Inclusive Growth Thinking in IDA

The influence of the growth diagnostic approach and inclusive growth analysis on Country Economic Memoranda and Country Assistance Strategies

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Prepared by (independent consultants)

Henrik Hansen and John Rand
Department of Food and Resource Economics
University of Copenhagen

Abbreviations and Acronyms

CAS	Country Assistance Strategy
CEM	Country Economic Memorandum
CGE	Computable General Equilibrium
CPS	Country Partnership Strategy
GDP	Gross Domestic Product
GPRS	Ghana Poverty Reduction Strategy
HRV	Hausmann, Rodrik, Velasco
ICA	Investment Climate Assessment
ICT	Information and Communication Technology
IDA	International Development Association
IEG	Independent Evaluation Group
IEGCR	Independent Evaluation Group (Country Evaluation and Regional Relations)
IGA	Inclusive growth analysis
INE	National Statistics Institute (in Mozambique)
IOF	Inquérito ao Orçamento Familiar (Mozambique Household Budget Survey)
MDG	Millennium Development Goal
NDP	National Development Plan
PARPA	Action Plan for the Reduction of Absolute Poverty (in Portuguese)
R&D	Research and Development
SEDP	Socio-Economic Development Plan
SEDS	Socio-Economic Development Strategy
SOE	State Owned Enterprise
TFP	Total factor productivity
VDR	Vietnam Development Report

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Summary

An informal working group, established during the IDA16 negotiations, has looked at the emerging inclusive growth agenda and the possible opportunities for IDA to support more broadly anchored patterns of growth in IDA countries by adopting an inclusive growth approach in its country work. The Working Group needs to look into whether the inclusive growth diagnostic approach is already influencing IDA's analytical work in-country and the possible further scope for orienting IDA country analytical work.

This report is a review of the extent to which the inclusive growth diagnostic approach has influenced IDA in its analytical work, and how this has translated into the strategic definition of its operations in selected countries to provide recommendations for strengthening inclusive growth in diagnostics and policy work. The report is a desk review of Country Economic Memoranda (CEM) and Country Assistance/Partnership Strategies (CAS/CPS) covering 4 IDA countries. The four countries are Ghana, Mozambique, Uganda, and Vietnam. The country selection was to a large extent systematic as nine criteria were given from the outset.

The reports from each of the four countries are evaluated along three dimensions; (i) objectives, (ii) quality, and (iii) coherence and relevance. The CEM and the CAS/CPS serve different purposes; therefore quality and analytic rigor is emphasized for the CEM while coherence and relevance is emphasized in the assessment of the CAS/CPS reports.

The assessment of the quality and of the coherence and relevance is based on the growth diagnostics approach and the inclusive growth framework when appropriate. The growth diagnostics approach, initially proposed by Hausmann, Rodrik and Velasco in 2005, focuses on identifying country specific binding constraints for purposes of policy reform. The World Bank has augmented the growth diagnostic methodology by an in-depth description and analysis of the labor markets to form a comprehensive inclusive growth analysis. The bridge between growth diagnostics and inclusive growth analysis comes from the role of employment: When labor is the most important asset of the poor, employment will be the transmission channel between individuals and growth. So the inclusive growth analysis suggests looking at productive employment in addition to analyzing causes of low investment in an economy.

In the descriptions of the CEM from each of the four countries it is assessed to what extent three central parts of an inclusive growth analysis have been followed. First, it is noted if the CEM incorporates all necessary elements sufficient for a comprehensive analysis of growth trends. Second, the CEM should convincingly provide tell-tale symptoms of a given constraint being binding. Third, the CEM should document a clear connection between the constraints identified and the policy recommendations made.

In the assessment of the individual CEMs it is found that the report from Ghana is generally satisfactory in terms of technical quality and consistency in the causal arguments.

The document is successful in defending the identified binding constraints to inclusive growth even though the growth diagnostic approach is not directly applied. Further, the CEM implicitly includes inclusive growth considerations in its analyses and recommendations.

For Mozambique the CEM does not quite live up to its promise of providing an organized framework for the development of long term strategy for a more inclusive and shared growth. A more direct use of the inclusive growth approach would have benefitted the report as a way to ensure that the CEM actually identifies the most binding constraints and provides convincing arguments for why the constraints are binding.

In contrast, the Ugandan CEM is of a remarkable quality. It is clear from the structure of the CEM that considerable efforts have gone into making the Ugandan CEM a prototype example of a contemporary World Bank analysis based on the growth diagnostics approach and even though inclusive growth is not an explicit part of the stated objective, employment generation, as well as both the pace and the path of economic growth are central themes of the analysis in addition to the recommended policy strategies and interventions.

Finally, as the World Bank has not written a CEM for Vietnam the Vietnam Development Report from 2012 is assessed instead. The annual report is much shorter than a CEM and the analyses are less technical. The overall conclusion is that the VDRcould benefit from a more thorough analysis of its growth prospects, and the description of the analytical tools used could be improved. On the positive side, the policy recommendations in the VDR are clearly related to the alleged constraints and they are actionable.

Moving from the assessments of the CEMs to the CAS/CPSs it is noted that while the content teams have considerable flexibility to customize the CAS/CPS there are certain topics a CAS/CPS typically covers. Furthermore, the organizing framework of a CAS/CPS is built on the results that the bank program expects to contribute to in support of the country's development goals. Hence, the CAS/CPS cannot be expected to have the same focus on growth diagnostics and inclusive growth as the CEM.

In the assessments of the CAS/CPSs focus is on whether the reports reflect the results of existing CEMs in the sense that they include the same constraints and reforms. Further, it is directly assessed if the macroeconomic framework and poverty discussions, topics that are typically covered in a CAS, refer to productive employment growth.

For Ghana the answers to the two central questions are that the constraints and reforms identified in the CEM are reflected in the CAS, although no direct reference to the CEM is given and, second, that the CAS does reflect inclusive growth thinking, but more focus on productive employment generation is needed. For Mozambique it is noted that the CPS explicitly mentions the CEM analysis, but the most binding constraints identified in

the two documents are not aligned. Further, where the CEM is relatively weak with regards to inclusive growth indicators, the CPS is very clear in aiming at designing a strategy ensuring inclusive growth and the strategy matrix has the necessary focus on employment generation with specific sector strategic recommendations. As for the Ugandan CEM, the Ugandan CAS is of high quality. There is good agreement between the identified constraints and both reports agree on the growth strategies. Inclusive and sustainable growth is explicitly a core theme of the strategy and the CAS specifies precise Bank group programs. Finally, for Vietnam there is good alignment between the VDR 2012 and the CPS, but the quality of the growth analysis in both reports is inadequate. In particular, the constraints to growth are postulated rather than identified from a rigorous analysis. Even so, by supporting the Vietnamese Government's development vision facets of inclusive growth are present in the CAS.

By way of conclusion, four points are emphasized:

1. The analytical quality of the reports varies too much.
2. Therefore, promoting a growth diagnostic and inclusive growth analysis as part of the World Bank Policy Analytical and Advisory Assistance toolbox is recommendable.
3. By combining different methodological approaches an important contribution of the CEMs will also be the provision of a consistent framework demonstrating the fiscal; balance of payments, and debt sustainability consequences of particular growth strategies.
4. None of the reports use fully fledged inclusive growth analysis as the methodological framework. However, elements of the inclusive growth analysis are present in seven out of eight reports. Therefore, the inclusive growth analysis should be suggested as an organizing framework, not as a rethinking of World Bank analytic work.

In addition it is recommended that the World Bank aims at producing a Country Economic Memorandum for each IDA country. For the CEM it is suggested that

- countries at applying a standardized analytical framework, as a supplement to the more country specific methodological approaches,
- there is focus on inclusive growth analysis,
- it is produced at regular intervals, and
- it has clear, actionable recommendations for policies and reforms.

1. Background

The World Bank spends significant resources on analytic work and World Bank country reports form the backbone for evidence based policy in many developing countries. World Bank views on key development questions and reform agendas are therefore highly influential in shaping the direction of reform-efforts within countries.

Inside the Bank and as well as within the broader development community there have always been debates as to whether poverty reduction or economic growth should be the principal goal for development policy and reforms. Four empirical insights have tilted the present focus of attention towards economic growth. First of all, it has been thoroughly established empirically that poverty reduction is driven mostly by growth gains. Second, it is also widely accepted that poverty lines are somewhat arbitrary and this has given rise to a movement towards using several standards, as they are viewed appropriate in the given context. Specifically, countries now often include an extreme poverty line, one or more national poverty lines, and global poverty lines in poverty profiles and analyses. Third, aspects of human well-being that are not reflected in GDP, such as health and education, are now routinely included as core development objectives, notably in the MDGs. At the same time it is widely recognized that without economic growth the prospects for attaining the MDGs are limited. Hence, the renewed interest in economic growth is based on the acknowledgment that growth is a complement to the broader development goals because economic growth makes these objectives easier to achieve. Finally, the Bank's set of fixed policy prescriptions (Stabilize, Privatize, and Liberalize) known as the Washington Consensus was abandoned in the early 2000s and replaced by a much less assertive approach supporting selective and more modest reform programs and policy diversity across countries (World Bank, 2005; Rodrik, 2006; Commission on Growth and Development, 2008). This has reignited the donor community's interest in supporting growth strategies alongside, and even replacing, poverty reduction strategies.

However, the long economic upswing of the 2000's with high growth rates in many developing countries was accompanied by a tendency to growing in-country inequality. This has led to concerns over the opportunities for welfare improvements foregone and the potentially destabilizing consequence of inequality. Furthermore, in the coming four decades the greatest wave of young people ever will enter the labor market, most of them in low- and middle-income countries. They will need to be able to secure and improve their living conditions through jobs and entrepreneurship so that these countries can propel themselves up the income hierarchy. While the recent World Development Report (WDR13) on jobs provides a wealth of information and useful insights into the different social and economic dimensions of the jobs agenda the WDR13 is silent on how individual countries should go about identifying and analyzing the constraints for

creating (good) jobs in country specific circumstances. This document suggests a helpful approach and systematic framework for this "identification" process.

Differences observed between countries in terms of their ability to help people lift themselves out of poverty despite comparable growth rates have stimulated a strong interest in exploring the causes of these differences and a considerable research effort is directed at finding answers to this question. "Inclusive growth" has become a denominator for the ambition to uncover why growth in some countries leads to rising income and generation of productive jobs for a large share of the population, but not or to a lesser extent in others. Thus, for most bilateral donor agencies the growth strategies that are formulated must be more than just a Washington Consensus with a twist of contextual flavor. They require a return to broad based, inclusive economic growth as a priority on the development agenda.

Various methodological approaches are now used in thorough country-specific growth analyses. Hausmann, Rodrik and Velasco (2005), henceforth HRV, have developed an evidence based methodology designed to identify the most binding constraints to growth in an economy. Their framework has been further expanded to identify the constraints to inclusive growth through productive employment. At a conference held in Nairobi in September 2011 the World Bank presented results of several pieces of research aiming at exploring different aspects of growth from an inclusive perspective undertaken under the Inclusive Growth Diagnostics Program. The HRV framework had influenced several of the studies. However, other approaches were also explored.

As an outcome of the IDA16 negotiations it was decided to establish four informal working groups who could carry on discussion on some of the more complicated issues that were difficult to deal with in the formal negotiations. Denmark and South Africa co-chair the informal Working Group on Inclusive Growth, which looks at the emerging inclusive growth agenda and the possible opportunities for IDA to support more broadly anchored patterns of growth in IDA countries by adopting an inclusive growth approach in its country work.

The Working Group met during the spring at the Annual Meetings of the World Bank in 2011 and at the Spring Meeting in April 2012. During its April session the Working Group discussed the emerging methodological framework for inclusive growth diagnostics based on a note entitled "Inclusive growth – a proposition for IDA" (Ianchovichina and Lundström, 2010) prepared for the meeting by the Danish co-chair. In part, the note reflected on the results of the aforementioned Inclusive Growth Diagnostics Program.

Based on these discussions participants agreed that the Working Group needed to look into whether the inclusive growth diagnostic approach was already influencing IDA's analytical work in-country and the possible further scope for orienting IDA country analytical work and strategic definition of operations in this direction. This would take the

form of a desk review of Country Economic Memoranda and Country Assistance Strategies covering 3-4 IDA countries undertaken by an independent consultancy, to be supplemented with interviews of World Bank country directors and country managers on their individual assessment of the advantages and drawbacks of IDA's adoption of such an approach.

This report, written by two independent consultants, is the review of the extent to which the inclusive growth diagnostic approach has influenced IDA in its analytical work, and how this has translated into the strategic definition of its operations in selected countries to provide recommendations for strengthening inclusive growth in diagnostics and policy work. The report is organized as follows. Section 2 specifies the criteria for country selection, while Section 3 presents the assessment methodology. In Section 4 the growth diagnostics approach and the inclusive growth analysis are briefly described and discussed, furthering the assessment of the quality of the Country Economic Memoranda (CEM) and Country Assistance Strategy / Country Partnership Strategy (CAS/CPS) reports. Section 5 presents the country report assessments while Section 6 concludes.

2. Country Selection

In order to assess the extent to which the inclusive growth framework has influenced IDA in its analytical work it was decided to review the CEM and the CAS/CPS of four IDA countries. The four countries selected for the assessment are Ghana, Mozambique, Uganda, and Vietnam. The country selection was to a large extent systematic as nine criteria were initially given:

1. A strong and long-standing IDA program, with the Bank in a position to influence development thinking and direction of effort overall.
2. A focus on Africa where IDA is likely to be extensively engaged for the foreseeable future, but including at least one country from another region.
3. At least one country with a demonstrated track-record of bringing the majority of the population into the mainstream of growth.
4. Focus on countries deliberately pursuing a policy of inclusive and equitable growth.
5. Inclusion of countries where the pace of poverty reduction has gone down and there are indications that this may be due to a lack of economic opportunity for the many.
6. Selecting countries with different geographical location, including at least one landlocked.
7. Inclusion of at least one country that has transited from conflict.
8. Inclusion of countries with mineral resources potential.
9. Selecting countries where the Bank has applied inclusive growth type approaches and at least one country where this was not the case.

Table 1: Country reports included in the study

Country, Report type	Title	Date of issue
Ghana, CEM	Meeting the Challenge of Accelerated and Shared Growth	November 2007
Ghana, CAS	Country Assistance Strategy Progress Report	March 2010
Mozambique, CPS	Country Partnership Strategy FY12-15	February 2012
Mozambique, CEM	Reshaping Growth and Creating Jobs through Trade and Regional Integration	March 2012
Uganda, CEM	Moving Beyond Recovery: Investment and Behavior Change, For Growth	September 2007
Uganda, CAS	Country Assistance Strategy For the Period FY 2011-2015	April 2010
Vietnam, CPS	Country Partnership Strategy FY12-FY16	November 2011
Vietnam, VDR	Vietnam Development Report 2012: Market Economy for a Middle-Income Vietnam	December 2011

In addition to the nine criteria it is necessary to have country reports of a recent date as both the growth diagnostic approach and the inclusive growth analysis are recent developments, whereby these analytical approaches can only be expected to have influenced World Bank documents after 2006/7. Ghana and Uganda are included also because the CEMs from the two countries are highlighted as "good practice World Bank reports" by the World Bank itself (go.worldbank.org/5PYL43EWZ0). Furthermore, the two reports were assessed by the Independent Evaluation Group (IEG) in 2010 and both the use of the growth diagnostic framework as well as the overall quality of the CEMs were judged to be satisfactory and highly satisfactory, respectively (IEGCR & IEG, 2010). However, since the two CEMs were issued in 2007 they both predate the systematic presentation of the inclusive growth analysis by Ianchovichina and Lundström (2009) as well as the three Inclusive Growth courses held in Ukraine (2009), Washington, DC (2010), and Nairobi (2011) (go.worldbank.org/677R9R65J0). Mozambique, having both a CEM and a CPS from 2012, is therefore selected as a third case. Finally, criteria 1, 2, 3, 4 and 9 lead the team to look at Vietnam even though this country does not have a CEM. Instead of the CEM the latest Vietnam Development Report (VDR 2012) is included as a case, partly because the annual Vietnam Development Reports represent highly profiled joint donor documents in Vietnam and partly because the Vietnamese CPS is the first World Bank report on Vietnam since its change in status from low-

income to middle-income country. The details of the 8 country reports included in the study are listed in Table 1.

3. Assessment Approach

The reports from each of the four countries are evaluated along three dimensions; (i) objectives, (ii) quality, and (iii) coherence and relevance. The CEM and the CAS/CPS serve different purposes; therefore quality and analytic rigor is emphasized for the CEM while coherence and relevance is emphasized in the assessment of the CAS/CPS reports.

In each of the categories a set of criteria are used for assessing the reports:

Objectives

- Are the objectives of the reports clearly defined up-front?
- Do the objectives include considerations about inclusive growth; productive employment, income generation, or poverty reduction?
- Are the objectives measurable and measured?

Quality (mainly of the CEM)

- Are the reports of good technical quality?
- Do the reports make use of analytic frameworks or models such as growth diagnostics, benchmarking, disaggregated analyses, sector dynamics analyses, or CGE models?
- Do the reports include analyses of employment and income generation?
- Do the reports include analyses of demographic trends and migration
- Are the data analyses relevant and well crafted?
- Do the reports give recommendations in a clear and actionable way?
- Do the recommendations include policies for increased productive employment?

Coherence and Relevance (mainly of the CAS/CPS)

- Are the policy strategies in the CAS (or CPS) based on the analysis and recommendations in the CEM when the latter predates the former?
- Do the reports give a coherent description of recent economic trends?
- Do the reports give a consistent analysis of the current situation?
- Do the reports include a well-argued and documented outlook leading to sensible and realistic recommendations?

Table 2 at the end of the report gives the specific country evaluations in a simple tabular form, while the more comprehensive assessment is given in Section 5. The assessment of the quality and of the coherence and relevance is based on the growth diagnostics approach and the inclusive growth framework when appropriate.

4. Growth Diagnostics and the Inclusive Growth Framework

The growth diagnostics approach, initially proposed by Hausmann, Rodrik and Velasco (2005), focuses on identifying country specific binding constraints for purposes of policy reform. Observing that countries who implemented a few well-targeted reforms have had better growth performance than countries that undertook comprehensive broad based economic reforms led HRV to the idea that each country faces its own set of binding constraints and that a few focused interventions alleviating these constraints will have a larger impact on growth than the "one size fits all", Washington Consensus, reform approach intended to simultaneously remove all distortions. The HRV methodology has subsequently been debated and criticized, and this has led the authors to present an adjusted version of the approach, described in detail in the Growth Diagnostic Mindbook (Hausmann, Klinger and Wagner, 2008) and in Chapter 3 in Rodrik (2007). In the following the main ideas of the HRV growth diagnostics approach are summarized and the links between that approach and the World Bank's Inclusive Growth Analysis (IGA) are described.

4.1. Growth Diagnostics in Theory and Practice

Three methods have traditionally been used in descriptions and analyses of a given country's growth performance: (i) growth accounting, (ii) benchmarking and (iii) cross-country growth regressions. A prominent example of a classical growth analysis with a strong focus on growth accounting and benchmarking, leading the way for many subsequent studies, is The East Asian Miracle report (World Bank, 1993). During the 1990s and early 2000s growth analysis changed, in particular the more academic studies, towards cross-country regressions and the focus of analysis moved from the proximate causes of growth—human and physical capital accumulation—to the deep determinants of long run growth, say, institutions, leaving less room for country specific growth strategies.

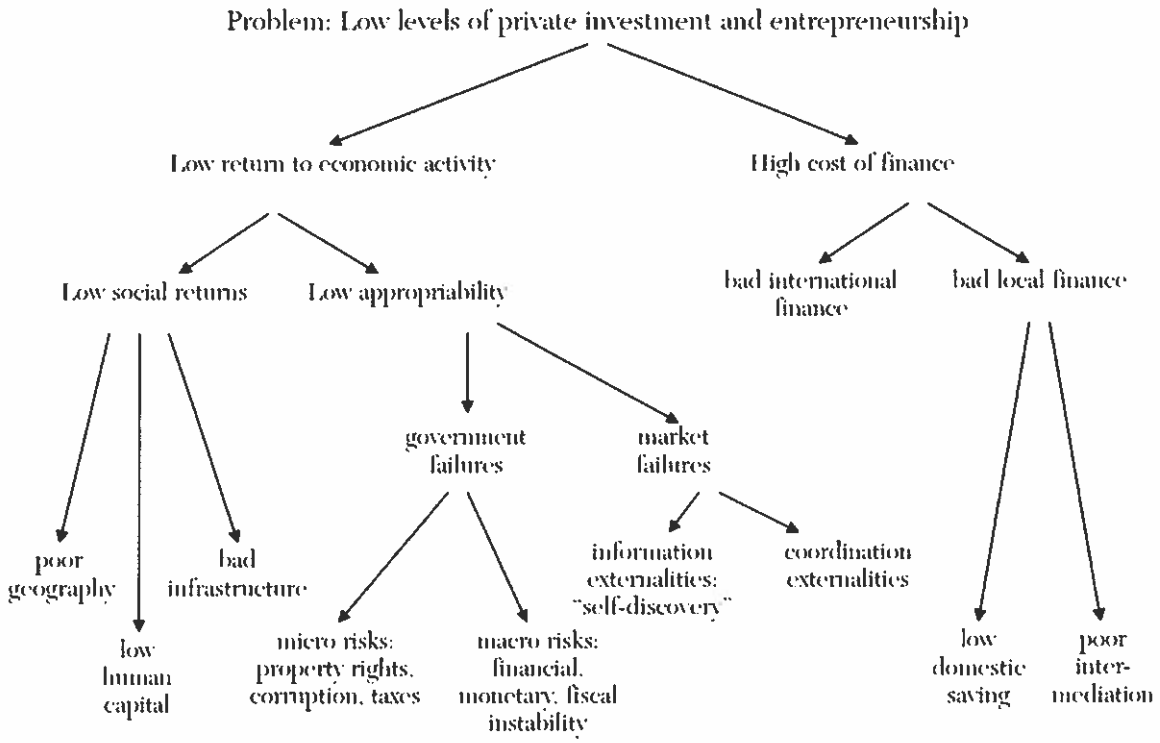
In 2005 Hausmann, Rodrik and Velasco presented a new approach by introducing a methodology which, in their view, opened for the possibility that the determinants of growth are country specific, and to a large degree complements instead of substitutes. The HRV growth diagnostics approach provides a framework for identifying and formulating hypotheses about the main constraints a specific country is facing. The analytic objective is to identify the constraint on the factor that offers the largest positive *direct* growth effect, such that the impact of easing this constraint should be sizable and beneficial even after possible opposing indirect effects are allowed for. As such, the approach takes economic growth to be an outcome of a constrained optimization process and it seeks to identify the factors that are most binding. The point of departure is a simple neoclassical growth model, which is only used to assist in identifying factors that are likely to constrain economic growth, and the methodology is often described by a decision tree as depicted in Figure 1.

By starting from private investment and entrepreneurship the HRV approach emphasizes the idea that developing countries' main problem is shortage of capital and productive capacity, and that the process of economic growth may be described as a generalized process of capital accumulation. This idea squares well with one of the main results of the Growth Report; that a common feature of high growth countries is that they all have high investment rates (Commission on Growth and Development, 2008).

Further, using the fact that a high shadow price of a factor reflects relative scarcity of the particular resource, a key element of the HRV approach is to use shadow prices to indicate potential constraints. Hence, starting from a simple condition describing the investment decision, low investment must be a result of the marginal benefit being low relative to the marginal cost, which again must be reflected in either low perceived return to investment or high costs of financing. (The first split in the decision tree in Figure 1).

Thus, as step one, the analyst must decide if private investment and entrepreneurship is low because of low returns or high costs (i.e., demand or supply factors). After this first decision the tree leads the analyst through different nodes further on as indicated in Figure 1. At each node there is an indication of a "symptom", which is a possible binding constraint.

Figure 1: Growth Diagnostics Decision Tree



Source: Hausmann *et al.* (2005); also in Rodrik (2006).

Following the initial formulation in Hausmann, Rodrik and Velasco (2005), there have been discussions about the precise structure of the decision tree and it has developed since then. Still, the main contribution of the methodology; using available evidence to piece together a coherent story of the problem, continues to be valid. The existence of constraints must be explained in a clear and consistent causal story. Unfortunately, it is not always obvious how this is to be done, and this is likely to be the most serious obstacle to the diagnostic approach.

Therefore, several descriptions of operational procedures have been put forward. Rodrik in 2007 posted a comment on his weblog (rodrik.typepad.com) describing some of the hallmarks of a successful growth diagnostics exercise:

(i) Move downwards in the decision tree, rather than upwards or sideways;
(ii) Work off a model of what drives growth in the economy;
(iii) Look for the tell-tale symptoms that a given constraint binds;
(iv) Look for clues showing that the hypothesized constraints are consistent with recent growth experience;
(v) Use micro-level surveys critically, knowing that complaints do not always accurately identify binding constraints;
(vi) Locate successful firms or sectors and trace their success either to their low intensiveness in the hypothesized constraints or to special circumstances that allowed these activities to overcome the constraints;
(vii) Combine cross-national benchmarking, micro- and meso-level surveys, and aggregate macroeconomic data in an eclectic manner as the nature of the question demands.

By following these rules-of-thumb the analyst should end up with a set of recommendations for a *limited number* of *concrete* actions that are *country specific* and *feasible* (administratively and politically).

Another operational procedure, which adds a sequential analytical process, is formulated in Hausmann *et al.* (2008):

(i) Describe the growth process and identify the country's current growth "state".
(ii) Go through a differential diagnosis following the principle that a constraint is binding if
    a. the shadow price of the constraint is high,
    b. movements in the constraint produce significant movements in the objective function,
    c. economic actors attempt to overcome or bypass the constraint, and

d. economic agents that are less likely to be exposed to the constraint are more likely to thrive and survive.

(iii) Identify possible "syndromes". (A syndrome is a logically consistent causal chain that accounts, as much as possible, for the observed facts.)

(iv) Implement a diagnostic that assesses state capability (Pritchett, 2008).

Even if the analyst strictly follows the simplified procedures outlined above the growth diagnostics approach involves many tests and alternative explanations that are difficult to structure. Therefore, Hausmann *et al.* (2008) provide an example in the form of a matrix providing an internally consistent identification of symptoms, where columns indicate constraints faced and rows represent symptoms (Figure 2). The matrix is an illustration, but it can be modified and extended for individual country cases. Once the matrix has been contextualized, the analyst should be able to derive well-supported hypothesis about the binding constraints.

In the assessment of the four country documents in Section 5 both the original "Decision Tree" in Figure 1 and the second generation "Constraints and Symptoms Matrix" in Figure 2 will be considered as good starting points for a HRV growth diagnosis.

Figure 2: A Matrix of Constraints and Symptoms

<table>
<tr><th colspan="2">Binding Finance</th><th colspan="6">Binding social returns</th></tr>
<tr><th rowspan="3">Low aggregate Savings</th><th rowspan="3">Bad finance</th><th colspan="2" rowspan="2">Lack of complementary factors</th><th colspan="3">Low appropriability</th><th>Coordination</th></tr>
<tr><th colspan="3">Government failure</th><th>Market fail.</th></tr>
<tr><th>Ex ante</th><th colspan="2">Ex post</th><th></th></tr>
<tr><th></th><th></th><th>Human Capital</th><th>Infrastructure & public goods (geography?)</th><th>Ex ante risks</th><th>Tax</th><th>Low property rights, crime & corruption</th><th>Low R&D Low Self discovery</th></tr>
<tr><td colspan="2">High lending interest rate</td><td colspan="6">Low lending interest rate</td></tr>
<tr><td colspan="2">Low net cash flow from banks</td><td colspan="6">High net cash flow from banks (dC/C - i)</td></tr>
<tr><td colspan="2">Investment elastic to interest rate</td><td colspan="6">Lack of investment response to interest rate change</td></tr>
<tr><td colspan="2">Access to external finance (EMBI, Default risk, CAD, Unsustainable debt)</td><td></td><td>Low infrastructure wrt comparable countries</td><td>High static markups & low entry; in industries with entry costs</td><td>Monopoly power high markups. Regulated entry</td><td>Expropriation</td><td>Low sophystication (EXPY) and few new industries</td></tr>
<tr><td colspan="2">Short loan duration, credit rationing</td><td>Inward migration high skills</td><td rowspan="2">Shocks to infrastructure (hurricane, war)</td><td>Political risk, social risk</td><td></td><td>Social unrest</td><td>Growth responds to new indus</td></tr>
<tr><td>High deposit interest rate</td><td>High spread</td><td>High returns to education</td><td>Tax policy risk</td><td>High taxes: Top marginal tax rate, corporate tax, VAT</td><td>Open conflict</td><td rowspan="2">Few products "nearby" to move (openforest low)</td></tr>
<tr><td rowspan="3">Negative relation between growth and current account.</td><td>If it's high risk, then low profits</td><td>Procyclical mincerian returns</td><td>Growth elastic to infrastruct. Change</td><td>Labor market risks</td><td>Restrictive labor regulations</td><td>Corruption (illegal tax rate) (Kaufman)</td></tr>
<tr><td>High operating expens /assets</td><td>Low tertiary for level of development</td><td>Congestion</td><td>History of expropriation</td><td>Inflaton tax</td><td>High protection costs (ICA)</td><td>High correlation of growth with TOT</td></tr>
<tr><td>Monopoly powers: high (P/E) ratio of banks</td><td>Returns decrease as education grows</td><td>Port quality. High losses in transport (ICA)</td><td>High expectation of losing future profits</td><td colspan="2">Cost of doing business</td><td>High returns to coordination activities</td></tr>
</table>

Source: Hausmann *et al.* (2008)

4.2. Potential Problems with the Traditional HRV Approach

Although the growth diagnostic approach has been fairly well received in the World Bank and in most academic circles, a number of scholars have commented on and criticized the approach. Subsequently both Hausmann and Rodrik, in varying author constellations, have further developed the approach and they have responded to and incorporated some of the criticism.

The strength of the approach is that it opens up for a formal analysis and debate about the structural problems affecting growth in the individual countries and it offers policymakers a coherent framework for analysis. However, as emphasized by Felipe *et al.* (2011) the key to benefiting from the full potential of the approach lies in a clarification of its primary objectives and also in understanding the limitations of the approach for operational use. In the following we therefore identify the five main points of critique of the HRV methodology as they are presented in the academic literature. The criticism can be categorized as related to; (i) policy, (ii) ignition versus sustainability, (iii) appraisal of shadow prices, (iv) simultaneity, and (v) data availability.

(i) Policy: The political capacity needed for successful reforms is a scarce resource in most developing countries. Therefore, an appealing feature of the HRV approach is the prescription that policymakers should not initiate too many reforms at once. However, Robinson argues that even focusing on a narrow set of economic reforms will not necessarily have the intended effect (Robinson *et al.*, 2009). Specifically, Robinson contends that in many African countries the industrial policies implemented were both needed and reasonable—they were, in fact, aimed at removing some of the most binding *economic constraints*—and they should therefore have ignited economic growth under the right circumstances. However, there was no hope that they could do this under the *political constraints* present in most African countries. By the HRV approach it is acknowledged that government intervention can be a powerful tool to promote economic growth, but the political circumstances that induce growth enhancing decision making processes in the interests of society are still poorly understood and, unfortunately, the HRV approach only diagnoses the economic constraints. This criticism has to some extent been addressed by Hausmann *et al.* (2008) and Pritchett (2008) as it is now emphasized that a complete growth diagnosis must also assess state capacity.

(ii) Ignition versus sustainability: Felipe *et al.* (2011) argue that the HRV approach implicitly assumes that adequate policies and reforms at each "growth stage" (igniting versus sustaining growth) are mutually independent. While Rodrik (2007) touches upon issues about the design of institutions for sustaining growth, HRV recognize that obstacles to igniting growth seems much easier to identify and address than obstacles to sustained growth. Unfortunately, the problem facing many economies today is not how to start growth but how to sustain a strong growth performance in the medium and long term. The focus on growth ignition may therefore explain why the decision tree used in

most studies conducted so far has focused on countries with low levels of private investment and entrepreneurship. But, once a country is growing an increasing investment rate may not be a necessary condition for sustained growth.

(iii) Identifying shadow prices: Identification of a country's binding constraints is, according to the HRV methodology, best done by looking at shadow prices in the economy; if lack of credit is a problem, then interest rates should be high; if human capital is a scarce resource, then the skill premium should be high; if taxes are overly burdensome, then informality should be widespread. However, Rodriquez-Clare (2009) notes a problem with this approach in that absence of markets makes it difficult to apply a "shadow price" approach. Studies following the HRV methodology often end up gathering information about shadow prices from qualitative measures and opinion surveys, which is precisely what the methodology is hoping to avoid. Felipe *et al.* (2011) agree with this problem of implementation and conclude that it will be inevitable for researchers to rely on theory and indirect evidence for judging the scarcity (shadow price) of a resource.

(iv) Simultanity: Adding to the problem of using shadow prices, Rodriguez-Clare (2009) argues that binding constraints may not always be reflected in high shadow prices, even if markets exist. As an example, lack of credit may be a constraint while at the same time interest rates are low in equilibrium due to weak enforcement of credit contracts. Another problem is complementarities. Removing constraints along one dimension may yield small benefits, while large gains would only result from simultaneous reforms. Here, the operational procedures suggested introduce a problem because independence of the nodes in the decision tree is assumed and not tested (Felipe *et al.*, 2011). For example, high cost of finance and low private economic returns may not be independent, as it is possibly the same forces that explain both causes. As highlighted in Dixit (2007) each case of development failure may have multiple causes acting simultaneously. Headey (2009) strongly seconds this critique by arguing that given the strong interconnectedness of the many of problems facing a typical developing country, the HRV approach of identifying and targeting the supposedly most binding constraint may be inherently impossible, and ultimately just as useless as targeting all problems at once. This final point is, however, mainly an empirical, not a theoretical problem.

(v) Data availability: Finally, adding to the empirical problems, one may also question if the HRV approach, given the available data, is able to convincingly find the most binding constraint in a typical low income country or if the constraint identified is simply limited to the case/node where information is most readily available.

Overall, the academic critique of the HRV approach is mainly about the limitations in terms of coverage (political constraints and constraints to sustained growth); about data (existence of shadow prices and the informational contents of observed shadow prices) and, of course, about the whole endeavor of splitting up a general equilibrium system into nodes in a decision tree. Interestingly, within the World Bank and in bilateral

donor agencies the approach has mainly been criticized for its narrow focus on the investment side of the aggregate economy. This is interesting because the Growth Report (Commission on Growth and Development, 2008), as already noted, finds high investment rates to be common to all the 13 high growth countries analyzed in the report.

4.3. Growth Diagnostics and Inclusive Growth Analytics

In line with the Growth Report, Ianchovichina and Lundström (2009) argue that economic growth needs to be inclusive in order to be sustainable and they emphasize two characteristics that are underexplored when following the original HRV growth diagnostic approach.

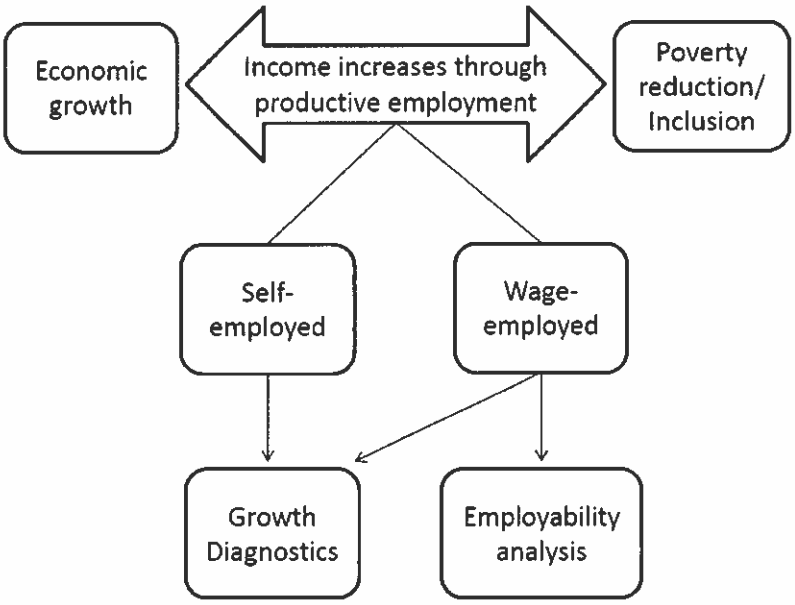
(i) While the recommendations resulting from a HRV analysis are meant to increase economic growth it does not follow that they will also lead to poverty reduction. Thus, there is a need to ensure that the increased growth is inclusive in the sense that it leads to increasing incomes for large population groups, in particular also the lowest income groups.

(ii) Even though the HRV approach may uncover important growth constraints, the analysis will not easily discover obstacles to structural transformation—for example movements of labor from agricultural production to manufacturing industry, or simply creation of non-farm employment in rural areas.

To advance the analysis of structural transformation and, more specifically, to look into whether the economic growth in a given country is inclusive and sustainable, Ianchovichina and Lundström argue that growth diagnostics should be augmented by an in-depth description and analysis of the labor markets to form a comprehensive Inclusive Growth analysis (IGA).

The importance of the labor market is underpinned by the argument that the main instrument for inclusive growth is creation of *productive employment* (see Figure 3). Employment growth is important in itself because new jobs generate income for the people in the economy. Moreover, labor productivity growth is equally important in the longer run as this is necessary for increased wages for the workers and increased profits for the self-employed. Remarkably, Ianchovichina and Lundström do not note that concurrent growth in employment and labor productivity require high capital accumulation—i.e., high investment rates—if production is as described by standard economic growth models such as the one underlying the HRV approach. This observation actually makes a HRV diagnosis a necessary, though not sufficient condition for finding constraints on inclusive growth.

Figure 3: Inclusive Growth Diagram

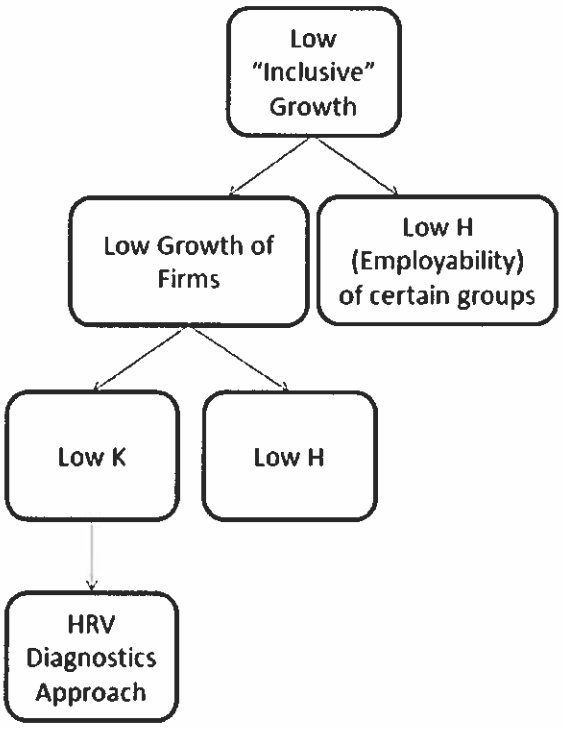


Growth Diagnostics: Constraints for firms viewed from the perspective of different economic actors
Employability analysis: Constraints for individuals viewed from the perspective of different economic actors.
Source: World Bank course on Inclusive Growth Analytics, available at www.worldbank.org

Still, the value added of IGA comes from determining the causes of observed growth and equity outcomes, and the greatest insights from IGA will come from the effort to link macroeconomic outcomes on growth and distribution to their specific sources. As such, IGA choices will be closely linked to the HRV approach, but the IGA augments the physical capital node of the HRV decision tree to include human capital and labor market (supply-side) considerations.

In order to analyze the obstacles and potentials in the labor markets it is necessary to look at both supply and demand. The analysis of aggregate labor demand is well covered by the HRV approach as this is an in-depth analysis of the overall business environment. On the supply-side the analysis must focus on the resources of the individuals; what in Ianchovichina and Lundström (2009) is called an "employability analysis" that looks at the individuals' health and education. In addition, to uncover possible obstacles to sector transformation, a disaggregated description of the labor market is needed, implying a description of current and potential employment by geographical region (and urban/rural), by sector, and possibly also by firm structure; containing the distinction between the formal and informal sector.

Figure 4: Inclusive Growth Analytics Tree



Source: World Bank course on Inclusive Growth Analytics, available at www.worldbank.org

The Inclusive Growth Diagram (Figure 3) combined with the Inclusive Growth Analytics Tree (Figure 4) provides an illustration of how to further understand the link between the HRV approach and the IGA as proposed by World Bank researchers (see the World Bank course on Inclusive Growth Analytics for additional information). The bridge between growth diagnostics and inclusive growth thus comes from assumptions about the role of employment: Given that labor is usually the most important asset of the poor, and a major determinant of poverty reduction, employment will be the transmission channel between individuals and growth. So the IGA suggests focusing on productive employment in addition to analyzing the investment channel. As such, an IGA should, at least, add two elements to a HRV style growth diagnostic framework:

(i) *An analysis of the overall dynamics:* drivers of past growth (sustainable versus dividend driven). Past dynamics and the potential in different sectors: the growth-poverty pattern, sector dynamics, labor migration and demographics, productivity dynamics, diversification, etc.

(ii) *A profile of all economic actors:* identifying the income-generating activities and resources (health, education/skills) of the different economic actors, especially the non-included group.

In the assessment of the country documents below, the distinction between a HRV growth diagnosis and an IGA is based on the degree to which an analysis of the overall growth dynamics and a profile of the economic actors are included in the reports.

5. Country Results

5.1. Assessment of the Country Economic Memoranda

In the individual descriptions of the Country Economic Memoranda it is assessed whether three central parts of an IGA have been followed. First, with the national accounts identities in mind, it is noted if the CEM incorporates all necessary elements sufficient for a comprehensive analysis of growth trends, including the aggregate demand sources (expenditure components) and sector decompositions. This should ideally also include an analysis of factor returns and growth contributions, including a discussion of the role of a factor accumulation versus TFP growth. Second, the CEM should convincingly provide tell-tale symptoms of a given constraint being binding. As part of this constraints identification, the CEM should use a differential diagnosis approach following the principles described above, leading to a thorough analysis of prices, and a requirement of consistent micro-level stories of successes and failures in accordance with the constraint hypothesized. Third, the CEM should document a clear connection between the constraints identified and the policy recommendations made.

5.1.1. Ghana

The Ghana CEM, from 2007, consists of three volumes. The first volume is a macroeconomic analysis describing Ghana's growth and poverty reduction experience. In one section a CGE model is used to analyze the achievement of the MDGs under different scenarios. Assuming macroeconomic and political stability, infrastructure is identified as the main constraint to both growth and poverty reduction. The second volume focuses on different sector relevant analyses; infrastructure, agriculture, export, investments (including doing business climate) and challenges related to Dutch disease. Volume three is more technical in nature, with specific analysis of poverty and measurement, labor market and skills, gender issues and a political economy analysis. Most of the following comments are directly related to the two first volumes, but they also take into account the detailed analysis of poverty and the labor market in Volume 3.

The CEM should be seen as a supplement to the significant focus Ghana and the World Bank had at the time on issues linked to health, education and public expenditure management. There was therefore both room and need for a report with emphasis on growth. Further, it should be noted that the situation in Ghana changed significantly shortly after the completion of the CEM. First of all, sizeable oil reserves were discovered and, second, the outgoing Government made major and non-transparent increases in public spending (and the deficit) in the run up to the election. These events have a

profound impact on the inclusive growth prospects of Ghana but, naturally, they are not covered in the CEM.

Analysis of Growth Trends

The CEM starts out with a very detailed description of both supply and demand-side structures of Ghana's growth. The description is broad and covers trend analysis of all national accounts identity variables as well as detailed sector analyses, including household level studies and a poverty mapping. The section also includes detailed growth accounting decompositions as well as a series of international benchmarking exercises. Finally, trends in employment and earnings are described as well as a detailed review of studies looking at poverty and inequality. As such, the report has the intended focus on inclusive growth analytics.

Constraints Identified

The CEM identifies three areas that are considered the most binding constraints to growth in Ghana:

(1) Severe infrastructure gaps (especially in energy and water & sanitation) - (§7)
(2) Low productivity (especially in agriculture) - (§8)
(3) Weak investment climate - (§9)

Not all constraints a country faces should be addressed when following the HRV/IGA approach and an important question is whether the CEM provides convincing arguments for the suggested constraints being the most binding. In the following we argue that the analysis of the constraints would have benefitted from combining the selected approaches with a more stringent HRV decision tree analysis to validate findings and recommendations.

The identification of all constraints is done in a traditional way by, for example, highlighting infrastructure gaps through several different benchmarking exercises and cross-country regressions. In the same manner the CEM identifies access to finance and other business climate dimensions as additional constraints, although these are not as important as the infrastructure constraints. Benchmarking exercises are accompanied by a CGE model adapted to a number of outcomes whereby the importance of the infrastructure constraints is analyzed not only from a growth perspective, but also from the view of poverty reduction.

In addition to cross-country regressions, the CGE models and benchmarking, the CEM also use growth accounting to document the recent increase in the contribution to total GDP growth of total factor productivity (TFP) growth. Moreover, the CEM assess the extent to which TFP growth is attributable to inter-sector and intra-sector labor reallocations, to technological changes, and to economies of scale. The sector-level analyses reveal a significant role of labor reallocation in explaining factor productivity growth and

that agriculture is responsible for a significant part of the recent increase in TFP growth. The CEM is generally successful in telling the stories linking documented policy improvements and observed changes in total factor productivity.

Reform Recommendations

In outlining a strategy to address the constraints, the CEM includes recommendations which are at a rather general level and few of them are directly actionable. Specifically, in order to alleviate the identified constraints the CEM recommends at least 6 areas that the government should focus on (§13):

(1) Eliminate current infrastructure bottlenecks by eliminating the short-term annual funding shortfall for infrastructure and by targeting the main bottlenecks in electricity (especially focusing on the access of electricity to firms), water and sanitation, ICT, and some rural roads. Greater emphasis should be placed on rural roads and connectivity of the poorest regions with the mainstream centers of economic activity.
(2) Widen the use of technology and ICT (R&D investments) and aggressively seek opportunities for greater private participation in infrastructure, especially in ICT (and partly energy).
(3) Transfer (within agriculture) of lessons of recent productivity gains in the cocoa sector due to better use of disease control, fertilizers, product varieties and contemporary agronomic techniques.
(4) Improve access to finance especially for small and medium-size enterprises.
(5) Accelerate tariff reform while safeguarding the poor's affordability.
(6) Strengthen regulation and depoliticizing sector management.

As such, the report helps outlining priority areas which should be the focus in the future, rather than prescribing appropriate action plans. One reason for this may be that the CEM tries to cover substantial ground, which may come at a cost of specificity.

Overall Assessment

The technical quality of the documents and the consistency in causal arguments is generally satisfactory, although each volume and, in particular, sub-sections vary in quality. Unfortunately, there is no clear relationship between the volumes. However, there are no obvious inconsistencies between the main messages in each volume either. As such, the document is successful in defending the identified binding constraints to inclusive growth even though a HRV/IGA framework is not directly applied.

Further, the growth analysis in the CEM is accompanied by a structured summary table (pages 12-13), which to a certain degree entails parts of the structural thinking underlying a HRV decision tree and, in addition, it provides a structured overview of the suggested policy agenda for continued accelerated and shared (inclusive) growth in Ghana. Thus, we find that the CEM in its analyses and recommendations implicitly include in-

clusive growth considerations. This is in accordance with the assessment in the evaluation by IEGCR & IEG (2010).

5.1.2. Mozambique

The Mozambique CEM, from 2012, consists of two volumes. Most of the following comments are directly related to the summary of main findings (page 9-26 covering points 1 through 73) and Chapter 1 which covers the growth diagnostics part of the CEM (page 27-42, covering points 1.1 through 1.44). In addition to the summary and the growth diagnostic the CEM has detailed chapters on trade, fiscal policy and megaprojects (Chapter 2), logistics (Chapter 3), supporting exports (Chapter 4), land tenure for growth and poverty reduction (Chapter 5) and professional services and development (Chapter 6). Volume II covers more detailed, sector-specific findings.

Analysis of Growth Trends

The CEM starts out by describing its focus on particular subjects and highlights that the important question for Mozambique is how to sustain high growth and reshape its pattern to generate more employment. As such, the report has an inclusive growth focus as it does not only aim at analyzing the pace of growth but also the pattern of growth and employment.

According to the report (bullet-point 7, page 10) four areas need to be addressed in order to reshape the pattern of growth:

(1) Macro policies and business regulations need to be friendlier towards businesses and reduce the bias towards capital-intensive growth;
(2) Factor markets should allow a more efficient allocation of resources to the most productive uses;
(3) Logistics infrastructure needs to reduce the costs of importing, exporting, and transporting, and improve the reliability;
(4) Institutions supporting exports are fundamental if small and medium businesses are to succeed in exporting and mastering the supply/value chain.

It is stressed that these areas are the focus of the CEM and that the wider agenda is not dealt with. It is acknowledged explicitly that a deeper perspective is needed in the future in order to establish a clear development vision and an inclusive growth strategy for Mozambique. As such the current CEM does not come full circle in the HRV/IGA sense, as it focuses on the dynamics of pre-selected constraints on selected parts of the economy. Especially the lack of focus on rural transformation, spatial dimensions of poverty and informal-formal transition patterns questions whether inclusive growth thinking is truly seen as a central part of the future development strategy.

The report is also somewhat selective in its analysis of growth trends, and not all aggregate demand sources of growth are equally covered in the trends description. This is un-

fortunate since some of the analyses in the report make us question if all appropriate data sources have been fully utilized. One example is the description of the remarkable growth and poverty reduction record Mozambique experienced from 1992 onwards. Average annual real GDP growth was 7.5 per cent from 1993 to 2010. The CEM correctly states that the poverty headcount fell from 69 per cent in 1996 to 54 per cent in 2002 and also that consumption per capita grew by a cumulative 50 percent over the same period. However, recent evidence from the household survey (IOF – see INE) carried out in 2008/09 shows that the poverty headcount rate has remained close to constant since 2002. This information is not included in the CEM, although this is important for understanding if the observed growth surge has been broad-based in the last decade. However, it should be noted that other bank documents have covered this issue in detail and addressing equity problems in Mozambique have high priority in Bank strategies (as emphasized below in the CAS section).

Overall, the analysis of growth trends lacks necessary detail to fulfill the requirements of the HRV/IGA approach. This will limit the opportunities for verifying whether suggested binding constraints, and changes herein, are in accordance with the observed growth trends. Examples of such potential problems are given in the next sub-section.

Constraints Identified

The CEM identifies four areas that are considered the most binding constraints to growth in Mozambique. In order to alleviate these constraints the report recommends that the government (§1.33);

(1) Reduce market distortions, improve the regulatory environment, and get more benefits from megaprojects.
(2) Undertake infrastructure investments to reduce the costs of trade logistics.
(3) Provide services to support exports of new products (improve the product space).
(4) Improve access to land for investors without disenfranchising existing land users.

The CEM is not overtly clear about which procedure the growth diagnostic in Chapter 1 uses as a tool of direction. The arguments and analysis do not follow a clear decision tree structure or an identification of symptoms. This creates some confusion when trying to understand the list of binding constraints given.

Taking the recommendation to reform the tax and tariff system as an example (§§2.11 to 2.17), the CEM highlights how Mozambique has made considerable progress in reforming its tax policy over the past 15 years, but the standard statutory tax regime continues to place a substantial burden on certain investors, notably small domestic entrepreneurs. Moreover, the past tax regime encouraged capital intensive enterprises as compared to more labor-intensive industries. This conclusion is supported by the results in the sector analysis in Volume II. Combined with a fiscal response analysis showing that the fiscal climate could be significantly improved by reducing simultaneously

fiscal incentives and the number and level of tax rates without compromising government revenues, the CEM leads to a clear conclusion that cutting statutory tax rates will remove a serious distortion to the doing business environment.

However, benchmarking Mozambique's fiscal pressure against other countries in Sub-Saharan Africa does not place Mozambique in the problem zone. This is noted in the CEM and it is also highlighted that Mozambique offers companies a wide range of fiscal incentives, so that the actual tax burden differs substantially from the statutory burden, in the end resulting in a very narrow tax base. It is also described how the distortionary tax system has increased the implicit cost of doing business in Mozambique in an unequal way. This is also apparent from the fact that the majority of firms report zero tax payments (see ICA, 2008), which also indicates that tax evasion is rampant and that tax administration remains weak.

The weak tax administration is also seen by the substantial variation in the effective tax rates paid by different firms within the same income range, even within sectors, which is not documented in the CEM but highlighted in the ICA (2008), suggesting inconsistencies in tax administration. It is, however, not clear from the analysis in the CEM whether the main constraint in the tax system is the discretion in tax exemption rules (and/or high statutory tax rates) or whether the primary cause for these inconsistencies is the excessive discretion enjoyed by inspectors and their rent-seeking behavior. Moreover, industry level analysis actually documents that the sectors enjoying the largest growth trends are the ones facing the greatest tax burdens, which again questions if high statutory tax rates are among the most binding constraints to growth in Mozambique. Overall, further discussion of whether it is the corrupt behavior of tax officials or the statutory tax pressure that is the most binding feature of the tax regime is needed. Hence, adhering to a HRV decision tree procedure we would argue that the CEM has not made persuasive arguments for taxes being a major binding constraint on growth.

Moving to education and skill constraints which is an important feature of the inclusive growth framework, §1.12 describes how the low educational levels in Mozambique remains a constraint on job creation in the formal sector. Moreover, §14 also mentions that strategic investments are needed in education to upgrade the skill base of the Mozambican labor force as a transition to a more manufacturing driven economy requires a higher education profile. So continuing to invest in and prioritize education is central for inclusive growth. However, it is at the same time highlighted that the continuing increase in demand for education will be dependent on an increase in households' disposable income (about which the report is silent). In identifying the binding constraints the CEM may be criticized for not following the HRV decision tree to the root of the problem. The CEM has a thorough description the dramatic change in student enrollments. Demand has been rising faster than the related infrastructure and training of teachers, resulting in quality issues both due to shortage of resources and absorptive

capacity. To increase completion rates, continuing effort is needed to further alleviate households' infrastructure and financial constraints. But this indicates that in order to get more students through the secondary school system, serious education infrastructure and household financial constraint problems must be addressed first. Hence, these issues may be the real binding constraints to increased secondary school completion rates. The CEM does not address this problem.

Reform Recommendations

The CEM is straightforward regarding the link between the identified constraints and the reform recommendations. However, the main recommendations listed in the CEM have the following characteristics:

- They cut across all sectors.
- They suggest general reduction of administrative transaction costs, with a special focus on reforming the tax and tariff system.

In addition it is recommended that Mozambique

- Improves the implementation of the land law,
- Improves trade logistics,
- Takes a more pro-active stand regarding the promotion of exports.

A surprising feature of the policy recommendations is that none of them are directly linked to the supply-side of the inclusive growth framework. This is puzzling given the emphasis on the significant education and skill constraints facing the Mozambique economy.

Overall Assessment

In the conclusion of the main findings of the CEM it is stated that "the objective of this report is to provide an ***organized*** framework for the development of a long-term strategy in Mozambique for a more ***inclusive*** and shared growth." (Page 26, bullet-point 70). This is a clear statement with implicit reference to both HRV growth diagnostics and IGA. However, the CEM does not quite live up to its promise. A more direct use of the HRV/IGA approach would have benefitted the report as a way to ensure that the CEM actually identifies the most binding constraints and provides convincing arguments for why the constraints are binding.

5.1.3. Uganda

The Uganda CEM from 2007 comes in two volumes. Volume 1 contains a selective summary and recommendations directly related to very detailed analyses in Volume 2. Volume 2 has eight detailed background chapters, of which several are either written by, or based on background papers by, prominent World Bank staff members. The structure of

the Volume trails the recommendations in HRV and, interestingly, also some of the modifications and corrections made in Hausmann *et al.* (2008) and in Pritchett (2008). Yet, while Volume 2 with its eight detailed background chapters, covering more than 260 pages, is heavy on data analysis and modeling jargon, Volume 1 summarizes the main messages—twice—in an accessible language, in only 53 pages. In addition, a section entitled "Specific recommendations for a growth strategy" in Volume 1 (§101) lists the top ten immediate growth recommendations while Annex 2 of Volume 1 extends the top ten to a list of 49 detailed action recommendations of which 30 are "Specifics for Action Now" leaving the remaining 19 as "Specifics for Action Soon".

The objective, a study of Uganda's growth, is motivated up-front in Volume 1 in a Foreword that also specifies the main recommendation, "getting the infrastructure basics right", and subsequently the structure of the report, the methodology *and* the limitations of the report. Thus, already in §17 it is specified that the report does not directly analyze priorities for human capital and skills development (although these are included indirectly as part of the growth diagnostics analysis) because this will be a topic for future analytical work. Furthermore, the report does not give detailed assessments of poverty and inequality as this was done in the 2006 Poverty Assessment Report. However, recent trends in poverty and inequality are described in chapter 2 of Volume 2.

Analysis of growth trends

The past growth trends are analyzed in two chapters in Volume 2 and summarized in §§41-66 in Volume 1. Chapter 1 in Volume 2 gives a very detailed account of the growth trends at the macro and sector levels. Uganda's growth performance is first compared to other countries in the region, and to other regions of the world. This is followed by growth decompositions both from the supply-side (by sector) and the demand-side (by expenditure components), and subsequently by input factor (an augmented Solow-decomposition). The latter decomposition is even augmented by an econometric analysis to try to account for the role of policy reforms in explaining total factor productivity growth and a qualitative analysis of short-term and transformational factors which explain the large residual value for TFP in the decompositions. At the end of Chapter 1 the analysis moves to the micro level looking for evidence of changes in productivity in firms and farms.

In addition to the growth analyses, the chapter has descriptions of the main demographic trends and employment. Employment is directly referred to in the key conclusions (page 1) and the key challenges (page 2) in Volume 2.

Key conclusions 4 and 5 are (p. 1):

4. The quality of growth seems to be improving. Many of the features of a dynamic economy are visible in Uganda's growth experience:

- farmers are switching to new higher value crops,
- labor is moving into new occupations,
- new products are being discovered, and
- new exports are emerging.
- the technology component of imports and exports is improving.

5. Human capital is improving from a very low base. Primary and secondary enrollment, and recently even university enrollment, has increased sharply. The seeds for an improvement in human capital have been laid. The labor force is set to expand dramatically in terms of size and skills.

The challenges are all directly related to demographic trends, employment growth, and regional diversity (p. 2):

1. High population growth and a high dependency ratio especially amongst poor families is a concern; this could limit domestic savings and investment and so provide a brake on national welfare unless Uganda can hasten a demographic transition.
2. Much of the growth in output and employment has been in informal and micro enterprises. 76 percent of new firms on the Uganda Business Registry in 2002 which were established between 1999 and 2002 employed less than 5 employees in 2002.
3. Much of the employment growth and new firm entry has been in services. Retail, restaurants, security services, health and education and more recently telecommunications sectors, have seen rapid job growth.
4. Employment in manufacturing and large-scale commercial agriculture has not grown so fast.
5. The Eastern and Northern Regions are trailing behind.

The key conclusions and challenges are summarized (in the text) in Volume 1, §§44-49. But the summary is less clear than the lists in Volume 2.

The agricultural sector is given special attention in Chapter 2 of Volume 2. By and large the chapter presents an independent growth diagnostics analysis for the agricultural sector including a view towards poverty reduction. The rich and detailed analysis in the chapter is completed by a list of eight challenges. These challenges are also given in Volume 1, §§58-65. Both places it is concluded that the primary challenge to sustained growth in productivity in Ugandan agriculture is the rising population (§58), and also that the recent expansion in off-farm employment is encouraging in this regard, but is discouraging in another (§59).

In conclusion, the analyses of the growth trends do include both the pace and the path of the growth and the structural changes, including employment and income generation, are well described.

Constraints Identified

Chapter 3 of Volume 2 explains the details about growth diagnostics and reports the results of an initial analysis. The chapter ends with a list of binding constraints (§376):

This growth diagnostic for Uganda concludes the following:

- Under-investment in infrastructure is the binding constraint to growth in Uganda;
- Electricity is the number one priority – with major investments needed in towns outside of Kampala to expand job creation;
- Trunk roads and main roads around Kampala need to be better maintained and expanded at key bottlenecks;
- The costs of power and fuel are too high;
- Financial intermediation is a future constraint that could quickly bind if infrastructure constraints are removed;
- Coordination gaps are leading to inefficiencies in infrastructure, and seemingly skills training.

Subsequently, infrastructure and the financial sectors are analyzed in detail in chapters 6 and 7of Volume 2 and this leads to the specific recommendations.

The main results of the growth diagnostics analysis are also reported in Volume 1, §§67-70 and the main results of Chapters 6 and 7 in Volume 2 are summarized in Volume 1, §§72-100.

In Chapter 6, in which the infrastructure situation and needs are assessed, there is direct reference to the Poverty Eradication Action Plan (§6.35). Further, in the chapter and in Volume 1 §§103-107 there is a presentation of different infrastructure constraints and growth opportunities, which adds important information about the different infrastructure policy interventions support different growth and poverty reduction objectives. Hence, when it is recommended to "scale up trunk road investments in Kampala, in selected other urban centers along the southern corridor (Mukono, Wakiso), on heavily trafficked trunk roads and by-passes, first by addressing the backlog of maintenance, then by increasing paving, (§101)" this has been weighted against the poverty reduction and growth impacts of improving feeder and district roads.

The constraints from financial intermediation are analyzed in detail in Chapter 7 of Volume 2. In this chapter, Section H describes issues and solutions for rural finance. It is stated that the lack of physical infrastructure and the lack of commercialization is a substantial impediment to financial institutions reaching out further and smallholders accessing formal sources of credit. Hence, the solution to rural credit problems must go hand-in-hand with the infrastructure interventions.

Reform Recommendations

§70 of Volume 1 give priorities for a growth strategy, split into strategic approaches and specific actions. There are ten strategic points and 49 action recommendations. As mentioned, the reform recommendations are very specific and divided into a top ten of immediate growth recommendations and a much longer list of 49 detailed action recommendations of which 30 are "Specifics for Action Now" leaving the remaining 19 as "Specifics for Action Soon".

The second and third strategic advices are clearly along the lines of inclusive growth thinking by linking short-term growth and structural adjustment in agriculture and by considering interventions to deal with the demographic pressure:

Advice 2 states: Don't neglect traditional agriculture whilst seeking to promote structural transformation, new exports, and value addition. The longer term aim should be to help the private sector to discover new and higher-value exports. Meanwhile there remain opportunities for short-term growth and poverty reduction through agriculture. Most immediately, addressing coffee wilt disease and banana bacterial wilt would inject significant productivity gains in coffee and matooke, two of the most important crops for smallholders. The rehabilitation of agriculture in the North could generate a significant increase in consumer demand, and a quick rebound in grain production. There is also significant short-term potential in simsim for export from the North. Longer-term there are prospects for cotton, livestock and hides and skins in the Northern Region. Elsewhere in the country, despite the more limited scope for opening up new land, substantial productivity gains are still possible from intensification through a faster roll out of the NAADS program.

Advice 3 is: Generate a rapid demographic transition with increased urbanization. Uganda must seek to bring down the high fertility rate quickly by implementing proven programs which will address the proximate determinants of fertility. Priorities are girls' education in the North, and better availability of modem contraceptive methods so that mothers can space births safely, and attain their desired number of children. Meanwhile Government needs to plan for a doubling of the workforce in 15 years, for increased urbanization, and for job-creating growth. Productivity growth in agriculture and off-farm enterprises in the North can supply short-term respite. But in the medium term more jobs off-farm in industry and services, will be needed to absorb the labor force whilst maintaining demand for food products. Otherwise, unless there is an increase in export demand or demand from processing industries, real food prices could decline faster than the rise in farm productivity. These off-farm jobs are most likely to occur in rural towns and especially around Greater Kampala. Uganda could see a more rapid acceleration in the rate of urbanization than in the past, and Government should start to plan how to provide the infrastructure requirements (water, roads, power) for larger urban areas.

Overall Assessment

The Ugandan CEM is of a remarkable quality. It is quite clear from the structure of the CEM's two volumes that considerable effort has gone into making the Ugandan CEM a prototype example of a contemporary World Bank country analysis based on the HRV growth diagnostics approach, and with a modern style of presentation.

Furthermore, even though inclusive growth is not an explicit part of the stated objective of the report, employment generation, as well as both the pace and the path of economic growth are central themes of the analysis in addition to the recommended policy strategies and interventions.

5.1.4. Vietnam

The World Bank has not written a CEM for Vietnam. However, the World Bank office in Vietnam produces an annual report (Vietnam Development Report, VDR) in collaboration with a group of Development Partners and the report is used as input at the annual Consultative Group Meetings in Vietnam. The annual reports are much shorter than the CEMs, consisting of only one volume, and the analyses are often less technical than the CEMs. Nevertheless, the VDRs are important inputs in the development debate in Vietnam and we are inclined to infer that the World Bank must be pleased with the VDRs exactly because no CEM has been produced although the Bank has supported Vietnam since 1993 and IDA is the second largest provider of aid after Japan.

The most recent VDR, from 2012, was written by a World Bank team in collaboration with a 'Donor Working Group' comprising of staff from ADB, AusAID, CIDA, DFID, EU, France, GIZ, Irish Aid, JICA, the Netherlands and the US. The focus of the VDR (2012) is Vietnam's transition from low- to middle-income country; *i.e.*, it is about sustaining inclusive economic growth. This theme is important for Vietnam and the HRV growth diagnostic approach and IGA stand out as obvious frameworks for the analysis. But, somewhat surprisingly, the report does not refer to any of these.

The report has four chapters. Chapter one provides the overall growth trends, while the subsequent three chapters deal with the main constraints: State owned enterprises (Chapter 2), Ineffective public investments (Chapter 3) and public information and transparency (Chapter 4).

Analysis of growth trends

The VDR starts out by a brief non-technical description of Vietnam's remarkable success story. Between 1990 and 2010, Vietnam's economy grew at an annual average rate of 7.3 per cent. The GPD growth was accompanied by high growth of international trade; large-scale inflows of foreign direct investment; a dramatic reduction in poverty; and almost universal access to primary education, health care, and life-sustaining infrastructure such as paved roads, electricity, piped water, and housing. Thus the growth was broad-based and inclusive.

The identification and description of the causes of the economic growth is also almost exclusively verbal, as the only data analysis given is a benchmarking of GDP per capita with the transition economies in Eastern Europe, a traditional growth accounting decomposition and plots of the investment ratio and annual FDI inflows from 2000, onwards. In the description it comes out clearly that the report fully adheres to the "institutions rule" view of growth, albeit the institutional reforms are praised for being bottom-up, gradualist and focused on improving the productive units in the economy.

Constraints Identified

The VDR argues that while Vietnam has addressed the symptoms of its current macroeconomic problems, it has yet to tackle their root causes. These root causes, the most binding constraints, are:

- *Ownership.* Vietnam's state-owned enterprises (SOEs) are one of the least efficient users of capital, but they are its largest owner.
- *Allocation.* The public investment program is becoming increasingly unaffordable and inefficient since allocation is based on administrative considerations rather than strategic needs and market-based mechanisms—creating excess supply in some areas and causing severe shortages in others.
- *Efficiency.* Because of both the widespread use of administrative measures to control prices, and limited access to basic information, Vietnam's economy is being deprived of the "oxygen" that keeps a market economy functioning efficiently.

It is not clear exactly how these constraints are identified from the growth analysis in Chapter 1. This is unfortunate as they do have a somewhat orthodox market fundamentalist flavor that would have benefited from being thoroughly evidence based. Even so chapters 2, 3 and 4 of the VDR each analyze one of the constraints.

In Chapter 2 the state sector (the SOEs) is analyzed and it is concluded, as seen above, that the state sector is inefficient compared to the private sector. However, the analysis supporting the statement is based on an efficiency analyses conducted across industry sectors without correction for sector specific differences in capital intensity and productivity. It is not clear why a proper analysis has not been conducted as the productivity of Vietnamese firms has been analyzed in several scholarly studies (e.g., Newman *et al.*, 2009).

In Chapter 3 the public investment program is analyzed. As for the SOEs in Chapter 2, large parts of the analysis are too simplistic to be regarded as inputs in a thorough diagnostic analysis. An example is the relationship between investment and growth in which there is no breakdown of investment, say, into public and private or equipment and non-equipment investment. Stunningly, empirical evidence for the increasing inefficiency of the public investment program is given by a plot showing an increasing in-

vestment/GDP ratio related to declining GDP growth rates in 2008, 2009 and 2010. Fortunately, the case studies in the chapter are better than the macroeconomic analyses.

In Chapter 4 the importance of transparency is illustrated by references to cross-country regressions, cross regional correlations and opinion survey data. The main arguments for why lack of transparency is a binding constraint on growth is that it fosters corruption and that market participants such as equity investors, exporters, importers, foreign exchange dealers, bondholders, banks, enterprises, and even farmers need information on almost a daily basis to operate in a market economy. This line of argument is convincing even though it is difficult to quantify the effect of transparency reforms.

Reform Recommendations

Each of the three chapters analyzing the constraints also provides a set of reform recommendations whereby the connections between constraints and reforms are clear. In addition, recommendations are typically formulated to be directly implementable.

An example is the recommendations for SOE reforms where the report proposes a framework, referred to as the "DREAM" framework—an acronym for Disclose, Regulate, Equitize, Accountable, and Monitor—that provides a broad range of ideas to address various weaknesses in the current regime governing SOEs. Each of these ideas is augmented by a section describing concrete reform and policy options.

For the public investment program the report proposes four ideas to strengthen the effectiveness of public investment:

(i) Clarifying and strengthening property rights to force competition for land into the market and out of the political arena,
(ii) Creating impartial agencies in key sectors to regulate infrastructure development,
(iii) Creating a mechanism to share revenues among local authorities to encourage development of regional and national infrastructure,
(iv) Strengthening the public investment management cycle.

Finally, for transparency the recommendations are, naturally, to increase the information flow from the government, in particular macroeconomic and fiscal data.

Overall Assessment

The VDR is a tell-tale symptom for why the HRV diagnostic approach and the IGA are needed. Vietnam is in a difficult macroeconomic situation with short-run imbalances and facing the difficult transformation from a low- to a middle-income country. This transformation is to take place at the back of the Great Recession. In addition, inequality has been rising in Vietnam and the impressive poverty reduction may lose momentum as poverty becomes more concentrated in geographic pockets dominated by ethnic minorities. Thus, Vietnam needs a more thorough analysis of the growth prospects, than is provided in the Vietnam Development Report

On the positive side, the policy recommendations in the VDR are clearly related to the alleged constraints and they are actionable.

5.2. Assessment of the Country Assistance Strategy/Country Partnership Strategy Reports

Although the CAS/CPS content teams have considerable flexibility to customize the CAS/CPS to the nature of the World Bank's engagement and specifics of the country there are certain topics a CAS/CPS typically covers. These include: poverty; gender; sociopolitical and institutional factors; macroeconomic framework; debt sustainability; external environment; governance; private sector development, and other cross-cutting issues. Furthermore, since 2005 the organizing framework of a CAS/CPS has built on the results that the bank program expects to contribute to in support of the country's development goals. Hence, the CAS/CPS cannot be expected to have the same focus on growth diagnostics and inclusive growth as the CEM.

In the following we focus on answering the questions:

1. Are previous CEM results reflected in strategy formulations in the CAS/CSP? Especially interesting is whether constraints and reforms identified in the CEM are reflected in the CAS/CSP.
2. Do the CAS/CSP reports include inclusive growth thinking? Specifically, do the macroeconomic framework and poverty discussions refer to productive employment growth?

5.2.1. Ghana

The most recent Country Assistance Strategy for Ghana is dated 31 May 2007, and its publication date is therefore very close to the publication date of the Country Economic Memorandum. As a result, many of the identified constraints in the CEM are fully reflected in the CAS. In 2010 the CAS was supplemented by a CAS progress report, assessing the implementation of the Bank's FY08-11 CAS at mid-term. Both CAS documents are closely linked to the Ghana Poverty Reduction Strategy (GPRS) paper, and it is noticeable that no references are made to the CEM in the 2010 CAS progress report, and none of the CAS documents have any reflections related to growth diagnostics. However, both CAS documents have a strong focus on poverty reduction and agricultural employment generation and productivity.

The CAS was initially aligned with Ghana's Growth and Poverty Strategy, and it basically has three broad objectives:

(i) Sustain economic growth of at least 6 percent per year.
(ii) Surpass the MDG of halving poverty to 26 percent before the end of 2011.
(iii) Start to reduce inequality.

This should be accompanied by improvements in (a) private sector competitiveness, (b) human capital development and (c) governance. The mid-term report states that these objectives remain relevant, but the original lending strategy requires modification due to the significant changes and challenges facing Ghana's economy (due to the oil discoveries etc.). As such the objectives of the CAS and the constraints identified and recommendations made in the CEM are not directly linked.

However, looking at the detailed matrices of the CAS and CEM reveals a considerable overlap between constraints, strategies and policy recommendations. Infrastructure constraints especially in energy, ICT, water and sanitation sectors are mentioned in both the 2007 CAS and the 2010 CAS progress report as a serious obstacles for continued growth and poverty reduction, and the CAS progress report has an evaluation of the developments within the sectors showing impressive progress in ICT and energy sectors especially regarding rural household electrification, whereas the overall transport infrastructure has not yet seen significant improvements. Agriculture productivity is highlighted as another focus area in both reports. Since the publication of the CAS and CEM, the sector has improved access to irrigation (benefitting especially small-holders) and stated goals in terms of crop yields per hectare and improved production has been reached. Investment climate issues are more central in the CEM as compared to the CAS, whereas the CAS (being closely linked to the GPRS) has a more pronounced focus on poverty reduction and inequality. In terms of establishing policies for improving productive employment both reports have an agricultural focus, which naturally links productivity increases to the stated poverty reduction strategy.

By providing a strategy matrix of long-term strategic development goals, the CAS offers relevant objectives to be studied in a future CEM. However, the long-term strategy development goals may be criticized for being too broad to be implementable in a growth diagnostics sense and for not providing a ranking of the main issues and obstacles faced for future sustainable growth and poverty reduction. Moreover, the strategy matrix also lacks focus on employment generation although the sections on modernizing agriculture and education goes some way in addressing issues regarding productive employment and inclusive growth.

Overall, the answers to the two central questions are that (1) the constraints and reforms identified in the CEM are reflected in the CAS, although no direct reference to the CEM is given, and (2) the CAS does reflect inclusive growth thinking, but more focus on productive employment generation is needed.

5.2.2. Mozambique

The most recent Country Partnership Strategy for Mozambique is dated 8 February 2012, and is therefore published relatively close to its Country Economic Memorandum. The CPS and CEM differ from each other both with regards to country descriptive con-

tent as well as in identifying constraints for future development. The differences between the CEM and CPS can be identified already from the country context and development agenda part of the document (Section 1). Where the CEM to some extent share the positive perception of Mozambique's poverty reducing efforts of the previous CPS (for FY 08-11), the most recent CPS is less optimistic about Mozambique's development path. As mentioned, the CEM is silent about the deceleration of poverty reduction between 2002 and 2008. In contrast, the CPS highlights this as the most serious development challenge in Mozambique today (§23).

The growth strategy outlined in the CPS is generally more in line with the most recent poverty reduction strategy paper, which aims to revive the poverty reduction agenda to foster a more inclusive growth path. Diversifying sources of growth is a central part of this strategy, where the focus is on integrating megaprojects with the poverty reduction strategy, as well as boost labor intensive sectors, especially focusing on agricultural job creation and productivity. Although these focus areas are mentioned in the CEM they do not directly form part of the key policy areas to be addressed. On the other hand, the CPS use the analytical work done in the CEM to redefine the most binding constraints for inclusive growth in some sectors (for example §32).

As the CPS takes Mozambique's own vision of its development goals and its strategy for achieving them as a starting point, there is a considerable symmetry between the poverty reduction strategy paper (PARPAII) and the CPS, but the direct links to the CEM are less clear. The CPS provides a structured overview the main objectives and the 17 outcomes that are defined in the CPS (encompassing 30 outcome indicators). The outcomes are defined in three pillars focusing on: (i) Competitiveness and employment, (ii) Vulnerability and resilience and (iii) Governance and public sector capacity. The first category is expected to provide support to the overarching CPS goal of broad-based, inclusive, and pro-poor growth (§73). Nine objectives underpin this goal:

(1) Improved regulatory environment
(2) Improved management of development process through spatial planning
(3) Increased crop yields and overall productivity
(4) Increased employment (especially in agriculture) and growth in the tourism sector
(5) Improved provision and management of road infrastructure
(6) Improved provision of water and sanitation service
(7) Improved access to electricity
(8) Improved access to affordable telecommunications
(9) Better educated, skilled, and healthier workforce

Several projects aimed at fulfilling these goals are described in the CPS (§74-91). However, the CPS document acknowledge that it is difficult to prioritize among these sugges-

tions, as more analytical work is needed to strategically choose and sequence suitable instruments to address sector bottlenecks and constraints.

Regarding the main questions it can be noted that the CPS explicitly mentions the CEM analysis, but the most binding constraints identified in the two documents are not aligned. Further, where the CEM is relatively weak with regards to inclusive growth indicators, the CPS is very clear in aiming at designing a strategy ensuring inclusive growth. The strategy may be criticized for being too broad to be implementable in a growth diagnostics sense and for not providing a ranking of the main issues and obstacles faced for ensuring inclusive growth and poverty reduction. However, the strategy matrix has the necessary focus on employment generation with specific sector strategic recommendations.

5.2.3. Uganda

Being dated April 27, 2010, the latest CAS for Uganda comes three years after the CEM. Nevertheless, there appears to be good agreement between the CEM and the CAS, probably because the analysis and recommendations in the CEM are in line with the Government strategy.

In February 2010, Uganda's Cabinet approved a National Development Plan (NDP) covering FY11-15. The NDP's main theme is Growth, Employment and Socio-Economic Transformation for Prosperity. The plan broadens the country's development strategy from poverty reduction to structural transformation to raise growth and living standards. The CAS is aligned with Uganda's NDP and it will support structural transformation of the economy. The CAS focuses on four strategic objectives and eleven outcomes. The objectives and outcomes are listed below.

(1) *Promote Inclusive and Sustainable Economic Growth.* There are four outcomes: (i) improved conditions for private sector growth; (ii) improved interconnectivity for regional integration; (iii) increased productivity and commercialization of agriculture; and (iv) increased efficiency and sustainability of natural resource management.
(2) *Enhance Public Infrastructure.* There are four outcomes: (i) increased access to electricity; (ii) improved access to and quality of roads; (iii) increased access to and quality of water and sanitation services; and (iv) improved management and delivery of urban services.
(3) *Strengthen Human Capital Development.* There are two outcomes: (i) improved access to and quality of primary and post-primary education; and (ii) strengthened health care delivery.
(4) *Cross-cutting: Improve Good Governance and Value for Money.* There is one outcome: strengthened accountability and efficiency of public financial and human resource management.

The first two and the last strategic objectives are clearly in agreement with the outcome of the growth diagnostic analysis while the third objective is a natural strategy in a broader development agenda.

The CAS also makes clear that the current sector distribution of IDA commitments is in line with the strong emphasis on infrastructure. Finally, the CAS specifies how the Bank has supported and will support the strategic objectives:

- The Bank's analytical and advisory activities (AAAs) underpinned investment operations and sector strategies, and informed the government's reform path.
- The Bank will focus on four outcomes to promote inclusive and sustainable growth.
- The Bank will support Uganda's effort to address its most binding constraint to growth—poor infrastructure.
- The CAS supports higher access to and quality of education and health care to improve human development indicators and enable the transformation of the economy.
- Strengthening value for money is critical for high-quality infrastructure investments and service delivery, and thus for structural transformation.

A detailed Country Assistance Strategy Results Matrix listing the 11 long term strategic development goals and the associated "Major issues and obstacles", "CAS outcomes", "Milestones", and "Bank Group Program" are given in Annex 1 of the CAS.

In conclusion, the Ugandan CAS, like the CEM, is of high quality. There is good agreement between the identified constraints in the CEM and the CAS and both agree on the growth strategies. Inclusive and sustainable growth is explicitly a core theme of the strategy and the CAS specifies precise Bank group programs, both for sector distribution of commitments and for the Bank's AAA to support the strategic objectives.

5.2.4. Vietnam

The CPS for Vietnam is dated November 7, 2011; this makes it the first CPS since Vietnam became a lower middle-income country in 2009. As the Bank has not written a CEM for Vietnam it follows that the policy strategies in the CPS cannot be related to a CEM but some coherence with the Vietnam Development Report 2012 should be expected as the two reports must have been written simultaneously.

The description of the recent economic trends as well as the current situation and the medium term prospects are dealt with in an old fashioned way compared to the detailed suggestions following the HRV approach. The CPS initially focuses on the recent macroeconomic instability; starting in the second half of 2010 following what the CPS denotes "delayed withdrawal of the fiscal and monetary stimulus measures introduced to deal with the impact of the global financial crisis." In the slightly more detailed description of the recent past (2008-2010) and the medium term prospects (2011-2015) it is stressed

that stabilizing the economy is crucial to Vietnam's medium-term growth prospects that otherwise remain strong. The data accompanying the description of the medium term prospects are scarce as they do not provide any decomposition of the economic growth, neither in terms of sectors, expenditure components, nor input factors. Furthermore, employment is only described by the urban unemployment rate and the BOP is only described in terms of the aggregate flows.

Following the short description of the macroeconomic situation and prospects, the CPS moves to the broader development agenda and describes five key challenges that need to be addressed over the next five years. These include economic competitiveness, sustainability of growth, pockets of persistent poverty and rising inequality, vulnerability and governance.

The section on economic competitiveness digs a little deeper into some of the causes of Vietnam's impressive growth performance in the past and in accordance with the VDR 2012 it points towards the large SOE sector as a growing source of inefficiency, weak competitiveness, and a constraint to private enterprise development. It is also stated that the quality of Vietnam's infrastructure is low, and skilled labor is generally in short supply. It is not clear to what extent these challenges are constraining growth, though.

The section on governance does directly mention that weaknesses in institutional capacity and public sector management continue to constrain Vietnam's development. (Institutional capacity and reforms was the central theme of the Vietnam Development Report 2010—*Modern Institutions*). Further, institutional constraints on inclusive development are identified indirectly in the CPS by the note that improvements in basic public service delivery and access are especially needed for Vietnam's poor, vulnerable, or otherwise disadvantaged people.

The section on poverty highlights the impressive poverty reduction in Vietnam from 1993, onwards. However, it is also stressed that a renewed effort is necessary to promote equality in outcomes for all, and to close wide and growing attainment and learning gaps between the poor and non-poor and between ethnic minorities and the Kinh majority. Specifically, a more results-oriented education system can equip workers with the skills to take advantage of the new opportunities and manage the employment risks that come with a changing labor market, while social and health insurance can help to shield people better from the worst shocks impacting employment. As such, aspects of inclusive growth; structural change and employment considerations, are included in the poverty section.

The Vietnamese Government's development vision for the next decade is laid out in its Socio-Economic Development Strategy (SEDS) 2011-2020. The SEDS gives attention to structural reforms, environmental sustainability, social equity, and emerging issues of macroeconomic stability. It defines three "breakthrough areas":

(i) Promoting human resources/skills development (particularly skills for modern industry and innovation);
(ii) Improving market institutions;
(iii) Infrastructure development.

The overall goal is for Vietnam to lay the foundations for a modern, industrialized society by 2020. The SEDP 2011-2015, approved by the new National Assembly in November 2011, elaborates the objectives of the SEDS and identifies the specific measures and resources that are needed for its implementation.

In conclusion, there is good alignment between the VDR 2012 and the CPS, but the quality of the growth analysis in both reports could be improved by applying the HRV/IGA framework. Still, by supporting the Vietnamese Government's development vision, facets of inclusive growth are present in the CAS.

6. Conclusion and Recommendation

Conclusion

While it is difficult to generalize from four cases, we think the following four points are worth emphasizing:

1. The analytical quality of the reports varies too much. The best report use a variety of analytical tools, including a HRV approach, and they make clear, sensible and realistic recommendations for future action. The Uganda CEM may possibly be used as a benchmark for "best practice" in terms of analytical approach.

2. The HRV growth diagnostic methodology clearly helped underpin the importance of understanding individual country economic mechanisms. The results and recommendations made thereby stand out as being more convincing, which may help in policy dialogues between governments and donors. Promoting a HRV growth diagnostic and inclusive growth analysis as part of the World Bank Policy Analytical and Advisory Assistance toolbox is therefore recommendable.

3. By combining different methodological approaches an important contribution of the CEMs will also be the provision of a consistent framework demonstrating the fiscal; balance of payments, and debt sustainability consequences of particular growth strategies. This illustrates that following a HRV diagnostic approach is important but it should be incorporated alongside the more traditional macroeconomic analytical tools (benchmarking exercises, growth accounting analysis, fiscal framework studies, etc.).

4. None of the reports use the full inclusive growth analysis as the methodological framework. Thus, inclusive growth analysis has only influenced IDA indirectly in its analytical work. However, elements of the inclusive growth analysis are present in seven

out of eight reports. Therefore, the inclusive growth analysis should be suggested as an organizing framework, not as a rethinking of World Bank analytic work.

Recommendation

Based on the findings in this desk study we believe the inclusive growth thinking in IDA should be strengthened. To this end we offer the following recommendation for consideration:

The World Bank should aim at producing a Country Economic Memorandum for each IDA country

- The CEM should aim at applying a standardized analytical framework, at least as a supplement to the more country specific methodological approaches
- The CEM should be focused on inclusive growth analysis.
- The CEM should be produced at regular intervals, say every 4-5 years.
- The CEM should have clear, actionable recommendations for policies and reforms.

Below we briefly argue for this recommendation.

The analytical methodology should be standardized across countries

As highlighted in a recent World Bank performance assessment review the HRV approach has brought into focus the need to be more selective of policy areas that need attention from a growth perspective. However, the same World Bank performance assessment concludes that countries should have the freedom to identify the growth framework that provides the most analytic and pedagogical vale in the country context. As such, there should be no mandating of particular approaches. We tend to disagree.

Deciding on a common analytical framework (benchmarking, growth accounting, HRV diagnostics approach and a fiscal framework study) will ensure a minimum threshold of technical quality. Moreover, using these analytical tools probably has the highest likelihood of leading to identification of the most binding constraints, which in turn could be analyzed more in depth in a supplement volume to the CEM. This would improve the way the analytic work can feed into directly implementable recommendations and interventions..

A more widespread use of a standardized analytical framework will overtime improve the analytical capacity of countries and it will also facilitate benchmarking of the identified constraints dimension across countries, complementing the current benchmarking exercises that are mainly comparisons of countries with similar resource endowments.

In general, analytical work identifying binding constraints is naturally confined to analyzing areas where information is available. Unfortunately, this may lead to a situation where identified constraints may not be the most binding, but just the area/sector where data was of sufficiently high quality. Clearly, a standardization of the analytical

framework will increase the demand for appropriate data. This demand should be encouraged even if individual countries and organizations may oppose it in the short run because it will require support and resources for additional data collection and capacity building of national statistical offices. By standardizing the analytical framework and the data requirements the data selection problem will be reduced over time.

The CEM should be focused on inclusive growth analysis

Currently CEMs differ significantly in comprehensiveness, depth and analytical detail. However, the selected reports all cover considerable ground and they are very comprehensive, rather than focusing on economic growth. By focusing on the growth mechanisms and constraints, the CEMs would be improved by concentrating the analysis to the macro economy and specific sectors of direct relevance to inclusive growth and constraints identification. Moreover, currently the sector chapters are rarely well-integrated into the core chapters of the CEMs and they tend to be very extensive, purely descriptive pieces. As such, they may be considered to be of limited value because the contents are only known to a very limited group of specialists. As highlighted in the recent World Bank performance assessment review the comprehensiveness and detail is a major part of the problem of cost and time overruns of CEMs. So by standardizing the analytical framework and focusing the aim of the CEMs will lead to a more timely use of the analytical work.

The CEM should be produced at regular intervals, say every 4-5 years

While the CEM, being a comprehensive analytical document, is important for the Bank's analytical and advisory assistance, the CAS/CPS is an important document for IDA lending. Unfortunately, there has been limited emphasis on timely production of the CEM. Therefore, it is difficult to find coherence between the CEM and the CAS. In several cases policy strategies in the CAS/CPS do not include results and recommendations from the CEM, even in cases where the CEM predates the CAS/CPS. By standardizing the analytical framework and data collection efforts and by focusing the analysis on inclusive growth, the CEMs should become more suitable tools for informing the CAS/CPS. However, for this to be the rule, the CEMs must be produced regularly. Producing regular reports would in all likelihood also lessen the resources needed for each individual report as much of the data gathering and analytical work would over time become incremental.

The CEM should have clear, actionable recommendations for policies and reforms

The growth diagnostic approach grew out of dissatisfaction with the simple minded policy advice in the 1990s. Therefore, the ultimate success of a growth diagnosis is not analytic rigor, although this is necessary, but identification of a few binding constraints and relevant and actionable recommendations for removing the constraints. This is also a natural requirement if the CEM is to inform policy makers, national as well as in the Bank and the international donor community.

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Table 2: The categories and criteria used for assessing the CEM/CAS reports

			Ghana	Mozambique	Uganda	Vietnam
Objectives						
	Are the objectives of the reports clearly defined up-front?		YES	YES	YES	YES
	Do the objectives include considerations about inclusive growth;	Productive employment	YES	NO	YES	NO
		Income generation	YES	NO	YES	NO
		Poverty reduction	YES	NO	YES	NO
	Are the objectives measurable and measured	Measurable	YES	YES	YES	YES
		Measured	YES	YES	YES	NO
Quality						
	Are the reports of good technical quality?		YES	NO	YES	NO
	Do the reports make use of analytic frameworks or models?	Growth diagnostics	NO	NO	YES	NO
		Benchmarking	YES	YES	YES	YES
		Disaggregated analyses	YES	YES	YES	NO
		Sector dynamics analyses	YES	NO	YES	NO
		CGE models	YES	NO	YES	NO
	Do the reports include analyses of employment and income generation?	Employment	YES	NO	YES	NO
		Income generation	YES	NO	YES	NO
	Do the reports include analyses of demographic trends and migration?	Demographic trends	YES	NO	YES	NO
		Migration	NO	NO	YES	NO
	Are the data analyses relevant and well crafted?		YES	NO	YES	NO
	Report gives recommendations in a clear and actionable way?		NO	NO	YES	YES
	Recommendations include policies for increased productive employment?		NO	NO	NO	NO
Coherence and Relevance						
	Are the policy strategies in the CAS (or CPS) based on the analysis and recommendations in the CEM when the latter predates the former?		NO	NO	YES	..
	Do the reports give a coherent description of recent economic trends?		YES	YES	YES	YES
	Do the reports give a consistent analysis of the current situation?		YES	YES	YES	YES
	Do the reports include a well-argued and documented outlook leading to sensible and realistic recommendations?		YES	YES	YES	NO