

## Did Conditionality Streamlining Succeed?

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### *What do we mean by conditionality?*

There are two opposing points of view. One, which I would describe as the International Financial Institutions (IFI) view, sees conditionality as ‘an instrument of mutual accountability.’ An alternative view says that in essence that what is controversial about conditionality is that it is an exercise of financial leverage, requiring governments to do things they wouldn't otherwise do, or to do things more quickly than they would choose to do. The significance of this is that the ‘mutual accountability’ view is consistent with the idea of domestic ownership; the second is much more difficult to reconcile with it. This is important because research in this area indicates that where there is a perceived conflict of interest between the lender and the borrowing government, it is domestic politics which usually comes out on top.

The rest of my comments are organized under the theme of this section, i.e., ‘What’s changed?’

### *What’s changed? (a) The policy environment*

Especially if we examine differences over a period of, say, two decades, one major change is that the overall policy environment has improved. That's extremely important. Governments everywhere around the world view policy differently from how they did twenty years ago. Essentially, the view long promoted by the IFIs has prevailed. The relevance of this is that it ought to reduce the need for conditionality, or at least the required rigor of it. The significance of these changes in attitude is particularly large for the IMF, because it is in macroeconomic management where the change is most evident. What’s relevant is that the improvements in the policy environment ought to have improved compliance with conditionality by bringing policy preferences closer together. But has it actually had these effects?

Another question is, to what extent did conditionality contribute to this turnaround in the way governments look at policy, as distinct from other influences, such as the research and persuasion of the IFIs and other donors, and changes in the intellectual climate coming from universities and think-tanks. To what extent did conditionality contribute to this or did the sometimes confrontational nature of conditionality-based negotiations actually get in the way?

### *What’s changed? (b) The multilaterals have been brought into debt relief*

The fact that since the advent of the HIPC schemes, the credits to low-income countries of multilateral lenders have been brought within the purview of debt relief is relevant because it ought to reduce the incentive for the IFIs to undertake defensive lending: new lending in order to make sure the past loans are serviced according to schedule. There is quite a lot of evidence showing the importance of defensive lending in the past, because of all the complications that arise when countries go into default. Conditionality exerts little leverage in such situations. Getting the IFIs’ credits into debt relief ought to have taken away a lot of the incentive for defensive lending, at least for low income countries, and that should be favorable to more effective conditionality. But does the reality conform to these expectations?

### *What’s changed? (c) There has been some acceptance by IFIs and other donors of the critique of conditionality*

There has been acceptance within the IFIs of some of the critiques of conditionality, and of the adverse evidence that has been accumulated by researchers on the subject. World Bank and IMF officials have acknowledged as much, and have contributed to the evidential base. Some bilateral donors cum major shareholders on the Boards of

the IFIs remain unconvinced, however, and this creates problems within these institutions in deciding how to move forward. This dilemma may be particularly acute for the IMF, to the still limited extent that there is a desire to move away from its traditional conditionality-based approach.

The IFIs *have* responded to the accumulating evidence and have sought to adapt in varying degrees (e.g., see Stefan Koeberle's paper). The concern that remains, however, is whether the extent of IFI adaptation has been proportional to the severity of the limitations of conditionality. I suspect that the IFIs remain still far too reliant upon a modality of questionable effectiveness. A point that should be stressed about over-reliance on conditionality is that it can result in a large waste of aid resources. One must reflect on all the money that went into structural adjustment from the IMF and the World Bank in the 1980s and early 1990s to governments with no serious commitment to policy reform. There was formerly a tendency to use conditionality as a substitute for government commitment; today it is universally recognized that to do so is a recipe for unsuccessful programs – which is not to say that it no longer happens!

#### *What's changed? (d) Streamlining has occurred*

A streamlining of conditionality has been under way in the IFIs, particularly in the IMF that has formally adopted such a policy. At the World Bank, there has been evidence of streamlining, in the sense that the number of conditions has been coming down, even though I'm not aware of a formal policy comparable with that of the IMF. However, questions remain about how much staff buy-in there is to the streamlining agenda. Judging from personal observations made eighteen months ago, there appeared to be variable acceptance of this policy among IMF staff, which was rather surprising and indicated that management was having difficulty in having the policy implemented.

But while the IFIs have been streamlining, HIPC countries have had a whole new dimension of conditionality added, i.e., that associated with PRSPs and with HIPC itself. This new layer of conditionality has included the introduction of so-called process conditionality, in other words stipulations that the government will do things in certain ways, e.g., adopting participatory approaches. This new development has the potential to take conditionality more deeply into institutional and political structures.

At the same time there has been a move on the part of some bilateral donors towards direct budget support, and that probably has increased economy-wide conditionality. Since there is no organisation charged with maintaining an oversight of the totality of conditionality that a government faces at a given time, nor its internal consistency, there is no way to assess the net effect these developments have had on borrowers, but there is a suspicion that for low income countries there has been no net reduction, despite streamlining.

#### *What's changed? (e) Attitudes on aid relationship and modalities have developed*

Attitudes on aid relationships and aid modalities have changed in favour of ownership, partnership and program lending. This is a positive and important change but the buy-in across donors has been uneven and some remain skeptical. A major subject of concern with the shift to program aid is its potential for adding substantially to conditionality. It could be that the relationships that have developed on a partnership basis are evolving as a substitute for conditionality but it could easily result in more old-style policy stipulations. It could go either way.

#### *Conclusion*

Overall, there is not enough up-to-date information on how the situation has developed in the most recent years and what the results have been. I suspect, however, that better information would show the changes in approach to have been indecisive thus far. Reliance on a flawed instrument remains high, especially in operations in low-income countries, and with it the potential for low-productivity assistance.