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## ALTERNATIVE CONDITIONALITY

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Alternative Conditionality by Frances Stewart

The term 'conditionality' describes the policy conditions prescribed by the IMF, which borrowing countries have to fulfill if they are to secure access to those of the Fund's resources characterised as 'high conditionality' funds. This paper considers the justification, desirability and possibility of Third World countries developing alternative conditionality both for negotiation with the Fund and for borrowing from other financial institutions that exist or might be developed.

Fund conditionality is becoming increasingly important for three reasons. First, the growing difficulties in borrowing commercially have caused an increasing number of countries to have recourse to the Fund. About one-third of developing countries are either negotiating with the Fund or are using Fund resources. Secondly, there has been a marked increase in the proportion of use of high-conditionality facilities. Whereas in 1973 about two-thirds of Fund lending was on a low-conditionality basis by 1980-1 about 75% of new lending involved high-conditionality. Hence the nature of conditionality has become of greater significance. Thirdly, the private sector has come increasingly to wait for agreement on Fund programmes before going ahead with its own lending (including roll-over of existing loans). Thus while the Fund accounts for only a small proportion of total balance of payments financing - in 1982 use of Fund credit and short term borrowing by monetary authorities from other monetary authorities accounted for $6 billion out of a total current account deficit among non-oil developing countries of $97 billion - its influence over other sources of finance is very large. This is illustrated in the case of Yugoslavia:

> "Western banks and governments ...... are counting to a large extent on Yugoslavia's reaching terms with the IMF on a new stand-by accord, before they commit themselves for 1984. Mr. Dragan [Vice - Premier in charge of the economy] has admitted that IMF backing 'is very important for the treatment of Yugoslavia by international capital markets and creditors', as well as providing the Government ... with support against its critics".(Financial Times, Dec. 5th 1983).

Fund conditionality is often viewed from two extreme positions: on the one hand, the Fund and others see conditionality as legitimate and necessary, and the particular conditions imposed as being virtually the only conditions possible to secure the necessary improvement in countries economic performance (See eg. Guitan). At the other extreme, the legitimacy of conditionality as such seems to be questioned by some LDCs, and some famous battles have ensued, as for example with Manley's Jamaica and with Nyerere and Tanzania. There have also been intermediate positions taken. Sidney Dell has criticised Fund conditionality for failing to take into account the source of balance of payments problems, and emphasising demand restraint as a cure even where it is quite apparent that the main source of the problems does not lie with excessive domestic expenditure. A study by the Overseas Development Institute has criticised features of the Fund programmes and has suggested some reforms, placing particular emphasis on developing programmes which minimise the costs of adjustment.

For the most part, however, an all-or-nothing attitude has been adopted by the major actors: the Fund has shown little flexibility with regard to conditionality, while countries have tended either to accept the package as a whole, or adamently to reject it while failing to suggest an alternative package. Where there has been some significant negotiation, as for example with some of the larger countries recently, it has been generally within a framework set by the Fund. In general there has been little serious debate about the nature of conditionality between countries and the Fund; where agreement has been reached it has been on Fund terms and reflecting Fund philosophy. That this is so is not entirely the responsibility of the Fund. Because of the all-or-nothing apprach taken by many countries in many cases the countries themselves have not made serious attempts to present alternatives and to negotiate on them.

The all-or-nothing approach taken by both sides has had a number of serious adverse consequences. First, quite a few countries have failed to reach any agreement over a prolonged period of time and have thus been left in the limbo of permanent crisis, operating on a hand-to-mouth basis for foreign exchange, with adverse consequences for long run development as well as political stability. Ghana's history over much of the last twenty years provides one example of this; Tanzania's recent history another. The recent coup in Nigeria has in part been attributed to prolonged negotiation with the Fund. (See The Guardian, Jan 2nd 1984 "Monetary experts argued yesterday that Nigeria's failure to reach a loan agreement with the International Monetary Fund was almost certainly a factor in the military's decision to remove President Shagari from office"). Secondly, many countries have reached an agreement with the Fund, but have then been unable (or unwilling) to execute the programmes, so that Fund finance has been withdrawn. In the year to April 1982, Fund loans were cut off because of failure to meet agreed performance targets in over one quarter of agreed loans. Countries involved included Romania, Zaire, Morocco, Bangladesh, Zambia, Costa Rica, Tanzania, Guyana, Madagascar, Senegal, Uganda Honduras, and Granada. (Financial Times, April 20th 1982) This group of countries, also, has faced prolonged crisis both of an economic and a political nature, with bad effects on long run development. Thirdly, in quite a few cases, where Fund programmes have been agreed and executed, serious political problems have followed. This has been the case in Egypt, in Sri Lanka and in the Sudan, for example. Fourthly, the programmes themselves - reflecting Fund philosophy, and with little input from the countries - have not been developmentally oriented, with a strong deflationary component. This will be discussed more below.

Many of the political and económic problems associated with negotiations over Fund programmes arise, in my view, from the rigid attitudes taken by both sides : on the part of some countries, it is the view that any conditionality represents an infringement of sovereignty, and hence attempts are rarely made (the Indian negotiations and the recent negotiations with Brazil may be exceptions) to present alternative conditions; on the part of the Fund, there is the view that their package represents the only acceptable adjustment package. If Third World countries sought alternative conditionality, more in line with their philosophy, objectives and individual circumstances, then many political problems might be avoided and more development-oriented adjustment might occur. But to develop such alternative conditionality requires countries to accept, in principle, the legitimacy of some conditionality. While for the Fund to accept alternative conditionality requires them to recognise the boundaries within which conditionality is justified. The next section will discuss these issues.

Legitimacy of Conditionality

All lenders make certain demands of borrowers; they may require sureties for the loans they make; the loans involve interest and repayment schedules and are associated with various provisions which come into effect if the borrowers default. For many lending transactions - national or international - the lenders are not in a position to impose any general policy requirements, nor are the borrowers, often being private firms, or individual parastatals, in a position to form policy at a national level. Banks lending to particular enterprises may well suggest, or even require, certain changes in the management of the enterprise so as to increase the likelihood of prompt repayment. Lending, as distinct from giving, takes place with the expectation of repayment plus servicing and hence the development of conditions associated with the lending is a legitimate aspect of such transactions. But in commercial transactions conditions are confined to those elements which are directly relevant to repayment.

IMF lending differs from commercial lending in three respects. First, the lending is to governments not to commercial entities and hence government policies are a legitimate area for negotiation in determining the conditions associated with loans. Secondly, governments only approach the Fund when they are in overall difficulties (which may be more or less acute, but are never totally absent). Hence it is likely (though not always the case depending on the source of difficulties and prognostication in the absence of policy change) that some policy change is necessary to eliminate the difficulties, as well as access to Fund resources. Only if the difficulties are clearly of a temporary nature due to factors outside the country's control, and ones which are likely to be reversed, is no policy change likely to be the appropriate response.

It follows from these two factors that the Fund's position in lending to governments in financial difficulties justifies some policy conditionality in a way that differs from most lenders. The third respect in which the Fund differs from other lenders is that it is not simply concerned with ensuring policy changes which would bring about a particular improvement in the balance of payments, and hence permit the fulfillment of the servicing and repayment condition* , but also it uses its unique lending

*The servicing plus repayment condition will be referred to in the rest of the paper simply as the 'repayment condition'.

position to impose a particular set of policies on borrowing countries, which it believes is good for them : this is what Sidney Dell has described as the 'grandmotherly' function.

This discussion suggests that some policy conditionality is justified (or legitimate) to bring about policy changes which make it likely that the repayment condition is met. Normally there are, as we shall discuss further below, a number of ways in which this might come about. While the legitimacy of Fund conditionality extends to ensuring a consistent and plausible set of policy changes, there is no legitimacy - if legitimacy is regarded as occurring when lenders impose requirements on borrowers to ensure repayment - in selecting a unique set of policy changes. Viewing the Fund as a lending institution, then, the legitimacy of Fund conditionality covers the repayment function, but not the grandmotherly function.

It may be argued that the Articles of Agreement of the Fund extend its functions (and legitimacy) beyond those of an ordinary lending institution, thus justifying the grandmotherly function. The Articles of Agreement could of course be changed. But taking them as they stand, they are open to a wide variety of interpretations when it comes to selecting particular policy packages: it would, I believe, be impossible logically to derive a unique set of policy changes from the Articles, and very difficult to argue that actual Fund conditionality represents a 'truer' interpretation of the Articles than many other policy packages. Article 1 of the Articles is appended to this paper. It is worth making two points about the provisions of this Article. First, for proper fulfillment of these obligations, the Fund must be able to influence the policies of all countries, especially dominant industrial countries. This is particularly the case for provision (ii)("facilitate the expansion and balanced growth of international trade, and to contribute thereby to the promotion and maintenance of high levels of employment and real income"), (iii) ("exchange stability..."), (iv)("multilateral system of payments ... and the elimination of foreign exchange restrictions") and (vi)("to shorten the duration and lessen the degree of disequilibrium in the international balance of payments of members.") Using its powers over borrowing countries alone to fulfill its obligations (eg. for reduction of trade restrictions) is similar to trying to meet first-best conditions in a small part of a second-best world. The net effect may be to place excessive burdens on borrowing countries (who generally can least afford it) and to bring about a worse situation, from a world point of view, than with alternative policies which take the second-best aspects fully into account.

Secondly, there are potential inconsistencies in the Articles of Agreement in a second-best world; for example, there may be conflicts between the objectives of sustaining employment, income and trade, and the obligation to dismantle exchange and trade restrictions, especially in the short run and in the context of world deflation. These potential inconsistencies permit differences in emphasis and interpretation of the various provisions. Hence the likelihood that a number of policy packages may be equally consistent with the Articles.

The Articles of Agreement, therefore, by no means justify the Fund's rather rigid interpretation of its grandmotherly function. In the rest of this paper we assume that legitimacy is confined to meeting the repayment condition; in devising alternatives countries may need to pay some regard to the Articles, but this is not likely to restrict the alternatives much, given the second-best issue and the variety of interpretation of the Articles possible.

If the idea of alternative conditionality is to be fruitfully pursued, both Fund and borrowing countries need to accept three general propositions:

- first, that a lending institution may legitimately require policy changes to meet the repayment condition - i.e. some conditionality is legitimate (legitimacy);
- secondly, that in most situations there are different packages possible which would meet the repayment condition (alternatives);
- thirdly, that any satisfactory set of policies must be jointly worked out by the lender and borrower, not simply imposed by the lender (joint development).

The last proposition is justified on three (related) grounds: first, it should ensure that the country's objectives and philosophy are taken into account in forming the package; secondly, it should make it more likely that the conditions will be adhered to, which is important in view of the large number which are abandoned soon after negotiation; thirdly, it may introduce some political realism into the programme, and thus avoid some of the political problems that have been associated with Fund programmes.

The first proposition - legitimacy - is always accepted by the Fund, but is often rejected by Third World countries, conditionality being accepted as an aspect of force majeure, rather than a necessary feature of lending to governments in crisis. It is vital that this should be accepted by Third World governments if alternatives are to be devised; this is also necessary for the successful operation of any Third World Bank. The second proposition - the alternatives thesis - seems to be rejected almost entirely by the Fund. The Fund has been strengthened in the rejection of the possibility of alternatives by the fact that very few governments have actually put forward coherent and convincing alternatives. This proposition then needs to be accepted by all parties. The third proposition - joint development - would probably get token assent from both Fund and governments, but the actual process by which programmes are devised does not suggest that joint development of a genuine sort often occurs.

The view put forward here about the desirability of alternative conditionality rests on two assumptions: first, that alternative conditionality is possible; secondly, that it would be preferred by some countries, in some circumstances. The bases for these assumptions are discussed in the following sections of the paper.

Is there an alternative conditionality?

Abstracting from short-term monetary movements, the underlying balance of payments position of a country may be thought of as consisting of three elements, the visible trade balance, the balance on the invisibles account and net long-term capital movements, or:

$$B = (Ex - Imp) + Inv_n + C_n$$

Improvement in this balance may then be brought about by a change in any of the three elements (each of which may be negative or positive). The first, the trade balance, may be improved by increasing exports or reducing imports or some combination. The invisible balance depends on obligations incurred on past debt and direct investment, on payments for other invisibles, such as consultants, insurance and so on, and earnings from such activities as tourism and migrants' remittances. The long term capital inflow depends on the general outlook for investment, and the particular incentives provided to foreign capital.

It is apparent from this very brief account that there are a number of ways of improving the underlying balance, while different elements in the total may be emphasised. Moreover, a variety of instruments may be used to affect the elements in the basic equation. For example, exports may be increased by improving supply conditions (eg. improving the transport network), or by increased incentive to export (eg. by devaluation or export subsidies) Imports may be reduced by a general reduction in demand, by increasing the relative price of imports, by improving the supply of import substitutes, by quantitative restrictions on imports, or by some combination of these policies. There are also alternative policies with respect to the other elements in the basic balance. The extent to which the various alternatives really are alternatives depend on the particular circumstances: for example, if full employment prevails (or some other capacity limitation) , the options are more limited. But in most realistic scenarios, alternative instruments are possible.

It follows from this very simple analysis that there exist alternative policy packages which would improve the basic balance in most circumstances. Hence it is incorrect to assume that any one set of policy prescriptions is uniquely possible, whether that set be proposed by the Fund, or by any other body.

Fund Conditionality

Fund conditionality differs between countries and has changed over time. Nonetheless, there are sufficient common elements for the concept of Fund conditionality to have quite considerable descriptive connotation.

Fund programmes contain three elements: preconditions, performance criteria and other policy elements.(See Bird). Detailed investigations of these three elements (not always possible for preconditions as they are rarely published) show emphasis on demand restraint, especially through control of government expenditure; credit control is almost invariably a major target and the main performance criterion; policies that are favoured include changes in various key prices (exchange rate, interest rate, price policy of parastatals), reduction of consumer subsidies, dismantling controls and outlawing of multiple currency practices.

For example, one Fund st udy (Reichman) of 21 programmes between 1973-5 found that all 21 laid down credit ceilings; exchange rate devaluation was involved in 10 cases; 10 contained trade liberalisation clauses; 16 had clauses to prevent an increase in external debt; and 16 had clauses about government pricing policies. A study of the 1969-78 period showed similar provisions (Beveridge and Kelly), but with some increase in certain conditions during the period: for example, clauses on domestic credit creation and/or budget balance were contained in around 60% in 1969, rising to 95% by 1978; required reductions in government expenditure rose from 10 to 47%; price policy for public enterprises from 5 to 75%; and a reduction in consumer subsidies from 0 to 60%. Towards the end of the 1970s, supply came to be acknowledged as an important aspect of adjustment. Supply policies were interpreted as consisting of policies towards prices and incentives, and were generally added to rather than substituted for demand conditions.(See Killick and Sutton).

The nature of Fund conditionality derives from three elements: the objectives of the Fund programmes, the philosophy of the Fund, in particular its view of economic causation, and the desire to institute programmes which are readily monitored.

According to Guitan, the objectives of the Fund are "to help members to attain, over the medium term, a viable balance of payments position in a context of reasonable price and exchange rate stability, a sustainable level and growth rate of economic activity, and a liberal system of multilateral payments." The philosophy of the Fund is broadly, although not rigidly, monetarist. Control of domestic credit supposedly secures the twin objectives of inflation control and improvement in the balance of payments (although strictly speaking the same instrument cannot attain both).Moreover, along with other monetarist views, it is believed that "the prevalence of inflation and balance of payments deficits, which are often associated with relatively high levels of economic activity .... soon lead to low rates of employment and growth"(Guitan, p 5). Consequently, while it might appear that the heavily deflationary policies would act against the declared objective of sustained growth, the reverse is claimed: they are necessary to permit sustained growth.

The use of domestic credit creation as performance criterion has the advantage of easy monitoring - too easy in a way, hence the high rate of breakdown of Fund programmes. To avoid a breakdown in Turkey recently, the Fund appears to have had to turn a blind eye to 'window dressing' of money supply figures, illustrating the point that there are disadvantages in having rigid and easily monitored criteria.(See Financial Times,Dec. 23rd, 1983).

Why alternative conditionality may be desired

Alternative conditionality may be desired because countries have different objectives from those espoused by the Fund, or because they have a different philosophy, leading to a different view of causality and a different value placed on various instruments of policy. In fact objectives, instruments and philosophy are often intertwined in logic as well as practice, but it is helpful to try and discuss them separately.

Objectives: Improvement in the medium term balnce of payments is a necessary aspect of any conditionality in the present context. However, the precise timing of the desired improvement may differ. Many countries would prefer a longer time perspective to that offered by the Fund. For some the very tight time perspective imposed necessitates very severe measures, which may work in the short run, but may impede long term adjustment. The Fund is to some extent constrained in its time perspective by its nature and constitution. Some relaxation of this constraint is necessary to meet countries' perspective on timing. It seems likely, however, that the Fund could take a longer time perspective even within the existing constraints. Some relaxation of the Fund's own financial constraints should permit a less risk averse attitude on the part of the Fund in determining timing.

In addition to the question of timing, there are differences in the weight placed on the various shared objectives: for example, countries tend to place greater weight on sustaining income and employment, and lesser weight on inflation control and 'orderly' exchange rates. Moreover, countries may have social objectives - eg. with respect to meeting Basic Needs, with associated objectives towards the distribution of the burden of adjustment as between different groups. These differences in objectives are likely to have major implications for the preferred adjustment package. Greater emphasis on sustaining output and employment means that expansionary adjustment is preferred to deflationary adjustment - viz. adjustment through expanded supply of exports and import substitutes, expansion of invisible earnings and improvements in the medium term capital account. Greater emphasis on social objectives means preference for policies which protect those most in need, especially health, education, sanitation and nutrition programmes that are directed towards the most deprived. Governments also face various political pressures/constraints which affect their objectives and chosen instruments. Most governments are vulnerable to urban unrest, and some get their main support from urban working classes. Policies which particularly affect this group - as for example, removal of food subsidies,especially when combined with exchange rate devaluation and control over wages - may completely destablise  the government. The riots in Tunis show the political sensitivity of food subsidies.

<u>Philosophy</u>: economic philosophy is a pervasive factor determining how people consider the economy works, and predicted consequences from particular instruments. The IMF broadly adheres to a monetarist view of how the world works, together with a neoclassical view of the effectiveness of prices. Although the declared intention is to react flexibly to the circumstances of particular countries, examination of programmes in practice suggests a very similar approach to each economy, more-or-less irrespective of particular circumstances.

One fundamental reason for alternative conditionality arises from differences in views on economic causality - largely stemming from differences in philosophy - which lead to differences in view about the effects of various instruments. Some of these differences stem from radically different paradigms, as between monetarists, structuralists, Keynesians and Marxists. Others concern differences arising within the same paradigm (eg. as to the precise supply elasticities). It is not possible here to summarise the nature of the many relevant differences. But it is useful to point to some of these differences which lead to a choice of different conditions in the adjustment package:

(i) The monetarist cum neo-classical adjustment package assumes that there are few structural bottlenecks. Yet in many countries - especially poor countries with heavy reliance on primary products - supply elasticities in response to price changes may be very low without other changes which relax bottlenecks, for example transport improvement. This was found to be a factor in Zaire, for example:

> "There has been little or no success in boosting food and cash crops or in modernising inefficient local industry. All sectors are hampered by a decrepit road and rail network which makes many parts of the economy only accessible by aircraft. In 1981, a combination of these factors led the IMF to abandon a three year $1.2 b. recovery programme"(Financial Times, Dec. 30th, 1983)

(ii) The role of institutions: reaction by institutions - for example, organised workers, marketing boards, parastatals - can thwart or offset the effects of changes in prices following devaluation. In such situations an adjustment package needs to take into account the institutional structure and may need to incorporate proposals to change it.

(iii) Country disequilibrium: almost by definition, the adjustment package is introduced when a country is in severe disequilibrium. The basic tools of neo-classical economics are designed to explore the implications of small movements towards equilibrium, and do not relate in the same way to severe disequilibria. In such situations, the sudden introduction of 'liberal' trade and exchange systems can have very severe effects on incomes, employment and inflation. This seems to have occurred in the case of the Southern Cone countries in the late seventies.(See Ffrench-Davies for developments in Chile).

(iv) World disequilibrium: policies appropriate to an expansionary world with few trade restrictions may not be regarded as appropriate to a situation with severe world imbalances, growing protectionism and financial crisis. In the former a strong case can be made for regarding a multilateral trading system as first best; but in the latter, it is possible that bilateral and regional arrangements may offer countries better prospects for expansionary adjustment.

(v) Growth and inflation: the Fund view, cited above, is that inflation control is necessary for sustained growth and (though this is made less explicit) sustained growth will be the outcome of successful inflation control.Inflation control is seen to follow from tight monetary policies.

As is well known, structuralists take a different view about the causes and cure for inflation. But apart from that, there are critical differences as to the relationship between growth and inflation. First, there is the issue of whether inflation is consistent with economic growth - here the experience of Brazil, among others, counters the view that it is not. Secondly, there is the question of whether the deflationary policies - which it is generally agreed will reduce output in the short term - will in fact lead to growth in the longer term. Much depends on the effects on investment, both in infrastructure (especially for low income countries), and directly productive investment.

These are just a few of the differences which would lead to differences in conclusion about instruments of policy. Empirical work has been surprisingly inconclusive about most of these issues, partly because the nature of the differences are not easily amenable to empirical tests, and where empirical tests do seem conclusive, imaginative economists may argue that there were special circumstances which render them inconclusive. This process must be familiar to anyone who has followed the empirical literature on monetarism and inflation. As far as Fund programmes are concerned, empirical investigations of their effects have shown rather limited effects, one way or the other (See Killick for a summary). On balance they seem to have some positive effects on the balance of payments (but even these are not statistically significant), and no significant effect on other variables like inflation, growth etc. These results do not endorse the view that the programmes would have devastatingly negative effects on growth and investment. But nor do they at all support the view that the programmes are effective in achieving their major objectives. Alternative packages have rarely been investigated, although Papanek found evidence of successful expansionary programmes in Bangladesh (1974-6) and Indonesia (1967-70) (In Cline and Weintraub).

Taking the differences in objectives and the differences in philosophy together could lead to a radically different adjustment package. Because of these differences, joint development of programmes could be very difficult, especially where philosophical differences are important. But only limited agreement is required, that is agreement that the package would be likely to achieve the required turn round in the balance of payments, so long as conditionality is limited to that.

Tanzania: an example

It is worth briefly exploring a particular example to show that alternative conditionality may make sense in an actual context. Tanzania has been selected since I visited Tanzania in 1981 to examine short term adjustment, while putting special emphasis on Basic Needs. (For more detail see Stewart). The alternative conditionality devised then is by no means the only alternative package possible; nor does it necessarily reflect the preferences of the Tanzanian government. All it does is to indicate that alternatives are possible.

Tanzania has experienced acute balance of payments difficulties for some years During this time, attempts to reach agreement with the Fund never had more than very temporary success. For much of the time, the World Bank has made some of its loans conditional on Tanzania reaching agreement with the Fund.

The source of Tanzania's difficulties have been two-fold: a severe deterioration in the terms of trade as a result of developments in the world economy, and a very poor supply performance with exports of agricultural products falling substantially in volume as well as price.

It seems that the IMF required a large devaluation, the removal of price and wage controls and relaxation of import restrictions, permitting imports to be allocated by price rather than administrative decision, together with the normal credit restrictions. Tanzania resisted these proposals vociferously, but seems to have offered little in the way of alternative conditionality. Hence a prolongation of the crisis. The crisis is having serious deleterious effects on productive capacity, agricultural production and therefore exports, since shortage of foreign exchange is limiting essential inputs to the agricultural sector and the transport sector. It is also limiting inputs to the industrial sector which produces the simple consumer goods, such as soap and textiles, which form the 'incentive' goods for peasant agriculture. The crisis is also beginning to have negative effects on Tanzania's previously rather good record on Basic Needs. Ironically, Tanzania has continued to receive high levels of aid per head, mainly in the form of finance for new capital projects, while shortage of foreign exchange for recurrent imports is reducing industrial capacity utlisation to below 25%.

An expansion of production of agricultural exports is essential for Tanzania to achieve improved balance of payments. To achieve such an expansion, a prior need is for flows of imported inputs to agriculture and transport, and for the production of simple consumer goods for the rural areas. Without these changes in price incentives, following devaluation, would be likely to have little or no effect. With them, supply should increase even without changes in price incentives. However, some devaluation would appear necessary to improve the financial position of the marketing boards, which were being run with very large deficits, absorbing a large proportion of bank credit and often failing to make payments to producers, or paying after a long delay. It should be emphasised that devaluation without an increase in production of consumer goods would worsen the situation, since the real incentive to rural producers would not increase, but there would be an inflationary impact on prices. Moreover, a large devaluation, if accompanied by price decontrol and wage control, would result in a very large cut in the real incomes of urban workers (perhaps by one half on the figures that were being discussed). These workers were already on very low incomes; but quite apart from the justice or otherwise of the distribution of burdens, to introduce a cut in real income of this magnitude would be likely to be politically dangerous.

The Tanzanian government has been strongly opposed to the Fund package, partly for the reasons just discussed: it was believed that the package would be economically ineffective and politically disastrous. In addition, there was a deeper objection to the package. It seemed to represent the antithesis of the values that lay behind Tanzanian socialism. While critics are quick to point out that many of Tanzania's policies have proved dysfunctional, in terms of growth and distribution, the government is not prepared to move far in what seems to be a laisser-faire and capitalist direction. The failure to reach lasting agreement, however, will probably do more damage , economically and politically, discrediting the socialist experiment more effectively than almost any adjustment package. Both Tanzania and the Fund need to abandon their doctrinaire stance and consider alternative conditionality.

There are many possible alternative packages. The following contains the main elements of one alternative:

(i)a large and assured inflow of untied foreign exchange over a period of at least three years. This is essential to make it possible to expand exports. Such an inflow could be financed by the Fund, the World Bank and a redirection of capital aid.

(ii) all foreign exchange to be directed towards priority purposes - viz.

agricultural inputs, transport and simple consumer goods.

(iii) a modest devaluation to improve the financing of marketing boards, and to provide some improved incentive to farmers.

This type of package might enable the country to improve the supply of exports and thus to provide a basis for recovery, and escape from the vicious circle whereby foreign exchange shortages result in reduced exports which increase the foreign exchange shortages. In contrast, a deflationary package which emphasised monetary aggregates alone would be likely to accentuate many economic and political problems. Indeed, this is what has happened, as noted earlier, in a somewhat similar case - that of Zaire.

A serious deficiency of the Tanzanian government has been its failure to present a convincing alternative to the Fund package. One reason for this is that <u>any</u> adjustment package involves difficult political choices. In the one briefly sketched above, the cancellation of many capital projects would not be popular, nor would some other changes in the system of price control and import allocation (not described above) that are also necessary. But another reason is a belief that the Fund would not seriously consider alternatives to its own package. In most cases, the Fund has much less to lose by failing to reach agreement than the country. Countries which are politically and economically peripheral are therefore in a much weaker position to argue for alternative conditionality than countries central to the world's financial system. A third reason for failing to put forward an alternative may be the need for 'alternative' technical expertise to do so. Tanzania has actually had a great deal of alternative expertise. But for some countries this can present a real obstacle.

## Conclusion

This paper has argued that Third World countries should present alternative conditionality to that of the Fund -i.e. policy packages which are likely to bring about the required turn round in the balance of payments, but which are more in line with the countries' own objectives, philosophy and circumstances.

It seems that the apparent rigidity and uniformity of Fund packages may in part be due to failure on the part of borrowing countries to develop and present alternatives. Expert advice in devising and negotiating on alternatives would be required for some countries, especially those which are small and with low incomes. This could be provided by various agencies, for example the Commonwealth Secretariat. There is a need for alternatives to be explored at a general level and experience accumulated, on which individual countries can draw when developing their own alternative. Properly developed, alternative conditionality should permit more expansionary adjustment, more politically acceptable programmes and consequently prorgammes which are agreed on more quickly and adhered to more persistently. While Fund conditionality tends to be rather stereotyped, a single model applicable to most countries, it is likely that there would be a number of alternative models, given that each would aim to incorporate special factors about the country, both economic and political. It seems probable that a different alternative would be suitable for low income countries, dependent on primary products; for mineral exporters; for countries with a strong manufacturing sector that has been inward directed; and for countries with outward-oriented manufacturing sectors. In addition size of country will alter economic possibilities. Political variables would provide a further source of differences.

If Fund agreement to alternative conditionality is dependent on the bargaining power of the borrowing country, then the development of the idea will initially depend on it being adopted by countries with a lot of bargaining power. It may then be generalised to countries with less power, using the 'uniformity' of treatment argument to justify the extension.

It is difficult to discuss the question of adjustment and conditionality on a country-by-country basis, separately from wider issues which affect the adjustment process; for example, greater availability of medium term finance would greatly assist more expansionary adjustment, and may, in some circumstances, be essential to it. Adjustment by surplus countries would contribute to adjustment by deficit countries. Some solution to the debt problem would radically change the context in which adjustment takes place. But even without any of these reforms at a world level, country adjustment could be improved with alternative conditionality.

Article 1 of the Articles of Agreement of the International Monetary Fund:

The purposes of the International Monetary Fund are:

(i) To promote international monetary cooperation through a permanent institution which provides the machinery for consultation and collaboration on international monetary problems.

(ii) To facilitate the expansion and balanced growth of international trade, and to contribute thereby to the promotion and maintenance of high levels of employment and real income and to the development of the productive resources of all members as primary objectives of economic policy.

(iii) To promote exchange stability, to maintain orderly exchange arrangement among members and to avoid competitive exchange depreciation.

(iv) To assist in the establishment of a multilateral system of payments in respect of current transactions between members and in the elimination of foreign exchange restrictions which hamper the growth of world trade.

(v) To give confidence to members by making the general resources of the Fund temporarily available to them under adequete safeguards, thus providing them with opportunity to correct maladjustments in their balance of payments without resorting to measures destructive of national or international prosperity.

(vi) In accordance with the above, to shorten the duration and lessen the degree of disequilibrium in the international balances of payments of members.

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