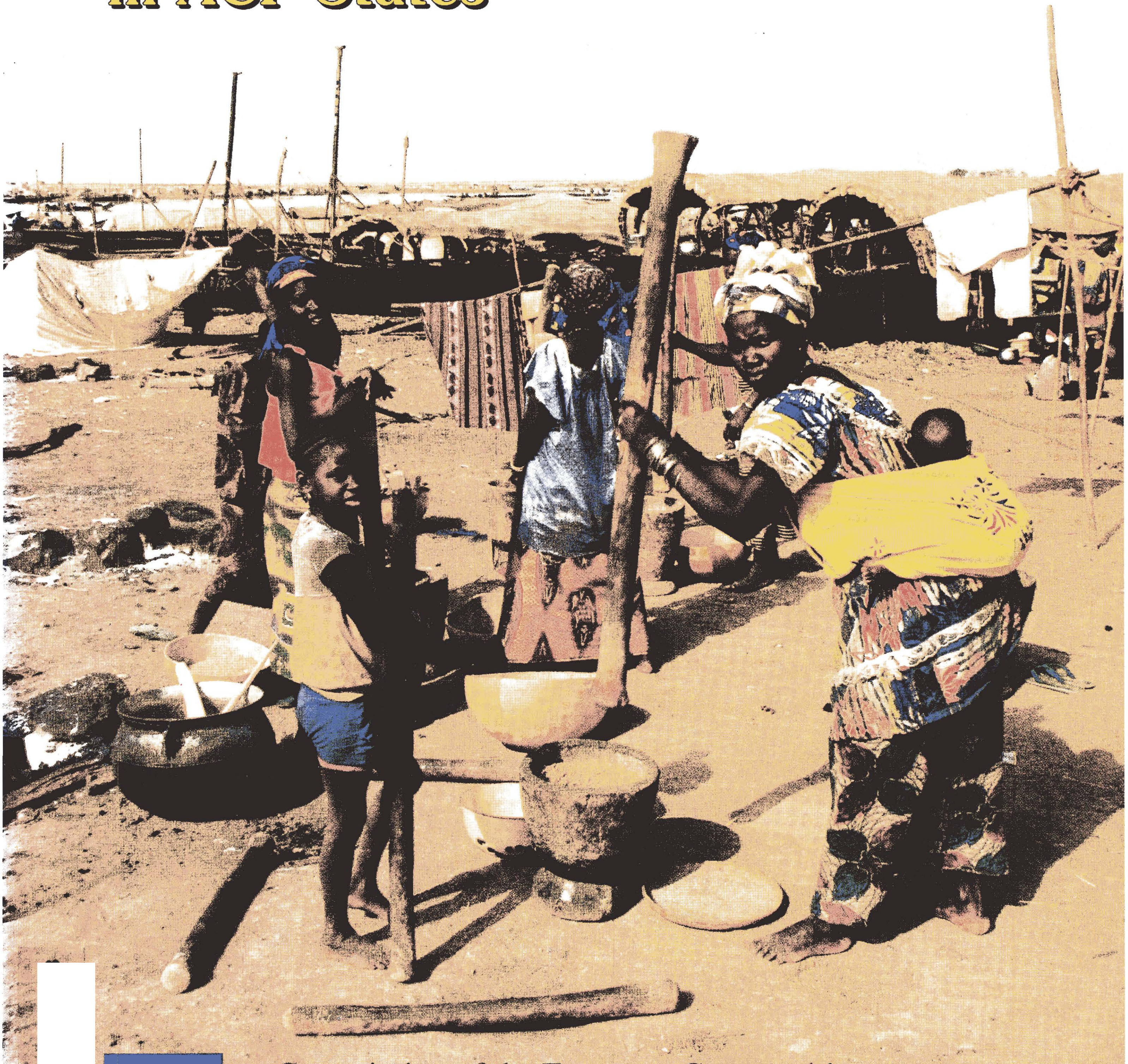
The role of the Commission in supporting structural adjustment in ACP States



Commission of the European Communities
Directorate-General for Development

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Foreword

Structural adjustment is one of the leading innovations of Lomé IV. The previous Convention, Lomé III, which provided Community support for sectoral policies in the ACP States, was the start of a gradual change in our approach, and the formal inclusion of a substantial piece of financial machinery to support the adjustment of ACP economies confirmed the trend and was a logical development of our cooperation.

The Commission made a major contribution to lightening the load of the poorest countries of Sub-Saharan Africa in 1988, with its special programme for the poor and heavily indebted countries in that part of the World, and it is extending and augmenting its efforts under Lomé IV, with long-term development aims as the priority. If we had continued our cooperation without referring to or helping to improve the macro-economic framework, that cooperation would gradually have lost its meaning and failed to fulfill its aim – although this should not lead us to react automatically in the search for an appropriate response to the need to improve the macro-economic framework.

As a consequence, this stance is also based on the extent of the financial needs (of the country) to be met by more than one donor, and on the time necessary for the programme to achieve tangible results.

The people involved in international aid diagnose and analyse adjustment-related issues in much the same way, but that is not to say that the policies they are aiming at are identical, although the principle of a united adjustment programme is certainly not questioned. The Commission believes that the adjustment process has to be organised with the ACP countries in a spirit of co-responsibility whilst rejecting the idea of stereotypes, thus gearing our support to the individual features of each country and region.

Long-term development will only really take a hold in the ACP states if the adjusting economies can boost their trade regionally and ensure that social justice is preserved. At the present time of major upheavals in contemporary history, we must respect the state of law and the rights of the poor and oppressed more than ever before. The way of the world tomorrow depends on whether we can come up with a proper response to these questions and expectations today.

Manuel Marin
Vice-President of the Commission

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I. Introduction

Since the early 80s, aid programmes, newer and more embracing than the conventional projects, have emerged among the whole panoply of instruments used to transfer financial and technical aid from the rich or relatively well-off countries to the poorest countries on the best possible conditions. The primary aim of the structural adjustment programmes has been to rationalise unbalanced economies and ensure rapid disbursement of funds.

These adjustment programmes – decried by some as an arbitrary means of cutting off the financial means which most of the developing countries had enjoyed so far and praised by others as the sign that a more realistic overall policy is at last being offered to the developing countries – have been seen in a new light, being the indirect proof that the rich country-poor country cooperation of the past 40 years has been a failure.

The international economic and financial situation changed significantly between the euphoric inter-oil shock-years (1973-1979) and the ensuing penury, and things had to be adapted or adjusted to the new situation. Most industrialised nations did this on their own, but developing countries needed very substantial financial support from the specialist development aid institutions, primarily the Bretton Woods organisations, the World Bank and the IMF, since the flow of private finance to the developing world thinned just when it was needed most. Financial needs were great and it was hoped to provide the best possible response in the drive to recover a balanced growth in the 69 countries of Africa, the Caribbean and the Pacific (ACP) States associated to the European Community. The EEC embarked on discussions and actions which led to a structural adjustment facility being included in the new Convention, Lomé IV, signed in December 1989. It was thus committed to joint effort, without of course neglecting the main aim of this cooperation – the harmonious, long-term development of the ACP nations.

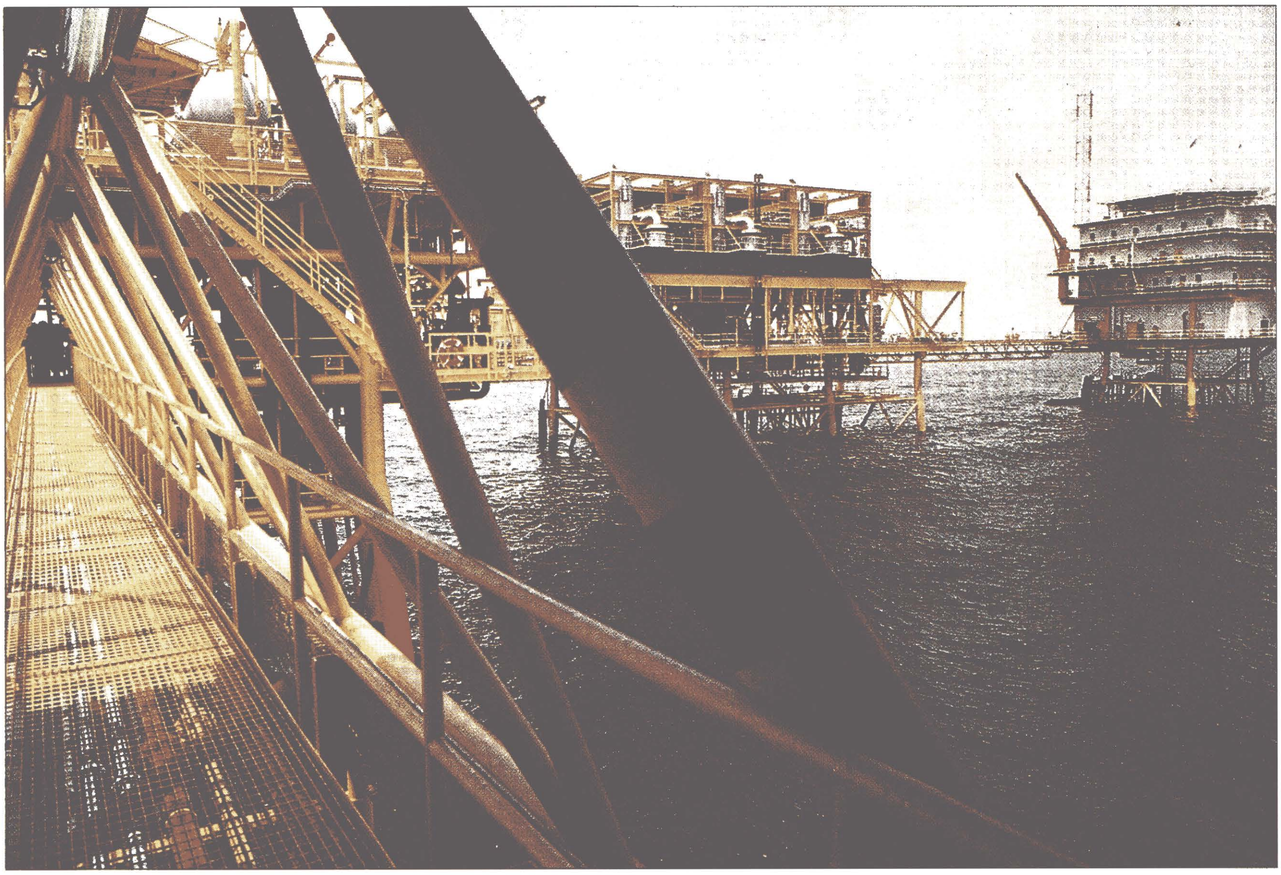
II. Adjustment – a new concept of the 1980s

1.Definition

Structural adjustment is primarily a coherent set of measures designed to reduce internal and external financial imbalances in the developing countries. Next, a set of general or sectoral financial programmes which are aimed at supporting the strong features of the economy undergoing treatment and setting it on the road to lasting growth.

2. Why is adjustment needed?

When the first oil shock occurred in 1973, ushered in by monetary upheavals on the eve of the events in the Middle East (the Six Day War and the formation of OPEC), the world economy began to overdraw.
External capital had to be found to make up for the cost of more expensive oil and to make sure that growth could continue to be financed. A more orthodox solution, though ruled out from the start, would have been to put a sharp brake on the economy by making adjustments between countries which now had spare income (the oil exporters), and those which were short (the industrialised countries especially) and would have needed to run down their reserves to pay for their soaring oil bills.
This did not happen. Policy in the 1970s was based on a wager and it worked until 1979, because countries in South America and Asia were able to sustain their growth. In order to win, four conditions had to be met. First, investments made with these ever-increasing borrowings had to be productive and profitable. Second, there had to be no significant drop in the growth of OECD countries so that exports generated by the investments could find an outlet there. Third, excessive capital should not be allowed to leave the borrowing countries. Fourth, stringent management was required to mobilise national savings and avoid slack budget policies based on what was relatively easy money. The euphoria of borrowing and the leaders' unorthodox management of public money all too often helped push ACP finances over the edge, with dire consequences for their people.
However, the right conditions were not always met, and the fact was cruelly exposed in late 1979. What went wrong? Nothing less than a radical change in America's monetary policy at the time when the second oil shock of the decade worsened the deficit of the balance of payments for the US economy and speeded up inflation.
The Americans halted inflation and redressed the dollar, but also pushed interest rates up dramatically. This made life difficult for countries borrowing in the short term or at variable rates of interest. Variable interest loans went from 16% to 43% of the total amount between 1974 and 1984 and the part of the debt quoted in dollars from 65% to 75% – particularly telling given the increasing percentage of loans made by the private sector in the 1970s. There were several reasons for this, starting with finance. Public sources of financing were unable to meet a demand they had indirectly helped to create by failing to take steps to redress the situation triggered by the first oil shock, so the private sector's importance grew in 1971-79,



Elf-Gabon

The second oil shock in late 1979 contributed to the ACP States' plunge into a severe financial crisis

with bank loans accounting for 10-30% of the developing countries' debts. It was over this period, in particular, that American banks financed loans to the developing world with Euro-dollars. The banks gradually transferred the risk of loss to their debtors by using variable rates of interest in the medium term. Many countries used these facilities regardless of the extra expense, because banks, unlike official bodies, set no conditions and, with the money they had piled up since 1974, could offer far larger loans.

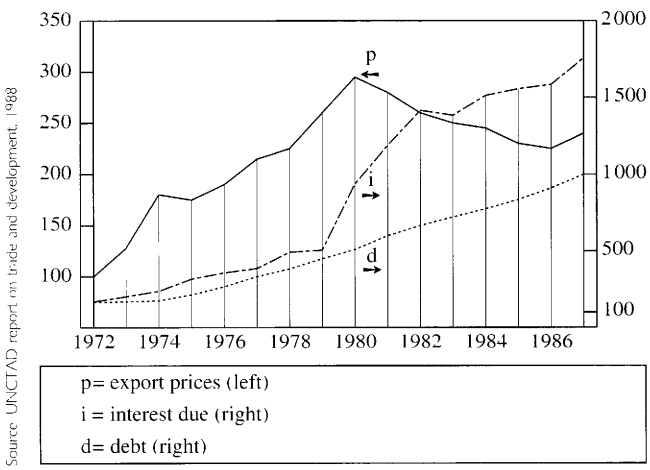
The changes over this period were motivated by ideological considerations. The euphoria of commercial banks was heightened when the monetary authorities in the industrialised world found recycling surpluses from the oil-producing countries through the market an ideal way of increasing the privatisation of the international monetary system. The result was a smaller role for the hitherto omnipresent IMF, which had lost its principal raison d'être. With floating exchange rates, it could no longer do what it had been set up to do when they were fixed, i.e. step in before devaluation where imbalances persisted. And the borrowers needed far more money than it could possibly provide.

After the speech which its then President Robert McNamara made in Nairobi in 1974, the World Bank looked to the theory of supply applied to development. The idea was to fight poverty by making major contributions in the form of loans to virtually every sector in the developing world, especially agriculture. But the one thing that was forgotten was that it matters less to supply capital than to make sure that supply is related to demand. This was subsequently to prove crucial.

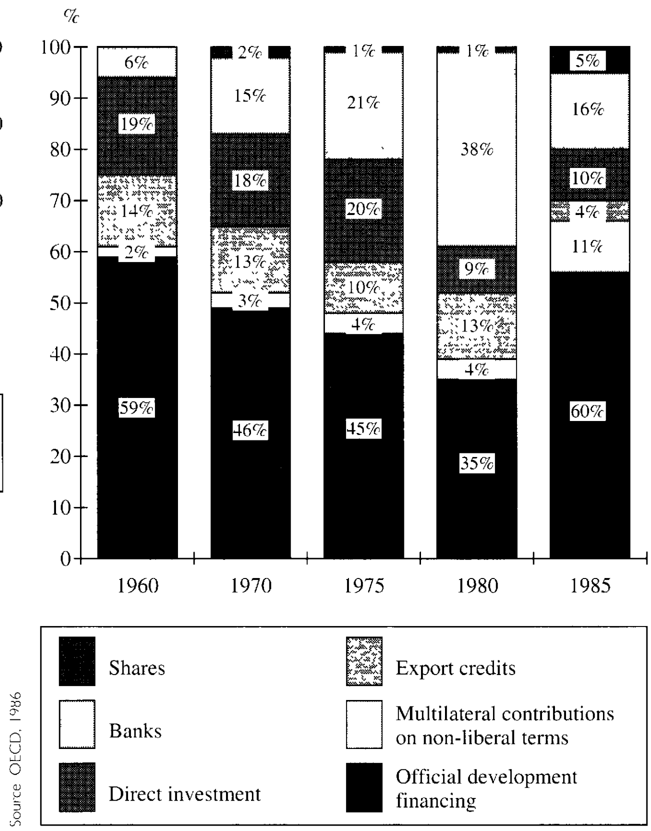
In 1980, things began to change gradually at first and then faster after the Mexican crisis of 1982, mainly because the commercial banks, which went on lending particularly to the middle-income countries of South America, suddenly woke up to their excessive commitments in these countries with the appearance of the first cracks in the spiral of debt. Interest payments on medium- and long-term loans alone went up by 50% of their face value and 75% in real terms between 1980 and 1982.

From 1982 onwards, the private loans which had softened the blows of economic turbulence so far nearly stopped. The developing nations lost their resources just at the time when they needed them

Debt, interest payments and export prices in non-oil exporting developing countries.



Structure of the net total of financial resources channelled into developing countries.



NB: these are round figures, so totals don't necessarily add up to 100%.

most (see graph) and found their parlous situation worsened by heavy recession in the industrialised world. Lastly, fluctuating trade did nothing to help the smooth functioning of most of the ACP States.

The increase in exports from non-oil exporting developing countries slumped to 2.5% in 1981 and -4% in 1982 (the average had been 25% in 1979 and 1980) while real interest rates went up by an average 12% between 1976-78 and 1981-82 (see graph).

Recession in the rich world hit the developing world particularly hard, because manufactures now made up a far bigger percentage of exports, and its export trade was suffering from protectionist measures forced onto it by crisis-ridden industrialised countries.

At least until 1981-82, that decline was accompanied by a sustained increase in the developing countries' exports, from an average 13% of GDP in 1970 to 23% in 1983. Of course, 1982 was crucial as far as debt as concerned. Between 1979 and 1982, the debt to GNP ratio had gone up 10 points and the debt to exports ratio by 40. The middle-income countries ran up three quarters of their debt between 1978 and 1982, most of it to make up for an unfavourable economic environment (higher interest rates for some, commodity price slumps for others and both for a third category of borrowers).

The 1982 crisis highlighted two risks, namely insolvency on the part of a major debtor (Mexico) and a liquidity crisis on the part of a major bank (Chase Manhattan). Insolvency was a risk because the amount which some countries had to repay depended on the commercial banks' policy towards them. The restrictive attitude of the commercial banks (the international number of which, the Bank for International Settlements suggests, dropped from 700 to 100 between 1979 and 1983) could well have been a nail in the developing countries' coffin.

However, there was no point in waiting for the same commercial banks to return to the euphoric rate at which they lent to the developing countries after 1982, particularly since rising interest rates in the USA from 1980 onwards made placements on the other side of the Atlantic more attractive. A better balance had to be found at a lower ceiling to reflect the resources of the moment.

The Courier

Tea-growing in Burundi

'The increase in exports from non-oil exporting developing countries slumped to 2.5% in 1981 and -4% in 1982, the average had been 25% in 1979 and 1980'

3. Adjustment – how?

First of all, the idea was (1) to reduce internal financial imbalances (budget) as well as external ones (balance of payments). Resource allocation and mobilisation was improved by removing protection for consumers (provided by subsidies and the freezing of prices paid to producers) or importers (reforming customs tariffs) or by juggling with monetary and tax policy (offering more attractive interest rates to depositors, raising the basis for taxation and so on). Public sector management was rationalised or reoriented (reducing the public sector's hold on the economy, reviewing public spending etc). In a second stage, global and sectoral adjustment loans were designed to give a boost to economies which were already moving along the right lines by providing financial support for all assisted countries, or for one or two promising sectors only. The re-

(1) General economic balance can be roughly described as follows:
$Y + M = C + I + X$, where (supply) = (demand)

Y = national product
M = imports
I = investment
X = exports
C = consumption

The first (tax, customs etc.) reforms were aimed at cutting imports (M) (supply) and consumption (C) (demand). In the longer term, the idea was for the transfer to occur from consumption to investment, leading in turn to an increase in production (Y).

scheduling or writing-off of official external debts (Club of Paris) and private ones (Club of London) ultimately completed the arrangements.
The immediate effect of these adjustment programmes, which involved a greater volume of finance than that of projects on average, was to give a new lease of life to countries starved of private external contributions and hungry for fresh money. Since the whole adjustment process had proved longer and more costly than anticipated, other funders, including the European Community, were gradually involved.

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Queuing in a bank in Niamey, Niger

One measure to reduce internal financial imbalances is to offer more attractive interest rates to depositors

III. The European Community – its framework of cooperation

1. Aid

Community aid is aid which the European Community grants to developing countries as part of cooperation agreements it has concluded, or in application of decisions it has taken with the Council's agreement (with a view to, say, handling an emergency). The most important agreements, under which financial cooperation is provided, are the Lomé Convention (69 ACP countries) and the Mediterranean agreements. When assistance is provided by unilateral Community decision, as in the case of food aid, emergency aid and development aid for Latin America and Asia in particular, there are no contractual commitments with the countries in question, even where cooperation agreements exist.

2. The Lomé Convention

For historical reasons, there are different financing systems for different kinds of aid. The European Development Fund (EDF) is the Community's longest-standing aid instrument. It was set up in 1958 and is still functioning under the Lomé Conventions (previously Yaoundé). Financing is ensured by contributions from the Member States, over and above the Community budget, but all other development spending is included in the budget.
Lomé IV, covering years 1990 to 2000, was signed in Lomé on the 15th of December 1989. The ECU 12 billion it provides for years 1990 to 1995 represent a considerable improvement in the Community's effort for the ACP countries, overtaking the 8.5 billion of Lomé III (1985-1990), the ECU 5.6 billion of Lomé II (1980-1985) and the ECU 3.45 billion of Lomé I (1975-1980).

3. The principles of Lomé policy:

- cooperation between two regional groups;
- sound, lasting and predictable cooperation based on legally binding arrangements laid down in a freely negotiated framework;
- global cooperation combining the whole range of aid and trade development instruments;
- finally, a permanent dialogue facilitated by the existence of three common institutions – the ACP-EEC Council of Ministers, the ACP-EEC Committee of Ambassadors and the ACP-EEC Joint Assembly.

CONVENTION OF LOMÉ IV: FINANCIAL PROTOCOL 1990-1995

(ECU million)

GLOBAL VOLUME = 12 000

EDF = 10 800

EIB = 1 200

STABEX = 1 500

SYSMIN = 480

GRANTS = 7 995

RISK CAPITAL = 825

Emergency/ refugee assistance [1] = 350

Interest rate subsidies = 280

Structural adjustment [2] = 1 150

Other grants = 6 215

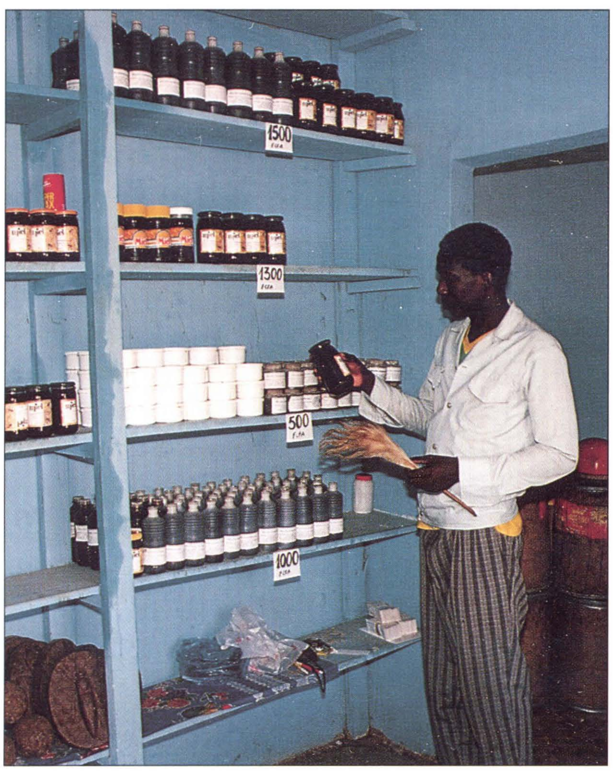
REGIONAL COOPERATION [3] = 1 250

(1) including: – emergency aid = 250
– refugees = 100

(2) specific resources plus, possible, a limited part of the indicative programmes

(3) including: – CDI = 60
– reg. trade prom. = 70
– Joint Assembly = 3

Note: on top of the ECU 12000 million for the ACP States, there are ECU 165 million for the OCT (EDF=ECU 140 million, EIB=ECU 25 million)



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A honey vendor in Bamako, Mali – an SME which was created thanks to a Community-financed credit line

'The Lomé IV Convention places greater emphasis on the private sector, with a fuller and more operational system of investment promotion, protection and support'

Lomé policy has not been fixed once and for all, for it can be adapted to trends in the partners' economic and social situation. The latest Convention, Lomé IV, contains a number of innovations including a chapter on debt and a chapter on population. It places greater emphasis on the private sector too, with a fuller and more operational system of investment promotion, protection and support. The provisions on human rights have been expanded, and new ones on decentralised cooperation added. Finally, there is also a major innovation: that of support for economic rationalisation policies in the shape of a structural adjustment facility.

IV. Community support for economic rationalisation policies

Community thinking on adjustment took shape in a Council resolution (i.e. approved by the Member States' Development Ministers), which laid down a Community approach to adjustment, on the 31 May 1988.

1. The 31 May 1988 resolution:

- The Council realised that support for ACP structural adjustment was to be an important part of the donors' development policies for far longer than anticipated and therefore approved the idea of Community involvement in the ACP adjustment process – which from then on had to be more pragmatic, more differentiated and easier for the recipient States to cope with.
- The call for coordination between the Community and the Member States and with the Bretton Woods institutions has to occur early enough in the proceedings for the Community's own ideas to be taken into account. This is to point out that the Community's intention is neither to open parallel avenues to those of the IBRD and the IMF nor to subject its action to decisions taken by them alone.
- Furthermore, in December 1987, a programme of more than ECU 550 million was set up for the poor and heavily indebted countries of Sub-Saharan Africa. The instruments used here – sectoral and general import programmes (see box) – were an opportunity for lightening considerably several ACP countries' debt burdens, with the Commission financing imports of essential products for the countries which were eligible.

SPECIAL COMMUNITY PROGRAMME, 1988-1990 Countries receiving Commission-financed import programmes		
COUNTRY	INSTRUMENT	RESOURCES (ECU million)
1. Benin	SIP (cash, kind)	31
2. Burundi	GIP	12
3. Gambia	SIP (kind)	5
4. Ghana	SIP (kind)	20,5
5. Guinea Bissau	GIP	9,4
6. Guinea Conakry	GIP	12,5
7. Equ. Guinea	SIP (kind)	1,5
8. Kenya	SIP (cash)	42
9. Madagascar	SIP (kind)	19,75
10. Malawi	SIP (cash, kind)	54,6
11. Mali	SIP (kind)	25
12. Mauritania	GIP	7
13. Mozambique	SIP (cash, kind)	70
14. Niger	SIP (kind)	14
15. Uganda	SIP (cash)	32,25
16. CAR	SIP (kind)	7
17. Senegal	SIP (kind)	11,5
18. Sao Tomé & Pr.	SIP (kind)	1,15
19. Somalia	SIP (cash, kind)	31
20. Tanzania	SIP (cash)	24,5
21. Chad	SIP (kind)	9,5
22. Togo	SIP (kind)	10
23. Zaïre	SIP (cash)	30
24. Zambia	SIP (cash, kind)	60
25. Sudan	SIP (kind)	15
TOTAL		556

All this largely foreshadowed the Community's position in the Lomé IV negotiations and the special adjustment provisions it includes.

2. The Lomé IV provisions (articles 243-250)

a) Structural adjustment support is part of the general cooperation framework aimed primarily at promoting long-term development in the ACP countries. The amount available for the facility (ECU 1150 million) is intended to boost the Community's range of conventional assistance measures (ECU 10.85 billion). The idea is to back up the ACP's own efforts to, inter alia:

i. create an economic environment which will help relaunch and speed up the growth of GDP and employment;

ii. ensure that adjustment is economically viable and socially and politically bearable.

This means, in particular, that public administration has to be improved and the private sector encouraged. Productivity in the key sectors should also rise and the economy as a whole diversify to make for greater flexibility and fewer internal and external imbalances.

b) The adjustment process has to fit in with the political and economic model of the ACP state in question. The latter's programme of reform is the basis on which the Community can prepare a series of support measures to suit the particular case. Special attention will be paid to the social, cultural and environmental conditions of each State.

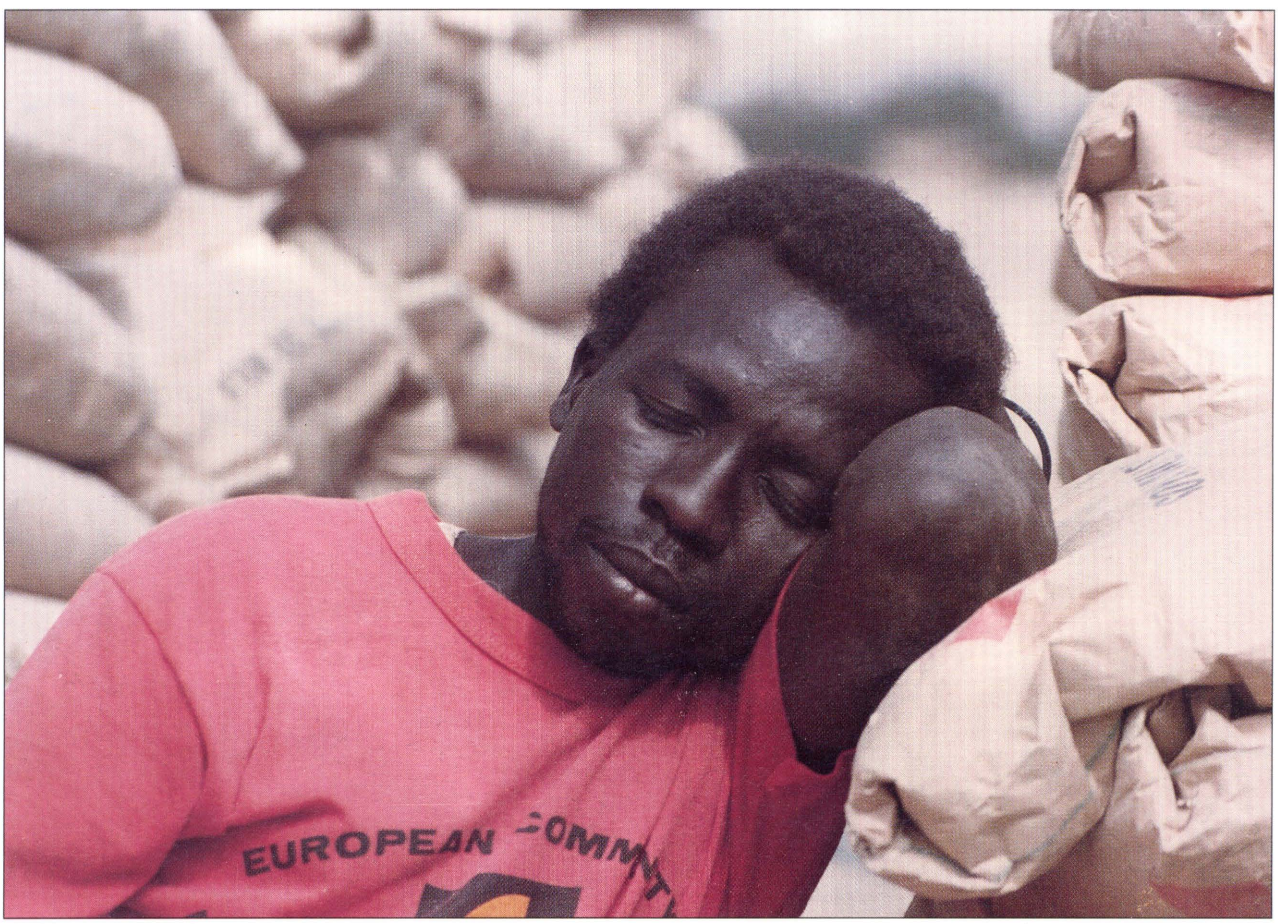
c) The means to be deployed are as follows:
- The (approximately) ECU 1150 million of the adjustment programme, which will be paid over swiftly in three ways:

i. sectoral import programmes in kind; and/or:
ii. sectoral import programmes in the form of batch-released foreign exchange to finance sectoral imports; and/or:
iii. general import programmes in the form of batch-released foreign exchange to finance general imports of a wide range of products.

- 10% of the indicative programme (which can, where necessary, be added to the basic amount) brings the Lomé IV contribution to adjustment up to ECU 2–2.5 billion.
- The counterpart funds accruing from the SIPs and GIPs will be used as a matter of priority, although not exclusively, to counteract the deleterious social effects of adjustment and help out with development schemes which are short of financing.

The counterpart funds which accrue in the developing countries are amounts of local currency obtained from selling economic operators aid in the form of products (food aid, for example) or foreign exchange to be used to finance imports (sectoral and general import programmes).

They have traditionally accrued mainly from food aid, are usually used to finance specific projects and programmes and, with the Community's involvement in financing import programmes for the ACP countries from 1987-1988 onwards, are becoming an increasingly



CEC – A. Singh

Food aid distribution in Sudan

'Traditionally counterpart funds have accrued mainly from food aid'

important part of its cooperation policy. At the same time, however, their macro-economic impact is such that they may well enter in conflict with the aims of stabilisation and adjustment. This is why the Commission took the initiative of redefining the counterpart fund policy in the Council of Ministers (leading to the Development Council's resolution of 27 May 1991) and the Special Programme of Assistance (leading to the adoption of rules of conduct on 17 April 1991).

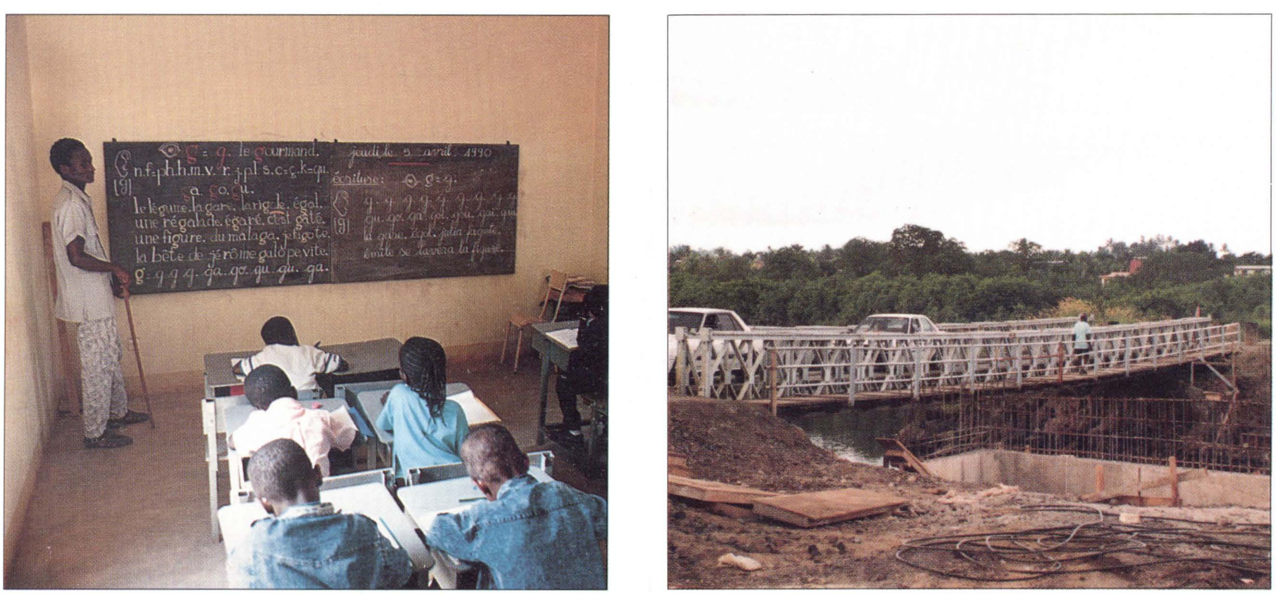
It was thus possible to strike a balance between the two "schools" (pro targeted counterpart funds and pro non-targeted budget use) and trigger a move towards greater convergence among donors. Discussions in fact revealed that narrower targeting of counterpart funds went hand in hand with an improvement in the budget procedure of the recipient State in terms of both the level (quantity) and composition (quality) of public spending.

The main lines of conduct in the Resolution are that:

- there should be only one policy use for counterpart funds, regardless of their origin, in the budget procedures of the recipient State;
- marginal counterpart fund recipients with no serious imbalances should be able to go on allocating these monies to specific projects and programmes in the traditional way;
- adjusting countries should reconcile the counterpart fund utilisation provisions with the demands of stabilisation and macro–economic reform;
- there should be only one account per donor to finance priority spending in the budget. Deflationary sterilisation may be taken into account in some cases;
- flexible, pragmatic coordination between the Bretton Woods institutions and other funders is needed to help the adjusting recipient countries to formulate and apply efficient budget policies.

In the coming years, the Commission will undertake to:

- improve the financial monitoring of counterpart funds in terms of constitution, management and financial control for all countries;
- play a bigger role in reviewing the public spending of adjusting countries so as to help them improve their budget procedures. In allocating resources, special attention will be paid to ensuring a proper level and composition of health and education spending – which is in fact one of the priorities laid down by Development Commissioner Manuel Marin.



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Article 226 of the Lomé IV Convention says that counterpart funds may be targeted to cover local spending, for instance related to the provision of pre-primary and primary education or to the rehabilitation, maintenance and upgrading of social and economic infrastructure

No fair, balanced resurgence of decently designed, decently articulated development can omit the non-productive sectors of society or underprivileged fringes of the ACP population.

The Convention (Article 226) says that counterpart funds may be targeted to cover local spending on:

- "Fund projects and programmes within the indicative programme;
- other agreed projects and programmes;
- specific budget headings under public expenditure programmes of the ACP States such as those relating to health, education, training, job creation and protection of the environment;
- measures to dampen the negative social consequences of structural adjustment. Such measures may include:

i. assistance to indigenous organisations such as cooperatives and other types of mutual-help ventures;

ii. nutrition and health support for target groups and modernisation of health facilities;

iii. retraining;

iv. the provision of pre-primary and primary education, particularly in depressed areas;

v. rehabilitating, maintaining and upgrading social and economic infrastructure;

vi. the payment of redundancy benefits to public or semi-public workers made redundant, as a contribution towards keeping them in employment for a specific period, or as a form of assistance for finding alternative employment;

vii. the provision or subsidy of basic tools;

viii. small labour-intensive projects which can be used to create employment for the unskilled, youths and women, and at the same time be used to provide training and help to rehabilitate or develop the infrastructure in both rural and urban areas;

ix. strengthening of the management capacity of the ACP State to administer social programmes;

x. appropriate measures to assist women, the aged, the handicapped and other vulnerable groups, for whom the social consequences of adjustment can be particularly severe".

V. The characteristics of Community support

Although aid agencies have much the same sort of machinery and instruments, they may well place stress on different sectors and approaches.

1. Approach

The basis of Community adjustment aid is priority on long-term objectives, this has to be geared primarily to the needs of the recipient countries, with the social and regional dimensions of adjustment getting special attention in each individual programme.
The Community's position, above all, is to provide a pragmatic approach. The ideological neutrality of Lomé policy rules out the possibility of the Community living by doctrines, be they neo-liberal or otherwise. It has of course borne in mind its long experience of cooperation with the ACP countries in devising this approach.

(a) Priority for long-term development objectives

Short- and medium-term policies, particularly those involving structural adjustment and stabilisation, must boost the ACP States' own long-term development aims and efforts. They must not be in any way at variance with their development priorities.

This should result in:

i. a balance between quick-disbursing aid and aid for long-term development;
ii. sectoral and development policies being consistent with financial and macro-economic measures.

The Community has always insisted that it would be wrong to convert the aid earmarked for long-term development (necessarily a large share of the resources available) into adjustment support, for adjustment is only a necessary but not sufficient condition of development – a position reflected in the way Lomé financial resources are allocated.
As to whether policies are consistent or not – conflicting objectives have sometimes led to different assessments by different funders. There may be a clash between, say:

- food security and the liberalisation of imports. In some countries, and those in the Sahel are a case in point, a policy of food autonomy can be seriously threatened by a sudden lowering of customs protection. Although the world market is a useful yardstick, it should not dictate to countries whose factors of production are specific and different from those in other countries which are of major importance or particularly high-performance producers;

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A Community-financed rural development project in Mali

'The Community has always insisted that it would be wrong to convert the aid earmarked for long-term development into adjustment support...'

- maintaining economic and social infrastructure and reducing the budget deficit.

b) A shared process

When it comes to adjustment, it is up to the ACPs to take the main initiative for diagnosing and analysing the problems and preparing the programmes of reform. It is their responsibility. What the Community can do is give them active support.
The Community will not assess a country's reforms on its own. Evaluation will be a joint process undertaken in the light of the principles and approach of the Lomé Convention. Thus adjustment support will be provided with due reference to ACP-EEC co-responsibility as expressed during the implementation of the previous Conventions.

c) Avoiding stereotypes

Adjustment support has to be in line with the individual features of each country, fitting in with its political and economic models and respecting the direction it has taken in development options and strategies.

This, and the ideological neutrality of Lomé, may seem to be plain common sense, but are worth emphasising nonetheless. The first adjustment programmes, let us not forget, were far too influenced by stereotyped macroeconomic models which glossed over the individual features of the different countries.

The Economic Commission for Africa (ECA) has also emphasised the fact that some policies (such as privatisation) were designed with a doctrine in mind, were badly adapted and failed to investigate matters such as whether there was a national private sector able to take

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'When aiming for economic growth and social justice, special care is taken with the most vulnerable sections of society, particularly the poor, the unemployed, women and children'

over. It was with this in mind that the ECA approved an alternative African framework for structural adjustment programmes in April 1989. The idea is less to replace the concept of structural adjustment than to adapt it in the light of the shortcomings of the first generation of programmes. These were over-stereotyped and doctrinaire, failed to control any social repercussions, glossed over the weaknesses of African economies and thus prevented the Commission from achieving its aims.

(d) The social dimension of adjustment

Social aspects, be they part of the process of reform (which is desirable) or the result of it (which is more usual) have to be taken into account at the beginning and remain a priority thereafter. When aiming for economic growth and social justice, special care is taken with the most vulnerable sections of society, particularly the poor, the unemployed, women and children.
Both the Community and the Bank are heavily committed to this.

The social dimension of adjustment
– the impact of the Commission. The experience of Togo

a) The Government brought up the social dimension of adjustment (SDA) for the first time in May 1988 at the conference of funders of structural adjustment and extra-project aid and the Commission, along with other funders (the World Bank and the UNDP), expressed an interest in joining in the discussion.
In July 1989, a poverty profile was produced with financing from the Bank's SDA Unit. Although the general effect of the first three adjustment programmes (1983-1988) had been positive, vulnerable groups were identified. A Ministry of Planning working party (one of the members of which was the local Commission Delegation) produced an analysis of statistics on the four key sectors of the social dimension of structural adjustment (nutrition, employment and income, health and education) confirming that the years of adjustment had worsened the situation in at least some of the prefectures.
At the same time, the Bank started on a 4th programme of structural adjustment and invited the Commission to take part in an integrated adjustment programme-SDA exercise in which social considerations would feature in the design of macro-economic and sectoral policies from the start.

b) The Commission's contribution to the social dimension, was reflected in the fact that the Commission was involved in:
- the three groundwork missions for the 4th structural adjustment programme (November 1989-April 1990) and, together with Bank's SDA Unit, getting better coverage for social issues in the aims and action programmes;
- identifying and protecting vulnerable groups;
- allocating a minimum social budget;
- forming and increasing resources in health and primary education.

This contribution involved financing from the 6th EDF regional resources (in support of the social dimension) for:

- one-off technical assistance to the Ministry of Planning to internalise the SDA analysis procedure, involving all the technical Ministries concerned, via an SDA Committee (an organising unit) in the Planning Ministry;
- expert advice on a joint study of the Togolese employment market.

On top of this, the SDA was included in statistics creation too, thanks to the financing of a permanent data bank on household living conditions, whereby the Consumer Budget Survey can now be finalised and put to use.
The SDA is thus an integral part of the groundwork for a Lomé IV import programme.
The Togolese Government has agreed to take steps, inter alia, to:

- allocate the relevant budget resources to the social sectors;
- identify priority programmes for target groups;
- develop instruments for better evaluation and monitoring of the effect of adjustment measures;
- take institutional measures to incorporate the social dimension.

The Commission has undertaken to target the counterpart funds on the social sectors.

(e) The regional dimension of adjustment (RDA)

Adjusting economies (making diagnosis and policies) must be analysed in a regional economic context which takes into account the demands of regional integration and increased trade.
The whole problem of structural adjustment is in fact closely tied up with that of economic integration and, although interaction between the two may well be a spur for the dynamics of both, it may also hold both back.
There is no doubt that the general imbalance in the African economies in the early 1980s put a firm brake on integration. But progress with adjustment over the past few years has made the prospects of integration far more promising, although adjustment still has to take the other regional partners into account and not impede the aims of integration. A unilateral liberalisation of imports from all destinations as opposed to regional, reciprocal liberalisation or rapid adjustment of domestic prices and exchange rate movements can create regional perturbation.

With African frontiers largely permeable, regional non-coordination of adjustment policies may be a fine incentive to informal cross-border trade.

This relatively new problem is raised by the new Convention, although the various funders may not have given it enough attention.

The regional dimension of adjustment

Any investigation into this matter and support for economic integration efforts must be carried out in a proper framework in which both aspects of cooperation can support and strengthen each other.

Possible schemes include:

i. regional coordination of national structural adjustment programmes to ensure that macro-economic policies are coherent – which means coordinating the content, pace and sequence of reform policies;

ii. regional coordination of sectoral policies in such areas as agriculture (regional agricultural areas), transport and transit (which are important for landlocked nations), trade (regional markets) and the movement of factors of prodcution (capital and labour). These various sectoral policies may, under certain conditions, have a significant integrating effect;

iii. regional structural adjustment programmes, in the light of the skills of various regional organisations. In Central Africa especially, the World Bank and the Community have joined with UDEAC members to investigate the possible financing of a structural adjustment programme for tax and transit arrangements. This regional programme may well be aimed at progress towards structural adjustment in each of the member countries of UDEAC, but the instruments of integration will be rationalised, encouraging the integration process in the long run.

More generally, the drive to rationalise operations, functions and even regional organisations should make it possible to approach the aim of economic integration more efficiently and rationally.

2. Eligibility for the facility

All ACP States are, in principle, eligible for structural adjustment support subject to the size, effectiveness and potential effect on the economic, social and political side of development of existing or planned macro-economic or sectoral reforms and in the light of any economic or social difficulties, which can be assessed through indicators such as:

a) levels of debt and debt servicing;

b) balance of payment problems;

c) the budget situation;

d) the monetary situation;

e) the rate of growth of real national income;

f) unemployment levels;

g) the situation in social areas such as nutrition, housing, health and education.

ACP States running recognised reform programmes which have the support of (at least) the main multilateral funders or which have reached agreement with, but do not necessarily have financial support from, these donors are considered as automatically meeting the conditions for adjustment aid.
No other countries are eligible as yet, although the Commission can, under certain conditions, send out missions to assess an applicant ACP country's programmes and efforts at its request.

Expert assessments by the Commission
– Rwanda and Suriname –

- In May 1989, the Commission responded favourably to Suriname's request to set up a structural adjustment programme to redress the profound imbalances in its economy. After a first exploratory mission in the summer of 1989, a multidisciplinary team of experts went out to Suriname twice (June-July and October 1990) and came up with a draft report for a priority phase of adjustment and structural adaptation. This appeared in December, just a few days before a military coup d'état leading to a change of government. In May 1991, further elections took place, leading to a democratically elected government.
  All this left the way open for the renewal of the dialogue with the new government, with a view to helping set up a programme of adjustment and reform – on the understanding that the Community would not be in a position to back up such a programme. The broadest support possible from international institutions was needed to back up any viable and effective programme.

The Commission felt that, more generally, its role was one of mediation and facilitation to help countries without reform programmes with the Bretton Woods institutions adjust viably in a coherent and palatable way that would attract support from the main funders and international institutions.

- In the case of Rwanda, the Commission made it possible for the dialogue with the Bretton Woods institutions to take off again. This was vital if the structural adjustment programme, which had been stumbling against the Bretton Woods institutions demand for heavy devaluation for several months, was actually to start. The Commission sent out an expert mission in June 1990, gave its assessment of the situation (i.e. the national currency had to be devalued and a full series of measures of accompaniment facilitated the completion of the operation) resulting in Rwanda being eligible for the adjustment programme in the first half of 1991.

3. Coordination with the Member States

One of the most important institutions for coordination between the Commission and the Member States is the European Development Fund Committee, in which the Member States are represented. The job of the Committee in programming is to assess the general framework of cooperation in each country, trends in Community aid and a general approach, particularly to the adjustment facility. It has to decide whether the country is eligible for adjustment resources and, where appropriate, (i.e. if there is any discussion about eligibility) look at the Commission's proposals on any follow-up action and ensure greater coherence and complementarity between aid from the Community and the Member States.
This well-tested method by no means excludes support deriving from contacts which already exist between the representatives of Community aid and aid from the Member States, or from any informal contact between the Development Directors of the Community countries. Quite the contrary.

VI. Development and adjustment

1. For or against?

Conflicting arguments in the sterile pro- and anti-adjustment debate are based on solid findings. Some produce figures to show that the countries benefiting from adjustment programmes have had better economic results, on average, than non-adjusting countries; other point to the decline in the major economic aggregates and the harsh daily reality of these countries, with dilapidated infrastructure, non-operational installations, a production apparatus virtually at a standstill, rising unemployment worsened by an equally bad situation in the State schools and more.

Assessments by the World Bank (including "Adjustment Lending: How it worked, how it can be improved", by V. Thomas and A. Chibber, 1989) are only moderate in their praise and one of the main reasons for their hesitation is the difficulty of defining the indicators of success or failure, for more is involved than comparing the performance of adjusting countries and non-adjusting countries. Others (cf J. de Melo's evaluation) have used nine indicators to do this – GDP growth, exports growth, the real exchange rate, inflation and the ratios of:

- investment to GDP;
- budget deficit to GDP;
- balance of current payments to GDP;
- debt servicing;
- external debt to exports.

If these ratios are applied to the developing countries (including 30 adjusting nations), the adjusting countries do slightly better than the non-adjusting ones and the 12 countries undergoing intensive adjustment noticeably better still. However, over the period we are looking at (1981-1986), several other key indicators deteriorated substantially too. Investment as a percentage of GDP slumped and the adjusting countries saw their debts soar. Budget deficits also increased, particularly in countries already heavily in debt – all of which must surely make us realise some limitations and shortcomings in adjustment policies, as they have been implemented. The artificially high standard of living of several States had to be brought down and financial adjustment, an automatic, ideal reducer, was of course needed, but economic and social adjustment are supposed to bring hope.

2. Adjustment – political, economic and social.

In the latter case, adjustment is a de facto component of any change in the political, economic and social area of any given country.

The societies of the rich and virtually permanently adjusting countries take notice of the external environment, but "dialogue amongst themselves". But in the ACP countries, whose adjustment process is initiated from the outside (or, at best, co-managed with the donors), it is all the more difficult to make a success of getting to grips with the real environment. Although currently productive investments need particular attention if the general balance is to be redressed, there are constraints which have to fall gradually if economic and social forces are to flourish (with the establishment of a State of law etc) and growth is to take off again.

Only then will meso-economic (i.e. midway between macro- and micro-economic) aid from the funders, particularly for economic (roads, communications and economic services), social (education and health) and market (product and input) infrastructure, have the right effect.

3. Focus on social considerations.

With far more financing being involved in any programme activity than in projects, sensitivity is stronger, and widely differing approaches are ruled out. This means more coordination between the funders... and not giving in to the idea of unit reduction. The Community, indeed, has a Council resolution (1988) providing for tighter coordination between the Commission and the Member States to make sure that they are pulling together in the design and follow-up of adjustment policies.

The aim is tighter coordination with all the funders (the Bretton Woods organisations especially) committed to adjustment support, which of course is vital, for one country can only have one programme of reform. But there is no question of the Community losing out on its autonomy of judgement or bowing to decisions it did not help take.

Blindly following others, or alternative approaches are ruled out. The Community will continue the policy of the first adjustment support operations and work – coordinatedly – with the ACP States and the other funders as laid down in Lomé IV.

Thus adjustment programmes have now been added to the conventional, and onerous, list of tasks of cooperation between the Commission and the ACP States. Serious financial crisis has forced adjustment upon these nations and the substantial contribution we are making to their recovery drive should do more than help with finances. It should incite the human societies concerned to keep their faith in better development.

The Commission intends to work with the Member States and the main funders to fit the adjustment facility into a long-term approach to development. Its determination is that non-directly productive sectors interests should never be sacrificed when establishing the budget, nor should the poorest be deprived of their share of resources.

The march towards fairer, better balanced development can begin again.

ANNEX I

Lomé IV Convention: Articles 224, 225, 226, 227, 243 to 250

Article 224

Within the framework of the Convention, development finance cooperation shall cover:

a) capital projets and programmes;
b) rehabilitation of projects and programmes;
c) sectoral and general import support programmes, in accordance with Article 225, which may take the form of:
i) sectoral import programmes (SIPs) through direct procurement,
ii) sectoral import programmes (SIPs) in the form of foreign exchange released in instalments for financing sectoral imports and/or
iii) general import programmes (GIPs) in the form of foreign exchange released in instalments for financing general imports covering a wide range of products;
d) budgetary support to alleviate domestic financial constraints through the use of counterpart funds generated by the various Community instruments;
e) support for measures which contribute to attenuate the debt burden and balance of payments problems;
f) technical cooperation programmes;
g) deployment of flexible resources in support of the efforts of grassroots communities;
h) recurrent costs (including current administrative, operating, and maintenance costs, both local and foreign) of new, on-going and completed projects and programmes;
i) on a case-by-case basis, supplementary expenses borne by the ACP States arising out of and strictly relating to the administration and the supervision of projects and programmes financed by the European Development Fund, hereinafter referred to as "the Fund";
j) credit lines, and support of regional payment mechanisms and export credit operations in the ACP States;
k) equity participation;
l) a combination of all or part of the above components integrated into sectoral development programmes.

Article 225

Sectoral import programmes shall be provided, upon request, from the resources of the indicative programme to support the measures taken by the ACP State concerned in the sector or sectors for which the assistance is requested in accordance with Article 281. The purpose of import programmes is to contribute to the optimal functioning of the productive sectors of the economy, to assist in the expansion of production and export capacity, to facilitate the transfer or development of technology and to help meet basic human needs. Import programmes may include the financing of inputs to the productive system such as capital and intermediate goods, raw materials, spare parts, fertilizers, insecticides and supplies to improve health and education services and standards. In addition, the resources provided under structural adjustment support may be used for sectoral import programmes as referred to in Article 224(c)(i) and (ii) and for general import programmes as referred to in Article 224(c)(iii).

Article 226

Counterpart funds generated from various Community instruments shall, except otherwise provided for, be used in a targeted way for the financing of local expenditure under:

a) Fund projects and programmes within the indicative programme;
b) other agreed projects and programmers;
c) specific budget headings under public expenditure programmes of the ACP States such as those relating to health, education, training, job creation and protection of the environment;

d) measures to attenuate the negative social consequences of structural adjustment; such measures may include:
i) assistance to indigenous organizations such as co-operatives and other types of mutual-help ventures;
ii) nutrition and health support for target groups and the modernization of health facilities;
iii) re-training;
iv) the provision of pre-primary and primary education, particularly in depressed areas;
v) rehabilitating, maintaining and upgrading social and economic infrastructure;
vi) the payment of redundancy benefits to public or semi-public workers made redundant, or as a contribution towards keeping them in employment for a specific period, or as a form of assistance for finding alternative employment;
vii) the provision or subsidization of basic tools;
viii) small labour-intensive projects which can be used to create employment for the unskilled, youths and women and at the same time be used to provide training and help to rehabilitate or develop the infrastructure in both rural and urban areas;
ix) strengthening of the management capacity of the ACP State to administer social programmes;
x) appropriate measures to assist women, the aged, the handicapped and other vulnerable groups, for whom the social consequences of adjustment can be particularly severe.

Article 227

1. Recurrent cost financing (to cover current administrative, maintenance and operating expenses) may be granted to an ACP State, in order to ensure that full use is made of investments which are of special importance for the economic and social development of the ACP State concerned and the running of which temporarily constitutes a burden for the ACP State or other eligible beneficiaries. Such support may, for new, ongoing or past projects and programmes, cover current administrative, maintenance and operating expenses such as:
   a) expenditure incurred in the start-up period, for setting up, launching and operating the capital projects or programmes in question:
   b) the cost of operating, maintaining and/or managing capital projects and programmes implemented earlier.
2. Special treatment shall be accorded to the financing of recurrent cost in the least developed ACP States.

Article 243

The ACP States and the Community recognize that the economic and social problems being experienced by ACP States are the result of both internal factors and external developments. They see the need for urgent action and share the view that short and medium-term policies must reinforce the long-term development efforts and goals of ACP States. To this end, they have agreed that the Convention should provide Structural Adjustment Support to assist ACP States in their effort to:

a) create an economic environment favourable to a resumption of, or to an acceleration in, the growth of GDP and employment;
b) improve the social and economic well-being of the population as a whole;
c) improve public sector management and provide appropriate private sector incentives;
d) increase the level of productivity in the key sectors of the economy;
e) achieve greater economic diversification as part of the effort to develop a larger measure of resilience in the economy and to reduce domestic and external imbalances while maintaining GDP growth;
f) improve balance-of-payments performance and the foreign-exchange position;
g) ensure that adjustment is economically viable and socially and politically bearable.

Article 244

Adjustment support shall be administered on the basis of the following principles:

a) the ACP States shall bear primary responsibility for the analysis of the problems to be solved and the preparation of reform programmes;
b) support programmes shall be adapted to the different situation in each ACP State and be sensitive to the social conditions, culture and environment of these States;
c) assistance shall be supportive of the ACP State's priority development objectives such as agricultural and rural development, food security, PMDT, and environmental protection and contribute to the attenuation of the debt burden;
d) adjustment support shall take place within the framework of the political and economic model of the ACP State concerned;
e) the right of the ACP States to determine the direction of their development strategies and priorities shall be recognized and respected;
f) both the reform and the support programme shall make provision from the outset to deal with the

negative social effects that may result from the process of adjustment efforts, in pursuit of the objectives of economic growth and social justice, particular attention being paid to the most vulnerable groups in the society including the poor, the unemployed, women and children;

g) the pace of the reform programmes shall be realistic and compatible with each ACP State's capacities and resources, while the implementation of support programmes shall be flexible and adapted to the management capacity of the ACP State concerned;

h) quick disbursement shall be an important feature of support programmes;

i) support shall be given in the context of a joint assessment between the Community and the ACP State concerned on the reform measures being undertaken or contemplated either at a macro-economic or sectoral level.

Article 245

1. For purposes of structural adjustment support, Community financial assistance shall be given in form of grants:
   a) as provided for in Article 1 of the Financial Protocol, and
   b) from the indicative programme, in accordance with Article 281(2)(e).
2. On the expiry of the Financial Protocol, appropriations set aside for structural adjustment support and not committed shall be paid back, save as otherwise decided by the Council of Ministers, to the assets of the Fund for the purpose of financing other operations falling within the scope of development finance cooperation, notably those relating to programmable assistance.

Article 246

1. All ACP States shall in principle be eligible for structural adjustment assistance depending on the scope of the reforms being undertaken or contemplated at the macroeconomic or sectoral level, their effectiveness, and their likely impact on the economic, social and political dimension of development, and on economic and social hardships being experienced, as reflected, by indicators such as:
   a) the level of indebtedness and the debt servic burden;
   b) balance of payments difficulties;
   c) the budgetary situation;
   d) the monetary situation;
   e) the rate of growth of real national income;
   f) the level of unemployment;
   g) the situation in social areas such as nutrition, housing, health and education.
2. ACP States undertaking reform programmes that are acknowledged and supported at least by the principal multilateral donors, or that are agreed with such donors but not necessarily financially supported by them, shall be treated as having automatically satisfied the requirements for adjustment assistance.
3. In assessing the social and economic hardships referred to in paragraph 1, particular attention will be given to the least-developed ACP States.

Article 247

1. The resources earmarked for structural adjustment support may be mobilized either at the beginning of, or during the Financial Protocol period, at the request of the ACP State concerned.
2. Such support for adjustment effort shall take the form of:
   a) sectoral or general import programmes in accordance with Articles 224c) and 225;
   b) technical assistance related to structural adjustment support programmes.
3. In addition, with a view of alleviating the ACP States' domestic financial constraints, counterpart funds generated by various Community instruments may be used in accordance with Article 226.
4. Structural adjustment support shall be implemented flexibly and the instruments chosen on a case-by-case basis.

A GIP designed in keeping with the approach to structural adjustment support laid down in the Convention will usually be the most appropriate instrument for countries carrying out macro-economic reforms. In the case of sectoral adjustment, the assistance will be given in the form of an SIP in kind or in foreign currency.

An SIP could also be used in a situation of macro-economic reforms with a view to achieving a greater sectoral impact.

Article 248

The implementation of each support programme shall:

a) be adapted to the needs of each recipient State;

b) ensure consistency between the use of the different support instruments and the approach of structural adjustment as defined in Articles 243 and 244;

c) ensure that the eligibility of ACP economic operators for access to the resources of the programme is as

wide and transparent as possible and that the best price/quality ratio is obtained on imported goods. To this end, this Convention's tendering procedures must be applied flexibly in order to:
- ensure the rapidity of disbursements;
- minimize the administrative burden on the State concerned;
- accord with the administrative and commercial practices of that State;

d) be the subject of an agreement between the Commission and the ACP body in charge of the implementation of the programme.

Article 249

In order to increase the flow of financial resources the Community, with the agreement of the ACP State concerned, may enter into co-financing arrangements with other donors or agencies. The various provisions of this Convention on co-financing shall apply. To this end and in order to ensure effective use of resources and to minimize delays, efforts shall be made, subject to the agreement of the ACP State concerned and with its effective participation, to:

a) co-ordinate the approach of the various donors towards structural adjustment support;
b) co-ordinate operational implementation in a simple and cost-effective manner.

Article 250

1. The ACP State's request for structural adjustment support shall contain the broad outline of the underlying problems being addressed by the ACP State and of the measures and actions being implemented or contemplated, the areas in which support is required, the social repercussions being experienced or envisaged and proposals to deal with them, as well as the cost estimates of the support programme for which assistance is being sought and the duration or likely period of completion.
2. The preparation, appraisal and financing decision for structural adjustment programmes shall be carried out according to the provisions on implementation procedures of Chapter 5 with due regard to the need to ensure the quick disbursing feature of structural adjustment programmes. On a case-by-case basis, retroactive financing of a limited part of imports of ACP/EEC origin may be permissible.
3. In the case of foreign exchange programmes, funds will be transferred to an ecu-denominated bank account opened by the ACP States concerned in a Community member State from which all disbursement covered by the programme shall be made. Such funds will be considered as an advance to be cleared by the submission of justification of the use of funds.

ANNEX 2

Economic situation and adjustment process in Sub-Saharan Africa – Council Resolution approved on 31 May 1988

1. At its last meeting on 9 November 1987, the Council (Development) agreed to give further though to the economic situation in sub-Saharan Africa and to the support that the Community and its Member States could provide for the structural adjustment process under way in a large number of countries in that region.
2. The Council has taken note of the Commission's analysis of the situation, which it shares to a very large degree. In particular it notes that, in addition to the fact that internal structures are frequently ill-adapted, the problems posed by debt servicing, the fall in certain commodity prices and insufficient external financial input are jeopardizing the ability of many sub-Saharan African countries to pay for the imports essential to their development. The international financial situation of the last few years has made matters worse.

   The Council notes with satisfaction that most of the countries in question have realized the seriousness of these problems and have undertaken restructuring and adjustment efforts. In that connection, it gives a reminder of the United Nations Programme of Action for African Economic Recovery and Development (1986-1990), adopted in May 1986.
3. The Community and its Member States reiterate their willingness to support the adjustment process now under way in those countries in whatever way they can.
4. After examining the problems posed by the implementation of structural reforms, the Council concludes that if viable and durable restructuring is to be achieved, the approach to be followed should take account of the following points:
   - reforms should be conceived and carried out in a pragmatic and differentiated manner, with due respect for economic policy options and taking account of the peculiarities and constraints of each country. It is essential in this connection that the governments of the countries concerned be involved to the greatest extent in analysing the difficulties to be resolved and in preparing reform programmes;
   - the Community's efforts to support sectoral policies should be continued within the framework of the priority given by numerous recipient countries to the objective of food security. However, sectoral policies should be designed to dovetail coherently with macro-economic adjustment measures;
   - although the adjustment programmes are intended to restructure the economy, re-establish macro-economic balances and bring lasting growth as quickly as possible, it is important to integrate into them other imperatives such as socio-cultural matters or environmental protection;
   - it is important, from the stage of planning any adjustment measure, to take into account its social dimension, particularly in order to reduce any negative effects it may have on the most vulnerable sections of the population and to promote simultaneously the objectives of economic growth and social justice;
   - the rate at which reforms are implemented must be compatible with the capacities and resources of each country and its development objectives, and must be bearable for its people;
   - it must be stressed that in these countries the continuation and the successful outcome of adjustment efforts are essential conditions for a recovery of economic growth. The medium and long term support of development measures and the support of adjustment measures by fast-disbursing means are complementary and both are indispensable.
5. The Community already contributes to the adjustment efforts of the sub-Saharan countries through the instruments of co-operation under the third Lomé Convention, in particular fast-disbursing instruments. It has recently added a special pro-

gramme for certain poor and heavily-indebted countries which, among other things, provides for the first time, under certain conditions, for the implementation of general import programmes. Through the same special programme the Community intends to increase and accelerate the fast-outlay sectoral import programmes provided for by the third Lomé Convention. These various measures will help to attenuate the shortage of currency and funds.

6. The Council invites the Commission and the Member States to ensure that the aid instruments at their disposal are used, as efficiently as possible, to support structural adjustment efforts as required, in particular by making available fast-disbursing aid. As far as the Community is concerned, instruments such as Stabex and food aid and the SIPs mentioned above should be better co-ordinated and used with great flexibility so as to giver greater support for the adjustment process.

7. The Council invites the Commission and the Member States to develop, in the States in question and in Brussels, more systematic co-ordination in the support for structural adjustment within the framework of the existing mechanisms and structures. In addition to a more systematic exchange of information, that will enable the operational measures decided on by each Member State to support the adjustment process in each country to be made more coherent.

   Furthermore, in certain cases, co-ordination of certain support instruments, for example the use of counterpart funds from import programmes or from food aid, might be useful.

8. The Council emphasizes the need for effective co-ordination between the Community on the one hand and the World Bank and the IMF, which play a leading role in the dialogue on structural adjustment, on the other. Such co-ordination must develop at operational level, but also upstream, so as to ensure greater convergence of political approaches and positions. It hopes that the Commission and the Member states will impress on those institutions the Community approach defined above. This is based in particular on its thorough knowledge of the realities and local constraints of the sub-Saharan, on its permanent dialogue with those countries, on the reliability and continuity of the aid it provides and on the contractual nature of the Convention of Lomé.

ANNEX 3

Use of counterpart funds generated by the various development assistance instruments – Council Resolution approved on 27 May 1991

1. The Council notes that in view of the increasing volume of counterpart funds generated by the various development assistance instruments, and their integration into the structural adjustment policies pursued by an increasingly large number of countries, it should be ensured that such funds are used for the optimum growth of the developing countries. It therefore agrees to define, on the basis of a Commission staff working paper, a number of general principles which should help to guide the policies to be followed in this area at Community and Member State level.

2. The Council points out here that the Community provisions on counterpart funds, which are still the basis of the relevant Community policy, were defined by the Lomé Convention and by food aid Regulation No 3972/86 and the Council Resolutions of 13 November 1988 and 21 November 1989. It further notes that in the case of the Member States other administrative or legislative provisions govern the detailed rules for the constitution and use of counterpart funds.

3. The Council underlines the importance of seeing, in all the countries benefiting from counterpart funds, that such funds are rapidly constituted, are the subject of transparent and stringent management and supervision and are used in accordance with the priorities agreed in the legislative or administrative instruments governing the projects of the Community and its Member States generating counterpart funds.

4. The Council recognizes that counterpart funds do not pose problems of the same type in all countries and that their use must be adapted both to the economic situation of the countries concerned and to the volume of counterpart funds generated there. It considers it necessary to step up Community co-ordination and co-ordination with other providers of funds, in particular the World Bank and the IMF, in this sphere, in particular in the countries pursuing stabilization and adjustment policies.

5. The Council considers in this light that for countries which are marginal beneficiaries of counterpart funds and do not have serious imbalances, the traditional practice of allocating counterpart funds, within the framework of the budgetary priorities and practices of the States concerned, to specific projects or programmes can be continued.

6. The Council thinks it essential nevertheless, for adjustment countries, that stabilization and reform requirements should be reconciled with the requirement to use funds in accordance with the texts governing the policies of the various providers of funds. In this connection, the Council would recall its Resolution of 16 May 1989 on co-ordination on support for structural adjustment.

   The Council holds that efficient and optimum use of counterpart funds should be based on the following principles:

i) the counterpart funds generated by the various development assistance instruments constitute resources which must be managed as part of a single and consistent budgetary policy in the context of a programme of reforms;

ii) the effectiveness of the support for structural adjustment depends on the policies and institutional reforms put in train, including those concerning public expenditure. The Community and the Member States should therefore make sure that counterpart funds are used consistently in broad budgetary headings of on-budget priority public expenditure. In respect of the countries subject to adjustment, the process of drawing up and monitoring this programme should be strengthened as regards both current and investment expenditure so as to ensure that public resources are allocated to the most urgent requirements in terms of effectiveness and fairness.

iii) the agreements concluded with the beneficiary countries concerning the management of counterpart funds must be consistent with the stabilization and adjustment targets agreed under the reforms.

iv) all counterpart funds of each donor should be consolidated in a single account by donor at the Central Bank consistent with that donor's statutory regulations. Donors should agree with the authorities in each recipient country on a common form for reporting on counterpart fund payments due to be collected from importers, and amounts actually paid.

7. The Council considers that the implementation of such principles also postulates a strengthening of co-ordination at the level of the Community and its Member States with the aim of:
   - planning, whenever possible, the constitution and allocation of counterpart funds;
   - undertaking, as part of concerted efforts by all the providers of funds, a progressive reduction in the accumulated stocks of counterpart funds which exceed the capacity to make effective and non-inflationary use of them;
   - simplifying, harmonizing and standardizing procedures for the constitution, use and monitoring of counterpart funds, according to the characteristics of each developing country and according to the budgetary rules of the developing countries and the Member States of the Community.

8. As for the Community as such, the Council, on the basis of the general principles defined above, and in order to implement the Lomé Convention, approves the Commission's approach giving priority, within the framework of the priority aims defined by the States concerned, to the social dimension of adjustment in the use of counterpart funds, in particular by providing for appropriate coverage of the education and health sectors and special attention for environmental protection. Such priority does not preclude other possible allocations for counterpart funds in accordance with the text of the Lomé Convention and the texts governing food aid.

9. In conclusion, the Council refers to the need for the Community to strive for greater co-ordination of budgetary policy with the other providers of funds, particular the World Bank and the International Monetary Fund, in order to ensure at a very early stage in the process, by means of appropriate exchange of information and active participation in the formulation of public expenditure and public investment programmes, that appropriate account is taken of Community concerns and that the level and composition of the budget are effective and equitable.

10. The Council stresses the need for all providers of funds, in implementing these principles, to strive for the greatest possible consistency among themselves. To this end, it invites the Member States and the Commission to make use of the forum for co-ordination offered by SPA to strengthen this necessary consistency in the effective and equitable use of counterpart funds.

11. The Council would ask the Commission to submit during 1993 a report on the implementation of this Resolution; if necessary, it will revise its guidelines.

ANNEX 4

Guidelines on counterpart funds

SPA working group on counterpart funds

A. Introduction

1. The SPA discussions of October 1990 raised a number of points related to the management of counterpart funds (CPF), which the donor community should address in the context of the SPA countries. Based upon SPA 2 pledges, CPF creation for the SPA countries was estimated to be substantial, amounting to the equivalent of US$ 4 billion annually derived from adjustment assistance of all SPA donors, mainly in the form of commodity imports.

i) The donor-recipient agreements on CPF management for the SPA countries should be consistent with their structural policies and reforms within a framework of external adjustment, stabilization and growth-oriented developmental objectives agreed to with the Bretton Woods Institutions (BWIs), taking into account the views of the donor community.

ii) Donors earmark the use of CPF in order to increase efficiency and equity of public expenditures. Under a structural adjustment programme, the efficiency and equity of public expenditure (including both recurrent and investment outlays) are to be achieved by setting their level and prioritizing their composition within a coherent framework of macroeconomic and developmental objectives. Such expenditure programmes are also subject to monitoring and periodic reviews. As progress is achieved along these lines, the case for earmarking CPF for specific uses decreases.

iii) Some donor agencies, dependent on budgetary appropriations and accountable for the use for public funds, may be subjected to strict legal requirements on CPF use hence, they may find it difficult to adopt a policy of total unearmarking of CPF use. As with the case of SPA donors' harmonizing procurement procedures for adjustment assistance, it is hoped that a set of consensus guidelines for the use of CPF would assist individual donors to review their bilateral procedures leading towards greater harmonization.

iv) In providing support for the priority public expenditure programmes of recipient countries, the donors and the BWIs should coordinate their approaches in a flexible and pragmatic way.

2. In view of the fact that the Development Assistance Committee of the OECD is presently working on the draft principles for programme assistance, it is suggested that any agreed SPA guidelines for the management of CPF be submitted as an input for the DAC exercise. The proposed SPA guidelines are presented below. Although they have been written in respect of adjusting countries in general and SPA countries in particular, many of the same principles apply to non-adjusting countries who receive programme food aid.

3. The satisfactory implementation of budgetary targets and expenditure priorities requires these to be clearly formulated and that there is adequate budgetary monitoring and control processes.

4. It is proposed that the new guidelines be implemented in SPA countries. It is moreover suggested that a special effort should be made in a few countries to be chosen as test-cases (1) on the basis of the following criteria:
   - the number of donors present;
   - the size of CPF relative to money supply and the budget;
   - the adequacy of the budgetary monitoring and control process.

5. The progress made in the application of the guidelines could be assessed after one year. This could in turn lead to an update and extension of the guidelines as appropriate. In this context, most working group participants suggest that, on the basis of this assessment, it would be desirable to go one step further. In particular they suggest that, in SPA countries with demonstrated capacity (or along with appropriate steps taken to strengthen such capacity)

for public expenditure planning and effective budget implementation, participating donors could establish, as a standard procedure, a single CPF account for the deposit of all counterpart funds. CPF from this account would be released in support of a priority expenditure programme as defined under guideline 1.

B. Guidelines on Management of CPF in Adjusting Countries

1. CPF generated from foreign assistance are budgetary resources accruing to the recipient country to be managed in the framework of a single and coherent budgetary policy (investment and recurrent budgets and, through them, the operations of the parastatal sector) in the context of a policy reform programme. Within such a budgetary framework, an important component should be a priority public expenditure programme that would broadly include outlays for investment, development and economic rehabilitation projects, and recurrent operations for essential maintenance and other productive socio-economic services.
2. Bilateral donor-recipient agreements on CPF management must be consistent with the objectives of external adjustment, non-inflationary growth, and the priority public expenditure programme agreed between the recipient country and the BWIs, taking into account the views of the donor community. Donors should give priority to supporting reform policies, including budgetary policy, when seeking agreement on CPF management.
3. The effectiveness of adjustment assistance depends on the policies and institutional reforms implemented, including those related to public expenditures. The recipient country, with the assistance of the donor community and the BWIs, should closely monitor public expenditure programmes, both investment and recurrent, to ensure that public sector resources are channeled in accordance with the priorities defined in the budget to address efficiency and equity considerations.
   Effective procedures for monitoring budget implementation should be ensured through provision, where appropriate, of technical assistance.
4. In providing recipient countries help with budget policy formulation, implementation, and monitoring for both investment and recurrent outlays, the BWIs should take into account the donors' views and financial support to a given country, at a sufficiently early stage in a flexible and pragmatic way.
5. All CPF of each donor should be consolidated in a single account by donor at the Central Bank consistent with that donor's statutory regulations. They should be used to finance broad budgetary headings of on-budget priority public expenditures as defined under guideline 1.
6. At the time of formulating next year's budget and its priority expenditure programme, the appropriate treatment of any outstanding balance on the CPF account at the end of a fiscal year as well as the new CPF creation projected for the following fiscal year would need to be considered. The use of the CPF account would continue to be flexible and consistent with the objectives of external adjustment and non-inflationary growth under the adjustment programmes agreed with the BWIs. It should be recognized that, in the light of these macroeconomic objectives, it may become necessary for donors to sterilize totally or partially in a coordinated way the past accumulations of CPF and/or the new creation of CPFs.
7. In order to ensure an efficient CPF management, the donor and the recipient, to the extent possible, should plan a multi-year rolling programme of food aid, and, subject to adequate policy performance, of adjustment assistance.
8. In the case of commodity/food aid, donors should value commodities either on the basic of import parity prices or on the basis of a pricing agreed under the policy reform programme, and should agree on a common time period by which CPF have to be deposited.
9. It is important that the role of CPFs in generating revenues for the government budget can be monitored. Donors should agree with the recipient government in each SPA country on a common format for reporting on CPF payments due to be collected from importers, and amounts actually paid.

(1) The proposals made concern the following countries: Burundi, Ghana, Madagascar, Mozambique, Burkina Faso, Rwanda.

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