

STRUCTURAL ADJUSTMENT PROGRAMS: AN OVERVIEW OF THE CONCEPTUAL FRAMEWORK

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1. INTRODUCTION

Beginning the 1950s and the ensuing two decades, the political economy of development predominantly focused on output maximization, irrespective of the distributional effects on the populace. This period is characterized by growing inequality and rampant unemployment. Matters further got worse subsequent to the financial crises in the developing countries when prices of oil and commodities drastically increased while prices of primary products, the major sources of foreign exchange, significantly decreased. By the end of the 1970s, this output-maximizing paradigm was superseded by the so-called Basic Needs Approach, which gave due considerations to poverty eradication, employment creation, income distribution and the provision of basic services to the people.

However, the financial crises that began in the 1970s persisted to the 1980s and produced chronic deficits in balance of payments and government budget, staggering inflation rates, and decline or diminutive economic growth. The rationale for stabilization and adjustment programs is thus to redress this trend and resume growth. In many of the cases, these programs were implemented without any regard to the human implications mainly because there was (is) an acute resource constraint and/or the responsibility is left to the adjusting countries.

Many scholars, researchers and policy makers were sceptical of the programs and advocated in various international fora that the human element is central and an integral part of the development process. It is irresponsible and unethical to turn down the welfare of the people since this neglect of the human element does not only undermine the productive capacity of the present population but the implications also extend to posterity. This scepticism is not to imply that the serious economist rejects the need for structural changes and adjustments. Adjustment is desirable and necessary if growth is to be restored. The concern is to combine the growth effort with poverty alleviation during adjustment. Some countries have creatively adopted the programs to their specific local conditions and resource endowments and achieved positive results.

This paper attempts to review, at the most general level, the literature and controversies on structural adjustment programs. It is organized in five parts. Section 1 is introduction. Section 2 outlines the main features of Orthodox Structural Adjustment Programs (SAPs). Section 3 provides the main critiques of SAPs. Section 4 is devoted to a discussion on alternative approaches. Section 5 concludes the paper.

2. CONVENTIONAL STRUCTURAL ADJUSTMENT PROGRAMS

In the past two decades, most developing countries suffered continuous economic recession, rapid inflation, deficits in balance of payments and government budget on account of external shocks, internal resource mismanagement, and policy shortcomings. The relative prices of imports drastically increased while those of export commodities, i.e. primary products, decreased and domestic production in general declined. This sharp deceleration in economic performance was further exacerbated by stagnation and recession of industrial market economies through reduced inflow of capital and aid to the developing countries. Whatever was earned from exports went to debt servicing and repayments and little was left to import raw materials, machinery and other growth supportive goods. Development assistance from the rich countries to the poor were generally curtailed pursuant to the recession in the industrialized countries. Bank lending to the developing countries sharply declined due to excessive accumulation of debts over the previous decades and the high interest rate the rich countries were prepared to pay to the international financial institutions.

This world-wide crisis triggered the construction of an analytical framework to correct current account deficits, fiscal imbalances, achieve economic recovery and promote growth in the developing countries. The big international financial institutions (IMF/ World Bank) believed that the causes of the economic crises in the Third World are structural and institutional and thus forged a strategy for economic recovery.

Earlier versions of SAPs can be broadly categorized into three sets (Cornia, 1988:48-68). These are expenditure-reducing policies, expenditure-switching policies and institutional-and-policy reforms. As such the paradigm is not new. It goes back to Adam Smith.

- i) The first set of expenditure-reducing or demand management policies are intended to reduce spending levels in the national economy. The policy measures in this set include stringent money supply, lowered bank credits, wage freeze and reduced public sector deficit. They all aim to curtail domestic demand and restrict real incomes. In such cases, the demand for both exportables and imports falls in the local market and hence the trade balance will improve. This policy is of course appropriate if domestic demand is in excess of the full employment level (Cornia, 1988:50). If domestic demand is below the full employment level, short-run equilibrium in the external balance is achieved at the cost of lower output, employment, capacity utilization and incomes in the economy. The output of tradeables may not fall since the reduced domestic demand may be compensated by rising exports but output of non-tradeables (construction, services) will most likely decline.
- ii) The expenditure-switching policies aim to redirect productive resources from the non-tradeable sector to the tradeable sector and from consumption to investment. This is to be achieved through the manipulation of relative prices of tradeables and non-

tradeables so that people produce for export and/or substitute imports. It is believed that consumers will shift from imports to locally produced tradeables and non-tradeables. The increase in output of tradeables is believed to be significant enough to counterbalance the declining production in the non-tradeable sector. Total output will at the least be maintained and external balance achieved. Expenditure-switching policies include exchange rate devaluation, trade interventions (export subsidies, import controls, tariffs, etc.), taxes, product pricing and measures to facilitate factor (labor and capital) mobility.

- iii) The institutional and policy reforms are rather ideological. They advocate the institution of a market-oriented national economy in order to enhance competitiveness and productive efficiency through market signals. It is believed that such an economic system can stimulate savings and exports, promote profitable investments, and encourage the adoption of production techniques commensurate with local factor endowments. The required policy reforms entail trade liberalization, reduced role of the state in the economy, fiscal reform, privatization, reform of the financial markets, reduced exchange controls, price reform, etc.

Finally, it is to be noted that such a classification of the adjustment package into three component parts may not be completely conclusive since some policy measures, like price reform, have both demand and supply implications. The three sets of policies also differ in terms of the time horizon in which they affect the national economy. For example, demand management (expenditure-reducing) policies have an immediate (short-term) effect on the level of spending while expenditure-switching policies require a longer time-lag (medium term) to change the structure of production. There is no theoretical basis to contend that the state cannot run economic enterprises efficiently. The reason for the bad performance of state-guided economies is mismanagement and misallocation of resources. It is not a question of ownership.

3. GENERAL CRITIQUES OF STRUCTURAL ADJUSTMENT PROGRAMS

We shall here concentrate on the general criticisms about SAPs derived from its theoretical inadequacy to achieve its very objectives and the next section will present some alternative frameworks. Many scholars, researchers and policy makers had severely criticized the program long before its adoption by developing countries on theoretical grounds.

First, the aim of demand restraint policies is, as discussed earlier, stabilizing in that they are designed to curtail demand. But such policy measures are meaningful only if domestic demand is above full employment level. Otherwise, demand restraint policy measures will lead to reduction in existing capacity utilization, employment level and thus output in general, owing to falling demand (Cornia, 1988:50)¹. The growth objective is therefore defeated, albeit it may be possible to achieve temporary equilibrium in the external balance. In such cases, these policy

measures cannot provide a solution to inflationary pressures in the economy as the problem stems from underutilization of existing productive capacity. The appropriate policy should be to find ways and means that will make it possible to utilize existing capacity at optimum level.

Second, the goal of expenditure-switching policies or supply-expansion policies is to divert resources from the production of non-tradeables to tradeables. The effects of such policies are not certain. The effect of such policy measures is first of all constrained by technical factors in developing countries as complete shifting assumes perfect mobility of capital and labor (Cornia, 1988:51). But, existing capital and labor are activity-specific and hence factor mobility is not vigorous at least in the shortrun. The realization of this objective thus calls for additional capital to create new capacity and facilitate the shift of resources to the tradeables sector. Secondly, the effects of exchange rate are not always clear as they seem to depend on the concrete conditions of a country. Devaluation is not a universal means to bolster foreign exchange earnings. It has been found that over 60 per cent of the export earnings of the sub-Saharan African countries derive from commodities whose price elasticity of demand is such that an expansion in the volume of exports results in a contraction in export earnings (Cornia, 1988:57; Loxley, 1989:13-32). If a country exports primary products with high price but low income elasticity and imports commodities with low price but high income elasticity of demand, the effect of devaluation is likely to be negligible or negative on export earnings. The issue of devaluation therefore demands a close investigation of the structure of production, exports and imports, its effects on flows of trade and the living standards of the majority of the population.

Third, the institutional and policy conditionalities to subscribe to a market-oriented economic system has provoked a bitter outcry in some government and political circles (Campbell and Loxley, 1989:3). Of course, the condition was easily welcomed by countries whose leaderships' ideology was in line with that of the international financial organizations and Western powers and they were the first to introduce SAPs. On the other hand, welfare-oriented governments were at first reluctant to accept these conditions for both ideological and economic reasons. It is argued that export-promoting strategies of IMF/Bank is based on a wrong interpretation of the historical experience of the now advanced countries. The Third World countries at present export few primary products for which the market is already congested. Increase in exports will only result in reduced prices. Further, in view of enhancing efficiency the developing countries are to open up their infant manufacturing industries to competition with the outside world and thereby weaken them. In other words, these institutional and policy reforms deprive the developing countries of the right to work out an inward-looking and distributionally effective development strategies (Campbell and Loxley, 1989:3; see also ECA, n.d.: 16-31). This is easier said than done, however. Those who are opposed to the adoption of SAPs have not as yet come up with an alternative approach.

At the general level, many economists are sceptical of these programs for they are couched in simple aggregate economic terms and their static perception of the development process (Campbell and Loxley, 1989:9; see also ECA, n.d.). Development dynamics is a long-term perspective and it is to serve the interests of the present and the future generations. Since these

programs aim at solving problems that have accumulated over years within the shortrun (1-3 years), many countries have been obliged to introduce spirals of adjustment and stabilization programs. That is, a sustained-growth momentum has not been attained even when positive results have been realized following the adoption of the programs. This shortcoming is attributed to inadequate meso, sectoral and micro policies as compared to macro policies. One simple example is the little or no consideration given to the food sector, which is believed to be the major source of inflation in the developing countries, and the neglect of the concern for the well-being of majority of the population. The success or failure of an adjustment program is determined, according to IMF/Bank, on the basis of highly aggregate economic criteria such as the expansion of money supply, budget deficit, external deficit and bank credit. The criteria do not attempt to look into the actual performance of the economy and the benefits accruing to the poor in a dynamic perspective (UNICEF, 1988, Vol. I: 1-8; Campbell and Loxley, 1989:3-4). The responsibility is left to the borrowing countries.

4. TOWARDS ALTERNATIVE APPROACHES

Some studies have clearly shown that conventional structural adjustment programs have not produced favorable results in terms of growth, income distribution and protecting the vulnerable, albeit external and internal imbalance may have been rectified (see UNICEF 1988, Vol. II; ECA n.d.: 16-18; Campbell and Loxley, 1989: 1-8). It is contended that the welfare of the poor has deteriorated through sharp rises in food prices, reduced subsidies, devaluation, reduced expenditure on both human and public expenditure and depressed wages even in countries where supply expansion policies have registered positive results. These unsatisfactory outcomes are attributed to the inadequacy of the programs and the world economic environment in general. The adjusting countries were faced with low commodity prices, little or no capital flows, high interest rates and recession in the industrial market economies. Drought has further compounded the economic difficulties of the poor in sub-Saharan African countries.

On the other hand, there are successful examples of SAPs (UNICEF, 1988, Vol. I: 131). These countries have managed to achieve both growth and cushion the poor (South Korea, Zimbabwe, Botswana, Chile, etc.). The adopted approaches of these successful countries within the general framework of SAPs have given insight toward alternative approaches that may help resume growth and alleviate poverty in the developing countries. The revised alternatives call for integrated macro, meso, micro, and group-targeted policies. They all recognize that the economic problems of the developing countries are structural and structural adjustments are long overdue. Their concern is how to adopt SAPs to local conditions and resource endowments. The following pages are devoted to a review of some of these new approaches.

A) The UNICEF Alternative

A study commissioned by the UNICEF on the outcomes of SAPs in some ten countries has revealed the inadequacy of SAPs from the point of view of promoting growth and protecting the well-being of the poor. (UNICEF, 1988, Vol. I:147-164; VOL II:165-182; Campbell and Loxley, 1989:1-8). The study has shown that conventional SAPs have been growth-retarding in many instances and the protection of the vulnerable have been ignored altogether. It is further argued that the welfare of the poor cannot be left to the spill-over effects of growth. Growth alone cannot guarantee the protection of the low-income groups. The objective of any development strategy should be to resume growth on a sustained basis and cushion the living standards of the poor. A conscious policy intervention is therefore needed to include the welfare of vulnerable groups in the development objective. In light of these considerations; the UNICEF study recommended a combination of the following six major ingredients for adjustment (UNICEF, 1988, Vol. I:131-146):

a) Expansionary Macro Policies

The aim of macro policies should be to maintain levels of output, investment and consumption; meet basic human needs and gradually accelerate the development process. And this requires a gradual correction of imbalances and more medium-term external financing than traditional SAPs. The focus should be on adjustment rather than stabilization. The emphasis should be to expand production and investment rather than curtail consumption.

b) Priority-based Meso Policies

In view of the stringent resource constraint in the developing countries, there is need to identify priority areas and restructure the allocation of resources accordingly. Such priorities should include activities that at the least help maintain the incomes of the poor and at the best improve them, produce basic needs and services of the population, and make investments and inputs available for growth and poverty eradication.

c) Restructuring of Sectoral Policies

There is need to restructure the productive sectors in the economy. It is believed that small-scale production yields better return than large-scale production. Such policies should aim to enhance productivity in small-scale agriculture, industry and services, expand employment opportunities in the informal sector and raise the incomes of low-income households.

d) Improving the Equity and Efficiency of the Social Sector

Governments should design policies that rechannel resources from high-cost areas to low-cost services and mobilize people for greater community participation in the areas of public works such as road construction, housing, water supply, sanitation, etc.

e) Compensatory Programs

Reduced incomes and increased food prices very often accompany recession and adjustment. Policies must therefore be formulated to protect the living standards of low-income groups at an acceptable standard. Such measures may include targeted food subsidies and employment creating schemes to raise the incomes of the poor.

f) Regular Monitoring

Economic reality suggests for eclectic approach during adjustment since no single appropriate package can be worked out a priori, however diligently one does his homework. There is therefore need to follow up changes and identify policy needs and vulnerable groups on a regular basis.

The above presentation is only a skeleton of Structural Adjustment with a human face. Detailed discussions about each element are to be found in the study sponsored by the UNICEF(1988, Vol:146-147). Structural Adjustment with a human face appeals to international financial organisations for a less deflationary approach and more financial inflow by lending more or deferring payments on debts. At the local level, the authorities should develop policy packages geared to achieve selected priorities within a given resource constraint. The thrust is to expand production and protect the poor.

B) The African Alternative Framework: ECA

The Economic Commission for Africa (ECA) also contends that orthodox approaches are "inappropriate" for Africa's socio-economic structures and development objectives. This is because Africa is characterized by weak production structures and imperfect markets; the realities of the international environment are not favorable; conventional approaches are designed to achieve limited objectives; the adverse and negative consequences of SAPs can hamper sustainable development; and the major actors, the people, are marginalized in the process of formulating and implementing such programs (ECA, n.a.:26). A holistic approach is thus called for. This alternative approach takes into account the main factors impinging on development; the material and human resources that can trigger dynamic development; the necessary institutional set-up that can create a conducive climate for change and development; and the interaction between the different elements of adjustment so that an appropriate policy package can be designed and implemented in a given country (ibid, p. 27-31).

To this effect, the proposed framework of analysis is based on three sets or categories of socio-economic variables (ibid, pp. 32-48). These are:

- a) identification of the forces at play in the pattern and rate of development: political, economic, scientific and technological, environmental, cultural and sociological;
- b) identification of available resources: human resources, natural resources, domestic savings and external financial resources; and
- c) identification of the needs to be catered for: mainly the vital goods and services of the population, and macroeconomic disequilibria.

The framework does not prescribe a standard policy for all countries. Every country has the option to design its own policy packages depending on circumstances and its long-run development objectives in light of the three modules above. The three modules are dynamic over time and should be examined in a dialectical perspective. This approach is believed to facilitate sequencing of adjustment and incorporate dynamic comparative advantage and development objectives. Well, the above model can admittedly help formulate a viable development program (resource-based and human-centred) for a country depending on local conditions and resource endowments. The associated policy measures and instruments however broadly fall within the bounds of conventional structural adjustments and have very much in common with what have been recommended in the UNICEF study (see UNICEF, 1988: 147-182; ECA, n.d.:32-48).

The departure is that the analysis entails a heavy thrust on the merits of a conscious state intervention and challenges the premise that productivity and efficiency can only be realized through privatization. The African alternative calls upon states to consciously manipulate relative prices, exchange rates, interest rates and the allocation of resources to restructure the economy, produce sufficient food, generate growth and make adjustment less taxing on the part of the masses. The central theme is to introduce structural changes in the pattern of production and not to best fit the programs of international financial organizations and the world market.

C) A Framework for Making Adjustment Work for the Poor in Africa - World Bank Version

It is now generally recognized that there is need to integrate economic reforms and social programs. The orthodox thinking of attaining only macroeconomic equilibria is giving way toward less demand restraint policies and more conscious integration of the social dimensions into economic and financial policies under adjustment. It is this new perspective that will facilitate the dual objectives of sustainable growth and poverty eradication in the developing countries, in particular Africa (World Bank, 1990:1-8).

The social effects of structural adjustment programs (macroeconomy) are transmitted to the microeconomy of households and enterprises through markets, economic infrastructures and social infrastructures. It becomes necessary therefore to establish how the macro processes affect households under adjustment. There are gainers and losers when an adjustment program is introduced. Policy interventions are therefore necessary to protect the losers. The problem calls for a systematic information system to gather and analyze relevant data on the disaffected social groups.

The key policy concern is how to assist the disaffected groups and develop safety-net or buffering programs without introducing distortions in economic performance. For this, policy makers need to consider the twin problems of poverty and vulnerability (*ex ante*). Poverty is a level of income in relation to some standard, while vulnerability is concerned with the effects of adjustment on households. Policy formulation for adjustment need to identify "the chronic poor" existing before the implementation of the programs, "the new poor" those who are eroded into poverty in the process of adjustment, and other vulnerable groups that are above the poverty line and yet negatively affected by adjustment. These three classes of people merit policy considerations in the processes of designing and implementation of adjustment programs.

The policy directions to this end cannot be conclusive because of the complexity of the problems and Africa's diverse economic circumstances. The following are suggested at the abstract level, however:

- a) Re-orientation of expenditure categories toward cost-effective core expenditures benefiting the poor: economic expenditures on agricultural research, extension services, small irrigation schemes, feeder roads, credit and marketing services stand out as important policy measures to raise incomes of the poor. Sufficient resources need to be devoted to rehabilitate and enhance human capital through the provision of basic health services and primary education and targeted food subsidies.
- b) Policy measures should give priority of loans to smallholder agriculture and favor borrowers among the poor.
- c) Poor households are adversely affected as producers, consumers and wage-earners through devaluation. This negative repercussion is most severe on producers of non-tradeables and the urban poor. Policies need to be designed to create alternative production patterns through targeted extension services and credit services when and where it is viable. The government may even deliberately raise official food prices accruing to producers of non-tradeables. This latter approach is of course to be integrated with targeted food subsidies to offset the adverse consequences on the urban poor.

Here again, no specific model of analysis is offered. Only a structure of thinking for policy design is provided. The required empirical study is a challenge. Existing econometric models

are inconclusive to assess the impacts of macro policies on the microeconomy (households) in a comprehensive manner because of data requirements and the intricacy of the interlinks (mesoeconomy). And yet one cannot afford to close his eyes to these problems. Some empirical studies should be undertaken. This is both prior to adjustment and during the implementation of the programs.

5. CONCLUSION

Orthodox Structural Adjustment Programs were initiated and introduced to resume growth and development through restructuring production toward comparative advantage in a static context. This approach was criticized, at the theoretical level, because it focused on correcting imbalances and attaining growth and disregarded the human element. Further empirical investigations on the outcomes of adjustment largely supported this scepticism about the programs. But some countries, notably Botswana, Chile, Zimbabwe and South Korea, succeeded in combining the growth effort with poverty alleviation within the general framework of SAPs. These positive results triggered the reconstruction of SAPs with a human face by the UNICEF. The UNICEF version of SAPs incorporates the dual objectives of growth and rehabilitation and enhancement of social services.

The shortcomings of traditional SAPs posed by the UNICEF have now won wide recognitions. The challenge to develop a conceptual framework to meet the two ends, growth and poverty eradication, is an ongoing one. There is no conclusive answer to date. We have reviewed two additional alternative versions of SAPs, one by the ECA and the other one by the World Bank. Reading these documents imparts that there is no theoretical departure (at the macro level) from the policy package forged by the World Bank and the IMF initially.

The difference is that the latter versions call for a gradual removal of macroeconomic disequilibria and more access to external finance. The latest conceptual framework proposed in the World Bank report provided an analytical tool that can help identify social groups that are disaffected by SAPs. However, there is a long way to go in this direction; existing models are inconclusive but indicative enough and the research requirement is enormous even if the data requirements are met.

In conclusion, the demarcation is illusive. The debate so far leaves much to be desired. The so-called new versions are supplements or elaborations or reinterpretations to local conditions and development objectives. The threads are not clearly delineated and connected in a holistic fashion. The challenge ahead is on the twin fronts of theory and empirical analysis. We have also learnt that the popular view that the policy package of IMF/Bank is rigid and a Hobson's choice to borrowers is unfounded. There is room to manoeuvre and adopt SAPs to the specificities of a country.

NOTES

1. This conclusion is also empirically supported by the experiences of many countries. See for example, UNICEF, Volume II; Campbell and Loxley, pp. 1-10; and ECA, *Alternative Frameworks*, pp. 16-25.

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