odi Poverty Briefing
5: May 1999

Making Adjustment Work for the Poor

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The picture in brief

Many developing countries are engaged in structural adjustment programmes (SAPs) sponsored by the IMF and World Bank. Evidence about the effects of these programmes on poverty remains tentative but it suggests:

- SAPs have revealed little ability to reduce poverty by accelerating growth, partly because of extensive slippage in implementation.
- SAPs have often been associated with growing inequalities or have been unable to prevent them. Most measures have impinged particularly adversely on the urban working poor, but devaluation, import liberalisation and export promotion measures have benefited a number of poor groups.
- Programmes are somewhat peripheral to the causes of poverty and are therefore unlikely to make a large impact in either direction. They do try to tackle some sources of low incomes and to stimulate job-creation, but results have been disappointing.
- SAPs have not made a decisive difference to social service provision, which has generally been among the more protected categories of government spending. However, there is little evidence of a shift in the composition of such spending towards primary level services which are more beneficial to the poor.
- Safety nets – intended to protect retrenched civil servants and other vulnerable groups – have had an improving record but are subject to severe limitations.
- Political realities usually do not favour the poor and many governments have proved reluctant to give high priority to poverty reduction. Policies based on the existing distribution of power often cannot easily be changed because those who benefit are often influential enough to block reform.

Overall, the strongest criticisms that SAPs cause poverty are not born out, and concern about poverty effects is not a sufficient reason for deferring adjustment. But SAPs have done avoidable harm and could made be more pro-poor.

Some challenges

- SAPs should be designed to minimise the costs and maximise the benefits to poor groups and pro-poor measures should be integral to the design of programmes. Particular care is needed when changing government spending patterns and with other fiscal measures. Safety nets should be improved particularly in the participation of, and accessibility to, poor groups.
- Even the most poverty-sensitive SAPs cannot be more than a modest part of an attack on poverty. The causes of poverty are better treated if governments adopt comprehensive longer-term anti poverty strategies rather than concentrating on improving SAP design. The need is for positive rather than ameliorative measures; improving rural infrastructure, providing better primary health and education services and treated water etc.

This series of Poverty Briefings aims to provide up-to-date insights on the issue of poverty, including the state of current understanding or opinion. Each paper covers new as well as old thinking on the issue, areas of debate, new approaches which are being tried, the options available, and the recent findings of research and experience.

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ODI wishes to acknowledge grants from the Swedish International Development Cooperation Agency and the UK Department for International Development towards this series. However, the opinions expressed are those of the authors.

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No simple answers

For at least the last decade there has been concern about the social effects of 'structural adjustment' programmes sponsored by the International Monetary Fund and World Bank. Many poor developing countries – particularly in Africa – are still undertaking such programmes and international debt relief remains conditional upon them. This paper summarises the evidence about the effects of SAPs on poverty and looks to ways these might be made more beneficial.

Even now, after nearly two decades of adjustment, no definitive judgement is possible – a fact which reflects the large difficulties standing in the way of definitive research. The obstacles are formidable. Above all, there is the problem of the counterfactual, which asks whether programmes have resulted in a better situation than would otherwise have obtained. The counter-factual cannot be observed, of course. It must instead be simulated. But neglecting the issue can seriously distort results or the way they are interpreted, with the temptation to attribute to SAPs deteriorations which are actually the result of the economic situation necessitating policy changes.

The research difficulties are further compounded by the sheer complexity of the poverty problem. There is no single class of 'the poor' and poverty groups must be defined according to the ways in which they fit into the economy and are affected by adjustment measures. Take, for example, the effects of a devaluation. This can be expected to benefit poor farmers producing cash crops, who will enjoy higher prices. It may also increase the prospects for employment in production of exports or import substitutes of the landless and the urban unemployed. Against this, the urban working poor are likely to suffer because of the inflationary effects of the currency depreciation, while the effect on rural food-farmers is indeterminate.

These complexities mean that it is difficult to generalise about overall effects. Thus, among smallholders there are liable to be differences in impact on those who are net buyers or sellers of food. Even more importantly, there are liable to be major differences in impact as between urban and rural poverty groups – but households often have a foot in both rural and urban economies. With most of the poor living in rural communities, changes in rural policies are likely to be particularly strong influences. A further complication is that it is rather rare for a given instrument to have unambiguous consequences for poverty, as already illustrated for the case of a devaluation. Most measures stand to harm some groups and benefit others. Often, measures have both income-raising and price-raising effects, giving rise to net benefits or detriments that differ across groups. Note, however, that the urban working poor are particularly put at risk.

In the face of these difficulties, this paper is organised around two questions: *Did adoption of a SAP cause an increase or decrease in poverty?* and *Was the SAP designed to promote the welfare of the poor?*

Have SAPs caused poverty?

Growth effects have been weak. One of the strongest results of recent research is that changes in measurable (income) poverty are most strongly influenced by the pace of overall economic growth. Poverty rarely declines in stagnant economies but it usually diminishes in rapidly-growing economies. Moreover, the evidence suggests, surprisingly, that the poorest groups also usually participate in the benefits of growth.

A crucial question, then, is whether SAPs have enhanced economic growth. So far as low-income countries are concerned, there is little convincing evidence that they have. Neither the IMF nor the World Bank have been able to demonstrate a convincing connection, in either direction, between SAPs and economic growth; most independent research similarly does not find a systematic connection. On this evidence, SAPs have little effect on poverty by stimulating growth – or by holding it back

This conclusion needs to be qualified, though, for there is evidence of positive association between SAP implementation and economic outcomes: well executed programmes are associated with faster growth. Implementation is often weak, however. One symptom of this is that SAPs have high mortality or interruption rates. Well over half of IMF programmes break down before the end of their intended life and, on average, Bank programmes take twice as long to complete as intended. Both shortcomings are largely due to non-implementation of policy conditions.

A further symptom of poor implementation is that programmes have only modest impact on key policy variables, even less on institutions. There is little evidence that IMF programmes exert restraint on domestic credit, although they do strongly influence exchange rates. There is also quite a strong association with reform of other price variables, such as interest rates. But SAPs have much greater difficulty in influencing institutional change, e.g. financial sector reforms and privatisation programmes.

Distribution effects have been obscure: Changes in income poverty can be broken down into changes resulting from the growth of incomes and from changes in the distribution of incomes. The evidence suggests that growth effects generally dominate but also that the responsiveness of poverty to economic growth is adversely influenced by the extent of inequality at the beginning. Unfortunately, there is evidence from a number of Latin American and some African countries that inequalities are tending to grow, and that in Africa they are often as large as the extremes usually associated with Latin America.

But what of the impact of SAPs? The evidence here is quite limited. No-one disputes that SAPs can have powerful distributional consequences, but these are likely to affect various groupings differentially, which makes it hard to generalise about overall effects. The most we can say is that it appears that SAPs have often either been associated with, or have been unable to prevent, growing inequalities.

What of the position of women, who are often regarded as being put particularly at risk by adjustment policies? Here too a dearth of systematic evidence makes it difficult to get far. SAPs may impact adversely on women constrained by household duties and discrimination in credit, product and labour markets from taking advantage of the new opportunities which SAPs may create. Some traditional divisions of labour in the rural economy, in which the menfolk are responsible for cash crops while the women grow the food, would tell against women when SAPs shift prices in favour of export commodities. However, a contrary speculation suggests that, since the incidence of poverty among households headed by women is greatest in rural areas and poverty in the towns is related more to the low-incomes of male household heads, then SAPs which shift relative incomes in favour of the rural economy may improve the relative position of female-headed households.

Unfortunately, there is precious little evidence that is more than anecdotal against which to test these speculations. Moreover, what does exist produces mixed results. We suspect, but do not know, that SAPs impinge particularly on poor women.

SAPs have little impact of the causes of poverty: Given the inconclusive nature of much of the evidence, we can instead examine the attributes of poverty groups, and the causes of their poverty, to assess the likely effects of the policy content of a given SAP. A bald summarisation of the chief causes of poverty is set out in the Box, organised under the headings of (a) incomes and productivities, (b) social-political factors and (c) inequalities.

What has been the impact of SAPs on these causes? Apart from the impact on government services, taken up below, the evidence does not add up to much. SAPs are not intended to address the demographic factors contributing to the poverty problem, nor the civil and political strife which aggravate it (although SAP conditionality is increasingly addressed to 'governance' issues). SAPs can do little for the empowerment of the poor. They are not addressed to the initial inequalities which aggravate the poverty problem. SAPs are addressed to some of the sources of low productivities which underlie the poverty problem, and to correcting past capital-intensity by raising the cost of capital relative to labour, but the responses of low-income economies to measures intended to shift prices in favour of job-creation have been disappointing. Overall, SAPs emerge as somewhat peripheral to the causes of poverty and are therefore unlikely to make a large impact in either direction.

Not adjusting is worse for the poor: We should remind ourselves of the problem of the counterfactual. The issue is whether adjustment has resulted in more or less poverty *than would otherwise have occurred*. The most substantial research which grapples with this problem was undertaken in an OECD study. For most of the economies covered by this project the results of alternative policy stances were compared with the outcomes of the adjustment measures actually chosen. When the option of not adjusting was simulated the results were conclusive: defining non-adjustment as governmental refusal to modify budgetary, monetary or exchange policies, the simulations found *all* adjustment policies were better for economic growth, and more equitable, than not adjusting.

Have SAPs protected the poor?

There are two chief aspects to look at here: (a) the ways in which the composition of government spending has been changed by the introduction of SAPs, particularly the social services, and (b) the effectiveness of 'safety-net' provisions designed to alleviate programmes' possible poverty-worsening effects.

SAPs have not made a decisive difference to social spending: To summarise drastically, research on the effects of SAPs on state spending points to the following conclusions:

- The interest cost of servicing public debt, domestic and external, has been rising in many countries, placing a squeeze on non-debt spending.
- When faced with the necessity to cut (non-debt) spending, governments generally try to protect social spending, with the heaviest cuts falling on capital budgets and economic services, so that social spending actually tends to claim a rising share of total non-debt spending.
- This relative protection has not prevented large absolute declines in social service provision in some (especially African) countries. This has often been worsened by a deteriorating quality of services (schools without books, clinics without medicines...). However, IMF data show increasing real per capita social spending in its programme

The Causes of Poverty in Developing Countries

Incomes and productivities: Since economic growth is the dominant influence, poverty should be seen as resulting from inadequate incomes and productivities, particularly in agriculture and other rural activities and in the urban informal sector. The poor have inadequate access to educational and other services, leaving them with few modern skills. Largely as a result, the assets of the poor have low productivities, reflecting weak ability to participate in modern production processes and little access to formal sector credit.

Socio-political factors: Economic dependency is a factor perpetuating poverty, i.e. a concentration of the un- and under-employed in poverty households, and exceptionally large family sizes resulting in heavy child dependency. Political fragmentation and civil strife are other potent forces. There is also the issue of power. The poor have little market power and this, in combination with often undemocratic political structures, feeds into weak political power. Additionally, political traditions are often top-down, excluding participation of the poor even in programmes intended to assist them.

Inequality: For a given total national income the amount of poverty will be a rising function of the degree of inequality. Inequality is typically large in many African and Latin American countries, with a more mixed picture in Asia. Capital-intensive growth, with a weak growth in job-creation, perpetuates poverty because access to jobs is of enormous importance to the poor, as a direct source of income and as the basis for the urban-to-rural remittances which are so important to many poor rural households.

Inequalities *within households* are a further aspect. These often disadvantage women, who frequently have fewer rights to productive resources and household income, are expected to shoulder a disproportionate share of housekeeping and child care, have poorer diets, suffer from greater insecurity, and often have an inferior say in household decision-making. In consequence, the gender dimension of poverty is now universally accepted as requiring special attention.

countries.

- Comparisons of expenditure patterns in SAP and non-SAP countries reveal little systematic difference, suggesting that programmes *per se* are not particularly a source of regressive budgetary cuts. This is reinforced by findings of a positive link between social spending and programme implementation: it may be that the worst outcomes are in countries which adopt SAPs but only half-heartedly.
- In many cases, SAPs have not been able to improve the quality of government spending. Micro-level changes in social spending patterns often reinforce the tendency for the richer portions of developing-country populations to capture a disproportionate share of social services, with shifts away from the primary education and preventative medicine services that bring greatest benefits to the poor.

Safety nets have had a mixed but improving record: Since about the end of the 1980s safety-net provisions have been increasingly employed to protect groups particularly vulnerable to adjustment measures, notably public-sector employees who lose their jobs as a result of civil service reforms and privatisations. These schemes have included targeted subsidies and transfers of various kinds; employment-creation and retraining schemes; and special infrastructural development schemes in poor areas. Early evidence suggested they had made little impression, reaching only a small fraction of the targeted poor and with regional, gender and class biases. But lessons have been learned and later results are more encouraging. Targeting and project designs have improved, and schemes have been made more accessible to the poor. However, their international sponsors are at pains to stress the limitations of what has been – or can be – achieved by safety net measures in the absence of a wider anti-poverty strategy.

Political realities do not favour the poor: One reason why safety net provisions have had a mixed record is that there has often been a trade-off between using these to assist vulnerable people or to compensate politically powerful special-interest groups who stand to lose from adjustment. This is an example of a wider difficulty: the apparent reluctance of many governments to place poverty reduction high among their priorities. The policies in place when a SAP is adopted are not accidental, the outcome of purely technocratic considerations. They also reflect the distribution of political power.

This helps explain the biases in educational and health budgets in favour of middle class users. Similarly, policy biases towards urban dwellers and the middle class – and the common difficulty, therefore, of shifting relative prices in favour of agriculture – reflect their greater potential for creating political trouble. Policies based on the existing distribution of power therefore often have large inertial force, difficult to change because those who benefit are often influential enough to block reform and to prevent targeting resources on those most in need of them.

Conclusion: the ill-effects of SAPs has been exaggerated ... but they should be made more pro-poor

Overall, the evidence surveyed above does not support the strongest allegations of those who criticise SAPs for causing poverty. However, adjustment programmes have had consistently adverse effects on the urban working poor, have had little demonstrated compensating ability to improve economic growth, have been unable to prevent widening inequalities and have often not effectively protected those placed at risk. While concern for the welfare of the poor is not a good reason for rejecting adjustment, more could be done to reduce programmes' ill-effects on vulnerable people. Some principles of policy are suggested:

- SAPs should be consciously designed so as to minimise the costs and maximise the benefits to poor groups – a principle that the IMF, in particular, has never accepted – and pro-poor measures should be integral to the design of programmes. Particular care should be taken with measures changing government spending patterns, and with other fiscal measures.
- Positive measures are better than ameliorative responses: strengthening the rural infrastructure, provision of primary health and education, and of treated water. Export promotion also has a good pro-poor record.
- Safety net provisions should continue to be improved in the light of emerging experience, particularly to improve participation of, and accessibility to, targeted groups.

Lastly, it is important to appreciate that even the most poverty-sensitive SAPs cannot be more than a peripheral part of an attack on poverty and that the cause of poverty reduction is not best served by excessive concentration on improving their design. What is needed most of all is for adjusting governments also to adopt comprehensive anti-poverty strategies, of which SAP measures can then form part.

References

This paper is based on Killick, T (forthcoming) *Adjustment, income distribution and poverty in Africa: a research guide*. Nairobi: African Economic Research Consortium. It provides full citations for the studies referred to. Mimeographed copies are available from ODI (£2.00). Other recommended readings include:

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 ISSN: 1465-2617

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