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Staff Country Reports

Republic of Tajikistan: Joint Staff Assessment of the Poverty Reduction Strategy Paper Progress Report

The attached Joint Staff Assessment (JSA) of the Poverty Reduction Strategy Paper Progress Report for the **Republic of Tajikistan**, prepared by the staffs of both the World Bank and IMF, was submitted with the member country's Poverty Reduction Strategy Paper (PRSP) or Interim PRSP (IPRSP) to the Executive Boards of the two institutions. A JSA evaluates the strengths and weaknesses of a country's poverty reduction objectives and strategies, and considers whether the PRSP or IPRSP provides a sound basis for concessional assistance from the Bank and Fund, as well as for debt relief under the Enhanced Heavily Indebted Poor Countries (HIPC) Debt Initiative. The Boards then decide whether the poverty reduction strategy merits such support.

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THE INTERNATIONAL MONETARY FUND
AND THE INTERNATIONAL DEVELOPMENT ASSOCIATION

REPUBLIC OF TAJIKISTAN

**Joint Staff Assessment of the Poverty Reduction Strategy Paper
Annual Progress Report**

Prepared by the staffs of the International Monetary Fund
And the International Development Association

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I. OVERVIEW

1. The Government of Tajikistan has completed and submitted the “PRSP Progress Report for 2003” (hereafter referred to as “the report”) to the Boards of the International Monetary Fund (IMF) and the International Development Association (IDA). The Poverty Reduction Strategy Paper (PRSP) was approved by the Boards of the IMF and the IDA in 2002. The first Joint Staff Assessment (JSA) stressed the importance of prudent macroeconomic management and acceleration of structural reforms for sustainable growth. Additionally, the JSA called for the inclusion of detailed costing of social and sectoral programs consistent with the medium-term expenditure framework, prioritization of expenditures in light of the high external debt burden and limited absorptive capacity, and improving monitoring and evaluation of the PRSP. These shortcomings were reiterated at the CG meeting in Dushanbe, in May 2003 and its follow-up meeting in London in February 2004.

2. The report presents the most recent poverty diagnosis based on the 2003 Tajikistan Living Standards Survey (TLSS) and a candid assessment of progress achieved in the first year of implementing the PRSP, and highlights key obstacles to policy implementation. The Government has taken steps in addressing the weaknesses of the PRSP, including re-prioritizing the externally financed public investment program (PIP) to reflect concerns about health and education spending, and improving monitoring and evaluation. Nevertheless, some issues remain to be addressed; these include detailed costing and prioritizing of programs proposed in the PRSP and broadening of consultation with stakeholders.

3. Macroeconomic management has improved and some structural reforms have been implemented, but serious institutional weaknesses hinder effective policy implementation. Privatization of a number of hitherto state-owned enterprises and increasing remittances from migrant workers have facilitated the development of private sector activities in the service

sector, and thus contributed to a gradual diversification of the sources of growth. Good progress has been achieved in maintaining fiscal discipline, and monetary policy management has recently improved. Reforms in the social sector (especially in education and health), and in the energy sector have been initiated, but institutional weaknesses and poor governance are delaying implementation. As a result, utilization of committed resources has been low—for instance, the World Bank disbursed only a tenth of its total commitments in FY2003.

II. UPDATED POVERTY DIAGNOSIS

4. The staffs commend the government's effort in completing the 2003 TLSS supported by DFID and the World Bank. The survey has enabled the government to monitor progress in reducing poverty and providing sectoral services for enhancing human development. At present, there are no officially accepted poverty standards in Tajikistan—three methods are used in measuring poverty, two of which are based on estimates of the cost of a food-basket that has not been adjusted since the Soviet period. The staffs, therefore, stress the importance of developing consensus about a national poverty line that would be used consistently.

5. Although poverty has declined significantly between 1999 and 2003, it is still widespread and living standards remain low. Preliminary results of the TLSS are encouraging as the poverty rate appears to have declined over the four year period by 8-18 percent (depending on the methodology used). The rate of decline in poverty, however, varies significantly by region and residence. The poverty gap and the severity of poverty have fallen, for each of the poverty lines used, but inequality has increased somewhat. Despite the apparent improvement in the overall poverty situation and a decline in the infant mortality rate, about 57 percent of the population still lives below the poverty line—PPP-based per capita expenditures of \$2.15 per day,—making Tajikistan the poorest country in Central Asia. In addition, progress in reducing poverty is threatened by the emergence of new challenges, including the emergence of new diseases such as TB and HIV/AIDS and destabilizing influences of crimes and drug trafficking.

III. PROGRESS IN PRSP IMPLEMENTATION

6. Macroeconomic management has improved, but progress in structural reform is mixed. The improvements in macroeconomic management have reflected in growth and continued reduction in inflation. Challenges remain, however, in governance, the development of the private sector, and in prioritizing expenditures in light of scarce fiscal resources and institutional shortcomings. Enhancing links between the PIP, the medium-term budget framework, and the PRSP would be essential for the poverty reduction strategy. This would help prioritize expenditures, identify any need for supplemental financing especially for priority projects, and facilitate contingency planning.

A. Macroeconomic Policies

7. Real GDP growth has been strong in recent years, averaging 9.5 percent in 2000-03, but real GDP at end-2003 was only 68 percent of its level in 1991. There are indications of

increasing diversification of the sources of growth, driven by nontraditional exports and workers' remittances from abroad. In this regard, the report could have assessed the gradual shift in the sources of growth and identified policy strategies for sustaining growth. The report could also have usefully discussed how the authorities intend to solve likely policy trade-offs resulting from required economic adjustment in the event of exogenous shocks.

8. Monetary policy implementation continues to be constrained by institutional limitations, despite recent streamlining of the functions of the central bank and reform of policy formulation. Inflation in Tajikistan was one of the highest among the CIS countries during the past few years, but recent focusing of policy implementation has helped reduce inflationary pressures significantly—the 12-month inflation rate declined to 5.1 percent at end-April 2004. In this context, it is necessary to enhance policy co-ordination between the Ministry of Finance and the NBT, improve institutional capacity, and develop additional monetary policy instruments to help sustain the reduction in inflation.

9. The authorities have maintained a prudent fiscal stance. Since the drafting of the report, the authorities have updated the macroeconomic framework to take into account the more recent higher growth rates, together with a more modest improvement in the revenue-to-GDP ratio. The latter partly reflects weaker commodity prices and is realistic if there is a concerted effort to improve tax administration and capture the new nontraditional sectors. However, the budgetary system remains weak. There is no formal system of cash management or cash forecasting, which leads to arbitrary variations in payment dates and inefficient use of resources. The system of payment prioritization is excessively centralized, and requiring daily decisions by senior Ministry of Finance officials. The staffs consider that a more determined effort at reforming public expenditure management is needed to deliver the poverty reduction goals.

B. Structural Reforms and Sectoral Policies

10. Improving the business environment for private sector development is critical for sustaining growth and poverty reduction. However, this priority is not clearly emphasized in the report. Although the Government has taken steps to reduce administrative barriers and streamline business registration, inspection and licensing procedures, improving the business environment remains a major challenge. Corruption and lack of transparency associated with weak governance increase the cost of doing business, worsen the investment climate and deter private investment (both domestic and foreign).

11. Regarding privatization, the staffs encourage the authorities to accelerate the sale of the over 400 strategic enterprises foreshadowed in the PRSP and to ensure that this process is fair, transparent, and efficient. The PRSP plans to implement energy sector reforms including restructuring of the sector and transforming Barki Tajik and TajikGas into joint stock companies during the reporting period. The staffs are deeply concerned about delays in implementing these measures, and regret that the authorities have further complicated the reform by making Barki Tajik a department of the Ministry of Energy in March 2004. This creates conflicts of interest and reduces transparency in operations. Additionally, the action

violates the thrust of the program for privatizing energy distribution companies. The staffs strongly recommend that the authorities reverse the action as soon as possible.

12. Reflecting the high priority of the energy sector, the authorities are in the process of formulating a comprehensive energy strategy over the medium term. While additional investments are required, these need to be better balanced with other sectoral needs in the PIP. To mitigate the poverty impact of increases in electricity and gas tariffs, a compensation mechanism financed by the budget in 2003 and 2004 has been established; however, its benefits do not reach the most vulnerable groups due to poor targeting. The authorities intend to improve targeting and streamline administrative procedures under the mechanism with assistance from the World Bank.

13. Preliminary findings of the Poverty and Social Impact Analysis (PSIA) of farm privatization carried out by the World Bank indicates that privatization has had differential impacts on the population. Delays in addressing the problems of the cotton sector have created rent-seeking opportunities for vested interest groups with a negative impact on government tax revenues, foreign exchange earnings and the welfare of farmers. The analysis confirms that farm privatization increases incomes and welfare of farmers, and lowers losses from rent-seeking as it weakens control of vested interest groups. However, children and workers were negatively affected as social services provided by state farms—kindergartens, schools and hospitals—deteriorated following the transfer to their parent ministries. The authorities, therefore, need to address the cotton farm debt and accelerate the privatization of farmland, and identify appropriate measures to mitigate the negative impacts of farm privatization.

14. The authorities should be commended for improving the quality and access to basic education by the poor. To achieve this goal, public expenditure on education has been increased and an education sector reform strategy has been developed. In addition to a re-drafting of the education law, full implementation of the strategy would require restructuring of school networks, increased funding to meet the recurrent costs, and re-aligning education financing to improve the efficiency and targeting of public spending. In this context, notwithstanding increased funding, some reduction in staffing from previous levels and commensurate increases in teaching loads will be required to accommodate the needed salary increases. Implementing the strategy will also require a further strengthening of donor coordination in the sector. The staffs urge the authorities to meet these requirements and arrest the recent decline in school enrollment.

15. The PRSP rightly focuses on health sector reforms aimed at improving the efficiency of the health-care delivery system, instituting financing reform, and promoting public health. Public spending on health in Tajikistan is among the lowest in the world, having declined from around 5-6 percent of GDP in the early 1990s to about 1 percent of GDP in 2002, or below US\$2 per capita. The current health delivery system is characterized by inadequacy of funds to meet the salaries of personnel, resulting in low productivity, low quality of health-care services at all levels and loss of qualified staff through emigration. The authorities have now initiated a commendable reform of the health-care system that focuses on shifting

resources from hospital services towards more cost-effective primary health-care and preventive services. Health financing reforms will introduce population-based health budgeting in place of input-norm based budget allocation to ensure a more equitable distribution of public resources. The staffs encourage the authorities to review the experiences gained from the rationalization of primary care services in two pilot regions, and carefully develop and roll out the plan to a national level.

16. It is important to note that given the decline in public service provision, community linked development initiatives (CLD) have taken the lead in providing basic services to citizens and supporting citizen mobilization to solve community problems in Tajikistan. In this context, the World Bank has followed a CLD approach in its assistance programs and has pursued strong donor coordination and consensus around a tangible CLD vision. This approach should bring government and communities closer within the context of strengthened local governance. In this regard, the experience and impact of the National Social Investment Fund of Tajikistan (NSIF) and other CLD projects in improving social services and reducing poverty could be brought out in the next progress report.

C. Expenditure Prioritization and Program Financing

17. Some improvements have been made in the prioritizing the PIP. While public spending on education, health, and multi-sectoral activities are projected to increase in the medium term, spending on agriculture, irrigation, and transport were reduced. Prioritization of investment projects outside the PIP is, however, a cause for concern. For example, neither the total cost nor the prioritization process that led to the construction of the Palace of Nations seem transparent. We would urge the Government to address such lapses as they undermine efforts at prioritizing the investment program.

18. Overall, progress in institutionalizing the medium-term budget framework has been slow. The authorities urgently need to establish a budget commission that includes stakeholders outside the Ministry of Finance in order to ensure strategic prioritization of public expenditures (including the externally financed PIP) in line with the PRSP process, and to build a consensus on policy reforms. The commission would also provide a forum for stakeholders to discuss various policy trade-offs within and across sectors, taking into account resource constraints and government priorities outlined in the PRSP.

D. Targets, Indicators and Monitoring and Evaluation System

19. The Government has adopted the recommendation of the UNESCAP to improve the technical capacity and oversight of the PRSP monitoring unit in order to improve monitoring of inputs, programs and beneficiaries, and broaden consultation with other stakeholders. The number of monitoring indicators has been reduced to a total of 94 indicators, compared with the original proposal of 136 indicators. In 2003, the Government drafted and published the Report on Achievement of Millennium Development Goals in Tajikistan with the support of the UNDP. The MDGs are, on the whole, in agreement with the priorities and tasks of the PRSP.

20. The staffs concur with the authorities that the quality of statistics especially on the social sector remains a major concern. These statistics are neither comprehensive nor reliable, and are not published on a timely basis. Further, limited data are available at the sub-oblast level. The definitions and methodologies used by various agencies for calculating monitoring indicators need to be harmonized. Also, the TLSS process should be institutionalized to enhance the process of monitoring poverty reduction and developments in living standards over time.

IV. GOVERNANCE AND THE PARTICIPATORY PROCESS

21. Further improvements in governance are essential for private sector development. The staffs welcome the authorities' plans to audit the state financial control committee (SFCC) with a view to broaden its role in safeguarding use of public resources. In addition the authorities need to formulate and adopt a coherent strategy for strengthening public administration and promoting transparency and good governance. Although the PRSP recognizes that development of an effective and high quality public administration is core to effective governance, little progress has been made in improving the quality of public administration. Progress on organizational reform of ministries has been slow, and duplication of functions among units still exists. Furthermore, the state continues to intervene in private sector activities, leading to inefficiency, non-transparency and corruption. Effectiveness of the civil service is hindered by low institutional capacity due to inadequate incentives and lack of professional training and career development for civil servants.

22. Despite the initial progress in involving all stakeholders in drawing-up the PRSP, the participatory process has weakened. For instance, stakeholders outside the executive branch, including civil society and parliamentarians, were excluded from the development of the PRSP Progress Report. The report was entirely prepared by the PRSPMU in the President's Office. The staffs note the continued limited involvement of stakeholders outside the Government (Parliament and civil society organizations) and therefore, urge the Government to take bold steps in involving civil society and parliamentarians in the formulation, implementation and evaluation of the PRSP. The establishment of an Aid Coordination Unit has improved donor coordination in support of the PRSP implementation. Following the CG meeting in May 2003 and the follow-up CG meeting in February 2004, donors have slowly aligned their assistance and coordinated their effort to maximize the effectiveness of assistance, especially in health and education. In addition, steps have been taken in harmonizing donor activities. For example, the World Bank and the Asian Development have jointly conducted their Country Portfolio Performance Review for the first time in March 2004.

V. RISKS TO THE STRATEGY

23. External shocks could limit the growth potential of the economy and compromise the authorities' ability to raise sufficient funds to finance the PRSP. Despite recent signs of increasing diversification of the sources of growth, Tajikistan is still heavily dependent on exports of aluminum and cotton which together account for over three-fourths of total export

earnings and employ a significant proportion of the labor force. Also, the increasing importance of workers' remittances in the balance of payments and growth of domestic absorption makes Tajikistan vulnerable to economic developments in Russia. Additionally, despite the participation of civil society in drawing-up the PRSP, the implementation may be hampered by vested interests (who might make implementation of structural reforms difficult), institutional weaknesses and poor governance.

24. The report is too optimistic in what is set to achieve, given the limited absorption capacity and slow progress of the reform agenda. The macroeconomic framework could usefully reflect Tajikistan's vulnerability to external shocks and other risks by including optimistic and pessimistic medium-term scenarios in the projections. This approach could be supplemented by a balanced discussion of how government proposes to resolve policy trade-offs in the event of external shocks. Moreover, weak institutional capacity was cited as one of the factors that delay the PRSP implementation. In this context, the authorities could intensify their efforts to strengthen the capacity of public officials by accelerating the reform of public administration, and better articulating their technical assistance needs.

VI. CONCLUSIONS

25. Modest progress has been made so far in improving policy effectiveness and reducing poverty but reforms need to be accelerated in the next few years. The staffs welcome the commitment of the authorities to address the shortcomings pointed out in the JSA of the PRSP by better refining the strategy. Nonetheless, the report suggests a number of areas where gaps remain in the strategy, and these constitute part of the agenda for further work. The next progress report could usefully address the following issues:

- Extending the macroeconomic framework and sectoral targets of the PRSP beyond 2006. The framework should include detailed costing and financing needs and an analysis of external and fiscal sustainability in light of the serious external debt service burden.
- Strengthening of reform efforts in the health and education sectors and accelerating these reforms through the use of pilot activities and community link development, wherever appropriate. Further, the reform of financing strategies need to be realigned with public expenditure management in order to enhance the efficiency of service delivery and improve access to these services, especially by the poor.
- Restoring the independence of Barki Tajik.
- Detailing measures and action plans to improve governance and accelerate private sector development.

- Strengthening the links between sectoral policies and poverty reduction and a detailed costing of efforts to sustain the recent modest progress, and analyzing the impact of the National Social Insurance Fund (NSIF) on poverty reduction.

26. Staffs of the World Bank and the IMF consider the country's efforts towards implementation of the strategy provide sufficient evidence of the authorities' commitment to poverty reduction, and the PRSP continues to provide a credible framework for Bank and Fund concessional assistance. The staffs therefore recommend that the respective Executive Directors of the World Bank and the IMF reach the same conclusion.