

Session 10

PUBLIC POLICY REFORM PROCESS: Political Economy Perspective

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Introductory Course on Economic Analysis of
Policy-Based Lending Operations

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The Policy Reform Challenge

- *To design, implement and sustain*
 - *Effective reforms*
 - *Relevant*
 - *To issues in the particular country context*
 - *Feasible*
 - *Implementable and sustainable*

Overview of Presentation

- ***What*** : ‘political economy dimension’ of policy reform
- ***Why***: so what? Why should we care?
- ***How*** can we make sense of it
- ***How to do it more effectively***
 - *Some lessons on policy reform process*
 - *Some lessons from ADB’s operations (and other IFIs)*

Political Economy Perspective

*Why bad things happen to
seemingly good policy ideas...*

An Example:

Reactions to a Program Loan

- “Water fees, a new instrument proposed by ADB, may succeed in snapping the bones of Thai farmers already heavily in debt”
- “The RID [Royal Irrigation Department of the Royal Thai Government] and ADB advisers should understand the culture of water allocation in Thailand.”
- “If the government has no choice but to follow the dictates of international monetary organizations...then maybe there is no need for a government. It’s as if we have no government left...[Today international monetary agencies decide and design everything for us...”]

Quotes from farmers’ representatives, community leaders and academics in *Farmers say no to new water burden*, Bangkok Post, June 11, 2000

George Abonyi/June 2007

Starting Point: Beyond “Rational Policy Analysis”

- Starting point: Technical/economic rationale for change
 - “with reform’ vs. “without reform (status quo)” → *expected benefits*
 - Important place to start thinking about policy reform
 - E.g. Provides technical/economic rationale for change
- BUT: necessary, not sufficient for undertaking reform
 - ‘can I get/maintain agreement, support’
 - ‘can it be done’
 - ‘perhaps yes, but is it worth the effort/cost’
- ‘Problems of implementation’: the norm
 - E.g. resistance to change, institutional constraints on actions
 - *Usual characteristic of policy reform environment*

Illustrations (ADB)

- *Philippine Power Sector Restructuring Reform*
 - Issue: Inefficient, high cost service, no innovation
 - Response: Expert analysis/panel recommended needed technical reforms—accepted by President
 - Outcome: Stalled for years in the Philippine legislature—questions about extent of support and/or ability to ensure change of President

- *Thailand Agriculture Sector Reform*
 - Issue: Transformation of Thailand from “water rich” to “water poor” country: water as scarce resource
 - Response: use of markets/prices to allocate water
 - Outcome: Blocked by coalition of farmers, NGOs

- *Indonesian Financial Governance Reform Program: The extreme*
 - Political survival and change

Policy Reform as 'Change'

- Reform is **HARD**: Policy makers need convincing rationale to initiate and sustain reforms
 - Usual focus in *policy analysis*: on expected benefits from change
 - Often neglects
 - What is being changed
 - How to do it effectively
 - What is the cost of change (resources, political, institutional)
- **policy reform as 'local earthquake'**
- Policy reform as commitment by “The Government”, e.g. MOF in agreement with IFIs, to undertake reform
 - beginning of extended/long-term, uncertain change process
 - Outcomes often differ substantially from expectations
- Reforms may be altered/reversed any time
- *Policy reform as 'evolving experiment' vs. 'blueprint'*

Examples

- Thailand's Agricultural Program Loan
 - proposed water user fees blocked prior to formal policy process, well before implementation, by opposing farmers' groups
- Philippine Power Sector Restructuring Program Loan
 - proposed reforms blocked during the policy formulation process (i.e. legislation stage) by opposing interests
- Thailand's Social Program Loan
 - proposed decentralization of state-run schools blocked at the implementation stage by opposing teachers
- Sri Lanka's Agricultural Sector Programme Loan
 - Government removed fertilizer subsidies, but a new government elected subsequently with mandate to restore subsidies

Policy Reform as Change: Lessons from Organizations

- Challenge: policy reform involves changing
 - Policies, rules, structures, systems, processes, incentives, expectations, behaviors, power alignments, relationships, capabilities,
institutions
 - *E.g. SOE reform/privatization (Thailand, Viet Nam)*
- Organizational change: approximately 30% success rate
 - Not ‘inertia’, but ‘dynamic conservatism’
 - *Not as an argument for avoiding change*
 - *But to show the challenge – add a dash of humility*
 - Ensure *preparation/patience/performance*

Success Rates for Different Types of Organizational Change

Source: Smith, Martin, 2002. "Success Rates for Different Types of Organizational Change".
Performance Improvement, Volume 41, Number 1, January.

Type of Change	# of studies	Total sample size	Median success rate
Strategy	3	562	58%
Restructuring/ downsize	9	4,830	46%
New technology	5	1,406	40%
Misc change efforts	1	23	39%
TQM efforts	5	863	37%
M & A	9	395	33%
Re-engineering/ process improvement	7	3,442	30%
Software implementation	6	31,480	26%
Business expansion	1	200	20%
Culture change	3	225	19%
Totals	49	43,426	33%

Policy Reform as 'Change': Crisis vs. Non-Crisis Conditions

- Crisis as 'window of opportunity' (e.g. Asian Crisis)
 - Focus attention
 - Create atmosphere of “no choice but change”
- BUT may be difficult to sustain change
 - Differences in crisis and non-crisis conditions; *BUT*
- *Policy reform: complex long-term change process*
 - *Whatever the context for initiation of change*
 - e.g. Key stakeholders need to buy in
 - e.g. Institutional capacity needs to be in place
- Challenge: create conditions to sustain reforms
 - Beyond the crisis

Illustration

- Indonesia financial sector governance
 - Asian economic crisis: devastating impact on economy, politics, society
 - Most severe economic collapse since WWII
 - “eye of the storm”: financial sector
 - Key problem: “opaque” rules for settling commercial disputes, e.g. bankruptcies, bad debts
 - Response (part of IFI-led reform package): establish commercial court system and legal framework (e.g. bankruptcy law)
 - Outcome: once crisis over, “problems of implementation”
 - Attempts to sustain overall reform
 - Sept. 2003: *Economic Policy Package Pre- and Post IMF* (White Paper) or “IMF Programme without the IMF”

Illustration

- Thai Agriculture Sector Program Loan
 - Thaksin elected PM in Jan. 2001 on an “anti IMF/reform” agenda
 - Thai Government cancels loan (2002)
 - *But continues elements of agriculture sector reform process under a domestic “populist” agenda*

Policy Reform Process

A Framework

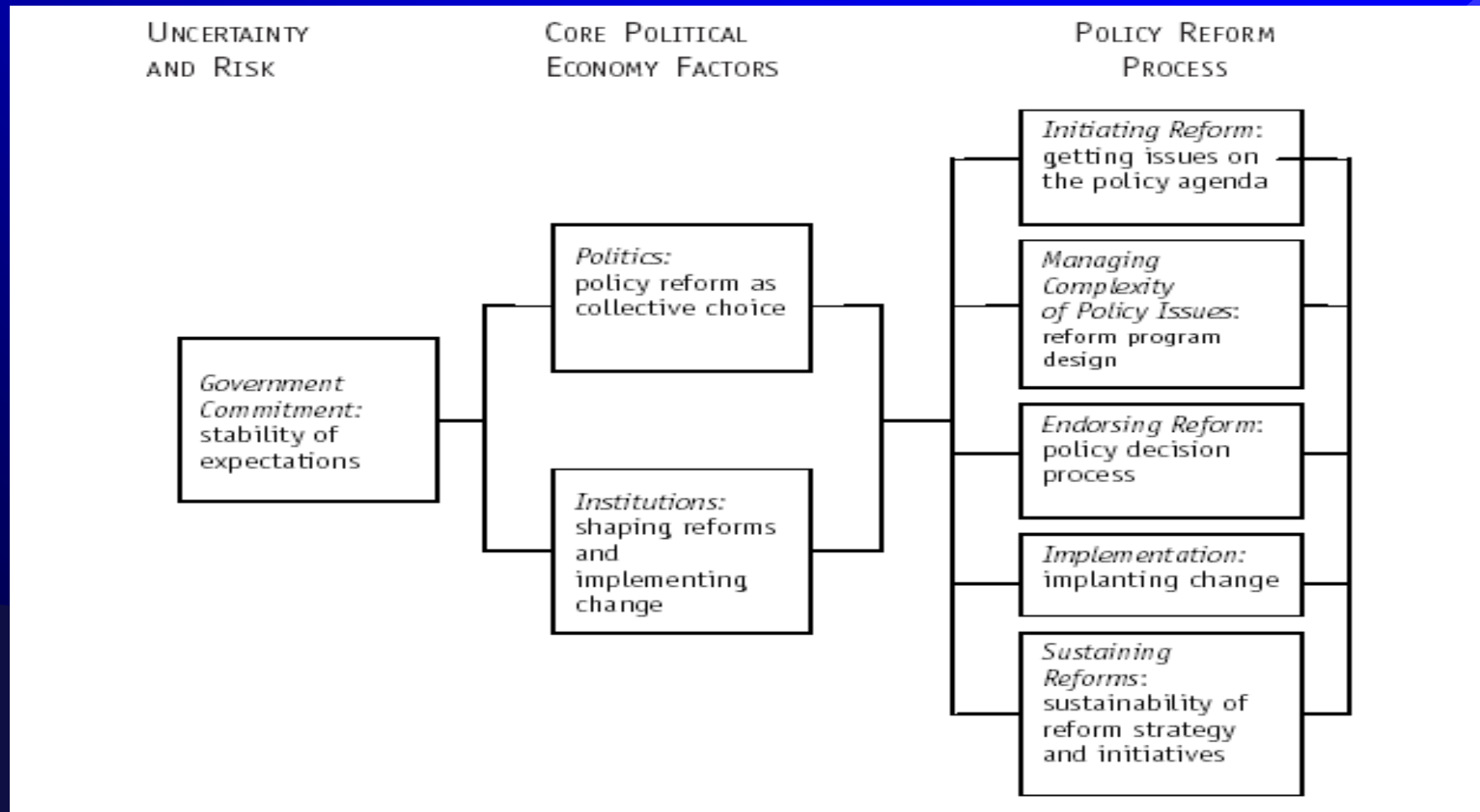
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Policy Reform Process: Overview

- How policy reform is initiated, defined, implemented
 - Set of linked decisions/actions → policy reform → leading to change
 - ‘multi-player’; ‘multi-level’; ‘multi-stage’
 - Relates to:
 - How issue gets on the ‘policy agenda’
 - How issue is defined (e.g. boundaries)
 - What should be done: alternative “solutions”
 - Reform strategy
 - Design/selection of a reform program
 - Implementation
 - What resources allocated to reforms and when
 - What institutions/organizations are involved
 - What sequence of actions taken
 - Sustainability
 - “ah, but will it last??”
- ➔ ***Role of politics and institutions at each ‘stage’***

Political Economy of Policy Reform: Framework – A “Process” Perspective

(Abonyi 2005)



Government Commitment

“Self evident: Evident to oneself and no one else”

Ambrose Bierce

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Government Commitment: Providing 'stability of expectations'

- Critical role of “Government Commitment” in policy reform—where “government” means *formal policy/decision making and resource allocation system*
 - creates for stakeholders (domestic and foreign) ‘*stability of expectations*’ with respect to reforms
 - E.g. Critical part of every IFI (e.g. ADB) PBL document is typical: “major assumption ...is...the Government’s **continued commitment** to proposed reform measures...”
 - Issue: *Is Government Commitment in place now? Does it stay in place as reform process unfolds? If not, why not?*
- *Are there certain times where Government Commitment is easier/harder to obtain/sustain, e.g. election cycle*

Government Commitment and “Ownership” of Reforms

- ❑ Commitment as function of “ownership”?
- ❑ But ownership by whom?
 - Government as “player” and a “game”
 - Commitment requires stable agreement among key stakeholders
 - Within government; within society; between government/IFIs
- ❑ Ownership of reform: a *political concept*
 - Coalition of stakeholders supports reforms *and* has power to work it through stages of the policy process
 - Key stakeholders have interest and power to influence policy reform process—e.g. formulation, implementation
 - Stable coalition among key stakeholders during the policy reform process

Example

- ❑ Different perspective on “ownership” and “government commitment”:
 - Viet Nam SOE Reform Programme
 - Thailand Agriculture Sector Reform
 - Indonesia IMF-led Reform Process

Government Commitment and “Mutual Understanding”

- Stable coalition (necessary for government commitment) is function of mutual understanding
 - Including between Government and IFI (e.g. ADB)
- Constraints on mutual understanding/agreement
 - Differences in data
 - Differences in interpretation of data
 - Differences on what is important (values/preferences)

Illustration of challenges of “mutual understanding”

- ADB’s Lao Second Financial Sector Program
 - Make publicly available financial status of State Owned Banks
 - “what do you *really* mean?”

Government Commitment: Dynamic Concept

- Commitment is a function of:
 - Understanding – *what, why, how*
 - Capability – *what will it take, and can we do it*
 - Intent— *should we do it* - usual meaning of “Government Commitment”
- ‘Government commitment’ is dynamic: may change over time
 - If “lack of commitment” to reform, i.e. actions not taken
 - WHY?—Why NOW??
 - E.g. limited understanding of role of reform
 - more information/more effective communication
 - E.g. political instability/uncertainty
 - requires building new coalition of ‘reform winners’
 - E.g. institutional capacity/constraints
 - capacity building/coordination
 - Different implications for reform process
- Government commitment is conditioned by
 - Politics (stability of sufficiently influential pro-reform coalition)
 - Institutions (capability to implement)

Illustration

- Thailand Agriculture Sector Reform Program
 - Government commitment seemingly reflected in Cabinet passing a plan for restructuring the agriculture sector (May 1998)
 - Followed by policy loan request to ADB (Jan. 1999)
 - Yet significant differences emerged among different “players” in the government; with supposed beneficiaries; with parts of civil society/NGO community; with ADB....because of limits on:
 - *Understanding*
 - *Capability*
 - *intent*

Politics of Policy Reform

"Politics: The conduct of public affairs
for private advantage"

Ambrose Bierce

ADB

Political Acceptability of Policy Reforms

- Policy reform: fundamentally political in nature
 - Diverse, conflicting interests; diffusion of power
 - Associated with any reform: “reform winners” and “reform losers”
- No simple incentive framework to align diverse interests
 - Requiring process of ‘mutual adjustment’
 - *Note: function of institutional context/framework*
 - Need ‘minimum necessary consensus’ of stakeholders
- Challenge: Assessment of political acceptability
 - Stakeholder analysis
 - “Stability analysis”

Illustration: Many types of politics

- Philippine Power Sector Restructuring and ADB Program Loan
 - Executive “commitment”, BUT
 - Legislative politics
- Agriculture subsidies in Sri Lanka
 - Government commits and removes subsidies
 - New government elected on platform to restore subsidies—politics at its most basic
- Thailand agriculture sector reform: water user fees for farmers
 - “popular politics”: “voting on the street”

Politics and consultation: Building necessary consensus

- Consultations with key stakeholders
 - Source of information
 - “Buying in”
 - Time consuming, complex, not fully predictable
- Issues
 - Who to ‘consult’
 - About what
- Strategies of consultation
 - More general: easier to reach consensus
 - Higher risk of future conflict over details
 - More specific: more difficult to reach consensus
 - Less risk of future conflict over details

Illustration

■ Thailand's Agricultural Sector Program

- Extensive consultations

 - But then extensive resistance—WHY??

■ Challenge of consultation: Thai example

- Who to consult

- About what

- When

Bureaucratic Politics of Policy Reform

- Government is not just a “player” in the reform process
- Government is also a ‘game’: multiplayer, multi-level
 - E.g. MOF may sign with IFI; but may not implement
 - Can it ‘ensure’ implementation?
 - Line agencies may not ‘own’ reforms/PBL
 - Especially if resources are uncertain
 - “politics of the budgetary process”
 - Differences (strong vs. weak systems)
- Bureaucratic politics: aligning incentives, coordination
 - What does ‘government commitment’ mean
 - WHOSE commitment in government
 - E.g. how stable within the bureaucratic game

Illustration

- Viet Nam SOE and Corporate Reform Program
 - Assumed key players: Executive (Prime Minister) and central agency—State Bank of Viet Nam
 - But implementation of reform involves Ministries, local governments, individual SOEs—with own interests
- Indonesian Financial Governance Reform Program and follow up TAs/lending
 - Key gap: strengthening institutional framework for supervision and regulation of financial sector
 - Creation of new institution: OJK – start up postponed 2003->2010
 - Position of MOF; resistance by Bank of Indonesia
- Thailand Agriculture Sector Program Loan
 - Ministry of Agriculture and Cooperatives
 - Royal Irrigation Department (RID)

Politics and 'source' of Reform Program: A cautionary note to IFIs

- Policy reform is fundamentally DOMESTIC “game”
- Source of issues/reform on policy agenda
 - Country/internal
 - Domestic political ‘game’ in progress
 - External (e.g. IFI)
 - May initiate and/or complicate domestic ‘political game’
 - May be difficult to predict, require more time and effort
- Implications? (addressed later)
 - “you can’t get there from here” (WB?)
 - May initiate and/or complicate domestic ‘political game’
 - or
 - “help step by step—including baby steps”?

Illustration

- ADB's Thailand Social Reform Program as part of IMF-led program
 - Decentralization of Ministry of Education
 - Resistance within Ministry of Education
 - From key departments, teachers
 - Initiated in 1999
 - Still an “on going game” in 2007
 - Limits to “external push for change”

Politics and 'scope' of Reform: Donor vs. Government Perspective

- **Narrow scope: few reforms**
 - Building stable consensus for change may be more manageable
 - Scope of change more limited
- **Wide scope: many reforms**
 - Building consensus may be more complex, but
 - Demands of change more extensive
 - BUT Note: expanding scope as 'side payment'
 - Can provide “bargaining room” to accommodate interests
- **Excessive externally-imposed reform agenda:**
 - “Donor control”
 - Limited country understanding/ownership
- **Note: ‘Each reform activity is a ‘game’ in its own right’**
 - Each has associated “reform winners” and “reform losers”

Institutional Context: from Implementation to Design

- “If anything can go wrong; it will.”

Murphy's Law

- “Murphy was an optimist.”

O'Toole's Commentary

Institutional Context: Meaning

- 2 meanings of “institutions”:
 - *Institutions as ‘rules of the game’*, e.g. legal system, property rights
 - Context for/conditions policy reform process/outcomes
 - *Institutions as organizations*, e.g. Ministry of Agriculture, Rural Irrigation Department
 - Means for translating policy decisions into actions
 - In practice: Policy reform involves networks of organizations
- Policy reform usually involves both

Illustration

■ Indonesia: business reform

– Institutions as “rules of the game”

- Establishment of strengthened legal framework for commercial law

- E.g. bankruptcy legislation

– Institutions as “organizations”

- Establishment of commercial courts

Institutional Context: Absorptive Capacity

- Institutions are the means by which policy decisions are translated into action.
- Often ignored at reform formulation stage: lack of realism about institutional capacity, existing and required
 - Constraints often surface too late
 - During implementation
 - When adjustment is more difficult
- → *Most effectively addressed at the design stage: logic: ‘from implementation to design’*

Institutional Context: Can it be done?

- Policy reforms require administrative, technical and organizational capabilities
 - Often differ from existing capacity
- Policy reform is about institutional capacity building
 - Needs to be reflected in reform design
 - *But*: Separation of design and implementation
 - Is there 'management perspective' on the reform design team??
- Institutional capacity building/organizational change is a long, complex, often uncertain process
 - **4 rules of organizational change**
 - **Time**
 - **Cost**
 - **Outcomes**
 - **Satisfaction**

Illustration

■ Viet Nam SOE reform

- “corporatization” of SOE involves changes in
 - Legal, financial, accounting
 - Administrative procedures
 - Technical and managerial skills
 - Performance evaluation
 - Reward system
 - Organizational structure
 - Organizational culture
 - Etc.

Institutional Context: Networks

- Policy reforms involve getting multiple institutions to work together within common framework
 - Coordination, alignment of incentives
 - E.g. not be the same as establishment of ‘coordinating committee’
- Requirement: assessment of institutional context
 - For program as a whole, e.g. agriculture sector
 - For specific reforms, e.g. strengthening extension services

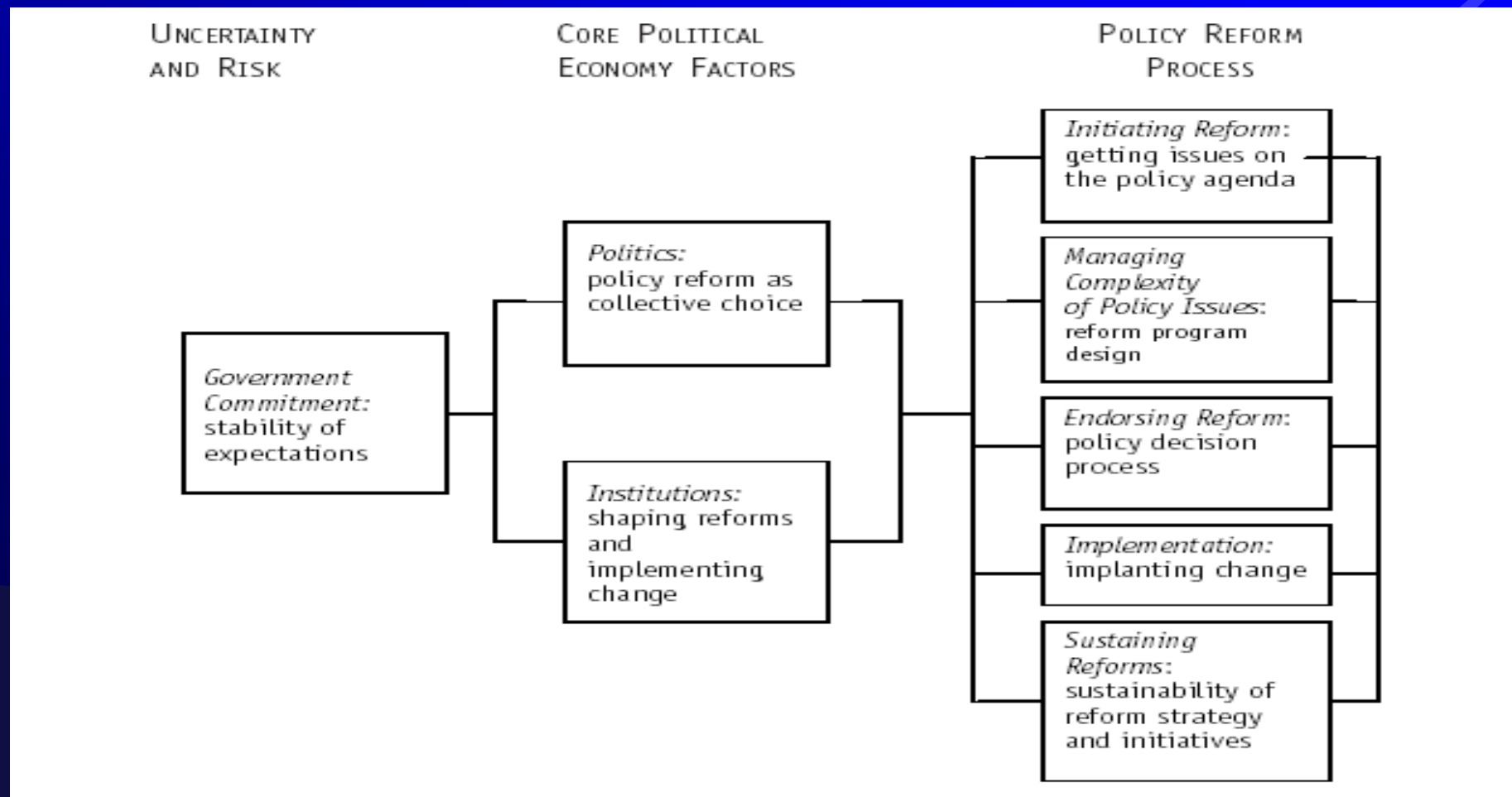
Illustration

- Thailand Agriculture Sector Program: “Establish a Unified Water Management System”
 - Ministry of Finance
 - Bureau of the Budget
 - Office of the Prime Minister (NESDB)
 - ***Office of the National Water Resources Committee***
 - Office of the Permanent Secretary of MOAC
 - ***Royal Irrigation Department***
 - Department of Land Development
 - Department of Fisheries
 - Agricultural Land Reform Office
 - Department of Agriculture Extension

Policy Reform Process: Key Steps

Political Economy of Policy Reform: Framework – A “Process” Perspective

(Abonyi 2005)



(1) Initiating Reform: Getting Issues on the Policy Agenda

- *Just because a policy problem exists does not mean it will be addressed*
 - *Requires policy makers to place issue on policy agenda*
- **Policy Agenda**
 - Set of problems/issues that capture attention of key decision-makers
 - Who control necessary resources and actions
- **Key dimensions**
 - Who “participates” in agenda setting process
 - E.g. stakeholders (external, domestic)
 - In what forums are issues put forward
 - Institutional context
 - through what process
 - Formal
 - Informal
 - *Note: often involves multiple forums*
 - How are the issues “framed”
 - “Expected benefits of reform” vs. “Expected costs of no reform”
 - Learning from “psychology of decision making”
- **Challenge: generating a “stable consensus” on policy agenda**
 - *Stakeholders and coalitions “of influence”*

Illustration

- Thailand: agriculture sector reform
 - domestic reformers, external agents (IFIs) and crisis as “window of opportunity”
 - Change in government: kept key reforms “on agenda”
- Viet Nam: SOE reform
 - Domestic priority BUT
 - Basic differences with IFIs (IMF, WB)
 - E.g. Over scope, pace of reform (“equitization”)
- Lao PDR: financial sector reform
 - Delays over bankruptcy law
 - What does it mean?

(2) Managing Complexity: Policy Reform Programme Design

- Policy issues/problems are “complex”—many possible interpretations
- Formulating the “policy issue/problem”: making complexity manageable
 - So we can act on it
- Boundaries: where does the problem start/stop
 - Whose boundaries
- Key elements/interactions
 - What is important; where do we focus our attention
- *How do alternative formulations of the problem alter institutional and political (stakeholder) map??*
- Reform program design
 - What do we need to change
 - Scope of reform program: “too much” vs. “too little”
 - How do we change it
 - Different options for design of reform program
 - How will we know that the change “works”
- *How do alternative reform program designs alter the institutional and political map?*
- **(And who is “we”)**
 - ***Who participates in framing the problem and design of reform program?***
- *Brief note on methodology—“structural models” (e.g. LFA)*

Illustration

■ Indonesian Financial Governance Reform

- Issue: devastated financial sector (Banks) crippling the economy
- Response: “Problem is the financial sector—the banks; focus on reforming the financial/banking sector” (*note scope of reform program*)
- Outcome: some success—but deep seated problems of economy
- *Alternative formulation*: “where does problem originate? Corporates”
 - Focus simultaneously on corporate reform
- Possible outcome: equal emphasis on corporate reform issues

■ ADB’s support for Viet Nam State Owned Enterprise Reform and Corporate Governance Program

- Issue: development of domestic private sector in a transition economy
 - key constraint: SOEs
- Response: focus on relatively small number of larger SOEs
- Outcome: difficult implementation process
 - History showed this was likely outcome
- *Alternative formulation*: focus on many small SOEs
- Possible outcome: easier to implement with immediate results
 - And “learning” + “demonstration effect”

(3) Endorsing Reform

- Legitimizing policies
 - approving reform strategy and program
 - What is approved? Reform strategy? Program? Measures?
- Where in the process are these decisions taken
 - Formal
 - Informal
- When are they made
- By whom
 - Stakeholders, coalitions
- Are these approval decisions “credible”
 - In signaling commitment to reform
 - E.g. ensuring implementing agency performance; committing resources
- How *stable* are these decisions
 - in signaling sustained commitment to implement reform
- *Elusive nature of “endorsing reforms”*
 - *Yet effective implementation can unfold*

Illustration

- Viet Nam SOE reform program
 - Who endorsed/approved it
 - Where/when
 - What was approved
 - Was it credible
 - Was it “stable”

(4) Implementing Reform: “Nominal reform” vs. “Implanting change”

- What is being “implemented”
 - “stroke of the pen reforms” vs. “implanting change”
 - Implementation as “implanting change through *institutions*”
 - As “rules of the game”
 - As organizations
 - ***Design reform for implementation***
 - Often insufficient attention: lack of realism in design of reforms about institutional capacity, existing and required
 - Constraints often surface too late
 - During implementation → When adjustment is more difficult
- *Most effectively addressed at the design stage:*
- ‘Design policy reforms for implementation’*
- NOTE: *Institutions are ‘political’: change involves winners and losers*

(4) Implementing Reform (cont.)

- Implementing reform through actions/inactions of *stakeholders (i.e. limiting resistance)*
 - Political stability of reforms over time
- Challenge: ensure/assess *political acceptability* of reform at design stage
 - “*stability*” of agreement/expectations among stakeholders
 - e.g. stability: no stakeholder/coalition has power and/or intent to block reforms at various stages in policy reform process
 - Role of consultation, participation

Illustration

■ Implementation and institutional capacity

- Philippines: Opening up Telecom. Sector
 - Challenges to National Telecommunications Commission as “regulator/supervisor”

■ Implementation and stakeholders

- Thailand agric. sector reform: water user fees
 - Extensive consultations
 - Yet extensive resistance

(5) Sustaining Reforms

- **Implanting enduring change**
 - over the long run
 - Managing “process of change” to ensure outcomes
- **Sustaining specific initiatives**
 - Ensuring enduring changes in incentives, behavior and performance at the organization level
- **Sustaining “enabling environment”**
 - Ensuring enduring changes in
 - rules of the game that condition behavior
 - “necessary conditions” for organizational performance

Illustration

■ Indonesia

- *Sustaining specific initiatives*
 - Commercial court system
 - Corporate governance
 - E.g. financial disclosure
 - The “political economy of accounting reform”
- *Sustaining enabling environment*
 - “Domestic LOI” for a “post IMF Indonesia”
 - Post-Soeharto → Pluralistic politics and reform

■ Thailand

- Anti-IMF (ADB) platform for PM Thaksin (Jan. 2001)
- Yet strong rural agenda and agriculture sector focus

Policy Reform Process

Some Lessons

ADB

Lessons

- Scope of reform program: striking a balance
 - Doing too little may be a problem
 - Doing too much may be equally problematic
- Timetable for reform
 - Implementing/sustaining reforms: complex, uncertain, long-term, institution-intensive process of change
- Crisis as “window of opportunity”
 - What reforms to initiate during a crisis
 - How to sustain reforms beyond the crisis
- Assessing Government Commitment
 - Understanding
 - Capability
 - Intent
- Mutual understanding -- Government/IFI

Key PE Factors in PBL Design

- Characteristics of the policy issue, i.e. relative complexity
 - The more complex the policy issue in terms of the number of factors and interrelationships involved, the greater the likely difficulty of change.
- Nature of the policy process
 - The more steps, institutions and participants are involved in approving or initiating reforms, the greater the likely difficulty of change
- Political dimension of the policy reforms involved, i.e. what is required to forge and maintain consensus;
 - The more stakeholders (e.g. groups, institutions) are involved, and/or the greater the intensity of differences among stakeholder preferences, the greater the likely difficulty of change
- Institutional requirements,
 - The more extensive the required changes in processes, systems, procedures, incentives and cultures, and the greater the number of agencies/institutions involved, the greater the likely difficulty of change.
- Mutual understanding between ADB and Government
 - The greater the gap between ADB and the Government on the nature, role, scope, design and expected outcomes of PBL the more likely are the difficulties in sustaining the necessary Government commitment.

Policy Process Checklist

- Key decisions or actions required;
 - What are necessary inputs for the decisions or actions
- By whom (institution; group; role);
- In what sequence;
- Relationship among decisions/actions and associated institutions/roles
- Over what time frame
 - Time horizon associated with each component decision/action,
 - Therefore time frame of the policy process as a whole
- What are potential constraints that could have significant impact on the policy endorsement and implementation process
 - On timing; content; etc. of key decisions/actions
- What are factors likely to influence whether constraints materialize

Lessons

- *Political acceptability of reforms*
 - Assessing political acceptability
 - Understanding the “players” and the “game”
 - Coalition building
 - Stakeholder consultation and participation
 - Ensuring/confirming mutual understanding (key players)
 - Promoting public awareness
 - Relationship between specific reforms and wider political/social/economic system

Political Assessment Checklist

- Who are the key stakeholders with interest in given PBL, i.e. effected by and/or likely to effect the proposed PBL in terms of its inputs, core activities, outputs or outcomes
 - Need clear understanding of structure/boundaries of policy issue/reform program
- What are the assumptions about existing or future behavior and preferences of these stakeholders on which PBL design and expected benefits are based
 - What must be assumed about the behavior and preferences of each key stakeholder in order for the PBL to be successfully approved, initiated, implemented, and lead to the desired outcomes;
- Which stakeholders perceive decreases (increases) in net benefits as a consequence of the PBL
- What specific elements of the PBL are likely to lead to resistance or conflict, e.g. result in perceived decreases in net benefits by particular stakeholders;
- Do these stakeholders have power and means to influence — at limit block — reform process (e.g. approval, initiation, implementation) either individually or in coalitions;
- If yes, do the stakeholders have (or under what conditions would they have) the incentive to do so; and
- How can they be induced to support or at least not oppose the proposed PBL
 - and/or how can PBL design be modified to account for differing needs and preferences not presently accommodated — while ensuring the basic contribution of PBL to policy reform.

Lessons

■ *Institutional feasibility*

- Assessing institutional feasibility of proposed reforms (rules, organizations)
 - Who will have to do what, when
 - Is the institutional capacity there to do it
 - Institutional interactions/network: implications?
- Composition of “reform design team”
 - Managerial skills represented?
- Participation of key stakeholders (e.g. implementing agencies) in design of reform programme
 - Can facilitate
 - Can constrain

Institutional Assessment Checklist

- Which are the core institutions involved in implementation of each PBL conditionality;
- What are key assumptions about implementation capacity of each core institution, implicit in each PBL conditionality, i.e. what must be true about specific capabilities of each institution for the required PBL activities to be successfully implemented;
- Are these assumptions realistic in light of existing capabilities of these institutions, i.e. can they do what is assumed they must do to implement relevant PBL conditions;
- What are key institutional 'steps' in implementing PBL conditionalities, i.e. what are decisions/activities of each institution necessary to implement each conditionality;
- How do activities/decisions of individual institutions necessary for implementing each PBL conditionality relate to each other, i.e. what are existing or required linkages, including coordination and cooperation, among institutions to ensure successful implementation;
- What are gaps between existing and required institutional capacity that could constrain implementation of particular conditionalities, i.e. at level of each individual institutions; in terms of coordination and cooperation requirements among institutions;
- How can these gaps be reduced, e.g. change the conditionalities; strengthen existing institutional capacity as part of, or complementary to PBL

Conditionality

The “so what” test

- *What specific difference would it make to the desired results of policy reform if this particular conditionality were left out of the policy matrix? Does it matter? i.e. is the difference significant in terms of the purpose and/or outcome of the reforms?*

- In this context
 - What is the logical relationship between this specific conditionality, and particular elements of the policy issue to which it is supposed to respond, e.g. what specific problems is it intended to help resolve? what is their relevance/importance in terms of the rationale for policy reform?
 - What is the logical relationship between this specific conditionality and particular expected outcomes, and in what particular ways do these outcomes contribute to the broader purpose and desired results of the policy reform?

Rethinking Policy-Based Lending

A Political Economy
Perspective

ADB

General Direction

- Shift away from traditional “ex ante conditionality” in policy based lending (e.g. “structural adjustment”)
 - Away from “promises of future actions”
- Evolution toward increasing focus on *results-based approaches*
 - Toward “actual actions taken/completed”
- Growing use of budget support as a core “instrument” in policy-based operations
- Increasing focus on understanding on how political economy factors shape policy reform and therefore influence policy-based operations

Expected Benefits

- Greater country control over the details of development programming and policy implementation (greater policy space);
- Enhancing country ownership of the development process
 - choice of policies and instruments
- Flexibility in resource use
- In principle, greater predictability of aid funds, tied to a country's budget cycle
- Increased harmonization among donors, and between donors and country

Risks

- At the same time, countries risk losing some measure of autonomy
 - because of greater donor scrutiny of and involvement in public financial management systems (budget)
 - Likely to be required to engage in wider and deeper policy dialogue over development priorities and resource allocation decisions;
 - May receive less overall donor support for project and program preparation; and
 - Risk increased donor pressure and reduced flexibility through ‘joint donor partnership frameworks’, particularly where country capacity is relatively weak

World Bank

- Basic framework for policy reform support
 - Development Policy Lending
- Key modality (instrument):
 - Programmatic Lending
 - A sequence of 1-tranche/1-year policy loans
 - In medium term framework (e.g. 3 years)
 - Increasingly based on completed “prior actions”
 - Increasingly in the form of “budget support”
 - Therefore increased scrutiny of the public financial management system (budget process)

IMF

■ Rethinking conditionality in 2002

- Drawing back from “structural adjustment” kinds of conditions (e.g. Indonesia) to core IMF focus
- Streamlining of conditions
- Focusing on critical conditions
- Increasing appreciation of “political economy”

Concluding Comment

ADB

So what???

■ Why the PBL

- what is the nature and specific characteristics of the policy issues that define the need for reform and for the particular PBL

■ What difference does it make

- What is the PBL's specific contribution to reform
 - What is the role of key PBL components in the reform process, e.g. the contribution of the expected outcomes of specific conditionalities to the desired results of reform

■ What is needed to make it work

- What are the critical success factors in PBL initiation, implementation, and sustainability, including, with respect to each conditionality:
 - Key steps and potential constraints in the policy-making process, including approval and initiation
 - Key institutional requirements for, and constraints on implementation

3 Cs of Policy Reform

■ **Commitment**

- of policy makers to policies/reforms
- of other key stakeholders involved, to change

■ **Credibility (of commitments)**

- of policies
- of institutions

■ **Confidence (in credibility of commitments)**

- Of stakeholders in policies and institutions (e.g. investors – domestic, foreign): “reforms will be implemented more or less as planned; with more or less the expected outcomes”

Addendum: Political Economy of Regional Cooperation

- Political economy factors are critical “drivers” of regional cooperation at strategy and project level
 - E.g. Greater Mekong Subregion (GMS)
 - E.g. Central Asia Regional Economic Cooperation (CAREC)
- Regional cooperation as “enlightened self interest”
 - Limits individual country freedom to act
 - But expands collective options
- Regional cooperation as a process of *mutual adjustment* conditioned by *institutional capacity*
- Example
 - Upgrade GMS East-West Transport Corridor (1992-2002)
 - “Technical design” as mutual adjustment