

# Précis

WORLD BANK OPERATIONS EVALUATION DEPARTMENT

SUMMER 1998

NUMBER 161

## Côte d'Ivoire: Devaluation's Benefits

**C**ÔTE D'IVOIRE'S FORTUNES HAVE FLUCTUATED dramatically over the past thirty years. Throughout this period the Bank has been firm in its support, especially since the boom of the 1970s gave way to the protracted crisis of the 1980s and early 1990s. As in many other countries, the Bank initially tackled the crisis by changing its assistance focus from investment loans to quick-disbursing loans aimed at policy reforms. From 1988 to 1996, adjustment loans accounted for three-quarters of all Bank lending to Côte d'Ivoire.

With the devaluation of the CFA franc in 1994, Côte d'Ivoire began a solid recovery. Today, prospects appear favorable for a resolution of the country's debt problem. According to an OED study\* of Bank assistance to Côte d'Ivoire, new opportunities are emerging for long-term growth and poverty reduction. The study found adjustment lending to be an appropriate instrument for providing massive financial assistance, supporting key reforms and rectifying institutional weaknesses, immediately after devaluation. Investment lending was particularly successful in fields in which the Bank had an ongoing and long-standing working relationship with the government.

The Bank must now orient its strategy toward deepening reforms to tackle problems that continue to plague Côte

d'Ivoire, putting its longer-term economic sustainability at risk. Major obstacles facing the country include a fragile public finance sector, a deficient judiciary system, a narrow productive capacity base, overall institutional weaknesses, widespread poverty, and lagging human resource development.

### The African Elephant

In September 1995, Côte d'Ivoire's government presented its economic strategy in a document called "l'Elephant d'Afrique." The image was chosen to project the message that this African elephant was ready to tread in the footsteps of the Asian tigers. The analogy raises a number of questions: After being hailed as Western Africa's "success story" in the 1970s, why did Côte d'Ivoire's



economy decline so sharply in the 1980s? What changed over the past 15 years to revive country optimism? What were the drawbacks in the Bank's strategy during the 1980s? How should the Bank proceed with regard to Côte d'Ivoire?

### *The Golden Years*

Through the 1970s Côte d'Ivoire maintained the same export-oriented policies that had proved so rewarding during the 1960s. Its primary exports, cocoa and coffee, were the engine for growth, accounting for a large share of GDP and for about 90 percent of total export earnings. From 1972 to 1977, cocoa and coffee prices increased five-fold, export earnings from the two commodities almost tripled, and total export earnings grew 120 percent.

The boom, however, led to over-expansive policies. Net foreign assets of the banking system hardly increased, domestic credit and money (M2) quadrupled, and the cost of living rose 30 percent compared to that of France (the parity of the CFA franc remained fixed at 50 CFAF per French franc, as it had been since 1946). Côte d'Ivoire was unable to obtain competitive status in the manufacturing sector because costs were too high and productivity too low. It failed to attract direct foreign private investment.

### *The Crash*

The situation changed dramatically in the late 1970s, when commodity prices started to fall. At first the government, believing the price drop to be temporary, maintained its investment program and increased its borrowing. But by the end of 1980, the government was forced to call on the Bretton Woods institutions for help. The Bank and the International Monetary Fund (IMF) response resulted in a series of adjustment programs. By 1985 public finances and the external balance had improved markedly, and the crisis appeared to be over.

The picture worsened again after September 1985, when the CFA franc appreciated sharply in relation to the US dollar. A subsequent collapse of cocoa and coffee prices aggravated the situation. By 1987 the economy was in a full-scale depression. From 1985 to 1993 Côte d'Ivoire's export earnings plunged 64 percent, per capita GDP fell 4-5 percent per year, and poverty increased sharply.

### *Poverty and Education*

The proportion of poor rose from 11 percent in 1985 to 37 percent of the population in 1995. The distribution of poverty also changed, and for the first time Côte d'Ivoire faced urban poverty. Côte d'Ivoire's record on basic education and health—the foundations for oppor-

tunities leading to better jobs and a higher quality of life—is not good and the Bank's intervention in the social sectors has not been markedly successful. The government spent more in education and health than most other African governments, but spending was not always directed where it would have been most effective. The Bank, too, had little success in improving the internal or external efficacy of the education system.

### *Devaluation*

On January 12, 1994, the parity with the French franc was changed from CFAF 50 to CFAF 100 in each of the 13 CFA countries. None of the feared catastrophes followed the devaluation. The 1994-96 macroeconomic objectives were reached for the zone as a whole and Côte d'Ivoire had one of the best performances, with a 7 percent growth of GDP in 1995 and 1996. This was due in large part to policies that sought to liberalize the economy and contain the public wage bill. The Bank, the study stressed, contributed to this achievement.

### **Bank Strategy**

Until 1981, all Bank assistance to Côte d'Ivoire consisted of investment loans, mostly in agriculture, transport, urban development, and water and sanitation. After the second oil shock (1979-80) and the emergence of the debt crisis (1982), Bank lending policy adjusted to the deterioration of the economic situation in many developing countries. First, the Bank created quick-disbursing instruments to cope with the crisis. It then promoted adjustment lending to promote policy reforms.

Côte d'Ivoire received its first adjustment loan from the Bank in 1981. Many more followed: during 1988-96 adjustment lending accounted for 80 percent of all Bank commitments to Côte d'Ivoire, compared with only 30 percent for the rest of Sub-Saharan Africa. This trend continued after devaluation: between 1994 and 1996 Côte d'Ivoire received half of all adjustment lending extended to the region.

The most obvious effect of this in Côte d'Ivoire was a steep decline in investment loans, which fell from 100 percent of all lending in 1981 to 20 percent in 1988-96. While this shift reflected a Bank-wide trend, it was greater in Côte d'Ivoire than in the rest of Sub-Saharan Africa.

### *Non-Lending Activity*

The Bank devoted substantial resources to assess the measures needed to support devaluation, enabling Bank staff to be better prepared for the after effects of devaluation. The Bank also increased its technical assistance in regional issues, with the transformation of the Union Monétaire Ouest Africaine (UMOA) into an *economic* and monetary

union (UEMOA). Technical assistance in public sector management and capacity building has been particularly important over the past 10 years.

Given the scope of its concerns and its status as major creditor, the Bank has a well-established role as aid coordinator. This is enhanced by a close relationship with the IMF and the International Finance Corporation (IFC).

### *Dialogue and Portfolio Management*

Disagreements between the Bank and the government during the 1970s stemmed primarily from technicalities—for example, whether to build a two- or three-lane highway. But after the crisis, the Bank and IMF persuaded the government not to carry out a number of costly, high-visibility projects and to reschedule the public and publicly-guaranteed external debt to Paris and London Club creditors.

By 1987 the Bank's management became convinced that a devaluation would be needed to restore competitiveness. Pending a devaluation (which would require caution and time for preparation), the Bank decided against issuing loans to Côte d'Ivoire exclusively on IBRD terms, given that loans would have to be repaid from government revenues.

Two sets of three adjustment loans were approved between 1988 and 1993 to lay the groundwork for devaluation by (1) launching reforms that would contribute to the success of the devaluation and (2) providing prompt financial support for the post-devaluation period. Only the first tranche of each loan was to be released before devaluation. After devaluation, Côte d'Ivoire was declared eligible for IDA credits only.

The devaluation removed a major constraint to policy dialogue, which subsequently gained prominence in the relationship between the government and the Bank. The nature of the dialogue began to change in the early 1990s, as the decisionmaking process became increasingly democratic. Dialogue has not always been easy (initially, for example, on poverty issues), but today it appears promising.

### **Bank Performance**

Since 1968 the Bank's commitments to Côte d'Ivoire have been much higher than in the rest of Sub-Saharan Africa (2.1 percent against 0.8 percent of GDP). But performance has not been impressive by standard pre-1995 criteria. Côte d'Ivoire ranked among weak performers in a 1997 report on adjustment lending in the region, and the time required to bring projects to the board for approval was well above average. The share of projects at risk, however, was much lower than average (11 percent in June 1997, compared with averages

of 40 percent for Africa and 24 percent worldwide).

Before 1980 performance was very good for agricultural and infrastructure projects, but surprisingly poor in the education sector, where projects were approved on the incorrect premise that the economy would continue to expand rapidly. Later education projects, approved in 1990 and 1991, were implemented during the country's financial crisis when educational improvements were not on the government's high-priority list. The outcome of four of five projects was rated as unsatisfactory.

The Bank may be criticized for overlending in the 1981-87 period, but even with perfect foresight it could not have prevented the 1987 crisis. During 1987-93 the Bank had to choose between a confrontational (ceasing all adjustment loans) and conciliatory approach. Bank management chose the latter. Bank staff can be credited with using the last set of adjustment loans in early 1992 to prepare the groundwork needed for the devaluation.

Because the success of devaluation surpassed expectations, the study gave the Bank top ratings for efficacy and relevancy. Poverty reduction was a major objective, and restoring growth was considered the chief means for reducing poverty.

The outcome of 40 percent of operations approved since 1981 was rated unsatisfactory, but these were carried out when public finance was tight and the government, in its efforts to plug budgetary holes, paid more attention to large, quick-disbursing adjustment programs than small, slow-disbursing investment projects. The poor outcome of many socially oriented projects may be explained by the fact that education, health, and environment were not on the government's high-priority list at that time.

### **New Opportunities**

With the solid recovery of the Ivoirian economy and the progress made under the Highly Indebted Poor Countries initiative, the Bank can now help the government to achieve sustainable growth aimed at reducing poverty. To achieve this goal, a change is needed in the nature and the mix of lending instruments.

*Sustainable growth.* The government has approved the framework of a pro-poor growth strategy that includes targets for social indicators in the year 2000. As spelled-out in the Country Assistance Strategy, the Bank must provide technical assistance to help authorities identify policy changes that would benefit the poor without significantly reducing GDP growth. It should also help the government select the indicators that are most relevant and readily monitorable.

*Lending instruments.* Adjustment lending, which was exceptionally high for Côte d'Ivoire, will still be needed to tackle financial gaps and reforms until 2000. However, its

## New Lending Instruments

THE BANK'S BOARD APPROVED TWO NEW investment products in September 1997: learning and innovation loans and adaptable program loans, designed to complement traditional lending instruments. The new products are expected to provide performance-based support for projects, reduce preparation times, emphasize supervision results, and reduce risks.

*Learning and innovation loans* allow countries to try new approaches by using loans of up to \$5 million, to be approved by the regional vice president. These loans, of which about \$200 million are expected to be approved each year, support programs to

build capacity or to develop models in preparation for a large-scale program, or to pilot promising but untested initiatives.

*Adaptable program loans* (about \$1 billion to be approved each year) provide support for long-term programs but fund only one sequence of activities at a time, with subsequent activities developed as needed. The Board approves the program (which sets the overall framework, performance parameters, and a ceiling for total lending) and the first loan. Subsequent loans are approved by the regional vice president, provided the program context has not changed significantly. The Board has the right to intervene before approval of a loan becomes effective.

share should be reduced to the benefit of new instruments—such as the proposed “learning and innovation loans” and the “adaptable program loans” (see box)—which appear better suited to many of today’s issues.

## Recommendations

*Adjustment lending should be adapted, and gradually reduced.* However, since adjustment lending may remain substantial over the 1997-99 period, problems could be minimized by avoiding large tranche releases. Lending operations should be programmed in sequences supported by technical assistance credits and appropriate nonlending activities. The experience of Côte d’Ivoire could be used as a test case for assessing the feasibility of the proposed new lending instruments in other countries.

*Cooperation between the Bank and the IFC* has recently improved, but closer cooperation would help to make the private sector the engine for growth.

*Greater attention needs to be paid to institutional issues* when formulating the investment projects, which will account for a growing share of Bank commitments in future. Progress is needed in implementation, especially of projects with a high social content. The Bank should press the government to release counterpart funds promptly and appoint qualified, motivated, and

responsible teams. For its part, the Bank should avoid too rapid staff turnovers.

*The Bank should help the government to identify policy changes that will benefit the poor* without dampening growth prospects, and should select indicators that can be properly monitored. *It should also help the government to improve the quality of its statistical data* and should pay greater attention to the quality of data needed for monitoring progress.

*Bank management, in its response to OED’s report agreed with virtually all the report’s recommendations and found them fully consistent with the strategy set forth in the new Country Assistance Strategy (CAS) for Côte d’Ivoire and the proposed 1997-2000 policy framework paper.*

*The Committee on Development Effectiveness welcomed OED’s report and the opportunity to discuss it in advance of its discussion of a new CAS by the Board of Executive Directors. The Committee noted that there were no fundamental disagreements between regional management and OED, as the proposed strategy for the CAS already addresses the OED report’s key recommendations.*

## Précis

\* Côte d’Ivoire Country Assistance Review, a World Bank Operations Evaluation Study, by Rene Vandendries, forthcoming. Available to Bank Executive Directors and staff from the Internal Documents Unit and from regional information service centers, and to the public from the World Bank InfoShop:

1-202/458-5454

fax 1-202/522-1500

e-mail pic@worldbank.org.

Please address comments and inquiries to the Editor-in-Chief, Elizabeth Campbell-Pagé, tel: 1-202/473-5365, fax: 1-202/522-3125, e-mail: ecampbellpage@worldbank.org

Please address publication requests and inquiries to OED, tel: 1-202/458-4497, fax: 1-202/522-3200, e-mail: eline@worldbank.org

This and other OED publications can be found on the Internet, at <http://www.worldbank.org/html/oed>

**DISCLAIMER** OED *Précis* are produced by the Operations Evaluation Department, Partnerships and Knowledge (OEDPK) of the World Bank. The views here are those of the Operations Evaluation staff and should not be attributed to the World Bank or its affiliated organizations.