



COMMISSION OF THE EUROPEAN COMMUNITIES

Brussels, 04.02.2000
COM(2000) 58 final

**COMMUNICATION FROM THE COMMISSION
TO THE COUNCIL AND THE EUROPEAN PARLIAMENT**

**Community support for economic reform programmes
and structural adjustment:
review and prospects**

EXECUTIVE SUMMARY

Support for structural adjustment programmes has become an integral part of the Community's financial and technical co-operation with ACP countries from Lomé IV onwards. This was extended to Mediterranean countries in 1992 in the context of the Redirected Mediterranean Policy. Since then, the Community has given significant financial support to structural reform, amounting to 2,334 million euros for 40 ACP countries and 705 million euros for 4 Mediterranean countries.

This Communication discusses the evolution in the support programmes. This discussion shows that the instrument has been increasingly used in favour of wider economic reforms as opposed to traditional economic stabilisation issues. This evolution is explained by the fact that in general macro economic conditions have improved, as well as by the change in the nature of the relationship between partner countries and the Community. In the Lomé context innovations are foreseen within the "post-Lomé" framework, while for the Mediterranean countries the Euro-MED initiative of 1995 has given rise to a re-definition of the relationship between Mediterranean countries and the Community.

The Community has also participated actively in the international debate on structural adjustment, especially in the context of the Special Programme of Assistance for Africa (SPA). In accordance with Council-approved guidelines, the Community has always advocated a long term view of reform processes, that is going beyond short term adjustments primarily based on financial stabilisation measures and uniform and pre-determined packages of reform.

The Communication confirms that three basic orientations of the instrument remain valid. This concerns firstly the importance of a stable macro economic framework that supports economic growth and consolidates internal and external macro-economic balances. Secondly, the poverty focus of the instrument is essential. This is fundamental in its own right, but also because fighting poverty is needed to ensure the necessary support for the sometimes-painful reforms needed. Lastly, developing stronger regional links within regions remains a priority; domestic markets of partner countries are small, while regional co-operation is now recognised as a source of economic dynamism and diversification.

This Communication underlines the need to deepen the Community's support for structural- and sectoral reforms. In that context, the Communication identifies the following priority issues: support for enhanced poverty reduction focus support for sound public finance management, support for fiscal- and tax reforms, and support for private sector development.

As for the management of the instrument and the evolution of the aid modalities, the Communication highlights:

- *the importance of a better integration of the instrument into the bilateral co-operation frameworks;*
- *the progressive abandonment of the use of import programmes in favour of direct budgetary support;*

- *the need for a strong Commission role, together with Member States, alongside the Bretton Woods institutions. Care should be taken that partner countries are not unduly burdened by different demands: there can only be one programme of economic reforms in a given country;*
- *the growing importance of support for specific sector programmes, in particular those that are linked to so-called 'second generation type of reforms' or linked to the implementation of association agreements;*
- *the need for improved monitoring- and evaluation mechanism with a view to increase transparency, improve programme design and enhance ownership. The development of performance indicators is envisaged and this might pave the way for performance-related allocations.*

The implementation of the conclusions of this Communication should be gradual and flexible, so as to take into account the diversity of conditions in partner countries.

Contents

1.	Introduction	5
2.	Support in ACP Countries.....	7
2.1.	Assessing past support	7
2.2.	Factors affecting future prospects.....	12
2.3.	Prospects and guidelines for the future	15
3.	Support in eastern and southern Mediterranean Countries	21
3.1.	Introduction	21
3.2.	Assessing past programmes.....	21
3.3.	Prospects and conclusions	25
4.	Conclusions and Guidelines for the Future.....	27
4.1.	Lessons from recent experience.....	27
4.2.	New relationships.....	28
4.3.	Priority issues	28
4.4.	Working methods and management.....	29
	Implementation	30
5.	Annexes.....	31
5.1.	Annex 1 List of decisions under the 7 th and 8 th EDF.....	31
5.2.	Annex 2 Impact of the programmes on medicine and vaccination policies.....	33
5.3.	Annex 3 Test case: reform of conditionality in Burkina Faso.....	34
5.4.	Annex 4 Weaknesses in current working practices	35
5.5.	Annex 5 Community Support to Mediterranean countries	36

1. INTRODUCTION

The Community first became involved in supporting structural adjustment processes in 1991 following the finalisation of the negotiations for the fourth Lomé Convention with the ACP countries. A first interim report laying down guidelines and detailed arrangements for this support led to a Council resolution in May 1992. In parallel, a Council Regulation of June 1992 introduced the possibility to extend assistance to Mediterranean countries in the form of structural adjustment support.

Based on the experience gained and on the evolution of the two instruments, a Council Resolution was adopted, which contained the following policy guidelines:

- consolidating the existing approach, endorsing the Union's main priorities as regards the long-term implications of adjustment programmes, integrating them into a regional framework, the social dimension and ownership;
- deepening positive aspects such as improvement of public finance, integration of programmes into regional or trade facilitation frameworks, promotion of a favourable environment for the private sector and for investments;
- broadening action by refining instruments and procedures (move from import support to direct budgetary support), reflecting on a new approach to conditionality and strengthening Community and donor co-ordination, particularly with, as well as, within the Bretton Woods Institutions;
- introducing more flexibility in the management of the instrument by adapting to the diverse country contexts. In particular, for the Mediterranean countries, the need was emphasised to situate support programmes in the context of future free trade agreements with the EU.

Since that time the Community gave considerable financial support to adjustment programmes implemented by the ACP or MED countries. A quick overview is given in the following table.

<i>ACP</i>	<i>Commitments (ECU million)</i>	<i>No. of programmes</i>	<i>No. Of countries</i>
7 th EDF	1,695	93	38
8 th EDF	639	24	24
<i>MED</i>			
4 th Protocol + MEDA	705	10	4

Support programmes related to the two regions have undergone several internal assessments and external evaluations, which concluded that important achievements were made in macro-economic stabilisation and the implementation of fundamental structural reforms. However, the impact on the welfare of the populations concerned was mixed.

The new international economic context (especially following the Asian and Russian financial crises), as well as the evolution of the co-operation frameworks in the two regions, call for a re-assessment of Community support to economic reforms and structural adjustment. This reflection has to take account of the broader international debate on the future prospects of development aid.

An important contribution to the international debate was the external evaluation, published in 1998, of the IMF's support under the Enhanced Structural Adjustment Facility (ESAF). The evaluation concluded that insufficient attention had been paid to the impact of reforms on poverty, to the pace and sequencing of reforms as well as to the issue of ownership. The evaluation also highlighted the need for support programmes to explicitly address the issues of corruption and poor public resource management.

There is now a consensus on the need to address economic and social problems jointly, to prioritise "ownership", institution building and sound management of public finances, including tackling corruption, and to place the fight against poverty at the centre of macroeconomic reform programmes. In summary, to concentrate more on the results of reform programmes designed by the countries themselves.

Given the broader scope of structural reform programmes, the main donors have progressively modified their support instruments to increase the coherence of their interventions. For instance the World Bank has adopted the Higher Impact Adjustment Lending and the IMF has replaced the ESAF by a new Poverty Reduction and Growth Facility. The Community will further integrate its structural adjustment resources in the broader context of its new co-operation frameworks : future post-Lomé agreement and the Association agreements with Mediterranean countries.

This Communication presents of the experience gained in the two sets of countries – ACP (chapter 2) and Mediterranean countries (chapter 3) – and it presents conclusions and prospects for the future (chapter 4).

2. SUPPORT IN ACP COUNTRIES

2.1. Assessing past support

An assessment of Community support to structural adjustment programmes under the 7th EDF and in the first year of implementation of the 8th EDF shows that the Community has been a key player in the ACP countries in both quantitative and qualitative terms.

The conclusions set out below are drawn from an internal assessment carried out in September 1998, covering 96% of amounts financed between 1991 and 1997 under the 7th EDF, and from 14 external evaluations¹ covering around 50% of the financial volume of Community support programmes to ACP countries. Additional data comes from monitoring of the 23 new programmes committed in 1998 under the 8th EDF.

2.1.1. Overview of financial support

Community support has gone to those countries implementing reforms approved by the Bretton Woods Institutions, which thus automatically qualify for Structural Adjustment Facility (SAF) resources under Lomé IV.

The 93 programmes implemented under the 7th EDF have involved 38 ACP countries to the tune of ECU 1 695 million - ECU 1 142 million from the Structural Adjustment Facility (SAF) and ECU 553 million taken from National Indicative Programme (NIP) funds. To these amounts must be added the funds committed for 24 countries in the first year of the Second Financial Protocol of Lomé IV (8th EDF), i.e. ECU 639 million (ECU 594 million from the SAF and ECU 45 million from the Nips).

These programmes are listed in Annex 1.

In addition to the funds to support structural adjustment, around ECU 715 million in Stabex resources were used in the same period to support structural and sectoral adjustment efforts.

It is worth stressing the significant role of the European Union (Member States and Community) in supporting adjustment programmes for the countries covered by the Special Programme of Assistance for Africa; the EU accounted for almost 40% of all adjustment aid in the period 1991-1996. If one counts the Union's contribution via the Bretton Woods Institutions, it accounts for more than 60% of financial support. Community support alone made up nearly 13% of support for structural adjustment from all donors. This figure should rise to 15 or 20% in the 1997-2000 period, testifying to the growing importance of Community support for the balance of payments and budgets in SPA countries.

A certain geographical concentration of funding is evident, given the needs and performance of the countries implementing reform programmes. African countries received 95% (Caribbean countries 4% and Pacific countries 1%) and seven countries (Burkina Faso, Côte d'Ivoire, Ethiopia, Ghana, Mali, Tanzania and Zambia) received more than 50% of funds available under the 7th EDF. Least-developed countries received 70% of the funds.

¹ Evaluations carried out by teams of external consultants between 1995 and 1997 in : Benin, Cameroon, Côte d'Ivoire, the Dominican Republic, Ethiopia, Ghana, Guinea, Malawi, Mali, Mauritania, Tanzania, Uganda, Zambia and Zimbabwe.

Support for structural adjustment represented roughly 22% of all EC development aid to ACP countries, ranging from 8% for Burundi to 46% for Ghana.

The criteria governing allocation between countries, under the 7th EDF, were based essentially on the need for foreign and domestic funding. The latter was estimated based on population size. The criteria have recently been changed to give priority to the poorest countries and those performing best in terms of economic and social policies, democracy and sound management of public finances (see Annex 2).

2.1.2. Arrangements for implementing programmes

Under the 7th EDF, support for structural adjustment was given through General Import Programmes. These supported the balance of payments with hard currency, which generated an equivalent amount in local currency, so-called Counterpart Funds, which financed the countries' budgetary expenditure.

When the Lomé Convention was revised in Mauritius, it became possible for countries with convertible and freely transferable currencies to receive direct budgetary support, enabling simpler administrative mechanisms to be used. This shift, in line with World Bank and IMF recommendations, meant that most support under the 8th EDF could be given in this way.

2.1.3. Objectives and results

In line with the objectives in the EU Treaty and with guidelines adopted by the Council in various resolutions, Community support has aimed to further integrate the developing country economies into the world economy, to combat poverty and promote sustainable economic, social and human development. In this context, one of the Community's prime concerns has been to protect and increase budget expenditure in the social sectors.

There can necessarily be only one macro-economic reform programme per country. It is this programme that the Community supports, once the programme has been approved by the Bretton Woods Institutions.

The Community's structural adjustment support has consisted of three key elements: policy dialogue with governments on the content of reform programmes (conditionality), use of the local currency (counterpart funds) generated by the sale of the foreign exchange provided by the Community support programmes (targeting) and institutional support (technical assistance).

The evaluations of Community support show that the Community has not always known how or been able to work with the ACP countries and the Bretton Woods Institutions to significantly impact the design of reform programmes. Community contributions have often been restricted to sectoral issues. This has in part been due to the reticence of the Bretton Woods Institutions to open up negotiations to other donors, but also to staffing restrictions in the Commission. For some time now, however, the Bretton Woods Institutions have been more willing to involve the Commission in negotiating programmes at least in certain countries.

Similarly, co-ordination between Member States, while generally satisfactory on the ground, is virtually non-existent in the Boards of the Bretton Woods Institutions. If co-ordination existed in these fora, the EU's role in policy development would without doubt bear more relation to its financial contribution.

2.1.3.1. Conditionality of Community support

Community support has been systematically conditional on the satisfactory implementation of the macroeconomic reform programme agreed with the Bretton Woods Institutions.

Beyond this, support for structural adjustment has often stimulated in-depth discussion on government policy that has led to disbursement conditions reflecting commitments made in supported sectors or fields. These specific conditions, consistent with the overall reform programme, have prompted a detailed dialogue as regards programming and budgetary execution, sectoral policies, institution building and regional integration.

The different external evaluations² show that Community support has enabled several countries to maintain or increase their education and health budgets and favoured vital reforms in healthcare and primary education systems, pharmaceutical policy and drug supply (see Annex 3), national road maintenance provisions, administrative decentralisation and other priority areas. More appropriate institutional instruments have been put in place, more equitable and transparent funding practices have been developed and the respective roles of government, private sector and civil society have been redefined, leading to civil service reforms. Support for structural adjustment has therefore been a powerful agent for change.

Another feature of Community support has been a growing emphasis on budget execution and the sound management of public finances. One of the main concerns has been to improve the budgetary process (programming, administration and monitoring of public expenditure) at both national and local government levels. The aim has been to consolidate reliable and transparent national procedures, particularly as regards public procurement, even if they have shown to be still insufficient.

Nevertheless, the evaluations highlighted a number of weaknesses or shortcomings regarding the impact of Community support:

- the objective of reducing poverty has too often been addressed solely via support for the social sectors, with insufficient attention given to questions of equity (both in term of income and gender) and the impact of economic policies on the distribution of wealth as defined in the 1993 Council resolution³;
- while many programmes have helped maintain or increase budgets earmarked for the social sectors, this has not always resulted in (i) the availability of funds in the most remote areas nor (ii) in improvements in services to the population (for example school and health centre attendance rates have sometimes dropped).

2.1.3.2. Targeting of Counterpart Funds

Apart from helping with the balance of payments, the implementing arrangements attached to Community support have sought to promote satisfactory execution levels for the types of

² See footnote 1

³ Which followed on the Communication on policies for poverty reduction of November 1993

public expenditure the Community wishes to prioritise, foremost of which has been non-salary recurrent expenditure in the social sector budgets.

In this context, the counterpart funds generated by the support have been used, in line with the Lomé guidelines, to favour health (35% of the funds) and education (30%). Among the other priority sectors have been road maintenance (8%), administrative decentralisation (3%) and rural development (3%). As for expenditure types, priority has been given to non-salary recurrent expenditure over investment and relieving domestic debt.

In many countries, the entire health and/or education recurrent budget (apart from salaries) has been secured, which has led to generally satisfactory levels of budget execution.

In other countries, the effectiveness of targeting has been more dubious as it has sometimes had undesirable effects. These include: (i) the imposition of donor specific procedures normally applied to traditional projects, and (ii) delayed implementation of budgets because onerous checks are required or the rationale of budgetary support is poorly understood.

2.1.3.3. Technical assistance

Often, Community support to structural adjustment programmes has involved technical assistance aimed at monitoring Community support and at strengthening the countries' institutions. Technical assistance focused on developing economic and sectoral policies or improving the procedures for drawing up and executing budgets. TA has also facilitated audits and programme evaluations and participation, with the World Bank and other donors, in numerous public expenditure reviews.

2.1.4. *Areas of particular concern*

It is worth underlining the efforts to make instruments more coherent and to facilitate specific actions relating to regional integration and debt alleviation.

2.1.4.1. Greater coherence between instruments

The Community has tried to improve the coherence and convergence of its aid instruments, particularly the support to structural adjustment and the National Indicative Programmes. In addition, a large proportion of Stabex and (more recently) food security assistance funds have been given, in line with structural reforms, in the form of budgetary support.

2.1.4.2. Support for regional integration processes

Particular importance has been attached to supporting regional integration processes, especially through the West African Economic & Monetary Union (WAEMU) and the Cross-Border Initiative (CBI). Funds of around ECU 100 million were set aside for countries that embarked on this course. The funds were added to structural adjustment grants and disbursed when reforms were actually implemented. This support was provided to offset the transitional costs of tax and/or customs reforms and to support liberalisation measures. Significant support was given in this context to capacity building.

2.1.4.3. Support for the Debt Initiative for the heavily indebted poor countries (HIPC)

Community financing for the ACP countries is basically given in the form of grants, the only loans that remain since Lomé IV being risk capital and loans from the EIB's own resources.

Hence, the Community's present role as a creditor is quite marginal (accounting for around 2% of the HIPC's debt stock).

Consequently, it is not only as a creditor but also as a donor that the Community has from the outset given its full support to the World Bank / IMF initiative to tackle the debt burden of the heavily indebted poor countries (HIPC). A salient feature of the initiative is that a country is deemed eligible (the "decision point") following a track record of reform. However, before receiving actual debt alleviation (the "completion point") the country must continue to implement reforms during an "interim period". These adjustments have a social dimension, which is important to support and promote. Nonetheless, the reforms carry social and fiscal costs and the Community wished to provide support during the interim period as well as reinforce the social content of the alleviation process.

Concretely, the Community incorporated a HIPC dimension into its structural adjustment support programmes and increased its structural adjustment grants to countries that had qualified (i.e. past their decision points) throughout the interim period. Around € 36 million have been allocated to date (under the 8th EDF) to the nine countries concerned.

The Commission has proposed to Member States and ACP countries to accelerate, broaden and strengthen the HIPC initiative. Firstly, the considerable extra financing required for commitments already given (as a creditor and as a donor) must be secured. Secondly, a third dimension will be added aiming to contribute as a major development partner to the global financing of the reinforced HIPC. The Commission prepared a Communication in that spirit.

2.1.5. Contributing to the international debate

The Community has managed significant aid resources in a field that demands skills and close monitoring of macroeconomic conditions, with relatively few staff in comparison to those of the Bretton Woods Institutions. Participation in international fora has therefore emerged as one of the most effective ways of sharing the European vision.

Among these fora, special status has been accorded to the SPA (Special Programme of Assistance for Africa). The SPA was set up in 1987 and twice a year brings together, under the chairmanship of the Vice President of the World Bank, virtually all donors giving support for structural adjustment in sub-Saharan Africa. With its aim of mobilising quick-disbursing aid, the SPA has over the years become an essential forum for reflection on how this aid should be made more effective.

This approach has produced results: gradually, the Commission has been able to share with its partners the Council guidelines on structural adjustment programmes that are coherent with long term development and regional integration. This view of things has informed discussions on the so-called "second generation" reforms aimed at sustainable changes at the institutional level. The idea of short-term adjustment, based primarily on financial stabilisation measures and predetermined packets of reforms and liberalisation, is giving way to a more gradual and realistic approach with a greater emphasis on the welfare of the population and on reducing poverty.

The Community's concern has been to put these guidelines into practice, which is why its influence has been felt in more specific areas, such as: (i) discussions on reforming conditionality, (ii) integrating the regional dimension into structural adjustment, and (iii) moving towards sectoral reform programmes.

On the reform of conditionality, for instance, the Community has instigated a debate in the SPA aimed at increasing the effectiveness of quick disbursing balance of payments support. A test has been launched together with nine donors and the government of Burkina Faso. The goals of the test are: 1) to improve and reinforce the ownership of reforms of recipient countries, 2) to smooth aid flows and limit “stop & go” situations by adopting new disbursement modalities, 3) to favour a medium term outlook by looking at outcomes of reforms rather than at policy measures implemented and 4) to improve donor co-ordination through joint evaluation missions (see annex 4). The preliminary results of this test have contributed to the proposals in this communication.

On regional integration, the Community has put the case in the SPA for taking account of the regional dimension of adjustment. Other donors, particularly the World Bank and the IMF, have become increasingly aware of this dimension in the past few years and the objectives of harmonising and liberalising customs duties have featured more and more explicitly in adjusting countries’ policy framework papers. Macroeconomic convergence between neighbouring countries is now a commonly used concept. On a practical note, the Community has taken part in the “co-sponsorship” of the most significant regional integration processes (WAEMU and CBI).

In the SPA, the Community is currently co-ordinating a task group on sector programmes. The issues at stake are central for the future of co-operation: finding ways of improving countries’ ownership of policies and making aid more coherent, encouraging procedural harmonisation among donors, and moving from a project-by-project approach to a more global approach consistent with a country’s macroeconomic prospects. Here the Community has sought to promote sufficient flexibility, highlight the essential role of the ACP countries and bring donor views closer together.

Finally, as regards the fight against poverty, the 1993 Council resolution⁴ stressed the need to take account of the impact on poverty of global factors, especially the liberalisation of trade. It also pointed to the need to feed results from poverty surveys into the process of formulating macroeconomic policies and sectoral approaches. Both in the SPA and in the DAC (OECD), the Commission has accordingly drawn attention to the effect on poverty of changes in trade conditions, inter- and intra-regional issues, and the importance of political dialogue and institution building. These are all crucial factors in the future ACP-EU partnership if it is to achieve its objective of reducing poverty and integrating countries into the world economy.

2.2. Factors affecting future prospects

There are several factors in addition to the above that lead the Community to question whether current guidelines are entirely relevant:

2.2.1. Economic developments

Changes in the economic circumstances of the ACP countries reflect overall progress in terms of macroeconomic stability and growth. This progress is not sufficient, however, to have an impact on Africa’s marginalisation in the world economy or give grounds to hope for a sustainable reduction of poverty.

After years of stagnation, economic growth climbed to an average rate between 4 and 5% in 1996. Inflation is now under 10% in significant number of countries but. Between 1992 and

⁴ See footnote 3

1996, general public deficits dropped from 8% to 4% of GDP. Article VIII of the IMF Articles of Agreement is now accepted by more and more countries, bringing an end to restrictions on current payments and transfers. Controls on prices, contracts and exchange transactions have been reduced everywhere and significant progress has been made on reducing the role of the state in the productive sectors. Without question, structural reforms like this will be a springboard for better integration into the world economy.

Nevertheless, these achievements remain fragile and must be put in context. While an upturn is forecast for 1999, growth was unfortunately considerably less in 1997 and 1998 than in 1996:

Growth in sub-Saharan Africa: 1996-1999

	1996	1997	1998	1999 (forecast)
Average growth (%)	4.9	3.2	2.1	3.1
Number of countries with growth of > 5%	19	17	13	
Number of countries with growth of < 3%	9	11	14	

Source: World Bank

Moreover, this growth is still not enough to keep pace with continued increases in population (on average 3% a year).

The recovery of the mid-90s hinged largely on increasing use of existing production capacity and rises in the prices of basic commodities (apart from petroleum products) - two factors that are now lacking. Although the ACP countries were relatively sheltered from the effects of the Asian crisis, they were and will continue to be affected indirectly because of its impact on global demand and the prices of raw materials and basic products. The Pacific countries have been affected most, but the drop in terms of trade for the African countries has been put at 7.4% (equivalent to a loss of about 2% GDP). Also, there are natural limits to growth in the use of production capacity. With domestic savings having fallen steadily for 20 years, ACP economic growth will be sustainable only if countries can stimulate a savings recovery and attract external funds. Unfortunately though, it is precisely here that adjustment programmes seem to have come up against the greatest obstacle. Not only was the ACP countries' share of foreign direct private investment in 1997 only 2% of all private investment flows to developing countries, but it is actually shrinking and concentrated in a few countries. In fact, international investors are rarely interested in anything other than mining and petroleum and those sectors that are growing are doing so more and more on an offshore basis. This structural weakness is exacerbated by the fact that the ACP economies are very sensitive to any form of shock. They are often dependent on a small number of export products and are particularly vulnerable to natural disasters, climatic vagaries and world market price fluctuations.

Africa and the ACP countries in general are already marginal players in the world economy and are becoming more so: the ACP countries' share in European trade went from 6.8% in 1975 to 4.6% in 1997 (3.2% not counting South Africa), and sub-Saharan Africa's share of world trade has been in constant decline (from 3.3% of all exports in the 1950s to 0.8% in 1995).

There are a few additional remarks to make:

Firstly, to make a sustainable impact in terms of reducing poverty and to reverse the current trend of ACP marginalisation (in other words, simply to retrieve what has been lost in the past

20 years), these countries must achieve growth rates of at least 6-7% (far above present levels) accompanied by action on human development and the fight against poverty. This kind of growth surge will not happen without substantial private investment.

Secondly, generalised statistics conceal the extremely heterogeneous nature of the ACP group of countries - this is even more pronounced within sub-Saharan Africa than in the Caribbean or Pacific. The disparities are clearly visible whether one looks at average per capita income, social indicators or just rates of economic growth (which ranged in 1997 from -8.7% to +12.7% in Africa). Some countries with good prospects for growth are emerging as development “magnets”, often attracting unemployed labour from neighbouring countries. Others are plunging into civil conflict with more and more repercussions in the surrounding region. Still others are putting long years of conflict behind them and facing a considerable need for reconstruction.

Thirdly, growth is often spread very unevenly both between and within countries. The current tendency is for the gaps between industrialised and developing countries to get wider and wider. For 89 countries, most of which are ACP states, the economic situation is worse than it was ten years ago, although the world as a whole is getting richer. In many countries, growth is accompanied by greater disparities in the incomes of the richest and poorest groups.

Finally, alongside these changes, the international picture is marked by a reduction in official development assistance. Since 1990, ODA has fallen in real terms and in relation to the beneficiaries’ GNP, reaching 0.22% of donors’ GNP in 1997 (the lowest since the United Nations adopted the target of 0.7%). Moreover, an increasing proportion of these funds goes to alleviating debt, which has less of an impact on growth and development. If one takes the developing countries as a group, this reduction is partly explained by the fact that the share of the burden shouldered by private investors has grown considerably. Taking the ACP countries in isolation, however, the overall balance remains negative.

These points all show the need to continue supporting the ACP countries financially, but also to pay more attention to the private sector, the institutional framework and the implementation rate and sequence of reforms.

2.2.2. Political developments

There has been significant progress in a number of countries in recent years as regards respect for human rights, democratisation and strengthening the rule of law. Several dictators have given way to elected governments, parliaments have taken on a more important role, constitutional and judicial structures have often been reinforced. Recent studies have shown that the countries where this sort of effort has been made are also those that have registered the most economic success - showing the importance of taking this dimension into account. Effective counterweights and freedom of expression - both of which have improved noticeably in many countries - have proved the best ways of combating corruption.

Alongside these positive developments, though, the political situation in Africa has suffered some dramatic setbacks recently. In central Africa, several previously localised conflicts have developed into regional wars fought mainly on the territory of the Democratic Republic of the Congo, but also in Angola and Congo (Brazzaville). In parts of central Africa, but also in some west African countries and Somalia, administrative and legal structures have become very fragile or even disappeared altogether, which has led to a sharp rise in the number of human rights violations.

The weight that the EU attaches to respect for human rights, democratic principles and good governance will increasingly influence how the Community's adjustment support is allocated and how programmes are implemented.

Given its fungibility, there is a risk that foreign aid, particularly in the form of support for structural adjustment, will allow governments to free up resources for military purposes over and above the right of self-defence recognised in the United Nations Charter (Article 51). In response to the proliferation of armed conflicts and military operations, the Commission has submitted a communication⁵ to the Council and the European Parliament setting out ways in which the Commission and the EU could react.

2.3. Prospects and guidelines for the future

The assessment of Community support to date, the questions raised by recent financial crises and the criticism made of previous working methods (developed in annex 5) all argue in favour of moving to a second generation of reforms.

Such a change would be marked by the Community deepening and broadening its range of interests, by an increased concern with the impact of the reforms and how they fit in to a long-term vision, and by new working methods.

These guidelines will determine the Community's future position both in the international debate (more co-ordination with the Member States; continued active involvement in the SPA and the DAC (OECD)) and in its support to ACP countries.

2.3.1. Consolidating past achievements

Although necessary for the Community to broaden its range of interests, this must not be at the expense of consolidating important achievements. Support for macroeconomic reforms, the social sectors, regional integration and sound economic management will be maintained and intensified.

2.3.1.1. Maintaining macroeconomic stability will remain a priority

The Commission believes that the existence of a stable macroeconomic framework is one of the essential conditions of development. It is for individual states to react to external or domestic shocks, but it is imperative that foreign aid continues to support the poor countries exposed to such circumstances. Mobilising quick-disbursing aid in support of countries implementing structural adjustment policies will remain a priority.

2.3.1.2. The Community will continue to give priority to the social sectors

Attention will be given here not only to maintaining or increasing budgets, but above all to results in terms of access to basic health and educational services, particularly for women and girls, and in terms of the quality of the services. Central to this will be the degree of coherence between budgetary provision and declared sectoral policies, clarifying the roles of governments and households in financing basic services, and taking due account of private sector activities.

⁵ Co-operation with ACP countries in armed conflict.

Attention will be paid to the coherence between support given under structural adjustment programmes and that given in aid of sector programmes developed by the recipient country. The former permits a focus on issues of sound budget management, coherence between sector programmes and the macroeconomic situation. The latter support allows a more in depth review of specific sectoral policies. However, both types of support aim to assist the same policies and to increase the positive impact of those policies on the services rendered to the population.

2.3.1.3. Support for regional integration will be maintained

The Community believes that regional integration and co-operation are important means of promoting integration into the world economy. This is particularly so in the ACP countries where the limited size of markets acts as a brake on economic development. Support to these regional efforts will be continued, thereby favouring economic growth, a necessary - but not sufficient – condition for poverty reduction.

The negotiating mandate for a new partnership agreement with the ACP countries advocates the gradual setting-up of Regional Economic Partnership Agreements (REPAs) aimed at creating free trade areas conforming to WTO provisions. They presuppose consolidation of the integration process within ACP regional groupings, which will receive continued support in the structural adjustment context. Reforms in the context of regional integration do, however, often have temporary negative effects on public finances or on the competitiveness of domestic firms. During a transitional period, budgetary support will help to offset customs revenue losses and to encourage the implementation of fiscal reforms. Technical assistance will concentrate on matters related to the overhaul of taxation systems and on strengthening trade-related fields (standardisation, notifications, support services, etc.).

2.3.1.4. Existing concern for the sound management of public finances will be intensified

The Community will support efforts to promote the rule of law, administrations' ability to manage resources transparently and effectively, stronger control mechanisms to combat corruption, and to involve citizens' in decision-making. Budgetary support, whether direct or indirect (GIPs), brings with it the need to monitor the correct implementation of budgets. Particular attention will be given to three aspects: the execution rate of the budget, proper implementation (particularly in the most peripheral structures), and effective and transparent budgetary procedures. Similarly, attention will be given to the sound management of revenue. In this framework, Community programmes will provide the necessary institutional support, promote the involvement of civil society in drawing up reform programmes and seek to improve procedures for managing public finances.

2.3.2. *New challenges*

But the Community's attention will also be directed to new areas of concern in future structural adjustment programmes - equity, private sector development issues, taking account of conflict situations, and improving monitoring and evaluation systems (including the reliability of available statistical data):

2.3.2.1. A new dimension in the fight against poverty

The Community will attach special importance to the equitable distribution of the fruits of growth. It will look here both at overall changes and the effects of globalisation on the rich country / poor country divide, and at changes within countries (the impact of tax policies on

the incomes of different social groups; the impact of economic policies on employment). Specific studies could be carried out on the problems of exclusion, particularly in towns and cities. Support will focus on gender inequality, acting as a constraint to growth and poverty reduction, and role of women in economic structure. Findings will be fed into the debate at international and country levels to assist with the formulation of policies to combat poverty.

2.3.2.2. Private sector development

More attention will be paid to questions of private sector development. In line with the Council Resolution⁶ on the private sector, this will be done, in coherence with current support to the sector and other Community instruments. This focus will primarily be seen in the strengthening of the rule of law and a justice system that inspires confidence and the adoption of laws and regulations suitable for a market economy. Secondly, the Community will encourage a dialogue between the public and private sectors and a discussion on redefining the respective roles of government and the private sector. The Community will seek to support delegation of competence from the public sector to professional organisations and the private sector where this will lead to more effective management while retaining the spirit of public service. Finally, the transfer and development of new and appropriate technologies – vital to ensure growth in the developing countries – will be supported. The Commission will intervene in a complementary manner to other donors and will, given its expertise, focus on actions in aid of regional integration. The Commission will assist the adoption of rules to prevent public monopolies from becoming private oligopolies.

2.3.2.3. The political environment and conflict situations

The Community must react coherently and even-handedly when countries cease to respect the principles of democracy and human rights. Conflict situations will be addressed in accordance with the guidelines in the Communication of May 1999 on “Co-operation with ACP countries involved in armed conflict”.

2.3.2.4. More effective monitoring and evaluation systems

Improved monitoring and evaluation systems are vital to improvements in transparency and the monitoring of the impact of reforms. The Community will support the development of reliable monitoring and information systems that are easy and quick to use, help decision-making in the social sectors, public finance, in monitoring the impact of sectoral policies. In particular, these systems should exploit new technology.

The Community will also support an exchange of experience and views between countries as well as the development of research and centres of excellence.

2.3.3. *A sharper focus on the impact of the programmes*

Community support will aim, above all, to give economic reform programmes a new dimension.

The Burkina Faso pilot on the reform of conditionality showed that one of the main reasons for the lack of ownership of reform programmes by large sections of the administration and

⁶ Council Resolution of May 1999, following the 1998 Commission Communication of November 1998 on a European Commission strategy for the development of the private sector in ACP countries

civil society was the absence of any short or medium-term, explicit and concrete objectives as well as the absence of any monitoring of results.

The Community will therefore seek to support governments in such a way that reform programmes are placed in a medium-term perspective enabling anticipated results to be carefully monitored and any necessary revisions to be made in case of less than satisfactory outcomes. In doing this, attention will be paid to any significant political, economic and social development affecting the reforms.

This will involve encouraging the shift from a phase of short-term reforms, during which most effort has been devoted to macroeconomic stabilisation, to a phase of more structural reforms, for which it is vital to state anticipated results as regards households, businesses and the way public and private services operate, and to build up a dialogue within countries on the objectives that have been set.

To this end, the Community will encourage governments, in agreement with the Bretton Woods Institutions, to include medium-term perspectives in certain key areas in their programmes: budgetary framework, impact of fiscal policies on revenues distribution, access to basic services, role of the State in household transfers and the trends in private investments.

These perspectives should be discussed with parliaments, representatives of civil society (including trade unions) and donors.

Under this new focus, a limited number of results indicators (consistent with those of the DAC (OECD)) will be identified and monitored and appropriate arrangements will be made for revising, when necessary, the adopted policies.

2.3.4. Changes in working methods

The fact that countries' situations vary so much - and the lack of ownership of reform programmes - argue for an approach that is differentiated so as to ensure that reforms are appropriate to the specific situation of the country.

The widening scope of concerns, the Commission's limited staff resources and the EU's significant financial contributions to the programmes would indicate that there should be greater co-ordination within the EU for it to make full use of its financial weight and its skills. It is also proposed that instruments be simplified so that Community efforts can be focused on priority areas.

2.3.4.1. Greater EU involvement in negotiating programmes

The proposal is for a gradual move away from specific Community-imposed conditionality towards greater involvement by the Community and the Member States (according to the skills they have developed) in drawing up the programmes agreed between governments and the Bretton Woods Institutions. Programmes taking on board the EU's concerns will be subject to no further conditions. If this is not the case, the Commission will communicate its concerns to the national governments and the Bretton Woods Institutions and reserves the option of asking for specific commitments. Beyond the areas of action set out above, the Community and the Member States will work to ensure that the programmes approved are implemented at a rate that is appropriate for the countries concerned.

The Community will encourage consultation mechanisms between governments, parliaments and civil society, *inter alia* providing necessary funding and supporting networks or organisations that further this process.

The Community will press for donors supporting reform programmes to be fully involved, along with the Bretton Woods Institutions, in negotiating them. When this is not possible, the Community will organise consultations with the Member States to inform the government and the Bretton Woods Institutions officially of any comments they may have. Against the background of the general debate on complementarity and stronger co-ordination, the time has come for this co-ordination to be extended to the Boards of the World Bank and the IMF.

2.3.4.2. A reform of conditionality and new disbursement mechanisms

The ideas set out above also lead to a re-examination of the disbursement arrangements for the Commission's support, in line with the negotiations for a successor agreement to Lomé and the lessons learnt from the pilot in Burkina Faso.

The mechanisms proposed are intended to reform conditionality by moving gradually from the current approach, whereby funds are solely disbursed as and when reforms are implemented, to an approach, which will also take into account the results of the reforms. This will grant governments more freedom in the design of their policies.

Under the future partnership, allocation of structural adjustment resources will be determined in the context of rolling programming.

In this framework, Community support to structural adjustment programmes will be conditioned upon the implementation of an economic reform programme, while restricting as far as possible the number of additional specific conditions. The size of any additional grants would be determined by the results achieved under the reforms. Results would be assessed on the basis of a limited number of indicators, chosen by the government and reflecting its policy objectives (e.g. health centre attendance, numbers of boys and girls in first year of primary education, private investment, etc.) and the quality of its budgetary management (implementation of the budget at the decentralised level, unit costs in public procurement, etc.). Attention would be paid to trends rather than absolute figures and any relevant external factors affecting the outcomes would be taken into account.

This "performance bonus" should mean that substantially increased funds could be allocated to the best performing countries. The approach will make countries freer to decide for themselves the ways and means of achieving the desired impact, will avoid conditionalities that are often perceived as having been imposed by donors, and will render more concrete the idea of ownership.

Study of the results achieved can then lead into debate with civil society, parliaments and governments on the policies that have been pursued and possible discussion of the reasons for particular failures. Such a review can not be merely mechanical but must form part of a continuous monitoring and evaluation process, which is capable of leading to revisions of the reform programme should they be necessary.

The current system of disbursement by tranches which are either allocated in total or completely blocked, when situations are usually neither wholly satisfactory nor the complete opposite, will thus gradually give way to this system under which amounts vary annually according to results.

One would thus go from a system of “stop-and-go” allocation (“yes” or “no”) to one of continuous allocation (“less” or “more”), encouraging the best performing countries and sectors and avoiding wasteful allocation to countries whose results are not satisfactory.

2.3.4.3. The appropriateness of targeting funds according to circumstances

New guidelines will be adopted as regards the targeting of counterpart funds generated by budgetary support.

Targeting counterpart funds will still be useful in countries with weak cash flow in that it guarantees that budgets can actually be implemented in the targeted sectors. Because funds included in the budget are totally fungible, however, this system is quite artificial in countries that execute their budgets correctly. In some cases, targeting has also been seen to have negative effects.

Targeting will be maintained, therefore, only for countries with significant difficulties as regards cash flow and budget execution. In other countries, it will be gradually abandoned in favour of monitoring overall budget execution with a particular emphasis on sectors where Community aid is concentrated, particularly the social sectors.

2.3.4.4. Improved technical and institutional support

Finally, the Community will give the necessary technical support to these programmes. This will take the form of technical assistance on macroeconomics, public finance, monitoring and evaluation systems, new technologies and sectoral policy, but could also include amounts for one-off measures to equip certain services (Treasury, customs, budget, statistical office) or support for departments in charge of data gathering.

Horizontal studies will also be financed and results fed into the international debate.

Support could be given to organising civil society and providing actors in development and the population at large with better information on the content of the reforms being implemented.

Finally, audits and evaluations will be carried out in support of programme monitoring.

These changes will doubtless be affected by certain problems: the proposals that results indicators be taken into account are certain to be associated with technical difficulties and questions of interpretation and data reliability. There will also be the difficulty of embarking on a more contractual approach with ACP states and the changes in habits that this will require. Arrangements will be established for monitoring the difficulties encountered and finding solutions. In addition, the changes set out in this Communication will be introduced as gradually as necessary to take into account varying circumstances. They will be introduced in the implementation of programmes funded under the 8th EDF and applied more widely with the next EDF.

3. SUPPORT IN EASTERN AND SOUTHERN MEDITERRANEAN COUNTRIES

3.1. Introduction

Structural adjustment programmes in the context of financial and technical co-operation with eastern and southern Mediterranean countries were introduced from 1992. Council Regulation of June 1992 introduced the possibility to extend support to Mediterranean countries in the form of structural adjustment programmes, drawing on the experience gained in this area with ACP countries. Under the Redirected Mediterranean Policy and the MEDA programme, structural adjustment programmes have become an established feature of the Community's co-operation with eastern and southern Mediterranean countries. In fact, between 1992 and 1998 a total of 705 MECU has been committed for structural adjustment programmes in Mediterranean countries.

The nature of the Community's structural adjustment programmes with eastern and southern Mediterranean countries has been evolving steadily. This has been the result of two independent factors. Firstly, there has been a gradual evolution in the way the instrument is mobilised. In this regard the Council Resolution of June 1995 introduced much more flexibility in the management of the instrument. The main justification for this was the need to respond to the diverse situations in partner countries. Secondly, with the Barcelona initiative there has been a fundamental change in the relationship between the Union and the Mediterranean partners. The above mentioned Council Resolution already anticipated this by emphasising the need to situate adjustment efforts in the context of a free trade area with the European Union. As it turns out, the MEDA experience confirms that the new partnership has become the most important shaping factor in the definition of adjustment programmes, as the association agreements serve as signposts for the definition of the reform process. An example is Tunisia where, together with the World Bank, the MEDA programme has supported an ambitious reform programme preparing the country for the implementation of the association agreement. The prospect of the signature of an association agreement with the European Union has acted as an incentive to fiscal reform in Lebanon. This has been supported by the Commission in close co-ordination with the IMF.

The Bretton Woods Institutions have shown a keen interest in the use of instruments like the support programmes developed by the Community in its co-operation with Mediterranean countries. This is consistent with the growing priority given to programme aid as opposed to project aid. The latter is not only cumbersome to implement, its impact is also often limited in time and space.

3.2. Assessing past programmes

3.2.1. Structural adjustment programmes under the Redirected Mediterranean Policy.

Financial and technical co-operation under the 4th protocol was shaped by the guidelines of the Redirected Mediterranean Policy. With the Redirected Mediterranean Policy greater recognition was given to a stable macro-economic framework as laid down in the Council decision of December 1991. This decision reserved a financial envelope of 300 MECU for structural adjustment operations in favour of Mediterranean countries. The implementation of the first batch of Community supported structural adjustment programmes in Mediterranean countries was characterised by:

- The Community financed programmes were in general implemented alongside programmes financed by the Bretton Woods Institutions. The Bretton Woods Institutions assumed the leadership role in the definition and the negotiations of the conditions of the adjustment programmes. At the level of the conditions there was no or only very limited Community specificity;
- A main feature of the programmes was to provide fast disbursing support; this approach was justified by the weak balance of payment situation of many countries with commensurate high external financing requirements;
- Community support was given in the form of import support programmes; the domestic counterpart funds were spent in agreement with the Commission. This was thought to be an effective way to maintain the level of social spending, in particular in favour of those adversely affected by the adjustment process, which was considered to be one of the most important justifications for Community support in this area;
- The use of the instrument was not fully integrated in the overall assistance strategy of the Community vis-à-vis beneficiary countries. The distribution of the 300 MECU envelope for structural adjustment among beneficiary countries was done on the basis of a number of ad-hoc criteria;
- In a limited number of cases the global envelope for structural adjustment was supplemented by bilateral protocol allocations.

A summary of the Community support programmes implemented to date from 1992 onwards is provided in annex 6.

3.2.2. *Structural adjustment programmes under the MEDA regulation.*

3.2.2.1. Main features of the MEDA structural adjustment programmes

During the protocol period financial and technical co-operation was mainly motivated by traditional development considerations. With the launching of the MEDA programme, the main objective of the Community's financial and technical co-operation with Mediterranean partners has become to assist the countries in the implementation of the association agreements. As the association agreements provide for the creation of a free trade area between partner countries and the Union, there is a need for a comprehensive process of economic transition implying wide-ranging reforms⁷. Therefore, apart from a process of gradual liberalisation, there is also the challenge of legislative reform. This concerns not only a more favourable regulatory and administrative environment (rules regarding competition, right of establishment etc), but also financial sector reform, better systems of property rights (including the system of land tenure), restructuring of public enterprises and privatisation, and increasing the efficiency in the delivery of infrastructure services. Also modernising and transforming tax systems into equitable, efficient and administratively practical taxation systems in support of economic growth is a necessity and an essential contribution towards improving the environment for investment financing and business. Strengthening social cohesion is another crucial and intrinsic part of the process of economic transition. Structural

⁷ This has also been underlined by the governmental group of experts on the economic transition in the conclusions of the meetings of 9 and 10 March 1998 and of 27 and 28 April 1999.

reforms that cannot count on a consensus in society about its objectives and methods are untenable. This implies the need for continued determined efforts to improve the standards of living of the poor and to take systematically into account the social dimension of the economic transition process⁸.

In summary, as a result of the qualitative change in the Union's relationship with its Mediterranean partners under the impetus of the Barcelona initiative, the nature of the Community's financial technical co-operation with Mediterranean partners has been reformulated. This has also had important implications for the structural adjustment programmes, of which the main characteristics can be summarised as follows:

- Support for structural adjustment has become an integral part of the Community's support strategy towards individual Mediterranean countries. This implies that allocations for structural adjustment operations are decided within the context of the elaboration of the national indicative plans;
- Structural adjustment programmes play in the first place a key role in supporting structural reforms that have a direct or indirect bearing on a country's preparation or implementation of the association agreement it has concluded with the Union. The primary role of the support is to act as a catalyst in favour of credible reforms.
- With the progressive liberalisation of the current account transactions of the balance of payment of most countries in the region, the justification to extend financial support in the form of import programmes has gradually disappeared. Financial support under the MEDA structural adjustment programmes has generally been given in the form of direct budgetary aid;
- The implication of the much-improved macro-economic situation in almost all partner countries has been that macro-economic stabilisation objectives do not constitute the core of the most recent programmes. Instead, recent programmes concentrate on structural reforms⁹. On the other hand, the consolidation of macro-economic internal and external balances remains an indispensable element of the Community's programmes, especially as most financial assistance is provided in the form of direct budgetary support. An intensive macro economic dialogue has therefore become a standard feature of the Community's programmes;
- There has been a concentration in the use of the instrument on a limited number of countries, i.e. Algeria, Jordan, Morocco and Tunisia. This is due partly to the fact that under the 4th protocol these countries were the main beneficiaries from the instrument, which, as discussed, was a decision, based on ad-hoc criteria. Another reason is that, with the exception of Algeria, these countries were the first that signed association agreements with the Union. There are however no à priori and compelling reasons to limit the mobilisation of the instrument to these four countries.

⁸ The importance of a national consensus in favour of important but difficult reforms and their ownership is equally pointed out in the recent external evaluation of the ESAF of the IMF (Enhanced Structural Adjustment Facility). IMF, External Evaluation of ESAF, Report of an independent group of experts, June 1998.

⁹ Annex III provides the comparative data based on the key macro-economic statistics for the partner countries.

3.2.2.2. Co-ordination with the Member States

Co-ordination with Member States has been essentially conducted in the context of the preparation and the implementation of the programmes concerned. Member States have also been consulted at the level of the MED-Committee in the framework of the consultation procedure established by the MEDA regulation. Co-ordination with Member States in the implementation phase has taken usually the form of de-briefing meetings following missions to beneficiary countries.

3.2.2.3. Co-ordination with the Bretton Woods Institutions

Structural adjustment programmes under MEDA continue to be implemented in co-ordination with the Bretton Woods Institutions. Co-ordination methods have however been adapted to take into account the specific relations of the Bretton Woods Institutions with the countries concerned, the programme of the Community and the preference of the partner countries themselves. As a consequence, in practice co-ordination with Bretton Woods Institutions takes different and adaptable forms. In some countries, co-ordination with the World Bank has been intensive. This is the case for Tunisia where two consecutive parallel operations have been financed. In other countries, the co-ordination is of a more global nature. As regards the IMF, regular exchanges take place between the services of the Commission and the staff of the IMF, in particular on those countries that benefit from the Community's structural adjustment support. The results of the regular consultations between the IMF and the partner countries, especially those in the context of the article IV consultations, are important elements in the evaluation by the Commission of the macro economic performance of the country concerned.

3.2.3. *Conclusions of a recent evaluation.*

In the context of the global evaluation of the MEDA regulation, the Commission decided to ask independent experts to carry out an external evaluation into the structural adjustment operations implemented under MEDA. A copy of this evaluation report has been made available to the Member States¹⁰. It is however worthwhile to recall the main conclusions of this report.

Firstly, and as regards the evolution of the instrument during the MEDA period, the report underlines that this evolution has been coherent with the enhanced dialogue that has developed between Mediterranean partners and the Union in the context of the Barcelona initiative. According to the report, support for structural adjustment has been an appropriate response to the economic and financial implications of the creation of an Euro-Med free trade area.

Secondly, the report argues that while there are no major questions regarding the legitimacy of the instrument as such, certain questions can be asked regarding its efficiency. This concerns for example the question of the eligibility. Under the current MEDA regulation this eligibility is not directly linked to the specific objectives of the MEDA programme, but to a set of rather general indicators inspired by the Lomé framework. The report suggests linking the eligibility in the first place to the specific transition costs that are incurred in the preparatory process towards free trade with the European Union.

¹⁰ F.P. Gruet et P. Plane, *Evaluation des facilités d'ajustement structurel dans les pays au sud de la Méditerranée*, 1999.

Thirdly, while the evaluators consider that the principle of direct budgetary support is appropriate in the context of the partnership, they insist on the importance of a better justification of the amount allocated for each individual structural adjustment programme, as well as its tranching. According to the evaluators the costs associated with each reform provides an important indication in this respect.

Fourthly, the evaluation report calls on the Commission to increase the specificity of the content of the programmes, in particular through giving a greater importance to conditions linked to:

- the creation of a free trade area with Europe;
- the socio-economic balance of the countries concerned as mentioned in the MEDA regulation.

Fifthly, and as regards the co-operation with the Bretton Woods Institutions. The report insists that conditions of programmes agreed between the Bretton Woods Institutions and the beneficiary country should not always become an integral part of the Community's support programme. It is suggested only to integrate such conditions in case they are key structural adjustment conditions or in case these conditions can be clearly situated in the context of the creation of a free trade area with the European Union.

Finally, the report makes a number of recommendations regarding the implementation, the follow-up and the evaluation of agreed programmes. As regards the implementation and the follow-up of the programmes the report calls on the Commission to strengthen its analytical capacity as well as to make available technical assistance in support of specific reforms.

3.3. Prospects and conclusions

The main conclusion the Commission draws from the evolution of the structural adjustment facility in Mediterranean countries is that it has gradually evolved towards an association facility. This corresponds to the ambitions and the objectives of the Barcelona initiative.

Other conclusions, the Commission draws are the following:

- The full integration of budgetary support in the bilateral financial and technical framework with Mediterranean partners has been beneficial and should be maintained. This integration will also allow systematic account to be taken of the needs for support resulting from the implementation of the association agreements. With the entering into force of more association agreements there is room to increase the specificity of the instrument;
- There has been a reduced emphasis on macro-economic stabilisation objectives of the programmes implemented under MEDA: This facilitates the concentration on the catalytic role of the instrument in favour of structural reforms. This does not preclude that instrument is in future mobilised in support of re-establishing macro-economic balances. The latter should however preferably be done in close co-ordination with other Community instruments (e.g. the macro-financial loans for third countries administered by the Commission) and the Bretton Woods Institutions, in particular the IMF;

- Co-ordination with the Bretton Woods Institutions is important and improves the credibility of the instrument. For that purpose a regular exchange of information between the Commission and the Bretton Woods Institutions is essential. Parallel programmes have proven to be an appropriate method of co-operation with the Bretton Woods Institutions;
- As regards programmes that are primarily designed to support structural reforms, the consolidation of macro-economic balances, both internally and externally, remains an important condition. It is inconceivable that financial support is given in the form of direct budgetary aid, when the budgetary and fiscal policies of a partner countries are inadequate;
- Specific sector reforms, in particular those that are linked to the implementation of the association agreement will increasingly become the focus of support. This will allow to introduce a greater European specificity in the programmes supported, as well as to extend this type of support to countries that so far have not benefited from this type of assistance;
- In view of the reform challenge initiated by the association agreements, there is a need to improve the social profile, including poverty reduction, of partner countries, without which it will be impossible for partner countries to face the increased competition resulting from the progressive implementation of the association agreements. Support for relevant reform programmes should be accorded a high priority;

At the level of the management of the instrument, there is a need to reflect on the programme cycle for this type of support. This should introduce a degree of flexibility, however without jeopardising the effectiveness and the efficiency of the instrument. The value of the Community's support will also be enhanced if adequate monitoring, surveillance, and evaluation mechanisms are put in place. This should avoid that operations are simple ad-hoc operations that are not properly followed up.

4. CONCLUSIONS AND GUIDELINES FOR THE FUTURE

The discussion of the Community's recent experience in the area of structural adjustment support shows a clear evolution. Both in ACP countries and in Mediterranean countries there has been a gradual development towards an approach in support of wider economic reforms as opposed to traditional economic stabilisation issues. This process has been facilitated by improved macro economic conditions in many countries, although there are important exceptions. Another important factor is the evolution in the nature of the relationship between the Community and the beneficiary countries. This concerns both the innovations foreseen within the "post-Lomé" framework, as well as the Mediterranean countries where the structural adjustment facility is mobilised to support an economic transition process in the context of the implementation of the Euro-Med association agreements. Hence in that region the structural adjustment facility has progressively developed into an 'association facility'.

The development towards a deeper approach in support of economic reforms is significant. This approach has in common that it supports so called "second generation of reforms", that is reforms aiming at the creation of transparent, efficient, and equitable regulatory systems, the creation of effective social safety nets, the reform of financial sectors, the reform of state-owned enterprises etc, taking into account the level of development of the countries concerned. Also governance issues are assuming gradually an increasing importance. Clearly, such an approach should take into account the considerable differences among partner countries, both as regards their level of development as well as in their relation with the Union.

4.1. Lessons from recent experience.

A progressive greater emphasis on "second generation reforms" should not ignore the lessons to be drawn from the recent experience in the area of support to structural adjustment. One key conclusion is the overriding importance of a macro-economic framework that supports growth and consolidates internal and external macro economic balances. Without this it is impossible to achieve sustainable growth, which is in turn a necessary condition for fighting poverty. A significant number of ACP and Mediterranean countries have made important progress in achieving macro-economic stabilisation. These gains are however sometimes fragile and in many cases the vulnerability of partner countries remains high. Future Community supports will thus continue to mobilise quick disbursing aid in support of economic reforms in countries exposed to external or domestic shocks.

The Community and Member States have long advocated a stronger focus on poverty reduction. This is fundamental in its own right, but also with a view to ensure the necessary support for the sometimes-painful reforms needed. The wider donor community has gradually accepted this poverty focus and this approach must now be consolidated and deepened. In particular attention should be paid to the coherence between budget programming, sectoral policies and reform initiatives, the distributive effects of expenditure and revenue policies, as well as the social implications of reform programmes in the context of a process of economic transition.

Small internal markets are in most ACP and Mediterranean countries important constraints to the development process. It is in this context that the Community has supported stronger regional links among partner countries. Such links facilitate the reform process and encourage wider regional co-operation. This orientation remains valid and should be deepened particularly in a global context in which regional co-operation is recognised as a source of economic dynamism and diversification.

4.2. New relationships.

The relationship between the Community and the ACP countries is currently under review in the framework of the negotiations for a “Post-Lomé Convention”. It is envisaged that the post-Lomé convention provides for a strengthened partnership based on a more contractual relationship that pays greater attention to the performance of individual countries. Regional trade agreements may also become a feature of this new relationship. These will replace the current unilateral preferential regime between the EU and ACP countries.

As for the Mediterranean countries, the Euro-Med initiative of November 1995 changed fundamentally the nature of the relationship between the Community and the MEDA countries. The objective is now the creation of an Euro-Med free trade area by the year 2010. In the context of this broad partnership, association agreements have been already concluded with a number of partner countries, while others will follow. These provide for the gradual creation of a free area, implying the need for a comprehensive economic transition process.

These evolving relationships between the Community and partner countries constitute in themselves a strong catalyst for governments to pursue reforms. Community support will be designed to support the implementation of these reforms and to facilitate transition.

4.3. Priority issues

The evolution of the structural adjustment instrument towards a broader instrument in support of economic reform implies a wider scope of application.

Therefore on top of the established priorities, i.e. support for a macro-economic framework in support of growth and the consolidation of economic stabilisation, effective social policies, and regional economic integration, Community support will concentrate on deeper structural and sector reforms. This concerns in particular:

- *Poverty reduction.* The support on social policies does not limit itself to maintaining or increasing the budget but concentrates more than before on the access to and quality of services rendered to the population. The equity problems, the distribution of growth and the effects of budgetary and fiscal policies are examined as well. Nevertheless, this approach of fight against poverty must set different accents and the concrete applications must be differentiated according to diversified regional contexts;
- *Support for sound public finance management.* This includes support for the development of adequate control mechanisms, capacity building, efficient and effective resource management, strengthening the rule of law to combat corruption, enhancing transparency and civil society participation.
- *Support for fiscal- and tax reforms,* i.e. the elaboration and implementation of efficient and administrative feasible reforms, taking into account the distributive impact of fiscal policies.

- *Support for private sector development.* It is generally acknowledged that the private sector must be the engine of growth. Community support will be geared towards the creation of an enabling environment for the private sector. This includes an adequate legal framework (commercial code, legislation on arbitration, bankruptcy, land tenure, property rights, privatisation, environmental protection, etc), trade and market liberalisation, financial sector reforms etc.

4.4. Working methods and management.

The discussion of the recent Community experience has demonstrated the need to adapt the working methods and the management of its support programmes. This should take duly into account the specificity of each country regarding its level of development, as well as regarding its specific relation with the Community.

The following conclusions are drawn:

- Given the importance of the macro-economic context, following eligibility criteria must be satisfied :
 - the country concerned must undertake a reform programme approved by the Bretton Woods institutions or implement programmes recognised as analogous, in coordination with those institutions, but not necessarily financially supported by them, in accordance with the scope and effectiveness of the reforms;
 - account must be taken of the economic situation of the country, at the macro-economic level (indebtedness, cost of debt-servicing, the balance of payments, the budget situation, the monetary situation, the level of per capita income and the unemployment level) and at the level of sectoral reforms.
- given the key role the Community support plays in the development strategy of partner countries, this support should be fully integrated into the bilateral co-operation frameworks. Therefore, the existence of a special and separate envelope for structural adjustment support does not seem to be justified any longer. This is already the case for the MEDA regulation and is now also foreseen for the “post-Lome” framework.
- The use of general import programmes has gradually been abandoned in favour of direct budgetary support in countries that have liberalised their current account transactions. Nonetheless the use of counterpart funds has continued to be a major component in the programmes for ACP countries. If countries have however liberalised the current account transactions of the balance of payments this is unnecessary and hence Community support will gradually, as is already the case for Mediterranean countries, take the form of direct budgetary support. To this end, the Community will integrate in its programmes provisions on overall public finance management, including an appropriate follow up through a system of performance indicators and the conduct of audits.
- disbursement of the support will be implemented in tranches in the form of direct budgetary support according to the compliance with the objectives and/or sectoral targets agreed within the support programme

- There can be only one programme of economic reforms in a country: the one of the country itself. Therefore Community support for structural adjustment and economic reforms should be properly co-ordinated with other donors, in particular Member States, and the Bretton Woods Institutions. This will also reduce the need for specific Community conditions. The Commission will, together with the Member States, seek a strong role alongside the Bretton Woods Institutions in their dialogue with the government on economic reform. However, should it prove impossible to reach full agreement with other donors, the Community should always reserve its right to attach a limited number of additional conditions to its support programmes. It should be also recognised that in the case of the Euro-Med association agreement, the nature of the reform process is to a large extent conditioned by these agreements. Hence a European specificity is to be guaranteed.
- The Commission attaches much importance to improving the monitoring and evaluation of the impact of the reforms and the policies. It appears, indeed, essential to precisely state and make public the expected objectives and results of the public reforms. The development of performance indicators will help to monitor and to evaluate the impact of the programmes. Such indicators will also assist in the identification of best practices. As a result the effectiveness of financial support will improve, which might pave the way for a possible introduction of performance-related allocations.
- Specific sector reforms, in particular those that are linked to so-called 'second generation type of reforms' or linked to the implementation of the association agreements will increasingly become the focus of support. This will especially be true in the countries that have a limited need for traditional stabilisation measures.
- In order to increase transparency, to improve reform programme design and sequencing as well as to enhance ownership, the Community will seek means to involve civil society in the design and monitoring of programmes. In this context it will be important to make explicit and public the objectives and expected results of the reforms. Together with partner countries efforts will be made to improve the efficiency and the effectiveness of the instrument. In order to achieve this, appropriate monitoring and evaluation systems must be put in place by partner countries with eventual assistance from the Community.

4.5. 4.5 Implementation

The implementation of the conclusions must be carried out gradually and flexibly so as to take into account the diversity of circumstances in partner countries, the domestic evolution in partner countries, the global economic context, as well as the overall context of the Union's co-operation with the ACP and Mediterranean countries.

5. ANNEXES

5.1. Annex 1 List of decisions under the 7th and 8th EDF

ANNEX 1

BILAN PAR PAYS DE L'UTILISATION DE LA FAS 7EME FED (1150 MECU)			
Pays (par ordre décroissant du montant décidé)	Montant décidé (MECU)	Montant payé (MECU)	Nombre de Décisions
Tanzanie	103.4	103.3	3
Zambie	96.4	96.4	4
Ghana	87.2	87	4
Burkina Faso	83.9	83	5
Ethiopie	78.4	77.5	1
Côte d'Ivoire	77.2	76.8	5
Mali	61.3	61.3	4
Ouganda	51.8	46.2	3
Malawi	47.5	47.4	3
Bénin	39.1	39.1	3
Zimbabwe	36	36	2
Cameroun	33.7	33.6	2
Sénégal	32.5	32.5	3
Mozambique	30	30	1
Guinée	26.4	25.6	3
Mauritanie	24.55	24.4	2
Rép. Dominicaine	22.8	22.8	2
Niger	22.4	22.4	3
Lesotho	21.58	21.58	4
PNG	20.5	20.5	3
Tchad	19.6	19.6	2
Haïti	17	16.9	2
Burundi	12	3.9	1
Sierra Leone	12	11.9	1
Madagascar	10.8	10.8	1
Centrafrique	10	9.8	1
Guinée Bissau	9.6	9.48	2
Gabon	8.2	6.6	2
Guyane	7.8	7.7	3
Congo	6.6	6.6	1
Comores	6.6	6.5	1
Gambie	6.2	6.2	2
Trinidad &	6.2	6.2	2
Djibouti	4.1	4.1	2
Jamaïque	2.5	2.5	1
Dominique	2.2	2.1	1
Sao Tome &	2.06	2.06	2
Grenade	2	1.9	1
38	1142.09	1122.22	88

OPERATIONS AJUSTEMENT STRUCTUREL EN 1998				
SUR LA FAS 8ème FED				
PAYS	Décisions	Compléments	Décisions	Paiements
(ordre alphabétique)	FAS	PIN	(FAS+PIN)	déc. 1998
Bénin	20,1	--	20,1	12,6
Burkina	26,95	--	26,95	21
RCA	7,2	--	7,2	
Tchad	16,8	--	16,8	10,4
Ghana	21,4	--	21,4	14,9
Cameroun	25	--	25	15
Cap-vert	9,4	--	9,4	8,4
Gabon	2,7	--	2,7	0
Guinée	21,4	--	21,4	15
Guyana	5,29	--	5,29	5,29
Côte d'Ivoire	32,4	2	34,4	16,4
Djibouti	2,6	--	2,6	0
Ethiopie	74,5	1,3	75,8	50
Mauritanie	11,2	--	11,2	0
Mali	29,4	--	29,4	20,4
Malawi	8,53	--	8,53	4,5
Mozambique	52,8	15	67,8	27,5
Niger	15,8	--	15,8	22,9
Rwanda	14,6	10	24,6	
Sénégal	27,9	--	27,9	24,3
Sierra leone	8,5	--	8,5	
Tanzanie	71,2	--	71,2	43,67
Ouganda	41,06	10	51,06	
Zambie	46,69	7	53,69	
Total	593,42	45,3	638,72	312,26

5.2. Annex 2 Impact of the programmes on medicine and vaccination policies

In the early 1990s, following the previous decade's serious financial crisis, many public health centres found themselves without medical supplies and medical purchasing centres were in a state of near bankruptcy.

The Community's support for structural adjustment was decisive in returning the situation to normality - and sustainability.

Policy dialogue was central, with certain governments showing a strong political will to change the status quo – ultimately, the centres' predicament was after all the result of policy mistakes. In order to adopt new policies based on the purchase of essential medicines, cost recovery and setting up rigorous management systems, decisions were called for beyond those that could be made in health ministries. Interministerial decision-making was easier in the context of discussions on structural adjustment reforms.

Financial support targeted under the Counterpart Funds has enabled supply systems to be re-established, providing working capital for the purchasing centres, and at all levels of the health pyramid, and in some cases paying off domestic debt. Using national procedures to buy medicines has meant that these could be improved and costs reduced by a focus on generic products, lending greater credibility to the purchasing centres and maintaining or improving quality controls.

Finally, the necessary technical support was given through structural adjustment measures or other instruments.

This work (supported in some cases by the World Bank, France or the Netherlands) has meant that viable, effective purchasing centres could be built up again in Benin, Burkina Faso, Cameroon, the Central African Republic, Côte d'Ivoire, Madagascar, Mali, Niger, Senegal, etc., and that people there have access to affordable basic medicines.

Some products, such as vaccines, must remain free of charge and the Community has asked governments to allow for such purchases in their budgets and ensured under CPF targeting that they can be funded.

As Mr Tertius Zongo, the Burkina Faso economics and finance minister has said, "The beauty of the regional support project to improve vaccine independence in the Sahel is that for the first time a group of low-income countries is being encouraged to include vaccines as a priority in their national budgets based on their chosen sectoral health policies.

This was not an easy decision, but courage and political will prevailed. The process involves Commission support to these countries' budgets via the structural adjustment Counterpart Funds to support and safeguard the budget lines earmarked for the purchase of vaccines and medical supplies.

One year on, vaccine independence is a reality in national policies. These countries now have lines in their operational budgets to cover all their vaccination requirements (...). Additional benefits have come from the dialogue that has developed among health ministry officials and between these officials and their counterparts in the finance ministries.

This cross-sector dialogue is proof of the Sahel countries' genuine ownership of their vaccination programmes."

5.3. Annex 3 Test case: reform of conditionality in Burkina Faso

In 1998, the SPA entrusted the Community with co-ordinating a nine-donor pilot project aimed at enhancing the effectiveness of quick-disbursing aid. The objectives are as follows: (1) to improve and bolster ownership of the programmes by the beneficiary countries, (2) to help smooth aid flows, making them less erratic and reducing the number of suspensions by applying new disbursement mechanisms, (3) to focus on the anticipated results of the reforms rather than the means of achieving them, thus encouraging a medium-term view, and (4) to improve co-ordination between donors via joint evaluation missions. Three such missions have taken place so far.

The main lessons we have been able to draw from this test case to date are:

Ownership on the part of the countries where the reforms are taking place is essential. All too often, programmes are perceived in terms of reforms, externally imposed in aid of distant, abstract objectives. Ownership involves above all the ability of governments to determine the substance of reforms and to conduct a political debate on what objectives should be set and what results anticipated. The administration and civil society should be key participants in this debate. Programmes are still too often discussed in a damaging atmosphere of secrecy.

Focusing on the impact of reforms and reflecting on the reasons for any failure to achieve the anticipated results mean that it is possible not only to enhance ownership but also to propose strategies geared to the reality on the ground and more in tune with the expectations of the population.

The disbursement mechanisms used currently are not conducive to this emphasis on results but make rather for a system of very short-term reforms generally perceived as being decided arbitrarily and imposed by donors. This test case pilots other disbursement mechanisms that avoid an over-abrupt stop & go rhythm. The proposals in point 3 of this communication flow largely from the findings of the test.

Co-ordination between donors means less time wasted for the civil service in the beneficiary countries, more common sense in discussions and less subjectivity in assessing results.

Nevertheless, this is a complex process: it is not always easy to find relevant, tangible indicators of what has been achieved, information systems are often deficient, but above all the shift from a dialogue on the design/adoption of reforms themselves to one on results demands a profound shift in mentality on the part of both governments and donors.

In the course of the implementation, it appears to be necessary to take into account the results of this test case. Indeed:

- In spite of the efforts to increase the ownership of the countries in the reform programmes and to encourage the participation of the civil society, it must be recognised that the ongoing programmes are still felt to be largely imposed by the donors, and the mechanisms have not been found to ameliorate the involvement of the civil society.
- In spite of the rationalisation efforts mentioned above, it appears that as regards the implementation of Community support, there are still too many specific conditions and which are insufficiently internalised by the administration.

5.4. Annex 4 Weaknesses in current working practices

Observations from the recent evaluation of IMF-backed ESAF programmes

This external evaluation, which was published in 1998, pointed out a series of shortcomings in the current programmes and made a number of recommendations with which the Community is largely in agreement.

The first criticism is of the insufficient attention paid to the impact of the programmes on poverty. Two aspects are looked at: changes in incomes and access to social services. The evaluation stresses the importance of taking account, at the outset of programme design, of studies identifying those among the poor who are likely to be affected adversely by the planned reforms, and to follow more closely changes in relative prices.

Secondly, the evaluation points to the importance of the sequence of the reforms and a medium-term perspective. Some reductions in income may be due to errors as to the sequence or rate of implementation of the reforms. The study shows for example that financial liberalisation was premature in some instances and by preceding stabilisation liberalisation ended up delaying that stabilisation.

A third finding concerns insufficient ownership of reform programmes and insufficient account taken of civil society. Both donors and beneficiaries accept that ownership is a necessary precondition for the success of reform programmes. Despite this consensus, however, it has proved difficult to give greater weight to this idea in practice. The ideal solution would allow governments to build a national consensus around a development strategy based on sustainable and equitable growth. However, this would involve changes in working methods in the countries themselves and in the international institutions, particularly the IMF.

The evaluation points finally to the insufficient attention paid to problems of corruption and reaffirms the importance to be attached to institutional support, to surveillance mechanisms to show whether resources are being used effectively and to stronger judicial systems.

5.5. Annex 5 Community Support to Mediterranean countries

Structural Adjustment Programmes in Eastern and Southern Mediterranean Countries

	Year	Amount (MECU)	Instrument – focus	Current status
Algeria	1992	70	Import programme. Counterpart funds: infrastructure for social housing	Completed
Algeria	1996	125	Direct budgetary aid (includes 35 MECU transferred from import programme mentioned above). Focus: structural reforms in social housing policy, external trade, privatisation and social security.	Under implementation
Jordan	1994	30	Import programme. Counterpart funds: social sector	Completed
Jordan	1995	20	Import programme. Counterpart funds: social sector	Completed
Jordan	1996	100	Direct budgetary aid. Focus: privatisation and enterprise restructuring, social protection and food subsidies, population strategy	Completed
Morocco	1993	80	Import programme. Counterpart funds: non-wage expenditures in the health and education sector	Completed
Morocco	1996	120	Direct budgetary aid. Focus: medium term economic and social strategy, improved legal framework, budgetary consolidation and reform, enterprise restructuring, private sector development	Under implementation
Tunisia	1992	40	Import programme. Counterpart funds: soil- and water conservation, integrated rural and urban development	Completed
Tunisia	1996	20	Direct budgetary aid. Focus: social sector (public expenditures), regulatory framework, private sector development.	Completed
Tunisia	1996	100	Direct budgetary aid. Parallel operation with World Bank ECAL I loan (Economic Competitiveness and Adjustment Loan), Focus: enterprise restructuring, external trade, financial sector reform, improved social expenditures	Completed