What does a qualitative analysis reveal about the reasons for non-compliance with IMF conditionality in PRGF programmes?

A case study of Kenya and Tanzania

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Introduction

Since the Second World War, the International Monetary Fund (IMF) is one of the major players in the field of international economics and international relations. Besides its task to facilitate the functioning of the global economy, one of its main roles is lending to countries in economic problems. However, there have been various critiques on the effectiveness of these lending programmes by the IMF (Vreeland 2006). In many cases it seems that the economic situation of borrowing countries did not improve or even worsened after the implementation of reforms advised by the IMF (Dreher 2004). It is not clear however whether the lack of improvement is due to bad advice by the IMF or because of an incomplete implementation of the reforms (Bird 1998). In order to solve this issue it is necessary to make a distinction between the compliance rate with conditions and the content of those specific conditions. If countries do not comply with a specific condition it is not possible to say anything about the quality of advice that underlies that condition.

However, debate still remains regarding the question why countries do not comply with the conditions imposed by the IMF. Is it because they cannot do so, because conditions are too stringent, or do they not want to comply? Various models have been proposed (Joyce 2003) but it is not yet clear which one has the most explanatory power. In addition, most of the research that has been done relies on cross-country evidence and uses an aggregate index of compliance which does not differentiate between different types of conditions. It is also largely quantitative, employing regression models that consider a variety of mainly economic variables, or standardized factors.[1] While these methods can be very useful, they do not take into account the specific contextual factors that could play a role. Therefore, this paper takes a qualitative approach instead, investigating the research question: What does a qualitative analysis reveal about the reasons for non-compliance with IMF conditionality in PRGF programmes?

To answer this question case studies are used, which are investigated with the method of controlled comparison. The cases that are examined are Tanzania and Kenya, two developing countries in the same region and with a similar colonial history. Both countries were involved in a PRGF programme between 2003 and 2007, but their extent of compliance differed. While it is important to consider the caveat of only two cases, the fact that this is

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[1] For example, there exists a code for democracy or no democracy, but subtleties with regard to the type of democracy are lost

the first paper that does a qualitative analysis of the reports of the programme itself, implies that these cases can nevertheless provide important insights. Moreover, the relevant factors revealed by this analysis are also identified by general theories of compliance,

The rest of the paper is structured as follows. Chapter 1 provides a brief review of the general literature on compliance and discusses the main authors of the literature on compliance with the IMF. It concludes with a description of the methodology and case studies that were used. Chapter 2 provides some background information on the IMF and the PRGF arrangement. Chapters 3 and 4 describe the findings of each case study. These findings are discussed in chapter 5, while the final section concludes by providing a summary, discussing the implications and considering some issues for future research.

1. Literature Review

The literature on compliance within the field of IR is large. It varies from a general perspective on the question why countries adopt and comply with certain rules, to specific studies on the effect of one variable on the level of compliance with a certain agreement. Nevertheless, most of the literature can be roughly divided into two approaches: the rationalist approach and the constructivist approach (Checkel 2001; Risse 2000). Within these approaches, a distinction can be made between scholars that treat a country, or a government as a single unit, and scholars that consider the variety of actors that play a role in the decision-making of governments. Sometimes these latter are treated as a separate approach: the domestic politics approach (Underdal 1998; Simmons 1998, Raustalia 2000). Most literature seems to agree on the fact that domestic politics do have an influence on compliance (Gourevitch 2002: 407, Haas 1997:21), however some authors approach this from a rationalist position and others from a constructivist position.

This section starts by describing the main characteristics of the rationalist and constructivist approach. Subsequently, the most important literature focused on compliance with conditions imposed by International Financial Institutions (IFIs) will be discussed. The section concludes with a description of the methodology used in this thesis.

1.1 The rationalist approach

Regarding the rationalist approach there are two main assumptions: 1) states are rational, interdependent decision-making actors; and 2) options are evaluated only in terms of costs

and benefits (Underdahl 1998, Hurd 1999, Raustalia 2000). These costs and benefits need not be material, they can also be non-material. An example of non-material costs are reputational concerns (Raustalia 2000). With respect to the evaluation of these costs and benefits, Hurd distinguishes between situations of self-restraint, in which the pursuit of self-interest plays a major role, and situations of coercion, in which an external restraint is the reason behind a certain decision (1999: 386). This rationalist problem structure shows why and how many international agreements try to include an incentive or punitive measures for non-compliance (Raustalia 2000: 403).

An advantage of the rationalist approach is its easy applicability to real-life issues and its large explanatory power (Underdahl 1998, Thompson 2002). An important critique to this approach however, is that it assumes that decisions are made by unitary actors, while in reality most decision-makers in international politics are aggregate actors, such as states and international organizations (Killick 1997:488). This implies that it is either assumed that all individual preferences are aggregated into the state's preferences, or that state decision-making is made by a single group (Thompson 2002). This is where the relevance of the literature on domestic politics becomes clear, since this strand of literature aims to explain how the preferences (and consequently decisions) of a state can be clarified, by looking at the domestic (political) situation.

1.2 The constructivist approach

The constructivist approach on the other hand, focuses on the ideational rather than the structural basis of policy. It marginalizes the role of interests and power as the main determinant of compliance. Alternatively, interests and power are considered to be based on ideas and knowledge (Underdahl 1998: 20). Furthermore, this approach considers the social construction of a state's interests: it aims to explain *how* preferences and interests are formed (Ruggie 1998, Raustalia 2000). According to Ruggie (1998), the main contribution of the constructivist approach, lies in its recognition of the influence of ideas through interaction.

Another important characteristic of the constructivist approach is its focus on a process of socialization (Raustalia 2000, Ruggie 1998, Hurd 1999) . Hurd argues that a state may comply with a rule because it considers this rule legitimate. In this case there is no calculation of self-interest but rather a sense of moral obligation. To achieve this perception

of legitimacy, a process of socialization is needed. Hurd describes this process as follows: 'the operative process in legitimization is the internalization by the actor of an external standard'(1999: 388). Checkel's work (1997, 2001,2005) also focuses on this concept of socialization. He argues that compliance with international norms can sometimes be explained as a rational choice, but in later stages often becomes embedded in the identity of decision-makers. From this perspective, the rationalist and constructivist approach can be distinguished based on their underlying logic. Rationalism uses a logic of consequences, while the constructivist approach assumes a logic of appropriateness (Checkel 1998, Fearon and Wendt 2002). Checkel's process of socialization incorporates aspects from both approaches, and thereby decreases the ideational gap between the two. He aims to synthesize the different methods, arguing they both offer valuable insights (1998: 488).

Checkel is not the only scholar that aims to combine both approaches. It is increasingly recognized that the approaches need not be mutually exclusive, but are complementary to each other (Fearon and Wendt 2002, Simmons 1998). The different approaches focus on different aspects of the compliance problem. This implies that their insights can be combined to improve our understanding of compliance (Underdal 1998: 23).

1.3 Compliance imposed by IFIs

The previous scholars examined compliance with international rules in general. Since this paper deals with compliance with conditions imposed by the IMF, this section discusses the literature that specifically focuses on compliance with conditions imposed by IFIs.

The majority of the literature investigating conditionality of the IFIs, aims to explain why states do or do not comply with conditions they initially agreed with (Bird 1998, 2002, Killick 1997, Simmons 2000). Bird and Killick both take a rationalist approach, focusing on the costs and benefits of (non)compliance as the main determinant for the decision to comply or not. They underline the importance of ownership: the larger the degree of ownership, the smaller the gap between the preferred policy of the borrowing government and the preference of the IFI (Bird 1998: 104). The same argument is made by Mayer and Mourmouras, who point out that ownership need not only refer to willingness to carry out reforms, but can also refer to the capacity and political ability to do so (2008: 117). Bird also points out the time-inconsistency problem of conditionality: most benefits of an IMF programme come with the announcement, while most costs occur during implementation

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(Bird 1998: 104). Often the amount of costs only becomes clear when reforms are implemented, meaning non-compliance does not have to be on purpose (1998: 105). To improve compliance, Bird and Killick both argue that stronger incentives ánd punishments are needed.

Simmons argues that international rules 'do alter governments' interests in compliant behavior' (2000: 819) and finds that reputational concerns are a major explanatory factor of compliance. She identifies regional standards of behavior regarding compliance, and explains how these regional standards alter the costs of non-compliance: 'non-compliance is much less costly for a particular government if many others are also in violation' (ibid:822). Her explanation describes a rational socialization process, combining insights from both rationalism and constructivism.

While the above-mentioned scholars do take into account the importance of the domestic political situation, Dreher (2003a, 2004) goes a step further by looking at the influence of IMF programmes on elections in borrowing countries. He finds that governments that complete an IMF programme twelve months before elections take place, in most cases increases their probability of re-election, but that this probability decreases if GDP growth is rising.

Besides articles that aim to explain (non)compliance, there is an interesting range of articles that investigates whether IMF programmes have a catalytic effect on the inflow of private capital (Edwards 2005, Jensen 2004, Bird and Rowlands 2002). This is an important issue since the IMF claims that the conditionality of its borrowing programmes have catalytic effects (Edwards 2005). This would mean that countries that are borrowing from the IMF are more likely to receive inflows of capital, in the form of foreign direct investment (FDI). The empirical evidence is mixed however. Bird and Rowlands review a range of empirical evidence and conclude that it is difficult to say whether an IMF programme will have a positive, negative or insignificant result (2002). Of course, it also depends on how one looks at it. Edwards finds evidence which suggests that an average state which is involved in an IMF programme experiences less outflow of portfolio investment than similar states which are not involved (2005:863). Jensen (2004) on the other hand, looks at capital inflows and

finds that countries that sign an agreement with the IMF attract 25% less FDI inflows than countries that do not sign an agreement.[2] Comparing the starting point of both scholars, Edwards point is that similar countries are less worse off under an IMF programme than those that are not. Jensen on the other hand, points out that the claim by the IMF that signing an agreement with the IMF leads to more capital inflow, is incorrect.

Finally, there are a number of scholars presenting evidence of US influence on IMF programmes (Steinwand and Stone 2008, Dreher 2007, Stone 2007). More specifically, they find evidence of US influence on the number of conditions imposed on borrower countries. Stone also finds evidence that countries who receive US aid are more likely to be offered a programme (2008: 616). These are important findings, because they call into question the independence and autonomy of the IMF.

To conclude a few observations can be made. First of all, it is clear that although the general theories of compliance seem to move away from an exclusive rationalist approach, most of the empirical research employed in these articles still makes use of rationalist frameworks. This is consistent with Ruggie's observation upon the applicability of this approach (1998). Furthermore, almost all scholars now acknowledge the important role the domestic (political) situation plays in compliance. Finally, most research is quantitative rather than qualitative: almost all scholars employ regression models that make use of panel data and focus on economic variables. This might be a logical consequence of the first point.

1.4 Methodology

As the previous section described, most research that has been done so far, is of a quantitative rather than qualitative nature. However, qualitative research allows for analysing both the 'visible' factors and the invisible ones. The relation between a borrowing country and the IMF for instance, would not easily emerge from numbers, but by analysing the tone of correspondence and reports, one can identify how this might influence the choice for (non)compliance. In quantitative research, that is mostly using regression models and large panel-data, it is necessary to predetermine the variables one wants to investigate. Considering that there is not yet a full theory of (non)compliance, it is useful to start with

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[2] Both scholars control for factors that lead countries to seek IMF support.

inductive research, using existing primary sources to find out which factors are most important. Moreover, regression models usually do not allow to take into account specific local political circumstances, while all existing literature agrees on the importance of these. Therefore, this thesis uses case studies to develop an explanation of the reasons for (non)compliance. According to van Evera, case studies are better at explaining how an independent variable causes the dependent variable to change (1997:54). Furthermore, a case study offers the possibility to do a deep qualitative analysis of the complex processes at work: 'Case studies are one of the best bridges from rich qualitative evidence to mainstream deductive research.' (Eisenhard & Graebner 2007:25). The case studies of this paper consist of two countries, Kenya and Tanzania. These countries were chosen because they were both involved in a PRGF programme during the period 2003-2007, but with a different extent of compliance. To limit the number of external factors that could influence (non)compliance, the countries that were chosen have a similar colonial history and lie in the same region.

The case studies will be investigated using the method of controlled comparison, more specifically structured focused comparison. This method uses the commonly known method of difference, but emphasizes the importance of structuring the investigation of each case study. The structuring can be achieved by formulating a range of standardized general questions to direct the examination of each case (George and McKeon 1985: 42).

The main source for the analysis are the official reviews of the PRGF programmes, written by the borrowing governments and the staff of the IMF. In addition, the discussion refers to some policy documents of the borrowing countries themselves, to support the results of the analysis based on the IMF documents. These sources are all listed in the references.

2. The IMF and the PRGF

2.1 The IMF
The IMF was established in 1945 as a framework for international economic cooperation. It was designed to prevent a repetition of the economic policies that led to the Great Depression during the 1930s. On the official website the objectives of the IMF are described as follows:

'The International Monetary Fund (IMF) is an organization of 188 countries, working to foster global monetary cooperation, secure financial stability, facilitate international trade, promote high employment and sustainable economic growth, and reduce poverty around the world.'

There have been various critiques on the IMF during its entire existence. Many of the initial critiques are still here today. One of the oldest critiques focuses on the extent of autonomy of the IMF. These critics argue that the Fund should not be considered an autonomous institution but instead represents the interests of the most powerful states (Stone 2008:592). This view is based on the way decision-making within the IMF is organized. Every member country is assigned a quota which reflects the size of its economy relative to other member countries. These quota then determine how much voting power a member country gets, as well as the maximum amount they can borrow and access to other IMF services.[3] Effectively, this means that richer countries have more influence on IMF policies than poorer countries and thereby the governance structure can be said to simply reflect the distribution of power (Krasner 1985). The IMF itself is clearly aware of the implications of this way of governance. Recently the Fund decided to rebalance the assignment of quotas in order to make sure that these reflect their actual size in the world economy. Furthermore, the number of basic votes was increased to ensure some level of participation in the decision-making by poorer countries (IMF 2013a)

A second critique concerns the soundness of its policy advice. It is argued that the IMF prescribes the same policy to a variety of countries which find themselves in very different contexts (Stiglitz 2002, Feldstein 1998: 29). This often results in disappointing results, not only in terms of economic recovery but also in terms of increasing poverty (Stiglitz 2002). Furthermore, a third critique focuses on the way specific (liberal) economic policies are imposed on countries with functioning democratic governments (Feldstein 1998: 28). Finally, critics point out that the excessive use of conditionality in IMF borrowing progress does not contribute to, and could even hinder economic growth (Goldstein 2001: 9). This last critique has been recognized by the IMF itself as well, by introducing an initiative to streamline conditionality (Stone 2008: 598).

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[3] An example is the share in allocation of special drawing rights: a reserve currency created by the IMF

2.2 The Poverty Reduction and Growth Facility (PRGF)

The PRGF was established in November 1999, to replace the Enhanced Structural Adjustment Facility (ESAF), as a means to prioritise the objectives of poverty reduction and economic growth in the provision of loans to the poorest member countries. Therefore, lending programmes under the PRGF are designed around Poverty Reduction Strategy Papers (PRSPs) in which a country describes its long-term strategy and policies to reduce poverty. PRSPs are created by the government of a specific country, but the government is required to use a participatory approach in which both domestic stakeholders and external development partners take place. Moreover, the IMF and World Bank always respond to a PRSP (progress report) with a Joint Staff Advisory Note (JSAN) in which they provide feedback on the strengths and weaknesses of the outlined strategy and propose recommendations. This way they can influence the proposed strategies to some extent.

A request for a loan under the PRGF is submitted by a country's government along with a Letter of Intent (LoI), and a Memorandum of Economic and Financial Policies (MEFP) which describes the policies to be implemented under the programme. The MEFP also includes quantitative and structural performance criteria, indicative targets (quantitative) and structural benchmarks, which are set after consultations between the country's authorities and the IMF. Performance criteria need to be met in order to complete a review and thus the disbursement of a subsequent tranche of the loan. If a performance criterion is not met, a formal waiver needs to be requested to the Executive Board of the IMF to enable completion of the review. Generally, the IMF states it will only grant waivers if the deviation is small or temporary, or if the government has taken or is planning to take adjusting measures (IMF 2013b) Indicative targets and structural benchmarks are used to assess overall performance, but do not require official waivers if they are not observed. Finally, it should be noted that loans under the PRGF are expressed in terms of Special Drawing Rights (SDR). SDR is an international reserve asset created by the IMF, whose value is based on four international currencies. SDR can be exchanged for any usable currency of an IMF member.

3. Case study 1: Tanzania

3.1 Political background and relations with the Fund

The United Republic of Tanzania was formed on April 26, 1964 when the former British Mandate Tanganyika and Zanzibar were united. Tanzania is a democracy but is generally considered as a one-party dominant system (Magaloni and Kricheli 2010, Morse 2013). This implies that there is an opposition which participates in elections but that it is highly unlikely that a different party than the ruling one will win (Magaloni and Kricheli: 124). The ruling party in Tanzania has been the Chama Cha Mapinduzi (CCM) since 1995. Observers do not consider the CCM openly authoritarian, but instead attribute its consistent hegemony to its strong party structure which effectively maintains the loyalty of the elite (Morse 2013: 8). Furthermore, it is important to know that Zanzibar is a semi-autonomous part of Tanzania, meaning it has its own government. In the context of IMF programmes, the IMF therefore sometimes holds consultations with the Zanzibarian authorities separately.

Tanzania became a member of the IMF in 1962, when it gained its independence from Britain.[4] Between 1962 and 2003, the year in which they requested the PRGF arrangement that is the subject of this research, they were involved in three earlier financial arrangements: the Enhanced Structural Adjustment Facility (ESAF) in the period 1991-1994; and in two consecutive PRGF programmes, between 1996 and 2000. While the ESAF programme was not very successful, considering that less than 50% of the loan was disbursed, the PRGF loans were almost completely disbursed and thus imply a relatively large compliance with the conditionality.

3.2 The PRGF arrangement 2003-2006

Tanzania requested a new arrangement under the PRGF programme in August 2003. The government applied for a new loan to continue the economic progress, in order to reduce the still widely spread poverty. Furthermore, the planned reforms are considered to be in the area of expertise of the Fund and the approval of the Fund of new loan disbursements is considered important to attract other donors. They opt for a low access arrangement (10% of quota), to signal the improved position of the country and to emphasize the progress towards exiting the PRGF (IMF country report 3/238). The request, of 14 million SDR, is

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[4] At the moment of entrance to the IMF Tanzania was still called Tanganyika

approved by the Executive Board of the IMF on the 28th of July, and the arrangement became effective on August 16, 2003.

Table 1:

Review	# of spc	# of spc met	# of sbm	# of sbm met	Qpc
1) February 2004	3	2	5	3	All met
2)July 2004	3	3	4	4	All met
3)February 2005	2	1	5	5	One not met
4)July 2005	3	2	6	6	All met
5)March 2006	1	1	6	5	All met
6)November 2006	1	1	5	2	All met
All	13	10	31	25	

Table 1 is compiled from tables in the appendices of the six PRGF reviews of Tanzania, that list the various structural performance criteria, structural benchmarks and quantitative performance criteria and the extent to which they were met. It provides a general overview of the extent of compliance of Tanzania. It shows that most of the structural performance criteria were met, as well as most of the structural benchmarks and the quantitative performance criteria. However, since numbers only do not provide an explanation, the next section analyses the reviews in more depth. The guiding questions during the analysis are the following: what kind of conditions did Tanzania have, and is there a pattern regarding the type which they did not comply with? What reasons do the authorities give for the non-observance of a specific structural performance criteria? How does the staff from the IMF respond to their explanation? What other factors could play a role in the extent of compliance?

3.2.1 Type of conditions

Structural conditionality in this PRGF programme focuses on the areas of tax policy and administration, financial sector reform and governance. Quantitative indicative targets and performance criteria concern the non-accumulation of arrears, limiting the domestic financing to the Tanzanian government and a minimum requirement for international

reserves of the bank of Tanzania. Performance criteria that were not met, include: the submission to Parliament of a new income tax law (first review), a minimum requirement of international reserves (third review), and the submission to Parliament of an amendment to banking acts (third and fourth review).[5] Given the small number of observations, there does not evolve a general pattern: the first criterion falls in the area of tax policy, the second is a macro-economic stability variable and the last one can be placed within the area of financial sector reform. However, all non-observed performance criteria were delayed, that is the required measures were implemented, but not within the time schedule that was set.

Structural benchmarks that were not met concern the licensing of a company for an export processing zone (EPZ, review 1) and the cabinet approval of a new anti-corruption law (review 5). All other structural benchmarks were met, although some with delay. In the final review, the three benchmarks that were not met, were included as new benchmarks for a Policy Support Instrument (PSI).

3.2.2 Explanations for non-observance by the Tanzanian and the reaction of the IMF

In the reviews, the explanations of the Tanzanian authorities and the comments of the IMF staff are clearly distinguished. With respect to the explanations that were given by the Tanzanian authorities for the non-observance of conditions, similarities can be found. The non-observance of the structural performance criteria and structural benchmarks, were all but one attributed to the need for more consultations with stakeholders(country report 04/58: 29-30, country report 05/181:46). More specifically, to conclude the structural performance criterion on the submission to Parliament of an amendment to banking acts, that was not met twice, the Tanzanian government needed more time to conclude discussions with the Zanzibar authorities(country report 05/181:46, country report 05/291:33).

Regarding the reaction of the IMF staff, no problem is made out of the non-observance of a structural performance criterion, but the staff rather 'expressed its understanding for the need to give parliament adequate time for consideration.' (country report 04/58: 8) Sometimes they even appraise 'the authorities commitment to full consultation with key stakeholders' (country report 05/181:19).

The one structural benchmark whose non-observance was not attributed to the need

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[5] In the third review a modification of this structural performance criteria was requested, in the fourth review the authorities requested a waiver because of a (second) delay

for longer consultations, concerns the licensing of a company for an Export Processing Zone (EPZ) that would export to countries under the South-African Development Community Agreement (SADC) and thereby does not meet the earlier set requirement that only firms exporting under the African Growth and Opportunity Act (AGOA) and Everything But Arms (EBA) are allowed this special treatment. The Tanzanian authorities defend this decision by arguing that the goal of the EPZs is to strengthen Tanzania's export performance and that the existence of other preferential trade agreements creates an opportunity to enhance the effect of EPZs (country report 04/58:9). The IMF staff accepts this decision, but underlines the importance of the authorities' commitment to only license companies that export all of their output to prevent unfair competition on the domestic market (ibid.)

What is interesting about this example, is that it reveals some of the interests at stake. Initially the IMF set the condition that only companies exporting to Europe or the US are allowed to make use of an EPZ (in which taxes are substantially lower). However, Tanzania rightly points out the advantages of exporting to other African countries with which it has a preferential trade agreement.

Finally, the one quantitative performance criterion that was not observed concerns a minimum requirement of net international reserves. The authorities explain that this was caused by one-off external payments and foreign exchange sales that were higher than budgeted. The one-off external payments include construction costs of the Bank of Tanzania (BoT) and the buying of debt on behalf of TANESCO[6] by the government, to decrease TANESCO's operating costs. The higher foreign exchange sales were mainly a result of higher oil prices (country report 05/181:34). Again, the authorities of the IMF do not make any problem out of this. They underscore the fact that the shortfall in reserves was temporary and that the overall position of Tanzania remained strong (country report 05/181:7).

3.2.3 Other explanatory factors

While the above explanations were provided by the Tanzanian authorities themselves, one can also reveal some other factors that play a role in the decision to comply. One of the most obvious ones is the influence of donors, which is mentioned in five of the six reports, both by

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[6] TANESCO is the Tanzania Electric Supply Company, this company relies largely on hydropower and is consequently very vulnerable to droughts: to ensure continued access to electricity, the operating costs needed to be decreased

the Tanzanian government and the IMF staff.[7] In the second review for instance, it becomes clear that some donors were delaying the process of the elimination of tax exemptions (country report 04/285:12). In the same review, the Tanzanian government underlines that donors requested higher expenditures, something which the IMF is opposed to (ibid:13). The relevance of this factor also becomes clear from a Tanzanian evaluation report, in which a strong emphasis is placed on the importance of harmonization of aid programmes ('Tanzania's experience in aid coordination, harmonization and alignment' 2004).

A second important factor is the Multilateral Debt Initiative (MDRI), which is granted by the IMF to Tanzania during the fifth review. Obviously, good performance during other IMF programmes enhances the chances of receiving debt relief. Considering that the MDRI mentioned above consists of a debt relief of 336 million US dollars, this clearly represents an extra incentive for high compliance.

A third factor for non-compliance, or delayed compliance, could be the lack of consequences of non-compliance. In Tanzania's case, the IMF staff proved to be very flexible and understanding, especially if the delay was explained to be caused by longer consultations with stakeholders.

4. Case study 2: Kenya

4.1 Political background and relations with the Fund

The Kenya African National Union (KANU) has been the ruling party from the first elections for African representatives in the British government, until 2002. Between 1963 and 1992, Kenya was officially a one-party state, until pressures from donors led to the establishment of multiparty elections in 1992 (Grosh and Orvis 1996: 51). Nevertheless, the KANU remained in power until the elections of 2002, which were won by the National Alliance of Rainbow Coalition (NARC), a coalition of two political parties. Between 2002 and 2007, the period in which the PRGF loan of this analysis was provided, the government was formed by the NARC for the first time. Generally, the political parties in Kenya are considered to be institutionally weak as a result of poor societal linkages, a lack of effective programmes and a lack of a clear ideology or vision (Mwangi 2008: 269). This results in a competition between the political parties, based mainly on ethnocentric feelings (ibid.). Furthermore, at least until

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[7] Country report 05/58:44, country report 04/285:10, country report 05/181: 17, country report 05/291:14, country report 07/138:5

2008, corruption played a significant role in both party and general elections. Campaign funds were raised through government expenditures that were channeled through fictitious companies, such as Anglo-Leasing (ibid.:276).

Kenya joined the IMF in 1964, shortly after the country gained independence from Britain in 1963. Previous to the PRGF arrangement that is analysed here, Kenya was involved in four earlier arrangements with the IMF. These involved three ESAF programmes and one PRGF programme. While the first two programmes were relatively successful, in terms of their nearly full disbursement, the last two loans were less successful, considering that only 20% of the loans were disbursed. This implies that the Kenyan authorities were not very successful in terms of implementing the reform policies as required by the IMF.

4.2 The PRGF arrangement 2003-2007

In November 2003, Kenya requested a new loan of 175 million SDR under the PRGF arrangement. The loan is requested to support the implementation of a range of structural reforms that will enable the government to attain its poverty reduction objectives. Furthermore, the poverty reduction strategy designed by the Kenyan government required an increase in donor funds. The authorities expect that the combination of policy reforms, improvements in governance and a coherent poverty reduction programme supported by the IMF, will help to attract sufficient donor assistance (country report 03/399:5).

Table 2:

Review	# of spc	# of spc met	# of sbm	# of sbm met	qpc
1)December 2004	5	2	7	2	Two not met
2)March 2007	7	2	6	4	Two not met
3)November 2007	<u>6</u>	<u>4</u>	<u>9</u>	<u>4</u>	<u>Two not met</u>
All	18	8	22	10	

Table 2 above was compiled in the same way as table 1, using information from tables in the appendices of the PRGF reviews of Kenya. It clearly exhibits some differences with the table

of Tanzania. Not only does Kenya perform structurally worse in terms of compliance, it also appears immediately that Kenya only concluded three reviews instead of six. This last point is especially interesting, because Kenya did draw almost the full amount of the loan: 150 million of the 175 that it was entitled to. However, before discussing the reasons for this occurrence and the implications it could have, the following section first summarises the main findings regarding the type of conditionality and the extent of compliance.

4.2.1 Type of conditions

Structural conditionality for Kenya included measures in the area of governance, financial sector reform , fiscal issues and private sector development, with a strong focus on governance. Quantitative conditionality concerns the non-accumulation of arrears, a maximum amount spent on government wages, no newly contracted debt by the government or the Central Bank of Kenya (CBK) and maximum changes in reserve money and net foreign assets. Of the ten structural performance criteria that were not met, four were in the area of financial sector reform[8], three in the area of governance[9], and the remaining three concerned fiscal issues.[10]

Quantitative performance criteria that were not observed are: the limiting of contracting non-concessional long term external debt (once), the maximum change in reserve money of the CBK (in two of the three reviews) and the non-accumulation of external arrears (in all three reviews). The structural benchmarks that were not met, were more or less evenly spread among all areas, no pattern could be distinguished.

Although Kenya clearly has a lower overall level of compliance, it did implement most of the measures required by the structural performance criteria, however later than planned. Moreover, they sometimes adjusted the measure from the initial agreement. An example is the wealth declarations of public officials, to which the public only gets restricted access instead of open access. A difference between the conditionality for Kenya and Tanzania is that some of the missed structural performance criteria were changed into prior

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[8] Specifically: Submission to parliament of a banking act amendment bill; no imposition of controls by the government on the determination by commercial bank fees, charges or interest rates (twice); Submit to cabinet for approval a strategy to initiate the sale of GoK and NSSF's share in NBK
[9] Specifically: Complete verification of the asset declarations of ministers and senior officials; Complete asset declaration of ministers, permanent secretaries and heads of state bodies; Issuances of new guidelines for wage arbitration by the Industrial Court
[10] Specifically: completion of an audit on the financial position of the National Social Security Fund; Finalize an audit of the stock of pending bills; make the Public Procurement Oversight Authority fully operational

actions for Kenya. A prior action implies that these actions have to be taken before the programme can be continued. Also remarkable is the fact that Kenya manages to defer from the same quantitative performance criterion twice or even three times. This will be discussed more in depth later.

4.2.2 Explanations for non-observance and the reaction of the IMF

Unlike Tanzania, the Kenyan government does not provide explicit explanations for the non-observance of each separate structural performance criterion. Instead, the Kenyan authorities describe the corrective measures they are taking to fulfill the requirements later (country report 09/225: 41, country report 09/137: 58, country report: 09/18:7). In the first review, they also provide a very general explanation: 'progress in implementing some key economic reforms has been impeded by the large amount of time devoted to constitutional reform, capacity constraints in key ministries and the slow resumption of donor budgetary assistance' (country report 09/225: 43).

The non-observance of one quantitative performance criterion that is specifically explained by the Kenyan authorities is the non-accumulation of external arrears. This criterion has been breached in all reviews because of 'a suspension of payments due to an audit of all central government contracts of commercial external debt' (country report 09/225:41). This audit was caused by the Anglo-Leasing scandal, leading to disputes about the necessity to pay a number of specific contracts that were considered fraudulent.

Looking at the reaction of the IMF staff, this does not show any serious concerns about the low rate of compliance. The IMF staff simply describes the performance criteria that have not been met and the remedial arrangements that are set up to correct this. Despite the low level of compliance, they support completion of the review and extension of the programme (country report 09/137: 4).

4.2.3 Other explanatory factors

Although it is not put forward as a reason for non-compliance, it becomes clear that privatization remains a controversial issue among the Kenyan public and its parliamentarians (country report 09/225:17). While the Kenyan government assures the IMF that it is committed to privatization and enterprise reform, it also explains that parliamentary support needs to be built for the reforms to take place. With respect to the privatization of public banks, the Kenyan authorities are especially careful, indicating 'that sales of banks to

multinationals reduced banking service penetration to rural communities and disadvantaged groups' (ibid: 18). This suggests that the Kenyan government does not actually want to implement these measures and thereby points to a lack of ownership about the IMF programme as a reason for non-compliance.

In addition, and similar to Tanzania, the factor of debt relief can also be found to play a role in the level of compliance in Kenya's case. While Kenya was not eligible for the HIPC or MDRI, involvement in the PRGF enabled them to attain debt rescheduling from the Paris Club. This point comes up in the second review (country report 09/137:23). Since this concerns an amount of 402 million US dollar, this obviously represents an incentive to request a PRGF.

Finally, the consequences of non-compliance are likely to play a role. In the case of Kenya, it is apparent that non-compliance can have consequences: the completion of first review of the PRGF arrangement of Kenya was delayed because a structural benchmark was not met. This is remarkable, considering that usually non-compliance with a structural benchmark is less important than non-compliance with a structural performance criterion, but in this case the non-observance of a structural performance criterion was not a problem for completion of the review, while the structural benchmark was. The problem here is thus that because the IMF is inconsistent in the application of its own rules, it becomes easier to not comply with all of them. This way, the IMF allows to stay involved in a PRGF arrangement as long as some steps in the right direction are observed. In fact, the IMF even approves an augmentation of the loan, because of an increase in oil prices and drought. This way the Kenyan authorities manage to bend the rules as is most suitable to them and reduce the costs of completing the first review later: in the end they still receive an amount of 50 million SDR over the first year.

Similarly, the second review is also delayed, and completed almost two years after the second review. It is remarkable that the IMF staff does not explicitly comment on this, the only reason mentioned for the delay by the IMF staff is the existence of governance concerns (country report 09/137:20). This time the Kenyan authorities request a reduction in access and extension of the arrangement, both of which are granted by the IMF. Again, the Kenyan government appears to be able to bend the rules as is most suitable for them. In the end this means that they managed to obtain 150 million SDR (85% of the approved amount of 175 million SDR), even though only three of the six required reviews were completed.

5. Discussion

Returning to the research question again, what did this qualitative analysis reveal about the reasons for non-compliance with conditions in PRGF programmes? In the comparison of the two cases, some factors stand out. Firstly, as was already discussed before, the reviews show that one of the most important reasons for non-compliance is a longer discussion with stakeholders (Tanzania) or more strongly, the failure to achieve consensus within the government and parliament on the measures required to be taken. Kenya in particular, makes it very clear that for instance the privatization of state-owned companies, is still a very controversial issue in the public opinion and in parliament. This could imply that the Kenyan government does not actually want to implement such measures, but has agreed with them in order to obtain the loan. In this respect, it is also important to take into account the domestic political situation. Tanzania's government has to deal with a weaker opposition than Kenya. In addition, the Kenyan government is brand new and might want to prove that it does not take every advice the IMF provides. The Tanzanian government on the other hand, also seems less opposed to the reform measures, considering the fact that they opt for a PSI after the completion of the PRGF. This implies that they continue their reform measures in cooperation with the IMF, without receiving any loans. Another factor that suggests they are less opposed to IMF reforms, is the fact that they opt for a low access loan, meaning they do not receive much money in exchange for the implementation of reforms.

The whole discussion above, relates to the willingness of the government to comply with conditionality and more generally to the literature on the importance of ownership. This concept proves to be a very relevant issue. In the Kenya case, it became evident that some laws that were controversial were eventually implemented, but were not followed in practice. In such a case, compliance with conditionality is a farce. One could argue that Tanzania is already in a process of socialization as described by Checkel. Tanzania seems to be willing to embed liberal economic principles in its policies, whereas Kenya remains strongly opposed to these principles.

This argument about ownership is also supported by documents from the borrowing countries themselves. The IMF conditions for Tanzania's loan were reflected in later policy documents and reports, such as the new income tax law on the website of Tanzania's

ministry of finance[11] and a corruption evaluation report from the department of Research, Control and Statistics ('The incidences of corruption in the land sector' 2005). For Kenya on the other hand, the IMF reforms were not clearly exhibited in later policy documents. In the 'Kenya Vision 2030' (2007) for example, the main Kenyan planning strategy document, the privatization of state-owned firms or the fight against corruption is not mentioned at all. This is quite remarkable, since these were two main issues in the IMF conditionality for Kenya's PRGF loan.

A second point which becomes very clear, is the importance of donors. Both countries explicitly state that they need the approval of the IMF to obtain more donor funds. However, in the case of Tanzania it also becomes apparent how much influence donors can have on the decision-making process as well as on the allocation of additional funds. One specific case even suggested that donors had delayed the implementation of a new tax exemption law in Tanzania. This way they also were a factor in non-compliance. Again, this point also becomes evident from a Tanzanian evaluation report ('Tanzania's experience in aid coordination, harmonization and alignment' 2004).

A third point concerns the granting of debt relief. While Tanzania, manages to attain cancellation of a large part of its outstanding debt, under both the HIPC and MDRI programmes, Kenya uses the PRGF programme to reschedule its debt with the Paris club.

These latter two points can be related to the literature on 'catalytic effects ' that was briefly discussed in the literature review. The difference is that most of this literature focuses on the catalytic effects with respect to investment flows, while the reviews show that these countries focus more on increased aid grants and debt relief. This is meaningful, since it reveals how strongly the PRGF programmes are related to aid dependency, instead of private capital as the IMF would probably prefer. Furthermore, the importance that both countries attribute to additional donor funds and debt relief, means that these two factors might represent larger benefits than the value of the IMF loan itself.

Finally, the fact that non-compliance does not always have consequences for the continuation of a programme is likely to be a significant factor. The case of Kenya exhibited that the Kenyan authorities managed to renegotiate the programme more than once and that the IMF is not consistent in the enforcement of its own rules. Knowing this, a

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[11]See: http://www.mof.go.tz/index.php?option=com_content&view=article&id=39&Itemid=54

government can consider which measures it wants to implement to keep the programme running, while defaulting or delaying on other ones.

So how does the above discussion relate to the general debate between rationalist and constructivist arguments? First of all, the relevance of rationalist theories becomes apparent from the importance of costs and benefits related to compliance. Higher aid flows and more debt relief clearly represent benefits of the involvement in an IMF programme. Also, the lack of strict consequences for non-compliance represent low costs for countries that do not comply. What is interesting with respect to the first observation though, is that these benefits are not always directly related to the extent of compliance itself. For debt relief in particular, it can be enough to be involved in an IMF programme, regardless the level of compliance. Donor funds seem to be more responsive to the level of compliance, considering the fact that Kenya does receive less donor funding than Tanzania.

The importance of a constructivist perspective becomes apparent in the process of socialization that can be distinguished in the case of Tanzania. It seems to be the case that the level of ownership is larger in Tanzania than in Kenya, or at least that the level of opposition to reforms is lower in Tanzania. This way, one could argue that the constructivist perspective explains *why* compliance for Tanzania is higher than for Kenya, while the rationalist perspective explains *how* this is possible. While the first points out factors that explain why Tanzania chooses to comply and Kenya does not, the latter underscores how these differences in compliance are facilitated. Furthermore, the constructivist perspective identifies political preferences as a main determinant for compliance, while the rationalist perspective focuses on the costs and benefits that are determined by these preferences. If a government's political preferences differ substantially from those of the reform agenda, the (nonmaterial) costs of compliance tend to be higher than the benefits. Finally, the costs of non-compliance are not high enough to punish low compliance, while benefits can be obtained without full compliance.

Conclusion

Emerging from the discussion on the impact and effectiveness of IMF lending programs, this thesis showed what a qualitative analysis reveals about the reasons for non-compliance with conditionality in PRGF programmes. It started with a description of the general debate on compliance between rationalist and constructivist scholars, of which the importance of domestic politics became clear. In contrast to most existing studies, this paper took a qualitative approach, using case studies and the method of controlled comparison. Factors like the domestic political situation, donor funds, debt relief and the lack of consequences for non-compliance are found to play an important role in the extent of compliance as well as the decision to get involved in an IMF programme. The difference in compliance between Tanzania and Kenya is traced to the extent of ownership that both countries reveal. In this respect, the concept of socialization as argued by Checkel proved relevant. With respect to the general rationalist-constructivist debate, this paper argues that constructivist arguments are more relevant at explaining why countries do not comply, while rationalist arguments put forward the framework that makes non-compliance possible. This is consistent with the view of other scholars that both approaches are complementary to each other, rather than mutually exclusive.

What do these results imply? From a pure functional point of view, this study shows that higher benefits from compliance, as well as higher costs for non-compliance, are needed to enforce compliance with conditionality. However, this paper also provided some examples where compliance did not mean enforcement of a specific reform. In the case of Kenya, a conditionality was complied with on paper, but in practice the measures were not implemented. In such cases, the importance of ownership comes back into the discussion. If programmes that are not sufficiently owned by the borrowing government are carried out anyway, conditionality does not prevent countries to defer from the structural reforms. Therefore, it might be useful to call into question the aim of the IMF to spread and impose specific liberal economic principles among all its members. Not only because the uniform applicability of these principles is contested, but also because evidence shows that it is not possible to enforce such reforms upon countries that have other preferences.

To conclude, some suggestions for further research are appropriate. First of all, more qualitative research is needed to test for the relevance of qualitative variables such as ownership and donor influence. Secondly, the (lack of) consequences for non-compliance

needs to be verified with other cases in order to determine the possible impact this has on the extent of non-compliance. Finally, in light of the increase in lending programmes to developed countries due to the economic crisis, it would be interesting to investigate whether there are differences in the extent of compliance between different IMF programmes.

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List of abbreviations

AGOA – African Growth and Opportunity Act

BoT – Bank of Tanzania

CBK – Central Bank of Kenya

CCM - Chama Cha Mapinduzi (ruling political party in Tanzania)

EBA – Everything But Arms

EPZ – Export Processing Zone

ESAF – Enhanced Structural Adjustment Facility

FDI – Foreign Direct Investment

HIPC – Heavily Indebted Poor Countries

IFI – International Financial Institutions (the IMF and the World Bank)

IMF – International Monetary Fund

JSAN – Joint Staff Advisory Note

KANU – Kenyan African National Union

LoI – Letter of Intent

MDRI – Multilateral Debt Relief Initiative

MEFP – Memorandum of Economic and Financial Policies

NARC - National Alliance of Rainbow Coalition

PRGF – Poverty Reduction and Growth Facility

PRSP –Poverty Reduction Strategy Paper

PSI – Policy Support Instrument

SADC - South-African Development Community Agreement

SDR – Special Drawing Rights

TANESCO – TANzania Electric Supply COmpany