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ACCELERATING ECONOMIC GROWTH THROUGH STRUCTURAL REFORM

April 2017

This paper has been prepared for review by the U.S. Agency for International Development under Dexis Consulting Group Contract No. AID-OAA-C-13-00075. It was prepared by John Mathieson with contributions from Amanda Saville of Palladium International LLC and Nicholas Klissas of USAID, and submitted by Erin Endean, Chief of Party, Improving Business Environments for Agile Markets Project (Palladium International LLC) to Contracting Officer's Representative, Paul J. Fekete.

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PURPOSE AND ACKNOWLEDGEMENTS

This report was commissioned by the Office of Trade and Regulatory Reform of the U.S. Agency for International Development's Bureau for Economic Growth, Education, and Environment, Office for Trade and Regulatory Reform (USAID/E3/TRR). It was conceived and overseen by Nicholas Klissas, Senior Legal Advisor, USAID/E3/TRR and alternate Contracting Officer's Representative (COR) for the Improving Business Environments for Agile Markets (iBEAM) contract. The principal author of the report is John (Matty) Mathieson. Nicholas Klissas (USAID) and Amanda Saville and Erin M. Endean of Palladium International LLC contributed to the report. The team interviewed many USAID officers, from various regional and technical bureaus in Washington, DC, as well as staff of the International Monetary Fund and World Bank to develop the insights presented in this report, and is grateful for the insights they provided.

This report serves as a conceptual analysis of structural economic reform and describes how structural reform can enhance economic growth and prosperity. The report presents a synopsis of structural reform, its application over time, and options for future initiatives. The analysis explores the relevance of trade agreements' potential contribution to structural reform efforts and points out ways that trade capacity building, regulatory reform, and other USAID assistance efforts can support such efforts. This report also suggests lessons that can be applied regarding policy targeting, grouping, sequencing, and other factors to heighten performance and results.

The underlying purpose of this analysis is to explore an approach that offers the potential of assisting developing countries to achieve accelerated growth and development. This would not only help improve standards of living and wellbeing in developing countries, but would also benefit the United States, since vibrant economies among our partners will not only be less dependent on foreign assistance but also will create opportunities for the expansion of U.S. exports and jobs.

The report is broad in scope, but does not exhaustively cover all issues raised. The analysis is intended for an audience of development practitioners, although it draws from and cites academic literature. While based primarily on secondary research, the study benefits from insights drawn from interviews with experts within and outside of USAID.

EXECUTIVE SUMMARY

Nations have always installed and adjusted economic policies to achieve competitive advantage and growth, and so the concept is by no means new. Structural reform was built into the Marshall Plan following World War II. Certain developing countries introduced policy reform in the 1950s and 1960s, and these efforts expanded dramatically in following decades. A broad range of reform programs were supported by USAID and other donors in the 1980s and 1990s under an array of rubrics such as private enterprise development and transitioning from import substitution to export promotion regimes.

A significant number of countries enacted structural reforms in the 1990s and 2000s, largely in conjunction with or following periods of financial crisis. Policy change initiatives continue today under an eclectic array of approaches and terminologies.

A current effort of certain institutions seeks to recast structural reform as embracing a range of policies that individually and collectively contribute to increased productivity and growth. This is an appropriate context for this report. Our working definition of structural reform in this report is “the process of improving policies, regulations, and implementing institutions to achieve higher rates of sustained economic and social growth and development.”

* * *

The motivation for USAID interest in exploring the relevance of structural reform approaches today is simple: Structural reform provides the best possible platform for generating accelerated economic growth.

The causal relationship between appropriate economic policy change and higher rates of growth has been confirmed and proven at the theoretical, empirical, and experiential levels. The key theoretical underpinning is productivity. Policy reforms establish greater competition and factor mobility in the supply side of the economy. This in turn generates increased productivity growth, which fuels overall economic expansion.

A significant body of empirical evidence finds that structural reform can enhance resource allocation and boost productive capacity. Statistical analyses have shown that gains from reforms vary, depending on factors such as types of changes implemented, initial economic conditions, or current levels of development. Nevertheless, reforms in all policy arenas – trade, investment, finance, product markets, labor markets, legal systems, etc. – yield positive macroeconomic results.

The actual experience of nations reinforces the conclusion that reform is linked to growth. Historically, economic expansions were largely the result of changes in resource levels (e.g., land, minerals, labor through immigration, etc.). More recently, growth trajectories have been ascribed to productivity gains and policy reform outcomes in East Asia, as well as in parts of Latin America, Eastern Europe, and a few countries in sub-Saharan Africa. Growth gains from policy reforms have been particularly strong in East Asia, exceeding five percent per year in recent history.

While the linkages between structural reform and economic growth have been confirmed, it is important to acknowledge that reform is not a panacea for growth and development. Reform is a necessary but not sufficient condition. For reforms to work, other factors such as political and economic stability, as well as investor confidence, need to be in place. In addition, to generate real sustained growth, reform efforts must be accompanied by investments in productive resources (e.g., education, infrastructure) and in industry competitiveness.

Reforms exert a range of impacts, mostly beneficial, on different sectors. Given the plethora of possible policy changes and underlying circumstances, it is impossible to estimate the effects of reforms on different sectors with any specificity. Nevertheless, there is sufficient evidence on the *direction* of impacts.

- Trade liberalization yields consumer benefits and productivity growth spurred by access to productive inputs and competition, but can also result in displaced labor in the transition period.
- Streamlining business processes leads to investment growth and job creation.
- Achieving an appropriate balance of regulations that channel behavior through incentives into productive rather than rent seeking activities can improve the outcomes of market forces.
- Reducing government interventions such as price and credit controls stimulates entrepreneurship, productivity, and output in agricultural sectors.

Benefits and some costs associated with policy changes can be identified for all sectors, such as financial and capital markets, infrastructure, and the legal system. Effective structural reform does not imply that all regulations are by definition harmful. Some rules such as competition policy and fair labor standards contribute to sustainable development. The goal of structural reform is to introduce “smart” regulations that steer economic behavior in the right direction but do not fundamentally suppress productive activities.

While structural reform is targeted primarily to achieve economic objectives, it can also produce social impacts, both positive and negative. However, if designed carefully, reform can contribute to socially desirable ends. Because it lifts productivity and economic growth, reform provides the wherewithal to support social investments and performance. Fiscal modifications that introduce progressive taxation reduce income inequality. Investments in education, health care, gender equality and financial inclusiveness can serve as both a cause and beneficial effect of sustained economic growth. At the same time, planners need to take care to ensure that reforms are environmentally sustainable and include protections for adversely affected groups.

U.S. Support for Structural Reforms

The United States actively supported policy reform programs even before USAID was established in 1961. USAID’s Bureaus and Missions have historically sponsored reform activities covering virtually all relevant policy areas. The private enterprise initiative of the 1980s spawned a variety of efforts, and USAID provided assistance to many countries involved in economic transition in the 1990s.

A number of activities and resources related to structural reform currently reside in the Bureau of Economic Growth, Education, and Environment (E3 Bureau). These include Inclusive Growth Diagnostics, Trade Capacity Building, Domestic Resource Mobilization, Land Tenure, and systematic assessments of energy and power sectors sponsored by the Office of Energy & Infrastructure Programs and the Office of Global Climate Change. Work on regulatory reform and enhancements to business-enabling environments also are housed principally in the E3 Bureau. Similar system methodologies for food sector strategies are taken by the Bureau for Food Security. The U.S. Government’s multi-agency Partnership for Growth program (implemented principally by USAID), now winding down, represented a targeted experimental approach to structural reform.

Regional Bureaus and Missions have traditionally supported structural reform efforts in their regions. Certain regions (Europe and Eurasia, Latin America, the Middle East, and Asia) have witnessed waves of reform activities at different times, and now offer assistance on a demand-driven basis when opportunities arise. Activities are currently diffuse as a result of competing priorities and limited resources for economic growth-related programming.

Despite this promise, efforts to change economic policy are difficult, due to inertia grounded in current perceptions, behavior, and expectations. The benefits of reform are only achieved over time, and reforms often incur intervening adjustment costs that undermine support. Regional dynamics frequently affect reform patterns, since nations often confront economic conditions comparable to their regional neighbors and seek regional competitive advantage. Reform plans need to address a series of challenges, some of which are technical, and others of which address unique political economy factors.

* * *

There is universal backing among donor institutions for appropriate policy change. Only USAID (see inset) and the World Bank, however, have consistently been major players in this arena. The IMF traditionally limited its focus to *structural adjustment* factors¹, but has recently taken steps to broaden the substantive purview of its assistance. The regional development banks concentrate on infrastructure and social programs, some of which have policy improvement components. Bilateral donor agencies deal primarily with poverty reduction, skills training, and sustainable environment goals in addition to infrastructure. Other multilateral institutions (e.g., the World Trade Organization (WTO), Organization for Economic Cooperation and Development (OECD), Asia-Pacific Economic Cooperation (APEC), and United Nations Development Programme (UNDP) advocate structural reform and offer limited technical assistance, but do not have sufficient resources for comprehensive initiatives.

Contemporary Trade Agreements Can Encourage and Support Structural Reform

Historically, nations have collaborated to establish bilateral, regional, or global agreements to liberalize trade policies. The initial focus was typically on tariff reductions and trade policies.

With tariffs worldwide already being reduced to historical lows, trade negotiators are seeking more and more ways to level the playing field and enable firms to compete more fairly. Hence, the coverage of contemporary trade agreements is expanding into new policy and legal areas that have material effects on productivity and growth. These include foreign investment rules, labor standards, e-commerce, dispute resolution, commercial law, state owned enterprises, competition policy, financial transactions, and property rights protection.

Linking reforms in these new areas to trade agreements provides a vehicle to motivate reform, codify current “best policy practices,” and spread structural reforms to signatory countries. For donor organizations, trade capacity building activities (i.e., assisting developing economies comply with such trade agreements) may need to encompass wider array of disciplines promoting structural reforms.

* * *

The findings of this report point to the potential value of fresh ideas and initiatives on structural reform. The benefits of appropriate policies have been proven, and there is new thinking on what works, what does not work, and how efforts should be structured. Most if not all donor organizations support the

¹ Structural reform should not be confused with structural adjustment. In a narrow sense, structural adjustment focuses on “belt tightening” through fiscal and monetary stances directed toward improving a nation’s ability to repay its external debt. This means reduced spending and/or higher taxes in fiscal policy, and higher interest rates and tighter money in monetary policies that are essential to restoring government budget and international payments balances.

concept, but there is no established leadership. Also, in an era of scarce resources, structural reform represents a relatively low cost but high impact activity.

USAID possesses a wealth of experience, expertise and analytic tools related to economic policy reform in the E3 Bureau and in regional Bureaus and Missions. The Agency's CDCS system provides an effective approach to develop country strategies, and the Inclusive Growth Diagnostics and other tools create important insights into policy constraints and possible reform targets. However, USAID's structural reform programs have been offered on something of an "a la carte" basis rather than as a comprehensively structured initiative. Several options for a more comprehensive approach are discussed in Annex D.

Future structural reform efforts can incorporate learnings from past efforts. A new focus on structural reform, drawing carefully on lessons learned from analysis and experience, could yield an important new chapter in development assistance. Strategic lessons include acknowledging that reform is not a panacea, takes time to work, and incurs costs that should be shared equitably. We also have learned the importance of ensuring that partner countries are motivated and can and will sustain support over time. Operational lessons are more tactical, such as the need to tailor programs, cluster and pace waves of reform effectively, and incorporate a component that deals with good governance.

Since each country is unique, it is a mistake to apply "cookie cutter" approaches; programs need to be tailored. Initiatives' success depends on sustained commitment in partner countries. Timing and sequencing is essential. Reforms exact economic hardships on certain groups, and so steps are needed to address transitional issues. These and other lessons should be built into reform activities.

A structural reform program should specify priority policy areas on which to focus efforts. Notwithstanding continuing controversy over which policies should be addressed under structural reform, it is possible to construct a policy agenda that can be adapted to meet varying circumstances. One could envision a three-tiered system. The first tier would consist of "core economic policy foundations" – essentially a nation's basic monetary and fiscal policies. The second would drill down to a country's "business operating policy platform," covering the rules that apply to all economic actors and deal with a host of business processes. The third tier would drill down further to "key sector policies" that concentrate on policies related specifically to critical sectors such as energy or food.

Effective monitoring and evaluation frameworks are critical and require finesse. Monitoring structural reform is complex. Productivity and growth are the result of multifaceted causal relationships and variables that are both quantitative and qualitative. There are often significant lags between the introduction of structural reforms and measurable results, whether directly attributable or not. Deficiencies remain in knowledge and in data quality and availability. Nevertheless, strong monitoring systems are not only necessary but also beneficial in stimulating motivation. A number of common sense steps can be taken to construct robust frameworks. A range of official and private organizations can collectively supply statistics covering macroeconomic performance; monetary, fiscal and trade policies; business operating policies; key sector policies; and social performance.

I. OVERVIEW OF STRUCTURAL REFORM

All functioning entities—businesses, countries or human bodies—rely on a number of systems or structures that collectively determine the ability of the entities to function, or even exist. Some of these systems are more critical than others, but all are important. This report explores a key system that plays a major role in determining the economic performance of every nation: its economic policy structure. Policies shape production and consumption, resource mobilization, commercial interactions, and other processes that collectively result in a country’s economic growth and its citizens’ wellbeing. Fundamentally, policies create a system of incentives affecting human behavior.

The analysis presented in this report is grounded by two indisputable principles. First, there is no such thing as a perfect economic policy structure. This is true simply because economic forces and conditions are always changing, leading to evolving challenges, opportunities, and threats. As a result, all countries continuously modify their policies. Second, because of their relative stage in nation-building, developing countries stand to benefit considerably from improvements in their economic policy structures.² As noted below, the preponderance of theoretical, empirical, and experiential evidence points to the value of prudent structural reform.

A. DEFINING STRUCTURAL REFORM

Structural reform holds a wide range of meanings to actors and analysts involved with economic performance and development. To gain a clear understanding of the issue, it is useful to review existing characterizations, set forth a working definition of the term, and establish a brief historical perspective of structural reform in practice.

The term structural reform has been subject to a wide range of meanings, because both “structural” and “reform” mean different things to different people. In addition, the term has been used extensively by bilateral and multilateral aid groups as well as by academic researchers, each of which has their own interpretation.³

In a tautological sense, some suggest that structural reforms are defined as government-instigated reforms that change the structure of the economy. Others emphasize productivity gains, characterizing structural reforms as those which foster economies that use productive factors as efficiently as possible. Still others view structural reform as the shift away from state-dominated systems and toward market-oriented economies.

Structural reform differs from structural adjustment, as in the structural adjustment programs and loans of the International Monetary Fund (IMF). In a narrow sense, structural adjustment focuses on “belt tightening” through fiscal and monetary stances directed toward improving a nation’s ability to repay its

² This principle also holds for industrial nations. This report focuses on developing countries, since they constitute the key partners of USAID.

³ NEU Newsletter for the European Union, “Structural reforms: what’s in a name?,” December 1, 2014.

external debt. This means reduced spending and/or higher taxes in fiscal policy, and higher interest rates and tighter money in monetary policies, as needed to restore government budget and international payments balances.

Structural adjustment refers to government actions aimed primarily at demand management or stabilization. The IMF recently noted that structural reform addresses economic structure issues beyond the monetary and fiscal policy changes related to structural adjustment.⁴ One could conclude that structural adjustment is related to the demand side of an economy, whereas structural reform is directed primarily at the supply side.

MANY DEFINITIONS OF STRUCTURAL REFORM

Definitions of structural reform vary in focus and coverage, but basically describe the same process.

- European Commission: “Structural reforms tackle obstacles to the fundamental drivers of growth by liberalizing labour, product and service markets, thereby encouraging job creation and investment and improving productivity. They are designed to boost an economy’s competitiveness, growth potential and adjustment capacity.”⁵
- IMF: Longer-term structural changes “. . . may involve the core *structure* of the economy, such as how prices are set, how public finance is conducted, government-owned enterprises, financial sector regulation, labor market rules and regulations, the social safety net, and institutions.”⁶
- Selected academic literature: Structural reforms are loosely defined as policy measures that reduce or remove impediments to the efficient allocation of resources, and involve such areas as the domestic financial system, trade policy and agricultural policy.⁷
- Asia-Pacific Economic Cooperation (APEC): “Structural policies refer to domestic policies and institutions that affect the operation of markets and the capacity of international businesses to access those markets and operate efficiently.”⁸
- U.N. Economic Commission for Latin America (ECLA): “By structural reforms we refer to the changes in regulations, tariffs, tax rates or the control of capital transactions that affect decisions at the micro level. Macroeconomic policy reforms involve fiscal deficit control, changes in monetary policy, and exchange rate management.”⁹

Structural reform can be defined narrowly to cover a distinct set of economic policies (e.g., those governing the activities of private enterprises) or broadly to encompass a wide range of policies and

⁴ International Monetary Fund, “Structural Reforms and Macroeconomic Performance: Initial Considerations for the Fund,” October 13, 2015.

⁵ European Commission, Economic and Financial Affairs, “Structural Reform,” July 30, 2015.

⁶ Khalid Abdel-Kader, International Monetary Fund, “What Are Structural Policies?,” Finance and Development, March 2013, p. 46.

⁷ Dwi Susanto, C. Parr Rosson, and Rafael Costa, “Structural Reforms and Agricultural Export Performance: An Empirical Analysis,” Selected Paper prepared for presentation at the Southern Agricultural Economics Association Annual Meeting, Birmingham, Alabama, February 4-7, 2012.

⁸ Asia-Pacific Economic Cooperation, “Structural Reform,” 2016.

⁹ “Indexes of Structural Reform in Latin America,” Samuel Morley, Roberto Machado, and Stefano Pettinato, U.N. Economic Commission for Latin America, Serie Reformas Economicas 12, 1999.

practices that affect both economic and social performance.¹⁰ For the purpose of this report, we will use the following working definition:

Structural reform is the process of improving policies, regulations, and implementing institutions to achieve higher rates of sustained economic and social growth and development.

This definition focuses on policy and regulatory instruments that enhance long-term economic growth performance. It does not encompass monetary and fiscal policy actions that are directed primarily at achieving cyclical fiscal balance and/or financial stability in the short- or medium-term. However, structural reform can include fiscal and monetary policy changes that affect long-term growth performance, such as fiscal shifts from government subsidies to investments in education or infrastructure, or policies aimed at augmenting growth potential, such as monetary policy changes that eliminate interest rate ceilings or that otherwise lead to expanded private sector access to credit. Additional detail and examples of sector specific structural reforms is provided in section II.B: *Sectoral Impacts from Structural Reform*.

While not expressly noted in the proposed definition, good governance is an integral part of structural reform. Policies and rules need to be applied uniformly, transparently, and effectively. Many reform programs focus on rooting out corruption more than on actual policy change. Good governance requires not only efficient administrative structures, but also fair adjudication systems.

The definition does not limit structural reform to any specific time frame, and so can cover short-term, medium-term and long-term initiatives. In the past, structural reform did not name greater social objectives such as greater equity or reduced poverty, as explicit goals. Practitioners assumed that these objectives could be sought following the achievement of accelerated growth. As will be noted below, these and other goals not directly related to economic growth are being increasingly taken into explicit account in structural reform activities.

B. A REVIEW OF STRUCTURAL REFORM IN PRACTICE

The process of structural reform to improve economic performance has received abundant attention in recent years, particularly with regard to nations experiencing economic or financial crises. In reality, structural reform has taken place since the beginning of civilization, as societies created and then continuously adjusted their frameworks for governing the supply and demand for goods and services.

POST-WWII: MARSHALL PLAN AND THE SPREAD OF STRUCTURAL REFORM

In recent economic times, perhaps the earliest example of systematic structural reform can be found in the Marshall Plan sponsored by the United States following World War II (see box). The program addressed a range of trade, investment and business policies.

Starting in the 1960s and expanding in the 1970s and 1980s, a number of developing countries began to introduce structural reform in meaningful ways, both on their own and in collaboration with donors. Many of these efforts, most notably in Asia, aimed at transitioning from import substitution strategies to

¹⁰ Examples of relevant social policy issues include retirement ages and benefits, health care, access to education, etc.

export promotion stances to take advantage of the burgeoning global market. These reforms involved reducing import barriers and installing policies to encourage inflows of foreign investment.

As the field of development economics matured, the academic world began to stress the importance of policy and institutional frameworks in shaping the prospects of accelerated economic growth. This led to the gradual expansion of projects and technical assistance directed in part or totally at structural reform.

Earliest Modern Example: The Marshall Plan

The Marshall Plan aimed to accelerate the reconstruction of war-torn countries, primarily in Western Europe. Conditions applied to aid recipients pushed them toward a market orientation and away from centrally controlled systems being installed in the east. The Marshall Plan dictated a reduction in many regulations, a lessening of trade barriers, and the adoption of modern business practices. Particularly noteworthy to current development practitioners is the inclusion of a technical assistance program aimed at productivity gains to enhance the productive efficiency of European manufacturers. The Marshall Plan has been called the most successful structural reform program in history.¹

1980S-1990S: MARKET FORCES AND THE WASHINGTON CONSENSUS

In the 1980s, USAID introduced a number of initiatives geared toward urging partner nations to adopt market-oriented systems. Under the banner of private enterprise development, the goal was to transform the U.S. relationship with developing countries from one dominated by aid flows to one driven by trade and investment transactions.

While structural reform activities had been pursued for decades, it was in 1990 that economist John Williamson first enumerated the overall bundle of reforms advocated by the major Washington-based financial institutions (IMF and World Bank), the economic agencies of the U.S. government, and numerous think tanks. He coined the term “Washington Consensus” for a commonly agreed set of ten policy instruments promoted by these players.¹¹

Ten Policy Instruments in the “Washington Consensus”

- 1. Fiscal Deficits** – achieving sufficient discipline to avoid large fiscal deficits relative to GDP
- 2. Public Expenditure Priorities** – shifting spending from subsidies toward pro-growth, anti-poverty services
- 3. Tax Reform** – broadening the tax base and introducing moderate, progressive marginal tax rates
- 4. Interest Rates** – maintaining rates that are market determined and moderately positive in real terms
- 5. The Exchange Rate** – adopting competitive exchange rates
- 6. Trade Policy** – lowering tariffs and liberalizing import restrictions
- 7. Foreign Direct Investment** – removing restrictions on inward investment flows
- 8. Privatization** – privatizing state-owned enterprises
- 9. Deregulation** – removing regulations that restrict competition or impede market entry
- 10. Property Rights** – assuring the rights of property owners

¹¹ John Williamson, editor, *Latin American Adjustment: How Much Has Happened?*, Chapter 2, April 1990.

While Williamson presented these policy instruments as descriptive rather than prescriptive, the Washington Consensus came to be known as offering the broad parameters of the desirable market-oriented approach to achieve economic development and stability. The concept has been subject to a long standing, contentious debate. Even today, skeptics of structural reform base their doubts on the perception that the term is synonymous with the “Washington Consensus.” They cite criticisms for which instruments are included as well as which are missing (e.g., labor market policies), for being inappropriate for certain nations, for representing a “cookie cutter” approach to economic stewardship, etc. Although the development community has essentially moved beyond the Washington Consensus, it nevertheless presents a reasonably comprehensive package of structural reform options.

EVOLVING THINKING ON GOVERNMENT INTERVENTION IN MARKETS

One of the more contentious issues associated with long-term structural reform revolves around what constitutes the optimal degree of government involvement in industrial development. The prevailing orthodoxy among development practitioners is that governments should appropriately set the rules under which markets operate, but not be actively involved in specific industries or sectors. Not only should they steer clear of government enterprises, but in addition governments should not attempt to “pick winners” by providing subsidies or incentives to targeted industries. Market forces alone should drive the growth or decline of specific sectors.

This guidance has been ignored in many countries. Following the example of Japan, which fostered certain industries such as automobiles, South Korea nurtured heavy industry by providing low or even negative interest credit to its large enterprises. Taiwan promoted labor-intensive manufactures through various Statutes for the Encouragement of Investment. Brazil supported ethanol production. A number of developing countries have provided incentives to select industries, citing the fact that the United States itself has taken steps to spur certain sectors such as railroads in the past and electronics in Silicon Valley more recently through government procurement and R&D grants and tax deductions. The “industry cluster” growth approach developed in the 1990s called for active public-private collaboration in high-potential industries and sectors.

The World Bank, the principal international financial institution focused on economic development, has experienced an interesting evolution in its stance toward government intervention in private markets as a part of structural reform. The Bank initially urged developing countries to produce and implement five-year development plans in order to map out their economic trajectories and utilize scarce resources effectively. Upon observing the general absence of critical masses of private enterprises, the Bank then suggested the establishment of parastatal entities to serve as public-private collaboration to jump start industries. Eventually, Bank economists determined that heavy government intervention was mistaken, and thus required the abandonment of state planning and the privatization of state enterprises. New and enduring emphasis has since been placed on the introduction of largely unfettered market forces.

The majority of the World Bank’s structural reform activities in the latter part of the 20th century were associated with the structural adjustment programs (SAPs) of the IMF and World Bank, usually implemented to deal with national crises. The required reforms were a key part of the “conditionality” that the Fund and Bank attached to their loans, and they focused on borrowers’ macroeconomic policies. Conditions are seldom welcomed by borrowers, and so the required reforms have been criticized as exacting excessive austerity on economies, opening up domestic industries to foreign investor domination through privatizations, and undermining national sovereignty. At the same time, the leaders of many recipient countries often quietly welcomed their ability to blame international donors and lenders for unpopular reforms.

1990S-PRESENT: BENCHMARKING ADVANCES IN STRUCTURAL REFORM

In recent years, a substantial range of policy reform efforts have been stimulated by the emergence of several sets of policy indicators, beginning in the 1990s. One such set was pioneered under USAID

support, and included data on 43 policy variables in nine areas (investment, pricing, imports, exports, financial sector, exchange rate, labor, taxes, and intellectual property rights). While this tool, the Commercial Policy Model, was applied in about twenty countries, it was not continued. However, a number of other data sets emerged and are still updated regularly. These include the Economic Freedom of the World index of the Fraser Institute, the Index of Economic Freedom by the Heritage Foundation, and the Global Competitiveness Report of the World Economic Forum. Quantitative data on more specific policy variables are available from other sources.

In the late 1990s, USAID launched its Commercial, Legal, and Institutional Reform (CLIR) technical assistance programs and tools. Under CLIR, technical assistance providers identified and assessed specific constraints to commercial activity in developing countries in close collaboration with public and private sector stakeholders, non-government institutions, and local subject matter experts. Variations of CLIR have sprouted following the 2003 launch of the World Bank’s annual “Doing Business” reports, including BizCLIR, a diagnostic tool which applied indicators and sub-indicators to identify reforms needed to improve countries’ statuses in the “Doing Business” rankings, and AgCLIR, a tool which focuses on the agricultural sector.

The World Bank-administered “Doing Business” is now one of the most widely used commercial policy databases.¹² The reports focus on domestic, medium-sized companies, and measures the regulations to which they are subjected through their life cycle.

DOING BUSINESS INDICATORS¹³	
Beginning with five indicator sets covering 133 economies in its 2003 report, the World Bank’s Doing Business 2017 Report tracks the following 11 indicator sets for 190 countries.	
<ul style="list-style-type: none"> • Starting a business • Dealing with construction permits • Getting electricity • Registering property • Getting credit • Protecting minority investors 	<ul style="list-style-type: none"> • Paying taxes • Trading across borders • Enforcing contracts • Resolving insolvency • Labor market regulation

The Doing Business project gathers, analyzes and presents quantitative data that compares regulatory environments across countries and over time. Nations have used this information to gain domestic public or public/private consensus in moving to improve the efficiency of regulation or implementing policies as they compete with other countries for investment capital (both domestically sourced and from abroad.) Empirical research has shown that there is a strong correlation between higher rankings and greater economic growth.

Policy benchmarking has inspired considerable structural reform activities, largely because it quantifies current policies and desired outcomes. Benchmarking has provided outside, objective measures of nations’ policy profiles, and changes over time have been easy to track. In addition, these data sets have been used for competitiveness purposes since they allow nations to see where they stand relative to

¹² USAID Supports the Doing Business project and jointly implements the Reformer’s Club with the World Bank, recognizing top performers annually. <http://www.doingbusiness.org/Reforms>

¹³ Data for Doing Business 2017 are current as of June 1, 2016. The first 10 indicators are used for rankings. Data for labor market regulation is available, but are not used for rankings.

their neighbors. Countries with higher rankings have “bragging rights” for their status, whereas nations with lower rankings feel compelled to take steps to improve their standing. A number of countries have explicitly used desired improvements in their index rankings as policy reform goals.

In summary, as shown in the preceding brief history, structural reform has been an active part of economic policymaking over the past half century. Successes, mistakes, and varying circumstances and outcomes have led to an evolution of this concept over time. What remains today is an eclectic set of views and approaches toward structural reform. The early promises of substantial and permanent gains from a standard formula of reforms have not materialized due to a variety of factors described later in this report. In addition, reforms have generated certain unforeseen and undesirable effects such as worker vulnerability and lack of inclusive growth that have created criticisms and political backlashes to reforms. As a result, structural reform initiatives are becoming more nuanced and adaptive to different circumstances.

C. IMPLEMENTATION APPROACHES

A considerable range of methods, each of which has merits and shortcomings, has been employed to implement structural reform. Historically, many countries used **self-administered strategies**, designing and carrying out policy changes based on their own merits. In recent decades, developing countries in particular have enlisted **donor support**. Countries at all levels of development have also been compelled to rely on **lender-enforced plans**. In addition, governments arrive at structural reform norms through **bilateral or multilateral agreements**.

Until the mid-20th century, **self-administered structural reform** was the norm. Nations continuously revise their economic policies to address changing circumstances, opportunities and instabilities. However, most find it easier to implement reforms in response to periods of instability or crisis than during times of stability and growth.

Starting with the Marshall Plan, bilateral and multilateral donors became more involved in structural reform agendas through the provision of both financial and technical support. The basic goal was to have recipient countries provide an effective policy foundation for growth and development.

Donor supported structural reform efforts have made use of both “carrot” and “stick” approaches. Grants or loans, perhaps coupled with technical assistance, have been extended as incentives to countries that pledge to carry out policy changes. Some of these efforts address macroeconomic policies, whereas others might incorporate policy reform components within sector-specific programs. Another donor-driven technique that can contribute to structural reform is public-private dialogue and support for industry alliances and/or private sector platforms to identify and advocate specific policy reforms that improve the business enabling environment. Most of these activities have been mutually designed and administered by donors and recipients.

The more coercive, “stick” approaches are typically those associated with the conditionality associated with **lender-enforced** structural adjustment loans. The structural adjustment programs (SAPs) are loans provided by the IMF and/or World Bank to countries experiencing serious financial imbalances. The SAPs require borrowing countries to make certain policy changes in order to obtain either new loans or lower interest rates on existing loans. This conditionality has been criticized because of the onerous economic and social impacts of reforms, and the fact that SAP conditionality did not sufficiently take local conditions, including political-economic factors, into consideration.

Finally, countries are required to comply with policy norms when they join **bilateral, regional or multilateral trade and investment agreements** that may require some signatories to undertake policy reforms to meet these compliance terms. In certain cases, as in many agreements under the World Trade Organization (WTO), developing countries may receive “special and differential treatment” as compared to developed members, under which compliance may be delayed or require technical assistance to implement. Participation in regional trade agreements such as the Central American Free Trade Agreement (CAFTA-DR) and the ASEAN Free Trade Area (AFTA) may entail meeting certain policy reform commitments pertaining to investment policy, regulation of services sectors, or other terms. Nations entering into Bilateral Investment Treaties (BITS) face similar commitments, as do countries seeking eligibility for the U.S. Generalized System of Preferences (GSP). BITS focus on commitments related to investment, such as protecting investor rights, encouraging the adoption of policies that treat private investment in an open, transparent and nondiscriminatory way, and supporting the development of international law standards consistent with these objectives. GSP country eligibility is based on mandatory and discretionary factors such as taking steps to afford workers internationally recognized worker rights and the extent to which intellectual property rights are effectively protected. Annex A discusses in more detail provisions of trade and investment agreements that often encompass structural reforms.

II. STRUCTURAL REFORM AND DEVELOPING COUNTRIES

A. THE CASE FOR STRUCTURAL REFORM AT THE MACROECONOMIC LEVEL

Structural reform does generate accelerated economic growth at the macroeconomic level. This has been proven by theory, empirical analysis, and actual country experience. The degree and longevity of greater growth depend on many factors such as types of reforms undertaken, levels of development of reforming nations, and prevailing domestic and international conditions, but the causal linkages between reform and growth are indisputable.

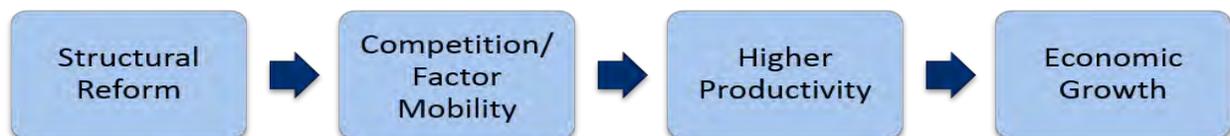
THEORETICAL UNDERPINNINGS

The relationship between structural reform and economic growth is based on a simple but compelling logic of economic supply. Economic output at the macroeconomic level is the end result of labor and capital inputs, with capital being defined as physical capital such as plants, equipment and infrastructure.¹⁴ The only way to achieve long-term economic growth is **either**: (1) to expand the absolute amounts of inputs through capital accumulation and population growth and/or greater labor force participation; **or** (2) to raise the productivity of capital and labor.¹⁵

Structural reform activities aim to reduce restrictions on the movement of goods, services, financial capital, and labor. This freer flow of economic factors generates greater competition and mobility of factors to areas where they can be more efficiently deployed according to market forces. The sum result is improved productivity of labor and capital, which in turn yields increases in output – economic growth.

While structural reform does confer additional benefits, it is the effect of reforms on productivity of economic factors that drives economic growth on the supply side. The accepted term applied to the aggregate productivity of all factors of production is **total factor productivity (TFP)**. This theoretical dynamic can be summarized by the following figure.

FIGURE I. STRUCTURAL REFORM THEORY OF CHANGE



¹⁴ Technology is also a key input, but most economists assume that technology is embedded in either capital or labor.

¹⁵ The definition of productivity in this context is to expand the ability of labor or capital to produce greater levels of output at the same level of input. Greater productivity is generated by new technologies, improved business models, and other forms of innovation.

EMPIRICAL EVIDENCE

A significant body of empirical evidence finds that structural reform can enhance resource allocation and boost productive capacity.¹⁶ Key sources of growth include improved resource allocation within sectors, structural shifts toward higher-productivity sectors, and catch-up growth by absorbing ideas and technology from advanced countries. Reforms that generate trade openness, efficient and developed financial systems, and economic institutions that promote competition, ease market entry and exit, and encourage entrepreneurship and innovation have been found to increase productivity growth at the cross-country, industry and firm levels.

Gains from reforms vary, depending on the types of reforms implemented, initial macroeconomic and political conditions, and the outcome explored (e.g., productivity, output, employment, etc.). Quantitative analysis points to the conclusion that there is a broadly positive relationship between different types of reform and productivity growth.

The IMF has drilled down further to determine that the potential productivity payoff of reforms varies for countries at different levels of development.¹⁷ While keeping in mind that all countries are unique and may display circumstances outside their assigned category, the Fund has determined that in general, reforms in particular areas can provide higher magnitude productivity gains for countries at different levels. The following table below illustrates the results of IMF research.

¹⁶ This section summarizes empirical findings of a wide range of economists presented in several “study of studies” reports by the IMF, including “Anchoring Growth: The Importance of Productivity-Enhancing Reforms in Emerging Market and Developing Countries,” IMF Staff Discussion Note, December 2013, “Structural Reforms and Macroeconomic Performance: Initial Considerations for the Fund,” IMF Policy Paper, November 2015, and “Structural Reforms and Productivity Growth in Emerging Market and Developing Countries,” IMF Working Paper February 2016.

¹⁷ “Structural Reforms and Macroeconomic Performance: Initial Considerations for the Fund,” Ibid. pp. 19-21.

TFP GROWTH GAINS FROM DIFFERENT TYPES OF STRUCTURAL REFORM, BY COUNTRY GROUPS			
Reforms	Advanced Market Economies	Emerging Market Economies	Low-Income Developing Countries
Financial Sector Reform			
Banking system reform	Minor Gain	Moderate Gain	Major Gain
Interest controls			Major Gain
Credit controls	Minor Gain	Moderate Gain	Major Gain
Privatization		Moderate Gain	Major Gain
Supervision	Minor Gain	Moderate Gain	Major Gain
Capital market development	Minor Gain	Moderate Gain	Major Gain
Trade Liberalization			
Tariff rates (average)			Major Gain
Institutional Reform			
Legal system and property rights		Moderate Gain	Major Gain
Infrastructure			
Public capital stock	Moderate Gain	Minor Gain	Major Gain
Market Deregulation			
Agriculture			
Policy environment for FDI	Major Gain		
Promotion of competition		Major Gain	
Hiring and firing regulations	Moderate Gain	Major Gain	
Collective bargaining	Moderate Gain	Major Gain	
Energy/transport/communications	Major Gain		
Innovation			
R&D spending	Major Gain		
 Major Gain  Moderate Gain  Minor Gain			

Source: IMF Staff Estimates

The next table draws upon and adapts the analysis conducted by the IMF as shown in the preceding table. The following table presents possible groupings of target reform categories for nations at different levels of development. This formulation based on quantitative analysis can provide insights and guidance into the possible clustering and phasing of priority policy changes. It should be noted that some focal areas appear in more than one country-grouping category, but may deal with different issues.

HIGHER TFP GAINS OF DIFFERENT REFORMS, BY COUNTRY GROUPS		
Advanced Market Economies	Emerging Market Economies	Low-Income Developing Economies
Growth “Sustainability” Focal Areas:	Growth “Acceleration” Focal Areas:	Growth “Foundation” Focal Areas:
<ul style="list-style-type: none"> • FDI policy environment • Energy/transport/communications deregulation • R&D spending • Hiring and firing regulations • Collective bargaining • Infrastructure investment 	<ul style="list-style-type: none"> • Promotion of competition • Banking system reform • Legal system & property rights • Hiring and firing regulations • Collective bargaining 	<ul style="list-style-type: none"> • Agriculture deregulation • Trade liberalization • Legal system & property rights • Banking system reform • Infrastructure investment

It is impossible to estimate growth outcomes of policy reforms with any degree of confidence, due to differences in the nature and extent of reforms, prevailing economic conditions, and many other factors. In the past, the Asian nations of Japan, South Korea, Taiwan and China witnessed prolonged periods of real growth in the 8-10 percent range coinciding with successive rounds of reforms, and Peru engineered a 10 percent turnaround in long-term growth rates. However, these economies were propelled by rapid global trade growth, tailwinds that have since subsided.

Quantitative analyses have typically focused on specific groups of countries and narrowly defined reforms. However, the IMF has estimated that low income developing countries (LIDCs) exhibited an increase in 5-year average productivity (TFP) growth of 5.5 percent following multiple waves of reforms. Advanced market (AM) and emerging market (EM) economies attained average increases of 2.0 percent. Separate cross-country research covering both rich and poor countries has shown that the correlation between TFP and GDP/worker is an almost perfect fit of 0.96.¹⁸ In short, productivity gains translate directly into increased growth. It is therefore reasonable to project that structural reform could yield incrementally higher economic growth on the order of 1-3 percent, and perhaps more in developing countries, under the right economic circumstances.

COUNTRY / ECONOMY EXPERIENCE

Every nation’s development path can be traced through a series of both cyclical episodes and structural transitions, each of which can push an economy toward either growth or decline. In the past, historians ascribed growth trajectories primarily to changes in resources (land acquisitions, minerals discoveries, immigration and educational advances, application of capital goods in mechanization, etc.). More recently, analysts of quantum shifts in growth trajectories have assigned most causality to reforms in national policy frameworks for governing economic forces. Several examples are summarized below.

It is important to acknowledge that these country experiences do not show approaches to install a uniform, orthodox set of policies such as the so-called “Washington Consensus,” described later in this

¹⁸ Evidence assembled by C.I. Jones, “The facts of economic growth,” Stanford GSB and National Bureau of Economic Research, working paper draft version 0.4, April 6, 2015, cited in “Economic Development and Productivity: The Crucial Linkage of Inclusive Growth,” Yuwa Hedrick-Wong, Mastercard Center for Inclusive Growth, August 12, 2015.

report, which has been subject to considerable criticism. Instead, these case studies represent examples where nations combined the adoption of appropriate policies with initiatives unique to each country's economic circumstances. These nations undertook tailored versions of structural reform rather than simply waiting for economic performance to improve.

Taiwan: Successful Sequenced Reform

Taiwan is an instructive example of successfully sequenced reform. Following the achievement of political stability after civil war and separation from China, Taiwan began in the 1950s with land reform, monetary reform and government budget balancing to achieve economic recovery and stability after a half century of colonization by Japan and the ravages of World War II and civil war in China. This was followed by the policy reform away from import substitution and toward export promotion in the 1960s. During this period, Taiwan's economic leaders worked closely with U.S. foreign assistance advisers.¹⁹ Taiwan enacted a "Nineteen Point Program" that addressed almost every major component of the country's economic, fiscal, monetary, and investment and trade policies. Taiwan also introduced a highly successful export processing zone (EPZ) program. This and subsequent waves of reforms set the stage for explosive, sustained economic growth and dramatically improved income distribution.²⁰

South Korea: Adapting Reforms to Evolving Conditions

South Korea also adapted its structural reform over time to meet changing challenges. As in Taiwan, South Korea's economy experienced foreign occupation and civil war. Again, once stabilization was attained, the country was by the mid-1950s an economic "basket case" with low per capita income and limited production. After depending largely on foreign assistance in the 1950s, South Korea instituted a first round of reforms in the early 1960s, beginning with changes in the tax, budgetary and foreign exchange systems. This was soon followed by other measures, including incentives such as obtaining low-interest bank loans, import privileges, permission to borrow from abroad, and tax benefits) for exporting and encouraging inflows of capital and foreign investment.²¹ The result was rapid growth, fueled by high investment rates, booming exports and a stable macroeconomic environment.

In the early 1970s, South Korea embarked on a second round of reforms, driven by a controversial move to stimulate the nation's heavy industries, including steel, machinery, chemicals, and shipbuilding. Policy changes included low interest rates and devaluation. This strategy led to another round of rapid growth, but eventually the requirements of increased foreign indebtedness generated external imbalances and the financial crisis of 1970-1980. The result in the early 1980s was yet another shift in reform, focusing on privatization, economic liberalization, and elimination of restrictions on market entry and exit. One major outcome of this latest round was an average annual TFP growth of 3.6 percent, driven by higher productivity growth across sectors.²²

¹⁹ Council for U.S. Aid (CUSA).

²⁰ The Taiwan Development Experience and Its Relevance to Other Countries, SRI International, Kwang Hwa Publishing Company, 1988.

²¹ "Economic Growth in South Korea since World War II," in Foreign Trade Regimes and Economic Development: South Korea, National Bureau for Economic Research, 1975.

²² "Anchoring Growth: The Importance of Productivity-Enhancing Reforms in Emerging Market and Developing Economies," IMF Staff Discussion Note, December 2013, p. 23.

Mauritius: The Path to a Middle-Income Diversified Economy

In the early 1960s, Mauritius faced bleak economic prospects as a low-income, agriculturally based economy with a rapidly growing population. The government undertook a pragmatic strategy of policy liberalization to develop the country's comparative and competitive advantages. A key trigger was the passage of the Mauritian EPZ law in 1971.²³ This law provided trade and investment incentives, essentially acting as a geographically limited exception to the nation's import substitution policies. The reform achieved the goals of employment creation, export diversification and growth, and eventually attraction of foreign investment. This experience led to continuous gains through further financial and trade liberalization, supported by equitable public investment, and anti-corruption law, and strong and inclusive institutions.

Peru: Reversing Decline with a Comprehensive Package of Reforms

Peru represents a case of a continuous wave of structural reforms carried out in the 1990s.²⁴ From the mid-1970s until 1990, due to severe swings in policies, Peru's economy was characterized by hyperinflation, boom-bust cycles, a Maoist guerilla insurgency, and negative growth. In the 1990s, a series of reforms turned around the country's poor performance. The reforms began in 1990 with trade liberalization and financial sector reforms. This was followed by a comprehensive suite of reforms covering price controls, obstacles to private investment, the labor market, industry and business markets, and the fiscal structure. These reforms led to the transition from declines in TFP in the 1980s and early 1990s to annual average TFP growth of 2.5 percent—among the highest in the region. TFP growth reversed the declines in average annual GDP; annual GDP growth went from negative 3.8 percent in the 1980s to positive 3.2 percent over 1990-2003 and doubled to reach 6.4 percent during the 2004-2013 period. This case indicates that it is probably easier for an economy to recoup lost economic output after a prolonged collapse than to start from a condition of low growth. It does, however, provide evidence that reform can have a material effect on economic recovery.

Malaysia: Waves of Reform as Part of Broad Economic Transformation²⁵

Malaysia is a case of continuous waves of structural reforms that adjusted the economy to changing circumstances while propelling the country's fundamental economic transformation. Malaysia also highlights the importance of maintaining long-term political stability and sound macroeconomic policies to implementing reforms effectively. The country began in the 1970s with successful reforms to raise productivity and eradicate poverty in the rural sector. Following rapid rises in fiscal deficits and public debt in the early 1980s, Malaysia embarked on a series of traditional structural reforms. The first wave in the mid-1980s to the mid-1990s was devoted to trade reforms, financial liberalization and infrastructure improvements. As a result, fiscal balance was achieved and private investment surged. Strong performance continued until the 1997-98 financial crisis, leading to temporary capital controls, comprehensive financial sector reforms, and an upgrading of regulation and supervision in the financial and corporate sectors. Once again, financial stability was secured, and growth resumed. In 2010 Malaysia

²³ "A Review of the Role and Impact of Export Processing Zones," Dorsati Madani, The World Bank, August 1999.

²⁴ "Structural Reforms and Macroeconomic Performance: Country Cases," International Monetary Fund, November 2015, pp. 17-20.

²⁵ "Structural Reforms and Macroeconomic Performance: Country Cases," International Monetary Fund, November 2015, pp. 13-16.

launched yet another wave of reforms aimed at private sector growth in higher value-added activities, and focused on innovation/technology policies and the quality of education and infrastructure.

To be sure, there are counter examples, because structural reform does not guarantee growth success and can be overtaken by a number of factors such as political crises, commodity price collapses, financial instability or natural disasters. However, the economic histories of these and other nations produce a number of important lessons:

- Political and economic stabilization are critical prerequisites of effective structural reform, since policy change is difficult to attain at the actual moment of crisis. However, the effects of instability have led to the mobilization of support for reforms once some semblance of stability has been attained. In addition, those undertaking reform programs need to monitor stability as efforts are undertaken.
- The specific forms of reforms that have spurred growth path “accelerations” have varied over time and by region. Several East Asian countries successfully adapted their trade and investment regimes to take advantage of global trade expansion in the 1960s and 1970s. China’s entry as a world economic powerhouse began with rural agricultural reform, soon followed by measures to take advantage of the country’s vast labor resources. Latin American nations have more recently reaped growth gains from the reduction of rigidities in financial, product and labor markets.
- Some economists point toward specific “triggering” reform efforts aimed at removing binding constraints to unleash growth. These can be very effective. However actual development histories show that most often, sustained economic growth has resulted from patterns of reinforcing waves of structural reforms, sometimes focusing on additional constraints. Initiatives to identify and address important binding constraints are valuable in their own right, but also give rise to opportunities to achieve additional gains through other structural reforms.
- Structural reform is not a one-time event that sets a nation on a course of unabated, accelerated growth. The experiences of Korea, Taiwan, Malaysia, Mauritius and other countries have shown that domestic and global conditions change continuously and need to be met by evolving and adaptive policy responses.

Effective structural reform programs should incorporate these lessons in order to avoid the problems encountered in the past under “cookie cutter” approaches.

CAVEATS

The preponderance of theoretical, empirical and experiential evidence leads to a compelling case in favor of structural reform to generate accelerated, sustained economic growth. Nevertheless, recent research and analysis has surfaced a number of lessons and caveat that should be taken into consideration in any reform initiative.

- Each country is unique, and so it is inappropriate to apply “one size fits all” reform strategies. Productivity and growth impacts of reforms depend on a range of country-specific economic, policy and institutional settings.

- As noted above, structural reform does not guarantee higher growth, and must be accompanied by identification of comparative and competitive advantages (e.g., market niches) and investments to improve economic resources (e.g., education and infrastructure).
- Structural reforms are difficult to measure in that they involve policies or issues that are not easily quantified.
- Reform programs require sustained commitment by partner countries. Reforms forced upon countries with little ownership of initiatives are likely to fail, such as in the recent case of Greece.
- Reforms can and do exact pain on certain groups. The removal of subsidies and worker protections, tariff reductions, and other changes can create economic hardships on certain workers, the poor, etc. This poses problems in maintaining political stability, and creates the need to acknowledge and address the needs of those affected by transition.
- Timing and sequencing of reforms is essential. Certain reforms can yield minimal results unless appropriate foundation-building changes are made. For example, trade liberalization may not yield gains until business formation and financial policies are improved and infrastructure improvements have been made.
- Strategies need to differentiate between reforms that require gradual implementation versus those that can be subject to “big bang” approaches. Some reforms require extensive institutional capacity building or transition time. Therefore, reform plans need to differentiate between gradual versus rapid implementation of specific policy changes.
- Reform plans must successfully address political economy challenges such as embedded corruption, resistance by powerful interest groups, or regional/national political dynamics.
- Structural reforms do not explicitly address equity, inclusiveness, and environmental sustainability. The potential impacts of policy changes on these goals should be assessed, and if necessary reform plans should include measures to avoid adverse impacts.

These and other complicating factors might lead to the conclusion that crafting and implementing structural reform initiatives is simply too difficult. On the other hand, the established gains from reforms, coupled with the fact that much has been learned from experience, suggests that reform programs are worthy of the effort.

B. SECTORAL IMPACTS FROM STRUCTURAL REFORM

Structural reform initiatives vary substantially, depending on their focus, breadth, timing and other factors. Similarly, the reforms generate distinctive effects on different economic sectors. This section explores major impacts by sector. The reforms and effects shown in the boxes refer to policy changes made within the sector.

TRADE LIBERALIZATION²⁶

TRADE LIBERALIZATION	
Examples of Structural Reform: <ul style="list-style-type: none">• Tariff reduction• Elimination and reduction of non-tariff barriers• Eliminate export taxes/subsidies• Streamline customs procedures and provide trade facilitation	Potential Impacts of Trade: <ul style="list-style-type: none">• Consumer benefits by providing a wider array of competitively priced goods and services• Increased efficiency spurred by competition• Identification of comparative and competitive advantages• Higher productivity growth• Need to address adjustment costs (e.g., initial deficits, displaced labor)

For literally centuries, international trade has been at the center of discourse on structural reform. The very origins of formal economics inquiry revolved around Adam Smith's and David Ricardo's calls to shape policies to take advantage of specialization and comparative advantage through trade.

Theoretical and quantitative research has proven beyond doubt that structural reforms to reduce tariff and nontariff barriers generate increases in trade volumes. Greater exports translate directly into GDP growth, and higher imports confer consumer benefits as well as providing inputs for productive activities which are increasingly important given the global rise of value chains. Through international competition, trade expansion also stimulates economies of scale, technology diffusion and higher productivity, which in turn stimulate overall economic growth. The power of this relationship is captured in the widely used term, the "virtuous cycle of trade and growth."

Economists agree that trade growth, fueled by a series of trade agreements to lower barriers, has powered worldwide economic growth since World War II. Over the 1985-2007 period, the global economy experienced substantial globalization and rapid economic growth. There is a strong consensus among economists that international trade contributed to the rise in overall prosperity, despite the often major adjustment costs faced by workers.²⁷

Since 2012, trade growth has slowed substantially, rising at just over 3 percent annually, less than half the average rate of expansion over the previous three decades. Even more disturbing is the fact that real trade growth, which averaged twice as fast as GDP growth during 1985 to 2007, has barely kept pace with GDP growth over the past four years. The IMF ascribes overall weakness in economic activity, particularly investment, for most of this decline. However, other contributing factors include the waning pace of trade liberalization and a recent rise in protectionism.

²⁶ Trade liberalization is meant to describe more "traditional" issues addressed in trade agreements, including tariff reductions and trade facilitation issues.

²⁷ World Economic Outlook, International Monetary Fund, October 2016, p. 64.

INVESTMENT AND INDUSTRY

INVESTMENT AND INDUSTRY	
Examples of Structural Reform: <ul style="list-style-type: none">• Reduce restrictions on foreign direct investment• Open up previously closed off areas to FDI• Streamline business formation process• Allow market-priced domestic and imported inputs• Simplify corporate taxation• Allow adequate capital repatriation	Potential Impacts on Investment and Industry: <ul style="list-style-type: none">• Higher investment growth• Access to foreign capital, markets and technology• Greater competition and productivity• Job creation

Private investment is both a leading cause and major effect of economic development. Investors continuously seek opportunities to generate income, and investments create products, exports and jobs. Entrepreneurs desire a minimum of restrictions on their activities and a “market friendly” business environment. Governments thus need to find an appropriate balance between market freedom and legitimate regulations to protect workers, consumers, the environment, etc. They must also channel human endeavors into productive pursuits through laws and culture. Governments also need to protect economies from monopoly practices and corruption.

In practice, structural reform has often focused on removing or reducing excessive restrictions associated with doing business. The areas of reform cover the entire business value chain: Registration/incorporation, labor hiring/firing, trade policies affecting equipment acquisition and sales, intellectual and other property protection, taxes, capital repatriation, etc.

Domestic private investment is critical to economic growth. Foreign direct investment (FDI) is also very important, because it brings not only capital and management expertise, but often also new technologies and access to foreign markets. FDI is attracted to countries with market-friendly policies. For example, researchers at the Institute for the Study of Labor in Bonn constructed a detailed data set on structural reform for 19 Latin American and 25 transitioning Eastern Europe nations, and analyzed their effects on foreign investment. Their main finding was the robust empirical relationship between structural reforms and FDI.²⁸ The effects of financial sector reforms and privatization were stronger than those of trade liberalization. Interestingly, the impacts of reform *efforts* were more powerful than those of reform *outcomes*. This implies that foreign investors are very receptive to the reform motivations of host countries. It helps explain the initial takeoff of investment and growth in India as a result of a shift toward pro-business attitudes rather than actual policy reforms, and the growth spurt in China following changes in agricultural policies and land use.

²⁸ “Foreign Direct Investment and Structural Reforms: Evidence from Eastern Europe and Latin America,” Nauro Campos and Yuko Kinoshita, IZA Discussion Paper No. 33332, February 2008.

AGRICULTURE

AGRICULTURE	
Examples of Structural Reform: <ul style="list-style-type: none">• Codify appropriate land rights/use laws• Permit private sales of output• Reduce/remove commodity price ceilings• Reduce/remove credit ceilings• Reduce restrictions on imported inputs• Assist provision of extension services• Reduce/remove export restrictions• Reform public procurement systems• Apply competition policy to cartels and closed industries	Potential Impacts on Agriculture: <ul style="list-style-type: none">• Improved land use patterns• Increased production• Higher productivity growth• Reduced food deficits/potential surplus• Greater agricultural exports and imports• Release of labor to industrial or service sectors• Stronger and more efficient global value chains• Enhanced food security

Agriculture is critical to most developing countries for both economic growth and food security objectives. It is especially so for those countries which have not yet established significant manufacturing or service sectors. Agricultural output not only feeds domestic populations, but also provides needed export earnings for many countries. Reform of agricultural policies has been proven to generate significant increases in agricultural productivity. The removal of commodity price ceilings, mandated government purchasing, credit constraints and restrictions on imported inputs stimulates agricultural efficiency. The resulting rise in productivity potentially offers greater employment opportunities by creating demand for skilled workers in higher value agricultural products, and also by releasing surplus labor to enter growing manufacturing or service sectors. Agricultural reform was the key initiator of China's accelerated growth path.

General structural reform also spurs agricultural export **and import** expansion, with important positive effects on food security. An empirical study found that reforms in three areas – finance, trade and agriculture – yield increases in agricultural exports.²⁹ Desirable improvements include reduced tariff rates, fewer restrictive credit constraints, and fewer government interventions, providing a solid policy foundation for pursuing structural reforms to generate trade and economic growth.

²⁹ “Structural Reforms and Agricultural Performance: An Empirical Analysis,” Dwi Susanto, C. Parr Rosson, and Rafael Costa, Paper prepared for the Southern Agricultural Economics Association Annual Meeting, February 4-7, 2012.

LABOR, JOBS, AND COLLECTIVE BARGAINING

LABOR	
Examples of Structural Reform: <ul style="list-style-type: none">• Ease hiring/firing restrictions• Open up closed professions³⁰• Introduce effective retraining programs• Provide protections for displaced workers• Allow use of alternative dispute resolution instead of court systems to settle individual and collective labor disputes• Allow collective bargaining• Improve educational systems, including vocational education• Introduce workforce development programs that respond to needs of employers	Potential Impacts on Labor: <ul style="list-style-type: none">• Greater labor market flexibility• Displaced workers• Enhanced competition and wages for qualified workers• Increased (long-term) job opportunities

The impact of structural reform on labor remains highly contentious and politically charged, for essentially two reasons. First, there is a widely held belief that reforms which aim at reducing restrictions to the free movement of goods, services and factors of production have the potential effects of destroying jobs, increasing inequality, enriching the already rich, and not doing much for the poor.³¹ Plant closings resulting from trade liberalization are highly visible and politicized. Second, over the years many governments have installed and maintained strict labor laws to protect workers from unscrupulous management practices. The cumulative effect of these laws has been rigid labor markets due to difficulties such as in hiring and firing employees. Attempts to amend labor laws to free up labor markets have typically met with severe political opposition.

To be sure, the economics profession has failed to give sufficient attention to the plight of workers displaced by structural reforms. Economic models focus on consumer and productivity gains which lead to more rapid growth, but these models generally assume that laid-off workers will find opportunities in growing regions and industries. Adjustment assistance programs, when they exist, are typically insufficient to address the age, lack of mobility and limited educational levels of certain displaced workers. The result has been major backlashes against reforms in developing and industrialized countries alike.

At the macroeconomic level, structural reforms can in fact lead to positive outcomes for labor.³² Changes which raise levels of productivity, consumption and consequently economic growth generate job opportunities, real wage increases and incentives for informal sector workers to enter the formal labor force. IMF economists stated that “In the current environment of persistent weak economic

³⁰ Closed professions are also called “closed shop” professions. The use of taxi medallions in Manhattan, limiting possibilities for entry into the lucrative taxi market, is an example.

³¹ “Structural Reforms and Labor Market Outcomes: International Panel Data Evidence,” Policy Research Working Paper 7122, World Bank Group, November 2014, p.21.

³² *Ibid.*, pp. 20-21.

activity in many advanced economies, there is a strong case for product and labour market reforms, complemented by macroeconomic policy support, to boost jobs and growth.”³³

Pro-labor groups have noted that structural reforms in labor markets have resulted in weakened and more fragmented collective bargaining in many countries.³⁴ While collective bargaining has been a cornerstone of the labor movement for many decades, linkages between collective bargaining strength and long-term employment outcomes have not been determined sufficiently.

A study by the Secretariat of the International Labor Organization (ILO) notes that overall, economists have failed to reach a consensus on the potential for structural deregulation to improve employment performance.³⁵ Some argue that regulations support fair employment conditions, and others see regulations as an obstacle to employment growth. In developing countries, the policy debate focuses on labor market flexibility and not on worker security, and the ILO supports a more balanced approach, sometimes dubbed “flexicurity” in Europe. Similarly, the structural reform approaches being developed by the IMF and World Bank place much greater attention on the issue of worker security. One way proposed to deal with this is to frame reform initiatives as shifting from job protection to worker protection. Another concern in advanced economies is the fact that automation and innovations such as e-commerce can adversely affect wage growth and employment in low-skill job categories.

FINANCIAL AND CAPITAL MARKETS

FINANCIAL AND CAPITAL MARKETS	
Examples of Structural Reform: <ul style="list-style-type: none"> • Remove interest rate ceilings/floors • Reduce/remove credit controls³⁶ • Improve banking supervision • Ensure market driven exchange rate • Introduce capital market instruments • Minimize government-mandated lending allocations 	Potential Impacts on Financial and Capital Markets: <ul style="list-style-type: none"> • Improved capital/credit distribution • More efficient financial intermediation • Greater participation and capital formation • Improved access to capital and credit • Higher efficiency/productivity in user industries

Financial markets are the mirror image of real product markets and are indispensable to production and commerce. Efficiently operating financial and capital markets supply the resources needed to support transactions and investments. Alternatively, financial markets repressed by credit controls, excessively

³³ “IMF calls for labour market reform to boost jobs,” The Guardian, April 6, 2016.

³⁴ “Structural Labour Market Reforms and the Collective Bargaining Landscape in Europe,” Social Europe, April 26, 2016.

³⁵ “What role for labour market policies and institutions in development?” Sandrine Cazes and Sher Verick, Employment Working Paper No. 67, International Labour Office, 2010, p.2.

³⁶ In the wake of the financial crisis and lessons learned from the financial contagion that affected emerging and developed economies that were fully integrated in the international financial system, experts at the IMF and other institutions are re-evaluating the conventional wisdom on capital controls. Some experts see targeted capital controls as a tool to protect developing countries from potentially destabilizing capital flows and spillover effects in times of global instability. “The Financial and Economic Crisis of 2008-2009 and Developing Countries,” United Nations Conference on Trade and Development, December 2010. “Capital Inflows: The Role of Controls,” Ostry et. al., IMF Staff Position Note, February 2010.

high (or low) interest rates, over valued exchange rates and government-administered lending allocations, stifle economic activity and growth.

A large body of analytical work has found that financial sector reforms have myriad positive effects because they can lead to the more efficient allocation of resources.³⁷ As a result, structural reform efforts have devoted considerable attention to efforts to improve financial sectors. IMF economists have determined that reforms in banking systems, credit controls and banking supervision produce strong productivity gains in low income developing countries.³⁸

INFRASTRUCTURE

INFRASTRUCTURE	
Examples of Structural Reform: <ul style="list-style-type: none"> • Create fiscal space for investment • Effectively plan and execute investments • Establish market prices • Privatize infrastructure where feasible • Provide for recurrent/upkeep expenses 	Potential Impacts on Infrastructure: <ul style="list-style-type: none"> • Enhanced access • Improved services • Reduced expenditures on subsidies • Inclusive networks of infrastructure services • Greater ability to maintain/upgrade services

As a key part of physical capital, infrastructure is critical to sustainable long-term development. Extending beyond roads, bridges, ports and other transportation facilities, infrastructure also includes water, sewerage, power and telecommunications. The quality and extent of its infrastructure dramatically affects a nation’s ability to produce and move goods and services, hence its productivity and competitiveness. Governments and private sectors alike admit there is a woeful underinvestment in infrastructure, with deficits not only in sub-Saharan Africa, but also in Asia, Latin America and even countries in the industrialized world.³⁹

Effective infrastructure systems are both the result and a major cause of economic growth. Without growth, nations cannot generate the “fiscal space” or wherewithal to invest in infrastructure. At the same time, inadequate or aging infrastructure acts as a drag on competitiveness and growth. A number of countries face situations in which state-owned enterprises in infrastructure are maintained for patronage purposes. These enterprises are not operated to provide services efficiently or to maximize returns, and the SOEs may block new entrants offering more efficient business models.

Well-designed policy and institutional structures play a decisive role in infrastructure development. Fiscal systems that create fiscal space (surpluses) and promote intelligent investments are key. In addition, an appropriate mix of public/private ownership and service delivery is needed to ensure efficiency, and may require full or partial privatization in many countries. Finally, market-oriented pricing structures are necessary to achieve cost recovery, avoid over- or under-consumption and generate funds for maintenance and future investments. Many nations tend to apply subsidies to water and power while at the same time charging excessive prices on telecommunications.

³⁷ “Structural Reforms and Macroeconomic Performance: Initial Considerations for the Fund,” IMF Policy Paper, November 2015, p. 14.

³⁸ Ibid., p. 31.

³⁹ “A Needed G-20 Consensus: A New Structural Reform Agenda for Developing Countries,” Beyond Macroeconomic Policy Coordination in the G-20, The Brookings Institution, November 1, 2011.

THE LEGAL SYSTEM

THE LEGAL SYSTEM	
<p>Examples of Structural Reform:</p> <ul style="list-style-type: none"> • Promote regulatory impact analysis to ensure new laws are efficient • Provide for notice and comment (good regulatory practices) • Examine impacts of laws on competition (e.g., by applying the OECD Competition Assessment Toolkit)⁴⁰ • Replace counterproductive laws • Improve efficiency and economic understanding of judges who enforce laws • Improve standing in World Bank Ease of Doing Business surveys • Ensure fair and effective implementation • Streamline permitting systems • Adopt secured lending and bankruptcy laws 	<p>Potential Impacts on The Legal System:</p> <ul style="list-style-type: none"> • Greater and more equitable justice • Clarity, transparency and certainty for economic actors • Improved efficiency in adjudication • Reduced corruption

Legal systems are at the core of the structure of every economy, since the policies and regulations governing economic transactions are-or at least should be-based on laws.

Effective legal/justice systems are a prerequisite for investment and business friendly environments by instilling confidence throughout economies.⁴¹ Experience has shown that in many countries, poor economic performance is found to be rooted in legal and administrative practices (e.g., land tenure systems, lack of arbitration rules or IPR infringement adjudication) as much as on what are traditionally considered economic policies. As a result, true structural reform consists of addressing policy change and legal change simultaneously. Each policy change needs to incorporate a strong and clear legal component governing implementation

FIGURE 2. LEGAL AND REGULATORY SYSTEMS RELATED TO STRUCTURAL REFORM



⁴⁰ The OECD Competition Assessment Toolkit helps eliminate barriers to competition by providing a method for identifying unnecessary restraints on market activities. See <http://www.oecd.org/competition/assessment-toolkit.htm>.

⁴¹ "Effective Justice Systems," European Community Europa 2020, April 21, 2016, p. 1.

and enforcement. At the same time, legal changes need to acknowledge and even foresee their impacts on policies and on economic performance.

As shown in Figure 2, legal systems cover most if not all business and economic processes such as trade, investment, and commerce. A number of well-known legal areas are grouped around property rights, business law, contracts, and commercial dispute resolution. They also govern other areas not shown, such as labor and financial practices. For these laws to function effectively, they must instill investor confidence by being pro-competitive, efficient, and just.

Transparency and predictability, as well as reasonable legal control over economic processes are critical requisites for sustained growth and development. Many of the key characteristics of “good governance” relate directly to both the laws on the books and the institutional structures for enforcing laws.

Legal reform should be an integral part of overall structural reform. Designing and implementing reforms should be based on a careful balancing of competing interests. In addition to formulating effective laws, governments need to ensure that laws are not implemented arbitrarily. Considerable attention in structural reform initiatives is often devoted to enforcement and elimination of corrupt practices.

INNOVATION AND INTELLECTUAL PROPERTY RIGHTS

INNOVATION AND INTELLECTUAL PROPERTY RIGHTS	
<p>Examples of Structural Reform:</p> <ul style="list-style-type: none"> • Enact best-practice IPR laws in areas of trademark, copyright and patents • Establish/maintain effective enforcement • Aggressively prosecute IPR violations • Adopt appropriate R&D incentives • Support innovation infrastructure efforts 	<p>Potential Impacts on Innovation and Intellectual Property Rights:</p> <ul style="list-style-type: none"> • Greater domestic innovation • Stimulated branding of local products, thus promoting higher quality and popularity • Higher foreign investment, access to international technology • Growth in innovation-driven productivity

Regulatory reform is a powerful stimulus to innovation.⁴² Reforms that enhance competition have been critical to the diffusion of technologies in both the manufacturing and service sectors. Administrative reforms reduce the cumulative burden on businesses, freeing up resources for research and technology development. According to a 1994 survey of over 2,500 European companies, firms indicated that regulations make it more difficult to minimize costs, organize in a flexible way, reduce time to market and reduce uncertainty.

Rules to protect intellectual property rights (IPR), or “appropriability conditions,” are embedded in patents, copyrights, trademarks, etc., and are among the key drivers of technological advance. IPR policies need to maintain a correct balance between rewarding inventors by limiting the appropriability of inventions and increasing returns on R&D, on the one hand, and promoting economic and social interests by allowing some use of inventions and enhancing technology diffusion on the other. In many developing countries, IPR laws or enforcement are lax, thus permitting undesirable levels of product piracy or technology theft. This in turn deters innovative firms from participating in those economies, which clearly dampens innovation and growth.

⁴² “Regulatory Reform and Innovation,” OECD, undated, p. 7.

Establishing effective IPR protection systems is a complex process. While model laws are available, in any specific country legislators must not only overcome opposition from vested interests, but also adapt the reforms to fit their nation’s overall legal system. Enforcement and adjudication systems require resources, training and anti-corruption mechanisms. The introduction of operable IPR protection systems do not generally generate near-term benefits, but ultimately provide a solid platform for national innovation.

THE FISCAL SYSTEM

THE FISCAL SYSTEM	
Examples of Structural Reform: <ul style="list-style-type: none"> • Rationalize tax structure • Reform tax collection institutions/processes • Utilize technology/training to ensure wider taxpayer compliance and reduce corruption • Adopt effective budgeting systems • Maximize growth-oriented budget allocations 	Potential Impacts on The Fiscal System: <ul style="list-style-type: none"> • Improved tax collection and more “fiscal space” • Greater domestic resource mobilization • Enhanced efficiency • Improved equity • Greater fiscal stability and resilience to shocks • Greater ability to self-finance development

Fiscal policies and performance are central to sustainable growth and development. Typical challenges to developing countries are inadequacies in fiscal systems’ ability to mobilize sufficient domestic resources for social and economic programs, excessive reliance on indirect taxes (e.g., tariffs, sales taxes) that create structural distortions, and/or government budget outlays that are biased toward subsidies to the detriment of appropriate investments in infrastructure, education, etc.

While structural adjustment programs tend to focus on various forms of “belt tightening” to achieve fiscal balance in the near- or medium-term, structural reform initiatives seek to address fundamental fiscal system issues.⁴³ In the realm of tax policy, direct taxation on income and property is less regressive, exerting less of a burden on the poor. Improvements in revenue system administration through technology, training and anti-corruption activities can mobilize more domestic resources. Government budget reforms can realign spending toward more effective delivery of public services.

PRIVATIZATION OF STATE-OWNED ENTERPRISES

PRIVATIZATION & SOES	
Examples of Structural Reform: <ul style="list-style-type: none"> • Honestly review SOE performance • Identify SOE candidates for sale • Establish legal framework for privatization • Conduct legitimate enterprise sales • Provide effective regulation of private firms • Separate SOE ownership from regulating agencies 	Potential Impacts on Privatization: <ul style="list-style-type: none"> • More domestic support for privatization • Government revenues from initial sales • Reduced costs for SOE subsidies • Greater efficiency in privatized companies • Ongoing tax revenues from private firms • Enhanced access to finance for investment

Privatization is not so much a “sector” as it is a potentially effective element of structural reform. There is a consensus among economists on the fact that overall, private enterprises operate more efficiently

⁴³ See the Declaration of the Addis Tax Initiative of the Financing for Development Conference (July 2015).

than state-owned enterprises (SOEs). To be sure, some government enterprises such as those which provide public services operate effectively. In addition, private firms are capable of excessive practices (e.g., exploitation of labor and the environment, monopolistic behavior, etc.). However, experience has shown that an appropriately regulated private sector is more productive and capable of generating long term growth than state-owned companies.

Conflicts of interest arise when a government regulator manages an SOE. The regulator may promulgate rules that stifle competition by private sector providers in order to maintain the viability and profitability of the SOE. Many SOEs get captured and operate for the benefit of their employees, who in some countries are major recipients of patronage by government leaders.

Privatization also creates incentives for positive returns on investment. SOE energy operators in many developing countries function at a loss because tariffs are set too low to please consumers/voters. The transfer of government enterprises to the private sector, if conducted carefully, can not only generate income from the initial sale, but also long-term revenue streams through taxation. More importantly, firms operating under market principles face much higher odds for being efficient, sustainable, and capable of creating surpluses for new investment.

C. POTENTIAL SOCIAL DEVELOPMENT IMPACTS

Structural reform efforts are primarily directed at economic objectives, specifically to lift productivity and economic growth, rather than at social goals. However, reforms can exert impacts on social development, both positive and negative. There is no guarantee that policy changes will positively affect social outcomes. However, if crafted carefully, policy changes can contribute to socially desirable trends.

OVERALL SOCIAL DEVELOPMENT

If successful, structural reform accelerates economic growth, and this provides the basic wherewithal to support social development performance. A nation's ability to feed the poor, provide adequate health services, and educate the population requires resources in the form of output and income.

EQUITY

Economic history indicates that traditionally, economic development often led to periods of increasing inequity before countries achieved improved equity. More recent experience has proven that attaining equity can be built into reform plans. In Taiwan, for example, the government's "land to the tiller program" and other policies dramatically reduced Taiwan's Gini Coefficient,⁴⁴ a measure which calculates income inequality, from 0.558 in 1953 to only 0.303 in 1980, proving that progress toward narrowing the income gap can be made while at the same time undergoing rapid economic growth.

Fiscal reforms that shift the burden from consumption taxes to income taxes can be progressive. Similarly, trade reforms which reduce tariffs on common consumer goods more than on luxury goods improve equity. To be sure, some policy changes such as lowering subsidies on basic goods can

⁴⁴ The Gini Coefficient is a mathematical measurement of a country's income distribution. The coefficient ranges between 0 and 1, with 0 representing perfect equality, and 1 representing perfect inequality. Therefore, a fall in the coefficient value represents the movement toward greater income equality. The world Gini Coefficient for 2016 was 0.52.

adversely affect the poor, and so implementation should include adequate safeguards, creation of targeted needs tested programs, and transition time to minimize these impacts.

EDUCATION

A rich body of literature proves the importance of educational attainment to stronger economic performance. A key goal of structural reform is to shift government budget spending from subsidies and other consumption items to investments in education, health care and infrastructure. Studies have shown that developing countries at lower income levels should invest more in primary education, whereas those at middle income levels should focus more on secondary and tertiary education.

HEALTH CARE

Access to basic health care is increasingly viewed not only as important in its own right, but also as a determinant of worker productivity. At the same time, the provision of health services is ultimately dependent on a society's ability to generate income. Therefore, better health outcomes are both a cause and an effect of economic growth. Economic policy reforms that accelerate growth can provide more "budget space" for health services, and increasing the priority placed on health in current government budgets can lead to improved health outcomes. Also, improved health outcomes in the near term lead to lower healthcare requirements and outlays in future years.

GENDER EQUALITY

Donors are placing greater emphasis on advancing women's economic empowerment. Research has shown that lack of women's economic empowerment limits the full growth potential of countries, and also leads to less favorable education and health outcomes for children. A recent World Bank report focused on four priority policy areas: reducing excess female mortality and closing education gaps, improving women's access to economic opportunities, raising women's voice in the household and in society, and limiting the perpetuation of gender inequality across generations.⁴⁵ Specific reforms could include reducing discrimination against women in the marketplace (e.g., owning property, accessing finance, etc.), and ensuring equal educational opportunities for women.

INCLUSIVE GROWTH AND SOCIAL PROTECTION

As noted above, certain structural reforms such as tax increases or energy price rises can adversely affect the poor and vulnerable in the short run. However, the World Bank and other donors are focusing on strengthening social safety nets, social inclusion and targeting resources on the most vulnerable groups.⁴⁶ Examples of social protection actions include temporary unemployment insurance and/or retraining programs for workers displaced by trade reforms, or food or energy vouchers for targeted impoverished groups affected by price increases for basic commodities.

⁴⁵ World Development Report 2012: Gender Equality and Development, The World Bank, 2012.

⁴⁶ "World Bank's Experience with Structural Reforms for Growth and Development," World Bank Discussion Paper No. 11, May 2016, pp. 11-12.

FINANCIAL INCLUSION

Structural reform initiatives often target an easing of financial repression, which can preclude the poor, women, other vulnerable groups and small businesses from accessing money and credit. Experience has shown that removing policy-induced credit restrictions, along with programs to extend micro and small business lending through modern secured lending laws,⁴⁷ can help unleash entrepreneurship and generate new sources of economic expansion.

ENVIRONMENTAL SUSTAINABILITY

Achieving acceptable environmental standards is deemed by many in developing countries as a luxury activity limited to rich nations. Unfettered growth of economic activities spawned by structural reforms can lead to air, water and land despoliation. Remediation can be much more expensive than mitigation of pollution. Donors are placing a higher priority on policy and institutional reforms aimed at environmental sustainability, in areas such as improved natural resource and environmental management, and green growth.⁴⁸

D. CHALLENGES AND BARRIERS AT THE COUNTRY AND REGIONAL LEVELS

Modifying economic policies is hard under any circumstances. Change requires altering perceptions, behavior, and expectations about future outcomes, and this is always difficult. Research has shown that structural reform is easiest to undertake during periods of economic crisis or downturns, since constituencies can be convinced that change is necessary. (The World Bank's Doing Business unit notes that most reforms occur in the first year of a new administration.) This is not the case when economic performance is strong or at least stable. It explains why the most prominent waves of structural reform have taken place either during or immediately after episodes of severe economic stress.

Another fundamental deterrent to reform is that while appropriate policy changes are likely to generate productivity gains and growth, it takes time for these results to occur. In the interim period, reforms can engender costs – to workers, consumers, industries and even entire economies – comparable to the side effects created by medicines. Those bearing near-term costs, even though they will benefit in the long run, may either (1) resist the policy changes, or (2) be neglected or not receive sufficient transition support. For example, the inadequacy of adjustment assistance programs attached to previous trade agreements has fueled the widespread opposition to freer trade, since displaced workers have been unable to shift to dynamic industries.

Regional dynamics affect reform patterns, since countries often experience economic conditions comparable to their regional neighbors, and since countries seek competitive advantages over their neighbors. The Central and Eastern European region, for example, witnessed a massive round of structural reform in the late 1990s as nations rushed to adopt market systems. Similarly, many Latin American nations undertook changes in the wake of the financial crisis of the early 1990s, and currently there is little appetite for further reforms. It has been suggested that a key reason for current resistance

⁴⁷ Laws modeled on the Model Law for Secured Transactions produced by the United Nations Commission on International Trade Law (UNCITRAL).

⁴⁸ Ibid. p. 12.

in Latin America was the lack of sufficient means for those in lower income groups to improve their lives, despite bearing the costs associated with reforms.

A considerable amount of change took place in the early 2000s in the Middle East until recent instabilities and conflict associated with the Arab Spring seized the region. In Africa, structural reform is taking place in only a limited way. Several reasons are cited, including volatility and lack of political will in many countries, lack of donor resources, complex regional unions, and a concentration of focus on meeting basic needs.

At present, the most eclectic and dynamic region is Asia, which is vast and comprises several groupings. The nations of East and Southeast Asia are economically aggressive and competitive with their neighbors, and so are much more willing to adopt “best practice” policies. Dynamic regional organizations like the Association of South East Asian Nations (ASEAN) and the Asia Pacific Economic Cooperation forum (APEC) promote the utility of structural reforms among members. On the other hand, countries in Central and South Asia are more traditional and cautious, placing a higher priority on maintaining stability based on the status quo. Within Asia, as in other regions, major changes in government can either open or close “windows of opportunity” for structural reform.

Beyond overall barriers and those posed by regional dynamics, each country faces a specific set of obstacles that must be overcome to achieve successful policy change. A set of important hurdles is presented in the following text box, which covers, respectively, technical and political-economic challenges.

OVERCOMING CHALLENGES TO STRUCTURAL REFORM

Technical	Political-Economic
<p>A number of impediments are technical in nature, and surmounting them requires sound analysis, planning, and execution.</p> <ul style="list-style-type: none"> • Diagnosing the economy. The first step to crafting a successful reform strategy is to develop an accurate diagnosis of the economy, including an honest assessment of its strengths, weaknesses and opportunities. A faulty diagnosis can thwart both current and future attempts to improve policies. • Identifying appropriate reforms. Governments establish an enormous array of policies affecting economic processes. Selecting target areas and specifying necessary changes requires considerable acumen. • Grouping and pacing reforms. Experience has shown that effectively combining reform packages and timing their implementation materially raises the prospects for improved outcomes. • Executing reform plans. Beyond planning, carrying out policy changes involves a wide range of actors and actions – legislative, legal and judicial, educational, institutional, etc. 	<p>Most economists concentrate on technical policy issues, often neglecting critical barriers associated with political processes, the power of key constituencies, corruption and other barriers that can act as binding constraints to reform.</p> <ul style="list-style-type: none"> • Creating an effective rationale for reform. Crafting a compelling call to action, supported by strong and clear arguments, is vital to alter attitudes and convince skeptical constituencies. • Building a critical mass of political will. Many government leaders have been convinced of the need for policy change, only to find they are unable to establish sufficient commitment by reluctant legislatures or bureaucracies. • Identifying and addressing sources of opposition. Any prospective policy change gives rise to opponents, and so a key element to any reform strategy should be to recognize sources of resistance and to deal with them effectively. Systemic corruption is often a prominent challenge to policy improvement. • Sustaining momentum. Nations which have been successful at transforming their economies have been relentless in monitoring change, honestly reporting successful results and shortcomings, and taking steps to energize reform constituencies continuously. • Culture Trap: Economies may enter into a less than optimal equilibrium, trapping it in a crippled situation. For example, Brazil's heavy regulation, social protections, and high tariffs allow informal SMEs to flourish as they can evade many of the costs of regulation. This impedes productivity improvements, however, as large firms of scale production must bear those extra costs.

III. USAID STRUCTURAL REFORM EFFORTS – PAST AND PRESENT

The United States engaged in structural reform activities even before USAID was created as an agency in 1961. As noted above, policy change was an integral part of the Marshall Plan. The United States also aided Taiwan and South Korea in reforms in the early 1960s.

USAID has sponsored numerous projects and programs at both the Bureau and Mission levels that encompassed structural reform, even though these activities were not carried out under the explicit rubric of structural reform. These have included:

- Fiscal system restructuring
- Export development
- Domestic and foreign investment stimulation
- Financial market development
- Tax reform
- Customs reform
- Trade policy restructuring
- Labor market transformation
- Intellectual property policy reform
- Business registration and permitting
- Competition policy reform
- Property rights, including land tenure

The specific focus and priorities placed on these efforts have evolved over time. However, with support from Central and Regional Bureaus, USAID Missions have consistently stood ready to support partner country efforts to improve their policy and institutional frameworks.

USAID became directly involved in structural reform initiatives in the 1980s under the influence of President Ronald Reagan's private enterprise development thrust. This included numerous projects to assist partner countries to stimulate free market economies. Specific activities were designed to promote inflows of foreign investment, reform capital markets, and take advantage of trade opportunities offered by the Generalized System of Preferences (GSP) and the Caribbean Basin Initiative (CBI).

In the 1990s and early 2000s, USAID accelerated work in this field with the passage of the SEED and Freedom Support Acts, which focused on transforming the countries of Europe and Eurasia into market economies. Developing countries received integrated packages of assistance, including programs supporting structural reforms. Transitioning countries were offered technical and financial help to adopt market-oriented economic systems. Among other initiatives, USAID established centrally funded projects to help nations upgrade their financial markets and commercial policies.

USAID continues to sponsor a range of efforts in the field of structural reform under a variety of names on an ad hoc basis. The following sections summarize some of the major efforts sponsored by central bureaus as well as within USAID's regions.

A. USAID/WASHINGTON INITIATIVES

As noted previously, USAID missions and bureaus have conducted structural reform initiatives throughout its existence. Over the past 10-15 years, USAID has developed or supported a number of tools to diagnose and identify reforms in policies, implementing regulations, institutions, and other areas that could facilitate improvements in the **Business Enabling Environment (BEE)** generally or for specific value chains. These tools include:

- **Commercial, Legal and Institutional Reform (CLIR) and BizCLIR** (its successor), which has been used extensively to identify policy constraints to business growth and entrepreneurship.
- **AgCLIR** and other variants (MicroCLIR, HealthCLIR, GenderCLIR), which assess micro-level policy impediments to important value chains such as agriculture and health or populations.
- **Competitiveness Impacts of Business Environment Reforms (CIBER)** to engage value chain participants to identify constraints to competitiveness, quantify costs and benefits of reforms, and develop advocacy plans for achieving reform.

Currently, USAID carries out a number of activities that relate to but are not formally under the name of structural reform. Most of these are located in the Agency's Bureau of Economic Growth, Education, and Environment (E3).

The **Inclusive Growth Diagnostic (IGD) by the Economic Policy Office** is a tool that relies on the systematic investigation of a country's economic conditions to identify and prioritize specific constraints to investment and growth. This approach is built on the assertion by economist Dani Rodrik and others that addressing specific "binding constraints" in a country is preferable to a more generic reform strategy. The IGD tool application is sponsored by the E3 Office of Economic Policy (E3/EP). Since 2010, 24 Inclusive Growth Diagnostic assessments have been completed at Mission request, and two additional studies are now under way. The IGDs include a productive space analysis and a competitiveness analysis. Sponsors feel that IGD applications can be effective when sufficient resources are available, and success depends on host country political situations and continuing levels of support.

Trade Capacity Building (TCB) is a set of activities to help partner countries to reform their trading systems and build their capacity to participate in international trade. TCB is overseen by the Office of Trade and Regulatory Reform (E3/TRR). E3/TRR maintains a database of U.S. Government trade activities and provides technical assistance to USAID missions. Since 2001, USAID has provided more than \$6 billion of TCB assistance to more than 110 countries. Technical assistance activities include many of the areas central to structural reform – eliminating subsidies, promoting technology transfer, developing a competitive workforce, encouraging trade finance through a well-developed financial sector, and promoting sound policies related to fiscal and monetary issues, anti-monopoly and commercial codes. USAID's Trade Capacity Building Policy, as of September 2016, is available at: <https://www.usaid.gov/documents/1865/policy-trade-capacity-building>.

Domestic Resource Mobilization (DRM) is a program to support the process in which countries transparently raise and spend their own (rather than donor) funds to provide for their people. DRM aims to achieve improvements in tax compliance and revenues through enhanced audits and simplified filing processes. DRM as well as **Public Financial Management (PFM)** are deemed critical in ensuring the sustainability of development gains. DRM programs are considered extremely cost-effective, often attaining revenues at a ratio of 20/1 for every assistance dollar invested.

The **Land and Urban Office (LU)** within USAID's E3 Bureau works to clarify and strengthen the land tenure and property rights of all members of society, as well as to ensure that land and urban governance systems are effective and accessible. The office works to enhance community and local government capacity, promotes effective land governance systems, and creates opportunities for investments to increase inclusive growth. The program has secured the land rights of 182 million people since 2013 through new laws and policies.

Cost-Benefit Analysis (CBA) is employed to determine the key variables that are likely to determine projects' success, calculate the net impacts of projects, and project whether projects can be sustainable upon completion of interventions. While CBA focuses on project-level microeconomic factors, analyses do take into consideration a range of policy issues such as taxes, subsidies, exchange rates and credit costs. Since 2010 USAID has applied CBA to over 60 projects in 34 countries in the agriculture, power, water, roads, and global climate change sectors.

In addition to tools and activities directed toward macroeconomic policies (in this case meaning all economic sectors), USAID addresses structural reform in specific sectors, particularly energy/power and food.

- **The Office of Energy & Infrastructure Programs** and the **Office of Global Climate Change** of the E3 Bureau collaborate closely to assist countries to create **energy and power sectors** which are sustainable and contribute to long-term growth. Key goals include utilizing all energy resources effectively, scaling up renewables, and adopting market prices and structures. They sponsor rigorous assessments of partner countries' entire energy sector value chains, from fuel to generation, procurement/transmission, distribution and consumption. The methodology identifies barriers, reform steps and achievements made over time. Examples of sector reform studies include Haiti, Jordan, Egypt, Saudi Arabia, Turkey, Qatar and United Arab Emirates.
- **The Bureau for Food Security** similarly applies a systemic approach to assisting partners to develop their **food sectors**. Initiatives often begin with the specification of the "system architecture," which spell out food systems in their entirety, including both policy and business factors. Assessments to identify blockages and determine strategies to address them have been conducted in 42 countries. Importantly, participation includes a requirement to report annually on progress made on strategy implementation.
- **The Development Credit Authority (DCA)**, through the use of partial credit guarantees, fosters innovation to mobilize local financing in developing countries. Guarantee agreements encourage private lenders to extend financing to small and medium-sized enterprises (SMEs) with less access to formal credit facilities. From 1999 through 2016, the DCA portfolio made \$4.8 billion in credit available in 76 countries.
- **The USAID Global Development Lab** seeks to increase the application of technological innovation to accelerate the Agency's development impact. The Lab serves as a central hub for shared learning on science, technology, innovation and partnerships. The Lab applies a number of innovative approaches to a wide range of issues such as digital payments, mobile banking, higher education solutions, entrepreneurship strengthening, and Ebola recovery.

B. SIGNIFICANT REGIONAL INITIATIVES

USAID's regional bureaus have traditionally supported structural reform efforts throughout their regions. Levels of activity have varied over time due to changing circumstances, host country interest

and commitment, and resource availability. The regions display significant differences among each other and within each region itself. All structural reform activities are demand driven in that they are requested and carried out by individual missions.

The **Bureau for Asia** has promoted considerable structural reform initiatives over the years. Asian countries tend to be receptive to reform activities for several reasons, including competition among each other, concerns over the regional economic power of China, and fear of potential political instability ignited by lack of economic progress. Reform activities tend to be clustered in Southeast Asia, where the role of the ASEAN community eases engagement with individual host countries. Reform efforts are less pronounced in south-central Asia due to different political environments as well as a dearth of economic growth funding, which is now limited only to USAID's Sri Lanka Mission. The Missions and Bureau essentially respond to windows of opportunity, which can open or close due to changes in government.

USAID has supported a number of reform programs in **Vietnam**, starting with the STAR Project, focusing on trade and investment. The Mission has technical assistance projects that contributed to changes in 200 laws removing institutional constraints to trade growth. Similar programs were begun in **Laos** and **Burma**. The Mission in **Sri Lanka** responded to government interest in improving trade and investment policy to enhance the investment enabling environment to stimulate foreign direct investment. Examples include commercial law work and efforts to improve Sri Lanka's standing on the World Bank's Doing Business Indicators.

The **Burma** Mission opened in 2012. While the initial focus was on overall governance, activities included helping the nation amend its foreign and domestic investment law, improve fiscal policy, and establish a unified foreign exchange rate. The Mission also collaborated with the U.S. Treasury Department on developing an effective tax payment unit. Conditions were also right in the **Philippines**, which became a successful **Partnership for Growth (PfG)** partner. A constraints analysis was conducted, concentrating on economic governance and competition policy. This was followed by a technical assistance package that addressed identified constraints in the areas of fiscal reform, anti-corruption, trade, competition policy, and entrepreneurship.

The **Bureau for the Middle East** carried out a range of structural reform efforts in the past, but there has been very little interest among partner countries and hence few reform activities over the last five years. The primary reasons are the urgencies associated with regional conflict and lack of political will. In **Tunisia** there have been some initiatives in the areas of business reform and tax and customs. Some public finance management efforts have taken place in **Libya**. Notwithstanding substantial reform activities in the past, there is limited current interest in structural reform in **Egypt** and **Lebanon**, although the recent election of a new president in Lebanon may change that situation. The Missions in **Iraq** and **Morocco** are currently concentrating on other priorities.

The Middle East Bureau is currently focused on a "bottom up" strategy promoting private sector-led job creation. Rather than attempting to identify problems from the top down, this approach is to explore the needs of companies and industries. Activities generating positive results include application of a firm-based approach to economic growth which seeks to overcome any non-policy constraints facing firms. Competitiveness briefings also work well in the region. These briefings, given to government officials and business leaders, describe the relative competitiveness of key sectors or industries, and often uncover policy constraints that diminish competitiveness.

The **Bureau for Africa** devotes some attention to structural reform—largely on power and trade capacity building activities. But the bureau primarily devotes the vast majority of Mission budgets and projects toward food security and health. To be sure, some efforts are given to reform policies and

systems in those sectors. In addition, there is growing interest in Domestic Resource Mobilization initiatives. Consideration of economic policy reform is complicated in Africa by several overlapping and competing trade and monetary unions, in which reform proposals by one country is often viewed by others as an attempt by the proposing nation to gain competitive advantage in capturing export markets or investment inflows.

As in Africa, the **Bureau for Latin America and the Caribbean (LAC)** is not now engaged in major structural reform efforts, but for a different reason. In the late 1990s and early 2000s, Latin America was a virtual hotbed of “Washington Consensus” reform activity driven by the financial crisis of the 1990s. Even though these reforms generated a considerable wave of growth and economic recovery, the policy belt tightening also exacted considerable pain on Latin countries. As a result, at least from the political perspective, the structural reforms were deemed a failure. Thus there is little appetite for new reform initiatives in Latin America. Countries in Central America are more amenable.

The LAC Bureau’s limited resources are spread between education, health, environment, democracy and economic growth. Most economic growth projects are devoted to agriculture, such as in **Haiti, El Salvador, Paraguay, and Guatemala**. The current focus on regional economics is on business support, including trade facilitation and digital development, and SME assistance. A number of Public Financial Management projects are under way.

The **Bureau for Europe and Eurasia** seeks to promote resilient and democratic societies, strengthen economic growth and energy security, and support European-Atlantic integration. Following the collapse of the Soviet system, this region was the literal epicenter of structural reform activities in USAID. Major projects in nearly all aspects of economic policy – monetary/fiscal, trade, investment, legal, etc. – were carried out to help these nations transform from centrally planned to market-oriented economies. USAID Missions sponsored efforts in 15 countries in Eastern and Central Europe to reform their commercial legal systems. While many of these initiatives have been completed, several activities are currently under way, such as structural reform programs in **Moldova** and **Ukraine** which focus on aspects of the European Union’s Deep and Comprehensive Free Trade Agreement (DCFTA).

C. OTHER U.S. GOVERNMENT AGENCIES INVOLVED IN STRUCTURAL REFORM

In addition to USAID, several other government agencies are engaged in structural reform initiatives in developing countries. The **Millennium Challenge Corporation (MCC)** is an independent agency that provides foreign assistance to reduce poverty through economic growth. Following a corporate values model, MCC engages with countries according to a competitive selection process in which performance on various structural reform and related policies is judged based on independent and transparency indicators. Continued support through MCC compacts is therefore predicated on country commitment and progress to implementing structural reforms.

The **Office of the U.S. Trade Representative (USTR)** oversees U.S. international trade, commodity and direct investment policy. USTR is responsible for negotiating trade and investment agreements, and so deals regularly with structural reform issues. USTR collaborates with the Department of State to negotiate bilateral investment treaties (BITs), and also deals with IPR protection issues. Accordingly, USTR provides advice and counsel on these issues to all U.S. trading partners, including developing countries. USTR supports the World Trade Organization’s technical assistance program. USTR also evaluates and designates country eligibility for participation in the U.S. Generalized System of Preferences (GSP) and other trade preference programs. Eligibility is subject to a number of mandatory and discretionary criteria, some of which are policy related (e.g., afford worker rights,

sanctity of U.S. property, access to markets, reduction in trade and investment barriers, etc.). (See Annex A for a discussion of trade agreements and structural reform.)

The **Department of Treasury's Office of Technical Assistance (OTA)** works with finance ministries and central banks in developing and transition countries to strengthen their ability to manage their public finances effectively and safeguard their financial sectors.⁴⁹ The OTA is selective—it works only with governments that are committed to reform—supports self-reliance, and works side-by-side with counterparts. In operation for more than 20 years, the technical assistance program consults with USAID, the Department of State, the IMF and World Bank and other stakeholders in developing and carrying out technical assistance programs.

In addition to these single-agency initiatives, the whole-of-government **Partnership for Growth (PfG)** program launched in 2011 represents an experimental approach to structural reform. The PfG is a partnership between the United States and a select number of countries (e.g., Ghana, El Salvador, the Philippines, and Tanzania) to accelerate and sustain broad-based economic growth. The approach, which requires ongoing partner commitment, includes the rigorous joint analysis of constraints to growth, the development of joint action plans, and high-level mutual accountability for implementation.

A key objective of PfG is to engage governments, the private sector, and civil society. Specific goals related to structural reform include improving regulatory capacity, strengthening the rule of law and anti-corruption measures, improving fiscal performance, and promoting human capacity development. Among the eight U.S. agencies involved are USAID, the Millennium Challenge Corporation, and the Departments of Treasury, Justice, Labor and State. Success in PfG programs has varied, and has been considered good in El Salvador and the Philippines. This initiative is currently winding down.

⁴⁹ Department of Treasury website.

IV. CONCLUSIONS

This report has sought to provide an overview on the complex history, application, and analysis of structural reform. The section begins with a synopsis of the existing state of knowledge and understanding of structural reform, focusing on strategic and operational lessons. It will then conclude by exploring linkages between structural reform and USAID priorities and goals. Annex A examines the relationships between structural reform activities and regional and multilateral trade agreements. Annex B summarizes the structural reform initiatives of institutions other than USAID. Annex C explores potential approaches for monitoring and evaluation systems for structural reform. Annex D presents options for USAID to consider for future structural reform initiatives.

A. STRUCTURAL REFORM TODAY

The central conclusion of this report is that structural reform, if carried out successfully, generates higher levels of productivity, which in turn results in accelerated rates of economic growth. This theme is fairly narrowly defined because it meets the test of economic analysis. However, structural reform also has a number of other salutary effects which are broadly understood to affect the means and ends of economic policymaking.

Appropriate policies unleash the energies and entrepreneurship of private enterprises, both large and small, that in turn constitute the backbone of every economy. Reforms can improve the efficient use of labor, capital and natural resources. Effective policy frameworks can, through growth, enable nations to establish the wherewithal to satisfy the economic and social needs of their people. In short, structural reform deserves to play a key role in economic development initiatives.

The process of adapting economic policies for the purpose of achieving accelerated growth and development has been applied in earnest over the past seventy years. Over that time, the experiences of so many countries and so many strategies have yielded a growing body of knowledge and lessons for the future. Nations have witnessed striking successes as well as disappointments. Economists have applied increasingly sophisticated tools to assess reform outcomes. Donor organizations have grappled with the challenge of coming up with winning approaches. This collective experience yields important strategic and operational lessons and guideposts for future structural reform activities.⁵⁰

STRATEGIC LESSONS ON STRUCTURAL REFORM

A number of lessons learned about structural reforms are strategic in nature, and focus on “whether” to undertake policy changes and appropriate expectations for initiatives.

- I. Adopting appropriate policy stances exerts a material, positive impact on economic growth and development.** Theory, empirical evidence and actual experience join to provide a compelling case for structural reform.

⁵⁰ These lessons are distilled from the literature, a review of country experiences, and recent analyses by the IMF and World Bank.

2. **The principal determinant linking policies to growth is enhanced productivity.** Performance will be enhanced if practitioners focus on productivity as the key dependent variable, achieved through improvements in factor markets and business practices.
3. **Seeking equity, inclusive growth, gender equality, social protection and environmental sustainability is smart economics.** Notwithstanding the core goals of productivity and competitiveness, reform programs that build in and expressly acknowledge these objectives will be more robust and politically palatable. Doing so can generate a virtuous cycle of momentum building for continuous reform.
4. **Structural reform can lead to greater economic resilience, the ability to adjust to shocks.** Improving factor mobility and the ease of doing business enhances a nation's capacity to adjust to fluctuating conditions, including both external macroeconomic factors such as commodity price collapses or financial crises as well as the impacts of natural disasters.
5. **Structural reform is not a panacea.** Achieving appropriate economic policies is a necessary but not sufficient step to raising economic growth rates. Policy change should be supplemented with growth-oriented investments (e.g., in education, infrastructure, health, etc.) and in efforts to strengthen foundations supporting industries that have comparative advantages and competitive niches.
6. **Motivation for policy change is highest during periods of economic stress or crisis.** Experience has shown that the "window of opportunity" is most open when governments and constituencies feel an urgent need for improved performance.
7. **Trade agreements and other international accords can encourage and support structural reforms.** Linking structural reforms to trade agreements provides an important vehicle to motivate reform, codify current "best policy practices," and spread structural reforms to signatory countries. The role of private international legal instruments promulgated by organizations like UNCITRAL should not be overlooked.
8. **Host countries must actively support policy change efforts.** Without engagement and continuing support by not only governments but also important constituencies, initiatives are inevitably destined to fail.
9. **Attaining positive economic impacts from reforms takes time.** Strategies need to manage expectations to avoid perceptions that immediate gains will result.
10. **Structural reforms incur costs, both transitional and permanent, which should be shared equitably.** Appropriate changes in taxes, tariffs, labor laws and other policies led to long-term gain, but certain economic dislocations are inevitable. Strategies need to incorporate shared costs, protections or assistance to support equitable growth.
11. **Reform planners must take into consideration and address "political economy" factors that are unique to each nation.** Political dynamics (e.g., recent or prospective government change), opposition elites, corruption and/or other features can dramatically affect program implementation and outcomes.

OPERATIONAL LESSONS ON STRUCTURAL REFORM

These conclusions are more tactical in nature, and refer to the manner in which structural reform programs are implemented.

1. **Each country is unique, and so structural reform initiatives need to be tailored.** Experience has shown that notwithstanding some similarities across groups of countries, no single “one size fits all” approach is appropriate.
2. **Policy priorities should be based on the varying needs of countries, which evolve over different levels of development.** While each nation is unique, the clusters of high value reforms for countries at various stages of development can provide useful guidance.
3. **Planners should consider the most effective pacing of policy reforms.** Experience has included both very gradual and immediate implementation. Something in the middle, allowing some time for adjustment without losing momentum, appears most effective.
4. **The clustering of “waves” of reforms implemented over time can enhance performance.** Some policy changes serve as a foundation for future reforms. In addition, attempting fully comprehensive reform at one time can overload systems and lead to undesired instabilities.
5. **Programs should be designed and implemented jointly by host country and foreign expert teams.** Experience has shown that jointly administered initiatives, with host country teams bringing local knowledge and commitment, and foreign teams bringing technical knowledge and “cover” for controversial actions, provide the best method of operation.
6. **A key and often neglected element of effective structural reform is good governance.** Without well-functioning government institutions and processes, policy changes alone will not likely achieve their objectives.
7. **Policy change programs should incorporate initial benchmarking and regular monitoring.** Reviewing and publicizing a set of quantitative and qualitative indicators can track performance and stimulate adjustment as well as build momentum.

B. STRUCTURAL REFORM AND USAID PRIORITIES

While USAID priorities have evolved over time with the introduction of new initiatives, budgetary constraints, and varying levels of cooperation from host country governments, the Agency has largely pursued interventions in a well-established set of focal areas. These priority areas (see box) contribute to USAID’s overall mission to “end extreme poverty and promote resilient, democratic societies,” with emphasis shifting depending on global crises, political-economic circumstances, and leadership in the United States. Further breakdowns of these priority areas surprisingly leads to greater overlaps rather than divergence. And though the majority of USAID programs are not explicitly directed at structural reform, structural reform activities could be, and often are, already implemented in a number of USAID’s priority areas.

USAID Priority Areas
<ul style="list-style-type: none"> • Inclusive, market-driven economic growth • Democracy, good governance, and human rights • Global health and health systems strengthening • Food security and agriculture • Resilience to climate change and environmental sustainability • Education • Conflict prevention and recovery, and humanitarian assistance

An example of a type of initiative stretching across multiple priority areas is the rise of public financial management (PFM) projects as donor funding decreases globally. This push for PFM includes improvements in domestic resource mobilization and application of innovative financing approaches. Structural reform activities that would usually have been pursued under the rubric of economic growth are now being pursued in broader priority areas such as health and

conflict prevention. In health, initiatives increasingly include components on capacity building for costing implementation plans at the national-level, and on taxation plans that earmark revenues for specific health programs. Overlapping reform activities, all with the ultimate goal of driving sustainable and inclusive development, provide a rich opportunity for coordinated structural reform in line with Agency, regional, and bilateral objectives.

Regional Missions in Asia; Central Asia; East, Southern, and West Africa; and Central America and Mexico have all outlined development objectives to advance, increase, or strengthen regional integration in their Regional Country Development Cooperation Strategies (CDCS). This objective provides obvious opportunities for structural reform initiatives. Indeed, many of the intermediate results and sub-intermediate results identify illustrative structural reform efforts to achieve their goals, though often not labelled as structural reform.

The breadth of topics encompassed under regional integration is also broader than reducing trade barriers and improving private sector access to markets. Cross-border energy and power trade is discussed in almost all regional CDCS's. Cross-border health systems strengthening, transboundary natural resource management, regional judicial reform, climate change resilience, and even early warning and response to crises and conflict are all outlined either as intermediate or sub-intermediate results of regional integration, or under their own development objectives. Each of these provides opportunities for targeted, efficient, and well-timed structural reform activities.

ILLUSTRATIVE LINKAGES BETWEEN REGIONAL USAID GOALS AND STRUCTURAL REFORM		Regional Goals						
		Trade and Regional Economic Integration	Cross-border energy and power	Health Systems Strengthening	Transboundary NRM	Regional Judicial Reform	Climate Change Resilience	Early Warning and Response to Crises and Conflict
Potential Structural Reform Activities	Constituency Building	X	X	X	X	X	X	X
	Financial Market Development	X	X	X	X		X	
	Public Financial Management	X	X	X	X	X	X	X
	Domestic Resource Mobilization	X		X	X		X	X
	Business Enabling Environment	X	X			X		
	Public-Private Dialogue	X	X	X	X		X	
	Investment Promotion	X	X	X	X		X	
	Subsidy Reform	X	X				X	X

The types of challenges each region faces and the actual bilateral programs being implemented in each of these regions suggest a strong emphasis on structural reform. In Moldova, for example, the Mission will review proposals for a 4-year Structural Reform Program in FY 2017-2018 that will focus on trade, policies for improved competitiveness, public-private dialogue, and other related issues. In Jordan, the bilateral mission is focused on accelerating inclusive economic development through the adoption of more business-friendly policies to increase competitiveness, as well as on improving fiscal stability and public financial management to help the government reduce food and energy subsidies. Jordan is a case

where several of USAID's priority areas overlap, as the country tries to absorb the influx of Syrian refugees into the workforce and into health, food, and education systems.

In summary, it is clear that there is significant interest in and opportunity for structural reform initiatives at the regional and bilateral mission level, albeit often not labelled as such. This provides a basis for more coordinated structural reform efforts at the Agency supporting opportunities for USAID Missions as well as greater coordination and collaboration with other donors and USG agencies pursuing similar or related activities. One could envision a "hub and spoke system" in which USAID Washington would develop a hub of structural reform capability that would extend spokes of assistance to Bureaus and Missions.

ANNEX A: STRUCTURAL REFORMS AND TRADE AGREEMENTS

In many cases, changes in economic policies are undertaken by individual countries, either on their own or in collaboration with donors or lenders. Increasingly, however, structural reforms are embedded in international agreements which have as one goal the adoption of policies which meet mutually agreed standards. The reason for this is because international commerce is most fair and efficient if all players operate according to common policy and regulatory norms in certain areas.

The earliest and most prominent multi-country economic agreements dealt with trade policies alone. Initially the focus was placed on achieving reduced and standard tariff levels among partners at the global, regional, or bilateral levels. Over time, negotiators added non-tariff barriers (NTBs) to trade, such as quotas, licenses, or standards and certification requirements.

In recent years, agreements have incorporated a widening net of economic policies, such as treatment of foreign investment, labor standards, financial transactions, and IPR protection. For example, the United States has entered into a number of **Bilateral Investment Treaties (BITS)** with trading partners to help protect private investments, develop market-oriented policies in partner countries, and support the development of international law standards consistent with these goals. In addition, recent and current regional trade negotiations have addressed an ever-broadening array of economic policy topics.

During the round of global trade negotiations that resulted in the creation of the World Trade Organization in 1995, a number of structural reform topics were introduced into the negotiations – many of which had been earlier embodied into bilateral or regional trade agreements. For example, the **Agreement on Trade-Related Investment Measures (TRIMS)** set limits on requirements countries to impose on foreign investors, such as local-content requirements, foreign exchange restrictions, and export mandates. The **Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS)** established minimum standards for laws and enforcement of IPR protection. And the General Agreement on Trade in Services extended to services sectors basic principles previously applied to trade in goods—nondiscrimination and most-favored nation treatment—while also providing a framework for WTO signatories to decide on how and when to open up services subsectors to foreign providers.

The following table presents the policy areas identified by the IMF as important determinants of productivity gains and economic growth. These are shown in the first column. The second column shows the international agreements that have incorporated some of these policy areas, and the third column indicates some of the specific policies addressed. While the table is not fully inclusive, it does reveal that international agreements cover a broad fabric of economic policies.

INTERNATIONAL AGREEMENTS ADDRESSING IMF POLICY REFORM AREAS		
IMF Policy Areas	International Agreements	Specific Policies Addressed
Trade	GATT/WTO, NAFTA, TPP, APEC, CAFTA, etc.	Tariffs, Non-Tariff Barriers, Rules of Origin, Customs Administration
Agriculture	WTO Agreement on Agriculture, NAFTA, TPP, etc.	Market Access, Domestic Support, Export Subsidies, Sanitary and Phytosanitary Measures
Industry	NAFTA, TPP	Standards, Energy and Basic Petrochemicals, Telecommunications, Textiles & Apparel, Automotive, etc.
Innovation	N.A. ⁵¹	
Financial/Capital	BITS, TPP	Investment, Capital Repatriation
Labor Market/Collective Bargaining	ILO, NAFTA, GSP, TPP	Unions, Collective Bargaining, Child Labor, Discrimination, Labor Standards, Occupational Safety
Legal	BITS, UNCITRAL, Trade Agreements, International Court of Justice	International Arbitration, Trade Remedies, Anti-Corruption
Banking	NAFTA, BASEL, TPP	Financial Services
Business	TRIMS, NAFTA, BITS, GSP, TPP	Competition Policy, MFN Treatment, Compensation for Nationalization, Performance Requirements, Dispute Settlement, SMEs
Infrastructure	NAFTA, TPP, Government Procurement Agreements	Government Procurement
Fiscal	IMF/SAPs	
Privatization	NAFTA, TPP	State Owned Enterprises
Property Rights	TRIPS, NAFTA, TPP	IPR Policies/Enforcement, Legal Protection of Property Rights

In view of the recent politicization of multilateral trade agreements, it is not clear looking forward whether this method of negotiating policy reforms among a large number of countries will be viable, at least for the near term. In addition, the specific structural reforms that individual countries need can easily fall outside the parameters of international agreements.

The proposed Trans-Pacific Partnership (TPP) took the recent trend of regional “trade” agreements expanding their scope to include investment, intellectual property, labor, e-commerce, digital trade, and other issues much further. Some economists have concluded that TPP was essentially a major structural reform initiative that cut across nations and markets by reducing barriers and harmonizing regulations.⁵²

Many of the policy areas identified as having material effects on productivity and growth are addressed in existing or pending agreements. Multilateral agreements, both binding and voluntary, provide an effective vehicle to motivate reform, codify current “best policy practices,” and spread reforms to all signatory countries. An important example is implementation of the Deep and Comprehensive Free Trade

⁵¹ The innovation category refers to research and development investment and activities, and not to IPR protection, which is covered by the property rights category.

⁵² TPP is a structural reform: Let’s evaluate it with structural models,” Fabio Ghironi, VOX – Centre for Economic Policy Research, July 3, 2016.

Agreement (DCFTA), sponsored by the European Community, which addresses a host of economic policy issues.

IMPLICATIONS FOR TRADE CAPACITY BUILDING

Linking reforms in these new areas to trade agreements provides a vehicle to motivate reform, codify current “best policy practices,” and spread structural reforms to signatory countries. For donor organizations, trade capacity building activities (i.e., assisting developing economies comply with such trade agreements) may need to encompass wider array of disciplines promoting structural reforms. Steps are already being taken in this direction. For example, the USAID’s Moldova Structural Reform Project is intended to help Moldova implement provisions of WTO agreements as well as the DCFTA with the European Union.

Multilateral “trade” agreements⁵³ represent one of the most efficient and effective platforms available for pursuing structural reform. Agreements are efficient because they encompass more than one and often many countries at the same time, thereby precluding the need to apply a country-by-country approach. In addition, they can cover numerous key economic policy issues, since most policies affect trade relations. They are effective because they bring the *gravitas* and persuasiveness of multiple trading partners to bear on participants’ reform efforts. This peer pressure can exert a powerful influence on nations to enact or sustain reforms.

⁵³ In this context, the term “trade agreements” is something of a misnomer, since agreements currently cover many policy issues in addition to trade policies.

ANNEX B: OTHER INSTITUTIONS AND DONOR ORGANIZATIONS PROMOTING STRUCTURAL REFORM

Multilateral and bilateral donor organizations have either pursued actively or at a minimum encouraged appropriate structural reform efforts for more than three decades. The key actors on a consistent basis over time have been USAID and the World Bank. The names under which these activities have been conducted have varied, as have the strategic and tactical emphases. But the backing of policy, regulatory and institutional improvements to achieve accelerated and sustained economic growth has been universal among donor agencies. Other international organizations (e.g., UN, EU, OECD, APEC, OAS, etc.) involved with economic affairs are also unanimous in their support.

MULTILATERAL INSTITUTIONS

The “major players” of donor organizations engaging in structural reform activities have been USAID and the World Bank. The International Monetary Fund (IMF) for many years focused on structural adjustment activities to assist member countries achieve financial balance, but has recently initiated efforts to respond to members’ requests for assistance on comprehensive structural reform. The regional institutions – Asian Development Bank (ADB), Inter-American Development Bank (IDB) and African Development Bank (AfDB) have carried out a limited number of efforts in this area, but most of their projects are devoted to infrastructure or social objectives. The same holds true of other bilateral programs such as those sponsored by Germany, the United Kingdom and Japan.

The World Bank. The World Bank Group (WBG) has engaged in structural reform efforts for over 35 years, and has significant experience in macro level, sectoral and industry-specific reforms. A recent report reviews and analyzes this evolving experience.⁵⁴ Efforts began in the early 1980s in a program known as “Adjustment Lending,” usually undertaken in concert with IMF programs, which focused on adjusting macroeconomic imbalances. The World Bank committed over \$27 billion to adjustment programs in 64 countries in the 1980s, and \$72 billion in 98 countries in the 1990s, accounting for 17 percent of total World Bank lending in the 1980s and 29 percent in the 1990s.

According to the World Bank, these activities achieved mixed results. Main criticisms included lack of recipient country ownership of programs, reforms did not account for costs borne by the poor and other short-term losers, little attention was placed on weak institutional capacity, and programs did not reflect the need for longer-term time frames and flexibility. Both external criticisms and internal assessments led the World Bank to adjust the program, which typically concentrated on three areas: reducing public spending to match available resources; removing trade restrictions; and promoting growth by strengthening institutional capacities and increased savings and investment. Overall, reform areas included macroeconomic policy, trade policy, agricultural policy, industry, the financial system and public enterprises.

⁵⁴ “World Bank’s Experience with Structural Reforms for Growth and Development,” MFM Discussion Paper No. 11, May 2016.

With additional time and experience, the World Bank came to acknowledge the need for yet further changes in strategy. In 1999, a new approach was adopted to support reforms that involved multiyear policy changes and institution building in low- and middle-income countries. A major focus was given to improving governance and accountability through institutional reforms. Starting in 2003, the World Bank has issued its flagship report, *Doing Business*, which provides annual quantitative data on the main regulatory constraints affecting domestic small and medium-size enterprises at the national level. In 2004 the World Bank issued a new operational policy, now called assistance Development Policy Lending, which supports policies and institutions to achieve sustainable growth and efficient resource allocation.⁵⁵ The World Bank has continued to provide vigorous support to structural reforms in member countries to promote accelerated, equitable growth and reduce poverty.

Many of the World Bank’s current structural reform activities are carried out under the organization’s Development Policy Financing (DFP) services. Relevant projects are in economic management and finance and private sector development. The DFP service provides IBRD loans; IDA credits/grants and guarantees budget support to governments for a program of policy and institutional actions to achieve sustainable, shared growth and poverty reduction. The World Bank is following a new approach to country engagement – the Country Partnership Framework (CPF), which replaces the Country Assistance Strategy (CAS). The CPF begins with a Systematic Country Diagnostic (SCD), which identifies the most important challenges and opportunities at the country level and includes consultations with stakeholders throughout the SCD process.⁵⁶

Current Areas of World Bank Structural Reform Support¹
<ul style="list-style-type: none"> • Promoting good governance and public sector reforms. • Increasing domestic resource mobilization. • Supporting inclusive growth. • Gender equality as smart economics. • Social protection. • Environmentally sustainable growth. • Enhancing competition for productivity and job growth.

International Monetary Fund. As noted above, the IMF has heretofore concentrated its financial and technical assistance to helping member countries achieve fiscal and financial balance. However, the IMF staff has determined that attaining stability and resilience to shocks depends on sustainable growth, which in turn is determined by more fundamental economic policies. In 2013 the staff issued a discussion note linking stability and growth to productivity-enhancing reforms.⁵⁷ More recently, the IMF published a staff report citing the importance of structural reform on macroeconomic performance, and presenting the case for more explicit IMF involvement in this area.⁵⁸

Other International Organizations. A number of other international organizations are engaged in functional areas that incorporate structural reform issues. Their major assistance to developing countries takes the form of detailed technical assistance. The **United Nations Development Programme (UNDP)** carries out a program on development planning and inclusive sustainable growth, including projects on development planning strategies, social protection strategies, poverty monitoring, enhanced economic governance, and advocacy for a new Global Partnership for

⁵⁵ From Adjustment Lending to Development Policy Lending: Update of World Bank Policy, June 2004.
⁵⁶ World Bank web site.
⁵⁷ Anchoring Growth: The Importance of Productivity-Enhancing Reforms in Emerging Market and Developing Countries, IMF Staff Discussion Note, December 2013.
⁵⁸ Structural Reforms and Macroeconomic Performance: Initial Considerations for the Fund, IMF Staff Report, November 2015.

Development – a more favorable international policy environment in areas such as international trade, foreign direct investment, intellectual property rights, technology transfer and migration.

The **World Trade Organization (WTO)** oversees the management of the international trading system, and provides developing countries with a limited amount of technical cooperation missions and training to build trade capacity. WTO's Aid for Trade program helps developing countries enhance the skills and infrastructure needed to expand their trade. The **International Labour Organization (ILO)** works with members to set labor standards, develop policies and devise programs promoting decent work for all women and men.

The **Organization for Economic Co-operation and Development (OECD)** focuses on the economic affairs of industrialized country members, but also works with governments and private sectors in developing countries. Key areas of work include better policies for development (e.g., environment and development, food security, strengthening governance, social and human development, trade and global value chains, etc.).

REGIONAL INSTITUTIONS / DEVELOPMENT BANKS

The majority of resources of the three major regional development banks are devoted to infrastructure and social objectives. However, each of these institutions does sponsor programs and projects that incorporate structural reform components.

- **Asian Development Bank (ADB)** projects in regional cooperation/integration and financial sector development often include policy/structural reform elements.
- **The InterAmerican Development Bank** embeds structural reform activities in projects in the reform/modernization of the state and financial markets sectors.
- **The African Development Bank (AfDB)** channels of regional economic integration, private sector development, and governance and accountability touch on economic structural issues, primarily through institutional strengthening.

An effective structural reform program is overseen by **Asia-Pacific Economic Cooperation (APEC)**, a forum for 21 Pacific Rim economies that promotes free trade and investment throughout the region. The program is unique, and operates on the basis of commonly developed goals and focal points, and member country designed, implemented and monitored action plans. The program is entering its third generation of reform plans.⁵⁹

- The first generation focused on the core priorities of regulatory reform, competition policy, corporate governance, public sector governance, and economic and legal infrastructure.
- The second expanded the scope to five broad pillars: (1) more open, well-functioning, transparent and competitive markets, (2) labor market opportunities, training, and education, (3) sustained SME development and enhanced opportunities for women and vulnerable populations, (4) effective and fiscally sustainable social safety net programs, and (5) better functioning and effectively regulated financial markets.
- The third draws on progress and lessons learned under the first two programs; it has three pillars for concrete reform actions by member countries: (1) more open, well-functioning,

⁵⁹ "Exploring Quantitative Indicators for Effective Monitoring of APEC-wide Progress on Structural Reform under RAASR 20016-2020," APEC Policy Support Unit, October 2016, p. 2-3.

transparent and competitive markets, (2) deeper participation in those markets by all segments of society, including micro, small and medium enterprises, women, youth, older workers and people with disabilities, (3) sustainable social policies that promote the above-mentioned objectives, enhance economic resilience, and are well-targeted, effective, and non-discriminatory.

APEC has reported progress through these phases, as well as continued commitment by member economies. The process is supported by the APEC Policy Support Unit.

OTHER BILATERAL DONORS

Bilateral donor agencies tend to focus on poverty reduction, infrastructure, social development, skills training, and sustainable environment. Activities in these areas resonate with the agencies' domestic constituencies and have less chance of encountering potential controversies sometimes associated with structural reform. However, as with the regional development banks, bilateral aid programs do include initiatives that touch on economic growth policy.

The **German aid agency, GIZ**,⁶⁰ offers products and expertise in management services, rural development, sustainable infrastructure, security, reconstruction and peace, social development, governance and democracy, environment and climate change, and economic development and employment. In economic development, GIZ assists partner countries in the areas of labor markets (vocational education systems, employment policies), financial systems (microfinance, rural finance, and capital market development), private sector development, and economic policy (advice on sustainable development, trade, quality infrastructure, the green economy, and regional economic integration).

The **U.K. Department for International Development (DFID)** works to end extreme poverty and build a safer, healthier and more prosperous world. Areas of involvement include health clinics, girls' education, disaster relief, etc. Examples of projects in economic growth are energy production in Africa, free trade agreement support, catalyzing investments to benefit poor people, and assessing the impact of corruption on private sector development.

To further its vision of inclusive and dynamic development, the **Japan International Cooperation Agency (JICA)** pursues four missions – addressing the global agenda (e.g., equity, climate change, infectious diseases, terrorism, etc.), reducing poverty through equitable growth, improving governance and achieving human security. In the field of economic policy, JICA support is primarily aimed at strengthening the structure of developing countries to manage fiscal and financial matters.

⁶⁰ Deutsche Gesellschaft für Internationale Zusammenarbeit, GmbH, formerly known as GTZ.

ANNEX C: MONITORING AND EVALUATION FRAMEWORKS

Monitoring the effectiveness and impacts of structural reform initiatives is of vital importance to nations undertaking policy change, but also their donor partners. A system that can track actions and results informs policymakers whether implemented reforms being made and are meeting their intended purpose. Positive results can create momentum for further reforms, and shortcomings can be used to guide mid-course corrections or reviews of the efficacy of implementation.

Monitoring structural reform is complex for several reasons. It involves a combination of qualitative and quantitative information, some of which can be drawn from international sources and some of which may be country-specific. While monitoring systems should be based on causal relationships (e.g., changes in “X” policies will generate “Y” outcomes, causality is not known with complete certainty, and these relationships are affected by numerous exogenous factors. In addition, there remain a number of important deficiencies in national and international data, as described in the following section.

Notwithstanding these complexities, a number of resources are available to guide M&E system design. One important resource is the M&E handbook for business policy reform sponsored by the International Finance Corporation (IFC) in collaboration with GTZ and DFID.⁶¹ USAID has substantial experience and expertise in crafting and employing effective M&E systems.

Effective monitoring and evaluation systems are not only necessary but also beneficial, since they contribute to reform efforts. Drawing from international experience and success, planners should consider basing these systems on a number of principles in addition to standard M&E practices.

- **Involve host countries in monitoring system design.** All reform assessments stress the importance of host country commitment. Putting this into practice, host country officials and experts should be actively involved in system design, not only to enhance local buy-in, but also to take advantage of local expertise.
- **Include both common program elements and tailored country elements.** Acknowledging the lesson that reform programs should be customized for each country, monitoring systems should also be tailored. However, a number of common, cross country components should be incorporated to allow for overall program evaluations.
- **Maximize the use of existing international data.** Monitoring system elements that depend on international comparisons should employ currently available statistics, since developing new data sets would be prohibitively expensive.
- **Divide systems into “policy” and “outcome” components.** USAID’s practice of identifying interim and final indicators has been in use for decades. In this case, policy changes

⁶¹ “The Monitoring and Evaluation Handbook for Business Environment Reform,” IFC Advisory Services in association with GTZ and DFID, June 2008.

are the core interim objectives, whereas economic performance measurements represent the ultimate goals.

- **If possible, include both hard data and soft data.** The value of employing hard data is clear (objectivity, transparency, etc.), but the inclusion of certain qualitative information based on surveys, process descriptions, etc. can provide beneficial information such as investor or consumer confidence, business forecasts, etc. As an example, researchers point to government attitude change rather than specific policy reform as triggering growth acceleration in India.
- **Regularly report on and disseminate information on activities and outcomes.** Many countries which engineered successful waves of policy reform employed the practice of regularly and honestly reporting on progress, problems encountered, and goals achieved. This not only contributes to program refinement but also to building confidence and commitment among outside constituencies.

Although crafting an M&E framework and locating relevant statistics has its challenges, it is possible to craft an effective and relatively robust system for monitoring and evaluation that uses existing data and applies a pragmatic approach.

As with all programs, monitoring depends on statistics, and one must deal with data availability, coverage, reliability, measurement, and timeliness. Structural reform involves policy inputs and economic performance outputs. Some policy variables can be easily quantified, but others are more qualitative. Fortunately, considerable progress has been made in quantifying policies and changes in them, as well as ranking country policy stances.

Unlike the outcomes of infrastructure programs, institutional development activities, or specific industry growth projects, which tend to be project specific and micro in nature, the results of structural reform efforts typically revolve around macroeconomic variables. Micro data can be collected by program staff, whereas to obtain macro statistics, one must depend on reliable international sources, especially if comparisons are sought. Once again, major gains have been made over the past two decades in the collection and dissemination of increasingly detailed and targeted statistics.

Several international bodies, including the IMF and APEC, have examined in detail the issue of structural reform data availability. Both have concluded that at least for now, it makes sense for reform analysts and practitioners to utilize existing data sources. The cost of collecting and refining new streams of statistics would be prohibitive. This conclusion is correct. A broad data set data for structural reform could be built utilizing the sources represented in the following table.

POTENTIAL SOURCES OF DATA FOR STRUCTURAL REFORM	
Macroeconomic Performance	
IMF	<ul style="list-style-type: none"> • International Financial Statistics • Direction of Trade • Balance of Payments Statistics • World Economic Outlook Database
Monetary, Fiscal and Trade	
IMF	<ul style="list-style-type: none"> • Monetary, fiscal and trade policy
WTO	<ul style="list-style-type: none"> • Trade policy (Trade Policy Reviews)
ITC	<ul style="list-style-type: none"> • Trade Map & Market Access Map - trade and tariff statistics
Business Operating Policies	
World Bank	<ul style="list-style-type: none"> • Doing Business indicators – ease of doing business
World Economic Forum	<ul style="list-style-type: none"> • Global Competitiveness Report (legal system and property rights, labor market regulations, etc.)
Fraser Institute	<ul style="list-style-type: none"> • Economic Freedom Index (legal system, regulation, access to finance)
Economist Intelligence Unit	<ul style="list-style-type: none"> • Competition policy, foreign investment policy, etc.
Key Sector Policies	
IMF	<ul style="list-style-type: none"> • Index of Agricultural Regulation
OECD	<ul style="list-style-type: none"> • Energy Regulation • Transport Regulation • Communications Regulation
Fiscal Monitor	<ul style="list-style-type: none"> • Infrastructure Investment
Social Performance	
World Bank	<ul style="list-style-type: none"> • World Development Indicators • Education Statistics • Gender Statistics • Health Nutrition and Population Statistics

To support a structural reform initiative, it is recommended that drawing from these and other sources, a global database covering as many countries and relevant variables as possible be prepared. This data set would be used for three purposes: (1) to assist in the preparation of diagnoses of specific partner countries through comparative statistics; (2) to develop milestones and track progress achieved in reform programs (as noted above, monitoring improvements in rankings or measures of “distance to frontier” in the World Bank’s Doing Business data can be a powerful motivational tool); and (3) to support general analyses to expand knowledge on structural reform.

Overall, a common-sense approach for monitoring and evaluation would be to apply a two-tiered system similar to that adopted by APEC in its structural reform program.⁶² In the first tier, a publicly available overarching set of global indicators would be used to assess progress across economies, including specific partner nations. In the second tier, assistance teams along with their partner

⁶² “Exploring Quantitative Indicators for Effective Monitoring of APEC-wide Progress on Structural Reform under RAASR 2016-2020,” APEC Policy Support Unit, October 2016.

counterparts would set forth specific action plans along with metrics to establish baselines and progress achieved. These metrics could include subsets of the overall indicators, as well as tailored measures which track particular aspects of the action plans.

ANNEX D: STRUCTURAL REFORM STRATEGY OPTIONS

Given the findings presented in this report, there is merit for USAID, its partners and other donors to consider continuing or expanding structural reform activities. This conclusion is supported by compelling logic. Developing country partners can achieve accelerated economic growth through thoughtfully prepared initiatives to improve their economic policy frameworks. New knowledge is enhancing the capacity to design nuanced reform programs that not only reduce or eliminate many of the problems encountered in the past, but also incorporate elements that more directly address the needs of disadvantaged groups and open opportunities for greater equity and inclusiveness.

While structural reform does not guarantee success on its own, and must be accompanied by other growth initiatives, it does represent one of the best alternatives for achieving development progress. In comparison to other possible interventions, structural reform is a relatively cost effective, high payout activity. Also, in addition to improving the performance and well-being of partner developing countries, the growth generated by reforms can benefit the United States. Successfully growing developing nations are less reliant on foreign assistance, and their higher income levels achieved create greater demand for imports, which can expand opportunities for U.S. job creation. Thus, structural reform efforts can establish “win-win” situations.

There are basically three options for USAID to contemplate looking forward.

- Option 1 would be a “business as usual” approach to continue existing efforts without fundamental change, responding to requests from partner countries on an ad hoc basis, and monitoring developments and the creation of new knowledge in structural reform, most likely by the World Bank, the IMF and academia.
- Option 2 would be to organize a modest pro-active program which draws from lessons learned, seeks collaborative linkages within USAID, and sets forth an updated implementation methodology.
- Option 3 would constitute the development of a comprehensive structural reform initiative. This option would be built from a series of program development steps, including the designation of an Agency office as “champion” of the activity, identification of a core team of experts within USAID’s existing staff, recruitment of both donor and host country partners, and training and promotional efforts. None of these steps would require any form of Agency reorganization.

If it is determined that some form of new program is warranted, a number of development elements could be explored. The components discussed below offer a range of options for further development.

- I. **Consider a “re-branding” of structural reform.** There is nothing inherently wrong with the term structural reform as defined in this report. The expression is currently being used by the IMF and World Bank to denote the systematic improvement of economic policy structures. However, there is a certain amount of “baggage” associated with the term, since many development practitioners perceive structural reform to be the same as either structural adjustment or Washington Consensus change, or some combination of the two.

For this reason, there may be some value in discussing the merits of a new terminology. Options could include “growth policy platform,” “policy architecture reform,” “policy system

transformation” or some other new phrase to represent the concept. USAID has developed economic growth frameworks that make little or no reference to structural reform.

2. **Designate an institutional champion.** New initiatives are difficult if not impossible to launch without an assigned champion responsible for designing and implementing a plan of action.
3. **Design the structural reform program.** The critical phase in the early development effort is to craft a compelling and logical plan to guide the initiative. This could begin with a strong conceptual framework of desired outcomes, followed by the identification of program scope and scale, components, phases, actors, processes and other design factors. The scope could range from a one-time assistance package to a multi-faceted activity involving structured stages and an integrated network of collaborating institutions. The plan could be developed by an internal USAID team, perhaps supplemented by a small number of external advisers.
4. **Identify a USAID team and gather information on the state of the art.** The Missions and Bureaus possess deep experience and expertise on the identification and application of structural reforms. As presented in this report, structural reform has an extensive history and set of organizational players. The knowledge base on the subject is broad and expanding over time, and this information is dispersed widely among academics, donors and international institutions. An effort to pull together in one place the various strands of knowledge – theoretical, empirical and experiential – will assist researchers and practitioners to consolidate and increase understanding, and to provide practical guidance on emerging initiatives.
5. **Identify and engage institutional partners.** USAID could design and implement a structural reform program on its own. This would be the simplest approach, since it would avoid the need to deal with a number of institutional complications in areas such as program leadership, coordination, cost sharing, etc. At the same time, this model would preclude a number of advantages associated with partnership, including access to broader expertise and financial resources, economies of scale, and increased support. Two types of partnerships are worth consideration:
 - **Core and support partners.** USAID could enter into a collaboration including one or two “core” partners and several “support” partners. The core partners would cooperate jointly on full program development and implementation. Based on current levels of knowledge and interest as presented in this report, the World Bank and/or the IMF would appear to be the mostly likely candidates as potential core partners with USAID. The support partners would offer their expertise and assistance in specific policy areas. Examples of support partners could be the U.S. Department of Treasury (monetary, fiscal), the USTR (trade, investment, IPR), the WTO (trade), and the MCC (overall development).
 - **Network of partners.** An alternative approach less formal than that described above would be for USAID to manage the core structural reform program by itself, but establish a collaborative network of other institutions. USAID would assume responsibility for the overall program, similar to the role of a “prime contractor,” and would operate a referral system to tap into the specialized expertise of outside institutions such as those noted above.
6. **Develop and conduct training modules.** Successful implementation of a structural reform initiative will require two types of training. Both would draw from the information base proposed above and cover the same technical material. The first training component would be provided to relevant USAID Mission and Bureau staff, as well as possible outside partner institutions. The second component would provide more extensive training for leaders and economic policy officials in developing countries. The latter modules would be provided after the countries have agreed to participate.

7. **Prepare informational and promotional materials for developing countries.** Given the requisite host country commitment to structural reform, leaders must be convinced that their efforts will be rewarded. This will require materials which provide honest but compelling arguments, as well as comprehensive discussions with leaderships.
8. **Beta test program.** A highly worthwhile but often neglected step in government activities is beta testing to work through the process, identify and address obstacles, and refine the overall concept. This testing could be carried out with one or two cooperative developing nation partners
9. **Establish partnerships with developing countries.** Once the initiative has been fully articulated and refined, USAID officers can confer with their counterparts to solicit participation. A number of programs such as those of the MCC and Partnership for Growth can provide insights into effective recruitment approaches.
10. **Launch structural reform program.** Following the completion of all necessary design and development tasks, the structural reform program can commence. Optimally the program would follow a comprehensive business plan that includes actions, key responsibilities, milestones and goals to direct implementation and provide performance metrics on which to base the usefulness and viability of the program.

POTENTIAL POLICY AREAS

Structural reform activities, as described in this report, have covered almost all of the myriad policies, rules and regulations that underlie economic intercourse. In fact, debates over what policy elements should or should not be addressed, as well as which should hold priority, has been a principal source of controversy over structural reform. If one begins with the common sense conclusion that policies matter, it is possible to construct a policy agenda that can be adapted to meet varying circumstances.

Building on existing knowledge and practical development experience, one could envision a three-tiered system for comprehensive structural reform.

The first and highest tier would consist of “core economic policy foundations,” essentially a nation’s basic monetary and fiscal policies. Effective monetary and fiscal systems are requisites to sustained growth and stability.

FIGURE 3. THREE-TIERED SYSTEM FOR COMPREHENSIVE STRUCTURAL REFORM

Core Economic Policy Foundation											
Tier 1	<table border="0"> <tr> <td>Monetary Policies</td> <td>Fiscal Policies</td> </tr> <tr> <td>Central bank operations</td> <td>Overall budget balance</td> </tr> <tr> <td>Money supply growth</td> <td>Revenue/taxes</td> </tr> <tr> <td>Interest rate policy</td> <td>Expenditure levels</td> </tr> <tr> <td>Foreign exchange rate policy</td> <td>Spending distributions</td> </tr> </table>	Monetary Policies	Fiscal Policies	Central bank operations	Overall budget balance	Money supply growth	Revenue/taxes	Interest rate policy	Expenditure levels	Foreign exchange rate policy	Spending distributions
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	Central bank operations	Overall budget balance									
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	Interest rate policy	Expenditure levels									
Foreign exchange rate policy	Spending distributions										
Business Operating Policy Platform											
Tier 2	<table border="0"> <tr> <td>Trade</td> <td>Starting a business</td> </tr> <tr> <td>FDI</td> <td>Access to credit</td> </tr> <tr> <td>Privatization</td> <td>Labor regulations</td> </tr> <tr> <td>Deregulation</td> <td>Enforcing contracts and legal recourse</td> </tr> <tr> <td>Property rights</td> <td>Resolving disputes and insolvency</td> </tr> </table>	Trade	Starting a business	FDI	Access to credit	Privatization	Labor regulations	Deregulation	Enforcing contracts and legal recourse	Property rights	Resolving disputes and insolvency
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	FDI	Access to credit									
	Privatization	Labor regulations									
	Deregulation	Enforcing contracts and legal recourse									
Property rights	Resolving disputes and insolvency										
Key Sector Policies											
Tier 3	Policies that specifically govern the activities of critical sectors (e.g., food, energy, productive resources)										

The second tier would concentrate on a nation's "business operating policy platform," or the rules that apply to all economic actors and cover a host of business processes.

The third tier would encompass "key sector policies," or those that specifically govern the activities of critical sectors. Examples would include food security systems for low income countries, energy systems for oil exporting nations, or business services systems. This tier could also include key productive sectors such as agricultural exports or tourism. Surveys and focus groups could identify issues and distinguish between policy impediments and privileges sought.

The policy categories are listed in descending order of priority. However, not all countries would require action in all of these areas. A thorough diagnosis could determine that policies are in place and appropriate in some or many fields. The diagnosis could pinpoint specific needs to be incorporated into a structural reform program. Alternatively, USAID could determine that a reform initiative would be limited to a certain subset of this list.

Any initiative should make clear that structural reform is not limited to a given set of policies, but rather is a flexible suite of policies that can be adapted to different country circumstances. The list of policy areas is indicative rather than comprehensive. The list could be reconfigured. In addition, practitioners would quickly note that there are many subcategory policies in each of the areas identifies. This list is intended for discussion purposes.