the reform.

policy reforms identified in PRSPs are stated as priority thematic areas where the policy actions that could be subjected to analysis have not yet been developed. The lack of specificity of policy actions can preclude meaningful PSIA at that stage. Second, the interactions among the proposed reforms create further complexities, making it difficult to assess precisely the impact of an entire program of reforms simultaneously.

13. The PSIA User's Guide recommends that country teams identify reforms in the government's agenda likely to have significant distributional impacts on different stakeholder groups, with a special focus on the poor and vulnerable. Reforms may be included in the government's agenda and considered a high priority for the operation for a variety of reasons, including their macroeconomic or fiscal impact, or because certain structural legacies constrain a country's development potential, or because a government would like to transform the governance structures for improved service delivery. If time and resources permit, PSIA should be carried out for all reforms with significant distributional impacts. But not all reforms are expected to have sizable impacts. For example, measures for improving budgetary processes may have only limited distributional impacts and not need PSIA in their design stage.

14. The selection process will inevitably be a matter of judgment at the country level (see Box 2.3 for suggested criteria). Even if some reforms typically have distributional implications, it may become clear that distributional impacts are negligible. For example, reforms of income tax brackets could have minor consequences for the overall income distribution of the country if the share of the population reporting income taxes is relatively small. In many low-income countries the share of the population filing for income tax can be as low as 10 percent. In such cases the usefulness of PSIA of tax reform would be low and should not be pursued.

**Box 2.3. Suggested Criteria for Selecting Reforms for PSIA**

- 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.

15. But even if the expected distributional impact is small, the national debate surrounding the reform may be such that PSIA would enhance the policy dialogue. For example, in many countries privatization of public assets may be perceived as being potentially detrimental to the poor, but it could have significant positive economic impacts. In these circumstances, PSIA can help understand the real distributional implications of such reforms and contribute to the design of policy actions and appropriate mitigation strategies, thus improving the likelihood of acceptance. And in countries with high ethnic tensions, or high levels of gender inequality, even a small perceived or realized gain of one group over another one may lead to serious social consequences. PSIA could help in dispelling wrong perceptions or in designing the reform in a socially acceptable form.

16. ***Working with In-Country Stakeholders and Other Development Partners.*** With the increased emphasis on country ownership and partnerships, the benefits of consulting with in-country stakeholders and development partners outweigh the transaction costs. In many cases, the PRSP process and the CAS process provide a useful basis for consulting the client on reform priorities for PSIA. Typically, the following stakeholders can help identify priorities for PSIA in any given country—central ministries of finance and planning, parliamentarians, key implementing agencies, private firms, civil society organizations, and other development

partners. If the PRSP and CAS process did not provide an opportunity to consult more broadly on PSIA priorities, consultation with key stakeholders can take place subsequently—either through formal consultation workshops, or more informally through a scoping mission. In several borrowing countries this has helped with selectivity and enabled transparency in the selection process, providing a justification for limiting PSIA to a few key reform areas. To be effective, consultation on reform priorities for PSIA should be undertaken as far upstream of the operation as possible to enable completion of the analysis in time to help the operation’s design.

17. The following questions can help guide decisionmaking on the need for PSIA:

- Has PSIA of priority reforms relevant to the development policy operation been carried out during formulation of the PRSP or the CAS?
- If not, has PSIA of priority reforms relevant to the development policy operation been carried out through core diagnostic ESW?
- If not, has PSIA of priority reforms relevant to the development policy operation been carried out through specialized sector work?

18. If the answer to any of the above questions is yes, the findings of the PSIA would be expected to be summarized in the Letter of Development Policy and in the documentation being prepared for Board submission. Annex 2.A provides a format to summarize essential PSIA information in a matrix. If the answer to all three questions is no, and if the operation is intended to support reforms with significant distributional impacts on different stakeholders, additional PSIA work may be warranted.

19. ***Focus on key policy actions within the reform.*** Most reforms involve significant policy and institutional changes, and impacts are generated by the policy actions emanating from these changes. Poverty and social impacts typically refer to changes in poverty, employment, asset endowments, access to goods and services, and inequality as a result of policy actions proposed or under implementation.<sup>5</sup> Good PSIA is possible only when the policy actions related to the proposed reforms have been clearly specified. If there is ambiguity on the policy actions, the task team should interact with the proponents of the reform—including those in the government and relevant line ministries, as well as those among development partners—to clarify the policy choices being contemplated.

### III. GOOD PRACTICES AND INTEGRATING THE FINDINGS IN OPERATIONS

20. The approach to PSIA should be country-specific and context-specific and should depend on the data, the capacity and analytical constraints, and the timeframe for the analysis. Given the challenges in practice, the tools and techniques used for PSIA typically vary greatly across countries, reforms, and circumstances. In some cases, international experience of similar reforms and knowledge of the country will form the basis of the analysis. In others, the use of analytical

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<sup>5</sup> The sustainable livelihoods framework, first popularized by the U.K.’s Department for International Development, describes five types of assets (sometimes called five types of capital)—physical, financial, natural, human, and social—that determine peoples’ livelihoods. Livelihoods can be affected by changes in the asset endowments, and in changes to the returns on those assets.

frameworks that exploit social and economic tools should be carried out. Regardless of the method chosen, the analysis should address the core issues outlined in annex 1. With the Bank in the process of mainstreaming poverty and social impact analysis, further country experiences are likely to provide lessons to be reflected in future staff guidance.

21. Although there is no methodological template for analyzing the poverty and social impacts of policy, it is possible to identify a number of elements that make for good practice PSIA (see Annex 2.A).<sup>6</sup>

22. **Anchoring PSIA in National Poverty Strategy.** Carrying out PSIA will vary according to the national political context, the enabling environment for participation, and the reform issues. An emerging good practice is for PSIA to be anchored in the formulation and implementation of national poverty reduction strategies to strengthen country buy-in and the impact of the analysis on policy. This is also critical to fostering greater national demand for analysis and a culture of evidence-based policymaking. Other emerging good practices include the following:

- (a) **Focus on upstream analysis.** To allow discussion of reform alternatives, PSIA should be carried out as far in advance of the policy decision as possible.<sup>7</sup>
- (b) **Build on prior analytic work.** PSIA should as far as possible make use of earlier analytic work and information pertinent to the reform.<sup>8</sup>
- (c) **Coordinate analytic work with operational design and policy dialogue.** PSIA work is more useful when closely coordinated with country operations and policy design, and when its results feed directly into the policy dialogue. Ensuring consistency between the analysis and operational design requires real-time interaction between the team conducting the analysis and the teams designing the operation.
- (d) **Build country capacity to sustain PSIA work.** When selecting analytical tools and methods, in addition to data limitations, capacity constraints to undertake PSIA, use its results effectively, and sustain PSIA through systematic monitoring and evaluation must be considered. PSIA should be carried out in a manner, and with a time frame, that maximizes the opportunity for national capacity building.
- (e) **Ensure stakeholder involvement and transparency.** The PSIA process should involve as many key stakeholders in the reform as possible, including civil society. The choice of the reform issue<sup>9</sup> and the research questions should emerge from broad discussion of the national poverty reduction strategy. The results of the analysis should be made public, wherever possible.<sup>10</sup> And the process of tracking impacts—and adjusting policy in the light of these impacts—should be inclusive.
- (f) **Integrate gender concerns systematically.** Women and men consistently encounter differing constraints and opportunities the world over, and their needs, interests, and

<sup>6</sup> More detailed guidance can be found in the *PSIA User's Guide* (2003), while guidance on individual tools is being published in a PREM-DEC toolkit on economic tools. In addition, Social Development has published a Sourcebook on Social Analysis, and further guidance on social tools is forthcoming.

<sup>7</sup> A good rule of thumb is 6–12 months before the policy decision is taken. If ex ante analysis is not possible, plans for the analysis should be included in the next phase of the program.

<sup>8</sup> These may be available for the country concerned or for similar countries facing the same reform issue.

<sup>9</sup> Country experience suggests that PSIA is more manageable where the analytic work is done separately for one or two reforms. Multiple reforms are best addressed sequentially or in parallel.

<sup>10</sup> Good Practice Note 1—Designing Development Policy Operations.

access to resources often diverge, particularly in poorer countries. If policy impacts are expected to have differential impacts on men and women, the PSIA design should capture these disparities, and the PSIA process should ensure that they are adequately addressed and monitored. Good practice involves including gender indicators and intrahousehold data, gender balance in the research team, gender balance in the selection of respondents, and a gender-neutral environment often requiring separate interviews or focus groups with women. Finally, when the analysis explores the sensitivity of proposed institutional arrangements to gender impacts, it becomes more feasible to identify opportunities to redress gender constraints during reform implementation.

- (g) **Ensure flexibility in the choice of institutions conducting the PSIA.** Depending on the country, different institutions may be best placed to carry out the PSIA. Besides the government, these might include the Bank, the IMF, bilaterals, civil society, research groups, and other development partners. The key is to embed the PSIA within the national strategy process—and conduct it such that it builds national capacity.
- (h) **Coordinate with development partners.** In countries where other development partners—such as multilateral and bilateral agencies, international NGOs or in-country organizations—are willing and able to engage in PSIA work, coordinating PSIA priorities and harmonizing analytical approaches can ease the pressure on the available analytical capacity. In several countries bilateral agencies are taking the lead on some PSIA. Coordinating with development partners does not relieve the Bank team of its responsibility to assess the relevance of the PSIA or to take account of its findings within the proposed operation.
- (i) **Conduct client consultation workshops.** Organizing workshops to discuss interim results with in-country stakeholders and development partners can help to interpret the results, provide insights to refine operational recommendations, facilitate donor coordination for country programs, and increase the likelihood of country ownership of reforms that draw on the PSIA. These workshops provide an opportunity to disseminate results more widely, demystify some myths about reform impacts, and encourage evidence-based dialogue on the reform.
- (j) **Integrate multidisciplinary approaches.** Policy and institutional reforms affect economic relations and social relations. Policy reforms need to be based on a proper understanding of how these interconnected relations may affect the proposed policy change, and how the policy change will alter these sets of relations. Sound policy design relies on multidisciplinary approach for understanding these relationships. Good practices in PSIA emerging from country experience suggest the following:
- *Don't* assume that policy changes will affect everyone equally and will lead to similar behavioral responses.
  - *Do* combine analytical techniques to analyze economywide impacts as well as impacts differentiated by social diversity and differences in asset endowments. Use social analysis to generate hypotheses that can be tested through econometric techniques. Complement economic modeling with social analysis to provide more detailed insights about particular stakeholders, such as the poor and vulnerable groups, or politically powerful interest groups, relevant to the reform.
  - *Do* combine quantitative and qualitative data to inform the analysis. Don't abandon the analysis if reliable, quantitative data are not available for some

countries. Do look for existing sources of information; often valuable sociological, political, and even microeconomic information can be pulled together to inform the analysis and policy dialogue.

- *Do* draw on economic, social, and political insights when considering policy reform options and assessing risks, including how political economy and social relations might affect reform outcomes and how the proposed reform might alter economic, social or political relations.
- *Don't* ignore the political economy. Many perfectly sound reforms have failed because of lack of ownership or political support for the reforms.

(k) **Initiate PSIA ex ante and monitor results during implementation.** Ideally, PSIA should be initiated ex ante. But poverty and social impacts cannot be fully known ex ante. In practical terms, policy reforms in any given domain tend to involve multiyear programs. For ongoing programs, it is feasible to look at poverty and social impacts of past policy actions to draw lessons for future reforms. Ex ante PSIA provides the empirical baseline and analytical structure for continuing analysis, but the results should be monitored and validated during implementation. Good practice suggestions include the following:

- Integrate monitoring of poverty and social impacts within national monitoring systems, such as the poverty monitoring established for the PRSP.
- Add relevant questions to ongoing household surveys to generate time series data for monitoring and evaluation. These could specify key indicators for relevant transmission channels to track the impacts of major reforms. If not already part of the survey design, add indicators on income inequality, mobility (including livelihood and physical mobility), and risk coping mechanisms (including social protection and social capital).
- Establish control groups for both quantitative and qualitative research.
- Establish systems to generate panel data. Look for disadvantaged groups based on geography, social, or livelihood characteristics, for whom the impacts could be tracked over time by building a system for purposive surveys and participatory monitoring and evaluation during implementation, to supplement the analysis of national household surveys.



## KEY QUESTIONS TO BE ADDRESSED BY PSIA: A SUMMARY MATRIX

1. Annex 2.A presents an example of a summary matrix that integrates the various elements of a good PSIA, as outlined in the PSIA User's Guide. It provides a framework for considering and articulating key aspects of PSIA for a given reform. It also offers a template for making explicit some of the results and assumptions underlying such analysis. The matrix can be used to summarize the core issues for each relevant PSIA in program documents for development policy operations. If necessary, it can also be adapted, as appropriate, within operational documents.
2. The matrix can be useful during the PSIA process. For instance, an analyst may wish to sketch out the priors in each of the seven key questions of good PSIA before undertaking an analysis—and then return to the matrix to validate or correct these hypotheses. The matrix can also help in assessing the value and relevance of prior analytic work as PSIA for the operation under consideration.
3. The matrix calls for the analyst to set out the reform components and the reasons for selecting that reform for PSIA (question 1) and the institutional mechanisms to carry out the reform (question 2). It then allows the analyst to summarize the anticipated impact of the policy reform on different stakeholders, as transmitted through five channels: employment, prices, access to goods and services, assets, and transfers and taxes (questions 3, 4, and 5). The analyst should explicitly recognize the stakeholders likely to gain from the reform, those likely to lose, and those likely to have significant influence over the reform.
4. The matrix also calls for an explicit statement of the assumptions underlying the reform. Depending on the country, conclusions on likely policy impacts will draw on different information bases and tools. In one country the matrix may be filled out using informed reasoning based on secondary data and qualitative field research. In another the conclusions may be based on empirically simulated effects derived from modeling techniques using data from recent household surveys and existing social analysis. In either instance, the matrix calls for a description of the information base and analytical methodology. The matrix also calls for the analyst to specify key risks associated with the reform, their likelihood and expected magnitude (question 6). Finally, it presents the impact that the analysis has had on national policy discussions (question 7).
5. Here are seven key questions and further guidance for filling in the matrix:

***(1) What reform was chosen for PSIA and why?***

Criteria might include prominence of the reform within the national policy debate, uncertainty of impact (particularly between short-run and long-run effects), size of likely impact, and controversy about the magnitude or direction of impacts.

**(2) *What are the implementation mechanisms for carrying out the reform?***

These mechanisms could be institutions and organizations<sup>1</sup> directly or indirectly involved in the reform and affecting its outcome. Examples include markets, legal systems, and government agencies.

**(3) *Which stakeholders are likely to be affected by the reform, positively or negatively? Which stakeholders are likely to affect the reform?***

Stakeholders might include:

- Affected groups such as the poor or non-poor, regional groups, socio-demographic categories, occupational groups, and ethnic and religious groups.
- Organized interest groups such as government agencies, trade unions, producer groups, civil society, the media, and other lobby groups.

**(4) *What are the principal channels for each of these groups or institutions to be affected by (or to affect) the reform?***

Impacts are transmitted through five main channels: employment and wages, prices of goods and services, access to goods and services, assets, and transfers and taxes.

**(5) *What are the expected direction and order of magnitude of the impact on the groups likely to be most affected? What are the key assumptions on which these impacts are predicated? (Specify the information or tools.)***

- Impacts involve attention to income and non-income measures of well-being (these may include access to basic services, vulnerability, inclusion, and human and social capital).
- Impacts should also be differentiated for short-run and long-run effects and direct and indirect effects.
- Examples of key assumptions are the entry of private firms following the easing of market restrictions, the existence of government capacity to regulate the private sector, the efficient administration of social protection payments so that targeted benefits reach the poor, and the improvements in local services for the poor following decentralization.

**(6) *What are the main risks that could change the expected impact of the reform? What is the likelihood and expected magnitude of these risks?***

Risks might arise from the political economy (the possibility that interest groups undermine the reform or capture benefits), exogenous shocks (a worsening in the terms of trade), the institutional context (the risk that the private sector does not respond as expected to the incentives), or other country conditions (conflict or social tensions).

**(7) *What is the process for feeding the analysis into national policy discussions? What impact has the PSIA had (is PSIA expected to have) on policy? (Ideally, give an***

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<sup>1</sup> Institutions are rules of the game (codes of conduct, norms of behavior, and conventions). Organizations are groups of individuals, bound by a common purpose, involving a defined set of authority relations and dedicated to achieving objectives within particular rules of the game.

*indication of how actual impacts will be tracked and how reforms will be adjusted in the light of findings.)*

- There could be various channels for feeding analysis into policy debate, including the country's PRSP team, consultation meetings around the national poverty reduction strategy, and the media.
- Policy impacts could include a fundamental rethinking of the reform, a decision to change the timing or sequencing of the policy, or the introduction of compensatory or complementary measures to mitigate negative impacts or strengthen positive impacts.

## ANNEX 2.A. PSIA SUMMARY MATRIX

<b>Reform:</b>						
1—What reform was chosen (major components) and why?						
2—What are the institutional mechanisms through which the reform will be carried out?						
3—What stakeholders are likely to be affected by the reforms? Which stakeholders are likely to affect the reform and how?	4—Through which channels are the stakeholders affected?					5—What are the expected direction and order of magnitude of impact(s)? What are the underlying assumptions?
	<i>Labor market</i>	<i>Prices</i>	<i>Access to goods &amp; services</i>	<i>Assets</i>	<i>Transfer and taxes</i>	
<i>Stakeholders affected (positively and negatively):</i>						
<i>Stakeholders with significant influence over the reform:</i>	<i>Possible support or opposition:</i>					
<i>What information basis and techniques were used to answer questions 3, 4 and 5?</i>						
6—What are the main risks which would change the expected impact of the reform? What are their likelihood and expected magnitude?						
<i>Type/nature of risk:</i>				<i>Likelihood</i>	<i>Expected magnitude</i>	
Political economy risks:						
Exogenous shocks:						
Institutional risks:						
Other country risks:						
7—What impact has the analysis had on national policy discussions?						

## TEN KEY ELEMENTS OF THE PSIA APPROACH

Chapter 3 of the *PSIA User's Guide* outlines 10 key elements of the PSIA approach. The degree of attention to each of these elements will vary by the country and reform:

- (1) Asking the right questions.
- (2) Identifying stakeholders.
- (3) Understanding transmission channels.
- (4) Assessing institutions.
- (5) Gathering data and information.
- (6) Analyzing impacts.
- (7) Contemplating enhancement and compensation measures.
- (8) Assessing risks.
- (9) Monitoring and evaluating impacts.
- (10) Fostering policy debate and feeding back into policy choice.

(1) **Formulate the right research questions.** Once the policy action choices have been clarified, task teams can go about formulating the key questions for analysis. Typically, the research questions should be derived from a scoping exercise that includes clarity on the policy change and assumptions about its design and expected consequences. Essential elements to consider include the following:

- Get clarity from the borrower on the desired impact of the reform, best stated by making transparent the assumptions about expected benefits, such as fiscal benefits, greater financial sustainability of the sector, or improved quality of services
- Identify the proposed institutional arrangements or institutional alternatives for reform implementation
- Make assumptions about the interests and concerns of key stakeholders
- Identify stakeholder groups, especially those vulnerable to impoverishment, whose welfare is of principal concern
- Make assumptions about the outcomes and impacts of the policy actions on poverty, employment, assets, access to services, and inequality.
- Make assumptions about behavioral responses of different stakeholders to the policy change.
- Consider the counterfactual—would people be better off without the reform? Can the country afford to not change existing policies?

(2) **Identify stakeholders.** Stakeholder analysis identifies the people, groups, and organizations that are important to consider when looking at the poverty and social impacts of reforms (Box 2.B.1). The analysis should examine:

- Stakeholders who may be affected by the reform, positively or negatively.
- Stakeholders who may affect the reform, by supporting or resisting it.

**Box 2.B.1. Stakeholders who may affect reforms**

- The borrower (Finance and Planning).
- Parliamentarians that ensure political support for the reform.
- Key implementing agencies that clarify policy actions under consideration and assumptions about impacts. They are relevant sector line agencies, appropriate levels of local government, and other partners such as private sector, NGOs with implementation role.
- Civil society stakeholders—research institutions, media, trade unions that can articulate and influence perceptions about reforms.
- Development partners that include donors and international NGOs.

- (3) ***Differentiate impacts based on expected transmission channels.*** Policy reforms can be expected to have an impact on various stakeholders through five main transmission channels—employment, prices (production, consumption, and wages); access to goods and services; assets; and transfers and taxes.<sup>1</sup> Each policy reform may have impacts through more than one channel. All applicable channels should be considered in PSIA design.
- (4) ***Assess institutions.*** Institutions determine the framework in which policy reforms may affect households and individuals and are the main arenas in which stakeholders interact with one another. PSIA needs to consider:
- How institutions and interests mediate the impact of policy reforms.
  - How the analysis of markets and organizational structures reveals the necessary conditions for the benefits of interventions to reach the poor.
- (5) ***Use existing sources of information.*** Over the years a wealth of knowledge and analysis has been generated on most borrowing countries. Nationally representative household survey data, while reliable, may not be available in many. So tapping alternative sources of information, especially those generated by in-country organizations and donor partners, can be invaluable.
- Draw on experiences of similar reforms in other countries, but control for variations in the country context.
  - Tap the often underused wealth of information in dissertation research on borrowing countries.
  - To obtain useful insights, examine the analysis of the effects of prior reforms conducted by non-Bank sources—the government, bilateral donors, local universities and research institutions, and civil society organizations.
- (6) ***Formulate testable hypotheses about likely distributional impacts of policy and select tools and methods to analyze the impacts.*** Organize research questions to test critical links between the policy objectives, policy actions, and their impacts on key stakeholder groups. Hypotheses should consider the expected nature of impacts.
- Long-term impacts may be different from short-term impacts. It may be easier to assess short-term impacts ex ante and long-term impacts ex post. But it is crucial that both short-term and long-term impacts are considered ex ante.

<sup>1</sup> See pages 4–6 and page 12 of the *PSIA User's Guide* for further discussion of transmission channels.

- Impacts may be direct or indirect. Typically direct impacts are easier to measure but some indirect impacts may need to be included for the analysis to be realistic.

The nature of effects also needs to be considered. Depending on the reform, the effects can be incremental (that caused by tariff increases, tax revisions) or involve major transformations in livelihoods (loss of employment due to restructuring of an entire sector) or asset entitlements (land reform) that can result in more complex and lasting effects on some people. In the latter case, the analysis should consider the nature of alternative opportunities available and the conditions needed to promote viable alternatives. The effects and the alternative opportunities may vary by:

- Geographic location.
- Age (younger workers being able to find alternative employment more easily than middle-aged workers).
- Gender (outmigration may be easier for men than women with child-rearing responsibilities).

In addition to individual characteristics, effects on institutions that provide risk-coping mechanisms should also be considered—such as government-administered social protection schemes or community-based social capital.

- (7) **Consider enhancement/compensation measures.** If the ex ante analysis reveals adverse effects on the living standards of the poor or other vulnerable groups:
- *Consider alternative design.* The design of the reform can be improved by including enhancement or mitigation measures, or a different sequencing of public actions.
  - *Consider direct compensatory mechanisms.* When adverse effects are unavoidable, consider compensatory measures on poverty, equity, or political economy grounds.
  - *Consider delay or suspension of reforms.* If the benefits of the reform are lower than the costs of mitigating or compensating the poor.
- (8) **Assess risks.** Risk assessment addresses the risk that some of the assumptions underlying the analysis may not be realized. These include the consideration of institutional risks, political risks, exogenous risks, and other country risks.
- (9) **Monitor and evaluate impacts.** Poverty and social impacts should be tracked during the introduction of the reform and evaluated ex post so that any necessary policy corrections can be made.<sup>2</sup>
- (10) **Foster policy debate and seek feedback for policy design.** PSIA results should be fed back into the development policy support operations at three levels:
- Feeding results back into the policy dialogue process.
  - Feeding results into operational design of the reform.
  - Integrating PSIA concerns into national monitoring and evaluation systems.

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<sup>2</sup> Monitoring and evaluation should be integrated within existing national monitoring systems.



## RESOURCES AVAILABLE TO TASK TEAMS

**PSIA Website:** Includes details on country examples, resources on tools and methods and PSIA training material

[www.worldbank.org/psia](http://www.worldbank.org/psia)

**PSIA User's Guide:**

<http://lnweb18.worldbank.org/ESSD/sdvext.nsf/81ParentDoc/PovertySocialImpactAnalysis?OpenDocument>

**Toolkit For Evaluating the Poverty and Distributional Impact of Economic Policies:**

<http://www.worldbank.org/poverty/psia/tools.htm>

**Consultants Roster:** A roster of consultants with various skills in poverty and social impact analysis has been prepared and will be periodically updated. The roster can be accessed at <http://www-wbweb.worldbank.org/prem/prmpo/psia/index.htm> or by sending an email to [psia@worldbank.org](mailto:psia@worldbank.org).

**Learning Program:** Country teams should communicate to the PSIA team if they have specific learning requirements. As new Learning Events are organized they will be posted on the PSIA website under the Training section.

**Reform Briefings:** Guidance documents on selected, key reforms are currently being prepared. When available, these will be posted on the website under a 'Reform' section.

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