STABILIZATION POLICIES IN GUYANA, 1977-1985

by

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the University of Manitoba in partial fulfillment of the requirements
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ABSTRACT

This study examines recent experience of Guyana in the
design and implementation of adjustment programs supported
by the use of IMF and World Bank resources. The analysis
covers primarily the 1977-1985 period. Specifically, the
study examines: the economic background leading to the emer-
gence of the economic crisis before 1978 and the causes of
the crisis thereafter; the theoretical and empirical nature
of IMF and World Bank financing and adjustment programs; and
the experience in implementing adjustment program in the
Guyana context, with a view to determining the reasons for
the difficulties Guyana continues to encounter. In light of
persistent financial imbalances during and after the
1977-1985 period, and hence the increasing urgency for solu-
tions to these problems, this study also formulates a simul-
taneous macroeconomic model relevant to Guyana's needs, to
analyse the relationship between key macroeconomic vari-
ables. Furthermore, foreign exchange constraint on economic
growth, an endogenised and explicit government budget con-
straint, quantitative restriction, and demand, supply and
monetary factors in explaining inflation are highlighted.

The results of the study do not support the proposition
that the aggravation of financial imbalances in Guyana

reflects overconsumption. These findings invalidate, in this particular context, those aspects of the IMF's economic policy which focus on the reduction of aggregate spending and changing relative prices. Rather, the study suggests that increases in financial imbalances were, for the most part, caused by external shocks and inappropriate policies. It is concluded that Guyana's prospects depend on a large influx of foreign capital to provide for the importation of essential inputs and technology normally required by LDCs. This, however, is only the necessary condition, the sufficient condition requires Guyana follow a careful structural adjustment program aimed at economic efficiency. Specifically, the need for democracy, the provision of the basic human capital and development and expansion of the agricultural, mining and industrial sectors are underscored. The analysis concludes with a plea for provision of appropriate adjustment assistance by the international community in general and the IMF in particular.

ACKNOWLEDGEMENTS

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Chapter I

INTRODUCTION

During the 1970s and early 1980s, many oil-importing
developing countries experienced severe external imbalances.
These were due in part to external shocks, such as deterio-
ration of the terms of trade, slow growth of world trade and
high interest payments on mounting debts, and in part to
internal shocks, such as inappropriate domestic policies.
While the severity of the nature of the shocks varied from
country to country, the persistence of the shocks found
expression in rising current account deficits and increasing
problems of servicing foreign debt. To finance the growing
deficits and ease debt servicing problems, many of these
countries turned to the IMF which provided assistance condi-
tional upon major adjustments in economic policy.

The adjustments often took the form of monetary and fis-
cal contractions and relative price changes. Despite such
measures, the oil-importing developing countries have been
experiencing mounting external imbalances with declining
imports, total GDP, per capita income and social welfare
(Helleiner, 1986). This led some critics to argue that poli-
cies advocated by the IMF are antithetical to economic
growth and development since they do not address the root

cause of the crisis which is structural, further aggravated by external shocks. In particular, the structuralists argue that these countries suffer from two basic rigidities: the inelasticity of production due to resource endowment and the slow and unstable rate of export growth which is inadequate to acquire vital capital and intermediate goods imports.

Guyana's experience seems to be no different from that of those countries. Hence, the main aim of this study is to make a contribution towards a proper understanding of what went wrong in those countries through a case study of Guyana. In particular, this study focuses on an evaluation of: the cause of the economic problem; the policy responses in light of the debate surrounding the IMF's and World Bank's stabilization programs; the future prospect of the economy in light of the present measures through a simulated macroeconomic model; and prospective solutions.

A central concern in this study is the importance of foreign exchange to finance crucial imports of capital goods and materials necessary for reducing excess productive capacity and for increasing productive investment. In the quest for the major factors that contributed to the economic problems and for prospective solutions, this study aims to challenge the view that price adjustments alone are likely to reduce excess demand and stimulate supply. In particular, Guyana's case study is used to show how a typical stabilization package of demand restraint and relative price

changes can lead a country to a reduction in total GDP, a higher inflation rate, a worsening of external and internal imbalances and a decrease in the population's standard of living. On the other hand, the structuralists' contention that an increase in adjustment assistance can have the opposite to the above effects is also analysed.

In detail, this study is divided into seven chapters and will proceed as follows. In chapter two, an overview of the Guyanese macroeconomic experience leading to the crisis and specifically to the increasing current account deficit is provided. Particular attention is given to an identification of the major factors that caused the external imbalance. This is done through the use of the decomposition framework of Bacha (1986) in which factors underlying the observed changes in the current account deficit are assessed in quantitative terms.

Chapter three reviews the standard stabilization programs of the IMF and World Bank and the academic debates associated with these. With the view that these programs neglected the structural characteristics of LDCs, an alternative program is discussed.

In chapter four, Guyana's experience with IMF/WB adjustment programs during the 1978-1982 and 1983-1985 periods is evaluated.

In chapter five, the behaviour of key macroeconomic variables and the effects of policy are examined. For this purpose, a simple macroeconomic model is formulated and estimated. The emphasis of the model is on the external dependence of the economy on capital and intermediate goods to foster growth. The model is also used to provide assessments of changes in a number of policy variables.

Chapter six discusses Guyana's macroeconomic prospects for the 1990's and required policy efforts. Specifically, the growth prospects are discussed. A structural adjustment strategy aimed at raising economic efficiency is emphasized whose success depends on increased democratisation, and appropriate demand and supply side policies.

Chapter seven concludes the study with a summary and some conclusions.

Chapter II

THE ECONOMIC CRISIS IN GUYANA

2.1   INTRODUCTION

This chapter discusses the economic crisis in Guyana dur-
ing the 1977-1985 period.   In   particular,   the focus is on
identifying the major   factors that caused the   crisis.   The
organisation of the chapter is as follows: sections 3-5 pro-
vide a historical review of the Guyanese economy,   within a
political context, leading up to the crisis;   section 6 dis-
cusses the nature of the crisis; section 7 analyses the ori-
gin of the   crisis;   and section 8   provides some concluding
remarks.

2.2   THE SETTING

Guyana formerly British Guiana, has   one of the lowest
population densities (9.5 per sq mile) in the Caribbean.
With a population of 800,000,   its composition includes peo-
ples of diverse cultural backgrounds. Table 1 shows that the
two largest ethnics groups are the Africans and East Indi-
ans, who are descendants of African slaves and East Indian
indentured workers. The vast majority of the population is
settled along the coastal belt which comprises approximately

TABLE 1

Ethnic Composition of Guyana's Population

ETHNIC GROUP	TOTAL	PERCENT
Indians	419,925	50.9
Africans	253,275	30.7
Mixed	94,875	11.5
Chinese	4,950	0.6
Portuguese	10,725	1.3
Amerindians	36,300	4.4
Whites	4,125	0.5
Other	825	0.1
Total	825,000	100.0

Source: Government of Guyana, Statistical Bureau;
Inter-American Development Bank
(Washington, D.C.) 1977.

10 percent of the total land area. Approximately 80 percent of the remaining land area consists of forest and is still unexploited despite traces of mineral wealth.

The country's economy is essentially oriented towards the exports of agricultural and primary products. The economy depends mainly on sugar, bauxite and rice which account for 40 percent of GDP and 80 percent of exports. Sugar and rice cultivation are found on the coastal strip in the rural areas and are predominantly East Indian activities. Bauxite production is carried out in the hinterland along with gold mining and forestry. The urban areas are predominantly occupied by those of African, Portuguese, European and Chinese origin. The Africans are involved in the bureaucracy with the elites dominating the state bureaucratic structure. The

Portuguese, Chinese and East Indians are involved in retail and wholesale businesses. The Amerindians are the natives of Guyana and live in the interior.

2.3 THE COLONIAL ERA

Guyana's initiation into the world capitalist system dates back to the eighteenth century with the production and export of sugar. At that time, sugar was evolving as the most valuable potential agricultural crop because of its increasing popularity in the European market. Thus, Western European imperialists did not hesitate to venture into the lucrative business. The uninterrupted occupation by the British after 1796 provided socio-political stability and an economic expansion of the economy because of increasing expectations of a larger British market for exports. By 1817, sugar became the sovereign staple of Guyana and the dominant factor of production was slave labour. In 1838, slavery was abolished and an imperialist wage-slavery mode with an influx of indentured labourers who lived under similar conditions as slaves evolved. This mode, however, was transient as contradictions between the indentured workers and planters led to social struggles which eventually led to a more "humane" habitat for the indentured workers during the 1890s (Mandle,1973). The dominant mode gradually became one of capitalism. The two principal classes were the plant-

ers (who were the capitalists) and the workers. The planters owned the plantations, controlled the institutions of the colonial state and secured the surplus value through wage labour and the market. Given the enormous power of the planters within the colonial system, they systematically took steps to block the working class from developing and from transforming itself into a class of independent agricultural producers. In particular, the planters were reluctant to: (1) make abandoned sugar estates available for peasantry, and when made available, there were conditions that the beneficiary should work for three days per week on the sugar estate at a lower wage; (2) consider alternative industries other than the sugar estates as a source of development despite recommendations made by a Royal Commission in 1937; (3) relax restrictions for land rights; (4) provide credit to local planters, businesses and peasants; and (5) provide technical service to rice farmers. The competition for resources led to a small local private sector restricted to agriculture, minor manufacturing, retail and wholesale business. This suppression of the working class together with surplus extraction resulted in a satellite economy.

At the time of independence in 1966, there existed fundamental structural features of a satellite or a dependent economy in Guyana. Firstly, there was a divergence between the goods supplied and domestic demand. In particular, a

major portion of the goods produced, i.e., sugar, bauxite
and rice, were exported while the bulk of the goods consumed
were imported, including intermediate and capital goods.
Secondly, two of the major exports, sugar and bauxite, were
produced and processed by foreign multinationals, indicating
dependence on foreign capital, technology and resources.
Thirdly, there was a dependence on a few dominant overseas
metropolitan markets, such as the U.K., Canada and U.S.A.,
for Guyana's primary product exports. For example, in 1952
and 1966 these countries accounted for 89 and 66 percent of
Guyana's exports, respectively. Fourthly, there were few
backward and forward linkages with the local economy, link-
ages were confined only to the dominant export commodities,
e.g., sugar cultivation led to related industries such as
rum, coastal shipping, local and foreign trade, insurance,
printing and other services. Fifthly, the structural depen-
dence of the nation with excessive specialization in a few
primary products with limited growth prospects and the
absence of large scale industrial enterprises gave rise to
high levels of unemployment which was estimated at 22 per-
cent during the 1960-1976 period. This high level of unem-
ployment was compounded with underemployment as peasants
were employed only for a part of a year (Spinner, 1984: p70,
p74).

Given the colonial relation in Guyana and the transforma-
tion of the working class into peasants, there were also

stagnant living standards and shortages of capital for development. This led to economic and social afflictions on the Guyanese. In particular, educational, medical and housing facilities were poor or inadequate as the capitalist transformation of Guyana led to a path of dependent growth. Economic growth was externally induced, as prosperity and recession in the metropolitan capitalist countries superimposed these cycles on the Guyanese economy. The beginning of the twentieth century was a period of stagnant growth for the nation as a result of difficulties in exporting sugar overseas due to the implementation of the British free trade policy (which was ratified in 1902) and the expansion of the European beet sugar industry (Rodney 1981). During and after the first World War, the economy boomed as a result of increases in the price of both rice and sugar. Also, there was an increase in the demand for bauxite which eventually led to the establishment of the bauxite industry. In the 1920s and the great depression, however, rice, sugar and bauxite prices slumped and this weakened the Guyanese economy. The second World War provided renewed impetus for growth as demand for Guyana's primary products overseas increased rapidly, especially bauxite. The rhythms of the business cycle in the metropolitan capitalist countries continued and during the 1953-1965 period, Guyana's average real growth rate was only a disappointing 3 percent per annum. The unemployment rate was stagnant at 22% and there were no unemployment benefits implying great hardship for the unemployed.

An understanding of Guyana's politics is paramount to the understanding of the economic development of the country prior to independence. During the 1950-1952 period, two charismatic leaders, Cheddi Jagan and Forbes Burnham, with others formed the People's Progressive Party (PPP) under the leadership of Jagan. The party won the first elections held under universal adult suffrage in April 1953. In October 1953, however, the British Government suspended the constitution until 1957, claiming that the PPP was turning the country into a communist state and therefore it was necessary to prevent communist subversion. During the 1953-1958 period, there was intense rivalry between Jagan and Burnham for sole leadership of the PPP which eventually resulted in a split of the party and the creation of the People's National Congress led by Burnham. The political parties were different in two important ways. First, they were apparently organised along racial lines with the PPP drawing support from Indo-Guyanese and the PNC drawing support from Afro-Guyanese. Second, there were ideological differences with the PPP espousing a strong socialist doctrine and the PNC advocating a moderate form of socialism. As a result of the ideological differences, Jagan was characterised as a communist and hence was seen as a threat by imperialist forces. In the 1957 and 1961 elections, the PPP won. Following the 1961 elections, tension mounted in the country with widespread strikes, robbery, riots and arson. The CIA was mainly blamed for the disturbances through its infiltration

of the US unions which provided support for the local unions in Guyana. Also, political rivalries can be partly blamed (Manley, 1982:7). It is argued that the hostilities against the PPP and its preoccupation with imperialist forces caused Guyana to regress in economic development during the 1953-1964 period. In 1964, elections were held and, through a constitutional change, a coalition government, comprising the PNC and the right wing United Force (UF) party, was formed.

2.4 THE POST INDEPENDENCE ERA

The years following Guyana's emergence as an independent nation were marked by slow growth and high unemployment. This state of affairs occurred, despite the implementation of a $300G million development plan for the 1966-1970 period. The main objectives of the plan were to reduce the high levels of unemployment and improve the standard of living of the populace. The plan was based on the Puerto Rican model, in which foreign capital was viewed as a panacea for under-development. The plan envisaged Guyana's development through agricultural diversification, increases in the export of sugar, bauxite and rice, and increases in industrial output (primarily through foreign investment). The combined dynamic effects of these elements were supposed to achieve the stated objectives. The plan, however, was explicitly abandoned

in 1969 after it had failed to achieve its declared objectives.

The abandonment of the 1966-1970 plan, the government asserted, was to give effect to its new socio-economic policy with the transformation of the country to a cooperative republic in 1970. The socio-economic policy was within the paradigm of cooperative socialism which was underwritten in its 1972-1976 development plan. The objectives of the plan were national self-sufficiency in food, clothing and housing, and a de-emphasis of the role of foreign investment. National self-sufficiency was to be achieved through increased state participation and an expanded cooperative sector. Cooperative projects would be financed from funds made available by the establishment of a cooperative bank in 1970. De-emphasizing the role of foreign investment was to be achieved by equity sharing or nationalization of foreign owned and controlled industries.

Nationalization was the most popular alternative and was widespread during the 1971-1976 period. The two bauxite companies in Guyana, the Aluminum Company of Canada (ALCAN) and Reynolds of U.S.A., were nationalized in 1971 and 1975 respectively. In the sugar industry, the holding of Jessels Security Limited of the U.K. and Bookers of the U.K. were nationalized in 1975 and 1976 respectively. By the end of 1976, approximately eighty percent of the productive economic activities were under government ownership and control.

Foreign financial institutions were also indirectly control-
led in Guyana through the proliferation of local financial
corporations which included an Agricultural Cooperative
Development Banking Corporation, a Mortgage Finance and an
Insurance Corporation.

2.5   POLITICAL DOMINATION

Under the ideology of cooperative socialism, the Peoples
National Congress (PNC), the ruling party, stressed the doc-
trine of "party paramountcy" as the   party was viewed as an
integral part of the state. This doctrine was of major con-
cern to opponents who feared a one party state in an already
dictatorial situation established through rigged elections
(Spinner, 1984: Chpt 8), in 1968 and 1973 as the PNC at any
one time only had a small minority support, mostly those of
African origin. The loyalty of the civil service, police and
army provided the PNC with continued power.

During the 1968-1976 period, the government consolidated
and strengthened its party control of the state through the
creation of the Ministry of National Development and Office
of the General secretary of the PNC. The PNC party was thus
offically financed by the state. The government expanded the
role of the state into import trades, wholesaling, retailing
and distribution.   "Cooperative socialism" was used as an
excuse for increased state expansion. However, opponents of
the government argue that the PNC was transforming coopera-

tives into a fascist alternative to genuine socialism (Jagan, 1975). The leader of the opposition Peoples's Progressive Party argues that the PNC does not have a principled position on cooperative socialism but instead, ad hoc measures which are bankrupting the country. Also, many private companies are masquerading as cooperatives, and thus creating a new breed of bureaucratic capitalists, mostly an African bourgeoisie, who replaced foreign owners of capital. However, this local bourgeoisie works in alliance with the foreign capitalists, and buttresses the system of imperialism. This was done by opening the way to imperialist dictation through 'aid with strings' (PPP, 1985:74).

The external dependence of the nation was unchanged in the post-election (1973) period. Guyana continued to depend heavily on: (1) foreign technology and capital because of the absence of local capital industries; (2) export of a few primary products since there has been virtually no diversification; and (3) export to a few dominant overseas markets. The extreme dependence and high level of public sector control over the economy have raised the issue of whether the country can complete the transition to socialism (Mandle,1982; Odle, 1976). There have also been issues raised with the ideological thrust of "cooperative socialism" as against "scientific socialism". Apart from the contradictions, whereby the cooperative mechanism is used to build up an African bourgeoisie, Odle (1976:33) among others,

argues that it is unclear how cooperative socialism differs from workers control as in the case of Yugoslavia or even from traditional Soviet decentralization.

With the production relation now changed in Guyana with the state owning 80 percent of the economy, absence of democracy was evident, at the political governmental, social and industrial levels. Workers' participation and control, which were promised at the time of nationalization, have not materialized. In the the rice sector, the system of farmers participation in the decision making, through election of a majority of the board of directors of the Guyana Rice Marketing Board (GRMB), was dismantled, and management was handed over to the bureaucrats appointed by the government.

In this regards, Thomas (1982) and Jagan argued that instead of increasing production, there has been an enlarged bureaucracy. The state expansion into local and foreign trade created a virtual monopoly and this led to preferences given to PNC business ventures and extortion demands from others for money for PNC coffers to avoid daily hassles and frustration. The government through the slogan of cooperative socialism has launched the nation into state capitalism.

Despite increased state ownership and control of virtually all aspects of economic activities, the external dependence of the economy on the metropolitan capitalist system

remains unchanged. This dependence continued to make the economy very vulnerable to business cycles of Guyana's trading partners. In the midst of growing domestic disaffection and the general and structural crisis of the world capitalist system, an economic and social crisis erupted in Guyana. By 1977, the crisis was entrenched and has ever since dominated the economic and social life of the country. Hence, it is important to understand the nature and the causes of the crisis. Accordingly, the next two sections address those issues.

2.6 NATURE OF THE CRISIS

During the early 1970s, the pace of economic activity in Guyana had accelerated. The growth rate of gross domestic product (GDP) was unprecedented, increasing by 7 percent in 1974 and 9.5 percent in 1975 (see Table 2). The rate of growth of exports also boomed. In nominal terms the value of exports in US dollars doubled in 1974 and rose by 36 percent in 1975 (see Table 4). In real terms, exports grew by 24 percent in 1974 and were stagnant in 1975. The latter indicates an increase in export prices during that year as shown in Table 3. The first oil shock that hit Guyana, occurred in the midst of an economic expansion and higher export prices and was, therefore absorbed, quite easily. However, since 1976 the pace of economic activity has slowed down markedly. The growth rate of real GDP averaged -1.3 percent

TABLE 2

Gross Domestic Product G$m

YEARS	NOMINAL	REAL	% CHANGE	NOMINAL (US$)
1973	645	1017	---	303
1974	950	1089	7.0	426
1975	1192	1192	9.5	468
1976	1136	1208	1.3	446
1977	1125	1174	-2.9	441
1978	1264	1146	-2.4	496
1979	1330	1132	-1.2	522
1980	1512	1156	2.1	593
1981	1597	1200	3.8	626
1982	1446	1063	-11.4	482
1983	1468	1019	-4.1	489
1984	1700	1024	0.5	400
1985	1964	1033	1.0	462

Source: Government of Guyana; Author's calculations.

TABLE 3

Terms of Trade (1975=100)

YEAR	EXPORT PRICE INDEX	IMPORT PRICE INDEX	TERMS of TRADE
1973	46	68	67.6
1974	72	94	76.6
1975	100	100	100.0
1976	73	102	71.6
1977	83	112	74.1
1978	85	123	69.1
1979	92	151	60.9
1980	110	186	59.1
1981	103	190	54.2
1982	94	184	51.1
1983	85	182	46.5
1984	88	180	48.9
1985	82	177	46.3

Source: World Bank, World Tables;
        Government Statistical Bureau.

for the 1976-1978 period. The rate of growth of exports also

TABLE 4

Balance of Payments US$m

YEARS	MERCHANDISE EXPORTS	MERCHANDISE IMPORTS	TRADE BALANCE	NET SERVICES	CURRENT BALANCE
1972	143.6	128.9	14.7	-30.1	-15.4
1973	135.7	159.4	-23.7	-87.1	-63.4
1974	270.1	230.3	39.8	-48.9	-9.1
1975	351.4	305.8	45.6	-70.2	-24.6
1976	279.5	330.9	-51.4	-91.4	-142.8
1977	259.3	286.7	-27.4	-70.3	-97.7
1978	295.6	253.5	42.1	-71.8	-29.7
1979	292.8	288.8	4.0	-86.7	-82.7
1980	388.9	386.4	2.5	-125.4	-127.9
1981	346.4	399.6	-53.2	-129.8	-183.0
1982	241.4	254.2	-12.7	-129.6	-142.3
1983	193.8	225.7	-32.4	-125.1	-157.5
1984	219.9	201.6	15.2	-111.6	-96.4
1985	214.0	209.1	4.9	-101.5	-96.6

Source: World Bank, World Tables;
        IMF, International Financial Statistics.

declined in nominal terms during the period, averaging -5.0 percent. As a result of this slackening in economic activity, Guyana's external position weakened. The current account deficit, as Table 4 indicates, increased from -US$9.1m in 1974 to -US$142.8m in 1976. As a percentage of GDP, the deficit increased from 2 percent in 1974 to an annual average of 20 percent during the 1976-1978 period. In 1978, as the benefits of the commodity boom were felt, the external position was steady with a current account deficit of only US$29.7m, which was 7 percent of the GDP.

Imports of goods and services, as Table 4 indicates, also followed the downward trend of economic activity, the rate

of growth of imports, in nominal terms, which averaged 33
percent p.a. for the 1974-1975 period declined annually at
an average of 4 percent for the 1976-1978 period. The compo-
sition of imports also shifted considerably. Table 5 shows

TABLE 5

Imports by Major Categories: % of Total Imports

YEARS	CONSUMER GOODS	INTERMEDIATE GOODS	CAPITAL GOODS	OTHER	FUELS AND LUBRICANTS
1972	36.0	23.6	30.0	--	9.4
1973	32.6	26.0	29.4	--	13.0
1974	19.0	36.4	25.2	1.0	18.2
1975	16.2	34.4	32.1	0.7	16.6
1976	17.8	33.7	32.7	1.0	14.8
1977	17.8	31.2	28.1	3.0	19.9
1978	18.5	35.4	21.5	0.8	23.9
1979	18.2	34.7	18.0	0.6	28.4
1980	13.0	23.0	19.2	0.5	35.0
1981	13.3	33.6	16.0	0.7	36.0
1982	13.1	30.3	16.6	1.0	39.0
1983	8.8	29.1	18.0	1.0	43.3
1984	10.4	25.0	13.8	0.0	50.8
1985	9.8	27.5	17.1	0.1	45.5

Source: Bank of Guyana Annual Reports, 1983.
Government of Guyana, Statistical Bureau.

fuels and lubricants which were approximately 10 percent of
total imports prior to 1973, increased to 18 percent in 1974
and remained at that level for the 1975-1978 period. In
1978, however, they were 28 percent as a result of the sec-
ond oil crisis. Consumer goods as a percentage of total
imports, on the other hand, declined from approximately 34
percent prior to 1973 to approximately 18 percent for the

1974-1978 period. There was virtually no increase in local production during this period. The evidence from the growing parallel economy suggests, however, that the decline in legal imports of consumer goods was to some extent offset by increased illegal imports (financed in part by unofficial and unrecorded exports). The percentage of intermediate goods, however, hovered at 34 percent for the 1974-1978 period. Capital goods, as a percentage of total imports, averaged 30 percent except for 1978 when they declined to 22 percent.

The slackening of economic activity and the high levels of current account deficit created financial constraints for the government. The budget deficit increased dramatically from G$35.3m (or US$15.8m) in 1974 to an unprecedented level of G$370.0m (or US$145m) in 1976. In 1978, however, the budget deficit plummeted to G$233.0m (or US$91.4m) as the benefit of the commodity boom was felt (see Table 6). The budget deficit was financed by increases in borrowing from abroad in the sum of US$64.5m in 1975 and US$53.2m in 1976. After 1977, however, foreign financing declined markedly to US$5.6m in 1977 and US$17.6m in 1978. The total external public debt increased from US$345m in 1974 to US$454.9m in 1976 and US$655.8m in 1978 (see Table 7). Thus, the total debt service increased from US$14.4m in 1974 to US$32.9m in 1976 and US$49.4m in 1978. The debt service ratio increased from 5.3 percent in 1974 to 11.8 percent in 1976 and 16.7

TABLE 6

Central Government Financial Operation   G$m

	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985
NOMINAL VALUES											
INCOME REVENUES	110	115	157	162	166	192	211	210	200	236	308
IMPORT DUTIES	42	52	39	34	36	37	47	29	29	29	30
OTHER REVENUES	324	210	159	169	193	222	304	311	336	335	357
TOTAL CURRENT REVENUES	476	377	355	365	395	451	562	550	566	600	695
CURRENT EXPENDITURES excluding Debt Charges	255	337	299	307	353	409	479	429	469	862	611
DEBT CHARGES	66	123	117	168	227	300	338	402	521	407	559
CURRENT DEFICIT	155	-83	-61	-110	-185	-258	-255	-281	-424	-669	-475
CAPITAL REVENUES	4	2	3	2	17	4	14	3	12	51	79
CAPITAL EXPENDITURES	351	289	151	115	207	345	424	790	349	608	523
OVERALL BALANCE	-192	-370	-209	-223	-375	-599	-665	-1068	-761	-1226	-919
DEFICIT:GDP	16.0	32.5	18.5	17.6	28.2	39.6	41.6	73.8	51.8	72.1	46.8
NET EXTERNAL BORROWINGS	130	128	26	49	68	57	282	510	84	54	
NET DOMESTIC BORROWINGS	62	244	183	174	307	542	383	1017	677	1029	

Source: Bank of Guyana Annual Reports;
International Financial Statistics.

percent in 1978.   Since 1976, domestic financing has become the dominant source of finance.   Total internal public debt increased from US$258m in 1976 to US$389 in 1978.   Another source of financing the deficit was a massive run down of international reserves. Table 8 indicates that net international reserves declined from +US$83.5m in 1975 to -US$42.7m in 1978.   Further, the inflows of capital from private institutions decreased rapidly, causing Guyana to depend wholly on non private international institutions.

TABLE 7

National Debt US$m

YEARS	INTERNAL	EXTERNAL	TOTAL	DEBT SERVICE	DEBT SERV. RATIO
1973	137.0	261.0	397.0	--	--
1974	121.0	345.0	466.0	14.4	5.3
1975	169.0	399.1	568.1	16.1	4.6
1976	258.0	457.3	715.3	32.9	11.8
1977	329.0	483.0	812.0	32.1	12.4
1978	389.0	655.8	1044.8	49.4	16.7
1979	498.0	713.7	1202.7	90.5	30.9
1980	642.0	742.9	1384.9	69.0	17.7
1981	593.0	852.6	1445.6	74.2	21.4
1982	919.0	833.0	1752.0	48.9	20.2
1983	1270.0	796.5	2066.5	55.5	28.6
1984	1518.0	677.1	2195.1	62.0	28.0
1985	1307.5	677.3	1984.8	50.4	23.6

source: Bank of Guyana Reports;
        IMF, International Financial Statistics;
        World Bank, World Tables.

TABLE 8

Net International Reserves and Real Imports (1977=100) US$m

YEARS	Total Net International Reserves	Real Imports
1972	43.1	---
1973	19.8	---
1974	47.3	---
1975	83.5	---
1976	-12.3	363
1977	-39.3	287
1978	-42.7	317
1979	-98.4	217
1980	-184.7	244
1981	206.7	251
1982	-315.4	162
1983	-421.2	141
1984	-470.6	127
1985	-550.0	129

Source: Bank of Guyana Reports

With higher import prices for intermediate inputs, fuel and lubricants, rigidities in production and scarcity of imported consumer goods, the pace of inflation gathered momentum. As Table 9 indicates, the rate of inflation

TABLE 9

Consumer Price Index: 1975 = 100

PERIOD AVERAGE	ALL ITEMS INDEX	% CHANGE IN CPI
1970	69.2	2.2
1971	69.8	0.8
1972	73.4	5.0
1973	78.9	7.2
1974	92.6	16
1975	100.0	7.6
1976	109.0	8.6
1977	118.0	7.9
1978	136.0	14.2
1979	160.0	16.3
1980	182.7	13.2
1981	227.9	22.1
1982	270.0	16.9
1983	309.0	13.5
1984	380.6	20.8
1985	450.0	16.8

Source: Bank of Guyana Reports;
IMF International Financial Statistics.

increased by 7 percent in 1973 and 16 percent in 1974. During the 1975-1978 period, the average rate of inflation was 9.6 percent. The inflation rates after 1975, however, were underestimated because items included in the CPI could not be obtained at their official prices due to the growing importance of the parallel market as a source of supply.

The period since 1978 has been characterized by declining and stagnant growth in real GDP, per capita GDP and exports, an increasing balance of payments deficit, growing external and internal debt, accelerating inflation and a flourishing parallel economy. These occurred in the midst of three successive IMF programs implemented in the 1978-1982 period which included wage suppression, cuts in subsidies, dismissal of workers, increases in interest rates, prices and taxes.

During the 1978-1982 period, real GDP and exports earnings continued to decline. The annual average growth rate of GDP was approximately -2.0 percent. With the exception of 1980, nominal and real value of exports declined in all years. In 1982, at the height of the global recession, the decline was approximately 30 percent in nominal terms. This poor performance of the economy in terms of output and exports has placed Guyana in a very depressing state. The external position worsened markedly as Table 4 indicates. The current account deficit increased from US$29.7m in 1978 to US$142.3m in 1982 or from 5.7 percent of GDP in 1978 to 29.7 percent in 1982 and to an annual average of 21 percent for the 1978-1982 period. As a percentage of exports, the negative current account balance also increased from 9 percent in 1978 to 54 percent in 1982.

The level of real imports has also declined markedly over the period by an annual average of 6 percent. The second

oil shock during the 1979-1981 period caused the percentage of fuel and lubricants to increase from 24.0 percent of total imports in 1978 to 39 percent in 1982 and to an annual average of 30 percent during the 1978-1982 period.[1] Capital goods component of total imports declined from 30 percent in the 1973-1977 period to 18 percent in 1978 and to 17 percent in the 1978-1982 period (see Table 5). The increasing percentage of intermediate goods and fuel and lubricants reflects the importation of only commodities essential for maintaining to some degree, existing productive capacities.

With the reductions in domestic income, increased government spending and relatively high (official) rates of inflation which averaged 16.5 percent, budgetary deficits also increased from G$233m (or US$91.4m) in 1978 to an unprecedented level of G$1068m (or US$356m) in 1982 or from 18 percent of GDP in 1978 to 73.8 percent in 1982. To finance the deficit, the government increased domestic borrowing from G$174m (or US$68.2m) in 1978 to G$1017m (or US$339) in 1982. The increase in dependence on the domestic banking system's resources was a result of loss of access to foreign credit due to the Guyana government's uncreditworthiness. In 1981, however, the government did manage to secure an emergency loan of US$130m from the government of Trinidad and Tobago. The result of increased domestic and foreign borrowing was

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[1] It is important to note that while the import bill for oil has been increasing, the country has been receiving diminishing quantity of oil. For example, in 1975, Guyana paid G$135m for 4.4 million barrels of refined oil but in 1982 the country received 2.8 million barrels for G$328.5m.

increased interest payments and national debt. Domestic debt, as Table 7 indicates, increased from US$389m in 1978 to US$919 in 1982. External public debt also increased from US$656m in 1978 to US$833m in 1982. The debt service ratio as a result, increased from 16.7 percent in 1978 to 20.2 percent in 1982. With the chronic foreign exchange shortage, external arrears escalated from US$40m in 1977 to US$126m in 1982. As a consequence, many suppliers ceased to export goods to Guyana other than on a cash basis. Net international reserves also declined rapidly from -US$42.7m in 1978 to -US$315m in 1982.

The 1983-1985 period was one of continued relatively slow growth of output and increased rate of inflation. Real GDP declined 4 percent in 1983 but increased marginally in 1984 and 1985. The rate of inflation continued to increase, averaging 17 percent during the 1983-1985 period. The annual average decline of nominal exports was 2.3 percent. In 1983, however, the decline was 20 percent. The level of imports, in real terms (US$), also declined over the period by an annual average of 6.3 percent. Consumer goods as a percentage of total imports declined from 13 percent in 1982 to 9.8 percent in 1985. Capital and intermediate goods imports also declined during the period. In 1984, capital and intermediate goods imports declined by 4 percent while imports of fuel and lubricants increased 7 percent. With few (if any) import substitutions, the parallel market has

been the main source of supply. The combination of minor increases in export earnings in the 1984-85 period and reductions in legal imports, due partly to the unavailability of finance to cover larger deficit, have improved the external imbalance during this period. The current account deficit decreased from US$142.3m in 1982 to US$96.6m in 1985 or from 29.7 percent of GDP in 1982 to 21 percent in 1985. External debt also decreased from US$833m in 1982 to US$740m in 1985. The debt service ratio, however, increased from 20.4 percent in 1982 to 23.6 percent in 1985. External arrears in 1985 were approximately US$615.6m. Net international reserves declines increased from -US$315.4m to -US$550m in 1985.

The budget deficit declined during the 1983-1985 period, from G$1068m (or US$356m) in 1982 to G$919.0m (or US$216m) in 1985 or from 73.8 percent of the GDP in 1982 to 46.8 percent in 1985. Domestic borrowings continued to be the major source of financing the deficit. Domestic debt increased from US$919m in 1982 to US$1307m in 1985.

2.7   THE ORIGIN OF THE CRISIS

The successive years of declining growth in real GDP and deterioration in the current account and budgetary balance are seen as being caused by a combination of external and internal factors. External factors included deterioration in the terms of trade, higher interest rates and low export

volumes. Internal factors on the other included industrial unrest, civil conflict, mismanagement and hence the consequences of a number of policy distortions such as, fiscal restraint, quantitative restrictions and political and social repression.

There are disagreements on the relative importance of those factors as contributors to Guyana's increasing imbalances. Specifically, government has used the oil crisis and the world recession as the principal scapegoats. Thomas (1982) argues that government's inefficiency played a large role. The magnitude of the factors (and in particular, external factors) contributing to the deterioration of the current account of the economy can be estimated from a simple demand driven macroeconomic model developed by Bacha (1986) and reformulated by Helleiner (1986) to accommodate available data. The equations of the model to be estimated are written in the appendix. The results obtained are shown in Tables 10 to 12. In Tables 10 to 12, variations in the ratio of the current account deficit to actual GDP between each year over the various periods and the base year are the results of the impact of external shocks, accumulated debt and domestic policy response relative to real GDP. External shocks are the cumulative effect of terms of trade deterioration, interest rate shocks, and other external shocks which included direct investment income from abroad and changes in unrequited transfers. Policy response is the

cumulative effect of domestic spending, exports promotion and import substitution. Policy response represents the cumulative effects of internal shocks. First, the effect of external shocks on the current account is discussed.

Table 4 shows that the Guyanese economy fared well against the oil shock in 1973. From a current account deficit of US$63.4m in 1973, the improvement was so remarkable that the deficit fell to US$9.1m and US$24.6m in 1974 and 1975 respectively. As a result, the current account deficit as a fraction of actual GDP, as Table 10 shows, improved by 0.3 and 0.2 percentage points in 1974 and 1975. External shocks in the form of deterioration in the terms of trade, a rise in interest rates and increased debt accumulation however, had an adverse impact. But world trade growth was favourable for the Guyanese economy during the period and offset these negative shocks. Despite substantial improvement in 1974 and 1975, the external balance once again worsened. The current account deficit in 1976 and 1977 as a fraction of actual output, deteriorated by 0.5 and 0.2 percentage points respectively. This resulted in part from a further deterioration of the terms of trade from 0.12 percentage points of actual output in 1974 to 0.19 in 1976 to 0.22 percentage points in 1977. Table 10 also indicates that there has been an acceleration of world trade growth of 0.8 and 1.4 percentage points in 1976 and 1977 respectively, to improve the current account, but this needs elaboration.

TABLE 10

Decomposition of C/A Deficit as a percent of GDP: 1973 BASE
YEAR

EXPLANATORY FACTORS	1974	1975	1976	1977	1978
1. External shocks 1)	-0.64	-0.21	-0.60	-1.18	-1.41
1.1 Terms of trade deterioration	0.12	0.16	0.19	0.22	0.26
1.2 Interest rate shocks	0.004	0.001	0.017	0.002	0.003
1.3 Retardation of world trade growth	-0.76	-0.37	-0.81	-1.40	-1.67
2. Burden of accumulated debt 2)	-0.016	0.027	0.046	0.068	0.061
3. Other external variables	-0.04	0.04	0.05	-0.03	-0.01
4. Domestic policy actions 3)	0.37	0.98	1.22	0.72	-0.03
4.1 Domestic spending 4)	0.45	0.99	1.14	0.60	-0.123
4.1.1 Gross investment	0.39	0.57	0.55	0.22	-0.19
4.1.2 Consumption	0.062	0.42	0.59	0.38	0.067
4.2 Trade ratios 5)	-0.082	-0.013	0.077	0.121	0.094
4.2.1 Export ratio 6)	-0.072	-0.043	-0.023	0.087	0.074
4.2.2 Import ratio 7)	-0.01	0.03	0.10	0.034	0.02
5. Interaction term	-0.01	-1.01	-0.26	0.61	1.24
6. Ratio of current account deficit to actual GDP	-0.33	-0.17	0.45	0.19	-0.15

1) A positive sign denotes an adverse external shock,
   such as a terms of trade deterioration, an interest
   rate increase, or a deceleration of world trade.
   A negative sign denotes a favourable external shock.
2) A positive sign denotes an unfavourable movement of
   other external variables, such as a net accumulation
   of foreign indebtness between the beginning and
   the end of the period. A negative sign denotes the opposite.
3) A positive sign denotes a deficit increasing policy action.
   A negative sign denotes the opposite.
4) A positive sign denotes an expansion of domestic
   spending which increases the deficit.
   A negative sign denotes the opposite.
5) A positive sign denotes a movement of the trade ratios which
   increases the deficit. A negative sign denotes the opposite.
6) A positive sign denotes a reduction of the exports to world
   trade ratio. A negative sign denotes the opposite.
7) A positive sign denotes an increase of the import content
   of domestic spending. A negative sign denotes the opposite.

This factor measures the ratio of Guyana's exports to actual GDP, but does so indirectly by measuring the ratio of Guyana's export to world export relative to change in the ratio of world exports to Guyana's actual GDP. The latter is regarded as the retardation of world growth and in Guyana's case, it is obvious that if the GDP growth rate is stagnant or negative (see Table 2), this expression for world trade growth, will be favourable. Thus, acceleration in the growth rate of world trade from the estimates in Table 10 is synonymous with a reduction in or slow growth in GDP in Guyana and this may be explained by domestic supply side shocks which the demand driven model is unable to capture.

After a sharp rise in the current account deficit in 1976 and 1977, the deficit as a fraction of actual output showed an improvement of 0.15 percentage points. This was due to an acceleration of world trade growth of 1.7 percentage points. External shock in the form of terms of trade deterioration was 0.26 percentage points while foreign liabilities in the form of burden of accumulated debt and adverse interest rate effects at 0.06 and 0.003 percentage points respectively, were much less significant.

Using 1978 as the base, Table 11 shows that external shocks in the form of terms of trade deterioration, rising international interest rates and foreign liabilities had adverse impacts on external balances during the 1978-1982 period. The current account deficit as a fraction of actual

TABLE 11

Decomposition of C/A Deficit as a percent of GDP: 1978 BASE
YEAR

EXPLANATORY FACTORS	1979	1980	1981	1982
1. External shocks 1)	-4.28	-7.11	-2.52	-1.85
1.1 Terms of trade deterioration	0.12	0.26	0.32	0.32
1.2 Interest rate shocks	0.02	0.01	0.03	0.01
1.3 Retardation of world trade growth	-4.42	-7.38	-2.88	-2.18
2. Burden of accumulated debt 2)	0.09	0.15	0.12	0.13
3. Other external variables	0.51	0.10	0.03	-0.08
4. Domestic policy actions 3)	0.85	-2.03	-1.47	-3.71
4.1 Domestic spending 4)	0.78	-2.05	-1.79	-4.14
4.1.1 Gross investment	-5.66	7.60	1.76	0.59
4.1.2 Consumption	6.44	-9.65	-3.55	-4.75
4.2 Trade ratios 5)	0.07	0.02	0.32	0.43
4.2.1 Export ratio 6)	0.12	0.01	0.07	0.33
4.2.2 Import ratio 7)	-0.05	0.01	0.25	0.10
5. Interaction term	6.93	9.72	4.58	7.43
6. Ratio of current account deficit to actual GDP	2.60	0.83	0.74	1.92

1) A positive sign denotes an adverse external shock,
   such as a terms of trade deterioration, an interest
   rate increase, or a deceleration of world trade.
   A negative sign denotes a favourable external shock.
2) A positive sign denotes an unfavourable movement of
   other external variables, such as a net accumulation
   of foreign indebtness between the beginning and
   the end of the period. A negative sign denotes the opposite.
3) A positive sign denotes a deficit increasing policy action.
   A negative sign denotes the opposite.
4) A positive sign denotes an expansion of domestic
   spending which increases the deficit.
   A negative sign denotes the opposite.
5) A positive sign denotes a movement of the trade ratios which
   increases the deficit. A negative sign denotes the opposite.
6) A positive sign denotes a reduction of the exports to world
   trade ratio. A negative sign denotes the opposite.
7) A positive sign denotes an increase of the import content
   of domestic spending. A negative sign denotes the opposite.

output deteriorated every year during the period with the largest of 2.6 percentage points occuring in 1979. Adverse terms of trade effects continued to be one of the main causes, rising from 0.12 percentage point in 1979 to 0.35 in 1982. In 1981, when the current account deficit as a fraction of actual output deteriorated by only 0.74 percentage points, the adverse terms of trade effect was 0.32 percentage points. The terms of trade losses came about primarily through increases in the import price of fuel and lubricants which coincided with the second oil shock in the 1979-1981 period. The effect of foreign trade growth, as the estimates in Table 11 indicate, was favourable. Foreign liabilities, such as burden of accumulated debt and interest rate shocks, were steady during the period.

Using 1982 as the benchmark, external shocks, excluding foreign trade growth, continued to have an adverse effect on the the current account deficit as a fraction of actual output for all years during the 1982-1985 period (see Table 12). External shocks in the form of terms of trade deterioration and accumulated debt seem to have the largest impacts. In 1983 for example, accumulated debt adverse effect was 0.53 percentage points. The adverse effect of terms of trade was 0.17 percentage points percentage points in 1984. The adverse effects of interest rates have been much smaller, hovering at 0.03 percentage points respectively during the period.

TABLE 12

Decomposition of C/A Deficit as a percent of GDP: 1982 BASE
YEAR

EXPLANATORY FACTORS	1983	1984	1985
1. External shocks 1)	-0.96	-1.01	-1.38
1.1 Terms of trade deterioration	0.06	0.17	0.09
1.2 Interest rate shocks	0.03	0.03	0.05
1.3 Retardation of world trade growth	-1.05	-1.21	-1.52
2. Burden of accumulated debt 2)	0.57	0.01	0.08
3. Other external variables	-0.16	0.04	-0.11
4. Domestic policy actions 3)	-3.33	-4.71	-6.46
4.1 Domestic spending 4)	-3.54	-4.97	-7.55
4.1.1 Gross investment	-0.79	-1.22	-0.35
4.1.2 Consumption	-2.75	-3.75	-7.20
4.2 Trade ratios 5)	0.21	0.26	1.05
4.2.1 Export ratio 6)	0.04	-0.17	0.30
4.2.2 Import ratio 7)	0.11	0.43	0.79
5. Interaction term	3.31	5.56	7.95
6. Ratio of current account deficit to actual GDP	-0.61	-0.11	0.08

1) A positive sign denotes an adverse external shock,
   such as a terms of trade deterioration, an interest
   rate increase, or a deceleration of world trade.
   A negative sign denotes a favourable external shock.
2) A positive sign denotes an unfavourable movement of
   other external variables, such as a net accumulation
   of foreign indebtness between the beginning and
   the end of the period. A negative sign denotes the opposite.
3) A positive sign denotes a deficit increasing policy action.
   A negative sign denotes the opposite.
4) A positive sign denotes an expansion of domestic
   spending which increases the deficit.
   A negative sign denotes the opposite.
5) A positive sign denotes a movement of the trade ratios which
   increases the deficit. A negative sign denotes the opposite.
6) A positive sign denotes a reduction of the exports to world
   trade ratio. A negative sign denotes the opposite.
7) A positive sign denotes an increase of the import content
   of domestic spending. A negative sign denotes the opposite.

While external shocks had played a major part in the worsening of the current account, a significant part can be attributed to the policy response which is decomposed into domestic spending and trade improvements. Table 10 shows that the effects of the government's expansionary policies during the 1974-1977 period were to worsen the deficit as a fraction of actual output by an annual average of 0.8 percentage points. In 1976 and 1977, the adverse effect was 0.99 and 1.4 percentage points respectively. During the 1978-1982 period, the effect of domestic spending was reversed. For all years, except 1979, the effect was to make the deficit as a fraction of actual output smaller, by 2.0 percentage points in 1980 and as much as 4.6 percentage points in 1982. In 1979, the adverse effect was 0.78 percentage points. During the 1982-1985 period, the effect of domestic spending was favourable. In 1983 and 1984 for example, the effect alleviated the deficit by 3.5 and a massive 7.55 percentage points respectively.

While the domestic spending effects were favourable, the total effects of the trade factors since 1976 seem to aggravate the deficit. The import factor indicates that there was virtually no import substitution in all years except 1979. The contribution of export volume growth to the change in the current account deficit as a fraction of output has been apparently adverse since 1977. For the 1977-1978 and 1979-1982 periods, the adverse effect averaged 0.08 and 0.13

percentage points respectively. During the 1983-1985 period, as Table 10 indicates, the effect was less adverse as the average was 0.03 percentage points.

In summary, the estimates in Tables 10-12 suggest that worsening of the deficit as a fraction of actual output during the 1974-1978 period was caused mostly from domestic policy actions relative to external factors. The reverse, however, occurred during the 1978-1982 period as external factors excluding foreign trade growth had the most adverse impact. During the 1983-1985 period, domestic policy actions seem to have had the most favourable impact on the deficit, especially in 1985.[2] External shocks, excluding foreign trade growth, continued to have an impact. While spending restraint by the government indicated favourable developments to alleviate the deficit, the export factor seems to suggest that policies to improve export performance were ineffectual.

The adverse effect of export decline can be seen through a qualitative analysis of the performance of the two most important productive sectors of agriculture and mining. Firstly, in the agricultural sector it seems relatively clear from Table 13 that sugar output declined after reaching a peak output in 1971. However, since 1977 the decline has been particularly severe. For the period 1970-1976 average sugar output was 319,000 tonnes, but for the period

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[2] The deficit decreased because it became literally impossible to finance it due to the country uncreditworthiness.

TABLE 13

Output and Export of Principal Commodities ('000 tons)

| | | | OUTPUT | | | EXPORTS | |
YEARS	DRIED BAUXITE	CALCINED	ALUMINA	SUGAR	RICE	SUGAR	RICE
1970	2290	692	312	311	142	297	59
1971	2188	710	305	369	120	337	68
1972	1652	690	262	315	94	300	70
1973	1665	637	234	266	110	225	48
1974	1383	726	311	341	153	302	51
1975	1350	778	294	300	160	205	82
1976	969	729	265	332	110	297	71
1977	879	709	275	242	212	208	66
1978	1022	590	236	325	182	280	105
1979	1058	568	160	298	143	264	84
1980	1005	592	212	270	166	248	88
1981	983	505	167	301	163	265	85
1982	783	391	73	288	182	251	38
1983	742	315	--	252	148	218	42
1984	769	516	--	242	180	201	51
1985	1049	580	--	243	156	212	32

Source: Government of Guyana Statistical Bureau.

1977-1985, the average output was 273,000 tonnes. This indicates a 14 percent decline in sugar output from the 1970-76 period and operation at only fifty five percent of capacity, given the estimated capacity output of 500,000 tonnes by the government in 1971 (Jagan, 1987). The most dramatic decline in sugar output occurred in 1977 when output fell by 27 percent. This decline was mostly caused by work stoppages due to a strike lasting 135 days because of the government refusal to pay G$238.9 million in accumulated profit sharing as was stipulated in its own Agreement.

While sugar production declined during the 1977-1985 period, there was also a decrease in the percentage of sugar output exported as a percentage of its peak output during the period 1970-1985. During the 1970-1976 period, 88 percent of total sugar output was exported as a percentage of peak output during that period. The percent exported in the 1977-1985 period was, however, only 73 percent. A decrease in the quantity of sugar exported was also accompanied by a fall in the average price received. Table 14 shows that the

TABLE 14

Average Values of Major Exports: US$ per long ton

YEAR	SUGAR	ALUMINA	DRIED BAUXITE	CALCINED	RICE
1972	121	54	9.0	48	173
1973	161	60	9.0	55	248
1974	427	71	9.0	74	432
1975	616	90	13.0	90	440
1976	370	95	16.0	102	406
1977	350	117	18.0	120	397
1978	327	128	19.0	137	359
1979	343	145	21.0	158	378
1980	485	193	25.0	202	432
1981	378	205	26.0	176	470
1982	385	--	--	--	536
1983	328	--	--	--	481
1984	325	--	--	--	--
1985	320	--	--	--	379

Source: Government of Guyana Statistics;
        International Financial Statistics

export price for sugar fell from US$616 per tonne in 1975 to an average of US$343 per tonne for the period 1976-1979. In 1985, the average price received was US$320 while the domes-

tic price, which was subsidized, was approximately one third of that amount. The combined effect of the reductions in export prices and quantities caused the values of sugar exported to fall by 40 percent of the peak value in 1975.

Turning to the rice sector, Table 13 indicates that rice production has increased steadily since 1974 with the exception of minor interruptions in 1976, 1979, and 1983. The most dramatic increase in rice production occurred in 1977 when output almost doubled. For the period 1970-1976, average production was 127,000 tonnes as compared with 170,000 tonnes for the period 1977-1985. This indicates a 34 percent increase in output. The increase, however, should be seen against the production levels of 1964 which was 176,000 tonnes. Also, it has been estimated that 34 percent of the rice lands were not cultivated during the 1970's and early 1980's (Jagan, 1982).

Despite the reasonably good output performance of the rice sector since 1977, the percentage of total rice production exported has been on the decline since 1981. In 1982, there was a 55 percent decline in the quantity of rice exported despite an 8 percent increase in production. Whereas, approximately 50 percent of rice produced is normally exported, during the 1982-1985 period only 25 percent of rice produced was exported. The decrease in the quantity of rice exported was due mainly to a decrease in the portion exported to the Caricom (Caribbean Common Market) coun-

tries.[3] In 1981 and 1982, 93 percent and 98 percent of total exports respectively went to the Caricom countries. During the 1983-1985 period, only 34 percent was exported to the Caricom countries. The Caricom countries imported less because of alleged poor quality and high price of Guyana's rice and also Guyana's monstrous unpaid debt, especially to Trinidad and Tobago, Guyana's largest Caricom buyer (Collymore, 1986). It is also important to note that Guyana receives a preferential price from the Caricom countries for its rice which is approximately 75 percent more than what non-Caricom countries are paying. This is because of an element of subsidization and protection for Guyana's rice in the Caricom.

The characteristics of declining output and export exhibited by the sugar sector were also evident in the mining sector. As Table 12 shows, dried bauxite production has decreased dramatically since 1976. During the period 1970-1976, average yearly output was 1,642 thousand tonnes while during the period 1977-1985, it was only 921 thousand tonnes. This represents a drop in output by 44 percent and 50 percent of the estimated capacity output (Thomas, 1982). Calcined bauxite, of which Guyana had a near monopoly, also showed a decline from an average yearly output of 709 thousand tonnes during the 1970-1976 period to 530 thousand

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[3] With the reduction of availability of wheat flour and the foreign exchange constraint, some of the increased production may have been used for domestic comsumption and illegal exports respectively, resulting in a decline in legal exports.

tonnes for the 1977-1985 period, i.e., a decline of 25 percent and production at 43 percent of estimated capacity. Alumina output also followed the downward output trend as yearly production for the 1970-1976 period was 283 thousand tonnes, but it was only 193 thousand tonnes for the 1977-1984 period, i.e., a 32 percent decline and production at 57 percent of capacity. Over all, the total output of bauxite products decreased from a yearly average of 2,634 thousand tonnes during the 1970-1976 period to 1,644 thousand tonnes for the 1977-1985 period. This represents a 38 percent decrease in yearly production which is also only 50 percent of the estimated capacity.

Since all alumina and bauxite produced are exported, and since price increases were proportionally less than declines in quantity exported, a decrease in production is associated with a decrease in foreign revenue. While diminishing foreign markets were considered to be at the core of the crisis in the mining sector, this was difficult to substantiate as the estimates in Table 13 reveal. Guyana's problems seem to stem from insufficient foreign inputs and inefficiencies, because Guyana can export all the alumina and bauxite products it produces. Guyana was, however, unable to satisfy the available markets through shortfall of production quantities ordered and inability to meet delivery schedules. This led to other suppliers, such as Jamaica and China, making serious inroads into Guyana's foreign markets (Thomas, 1982).

2.8   CONCLUSIONS

The balance of payments crisis during the 1976-1985 peri-
od, seems to have been brought about by both external and
internal factors. The decomposition scheme indicates that,
during the 1974-1978 period, it was internal factors that
dominated, while during the 1978-1982 and 1983-1985 periods,
it was the external factors excluding foreign trade growth
that prevailed. Given the severity of both factors in agg-
ravating the current account deficit, one important observa-
tion from this analysis that ought to be underscored is the
continued adverse performance of the export sector which
invariably depends on total output. With the economy con-
tinuing to depend on foreign intermediate goods, capital
goods and technology, it seems that export earnings consti-
tuted a crucial constraint on economic growth. With the
external shocks, it seems as if an alleviation of the crisis
depends critically on the provision of foreign exchange to
import inputs, accompanied by sound government policy.
Accordingly, the next chapter examines the menu of policies
that developing countries can choose from to alleviate their
crises.

Appendix A

METHODOLOGICAL NOTE (HELLEINER, G.,1986)

The current account deficit (D) at time (t) is given by

$$D(t) = M(t) + V(t) - E(t) - T(t) \quad \ldots (1)$$

where $M(t)$ and $E(t)$ are imports and exports of good and non factor services respectively, $V(t)$ is net factor services to abroad and $T(t)$ is unrequited transfers.

$M(t)$ is expressed as the product of price (Pm) and volume indicies (J):

$$M(t) = Pm(t)J(t) \qquad \ldots (2).$$

The volume index (J) is further expressed as the product of an overall import coefficient (j) and real domestic absorption (A):

$$J(t) = j(t)A(t) \qquad \ldots (3).$$

Domestic absorption is the sum of consumer spending (C) and investment (I):

$$A(t) = C(t) + I(t) \qquad \ldots (4).$$

$V(t)$ is expressed as the cumulative of net interest to abroad (Vi), other net investment abroad (Vd), and net workers remittance abroad (R):

$$V(t) = Vi(t) + Vd(t) - R(t) \quad \ldots (5).$$

Net interest is the product of the current dollar interest rate (r) and net stock of foreign debt at the end of the previous year (F):

$$Vi(t) = r(t)F(t-1) \quad \ldots (6).$$

Et is expressed as the product of the price (Px) and volume indicies (X):

$$E(t) = Px(t)X(t) \quad \ldots (7).$$

The export volume index (X) is further expressed as the product of an overall export coefficient (x) and the real value of world trade (W):

$$X(t) = x(t)W(t) \quad \ldots (8).$$

T(t) is unrequited transfers.

Substituting equations (2) to (8) into equation (1) and dividing the result by the gross domestic product (Y) in nominal domestic currency gives

$$D(t)/Y(t) = j(t)Pm(t)[C(t)/Z(t) + I(t)/Z(t)]$$

$$+ r(t)F(t-1)/Y(t) + Vd(t)/Y(t)$$

$$\_ R(t)/Y(t) - x(t)px(t)W(t)/Z(t)$$

$$- T(t)/Y(t), \quad \ldots (9)$$

where Z is the real gross domestic product.

By taking the first difference of equation (9), the final formula is obtained.

$$d[D(t)/Y(t)] = \{j(s)[C(s)/Z(s)]dpm(t)$$

$$- x(s)[X(s)/Z(s)]dpx(t)\}$$

$$+ [F(s-1)/Y(s)]dr(t)$$

$$- x(s)px(s)d[W(t)/Z(t)]$$

$$+ r(s)d[F(t-1)/Y(t)]$$

$$+ d[Vd(t)/Y(t)]$$

$$- d[R(t)/Y(t)] - d[T(t)/Y(t)]$$

$$+ j(s)pm(s)d[C(t)/Z(t)]$$

$$+ j(s)pm(s)d[I(t)/Z(t)]$$

$$+ pm(s)[A(s)/Z(s)]dj(t)$$

$$- px(s)[W(s)/Z(s)]dx(t)$$

$$+ \text{interaction term} \quad \dots (10),$$

where the symbol d before the variable indicates the change in value of this variable between each year and the base year, and where the symbol s indicates the year for the weights of the decomposition term. The symbol s employed in this estimate is the average of the current year and the base year.

The term in equation (10) are identified as: Variation in the current account deficit ratio to GDP between final year and base year = terms of trade deterioration + interest rate shock + retardation of world trade growth + burden of debt accumulation + change in direct investment income - change in workers' remittances - change in unrequited transfers + consumption contraction + investment reduction + import replacement - export penetration + interaction effects and adding-up errors.

In Tables 10 to 12, changes in direct investment income, workers' remittances and unrequited transfers were consolidated as "other external variables".

Chapter III

LITERATURE REVIEW ON EVALUATION OF STABILIZATION
PACKAGES

3.1   INTRODUCTION

This chapter discusses the IMF and World Bank's stabili-
zation programs, both theoretically and empirically. Since
the literature on stabilization is vast, it is important at
the outset to mention that a review of the mountain of lit-
erature is beyond the scope of this study. This study,
therefore, presents an analysis of the main features of the
IMF and World Bank's stabilization programs. The organisa-
tion of the study is as follows: section 2 discusses the
objectives of stabilization; section 3 discusses the stan-
dard IMF program, focusing on its conditionality and theo-
retical base; section 4 discusses the critiques of IMF con-
ditionality; section 5 assesses the IMF programs and
practice; section 6 discusses an alternative to the IMF pro-
gram; section 7 discusses the World Bank's program, empha-
sizing its similarities with and differences from the IMF
program; and section 8 provides some concluding remarks.

3.2   OBJECTIVES OF STABILIZATION

Stabilization policies prescribed for an economy are gen-
erally geared to smoothen and stabilize cycles of economic
activities.   In   particular,   countries   seek the   internal
goals of increases in economic growth or full employment
with reasonable price stability, the external goal of bal-
ance of payments equilibrium and social goals, such as those
of reducing inequality and poverty. Depending on the circum-
stances in an economy, those goals usually vary in impor-
tance and in the degree of difficulty in meeting them.

Often, stabilization programs are undertaken when there
is external imbalance. External imbalances can emerge for a
number of reasons which can, however, be categorized under
the two broad headings: internal and external factors.
Between 1950 and 1973, internal factors were the most common
source of imbalance globally, however, changes in the exter-
nal economic environment after 1972, such as deterioration
of the terms of trade,   rising international interest rates
and recession, have resulted in special attention being paid
to external factors. Even where the source of the imbalance
is external, however, internal policy responses can either
mitigate or exacerbate the problem so the break down between
external and internal causation is not a clear one.   Some
authors reduce the persistence of crisis, therefore to
domestic policy shortcomings.   For example, it is argued
that adverse external trends are compounded as "external

inflationary pressures from rapid increase in the cost of imported manufactures have been intensified by an expansionary monetary policy. Export growth has been handicapped by overvalued exchange rates, inadequate price incentives for producers, and the mismanagement of agencies handling credit, marketing, and export promotion .... (Further) some developing countries postponed domestic policy reforms, or introduced them only slowly, and relied on increased external borrowing ... (and) deficit spending" (Stern 1983:88).

Indeed, it seems as if developing countries must act on external imbalances within the external context they face. While measures to alleviate external imbalance include a wide range of policies, from fine tuning aggregate demand to stimulating supply, achievement of the stabilization objective is a difficult process. The adoption of certain policies can make matters worse if they are influenced only by stabilization. For example, macroeconomic analysis predicts that cutting government spending may reduce the size of the deficit, however this may also result in an increase in the incidence of poverty and a worsening of the distribution of income. Hence, there exists the possibility of contradictory objectives.

The wide range of policies available to alleviate external imbalances can be divided into four headings. These include: (1) aggregate demand restraints; (2) exchange rate and other policies with the intention of "getting prices

right"; (3) liberalization of trade and prices; and (4) quantitative restrictions. Macroeconomic analysis predicts that the effect of restraining aggregate demand is reduced aggregate spending, hence lower prices for nontradeables. This will automatically lead to a rise in exports and a fall in imports. Exchange rate policies and those for liberalization are based on market analysis which predicts that changes in relative prices will: (a) allocate resources more efficiently and hence to the export sector; and (b) depress imports and simultaneously cause a switch from imports to domestically produced goods. Quantitative restrictions are based on the assumptions that there are fundamental problems of establishing prices, allocating resources and distributing income, hence, government intervention is required.

When external imbalance becomes serious, that is, when imports can no longer be reduced and/or difficulties are experienced when making interest payments and principal repayments, it is argued that adjustment tends to be costly and disruptive. To ease the burden of adjustment, the help of the IMF and World Bank is often sought. The IMF lends to the member country, experiencing temporary balance of payments imbalance, with the objectives of correcting the imbalance and simultaneously fostering national and international prosperity. In light of these objectives, the IMF designs its stabilization program.

When the need for adjustment continues, due mainly to the severity of the balance of payments imbalance, and financing from the IMF and other external source being limited, help is often sought from the World Bank's program of structural adjustment loans (SAL). The SAL is designed with the objective of strengthening the balance of payments and reorganising the country's development strategy over the medium term (Stern, 1983).

3.3 IMF CONDITIONALITY AND THEORETICAL BASE

When using the Fund's resources, except when drawing from their reserve tranches, the members are expected to follow certain policies of the Fund which, it asserts, would assist in mitigating the balance of payments disequilibrium and simultaneously assure the revolving character of its resources. This conditionality acts as a co-insurance against moral hazard and is in accordance with the Fund's objectives of balanced growth of international trade which will contribute to high levels of employment, real growth and the development of productive capacity. It is also placed on members, supposedly, indiscriminatingly by focusing on the nature of the problem which can be transitory, such as cyclical declines in exports; or long term, such as deterioration in the terms of trade, excessive domestic demand, cost-price distortions or overvalued exchange rates.

IMF's conditionality is based on the premise that members' external imbalances are the result of excessive demand pressure on resources and market regulations, which are brought about by excessive money creation through credit, and government intervention. The Fund asserts that this imbalance can only be mitigated by sound policies which often include demand restraint policies, dismantling of quantitative restrictions and policies to change relative prices, such as devaluing the exchange rate to appropriate levels. The adoption of these policies is important for the achievement of the performance criteria required by the IMF which often include: (1) limits on domestic assets; (2) limits on net domestic bank credit to the non financial public sector; (3) targets for the net international reserve position; (4) limits on new public and private debts; and (5) no further restrictions on imports and introduction of new multiple currency practices. These requirements have to be met periodically (annually or quarterly) so as to provide continued access to IMF's resources, private loans and debt rescheduling. It is important to note that while the Fund acknowledges that adjustment will be painful, it argues that the situation might be worse and hence more painful without its lending.

3.3.1 Standard IMF's Policies for Stabilization

Given the nature of the balance of payments problem, the member's policy objectives and measures to achieve these objectives, the Fund supports programs focusing on a limited number of macroeconomic variables that emphasize, but are not restricted to, demand management policies. The demand management policies are intricately related to the monetary approach to the balance of payments (MABOP) and form the foundation for other related policies such as those of the supply side and those to improve international competitiveness. The Fund's package often includes: (1) placing limits on the money supply and credit to restrain excessive demand; (2) devaluation of overvalued exchange rates; (3) increasing interest rates to real positive levels; (4) increasing public goods prices (i.e., reducing subsidies on food, welfare services and liberalizing price controls) to market levels; (5) reduction of real wage; and (6) liberalization of trade and foreign exchange.

The Fund's position on the use of these policies rests on the tacit assumption that the imbalances are due to internal mismanagement, widespread government intervention or failure to adopt policies in face of external shocks. In adopting these policies, the Fund contends that the program country may be able to secure larger levels of non official capital inflows by being creditworthy through the IMF's de facto guarantee. These policies the Fund argues would also foster

long term growth, balance of payments and fiscal equilibrium, and price stability. Generally, the demand management policies would affect aggregate absorption, while supply side policies would affect factors of production through the allocation of resources, all of which intend to expand exports and reduce imports by excessive import substitution. It is argued that export promotion will generally create more employment since the exports of the large number of developing countries are relatively labour intensive. Increase in employment, the Fund argues, may also lead to a more equitable distribution of income. In addition to these gains, it is argued that the potential for dynamic gains are even greater. In particular, it is argued that trade introduces new technologies and skills which have the possibility for triggering supply shocks which can improve the living conditions of the population. The important conclusion from export promotion is that there is likely to be "expansion of a resource based commodity, this in turn induces high rates of aggregate and per capita income" (Meier,1984:491).

With a belief in such outstanding advantages from trade, it is not surprising that the Fund requires reduction of protection and government intervention, and more dependence on market incentives to correct both internal and external imbalances. The stabilization package, as a result, seems to be more in line with the orthodox economic approach to stabilization (Loxley, 1986).

3.3.1.1   The Monetary Approach to Balance of Payments (MABOP)

The MABOP emphasizes that an excess supply of money is the counterpart of an excess demand for goods and results subsequently, in balance of payments disequilibrium and price increases. Thus, the crucial element is to restrict the money supply by constraining the ability of government and the private sector to borrow. The theoretical development of the monetary approach to balance of payments is credited to a number of intellectuals from diverse backgrounds. These include the writings of J. J. Polak (1957), Mundell (1971), H. Johnson (1977), R. Dornbush (1973) and M. Mussa (1976). It is argued that the balance of payments is essentially a monetary phenomena and should be analysed in terms of monetary instruments, i.e., money supply and money demand. To understand the implications of the approach, we look at the basic features of the model.

The supply of money is given by the basic equation:

$$MS = v (F + D) \quad . \quad . \quad . \quad . \quad (1)$$

where v is the money multiplier, F is international reserve in domestic currency value and D is the domestic credit. The demand for money is given by:

$$Md = k(P,Y) - 1(i) \quad . \quad . \quad . \quad . \quad (2)$$

where k denotes the proportion of money income (Y), P is the price level and 1 denotes the interest sensitivity of the asset demand for money. The balance of payments identities are given by:

$$F = X - M + B(i) \ . \ . \ . \ . \ (3)$$

where (X - M) is the trade balance and B is the capital account - a positive value of B is associated with a net capital inflow (or surplus) and a negative value of B is associated with a net capital outflow (or deficit), i is the domestic interest rate.

Equilibrium in the money market occurs when the supply, eq. (1), and demand, eq. (2) for money are equal. That is,

$$Md = k(P,Y) - 1(i) = v(D + F) = Ms \ . \ . \ . \ . \ (4)$$

or, $F = \{[k(P + Y) - 1(i)] \ / \ v\} - D \ . \ . \ . \ . \ . \ . \ . \ (4a)$

or, $F = (Md \ / \ v) - D \ . \ . \ . \ . \ . \ . \ . \ . \ . \ . \ . \ . \ . \ (4b)$

Equation (4) indicates the relationship between external balance (F), domestic credit (D), and money demand (Md). From equation (4b), the external balance (F) depends on the difference between the demand for money (adjusted by the money multiplier (v)) and the amount of domestic credit (D). With the assumptions (Polak, 1957) that: (1) capital is immobile; (2) the exchange rate is fixed; (3) the velocity is constant; (4) money supply is equal to nominal income

from assumption 3; (5) credit and exports are exogenously determined; and (6) import is a fixed proportion of last period's nominal income, equations (4a) and (4b) indicates that a deficit on the balance of payments implies a decrease in reserves. This, however, can only persist if domestic credit is positive or there is a decrease in the monetary base through dishoarding. Dishoarding, however, can only be temporary; as such, a balance of payments deficit can only persist if there are excess money balances. These excess money balances according to the monetary approach will ultimately leak abroad, i.e., be used for buying foreign interest-earning assets and/or foreign goods. These transactions require foreign currency which domestic currency is used to buy, thus, there is a decrease in the foreign reserve held at the central bank.

Under the assumption that the domestic economy of the developing country is integrated with the world economy, it implies the presence of capital mobility and the assumptions of the extreme monetarists that income, prices and interest rates are exogenously determined. In particular, the income level is determined by flexible wages while interest rates and price levels are determined by arbitrage from the world market. Under these assumptions, equation (4a) indicates that an increase in prices (P) or a decrease in real income (Y) will increase the demand for money, hence, an increase in reserves which will result in an external balance surplus

(F > 0). An increase in the interest rate will decrease the demand for money which requires a reserve outflow, thus causing a payment deficit.

In conclusion, the monetary approach underlines the core of the stabilization programs stipulated by the IMF. That is, to eliminate a balance of payments deficit, there should be quantitative control over credit since excess money supply is the counterpart to losses in international reserves. Often, the control over credit focuses on reducing government budget deficits since spending beyond its income requires borrowing, hence money creation. As a result, a typical fiscal package of the Fund usually includes expenditure reducing policies, such as removal of subsidies, reduced capital and recurrent government spending. Also, there are tax increasing policies, such as establishment and increases in user fees for social services and other indirect taxes which may also help to change relative prices.

3.3.1.2   Devaluation

Devaluation is a principal short term policy tool often included in the IMF stabilization program. It is prescribed from an attitude of theoretical eclecticism, that is, the best of the traditional competing theories are used without losing the consistent theoretical structure. The IMF asserts that an overvalued exchange rate causes: excess demand for foreign exchange which triggers reserve losses

and external imbalances; rationing which causes inefficient allocation of resources, increasing cost of bureaucracy and corruption; capital flight; a parallel market; and a biased trade regime (Nowak,1985; Khan and Knight,1985). Thus, a devaluation or 'an appropriate exchange rate' can mitigate not only the balance of payments problems but also, foster growth and development.

Devaluation is often used when there is 'fundamental disequilibrium' and is, supposedly, to be used occasionally so as to promote exchange stability. Advocates of the policy argue that a devaluation is equivalent to a reduction in the real money supply because the price of tradeable and non-tradeable goods and services will increase, thus reducing the real value of money balances and consumption. In this respect the outcome is similar to that of the monetary approach. Also, if prices for non-tradeable goods remain constant while those for tradeable goods increase, resources will move into tradeable production. This will cause an increase in the quantity and value of exports. Thus, a devaluation can improve the balance of payments by affecting both the demand and supply sides by reducing real balances, and hence absorption and by reallocation of resources through relative price changes. Together, these would serve to increase exports and reduce import demand. This outcome will, however, depend crucially on appropriate demand restraining policies, as emphasized by the IMF. Other rea-

sons for devaluation include: (a) the opportunity for export and profits will be more lucrative given improved competitiveness from a devaluation, thus an attraction to foreign investors; and (b) resources will be used more efficiently, since a devaluation entails fewer restrictions and controls.

3.3.1.3   Liberalization of Prices, Foreign Exchange and Trade

The IMF often includes in its standby agreement measures for deregulating the economy by removing price, interest rate, trade and exchange controls and subsidies. The rationale for this is that government intervention is a major source of inefficiency, especially in the allocation of resources. The market, the advocates contend, is a superior mechanism for the allocation of resources; given the adverse effects of regulations. Further, it is argued that the rigidities introduced by quantitative controls may not only reduce current but also potential output from lack of potential investment due to lack of confidence in the country's currency and economy. The end result may well be an exacerbation of the production crisis. As a result, the IMF emphasizes the importance of 'getting prices right' as a concomitant to efficient allocation of resources through market processes, which will bring about balance growth and economic stability.

Liberalization of prices is advocated because it will not only eliminate the distortions in the relative prices, often caused by imperfect markets, government regulation, taxes, subsidies, and other quantitative restrictions, but also because it will reduce absorption and hence, an improve the external balance.

Often, two sources of inefficiency are underscored by the IMF, those from energy and agricultural pricing policies (Khan and Knight, 1985). It is argued that despite the rapid increases in energy prices during the last decade, developing countries have not passed on higher prices to the consumers. Instead, the governments have been subsidizing energy and absorbing the cost in its budget deficit. Also, it is argued that, such a policy tends to slowdown the shift to less energy intensive productive technique and consumption. Thus, there is an adverse effect on resource allocation. With regards to agricultural pricing policy, it is argued that the policies of the Marketing Boards, present in most countries, often set prices which deviate from prices in the competitive market and hence don't provide enough incentives for increases in production.

Liberalization of nominal interest rates is advocated to increase savings from both domestic and foreign sources. It is argued that the increase in interest rate to positive levels, will not only raise real savings but also increase the flow of capital from abroad and allocate resources more

efficiently, thus fostering growth and alleviating the external imbalance.

Liberalization of trade is advocated to promote export and growth by correcting the shortcomings of import substitution or inward oriented strategies of development. These shortcomings include: (1) the development of the the manufacturing sector at the neglect of others; (2) higher domestic cost of production, resulting from inefficient plant size; (3) increased unemployment because of the capital intensive nature of the strategy; (4) small foreign exchange savings because of increased capital goods importation; (5) distortions and welfare losses resulting from higher prices of manufactured goods and lower relative prices for agricultural output; and (6) increased budget deficits resulting from decreased revenues and increased subsidies given the poor performance of other sectors in the economy (Meier, 1984).

Theoretically, it is argued by Belassa (1982), Krueger(1981) and others, liberalization will cause resources to shift from import competing activities to export activities. Production would occur according to comparative advantage where there would be an increase in both traditional and non traditional exports from minimum efficient plant size, increasing returns to scale and the mechanisms of competition.

Krueger (1981) argues, that the liberalization of trade and payments provides the potential for developing countries to raise their long-term annual growth rate by 2 or 3 percent per annum. Krueger contends that trade regimes biased towards import substitution are inefficient because of misallocation of resources. She argues that trade liberalization will entail expenditure switching from import substitutes and increased investment output in the (favoured) export sector. Further, liberalization will have to be genuine to provide investors with confidence as to the persistence of such policies. Where this is so, the stabilization programs are more credible and hence output and growth are greater. Krueger also argues that import liberalization can be used to reduce inflation. She argues that in the presence of quantitative restrictions, the price for imports includes a premium on import licenses and is therefore greater than the price prevailing when there is free trade.

Liberalization of foreign exchange is advocated to eliminate the distortions of exchange controls which often result in: (1) misallocation of resources because import transactions are restricted, hence sacrificing the benefits of free trade; (2) rationing which can lead to favouritism, corruption and even discrimination, hence problems of equity; (3) lack of economic freedom since imports are restricted; and (4) the establishment of a parallel market where something similar to (or greater than) the free market price normally reemerges.

While all the factors listed above vary in their impact on welfare and growth, it is argued that the consequences of a parallel market are often devastating, exacting heavy welfare and production costs from the economy (Bhagwati and Hansen,1973; Sheikh,1974; Krueger,1974; Bhagwati,1978; Nowak,1984). In particular it is argued that, the consequences of higher premiums in the black markets (including smuggling) are: (1) inefficiency through a reallocation of resources to the non-traded or inefficient import competing goods sector since higher prices (often from the depreciated exchange rate in the parallel market and scarcity of goods in the official market) of illegal imports cause those firms to operate which would be doomed in a free market; and (2) misallocation of resources as productive resources are used for rent seeking. The diversion of resources from productive to unproductive activities may well result in an immiserization of growth.

Three major studies illustrate the consequences of a parallel economy. Bhagwati and Hansen (1973), restrict their analysis to a smuggling situation and test the welfare implications. They conclude that smuggling cannot be welfare ranked vis-a-vis a non-smuggling situation. Their conclusion emanates from the welfare effects of a trade diverting customs union where there is a terms of trade loss from the partner (smuggling sector). If the smuggling sector brings in imports that are cheaper than legal imports, then

there is trade creation (welfare improvement). However, if smuggling brings in imports that replace lower cost legal imports, then there is trade diversion (welfare reduction or immiserization). Bhagwati and Hansen further note that when there is a prohibitive tariff, the nonsmuggling situation is autarkic. The presence of smuggling is thus an evasion of the trade barrier and is similar to a trade creating customs union where there is welfare improvement. The model, however, implies that the tradeable goods are invariant to smuggling.

An extension of the Bhagwati and Hansen model by Sheikh (1974) illustrates that the production of exportables will change with smuggling. Sheikh makes the assumptions that illegal trade requires the use of primary (domestic) resources (i.e., a third non trade good), risks and increasing resource cost (i.e., cost of circumvention). From his analysis, Sheikh concludes that the production of the tradeable good decreases in the presence of smuggling, because fewer resources are available for production since more are drawn into illegal trade. Sheikh's model also has the possibility for welfare improvement when legal and illegal trade coexist in the presence of a tariff which is distortionary.

In an alternative to Sheikh's and Bhagwati and Hansen's models, Krueger (1974) assumes that the policy intervention of quantitative restrictions is distortionary and illustrates activities of rent seeking, i.e., activities which

carry premiums or windfall profits as a result of such poli-
cy. From the analysis, Krueger shows that with fixed labour
involved in the distribution of imports and agricultural
output, the presence of import restrictions gives rise to
rent seeking because of higher premiums, causing more people
to be employed in distribution-cum-rent seeking. This
results in a real production cost as less agricultural out-
put is produced from the movement of labour away from pro-
duction. The cost of quantitative restrictions in Krueger's
analysis is similar to that of Sheikh's where the cost is
production foregone plus the tariff. The conclusions from
Krueger's analysis, however, can be generalized to situ-
ations where price controls or exchange controls give rise
to black markets, since higher premiums will result in more
people participating in distribution.

Production costs of smuggling are not the only conse-
quence of the parallel economy. It is argued that it reduces
government revenues (Tanzi, 1984), foreign exchange reserves
(Nowak,1985) and negatively affects the moral fibre of soci-
ety (Gray and Walter,1975), which seem to aggravate the
problems the authorities intend to cure. For example, price
control to protect consumers from high prices often results
in higher prices through the black market than through the
free market (Gonensay, 1966). Further, exchange controls to
restrict the depletion of foreign exchange and as an alter-
native to devalue the currency, often result in increased

capital flight and larger depreciation (Nowak, 1985). Restriction of imports to promote the domestic objective of import substitution or self sufficiency often result in increased scarcity from the diversion of resources. The consequences of these further result in implications for policy which sometimes work against the goals. For example, expansionary policy which is aimed at stimulating growth may instead trigger accelerating inflation.

3.4   CRITIQUE OF IMF'S CONDITIONALITY

The Fund's conditionality has been systematically criticized as being bitter medicine imposed on the member country. The adversary relationship between the IMF and the member country, focuses on the nature and form of IMF's conditionality. First, critics such as, Rweyemamu, 1980; Dell,1982; Dale,1983; and Spraos,1984, argue that the conditionality is rigorous and undifferentiated and causing the deficit countries to underutilize their conditional facilities. The reluctance to accept IMF conditionality usually causes developing countries to postpone going to the IMF until their economic problems are intensified. The developing countries, as a result, treat the IMF as a last resort (Moffit,1983:124) and as such, will need more strenuous adjustments - hence more stringent conditionality.

Second, it is argued that the Fund doesn't provide enough effort to determine the actual or potential cause of the

imbalance experienced by developing countries. That is, whether it problems are internal or beyond the country's control, such as external shocks and structural problems. Only through this distinction, Rweyemamu (1980) argues, can the magnitude of adjustment, the financial support and conditionality be properly assessed.

Third, it is argued that performance tests are often rigid and usually based on inadequate data (that is common in LDCs) and imprecise projections (Rweyemamu,1980:90). Since continued funding depends on these tests, it is argued that the need for changing the underlying assumptions and nature of the performance criteria is great. In particular, Rweyemamu (1980) argues that there should be provisions for inadequate data and also unforeseen shocks. Spraos (1984) on the other hand argues that instead of the increasing use of policy instruments as performance criteria, policy targets should be considered. Spraos argues that policy targets require firm commitments while instrument should be flexible and adaptable to change. The former, he argues, is more likely to succeed.

Fourth, it is argued that the responsibility of adjustment in light of the magnitude of the external shocks is one-sided. In particular, critics argue that adjustment should not be borne by LDCs alone but also by countries running balance of payments surpluses if global monetary order is to be maintained.

Fifth, critics argue that the IMF conditionality is based on monetarist grounds where the emphasis of theory and policy has been embedded in macroeconomic variables following the doctrine of the monetary theory of balance of payments adjustments and laissez faire ideology. Further, the IMF focus on the monetary approach rests on the presumption that the use of market analysis is superior to macroeconomic analysis, where prices and wages change to bring markets into equilibrium.

Finally, it is argued that the Fund's instruments are within a capitalist framework that encourage private enterprise and markets. This reliance on competitive market laws and the price system is contentious to many developing countries because of the systems' politics and not necessarily its economic analysis. There are, however, strong economic reasons for state and market interventions.

In addition to these criticisms, IMF conditionality has been criticized on both theoretical and empirical grounds. This will be the focus of attention in the next two subsections.

3.4.1 Relevance and Effectiveness of Fund Supported Programs

Given the Fund's monetary framework, the theoretical presuppositions, efficacy and adequacy of the rules and mechanisms are frequently questioned. The criticism are mostly

associated with the Keynesian and structuralist school of thought. The Keynesians criticise the very foundation on which the IMF's monetary theory is based on. The criticisms are concerned with three main issues: (1) concentration on monetary factors to the exclusion of other real factors; (2) reliance on the Walrasian law of general equilibrium; and (3) the unrealistic assumption of full employment and constant velocity of circulation.

With regards to the first issue, Frenkel and Johnson (1976) argue that the model pays little attention to real variables, such as real income and resource absorption, operative in an economy. The real sector of production is merely a derivative from money supply and money demand. Corden (1977:48) further stresses that "the strongest argument one can make for it as the key figure is that it focuses on the central bank's principal portfolio problem. The difficulty here is that the country, and more particularly the public sector, consists of more than the central bank".

The dependence of the monetary approach on the Walrasian law of general equilibrium, it is argued, has given rise to a theoretical difficulty. Tsiang (1977:336) elucidates that Walras' Law "applies only to simultaneous settlement of all exchange transactions on all markets at a single set of prices" which cannot be achieved in the real world because transactions are not simultaneous and expenditures are not synchronized. Thus, "if the modern monetary approach to the

balance of payments claims Walras' Law as its theoretical foundation, then it is built on shaky grounds".

The validity of the assumptions of full employment and the constancy of the velocity of circulation have also weakened the credibility of the approach. Frenkel and Johnson (1976:25) argue that "the assumption of normally full employment reflects the passage of time and the accumulation of experiences of reasonably full employment as the historical norm". The norm in underdeveloped countries, however, is tied to the experience of significantly less than full employment of all factors. Thus, they argue, the assumption of full employment is unrealistic. With regards to the constancy of the velocity of circulation or approximately so, the Keynesians argue that velocity is a function of a number of variables such as the price level, interest rates, wealth and real income. These variables, it is argued, undoubtly, affect the velocity of circulation throughout the various business cycles. For example, it is argued that the overall velocity of the entire money supply depends upon how it is divided between transaction and asset balances. As a result, there are limitations on the use of the assumption of equilibrium of money supply and demand.

The structuralists critique begins with the assumption that common characteristics such as dependence on imported capital goods, inelastic food supply, low productivity in agriculture, reliance on primary commodity exports which are

highly inelastic (both in demand and supply), imperfect market structures, and underdeveloped financial institutions are present in LDCs and are significantly different from DCs. As a result, the impacts of IMF's stabilization program in LDCs are different from those experienced in DCs. The critique focuses on the short term impact of the IMF's package on the achievements of the supposed goals of an improvement in economic growth, the balance of payments, reduction in inflation and distribution of income.

The structuralists argue that the demand restraining measures prescribed by the IMF are inimical to growth. They claim that the balance of payments problems facing the LDCs are essentially 'development deficits' resulting from increased importation of capital goods for industrialization. Thus, correcting a 'development deficit' by restraining demand is synonymous with retarding growth as the bottlenecks are perpetuated from the nonavailability of resources. The situation is further worsened when demand restraints are adopted to correct external imbalance caused by external shocks. In particular, Taylor (1983) argues that the restriction on credit does not only cause an increase in interest rates, hence an increase in capital costs, but also causes a decrease in the importation of intermediate goods which may lead to a recession.

The characteristic of underdeveloped financial markets in LDCs, the structuralists argue, provides limited scope for

the efficacy of monetary and fiscal policy. Some structuralists argue that these instruments will only affect the organised market while the unorganised market will be unaffected. Others argue that an increase in interest rates will not raise real savings but may shift financial savings from the unofficial to the official markets. Further, it is argued that savings and capital flows tend to be related to the political climate and nature of the economic system in developing countries. It is argued that regardless of the magnitude of the increase in interest rates, savings are unlikely to increase if there are serious political instabilities. Also, if the government is espousing a socialist path then savings and even capital flows would depend on the ability of the government to stimulate more savings and secure more capital inflows through non-price means. Further, it is argued that imperfect, fragmented and underdeveloped product and resource markets also impede the equilibrating mechanisms of the price system in allocating and distributing resources to foster growth.

Other criticisms stem from possible major shortcomings of the orthodox, export oriented, strategy which may result in slower growth. A list of the shortcomings include: (1) persistence of inefficiency through poor management, poor quality products, workers alienation and excessive scale; (2) relative price increases biased towards export industries which might raise profits in inefficient export industries

at the expense of others; and (3) inconsistency of measures
to enhance competition as increased production for export in
the international market may result in oligopolistic or mon-
opolistic market structure in the export sector while compe-
tition is advocated in the whole economy (Meier,1984).

Some critics also question the efficacy of the IMF stabi-
lization package for growth and development. Cheryl Payer
(1974) argues that the export promotion strategy of the IMF
would strengthen the LDCs' dependency on the DCs by pushing
the LDCs into the whims of the market and into a debt trap
from the infusion of private and official capital. This may
result in a surplus drain and frustration of autonomous
development since MNCs and International banks are likely to
have greater control over domestic economic activities.

In summing the critics arguments, Dell (1982, 598) argues
that the use of tight monetary policy to deal with the prob-
lem is costly and contradicts the IMF's priorities of growth
because "in a situation of increasing inadequate effective
demand, growing underutilization of productive capacity and
soaring unemployment, the pressure continues for even great-
er reduction of demand, which is likely to increase the vol-
ume of idle capacity and unemployment still further."

Turning to inflation, the structuralists argue that the
demand restraining policies adopted by the IMF views infla-
tion as essentially, demand pull. The efficacy of these pol-

icies in controlling inflation occurring from other sources and conditions is questionable. The structuralists argue that bottlenecks, as well as external shocks such as increased debt payments, deterioration in the terms of trade from rising import prices, retardation of world trade growth and the denial of aid and grants, often accounts for a large part of the inflation in LDCs. It is argued that if inflation is related to monetary factors, then this is caused through the overall structural conditions existing in the LDCs. The IMF package is also likely to be inflationary because of the imperfect market structure. In LDCs, perfect competition is almost nonexistent. Monopolistic and oligopolistic market structures are more prevalent, and as a result, prices are higher. The elimination of price controls and subsidies also cause prices to increase. Increases in interest payments, resulting from allowing interest rates to move to positive levels and from credit contraction, may cause cost-push inflation. The overall effect of these increases in prices may very well be wage-push inflation, as unions fight to preserve income shares.

Devaluation also causes inflation and stagflation. Taylor (1983) argues that a devaluation will increase the domestic price of imports and production which uses imported goods. As a result, the domestic output price will increase. Stagflation may occur if there is a decrease in aggregate supply due to higher costs of imports from the devaluations.

The efficacy of the IMF's package for improving the balance of payments is also disputable. First, it is argued that because small open economies often subscribe to a fixed exchange rate, it makes the monetary authority impotent in controlling its monetary policy. It is argued that because there is often a lag between the acknowledgement of the need for a devaluation and the actual devaluation, expectations often arise. These can lead to import hoarding and delay in repatriation of export earnings which initially may result in a large decline in reserves. After the devaluation, the situation is likely to be reversed. Such instability means large shifts in the demand for money which may result in difficulties in controlling monetary conditions. If the authorities try to offset the initial monetary contraction, this may heighten external imbalance because of changes in the monetary base, which may add to the excess demand pressure. Speculation may also make it difficult to ascertain the magnitude of the devaluation needed to correct the external imbalance.

Second, Crockett and Nsouli (1980) argue that capital flows are governed by factors such as political stability and exchange controls rather than interest rate differentials. It is more likely that freeing the interest rate to positive levels or increasing it by restraining aggregate demand, will not result in an inflow of foreign capital to improve the external imbalance.

Third, Johnson (1980) argues that a devaluation is like a lump sum tax on cash balances and questions whether a balance of payments deficit is sufficient to render devaluation as a necessary policy. Instead, policies of reducing the money supply or taxing cash balances may be a better alternative.

Fourth, it is argued that the efficacy of a devaluation depends on the elasticity of imports, exports and inflation. Specifically, it is argued that if a country faces an inelastic demand for its exports, a devaluation will have an adverse effect on its terms of trade. Further, even if both imports and exports are influenced by relative prices, a devaluation will be ineffective if inflation rises proportionally to offset the impact of lower domestic prices relative to other countries.

Fifth, it is argued that the index used to devalue the exchange rate of a currency (in particular, a developing country's currency) has a number of shortcomings. There are four basic models used to calculate the real effective exchange rate of a country, which are: the IMF's Multilateral Exchange Rate (MER) model; the Export-Weighted index; the Import-Weighted index and; the Bilateral trade index. The MER model is very comprehensive and is used for industrial countries. The MER model takes into consideration the trade and payments structure of a country, and these include the price effects of exchange rate changes, the price elas-

ticity of different products, the competitiveness of the country's exports, patterns of bilateral trade, and the effects of capital flows (Crockett and Nsouli, 1980). The other three models are simpler and mostly used by developing countries.

The three simpler models do not take into consideration some of the important elements considered in the MER model. Elements such as repercussions on prices, substitution effects and capital flow consequences are not considered. Further, the use of the Import-Weighted index, which is viewed as the closest approximation to the real effective exchange rates for developing countries, may cause varying cross rates for other countries within a common trade area that pegged their currencies to different baskets. Thus, problems of trade may be created if exchange rates are adjusted on this basis.

Sixth, it is argued that liberalization of trade does not protect the economy's depleted foreign exchange reserves. Critics argue that given the balance of payments problem and the often use of devaluation, liberalization may increase capital flight and simultaneously, destabilize the economy and worsen the external imbalance.

The distributional implications of the Fund stabilization programs are essentially the outcome of political allegiance. It is argued by the structuralists and radicals

that the Fund's program tend to serve the interests of the capitalists at the expenses of the working and popular classes through reduced real wages and social services. Wealth tends to be concentrated in the hands of a small group of capitalists and the land owning class, while the vast majority suffer from real wage reduction and employment declines which may intensify if long term growth is reduced (Taylor, 1983). The distributional implications stem from specific policies within the package, with the most important occurring through devaluation. Since a devaluation increases the price of importables, the real wage of workers may deteriorate considerably since wage earners are normally not compensated for the increase in domestic price level as part of the IMF's conditionality. At the same time, owners of firms in the traded goods sector (exports) may gain, given higher prices of tradeables resulting from the devaluation. Further, even if workers' wages in the export sector, are indexed to domestic price increases, their wage share may still deteriorate relative to the owners. Since the domestic price level is derived from a combination of the traded and non-traded goods prices, its percentage increase and hence compensation is normally less than the percentage increase in the price of exportables from the devaluation. Non-traded goods sectors owners may also lose from higher import price if they use more foreign factors of production relative to those using domestic factors. From the increased profitability in the export sector, increases in research

and development may further strengthen the property rela-
tionship as welfare improves in one sector (traded) and
decreases in the other (non-traded).

The distributional implications have major repercussion
for social and economic development. In particular, it is
argued that society is now engaging in class struggle
instead of coalescing its ability to improve the basics of
human survival. The increasing emphasis on international
specialization by the orthodoxy might not only produce inap-
propriate products but reinforce the frustration for indi-
vidual freedom. Further, it is argued that there are far
reaching political implications from the use of orthodox
policies. Loxley (1986), argues that the introduction and
promotion of such strategies may give rise to political
repression and even dictatorship. Countries such as the
Pinochet regime of Chile and the Marcos regime of the Phil-
lipines are excellent examples of human rights violation,
which seems to be an off shot of the orthodox package.

3.5 ASSESSMENT OF IMF PROGRAMS AND PRACTICE

While there are many criticisms of the Fund's program,
the Fund has challenged these with cross country studies of
the actual effects of its supported stabilization program.
In particular, the Fund based its arguments on a study done
by Donovan (1982) which involved sixty-four cases receiving
the upper credit tranche standby arrangements during the

1971-1980 period. In Donovan's study, 35 cases were record-
ed as experiencing an improvement in their balance of pay-
ments - a success rate of 55 percent. On the other hand, the
growth rates of real GDP and inflation reduction has been
marginal. Donovan (1982:179) concludes that the "external
efforts appear to have been less severe than has been sug-
gested by participants in the controversy on the Fund condi-
tionality". More recent evidence however contradicts the
IMF position on its standby arrangements. Loxley (1985)
reworked Donovan study with similar data, finds nothing to
support Donovan's conclusion that the external sector
enjoyed an improvement for low income countries. He further
argues that many countries with standby and extended
arrangements have either suspended or experienced a break-
down in their arrangement because of their inability to meet
performance criteria. Killick (1984) investigating the
effects of 38 programs implemented by the Fund during the
1974-1979 period, reported that the known statistical sig-
nificance towards an improved balance was slight while the
growth rates were largely unaffected.

In a recent study of 18 Latin American countries, Pastor
(1987) finds that the program countries did experience sig-
nificant balance of payments improvement. This was caused
mainly from an increase in capital inflows induced by the
IMF's seal of approval and not from significant improvement
in the current account. He also finds IMF's programs to have

mixed impacts on the growth rates and be associated with accelerating inflation and a declining wage share.

Diaz-Alejandro (1981) also argues that Latin American Southern Cone countries that adopted the IMF package, showed disappointing results with regards to inflation because of frequent devaluations. With regards to the bias towards import substitution, he argues this infringed on the long run performance of the countries and when trade liberalization was adopted, exports responded favourably. Crawling peg exchange rates however, worsen the balance of payments because increased capital flows appreciated the exchange rate and made export less attractive.

While the empirical evidence, drawn mostly from cross country studies, indicates that certain policies of the Fund may indeed reduce growth without any significant improvement in the balance of payments or inflation, it is argued that this should be viewed with caution since there are several methodological problems that render the results questionable. In particular, Goldstein and Monteil (1986) illustrated that the estimated program effects from most of the cross country studies may not be representatives of the "true" program effects, because of methodological problems or pitfalls.[4] First, most of the cross country studies are not subjected to tests of statistical significance in the presence of observed difference when the performance of pro-

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[4] This, however, is not true of Loxley (1985) and Pastor (1987).

gram countries are compared with nonprogram countries. These differences it is argued would not be judged statistically significant at the conventional levels of significance. Second, those studies tend to compare the mean effects during and after the program and in doing so, they ascribed all the changes in outcome to the program alone. This, it is argued, invariably overstates or understates the true outcomes since some of the outcomes may be due to external shocks. Third, most of the studies tend to select program countries in a nonrandom way. This, it is argued, may cause the pre program differences in macroeconomic performance to affect the change in estimated performance. Fourth, it is argued that most of these studies failed to capture the total effects of the Fund programs since they did not allow for estimation in the absence of such programs. Finally, it is argued that most studies tend to compare the relationship between actual performance and performance criteria. This method is often misleading since countries whose programs were cancelled because of failure to comply with IMF conditionality are normally excluded. One must be cautious, therefore, in using the studies of performance of countries under IMF policies.

3.6   ALTERNATIVES

While there are many criticisms of the Fund's package, the alternatives proposed by critics, seem on the one hand to lack a coherent theoretical base and on the other, to lack concrete exposition. The alternatives, as a result, tend to be more in line with guidelines for stabilization rather than with the issues (Khan and Knight,1985; Loxley,1986). However, if one pieces together the guidelines from the critique, as Loxley, (1986); and Killick and others, (1984) did, an alternative can be outlined.

The alternative approach proposed by nearly all the authors focuses on the structural nature of the economy, emphasizing a more gradual and equitable adjustment with popular political support. In particular, the approach considers the gamut of socio-political and economic characteristics, where allocation and distribution may take place in a different way than in an unfettered market. As a result, selective policy instruments, which involve both market and nonmarket interventions, with sectoral priorities are emphasized.

The basic premise on which the alternative package is proposed is that exclusive reliance on export production, through the outward oriented model of growth, would not permit all LDCs to attain high rates of economic growth. Prebisch (1959) among others, argues that adverse world markets

conditions for primary exports, lack of substitutability, imperfect knowledge, non integration of LDCs' financial market with those abroad, and lack of competitiveness in manufactured exports are some of the impediments to fostering growth through the export oriented model recommended by the orthodox theorists. If, however, these factors were or are reversed, then the balance of payments and growth are likely to be more responsive to the orthodox stabilization package. But, because LDCs often confront some, if not all, of the above structural constraints, the efficacy of the orthodox package seems doubtful. Hence, in general, the alternative approach that is proposed, is a blend of the inward and outward oriented models of growth. In particular, there is emphasis on diversification and increasing traditional output. The alternative emphasises the provision of basic social capital and basic needs to achieve these goals, hence fiscal and monetary policies that are different than those advocated by the IMF. Other policies recommended include crawling peg and dual exchange rate systems, selective subsidies and taxes, and market interventions.

The provision of basic social capital and hence infrastructure is underscored by the structuralists as a prerequisite for productive investment and economic growth. It is argued that adequate health, education, housing and transport facilities are essential to increase labour productivity and production by providing the means to expand produc-

tion and take advantage of economies of scale. For example, it is argued that without proper transport facilities, crops may perish and not be marketed, despite high prices and increased production.

The crawling peg exchange rate system is recommended, instead of sudden and large devaluation which may be ineffective because of inelastic demand for imports and supply of exports and also inflationary pressures. The system, it is argued, may reduce fluctuations in output, inflation and at the same time keep the real exchange rate constant. Under a crawling peg exchange rate system, the nominal exchange rate is devalued steadily at a rate greater than or less than the difference between the domestic and foreign rates of inflation (Taylor, 1983:198). Latin American Southern Cone countries which adopted crawling peg exchange rate systems, however, have had their balance of trade worsen because of increased capital inflows which appreciated the exchange rate and made exports less attractive (Diaz-Alejandro, 1980; Taylor,1983). Because the crawling peg adopted as part of a package involving liberalization of trade and capital flows (Taylor,1983), it is argued that the system might be applicable to countries which practice trade and currency controls and do not attract capital inflows.

A dual or multiple exchange rate system is another alternative proposed instead of devaluation to a uniform rate. With such a system, there are more than one rate. There is

an official rate, often at an appreciated rate, set to
prioritize the allocation of foreign exchange for essential
inputs, goods and services. The other rate is set or estab-
lished by market forces, at a formalized parallel rate,
often a depreciated rate, to discourage non essential
imports and to provide incentives for non traditional
exports. The system can also be used as one of subsidizing
exports and taxing imports. The system, however, may result
in capital flight through underinvoicing of exports or over-
invoicing of imports if international capital is highly
restricted. Also, administering the system might be diffi-
cult.

As a remote possibility, the alternative of a flexible
exchange rate system, may be proposed. However, with vola-
tile exchange rate, it is argued that the equilibrium estab-
lished may mean slower growth and increased unemployment.
Also, the short run equilibrium might be inconsistent with
long term equilibrium which may mean a sustained deficit to
correct structural rigidities (Crockett and Nsouli,1980).

For reasons similar to those used against the flexible
exchange rate system, the structuralists argue that, given
the specific rigidities in the LDCs, the equilibrating
mechanism of the price system is inefficacious to promote
growth and permit a desirable distribution of income. In
particular, the structuralists argue that market outcomes
such as, price and interest rates, are poor guides to

improve efficiency and resource allocation since all the benefits and costs associated with production and consumption are not fully reflected in the market supply and demand curves due to spillovers or externalities. Further, market outcomes may not reflect the wishes of society. In particular, the distribution of income is often quite unequal and therefore may lead to the production of luxury goods for the rich while denying the basic needs of the poor. This provides a rationale for government to play an active role in modification and supplementation of the operations of the market in general and provision of means for the basic human needs in particular.

While there are some groups such as, the liberals and socialists, that look upon an expansion of government's role as a panacea for society's socio-economic ills some, such as the conservatives, espouse a limited role. A vast majority, however, would agree that governments do have some obligations in providing the stated economic objectives. Those who espouse a limited role for the government often do so on the assumption that governments are inefficient and ineffective when performing their roles. There are no qualms concerning their disenchantments, since, political processes may not bring about superior results where the market has been less satisfactory. There are more or less deficiencies in the political processes and bureaucratic agencies as there are in the market. However, there is often significant

divergence between 'sound economics' and 'good politics' which result in government inefficiencies. If the imbalance is caused by government's mismanagement thorough extragavant unproductive spending, then policies proposed by the orthodoxy to restrain government spending may be relevant.

When the share of the public sector in domestic economic activities is large, the scope of government's role is likely to be greater, requiring more than modification and supplementation of the operations of the market. In particular, economic planning or central guidance is often necessary. Planning is viewed as a solution to the economic problem i.e., the allocation of resources and the reconciliation of or arbitration between different interests (Meier, 1984). Within this purview, policies are focused on specific sectors and situations, in terms of their impact on growth, balance of payments and distribution. For example, as an alternative to monetary contraction and liberalization of price and interest rates, selective control or financial planning, can be undertaken. This alternative has low administrative and welfare costs if one considers the externalities of the orthodox package. Indigenous entrepreneural talents and allocation and distribution of resources are considered. Selective control can be viewed as complementary to development programs in which planned investments and savings are equal. The efficacy of selective credit control will, however, depend on the degree of autonomy of the cen-

tral bank and substitutability between financial market instruments by borrowers and lenders. In particular, the less the substitutability between credit to different sectors and for different purposes, the more effective is selective credit control (Khatkhate and Villanueva, 1980).

Regardless of the economic system, the proposed shift to a gradual and equitable adjustment process will mean a longer time for balance of payments and growth objectives to be achieved. Hence the need for foreign financing is likely to be greater than that which might be required under the orthodox approach. To this end, LDC's have been insisting on monetary reform in general and, specifically, that additional resources be linked to the form of adjustment required.

In conclusion, the alternative approach outlined has some characteristics which are distinctly different than those of the orthodox approach. In particular, more emphasis is placed on the structural characteristics of the economy, calling for policies that are flexible. Also, an equitable adjustment mechanism is emphasized which provides a rationale for government intervention. Equitable adjustment is pivotal because it is "more likely to be acceptable to the majority of the population and less disruptive of development in most countries" (Meier,1984:120). Despite the attractiveness of the alternative, one should note that panaceas do not exist. Hence, policies based only on structural rigidities, and equitable distribution of income may have to be undertaken with caution.

3.7   THE WORLD BANK

The major objective of the World Bank is to provide cred-
it, from its capital funds and commercial institutions, to
assist underdeveloped nations in achieving development and
growth. In carrying out its objectives, a new form of lend-
ing to provide long term, five to ten years, balance of pay-
ments financing was introduced in 1979. The Bank justified
its new program in terms of supplementing the short term and
inadequate finance available from commercial banks and the
IMF, and providing long term lending in support of stabili-
zation programs. In particular, the rationale is to provide
enough resources to import intermediate and capital goods
that would enable the economy to make the necessary adjust-
ments and be self-sustaining in the medium term.

The Bank's lending for structural adjustment begins with
an initiation of a stabilization program, often supported by
the IMF. This precondition, the Bank argues, would set the
stage for detailed policies to restructure the economy for
enhancing production, productivity and trade. The policies
included in the Bank's program stem from its contentions
that the failures experienced by LDCs in achieving their
goals are indicative of their poorly conceived domestic pol-
icies and institutions. In particular, the Bank argues that
policies and institutions which condone or promote extensive
government regulation of the market and increased role for
the public sector, seem innocuous at first but are deadly in

stifling growth as efficient allocation of resources is hindered. This results from distortions such as overvalued exchange rates, low producer prices, high urban wages and negative real interest rates.

As a result, the policies included in the Bank's program which set the precedent for the conditionality, focus on instruments to correct the deficiencies in the working of the market. The objective is 'getting prices right' to provide incentives for increasing private investments, nontraditional exports and agricultural output, reducing private consumption of energy, imported non-food consumer goods and other luxuries.

The policies are essentially supply side and are geared to compliment the demand side policies of the IMF. In practice, the policies advocated are: (1) gradual elimination of quantitative restrictions such as, import controls and tariffs, and modification of the price, tax and subsidy systems to correct import biases and foster production and exports from sectors with comparative advantage; (2) redistribution of resources to productive projects in the industrial and agricultural sectors which would generate acceptable rates of returns and net increases in foreign exchange, which would use less scarce capital and more labour, and which have short gestation period; (3) gradual elimination of subsidies in welfare programs and nondevelopmental activities such as administrative services, and implementation of user

fees to reduce the government deficit; (4) tighter financial discipline, more accountability and dismantling of state (marketing) organisations to foster increased efficiency in the provision of inputs and technical services; and (5) use of some portion of the loan to import essential raw materials, spare parts and other equipments.

Initiation of these policies and satisfactory progress on implementation through an agreed monitorable action program are identified as preconditions for the borrowers' access to subsequent tranches of the structural adjustment loan. Stern (1983) argues that while this procedure seems to be a form of conditionality, it is not different from that of the Bank's project lending.

Because the program initiated by the Bank is similar to that of the IMF's facilities, there are many issues raised. The Bank is accused of encroaching upon the responsibilities of the IMF i.e. stabilization of the balance of payments. The Bank counters this by emphasising the longer term, developmental focus of much of its conditionality although there can be no denying that its balance of payments support is overlapped with IMF assistance. It is argued that the functions of the two institutions are beginning to converge in other respects despite their distinct formal roles. Evidence to support this argument stems from the IMF adoption of long term Extended Fund Facilities resources for balance of payments problems suggesting that Fund programs now

address the structural aspects of imbalance, which in turn requires the conditionality for supply side policies. Also, the frequent use of supply side policies, such as exchange rate and interest rates changes and liberalization of prices and trade, has indicated a complementarity of the Bank's and IMF's arrangements and actions.

Differences between the Bank and the IMF stem from their distinct specialization as Stern (1983:102) succinctly explains that "the difference lies in the orientation of each institution's staff and the experience and expertise it is capable of mustering ... the Fund's involvement is restricted to a single type of operation - balance of payments supports - with relatively infrequent and limited staff visits to a country, whereas the Bank has many missions relating to a wide range of operations. Fund support is generally, though not always, seen as a rescue operation to a crisis ...(whereas) the Bank's individual SAL operations have a much lower profile and are negotiated at a less intensive pace". This difference, however, has been reduced by increasing collaboration on policy analysis, conditionality and information sharing (Loxley,1986).

The structural adjustment program is still in an infant stage; as a result, an assessment is difficult. However, the nature of the program and its theoretical foundation can be evaluated. It is argued that the Bank's lending is different from the IMF's in a number of ways. First, the IMF's

conditionality focuses on a few quantitative macroeconomic indicators while the Bank's concentrates on policy initiatives in a great number of areas at the sectoral and institutional levels. Second, payment terms of the Bank are superior because of lower interest rates and a longer maturity date. Third, the size of the Bank's loans is not limited to the members' subscriptions. Fourth, the politics of the Bank are less visible than that of the IMF. For example, the Bank was more sympathetic with the needs of Grenada and Tanzania, while at the same time, both countries were denied IMF loans.

Theoretically, it is argued that the outward oriented strategy the Bank advocates has all the shortcomings of the IMF's strategy and that it literally underwrites the IMF strategy. In particular, the growing protectionism in the DCs, serious deterioration in the terms of trade of the LDCs, retardation of world trade growth, and under capacity production in many industrialized countries, may provide little scope for success and hence adoption of outward oriented strategies. The Bank's promotion of a laissez faire system is also criticized for furthering the cause of capitalism both locally and in the international arena. It is argued that the Bank eschews public sector projects while actively promoting private enterprise. The Bank argues that state intervention is not recommended because it is the cause of inefficiency. Critics, however, argue that the Bank

underestimates foreign influence and it own policies which often promote inefficiency. Further, the favouring of open trading policies, it is argued, is designed to promote world capitalism and in particular, a peripheral form of capitalism where foreign capital replaces local capital and hence a new class of capitalist and more foreign dependence results.

Associated with the Bank's program is the possibility of massive redistribution of income and wealth, where the plight of the (majority) poor is, often , not alleviated. In particular, the promotion of private enterprise, increases in user fees for essentials, and restraint on urban wages might directly lead to deterioration in the standard of living of the poor while at the same time strengthening the structure of property relationship. The Bank, however, has recently recognised the distributional impacts of its lending but has not made this matter an immediate concern because of competition among the vested interest (Brett, 1983).

While there are many weaknesses of the Bank's lending, credit should be given for its initiatives in providing additional balance of payments support, less rigid conditionality, lengthening the term of loans to allow for adjustment and promoting sensible supply side policies. As a result of its shortcomings, recommendations for improvement include those made for the IMF such as: a balance between public sector and private sector activities; provision of

appropriate products such as those to satisfy basic needs; promotion of a balanced import substitution and export strategy which takes into consideration the structural characteristic of the economy and their potential impacts on distribution, self sustaining development and growth; increasing the Bank's resources to make structural adjustment lending a standard component of its overall lending which should run parallel with project loans; more collaboration between the IMF and the Bank to foster policies which are mutually reinforcing and with the same objective of improvement in resource management; providing frank and authoritative assessments on the creditworthiness of countries to encourage cofinancing by commercial banks; being more authoritative in putting pressure on bilateral donors who are stalling in fulfilling their commitments, providing more political tolerance and compromises to non-capitalist countries so that they too can seek assistance at an early stage of balance of payments difficulties.

3.8   CONCLUSIONS

From the discussion of the IMF and World Bank's package, the neglect of the socio-political and economic characteristics present in LDCs seems to raise doubts about the success of IMF orthodox stabilization and adjustment programs. One finds from the outset programs are suspect because important

agents in the drama, such as wage earners are neglected. For example, one has to understand that in principle, a fundamental part of the objective of stabilization ought to be to take account of the preferences of the people in the country and the impact on them of proposed programs. However, when LDCs seek foreign assistance to correct an external imbalance, these preferences are often neglected. In particular, domestic policies that reflect national goals are often modified to take into account elements (conditions) deemed important by foreign institutions, so as to permit access to funds. The imposition of outside conditionality may be seen as a requirement to achieve objectives sought by foreign rather than domestic authorities. The result might be conflicting objectives, and hence the necessary political support for stabilization programs might be weak or missing altogether.

Chapter IV

ADJUSTMENT POLICIES IN GUYANA

4.1   INTRODUCTION

This chapter examines Guyana's economic and political policies during the 1977-1985 period. In particular, the focus of the analysis is on the policies adopted through the influence of the IMF and World Bank programs during the 1978-1982 period and those adopted independently during the 1983-1985 period. The organisation of this chapter is as follows: section 2 discusses the nature of the policies; section 3 discusses the adjustment measures in view of the IMF and World Bank's conditionality; section 4 reviews the performance of the economy during the 1978-1982 and 1983-1985 periods, with an ultimate concern being the impact of the policies on the balance of payments, inflation, growth and income distribution; and (5) an overall evaluation in validating or invalidating the response as the correct approach for alleviating the crisis.

4.2   NATURE OF POLICIES

With the introduction of the 1972-1976 development plan, the economic policies of the government were within a socialist framework. There was a de-emphasis of private foreign investment and more emphasis on public ownership and control of vital economic activities in the productive and financial sectors.   The policies included nationalization, regulation of trade, prices and finance.

As we have seen, the period after 1975, however, was marked by rapidly falling export prices and increasing import prices. As a result, the balance of payments deteriorated rapidly while inflation skyrocketed. As the situation continued to deteriorate the government, with a weakened bargaining strength, was forced to submit to one of the IMF's standard austerity programs. The program was for one year and the loan was valued at 6.25 million SDRs.   The agreement, outlined in a Letter of Intent, meant a change in the nature of the government's policies. The program was based on the monetary approach to the balance of payments as the focus was on controlling the budget deficit and hence domestic credit through appropriate pricing and fiscal restraint. Also, there was an emphasis on concessions to foreign business as a mean of providing confidence and stability for the inflow of foreign capital and investment. Specifically, the agreement stipulated that the government would: (1) increase revenue through higher sales tax and

progressively eliminate subsidies on consumer goods; (2) increase prices for goods and services produced by state corporations to compensate for higher costs; (3) reduce the amount of foreign arrears; (4) rescind the prohibition on transfers abroad of funds arising from depreciation allowances of foreign based companies; (5) refrain from implementing multiple currency practices and restriction on payments and imports for balance of payments reasons; (6) restrain wages; and (7) increase domestic credit by no more than 8 percent (Jagan, 1982; Thomas, 1982). These measures were supposed to achieve: (1) a 5 percent rate of economic growth; (2) reduction in the balance of payments deficit; (3) a 10 percent reduction in imports; and (4) a reduction in foreign commercial debts (Spinner,1984:167).

At the end of the one year agreement in August 1979, the situation continued to worsen. The IMF recognised the fundamental nature of the crisis and negotiated a three year loan from the Extended Fund Facility for 62.75 SDRs. The performance targets set by the IMF were basically the same as the 1978 agreement, however, a key additional element was that domestic savings be increased. The policy instruments to achieve these targets were once again "appropriate" pricing, fiscal restraints and a reduced role for the state. The policies included: (1) wage restraint; (2) progressive elimination of subsidies and price controls; (3) adjustment of energy prices to world level; (4) payments of overdue for-

eign commercial debt; (5) increase in interest rates; (6) increase in taxes; (7) rationalization of the public sector; and (8) appropriate monetary policy to support these policies.

By July 1980, the IMF recognised that a more growth oriented program was needed with less emphasis on restricting demand and hence more on external funding. The Fund, therefore, negotiated a new three year Extended Fund Facility loan initially of 100 million SDRs and subsequently increased to 150 million SDRs. The arrangement included the following performance targets: (1) six percent rate of economic growth; (2) reduction in the current gap of the balance of payments by no less than 20.4 percent of the GNP; (3) reduction in the balance of payments deficit to US$30m; (4) increase in the surplus of the public sector to 6 percent of the GNP or G$137m; and (5) external payments be eliminated when the gross foreign assets of the central bank achieve a level of US$52m (Jagan,1982). Measures to achieve these targets were: (1) a 15 percent devaluation of the currency; (2) increases in tax; (3) reduced current expenditures; (4) a cut in the public sector investment program; and (5) introduction of an investment program which would exploit Guyana's natural resource base in agriculture, forestry, mining, and hydroelectric power (IMF Survey, 1980&1981). These policy criteria were further expanded to include those indicated in the agreement of a World Bank

structural adjustment loan, valued US$22 million, which complemented the IMF's loan. The thrust of the Bank's program was on the supply side with the objectives of increasing production, productivity and exports by "appropriate" pricing, less government regulation of the market, an increased role for the private sector and concessions for foreign capital. Specifically, the World Bank's package provided for: (1) use of US$14m to purchase inputs and spare parts for the key productive sectors; (2) wage incentives for key sector employees; (3) use of US$8m for the establishment of an Export Development Fund to provide credit to the manufacturing sector; (4) increase credit to the private sector; (5) introduction of an investment code to attract private foreign capital; (6) formation of an industrial development advisory council with strong private representation; (7) periodic adjustments of farmgate prices; and (8) reorganisation of the Ministry of Works to include a specialized function in engineering consultancy (Thomas, 1982).

In 1982, the government was forced to withdraw from the IMF's and eventually the World Bank's program because of its inability to meet the performance targets. In mid 1982, the government began renegotiations which continued into 1983 and 1984. The government undertook new initiatives in the form of an 'action programme' to mend relations with the IMF. The program was in vast contrast to earlier defiance as it abandoned every pretence of 'cooperative socialism'. The

program proposed a new investment code to increase foreign and local private investment and a reduction of the scope of the state in the major sectors. The IMF demanded a stricter austerity programme (because of previous failure) which included progress with the World Bank's program, more concessions for foreign capital, greater reduction of the state role in the manufacturing, rice, forestry, bauxite and fishery sectors, a 66-100 percent devaluation of the currency, increase in the price of water, fuel, rice, electricity and sugar (by removing subsidies on locally sold sugar). Negotiations reached a deadlock when the government refused to undertake privatization of the key sectors and a harsh devaluation (Spinner, 1984). Also, Guyana falling into arrears payment, to the sum of US$16m in 1984 and US$32m in 1985, has contributed to the breakdown in negotiations (PPP, 1985).

4.3   ADJUSTMENT MEASURES

4.3.1   1978 Stand-BY Arrangement

In response to the deteriorating situation the government overturned almost every aspect of its previous economic policies to meet IMF guidelines of the 1978 Stand-by arrangement. The government readily undertook measures prescribed by the IMF with the exception of external policies. Since excess demand was considered to be the main cause of the instability, the emphasis was on strict control over credit.

There were revenue increasing and expenditure reducing policies which were supported by tight monetary policies.

Measures to increase revenue included improvement in tax collection management, increase in tax rates, introduction of new taxes and reduction in subsidies. In 1978, the following measures were implemented to fulfill IMF's requirements: (1) 100 percent increase in motor vehicle licences and registrations; (2) 50 to 70 percent increase in excise duties on imported and locally produced alcoholic beverages; (3) 10 to 22 percent increase in consumption taxes on a number of consumer goods which included gasoline, cigarettes and furnitures; (4) 150 percent increase in stamp duty on passports; and (5) 10 percent increase in sales tax. It is important to note that the government did not rely on higher tariffs to control imports. Instead, it used quantitative restrictions which included banning imports of luxury goods and food which it claimed could be produced locally.

The expenditure reducing measures implemented were as follows: First, there was a freeze on wages in the public sector despite an agreement signed between the government and the Trade Union Congress (TUC) for wage increases during the 1977-1980 period. Second, there was an increase in retrenchment of state employees.[5] Estimates indicate that labour retrenchment amounted to 6,000. Third, there was progressive removal of subsidies on consumption goods such

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[5] There is no official estimate of the percentage of public sector employment.

as, flour, rice, water, cooking oil, electricity, transport and poultry feed. As a result, total subsidies were reduced from G$83m in 1976 to G$58.9 in 1978. Fourth, there was a decline in government current and capital spending on goods and services by 6 and 24 percent, in nominal terms, respectively.

To support these measures, the government, proceeding with the IMF agreement, set limits on net domestic assets of the central bank and wider credit limits to both the private and public sectors by the banking system. In 1978, domestic credit and the money supply increased by 10 and 11 percent respectively. In 1978, interest rates were also increased (see Table 16). Interest on deposits increased by 3 percentage points while the prime lending rate increased by 2 percentage points. Government bond yield, however, increased by only 1 percentage point.

TABLE 15

Summary of Macroeconomic Indicators

POLICY INDICATORS	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985
Average exchange rate (%Δ)	-	-	-	-	-	20	-	-	25	-
Average wage increase (%Δ)	15	53	31	-	-	27	-	-	10	10
Real effective exch. rate (%Δ)	3	-1	-25	11	14	10	-28	-11	16	
Personal emoluments (% of gov't. exp.)	20	35	35	30	25	30	28	25	24	30
Real curr. govt. exp. (excl. debt charge) (%Δ)	12	-13	9	-19	.2	-7	-24	-4	49	-40
Real curr. govt. exp. (%Δ)	24	-12	13	-9	6	-7	-13	4	4	22
Real total gov't exp. (excl. debt charge) (%Δ)	-10	-31	-6	-3	18	-4	14	-41	47	-35
Real total gov't exp. (%Δ)	-1	-27	10	12	17	-5	10	-28	14	-24
Money supply, M2 (%Δ)	9	23	10	7	19	17	27	21	18	9
Bank credit to public sector (%Δ)	127	39	11	26	38	22	41	29	18	33
Bank credit to private sector (%Δ)	3	-7	8	34	17	33	20	21	22	10

PERFORMANCE INDICATORS	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985
Real GDP (%Δ)	1.3	-2.9	-2.4	-1.2	2.1	3.8	-11.4	-4.1	0.5	1.0
Exports US$ (%Δ)	-21	-7	14	-1	32	-11	-30	-20	14	-3
Imports US$ (%Δ)	8	-13	-12	14	34	3	-37	-7	-11	4
Balance of trade US$	-51.4	-27.4	42.1	4.0	2.5	-53.2	-12.7	-32.4	15.2	4.9
Balance of payments US$	-142.8	-97.7	-29.7	-82.7	127.9	-183.0	-142.3	-157.5	-96.4	-96.6
Consumer price index (%Δ)	9	8	14	16	13	22	17	14	21	17
Total real consumption (%Δ)	15	-9	-11	-11	3	-10	-20	-13	-3	12
Private real consumption (%Δ)	10	-5	-11	-15	-1	-8	-19	-18	-	16
Govt. real consumption (%Δ)	25	-17	-12	-	10	-14	-22	-	-9	9
Real gross fixed invest. (%Δ)	15	-25	-31	49	-1	3	-37	-6	-8	12
Real gross fixed invest:GDP	37	29	21	31	30	33	30	27	23	21
Total deposits (%Δ)	7.2	18.2	11.5	15.2	23	18.3	26	22	17	18
Savings deposits (%Δ)	11	18	12	19	23	22	32	23	17	19
Unemployment rate	20	20	22	25	30	30	30	35	35	-

Sources: World Bank, World Tables;
Bank of Guyana Reports;
LACA, 1982-1986.

TABLE 16

Selected Interest Rates in Guyana

TYPE	1977	1978	1979	1980	1981	1982	1983
Bank Rate	6.50	8.50	10.50	12.50	12.50	14.00	14.00
SAVINGS RATES							
Small Savings	3.50	6.50	8.50	10.50	10.50	11.50	11.50
3 months time	4.00	7.00	9.00	11.00	11.00	12.00	12.00
6 months time	4.50	7.50	9.50	11.50	11.50	12.50	12.50
12 months time	5.50	8.50	10.50	12.50	12.50	13.00	13.00
Gov't Bonds	7.00	8.00	11.00	11.00	11.00	15.50	14.50
Treasury Bills	5.88	7.80	9.72	11.62	11.62	12.75	12.75
LENDING RATES							
Prime	7.50	9.50	11.50	13.50	13.50	15.00	15.00
Average	8.90	10.50	12.75	13.88	13.94	16.21	16.21

Source: Bank of Guyana Reports.

4.3.2   1979-1982 Extended Agreement

During the 1979-1982 period, the stabilization program undertaken by the government consisted of aggregate demand, aggregate supply and external policy measures.

4.3.2.1   Aggregate Demand Policies

In light of the continued current deficit after 1978, new tax measures were implemented. There were an 8 percent ad valorem tax on specific imports and a 37 percent increase in excise tax on tobacco. The expenditure reducing measures were as follows: First, the freeze on wages continued. Second, there was an increase in retrenchment of state

employees. Estimates indicate that labour retrenchment amounted to 14,000 during the period. The combined effects of the wage freeze and retrenchment resulted in a decline of labour cost, as a percentage of government spending, from 35 percent in 1978 to 28 percent in 1982. Third, the progressive removal of subsidies on consumption goods continued. As a result, total subsidies were reduced from G$58.9m in 1978 to G$25.2 in 1982. Fourth, there were declines in real government current and capital spending on goods and services. However, both current and capital spending rose in nominal terms.

During the period, domestic credit increased at an annual average rate of 31 percent while the growth rate of the money supply was 18 percent. In 1979, however, the money supply grew only 7 percent. A major factor in the growth rates of domestic credit was the growth rate of public sector credit which was 32 percent during the period. Private sector credit also increased at an average rate of 28 percent but accounted for only approximately 16 percent of the total credit.

The level of interest rate was also adjusted during the period (see Table 16). In the 1979-1980 period, the growth rate was 2 percentage points per annum, except for government bonds which increased by only 1 percentage point. In 1981 interest rates remained unchanged, however, in 1982, the prime lending and bank rates increased by 1.5 percentage

points reaching 15 and 16.21 percentage points respectively. Rates on deposits, on the other hand, increased between a range of 0.5 and 1.5 percentage points reaching 11.5 and 13 percentage points for small savings and 12 months deposits respectively.

While the aggregate demand management policies were viewed as having a simultaneous effect on the fiscal deficit and consumption, the government also placed primary reliance on quantitative restrictions to deal with excess external consumption. Specifically, the government implemented the following restrictive measures: (1) banning and/or imposing quotas for certain consumer goods; (2) reduction and inter-mittent suspension of tourist travel exchange allowances; (3) suspension of emigration allowances for Guyanese nation-als; (4) prioritizing the allocation of foreign exchange by imposing import licensing; (5) limiting the export and import of Guyanese currency by travellers and traders; (6) periodic prohibition of transfers arising from depreciation allowances by foreign based firms; (7) suspension of cash gift allowances abroad; and (8) suspension of students main-tenance allowances for all those studying in 'hard currency' countries. The government also altered prices to restrain imports by changing the exchange rate. Specifically, the exchange rate was changed from $2.5G for $1US during the 1967-1980 period to $3G for $1US in 1981; a devaluation of 20 percent.

4.3.2.2 Aggregate Supply Policies

Faced with an exacerbation of the crisis, the IMF and subsequently the World Bank introduced supply side policies in their packages. These included policies to rehabilitate and increase the productive capacity of the economy. The focus was on means to increase production and productivity in the key industries i.e. the bauxite, sugar, and rice industry. In particular, the agreement stipulated that there would be a reduction in government regulation and an increase in the use of private capital and technology to exploit and restructure production. Also, incentives would be provided to stimulate both domestic and foreign savings and investment.

In the bauxite industry, the government contracted US Engineers and Consultancy firm to study the problems and advise on appropriate systems and procedures which led to the hiring of the following foreign firms: (1) Kaiser Aluminum to overhaul the alumina plants; (2) Green Construction Co. to eliminate the lags between stripping and mining at the principal mine; (3) Touche Ross to revamp the accounting systems and practices; (4) Austroplan to upgrade the efficiency of the ore handling procedure; (5) US Steel to increase efficiency in the Berbice Branch of calcanining operation; and (6) Maschines Export/IBK Consulting Enterprise to advise on technique and systems for effective forward planning and mine development (Jagan, 1982; Barry, Wood and Preusch, 1984).

Other measures adopted to improve efficiency included a reduction of the work force by 25 percent, closing four of its seven mines that were characterized as marginal and using a part of the bauxite sales revenue for basic maintenance work.

Since the sugar industry was plagued with similar problems, the initiatives were similar, except for the use of foreign firms. The measures adopted to improve production processes and regear the industry included: (1) careful monitoring of production levels, field and factory productivity and overall production costs; (2) rationalization of the labour force by reducing employment by 12 percent; (3) curtailing overseas working capital to reduce foreign liabilities; (4) mechanization of harvesting in some estates; (4) abandoned marginal lands that have been cultivated; (5) phasing out two estates that were making losses; (6) using a part of the foreign revenues to buy spare parts and basic maintenance; and (7) eliminating the middleman for the sale of sugar overseas (Collymore,1984).

In the rice sector, production continued to increase but fell short of targets every year. To boost production and productivity, the government in 1981, reorganised the management system. In particular, there was regional decentralization of management functions and direct responsibility of regional managers to the regional administration. In 1982, some of the functions of the Guyana Rice Marketing Board

were transferred to other government agencies and the private sector. In particular, the importation and distribution of inputs, provision of credit and the undertaking of research and other support services were taken out of the Board's control.

Other policies adopted to increase the volume of goods and services supplied by the domestic economy focused on ways to improve resource allocation and increase the rate of growth of capacity. First, there were changes in the interest rate to stimulate a larger volume of financial savings which would invariably encourage private investment. Second, there were attempts to eliminate distortions in resource allocation by rationalizing prices. Specifically, the government progressively eliminated subsidies and increased prices on consumer goods. While the government was reluctant to remove price control, it readily undertook measures to increase prices through increases in consumption tax and excise duties. Removal of subsidies which started as early as 1977 had been practically completed by 1982. Subsidies on basic consumer goods, such as flour and rice were removed and so were those on energy and agricultural inputs. Third, a devaluation was undertaken in 1981 to stimulate supply by permitting an increase in product prices in domestic currency relative to the price of non-tradeables.

Fourth, tax concessions were implemented through the 1979 Investment Code to encourage foreign investors to invest in

Guyana. In particular, a tax holiday of 5 years, duty free imports, generous depreciation allowances and concessions for remitting profits and depreciation were provided. For local investors, tax allowances were available for agricultural imports and other capital goods which would use local inputs with a large value added.

Fifth, there was a drastic change in the government investment policy relative to those in its 1972-1976 plan. A new Investment Code in 1979 espousing an 'open door' policy to foreign investors was introduced. The government promised that there would be no nationalization of any enterprise established after independence and new foreign investors would be given generous tax and remittance concessions and subsidies. Also, further assistance would be provided by the establishment of a National Research and Scientific Council in the form of direction in the utilization of technology and other support services. It is important to note that the aspect of the investment program which comprises a hydroelectric project was never implemented.

Finally, import controls were implemented with the view that they can simultaneously reduce foreign expenditure and increase domestic supply through import substitution.

4.3.3   1983-1985 PERIOD

Relative to the 1978-1982 period, the policy thrust of
the government during the 1983-1985 period did not change
significantly.   The period was marked by restrictive demand
management policies, supply side policies and external poli-
cies.   On the demand side there were revenue increasing and
expenditure reducing measures.   In 1983, new tax measures
were once again introduced to narrow the deficit. The meas-
ures adopted include: (1) a penalty for late payment of tax-
es; (2) a ceiling of 50 percent on the average rate of per-
sonal income tax; (3) an increase in property tax; (4) a
further increase in excise and consumption taxes on alcohol-
ic beverages and cigarettes; (5) a 100 percent increase in
travel tax; and (6) restrictions on the deductability of
donations.

While no new tax was implemented in 1984, the government
in 1985 imposed G$30m in new taxes. There were increases in
both consumption and excise taxes. Also, there were increas-
es in travel tax, passport fees and surcharges on fuel and
electricity.

The measures adopted to reduce expenditure continued to
be wage restraint by freezing wages, except in 1984 and
1985, when the minimum wage was increased 10 percent.   The
retrenchment of state employees continued and the estimated
total in 1983 was 10,000. While there are no estimates for

the 1984-1985 period, the 1984 budget proposed more layoffs (LACA, 1986). Government elimination of subsidies on consumption goods and agricultural inputs continued during the period as subsidies were reduced from G$25.2m in 1982 to G$14.2m in 1984. Also, budget estimates for 1985 proposed no significant increase. Government current and capital spending on goods and services were, however, increased in nominal terms during the period. Capital expenditure increased dramatically by 86 percent in nominal terms in 1982, from G$424m to G$790m as the government made capital contributions to the major public enterprises to wipe off their escalating debt. Such funding declined, however, in 1983 to G$349m as Table 19 indicates.

During the period, domestic credit increased at an average rate of 27 percent. This was caused mainly from increased public sector borrowings which grew 29 percent in 1983 and 33 percent in 1985. The money supply increases, however, were modest when compared with domestic credit. The average annual rate of growth was only 16 percent. In real terms the increases were zero or less since inflation was running at 17 percent per annum. Interest rate in this period did not change.

On the supply side, foreign firms continued to be contracted to manage the bauxite industry. In the sugar industry, the government closed two factories. In the rice industry, a project of bringing 37,000 acres of rice land under

an IDA loan valued US$40m was initiated in 1983. In 1985, the Board was restructured and a separate marketing entity was established to promote sales abroad. Private farmers and millers were permitted, within limits, to sell rice directly to non traditional foreign markets. Also, a new price determination mechanism through the Ministry of Agriculture was established to revise and increase prices paid to farmers to provide the necessary incentives to expand production.

The external policies adopted continued to be a blend of quantitative restrictions and price changes. In 1984, the Guyanese dollar was devalued by 25 percent to a value of $3.75G for $1US. This devaluation was implemented because the authorities were concerned that the effective exchange rate had revalued and would have a negative impact on the country's competitiveness and hence wider balance of payments deficit and that the growing magnitude of the parallel economy had to be curtailed.

4.4   POLITICAL POLICIES

Virtually all economic activities have been guided by political considerations in Guyana. With the introduction of the 1972-1976 plan, the government explicitly espoused the ideology of 'cooperative socialism', where cooperativism would be the dynamic principle of socialist transformation of the economy based on self-reliance and self- sufficiency.

The government promised that the political system would extend socialist democracy by providing every Guyanese with the right to work for and share in the economic well being of the country and to ensure equality of opportunity in the political, economic and social life of the country.

In pursuit of these objectives, the government proceeded with nationalization of the major industries and regulated trade. The government also made concessions to the opposition People's Progressive Party and its affiliated union, the GAWU and farmers' representative, the RPA. A minimum wage agreement was also signed with the TUC for a period of 4 years. This was seen as an indication of industrial democracy. Political democracy was also promised through free and fair elections and even a possible sharing of power between the two rival political parties (Premdas and Hintzen 1983).

As the economic crisis loomed in 1977, there was increased opposition to the government's austerity measures. The government reacted with raw coercive force and constitutional changes to provide it with more power in carrying out its austerity measures. In particular, the police and army were used frequently to harass and arrest opposition party officials and workers who protested food shortages, declining real wages, and deterioration of basic social services. Political assassination and direct repression of social and political groups were frequent (Guyana Human Rights Report,

1984). Victimization of workers through demotion, transfer or dismissal were common. There were also other policies used to provide the government with more power. The army and police were used in blatantly rigging the 1979 and 1980 elections. These provided the base to alter the country's constitution where the president elected for life, Forbes Burnham, could unilaterally make laws by decree in the name of 'national interest'. In consolidating its power, the government adopted policies that favoured its supporters which would ease their burden of adjustment. These policies included: (1) providing party loyals with highly paid and prestigious positions vacated by private sector workers; (2) expanding the state administrative bureaucracy through the doctrine of party paramountcy to staff party supporters (Thomas, 1982); and (3) expanding its control over the distribution of economic resources and basic goods (GHRA, 1984).

As part of its ideological thrust, the government adopted a food policy which it deemed 'anti-imperialist'. In particular, there has been the campaign of 'eat what you produce' as the government banned virtually all imported food including wheat flour. This policy was carried so far that the government even refused permission for gifts of foodstuff from private and inter-governmental organisations. In 1983, two consignments of wheat flour and milk from the World Food Program were refused and had to be transshiped to Barbados despite widespread scarcity and poverty in Guyana.

The government foreign policy was highly unstable, veering rapidly between the East and West. In the early 1970's, the government began a series of diplomatic relations with China, U.S.S.R. and Cuba as it was espousing its socialist or anti-imperialist path. As the economic crisis intensified, the government made dramatic overtures to the West as it adopted the IMF/World Bank programs. When the inflow of funds from the West stopped, the government once again turned to Eastern Europe, Cuba and China for financial help.

4.5 ASSESSMENT OF THE IMPACT OF ADJUSTMENT POLICIES 1978-1985

There are no fewer than five yardsticks to evaluate performance under Fund-supported programs (Goldstein,1986; Guitian,1981). These yardsticks, however, do not reduce the difficulty in assessing performance. Without discussing the strength and weaknesses of the yardsticks, in this study, the two most common yardsticks will be used: (1) comparison of the performance under the program with that specified in its target, and (2) comparison of the performance under the program with that before the program. It is important to note that both of these yardsticks are insufficient in evaluating the independent effect of Fund programs. For example, non program factors may influence programs factors, thus causing the effects to be understated or overstated. Consequently, the results should be viewed with caution.

With regards to the first measuring rod, Table 17 shows

TABLE 17

Before-After Comparisons of Macroeconomic Outcomes

YEAR	GDP (% CHANGE)	CPI (% CHANGE)	BUDGET DEF.:GDP	CURRENT ACC.:GDP	COMMER. DEBT US$
1977	-2.8	7.9	18.5	22.0	39.0
1978	-2.4	14.2	17.6	5.7	40.0
1979	-1.2	16.3	28.2	15.6	37.5
1980	+2.1	13.2	39.6	16.9	326.5
1981	+3.8	22.1	41.6	27.7	95.4
1982	-11.4	16.9	73.8	29.7	83.3
1983	-5.1	13.5	51.8	27.5	71.0
1984	+0.5	20.8	72.1	19.6	56.7
1985	+1.0	16.8	46.8	20.9	47.3

SOURCE: International Financial Statistics,
Bank of Guyana Reports.

how the Guyanese economy performed relative to the previous year. In terms of growth rate of real GDP, there was a deterioration for all years, except 1980 and 1981 when there was a marginal improvement.   Real GDP declined by -2.4 percent in 1978 and -11.4 percent in 1982. The latter is the lowest growth rate experienced by the Guyanese since the country's independence in 1966.   Inflation also worsened during the period, except for 1980 when there was a slight improvement. Inflation rate accelerated from 7.9 percent in 1977 to 13.2 percent in 1980 to 16.9 percent in 1982.   In 1981, the rate was 22.1 percent, the highest experienced by the economy in two decades.   In the external sector, the current account deficit as a percentage of GDP improved considerably in 1978 but deteriorated during the 1979-1982 period, climbing to 29.7 percent in 1982.

Turning to policy indicators, the authorities were unable to increase the level of revenue and decrease the levels of expenditure. Tax revenue as a proportion of GDP declined from 35 percent during the 1975-1977 period to 32 percent during the 1978-1982 period. On the other hand, government expenditure as a proportion of GDP, which had averaged 57 percent during the 1975-1977 period, increased to 72 percent during the 1978-1982 period. Accordingly, the budget position worsened for all years, except for a one percent improvement in 1978. As a consequence of the trends in revenue and expenditure, external commercial borrowings and hence foreign commercial debt increased during the period, except for 1979. In 1980, commercial debt was US$326.5m with supplier credit accounted for approximately 69 percent of the total.

The results of the second measuring rod are shown in Table 18. The results indicate that the performance were less favourable than the targets. The growth of real GDP was negative for all years, except 1980 and 1981, and averaged -2 percent which was far below target levels. While there wasn't any explicit target set for inflation, the performance was undoubtly highly unfavourable, as it climed into double digit figures. The targeted improvement in the current account position as a proportion of GDP, as the data indicate was also never met. The overall balance of payments were less favourable than targeted.

TABLE 18

Actual Results and Targets under Fund-Supported Adjustment
Programs, 1978-1982

VARIABLES	1978 STAND-BY PROGRAM	1979-1982 EXTENDED FACILITY
	Annual Rates of Δ	Annual Rates of Δ
REAL GDP		
TARGET	5%	6%
ACTUAL	-2%	-2%
NOMINAL EXCHANGE RATE		ΔDuring Period
TARGET	--	15%
ACTUAL	--	20%
	% OF GDP	% OF GDP
BUDGET DEFICIT		
TARGET	<18%	<18%
ACTUAL	17.6%	45%
CURRENT ACC. DEFICIT		
TARGET	--	20.4%
ACTUAL	5.7%	22.5%
	Million of US$	Million of US$
OVERALL BAL OF PAYMENTS		
TARGET	--	$30.0
ACTUAL	--	$83.7
COMMERCIAL DEBT		
TARGET	--	NIL WHEN FOREIGN ASSETS=US$52M
ACTUAL	--	US$83.3 IN 1982

SOURCE: Targets from IMF Surveys; Jagan,1982; Spinner, 1985.
        Actuals calculated from Intern. Financial Statistics.

Turning to policy indicators, the data show that except
for 1978, government deficits as a proportion of GDP were

much greater than targeted. Consequently, the rate of growth of domestic credit to the public sector increased more than planned during the period. With regards to exchange rate adjustment, the data show that this was in line with the program targets while external commercial borrowing was, however, greatly in excess of targets on account of the worse than expected balance of payments.

The results indicate that there was indeed a deterioration of the economic situation in Guyana under the Fund-supported program. The situation continued to deteriorate after the program but marginal improvements were noticeable in 1984 and 1985. The growth rate of real GDP was negative in 1983 but positive in 1984 and 1985. Real GDP per capita, however, declined after 1982. Inflation rose sharply in 1984 but in 1985 moderated to an annual average rate of 17 percent. The current account deficit as a ratio of GDP also moderated in the 1984-1985 period relative to the 1981-1983 levels. During the 1980s, inflation, current account deficits and government deficits continue to be high while real incomes remain depressed relative to levels prevailed in the 1970s.

Given the continued seriousness of the economic situation, it is essential to examine the reasons why the programs failed. The following analysis focuses on an examination of aggregate demand, aggregate supply and socio-political policies.

4.5.1   Aggregate Demand

Of all the adjustment policies adopted to restrict demand, it seems that fiscal adjustments in the form of revenue increasing policies were adhered to tenaciously. This adherence, however, did not lead to increases in real revenues. During the 1978-1982 period, real revenue declined at an annual average rate of 8 percent. Revenue from taxation in general declined at a rate of 6 percent. Specifically, tax from income declined at an annual average rate of 9.9 percent. The evidence, as a result, seems to suggest that the revenue decline was caused by an induced recession. The decline in revenue was also a result of the decline in import duties which had an average annual growth rate of -17.8 percent. This decline reflects the closed nature of the economy. While tax revenue from income and imports declined, there was a 1 percent increase in excise tax revenue, reflecting the increase in taxes on consumer goods such as, alcoholic beverages, gasoline, cigarettes and furniture.

Expenditure reducing measures attempted by the government had mixed results. Real expenditure declines only occurred in 1981 when the total decline was 5 percent. During the 1978-1982 period, the average annual rate of growth was 5 percent. Partly responsible for the increase, was escalating debt charges, as real government spending excluding debt charges increased at an average annual rate of 4 percent.