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The Impact of The Poverty Reduction And Growth Facility On Social Services in Ethiopia

STUDY REPORT

First Draft

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EXECUTIVE SUMMARY

Ethiopia's past is characterized partly by socialism, civil war, recurrent drought, and economic mismanagement. Its economy is heavily dependent on agriculture, with 80% of its population living in rural areas being employed in the agriculture sector. The dynamics of population growth low productivity, compounded with some of the forementioned factors have remained major bottlenecks to economic growth and poverty reduction.

Series of Economic Reform Programs (ERPs) have been introduced to facilitate transition from a command to a market oriented-system, which is hoped to restore macroeconomic stability and create a favorable business environment. The first reform program was the Structural Adjustment Facility (SAF) introduced in 1992 by the fund. It initially aimed at stabilizing the economy and breaking with the order of central planning. The SAF was followed by an ESAF in 1996. ESAF was introduced and have the objectives of bringing a faster rate of growth of national income, lower inflation, increased openness, and improvement in investment.

In 1999, the new orientation towards poverty reduction is most dramatically indicated in the replacement of the ESAF by the Poverty Reduction and Growth Facility (PRGF). The PRGF became a new conditionality to get new loan from the fund and reference for other donors and creditors to support developing countries economy. The first PRGF in Ethiopia was approved in 2001 for SDR 86.91 million (about US\$110 million).

This paper briefly examines the nature of poverty reduction efforts under the IMF supported three-year Poverty Reduction and Growth Facility (PRGF) arrangement approved in March 2001, the processes involved in its formulation and implementation with a particular emphasis on its impact on social services in Ethiopia.

The following are evident in the findings from the on set;

- That though broad participation and ownership principles make an integral part of the PRGF, the PRGF was not open to discussion to the public or civil society. This impacts the issue of ownership as well.
- In the case of Ethiopia, the major tenets of the macroeconomic framework were written and published in 1998 in the Policy Framework Paper. Thus in practice, the PRSP draws the macroeconomic component of the PRGF.
- Poverty and social impact analysis (PSIA) are meant to provide information on the trade-offs among different policy options for achieving both growth and reducing poverty with the timing and sequencing of possible reforms, estimate the risks involved to consider appropriate compensatory and complementary measures. The results of the analysis show that the reform has not had a major adverse effect on the poorest 40 percent of the population. The PSIA of the VAT should have been conducted before the introduction of the VAT. Besides, other PSIA studies should have been conducted to see the impact of major structural reforms on the lives of the poor.

On the impact of the PRGF on poverty reduction and provision of social services in Ethiopia

The study reflects that after the program completion

- The macroeconomic stability attained it's inflation target (Though volatile reflecting agricultural conditions and external shocks), targets on international reserves generally met, current account deficits have improved and external borrowing has generally been in

- line with program assumptions. At the same time the debt burden both domestic and external debt has been growing.
- Poverty-reducing spending under the PRGF arrangement rose from 8 percent of GDP in 1999/00 to 15 percent of GDP in 2002/03.
 - Though foreign borrowing has generally been in line with program projections under PRGF, external debt ratios have increased more than projected, especially compared with the original program targets at the end of PRGF it amounted to 99 percent (the original projection being 90 percent).
 - Agriculture remains the mainstay of the economy. However, little progress has been made towards achieving the government's objectives on agriculture and food security.

Public Expenditure and Performances

Public expenditure generally has shown an increase during the program period. The performances of the sectors in light of meeting the MDGs is crucial.

Education

- Perhaps this is a sector likely to meet the MDG targets. However, it is not without serious challenges to reach the target.
- Though enrollment rates especially primary education enrollment rates have grown significantly, the focuses were only the quantitative increase of enrollment rates, schools and teachers over years.
- The difficulty to keep up with the very rapid increase in the number of students has led to situation of compromised quality. The quality of schooling has gone down made worse by overcrowded schools, insufficient school supplies, crumbling school buildings and facilities, poorly trained, demoralized and demotivated teachers and lack of general discipline in the public school system. The number of teachers have not also increased as the number of students.
- Gender and regional disparities also pose challenges to the educational system.

Health

- Health expenditure in Ethiopia, both public and private, is very low.
- Health services are severely limited. Ethiopia has one of the world's highest ratios of population per doctor and per nurse; and there are only 384 health centres serving a population of over 67 million. Coverage has increased in the past 5 years; the proportion of the population within 1 km. of a health facility rose from 52% to 61%; but utilization remains low, and lower-tier facilities are often by-passed because they lack staff or drugs.
- Regional differences are quite large; and the share of operation and maintenance expenditures is low in most of the regions. Availability of essential drugs has improved recently, but shortages are still common in public facilities.
- Demographic and Health Survey however shows that the poor are much less likely than the better-off to benefit from immunization and other specific public health interventions.
- HIV/AIDS poses additional challenge to the health system now and in the future.
- Regarding the role of the private sector in health, there has been a little progress recorded in opening clinics and hospitals in bigger cities, but this is quite far for the mass of the rural population.
- Generally Despite efforts by the government, the donor community and civil society to reduce poverty in Ethiopia, poverty is still rampant.

Reversing the negative impacts

- Generally, notable progress has been observed in the midst of such challenges as a result of the increase in poverty reducing spending. This is indicative of the fact that if it is done in an enhanced manner, it will be possible to address the basic human needs. This calls for the involvement of all development partners and stakeholders.
- There is a need for the Bank and the Fund to focus more on broad participation by all stakeholders for better ownership of the programs than program conditionalities and their observance.
- The IMF, with the Bank, should give serious considerations to social impacts of the reform measures especially in countries like Ethiopia where PSIA is at its infancy. Based on the results, the Fund needs to reconsider the conditionalities and/or introduce safety net measures for the severely affected.
- Increase the support to the country according to its identified priority areas.
- Debt relief is also crucial for the country's future development.
- Government should ensure the preparation of PRSPs to take a more participatory process, i.e. sustainable involvement and public debate of the civil society, the poor, the government and donors.

1. Introduction

With a population of about 70 million, Ethiopia is one of the poorest and least developed countries in the world. The annual population growth rate is estimated at 3%. The UN's Human Development index, in 2004, ranked Ethiopia 170th out of 177 countries. Its economy is heavily dependent on agriculture, with 80% of its population being employed in the agriculture sector. The challenges facing the country are multifaceted. The dynamics of population growth is very high, its economy is highly dependent on unreliable rainfall, very low productivity, and structural bottlenecks.

This paper briefly examines the nature of poverty reduction efforts under the IMF supported three-year Poverty Reduction and Growth Facility (PRGF) arrangement approved in March 2001, the processes involved in its formulation and implementation with a particular emphasis on its impact on social services in Ethiopia.

2. Overview of the Macroeconomic Framework in Ethiopia

Real GDP growth during the 1990's and 2001/02-2004/05 averaged 5%. However the performance of Agriculture was very poor during this period. On the other hand, population had been growing on average, by 2.9%, implying about 2% growth rate of per capita income. The inflation rate in the 1990's, was below 5% while it peaked to 10.1% on average during the years 2002/03-2004/05. Due to high dependence on the agricultural sector growth was highly volatile. This is as a result of agriculture being highly dependent on rainfall. During the last three years export earnings have been growing dramatically averaging 23%, and imports have been growing on average by 29%.

Fiscal years 1998/99 to 2001/02 however saw pressure building up in the macro economy due to the conflict with Eritrea, deterioration in the terms of trade and effect of continuous drought. The tax revenue increased to 12.8% of GDP in 2004/05 from its level of 10.4% of GDP in 2000/01. External resource flows to the country has been increasing. External grants rose to 4.6% of GDP in 2004/05 from its level of 4.3% of GDP in 2000/01. External grants in the form of budget support increased significantly and its composition has shifted significantly from loans to grants. Government expenditure also showed an increasing trend during this time. While defense expenditure remained same, poverty targeted expenditures rose significantly from its level of 12% of GDP in 2001/02 to 14.5% of GDP in 2004/05. During this period, capital expenditure rose significantly. Ethiopia's monetary policy has continued to focus on maintaining price stability and achieving international reserve targets. Accordingly, broad money supply increased by 19.6 percent in nominal GDP on average from years 1999/00-2004/05.

Agriculture remains the mainstay of the economy contributing on average about 45% of GDP and 85%-90% of export earnings of the country. A single commodity coffee accounted on average for about 35 percent of export earnings. The share of industry has never exceeded 15% of GDP. The import structure of the country shows dominance of basic commodities, for instance, fuel and capital goods.

The macroeconomic policies of the fiscal years 2001/02-2004/05 are built on the continuing support of the IMF program under a three-year Poverty Reduction and Growth

Facility arrangement. The fiscal policy during the last 5 years is aimed at reducing the deficit to a sustainable level while at the same time reorienting investment and current spending in key sectors such as agriculture, water, education, health and road construction.

3. Poverty Reduction Programs in Ethiopia

The initiative to formulate Poverty Reduction programs Ethiopia cannot be seen in isolation from the broad development framework of the country and the influence of the international environment. The 1990s saw the orientation of the earlier development approaches like Structural Adjustment Programs (SAPs) geared towards realizing growth and poverty reduction. Ethiopia also entered the 1990s with the objective of reversing the deterioration of economic and social conditions by creating the necessary policy and institutional environment for poverty reduction.

Given the agrarian nature of the Ethiopian economy, the Agricultural Development Led Industrialization Strategy (ADLI) adopted in 1993 was presumed to be a necessary step that could lead to reducing poverty, enhancing industrial development, and ensuring a dynamic and self-sustaining growth. Thus, the rationale for promoting ADLI is grounded in state of affairs characterizing Ethiopia's rural economy and livelihood systems, prevalence of high incidence of poverty in the Ethiopian countryside, and the existence of considerable potential for growth with abundant under-utilized factor endowments.

Series of Economic Reform Programs (ERPs) were introduced to facilitate transition from a command to a market oriented-system, which is hoped to restore macroeconomic stability and create a favorable business environment. Stabilization and structural adjustment programs were adopted with the objective of liberalizing economic activities. The adjustment programs were intended to restore growth and efficiency and rationalize the role of the state. Most importantly, public expenditure was strengthened and made to focus on building the human and physical capacity of the economy. Accordingly, key Sector Development Programs (SDPs), including education, health, road, and agricultural extension programs were formulated and implemented. Resource allocation favoring vulnerable groups/regions was further reinforced and managing sector development programs were emphasized. Moreover, other policies such as, the National Policy of Ethiopian Women and the National Environment Policy were brought into focus by way of mainstreaming the concerns of women and environmental issues in the development process. While implementing SAP, Ethiopia developed an Interim Poverty Reduction Strategy Paper (I- PRSP) in 2000 and launched the full-PRSP known as Ethiopia's Sustainable Development and Poverty reduction Program (SDPRP) in 2002 that targets economic growth averaging 7% a year in order to reduce poverty by half in 2015. In October 2005, the second phase of the PRSP process, a Plan for Accelerated and Sustained Development to End Poverty (PASDEP), has been put into action as a guiding strategic framework for the five-year period 2005-2010. The PASDEP carries forward important strategic directions pursued under the SDPRP related to human development, rural development, food security, and capacity building but also embodies some bold new directions. Foremost among them is a major focus on growth in the coming five-year

period – with particular emphasis on greater commercialization of agriculture and the private sector- and a scaling-up of efforts to achieve the Millennium Development Goals.

4. The Poverty Reduction and Growth Facility (PRGF) Program and Conditionality

Ethiopia adopted the structural Adjustment Programs prescribed by the IMF and the World Bank in 1992. The first adjustment program was the Structural Adjustment Facility (SAF). It initially aimed at stabilizing the economy and breaking with the order of central planning. The SAF was followed by an ESAF in 1996. ESAF was introduced and have the objectives of bringing a faster rate of growth of national income, lower inflation, increased openness, and improvement in investment. To accomplish these objectives the country was required to have macro economic stability. Such measures included the reduction of public sector deficit by way of restraining government expenditure and privatizing public enterprises. Further requirements include restricting money growth close to the level of economic growth and adopting interest rate policy designed to promote domestic saving. Exchange rate adjustment mainly through devaluation and trade and payment liberalization towards opening the economy to the rest of the world are also indispensable components of the structural adjustment policies of the Fund and the Bank. Deregulation of the prices of goods, services and factor inputs is another prominent conditionality. Reform on the banking system and financial sector is also another important requirement for structural adjustment program. Other major reforms on the financial sector include, reduction of financial repression by removing ceilings on interest rate, restoration of solvency to the system and improvement in bank infrastructure.

In 1999, the new orientation towards poverty reduction was most dramatically indicated in the replacement of the ESAF by the Poverty Reduction and Growth Facility (PRGF). The PRGF became a new conditionality to get new loan from the fund and reference for other donors and creditors to support developing countries economy. The PRGF was approved in 2001 for SDR 86.91 million (about US\$110 million). The conditions to be put in the PRGF program were to emerge from the recipient country poverty reduction strategy, as laid out in its Poverty Reduction Strategy Paper (PRSP) or Interim- PRSP. It is assumed that important social and sectoral programs and structural reforms aimed at poverty reduction were identified and prioritized in the country's PRSP. It was also expected that the document be produced in a transparent process involving broad participation from the government, nongovernmental organizations, civil society and donors. In this regard, locally produced PRSPs were expected to generate fresh ideas about strategies and measures needed to reach shared growth and poverty reduction goals.

The broadly PRGF supported programs in Ethiopia have the following key features: - (IMF, March 2002)

- | |
|---|
| <ul style="list-style-type: none"> ○ Broad participation and greater ownership, ○ Embedding the PRGF in the overall strategy for growth and poverty |
|---|

- reduction,
- Budgets that are more pro-poor and pro-growth,
 - Ensuring appropriate flexibility in fiscal targets,
 - More selective structural conditionality,
 - Emphasis on measures to improve public resources management/accountability,
 - Social impact analysis of major macroeconomic adjustments and structural reforms.

In this context, targets and policies embodied in PRGF supported programs were expected to emerge from the countries own poverty reduction strategy spelt out in the PRSP of the specific country. Ownership was to have dual advantages. First the authorities would have more knowledge to recognize specific conditions of the country. Second, commitment to implement development strategies and programs identified in the PRGF would be high as the government and other stakeholders participate from the beginning. In the process of developing ownership countries would be in a position to plan, design, implement, monitor, and evaluate their development strategies. (IMF, December 2001)

To support the reform agenda indicated in the PRSP, the PRGF was envisaged to (a) Increase annual economic growth from 5 percent to about 7 percent (b) limit inflation to low single digits, and (c) raise the import reserve cover to about four months. To achieve such objectives the program focused on four policy components (a) the reorientation of budgetary resources from defense towards poverty alleviation outlays, (b) tax reforms that lay the foundation for strong revenue performance, (c) improved monetary management and financial sector reform, and (d) capacity building and regulatory reforms to improve the delivery of government services and to promote private sector development.

Under this three year arrangement, six reviews have been conducted. The table below shows the PRGF implementation sequence table in Ethiopia.

PRGF Sequence Table	
March 2001	IMF Approves PRGF Arrangement for Ethiopia
August 2001	First Review
March 2002	Second Review
October 2002	2002 Article IV Consultation and Third Review
September 2003	Fourth Review
March 2004	Fifth Review
January 2005	2004 Article IV Consultation and Sixth Review

N.B. All reviews were been made as scheduled but the fourth review was delayed by 6 months because of delay in the completion of financial audit of the Commercial Bank of Ethiopia (which was a benchmark). Thus the arrangement was extended by four months.

Source: Compiled from press releases by the IMF

- *A comparison of program conditionalities and compliance under SAF, ESAF and PRGF*

The number of program conditionalities increased significantly under PRGF as the table below demonstrates. However, the government and the Fund had uneasy relations under the three-year ESAF arrangement. Only two of the six disbursements were made during ESAF. The mid-term review of the first annual ESAF arrangement was not concluded largely due to a failure to reach understandings on the structural reform agenda (including external current account liberalization and CBE reform) and the start of the conflict with Eritrea.

According to the Fund's last and sixth review of the three years PRGF arrangement, program compliance under the arrangement has generally been categorized good compared with the experiences under the previous programs and especially the ESAF. The reforms under PRGF include liberalization of the external sector and interest rates, the reorientation of spending to poverty alleviation, the speeding up of tax reform, privatization, and the strengthening of the financial sector, including by removing barriers to foreign bank entry. The government, however, resisted to allow foreign bank entry to the financial sector in that it would be premature and that priority should continue to be given to strengthening the domestic banks and enhancing supervision by the NBE the importance of fostering microfinance institutions.

Ethiopia: Program conditions under SAF, ESAF and PRGF

	Number of Structural Conditions				
	Structural Benchmarks (3 yr total)	Performance Criteria (3 yr total)	Prior Actions (3 yr total)	Total Structural Conditions	
				3 yr total	Avg per yr
SAF Program, 1993-95	17	0	0	17	5.7
ESAF Program, 1997-99	8	4	0	12	4.0
PRGF Program, 2001-03	9	7	19	35	11.7

Source: Adopted from EPA, 2004:18

5. The PRSP processes in Ethiopia

The preparation of PRS in Ethiopia commenced following the approval of the Interim Poverty Reduction Strategy Paper (IPRSP) by the Executive Boards of the Fund and the Bank in November 2000. In subsequent years, activities pertaining to the preparation of PRSP and subjecting the same to public consultations were allegedly undertaken. The

PRSP Document, “Sustainable Development and Poverty Reduction Program” (SDPRP), was finalized in July 2002. According to the Ministry of Finance and Economic Development of the Government of Ethiopia, SDPRP went through a series of consultation processes that were officially launched between August 2001 and March 2002. Consultations took place at the Woreda, Regional, and Federal levels inducing the participation of 6000, 2000, and 450 persons respectively. Participants were drawn from government agencies, non-governmental organizations, community representatives and prominent individuals, religious groups, women’s groups, professional associations, journalists, and the business community (*Ibid.*).

The Ethiopian Government issued the Interim Poverty Reduction Strategy Paper (IPRSP), which outlined poverty reduction approaches based on a) Agricultural Development-Led Industrialization, b) judicial and civil service reform, c) decentralization and empowerment, and d) capacity building in the public and private sectors as its major contents. These were presumed to help in realizing goals and objectives relating to poverty reduction (MOFED 2000). In addition, the document incorporated sectoral and sub-sectoral development programs (agriculture, education and health, infrastructure). As could be observed in the policy reduction matrix of I-PRSP covering the period between 2000/01 and 2002/03, the Government pledged to address concerns associated with poverty through a series of policy measures and interventions that were deemed crucial in bringing about improvements in food security, agriculture, industry, and prevention of HIV/AIDS. Poverty reduction program indicators of I-PRSP embraced such welfare components as reducing poverty and inequality through increase in average income, progressive increase in average yield per hectare, augmenting the share of education, agriculture, and health in budget allocation, and improving access to health and educational services and clean water. On the other hand, reduction of infant, child, and maternal mortality rates were set as targets to be achieved during the period in question.

6. Components of the PRGF of key concern to Ethiopia

6.1. Public Participation on policies and objectives under the PRGF

Though broad participation and ownership principles make an integral part of the PRGF, the PRGF was not open to discussion to the public or civil society. The explanation for this was mostly the difficulty of presenting the highly technical macroeconomic issues to ordinary citizens. Thus the process had limited impact in generating meaningful discussions, outside the narrow official circle, of alternative policy options with respect to the macroeconomic framework and macro-relevant structural reforms. This reflects in part the absence of any mechanism to ensure that key issues were aired and the broader debate well-informed.

Ownership under such a situation is also mixed. The approach has often generated relatively strong ownership in a narrow circle of official stakeholders responsible for driving the process, but much less among other domestic stakeholders. The perception that the approach is overly influenced by procedural requirements of the Bretton Woods Institutions (BWIs) is widespread.

Issues pertaining to the preparation and subsequent submission of I-PRSP in terms of the participation of the public in general and stakeholders in particular attracted some controversy. While the government alleged that this was preceded by extensive debates (MOFED 2000: 38), (Dessalegn 2001: 5) others observed that that the government's claim of involving people in discussion in connection with the May 2000 Elections cannot serve as a substitute for open public debate of the document. The government was criticized for lack of transparency in the formulation of the PRSP from the beginning. It is argued that the government did not invite public consultation on the interim PRSP nor even make the document available to the public until other non-governmental organizations like FSS launched a series of debates on poverty and initiatives associated with PRSP (*ibid.*). Critics objected the manner in which the public debate was stage-managed by the government when it finally invited public consultation on the subject. It was alleged that the debate was not on poverty in Ethiopia and how to combat it, but was rather on the contents of the government's key development policies such as the Agricultural Development-Led Industrialization Strategy (ADLI), the Five-Year Plan of Action, and the Rural-Based Development Strategy, which impoverished the discussion on poverty reduction drives. The implementation of the PRSP was not undertaken in a transparent way: the government did not provide information on how budgets were allocated, how the programs involved were implemented, and what kind of targets were designed (Kassahun and Tekie 2003). There appears to be no attempt to identify the programs that have been specifically designed with the PRSP in mind and which programs are regular programs of the government.

6.2. The PRGF and PRSP

The link between PRSP and PRGF is crucial to see the extent to which the PRGF has been drawn from a country's PRSP. In the case of Ethiopia, the major tenets of the macroeconomic framework were written and published in 1998 in the Policy Framework Paper. Thus in practice, the PRSP draws the macroeconomic component of the PRGF. This has been stated in the SDPRP itself as "...Macroeconomic Framework in SDPRP is consistent with our three year PRGF program with the IMF" (SDPRP 2002).

6.3. Social Impact Analysis of Major Structural Reforms

Poverty and social impact analysis (PSIA) meant to provide information on the trade-offs among different policy options for achieving both growth and reducing poverty. It will also assess the timing and sequencing of possible reforms, estimate the risks involved, and consider appropriate compensatory and complementary measures. However, PSIA is currently at its early stage in Ethiopia.

The single PSIA was conducted on the tax reform which introduced a value-added tax (VAT) which replaced sales tax in Ethiopia in January 2003. The newly introduced VAT has a uniform rate of 15 percent on most goods and services, with a zero rate on exports and exempted goods and services as opposed to the sales tax which was levied on imports and domestically produced goods at a top rate of 15 percent but some ranging between 5 to 15 percent and services like medical and educational services were completely exempted.

Compared with the sales tax, the new VAT taxes services in addition to production of zero-rating to exports, and giving exemptions to fewer basic products. The VAT was expected to enhance revenue, improve economic efficiency, promote exports, and foster growth. However, the broadening of the tax base, the increase of the tax rate, and the choice of exemptions has had differential effects on the income/expenditures of different groups of the population. This has been the justification to conduct the PSIA on the new tax reform. According to the results published in IMF's working paper "Social Impact of a Tax Reform: The Case of Ethiopia", the reform has not had a positive effect on the poorest 40 percent of the population. However, the VAT is progressive in its incidence, and the higher revenues brought about by the VAT could provide additional funds for poverty-reducing spending, including primary education.

Though a good step, the PSIA of the VAT should have been conducted before the introduction of the VAT. Besides, other PSIA studies should have been conducted to see the impact of major structural reforms on the lives of the poor. The most usual excuse is the lack of donor funds. However, enough resources need to be allocated for such a purpose.

7. Impacts of the PRGF on poverty reduction and provision of social services in Ethiopia

Five years passed since the inception of the PRGF/PRSP process. The assessment at the end of the program period indicates mixed results. According to the Ex-Post Assessment (EPA) report, the macroeconomic stability attained is inflation was brought down (Though volatile reflecting agricultural conditions and external shocks), targets on international reserves generally met, current account deficits have improved and external borrowing has generally been in line with program assumptions. However as to the report growth was weaker than targeted and highly volatile. The main reason for weak performance was weak agricultural growth. The IMF accepts that macroeconomic stability was attained during the program periods. But this also has a lot of shortcomings and it is impossible to conclude that stability has been attained during the period. Inflation target though achieved was highly volatile during the program period. In addition the fact that it was low does not mean good, because low inflation rates has high tendency of decreasing employment and production. At the same time the debt burden both domestic and external debt rose considerably during the program period.

7.1 Poverty Targeted Expenditure

Poverty-reducing spending under the PRGF arrangement rose from 8 percent of GDP in 1999/00 to 15 percent of GDP in 2002/03. Poverty targeted expenditures (Expenditure on Education, Health, Agriculture, Water, Roads) have grown significantly (by 206 percent) during the years 2001-2004 (See Annex II). Expenditures for all poverty-targeted expenditures have been 4.5 billion Birr and it grew to 9.2 billion Birr. The increase in education expenditure is high that between the periods 1994-1997, it has grown by 260%. Also expenditure on health has increased by 97.7% in this period.

7.2. Debt and Debt Sustainability

Though foreign borrowing has generally been in line with program projections under PRGF, external debt ratios increased more than projected, especially compared with the original program targets, due to unanticipated declines in GDP. The ratio of external debt to GDP amounted to 83 percent at the end of the ESAF (the original projection was 68 percent) while at the end of PRGF it amounted to 99 percent(the original projection being 90 percent).

Even after the expectation that HIPC Initiative would reduce the present value of debt to exports ratio to 150 percent, the ratio is projected to increase over the next few years and remain above 200 percent through 2010. This has left Ethiopia to remain one of the most vulnerable highly indebted countries, though its debt service burden remains low.

Debt sustainability remains unstable even after three successive Fund-supported programs and the HIPC completion point, and fiscal and external deficits remain large.

7.3. Food Security and Agriculture

Agriculture remains the mainstay of the economy. However, little progress has been made towards achieving the government's objectives on agriculture and food security. With only minor exceptions, the same policy intentions were restated during each of the annual arrangements under the Fund-supported programs. The principal objective of the government's agricultural policy since the start of the reform program was to ensure food security through increased production, employment and income, and to increase foreign exchange earnings through increased exports. Yet agricultural productivity remained broadly unchanged during the program period, production remained extremely vulnerable to recurring droughts, and food insecurity remained a critical problem (with around five million people requiring food aid, even in a "normal" year).

According to the Citizens Report Card (CRC)* published by PANE (Poverty Action Network Ethiopia) 2005, reveal that roughly one fifth of the farmers included in the survey have borrowed money for agriculture and related activities. It also indicates the absence of formal marketing support. More than half of the farmers included in the survey reported loss of crops and cattle. Agricultural extension services scoreboard for the rate of satisfaction is amongst the least from the other sectors covered under the survey (Education and Health).

8. Public Expenditure and Performances of selected sectors

8.1. Education

As indicated in the SDPRP document, the objective of the education sector is to facilitate access to elementary education for all citizens along with improving quality and ensuring relevance to socio-economic development. The general education system in Ethiopia consists of four levels. Primary schooling is divided into 2 cycles (grades 1-4) & second

§ The CRC reflects the results of a survey conducted in rural areas of 3 regions (Oromiya, Tigray and SNNPR) and one urban area (Dire Dawa).

cycle (5-8) Junior secondary (grades 9-10) is the terminal level for most students entering secondary while grade (11-12) are for those students going on to university.

The education program launched under SDPRP is a very big push to increase primary school enrollments, including:

- promotion of universal free primary education;
- considerable increase in the number of teachers, education spending, construction of new schools, and availability of textbooks;
- special programs that are responsive to the needs of pastoral areas where it is more difficult for children to attend school;
- greater shift to community control over schools and resources enabling communities and parents to have more say in education and school management;
- programs to improve the quality of education by upgrading teacher training, revising curricula and textbooks, and improving English language teaching;
- efforts to increase the number of girls in school; and
- special programs to use information technology, computers and television in teaching all over the country.

Total education sector spending in 2001/02 was ETB 2.9 billion (US\$ 333 million), or 14% of total public expenditure. Two-thirds is spent on primary and secondary schooling, and the balance on technical and university education. Budgets increased by over 50% in real terms in the past five years, reflecting a conscious effort to redirect resources and expand access to education. Spending on education as a share of GDP (4.5%) is now comparable to other low-income countries, but in absolute terms, at about US\$3.50 equivalent per capita, recurrent spending is below that in most other very-low-income countries. The composition of education spending appears broadly appropriate, but the over-riding issue is the insufficiency of spending at all levels.

General (Primary and Secondary) Education Spending

Primary school enrollments almost doubled, from 4.5 million students in 1996/97 to 8.1 million in 2001/02, consistent with government's education-for-all policy. Gross enrollment is currently about 62%. The expansion has placed tremendous strains on the system, and quality has suffered.

In terms of gross enrollment rate (GER) at primary level, the achievement in 2004/05 is 79.2% (female 70.9% and boys 87.3%), which is higher than the revised 70% target set for ESDP. Similarly, the net enrolment rate (NER) has also increased from 24.9% in 1996/97 to 67.8% in 2004/05.

However, looking into the regional perspective, the gap in the GER at primary level is very wide. For instance in 2004/05 Addis Ababa and Gambella, have GER of over 125%, while the GER for Amhara, SNNPR and Direedawa, ranges from 75.9% to 80.3%. The two predominantly pastoralist regions, Afar and Somali, have 17.1% and 20% GER respectively. Although there is an encouraging progress in enrollment, the variations between regions evidently demonstrate that there is a lot to be done to achieve UPE and maintain equity among regions.

The GER at primary level in rural areas increased from 45.3% in 2000/01 to 67.3% in 2004/05, which is an increase of about 50% in four years. However, the rural-urban gap in GER remained wide. In 2000/01 the urban-rural gap in GER at primary level was 88.6 percentage points. In 2004/05 this gap was not reduced significantly, it remained at 85.3 percentage points.

Total recurrent spending on general education in 2001/02 was ETB 1.4 billion (\$ 159 million); about 67 % of it at the primary level and 33% at secondary level. Despite increases in education budgets, recurrent spending per student had declined by about 20% over the past five years, as the result of massive enrollment increases. Educational outcomes are difficult to assess in the absence of standardized testing. Intermediate indicators show improvement in getting students enrolled in school, but less success in keeping them there. High student-teacher ratios and drop out rates are limiting the effectiveness of money that is currently being spent.

The average number of children in a class has deteriorated to 73: 1 at the primary level, and 80:1 in secondary school. These averages mask large variations, and it is not uncommon to come across 120 students or more in a single class which impacts the quality negatively.

Salaries consume 93% of recurrent spending, leaving little for non-wage operating costs. Some items are dramatically under-funded - for example budgets for building maintenance have declined over the past five years, while the stock of schools has increased. Textbook availability, while improved, is still a major problem, with an average of only about one textbook to every three children. The costs of correcting some of these problems are not huge. To provide minimum non-wage recurrent inputs is estimated to cost ETB 200 million p.a. (\$23 million); to provide a full set of textbooks at the primary level is estimated to cost ETB 178 million (\$21 m.) p.a. The largest problem in a fiscal sense is the deficit of teachers: to restore the student-teacher ratio to a reasonable level, even without allowing for any growth, would cost an additional ETB 333 million (\$39 m.) annually, requiring an immediate 33% increase in current budgets. Relatively small amounts of non-wage recurrent funding, if predictable and regular, could be extremely useful. The current education strategy proposes such grants to schools, but the Regions lack the resources to finance them.

Efficiency is reduced by high drop out rates: 29% of students drop out in grade 1, and over 55% leave before the end of grade 3; for these children little effective education is taking place.

Gender disparity is another challenge facing the education sector. In terms of enrollments, Current trends suggest that the Ethiopia is potentially in a position to reach this goal; currently about 40% of students are female in both primary and secondary school. At the university level, where only about a quarter of students in public institutions are currently female, the challenge is greater. Furthermore, drop out and repetition and diversity of the fields after the secondary level need special attention.

Though enrollment rates especially primary education enrollment rates have grown significantly, the focuses were mainly on the quantitative increase of enrollment rates, schools and teachers over years. However, very little about improving the quality of education has been done. The difficulty to keep up with the very rapid increase in the number of students has led to situation of compromised quality. Many researchers believe that the quality of education has fallen very dramatically in recent periods. According to the World Bank's review of Education Sector Development (ESD) Mid-term review conducted by the World Bank, the quality of schooling has gone down made worse by overcrowded schools, insufficient school supplies, crumbling school buildings and facilities, poorly trained, demoralized and demotivated teachers and lack of general discipline in the public school system. Furthermore, large regional differences are witnessed in terms of participation in the education system.

Furthermore, The CRC (2005), findings on education highlighted that the costs of education varies across regions. According to the Citizens Report Card recommendations, this requires reconsideration of the existing policies.

8.2. Health

The overall objective of the sector is to increase access to health services. The Health Sector Program accords priority to prevention of diseases, enhancement of preventive health services, broadening of health service coverage, and maintenance of quality health care. The Program targeted the most common poverty-related diseases: malaria, tuberculosis, childhood illness, and HIV/AIDS. Emphasis was also to be given to measures to improve mother and child health care (MoFED, 2002).

Health expenditure in Ethiopia, both public and private, is very low. However, the obstacles to effectively delivering health services are large -- the population is largely illiterate and dispersed in rural areas with difficult access, fertility is high, and sanitation is limited. Nevertheless the leading causes of mortality and morbidity are related to infectious diseases, most of which could be substantially reduced with cost-effective public interventions.

Health services are severely limited. Ethiopia has one of the world's highest ratios of population per doctor and per nurse; and there are only 384 health centres serving a population of over 67 million. Coverage has increased in the past 5 years; the proportion of the population within 1 km. of a health facility rose from 52% to 61%; but utilization remains low, and lower-tier facilities are often by-passed because they lack staff or drugs. The decline in immunization coverage is a cause for concern, given that immunization is one of the most cost-effective health interventions available.

Over the past decade health spending increased from 0.9% to 1.5% of GDP; but the bulk of this increase took place in 2003, and recurrent per capita spending has been fairly stagnant since. Subsequent increases have taken place mostly on the capital budget; they have been volatile from year to year, and substantially under-spent in some years.

On average, total spending (including capital) increased only from about US\$1.2 per capita in 1996/97 to \$1.4 in 2001/2002 Ethiopia spends a lower than average share of the budget on health.

The fact that recurrent spending has remained constant in real per capita terms while capital spending increased lends support to concerns that facilities may be being built that cannot be properly staffed and operated, and also suggests there are operational constraints to raising recurrent spending. According to MoFED data, execution of the budget was only 8% in 2001, mostly due to lags in capital spending. Problems in implementing investment plans, and difficulties in utilizing donor funds are the main reasons for low execution. Public spending is somewhat biased towards hospitals and urban services, although the extent of the bias is not as extreme as in some other countries. In 2001/2 38% of recurrent expenditure took place at the hospital level, and 3% at the health post and centre level".

The composition of recurrent spending is reasonable: approximately 61% of the recurrent budget pays for salaries, while 26% goes to medical supplies. Regional differences are quite large; and the share of operation and maintenance expenditures is low in most of the regions. Availability of essential drugs has improved recently, but shortages are still common in public facilities. Funding for drugs has increased five-fold from 1996/97 (EFY89) to 2001/02 (EFY94); a substantial part of the increase came from the government's own budget.

Evidence on who benefits from public health spending is mixed: Welfare Monitoring System data suggest that the poor use public facilities as much, or more than the non-poor, possibly because they use rural facilities which are bypassed by the better-off. The Demographic and Health Survey however shows that the poor are much less likely than the better-off to benefit from immunization and other specific public health interventions. Increasing the effectiveness of spending depends on improving staffing. Current plans for a major expansion of health workers would put Ethiopia on a path to achieving coverage targets in terms of aggregate supply. The issue however is not just (or mostly) the supply of staff, but their utilization, posting, management, supervision and incentives.

In the short run, as long as the public sector cannot provide the conditions necessary to retain highly skilled health professionals, the emphasis should be on hiring and gradually upgrading lower-skilled community outreach workers, and paramedic staff such as midwives and nurses.

HIV/AIDS poses additional challenge to the health system now and in the future. HIV/AIDS prevalence is estimated at 6.6%, with about 2.3 million people currently infected, and some 1.2 children have already lost one or both parents. High prevalence among 15-24 year olds suggests Ethiopia may be on the cusp of a more rapid spread of HIV/AIDS in the next 5 to 10 years.

Regarding the role of the private sector in health, there has been a little progress recorded in opening clinics and hospitals in bigger cities, but this is quite far for the mass of the rural population.

CRC reflections on the health sector reveal similar drawbacks underlining the fact that both urban and rural populations agree on the fact that the provision of health and sanitation services has improved over the past two years. Accordingly, more than a third of rural respondents travel a distance greater than ten miles to reach a health facility. Among the areas that need to be addressed with regard to the health sector include: the remoteness of health facilities, the unavailability of drugs and wide variation in costs.

8.3. Employment and labor market

After nearly two decades of experiencing command economic system, Ethiopia resorted to a more liberal economic system where market forces and private sector has greater role. Ethiopia started restructuring its public enterprises with a view of enhancing efficiency and promoting the role of the private sector in the economy. To this effect it enacted a new public enterprise law in 1999/2000. The objective of the public enterprises reform goes beyond making the public enterprises more efficient. It aims at altering the role of social forces in the economy in favor of the private agent vis-a-vis the government. Following this, Ethiopia embarked on the privatization program.

According to a study conducted by CETU (2001), from the Trade Unions perspective, privatization has encouraged private employers and some government organizations to adopt a more hostile reaction to workers and of their unions. The benefit of privatization has been highly emphasized while its social dimension is superficially stated. Thus the study conducted attempted to analyse the impact of privatization on the labor market.

According to the study, a significant number of workers from the privatized enterprises have been retrenched, some enterprises closed operation after privatization (which had severe impacts on the workers), while factors like bankruptcy and foreclosure threatened workers well being. No basic assistance measures have been considered either by enterprises or by the responsible government offices for retrenched workers. Furthermore, job security is threatened by the increasing number of returned licenses and slow down of the implementation of approved investment projects and foreign investments.

Most Trade Unions have not been in favor of the privatization program. This is mainly because of lack of transparency and consultation mechanisms. Neither workers nor their representatives have been consulted at the inception or in the due process. A significant majority of the trade unions claim that fundamental rights of workers has been violated. In some enterprises, even pension rights of workers have been denied.

9. Reversing the negative impacts of the PRGF on social services

Despite efforts by the government, the donor community and civil society to reduce poverty in Ethiopia, poverty is still rampant. A significant portion of the Ethiopian population lives in abject poverty lacking the basic necessities of life. According to available data, 45 percent of the total population is categorized as absolutely poor, i.e. they are unable to get the basic necessities every day. Now the country is under a ‘Trap of Poverty’. It is thus crucial to address what should be changed and done to mitigate poverty and achieve the MDGs. The following should at least be made to bring about sustainable growth and come out of the poverty trap.

Though a number of reforms have been made by the IMF and the World Bank in their policy perspective that they followed to the developing countries, it suffers from a number of problems. It is believed that the structural adjustment program requirements based on the classical economic theory that output, employment and prices (including wages, interest rates the exchange rates) are best determined by the free play of market forces and that prices are the most effective instruments for the efficient allocation of resources. In most of the developing countries, particularly in Sub-Saharan Africa, however, realities proved the other way round. Practically, countries adopting the structural adjustment program are forced to move towards freer markets with out being in a position to take full advantages of available market opportunities. To this end, because of the low capacity to adjust their supply, programmed countries fell to enjoy the expected results. In other cases, countries those managed to prop up their export supply highly affected by significant fall in price. Coffee export prices could be cited as a case in point.

Though policy changes have been made towards the PRGF/PRSPs, and it is claimed that there is high ownership for countries themselves, the basic policies of the donors have not changed as expected. Their conditionalities that have been in the structural adjustment programs have not changed dramatically. Hence, to reverse the negative impacts of the Poverty Reduction Growth Facility (PRGF) on poverty in Ethiopia the following measures have to be taken. Though there is no ongoing long term program with the Fund, the lessons to be drawn from the Ethiopian experience will help governments, the Fund and other stakeholders for future programs and undertakings of the poverty reduction measures.

- There is a need to focus more on broad participation by all stakeholders for better ownership of the programs than program conditionalities and their observance. The macroeconomic issues that are beyond the grasp of ordinary citizens should be leveled for open discussion by all stakeholders.
- The IMF should, with the Bank, give serious considerations to social impacts of the reform measures especially in countries like Ethiopia where IPSA is at its infancy. Based on the results, the Funds needs to reconsider the conditionalities and/or introduce safety net measures for the severely affected.
- As also put by the Government after the completion of the program period, the Fund’s reflection on

For the Governemnt,

- PRSPs should be prepared with a more participatory process, i.e. sustainable involvement and public debate of the civil society, the poor, the government and donors. More open and comprehensive public consultations and more participation of endogenous professionals from the country who knows the dynamics of the economy very well is mandatory to alleviate poverty.
- Further a strategic partnership between the government, the NGO sector and the private sector is important in alleviating poverty.
- The PRSPs does not give detail analysis of the level and magnitude of poverty in urban and rural Ethiopia. A key component of the reform agenda for the rural population of the country is ownership of land. The need to change the current policy of state ownership of rural land is very crucial issue in this case. Agriculture is expected to bring about growth to this country and unlike this the PRSP says very little about the agenda. The existing policy has not worked well in motivating the peasant farmer to raise production and increase investment on the land. To protect natural resources and the fertility of the land a new land tenure policy is definitely required.
- The PRSP should focus on Education and Health sectors comprehensively as key sectors and should follow appropriate policies to improve performance in these sectors. The PRSP focuses on the quantitative increase of enrollment rates, schools and teachers over years. However, it says very little about the quality of education. Therefore more emphasis should be given to the quality of education.
- Devise strategies for increasing domestic revenue, regional networks etc
- Impacts of policies on the poor, like the impacts of privatization on the labor market, should be assessed and safety net measures will have to be provided.

Donors

- Generally, notable progress has been observed in the midst of such challenges as a result of the increase in poverty reducing spending. This is indicative of the fact that if it is done in an enhanced manner, it will be possible to address the basic human needs. Otherwise, improvements at the existing rate will not be adequate to bring Ethiopia up to the levels of human development to which it aspires. The Millenium Development Goals will be difficult to achieve, except perhaps in education. The total cost of the inputs needed to reach the MDGs, in terms of social sector budgets alone, according to World Bank estimates would be very roughly ETB 12 billion (US\$1.4 billion) annually, or about four times recent annual spending on basic education, health, and water supply. Thus donors in this regard should:
 - Increase the support to the country according to its identified priority areas.
 - Debt relief is also crucial for the country's future development.

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