

**The Social Costs of Adjustment:  
The Case of Morocco**

by

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Submitted to the Department of Urban Studies and Planning  
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### **Abstract**

This thesis explores the social implications as well as impact of the Moroccan World Bank-supported adjustment program. It determines which social groups are affected by the different measures included in the program; which policy reforms have the most deleterious effects on the poor; and what measures can be taken to alleviate these costs.

There has been increasing awareness that adjustment is proving to be a longer and more complicated process than originally expected, and that consequently, the social costs of adjustment extend beyond the short-run. It is therefore recognized that the poor need to be protected from the negative impact of austerity measures such as demand restraint and cuts in government spending, as even if growth is revived, the poor will only benefit to the limited extent that trickle-down occurs.

Hence, adjustment programs need to be redesigned to protect the poor's welfare and standard of living. Several recommendations are suggested. In the mainstream, these include improving the efficiency in resource allocation by better targeting scarce resources towards those most in need. In addition, in the spirit of "redistribution with growth", increasing the access of the poor to productive assets (such as land and credit), as well as to education and health services, is advocated so as to encourage the poor's participation in the adjustment process.

Less "orthodox" recommendations to protect the poor focus on improving the design and implementation of the adjustment program. Structuralists support a more gradual adjustment process;

less emphasis on contractionary policies; and a lower degree of liberalization in trade and industry, and the agriculture sector, as well as in financial markets. Moreover, they underscore the need for compensatory programs for the poor, and the need for additional external financing. Finally, structuralists recommend that the programs be redesigned to more adequately reflect institutional settings and the circumstances of the country in question; in this case Morocco.

In brief, “listening to the people”, as well as drawing them into the growth process is advocated as a means of ensuring the viability of the program and the welfare of the poor. Such policies to mitigate the social costs of adjustment are feasible without undermining the objectives of adjustment. Adjustment programs can and should promote social development and economic adjustment simultaneously. Without these dual objectives, the sustainability of the programs becomes questionable.

Thesis Supervisor: Lance Taylor  
Title: Professor of Economics

## **To my parents**

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## Table of Contents

Introduction .....	6
Chapter I. Background .....	8
A. The Political Setting .....	8
B. The Economy .....	9
C. Poverty and the Welfare Problem .....	10
1. Identification of the Problem .....	10
2. The Causes of Poverty .....	13
2.1 Theoretical and Empirical Findings	
2.2 Characteristics of the Poor	
The Poor	
The Ultra Poor	
Chapter II. The Social Impact of Structural Adjustment:	
Emphasis on the Poor .....	22
A. The Structural Adjustment Program .....	22
B. The Costs of Adjustment .....	23
1. Transitional and Long-Term Costs .....	24
2. Structural Adjustment and the Distribution of Income .....	26
2.1 Distributional Effects of Trade Policy Reforms	
2.2 Distributional Effects of Tax Adjustments	
2.3 Distributional Effects of Agricultural Pricing Policies	
2.4 Distributional Effects of the Provision of Social Services	
2.5 Distributional Effects of Monetary and Fiscal Policies	
2.6 Distributional Effects of Adjustment in Wages and	
Administered Prices	
Chapter III. Policy Reformation and Recommendations .....	61
A. Overview .....	61
B. A More Desirable Distribution of Income? .....	62
C. Orthodox Recommendations for Protecting the Poor .....	66
1. Improving Access to Productive Assets .....	69
2. Raising the Returns on Assets .....	70
3. Improving Employment Opportunities .....	71
4. Ensuring Access to Education and Health Services .....	73
5. Supplementing the Resources of the Poor with Transfers .....	75
D. The Heterodox Approach .....	78
Chapter IV. Conclusions .....	84
Bibliography .....	87

## **Introduction**

Recently, there has been growing controversy surrounding the impact of adjustment programs on social welfare. This thesis focuses on the Moroccan adjustment program which provides evidence of a deterioration in social conditions. The controversy arises because despite available evidence, orthodox economists argue that it is difficult to isolate adjustment as the sole cause of deteriorating social conditions, and that the failure to adjust may prove even more costly to the poor.

The main argument is that adjustment and improved standards of living need not be mutually exclusive, rather that policies to mitigate the costs borne by the poor can be integrated in the adjustment program without undermining its objectives. Indeed, protecting the poor's welfare from the negative impact of austerity measures ensures the sustainability of the program. Hence, social development can, and should be promoted simultaneously with economic adjustment.

The thesis is organized as follows: Chapter I presents the political, economic and social characteristics of Morocco. Chapter II first briefly describes the World Bank-supported structural adjustment program that Morocco embarked on in 1983. It then reviews the theoretical implications for the poor of the policy measures included in the program from both the neoclassical and the structuralist perspectives; this is followed by an exploration of the actual social impact on the poor. Chapter III reviews "orthodox" as

well as "heterodox" recommendations to safeguard the interests of the poor during the program as well as in the longer-run, and determines to what extent these are reflected in the design of the Bank-supported program. Finally, chapter IV presents lessons - that the assessment of the Moroccan experience has provided - for improving the design of the Moroccan program, as well as that of future adjustment programs.

## **Chapter I. Background**

### **A. The Political Setting**

Morocco gained political independence from France and Spain in 1956, after a colonial rule that lasted 44 years, the shortest such period in North Africa. The new state is a kingdom, ruled by the Alawi dynasty.

Since 1975, Morocco has been engaged in a difficult and expensive desert war against the Western Saharan nationalist movement, the Polisario Front, which has received support from Algeria. By 1985, Morocco had control over four fifth of the area of the Western Sahara, and in 1988, though important differences persist, progress was made in reaching a settlement of the Sahara question.

Today, the role of the monarchy may not be questioned. However, social inequality and official corruption within the country's traditional and patrimonial system contribute to a feeling of growing discontent among the population. Given that power is centralized in the monarchy, political parties and unions have little influence in their own right. Opportunity for a more equitable distribution of the nation's wealth is limited, as influence is based on personal relationships, and access to resources is largely determined by family or political connections. The population's growing discontent has been further exacerbated by severe economic problems and the costs of the war in the Sahara, and resulted in two serious outbreaks of urban unrest and violence in the first half of the decade.



## B. The Economy

With a GNP per capita of 590 (1986 US Dollars), Morocco ranks among the lower middle-income (LMI) countries.

Morocco's economy has an important agricultural sector, which although amounting to only 21% of GDP, provides employment for 41% of the estimated 5.7 mn labor force (according to 1985 statistics). The second largest sector is services which is dominated by commerce and employs 35% of the labor force. There is also a relatively diversified manufacturing sector which constitutes 17% of GDP, and a mining sector dominated by phosphates and which amounts to 7% of GDP.

Phosphates are Morocco's leading exports, followed by agricultural produce, particularly citrus fruits. However, Morocco has not reached agricultural self-sufficiency (this is in part the result of the severe droughts of the early 1980s) and is dependent on oil imports. This dependency has translated into heavy food and energy import costs, which in turn have produced a structural deficit in merchandise trade. The deficit has been in part offset by tourism and workers' remittances which are equal in weight to phosphates revenues, although recently there has been worrying evidence of a declining trend in worker's remittances. Moreover, due to a growing foreign debt burden, the economy has suffered successive current account deficits in recent years.

Starting from a low debt position in 1974, Morocco became by 1985 one of the most highly indebted countries in the world with an

external debt of \$12 billion, three times the export revenues, and a debt ratio of 70% before rescheduling. These figures are largely attributable to the government deficit.

Morocco has a mixed economy, and apart from a short lived Moroccanization (majority domestic shareholding in all businesses), economic policy has been essentially liberal, its support base being the traditional bourgeoisie which has long established interests in trade and services, and foreign economic interests which the government attempted to maintain following independence.

Since 1983, the economy has been undergoing substantial reforms as part of a World Bank-supported adjustment program designed to enable the country to cope with its balance of payments crisis. More recently, an agreement was reached on the terms for economic unity and cooperation among North African countries or the Greater Maghreb. This will allow Morocco to diversify its export markets in anticipation of the approaching 1992 deadline for an integrated European market which presently absorbs 60% of its exports, particularly agricultural.

## C. Poverty and the Social Welfare Problem<sup>(1)</sup>

### 1. Identification of the Problem

Despite a significant reduction of poverty over the last 20 years, Morocco's current poverty rate of 30% is still relatively high

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(1) This section of the chapter makes extensive use of the World Bank Social Sector Strategy for Morocco (1988).

by international standards. With 30% of its population below the poverty line (according to World Bank definitions), Morocco counts 6.6 million of the world's poor.

Although a satisfactory rate of growth has been achieved in recent years, economic progress has failed to reach large sections of the population as evidenced by the unfavorable levels of social indicators such as child death rate, infant mortality, and the illiteracy rate (Table 1). On the other hand, other social indicators such as gross primary and secondary school enrollments, and the crude death rate per thousand have marked significant gains (Table 2), reflecting the high level of GDP (10%) that was devoted to the implementation of social policies over the past two decades.

Despite these social achievements, Morocco's social indicators still compare poorly to the averages of other lower middle-income countries (Table 1), and even trail behind the indicators of countries with lower per capita income such as the Philippines, Indonesia, and Sri Lanka (Table 3). Moreover, these national averages understate the magnitude of the poverty problem for the rural population, the poor, and women for whom social conditions tend to be worse. For instance, the infant and child death rate are higher in rural than in urban areas, as is population per physician. And, education levels (and therefore literacy) are considerably lower among women and the absolute poor (those living below minimum requirements of food and shelter). (Table 2)

A distinction is necessary between the poor and the ultra-poor who consume less than 75%-80% of the minimum nutritional

requirements; and within these two categories, different absolute poverty measures are defined for urban and rural areas, in recognition of the differences in rural and urban dietary and other consumption habits, and consumer prices. (Table 4)

Preliminary analysis shows that the incidence of absolute poverty in the population declined during the 1970–1985 period from 38% to 29% in urban areas and from 45% to 30% in rural areas. On an aggregate level, the percentage of the population below the poverty threshold declined from 41.5% in 1970 to 29.5% in 1985. However, the absolute number of poor increased slightly from 6,500,000 in 1980 to 6,600,000 in 1985. Table 5 indicates that in 1985, 16% of the total population were ultra poor (18% of the urban population and 14% of the rural population). This translates to 1,830,000 people in urban areas and 1,730,000 in rural areas (WB, 1988: 2).

The evolution of income distribution is another indication of whether there have been reductions in poverty through the benefits of the rapid development of the 1970s and early 1980s and through greater equity. In 1985 the distribution of expenditures was uneven with greater inequality in urban areas where the Gini coefficient is 0.41 as opposed to 0.37 in rural areas. It is hence fair to conclude that little reduction in inequality has been achieved over the fifteen-year period 1970-1985.

Despite rapid economic development in the 1970s and early 1980s, poverty alleviation and reduction has not been remarkable.

This is an important consideration, not only for humanitarian reasons, but also for the long-term economic growth of Morocco.

Although the effort for the reduction of poverty may absorb resources valuable for the short-run growth of the economy, such an effort may strengthen the long-run resource base of the economy. First poverty reduction would expand and improve the human capital basis of the Moroccan economy; second it would increase the national income; third it would decrease government expenditures on nutrition, health care, and other welfare programs (although, as will be shown later, government expenditure on social services are already too low); and fourth it would decrease fertility and the population growth rate, allowing for faster growth of per capital income.

## 2. Causes of Poverty

### 2.1 Theoretical and Empirical Findings

Theoretical and empirical findings in developing countries indicate that poverty is due to, inter alia, joblessness, low productivity, and low wages. These in turn have been found to be connected in the case of the poor with three major factors: One is the low human capital development, i.e. lack of education, literacy, and vocational skills because of large household size and high fertility rate, but mostly because of demand factors such as the opportunity cost of sending children to school, as well as, on the supply side, the inadequate provision of social services. The low human capital development is also the result of inadequate nutrition

and a poor health status, again the reflection of inadequate supply of social services or lack of accessibility to health facilities.

A second factor is the limited access to productive inputs such as credit, capital, and technology, and the third factor is the specific sectoral and labor market dynamics of the economy, such as slow job creation, low quality of new jobs, and rapid labor force growth.

Research also indicates that poverty in developing countries is equally related to large household size; lack of productive assets, particularly land; and ownership of unproductive assets.

## 2.2 Characteristics of the Poor and Ultra-poor in Morocco

### The Poor

The poor are almost equally distributed in rural and urban areas, as indicated by the small variation of per capita expenditure across regions. Hence poverty in Morocco, unlike most other low middle-income countries, is not simply a rural phenomenon (Table 5). Most of the households in Morocco are large, consisting of more than 4 persons. In 1985, 72% of the poor households in rural areas and 76% in urban areas comprised 5 or more persons, and 31% and 25% of poor households in urban and rural areas respectively had more than 9 persons. The overwhelming majority of the poor household heads: 82% was over 35 in 1985, of which 44% were between 35 and 60 years old, and 38% were 60 years old and over. This age composition is almost the same in both urban and rural areas.

Again, the overwhelming majority of the poor-household heads: 85% and 87% in urban and rural areas respectively, had no education according to a 1985 survey, with low enrollment of poor children due to the demand and supply factors mentioned earlier. These statistics confirm the causal relationship between low human capital development and poverty.

In terms of occupational profiles, the 1985 consumption survey indicates that 39% of the poor household heads in rural areas were farmers, 17% agricultural workers, around 10% non-agricultural workers, and 21% were inactive (not looking for a job); 56% of the rural poor were therefore heavily dependent on agriculture. In urban areas, poverty was spread among a number of socio-economic groups: merchants counted 13%, service and office employees 21%, non-agricultural workers 20%, and 23% were inactive. "The inactivity reflects, in most cases, inability to supply labor and ultra-poverty status." (WB, 1988:4)

The available data regarding asset ownership of poor households are incomplete. However, research undertaken by Ennaji (1986), as well as research in other countries has indicated that poverty is connected to lack of productive assets or the ownership of unproductive assets, such as small farms with inferior land quality. Ennaji writes:

In North Africa, Morocco can be taken as an example to illustrate the problem of farmers without land. He adds: The economic difficulties of most farmers lie in this new social framework: the land is owned by a minority, and the high population growth rate has increased the

imbalance between available resources and the needs of the population. (Ennaji, 1986: 42)

Ennaji explains that since most of the rural poor no longer possess sufficient means of production, they are driven to sell their labor for a subsistence wage in several economic sectors, engaging in such activities as gathering, handicrafts, and petty trade. Hence, few are left to work on the farm. Women sometimes leave the home in search of paid work, children are taken out of school to do odd jobs and seek work elsewhere when they reach adulthood; thus the family breaks up. “The changing rural world has completely disrupted the living conditions of the poorest members of the community” (Ennaji, 1986: 42).

Moreover, the breaking down of traditional institutions has not as yet been replaced by new structures such as government services and local authorities. This is confirmed by the World Bank social sector strategy for Morocco which states:

Municipal and provincial governments spend only limited funds on social service provision. The private sector’s participation in the provision of basic social services, such as health and education, especially for lower income groups, is also minimal. This suggests that at present the key policy variables regarding the provision of social services in Morocco (in the domain of education, health, professional training and youth services) is the central government social spending. (WB, 1988: 5)

However, indicators clearly show that the magnitude of public spending on social programs does not match the basic needs of poor households. Hence inefficient and/or inequitable social services provision can be considered another significant contributor to the



poverty situation in Morocco. The magnitude and trends in government social spending will be reviewed in greater detail in Chapter II.

A final characteristic of the poor, their health status is where the most difference is apparent between the rural and urban areas. Conditions of relatively high maternal mortality rate, child death rate, infant mortality rate and low life expectancy continue to persist, and they are worse for the rural poor.

#### The Ultra-Poor

There is little information regarding the characteristics of the ultra-poor in Morocco. In general, ultra-poor households are very large with over seven members, have higher child/adult ratios, higher female/male ratios than the rest of the population, and expenditure per person falls below the ultra-poverty threshold. The group mostly consists of women and the elderly. Its general economic characteristics are: lack of ownership of productive assets, or the ownership of land which is fragmented and remote. Many of the ultra-poor are casual adult laborers; urban and female ultra-poor exhibit higher employment rates; and female ultra-poor feature sharply lower participation rates in towns than in rural areas. (WB, 1988:5)

**Table 1**  
**Comparison of Morocco's Most Recent\* Social Indicators**  
**with the Averages for Lower Middle Income (LMI) Countries**

Social Indicators	Morocco	LMI Average
<i><b>POSITIVE</b></i>		
GDP Growth Rate (percent)	3.3	1.8
Life Expectancy at Birth (years)	59	58
Birth Rate (per thousand)	33	35
Crude Death Rate (per thousand)	10	10
Calorie Supply (per capita)	2,729	2,511
<i><b>NEGATIVE</b></i>		
GNP Per Capita (dollars)	590	750
Infant Mortality Rate	90	77
Child Death Rate (per thousand)	52	11
Population Per Physician (per thousand)	18.6	7.9
Gross Primary School Enrollment (percent)	72	104
Male	87	111
Female	58	100
Gross Secondary School Enrollment (percent)	31	42
Male	38	50
Female	25	41
Overall Adult Illiteracy Rate (percent)	60	NA
Male	40	NA
Female	80	NA
Moderately Malnourished Children (percent)	40	NA

Sources: The World Bank, 1988. World Development Report, 1988.  
Washington, D.C.: The World Bank UNESCO, 1988.  
The State of the World's Children, 1988. Oxford University Press.  
In Morocco: Social Sector Strategy (WB, 1988).

Note: \*Time of references varies by indicator and represents most recent information. Year of reference for any indicator is 1981, 1985, or 1986.

**Table 2**  
**Trends in Morocco's Social Indicators**

Social Indicators	1965	1973	Most Recent*
GNP Per Capita (dollars)	220	446.6	620
Life Expectancy at Birth (years)	49	53	59
Birth Rate (per thousand)	49	44	33
Crude Death Rate (per thousand)	18	15	10
Infant Mortality Rate (per thousand)	145	120	90
Child Death Rate (per thousand)	32	48	52
Population per Physician (thousands)	12.1	13.1	18.6
Gross Primary School Enrollment (percentage)	57	62	72
Male	78	78	87
Female	35	45	58
Gross Secondary School Enrollment (percentage)	11	16	31
Male	16	21	38
Female	5	12	25

Sources: The World Bank, 1987. *Social Indicators of Development*, Washington, D.C.  
The World Development Report, 1988. Washington, D.C.: The World Bank, 1988.  
*World Development Report, 1988*. Washington, D.C.: The World Bank.  
In Morocco: Social Sector Strategy (WB, 1988).

Note: \*Time of references varies by indicator and represents most recent information.  
Year of reference for any indicator is 1981, 1985, or 1986.

**Table 3**  
**Morocco: Basic Indicators**  
**Comparison with Countries with Lower Per Capita Income**

	GNP per Capita ('86US dollars)	Pop. Growth Rate 1980-1986	Gini Coefficient		Unemployment		Infant Mort. Rate (per 1000 births) 1986	Life Exp. 1986	Child Death Rate 1986	Primary School Enrol. (% of age group) 1985	Matern. Mort. (per 100,000 live births) 1980
			Coeff.	Year	Rate	Year					
MOROCCO	590	2.5	0.41	1985	10.72	1982	90	59	52	81	327
PHILIPPINES	560	2.5	0.52	1983	5.3	1981	46	63	4	106	80
YEMEN, ARAB REP.	550	2.5	0.36	1986	12.5	1986	152	45	34	67	n/a
INDONESIA	490	2.2	n/a	n/a	n/a	n/a	87	56	12	118	800
YEMEN, PDR	470	3.1	n/a	n/a	n/a	n/a	142	46	30	66	100
SRI LANKA	400	1.5	0.52	1982	11.7	1982	29	70	2	103	90

Source: The World Bank. 1988. World Development Report, 1988. Washington, D.C.: The World Bank.  
 In Morocco: Social Sector Strategy (WB, 1988).

**Table 4**  
**Absolute Poverty and Ultra-Poverty Threshold**  
(in 1985 dirhams)

		Ultra-Poverty Threshold		Poverty Threshold	
		<i>Urban</i>	<i>Rural</i>	<i>Urban</i>	<i>Rural</i>
1	Food Expenditures	1,246	1,004	1,555	1,264
2	Non-Food Expenditures	762	278	954	349
3	Absolute Poverty Line per person/year	2,008	1,453	2,509	1,613

Source: Bank staff calculations based on the 1970 and 1985 Household Consumption Surveys.  
In Morocco: Social Sector Strategy (WB, 1988).

**Table 5**  
**Socioeconomic Characteristics of Major Poverty Groups**

	Geographic Composition of the Population %	Geographic Distribution %		GINI	Major Poverty Group
		Poor	Ultra-Poor		
Urban	43%	29%	18%	0.41	Unemployed and workers in informal sector
Rural	57%	30%	14%	0.37	Landless farm workers
TOTAL	100%	29.50%	16%	—	—

Source: Morocco: Social Sector Strategy (WB, 1988).

## **Chapter II. Social Impact of Structural Adjustment: Emphasis on the Poor**

### **A. The Structural Adjustment Program**

The economic turbulence of the late 1970s and early 1980s has translated into a loss of a decade or more of economic progress for most of the developing world.

In Morocco, the past decade has been characterized by urban drift (a decade long drought having gradually driven thousands of poverty-stricken farmers from rural areas to urban slums); rising protective barriers in industrial economies; sluggish industrial development in a country that is oil-poor; low prices of phosphates on the depressed world market; and serious agricultural failings. The result has been an alarming growth in foreign indebtedness, sharply reduced investment in development projects, and increasingly widespread poverty.

In 1983, after Morocco's access to international markets was sharply reduced, a new government was appointed to confront the economic crisis. Under the advice of the International Monetary Fund and the World Bank, the government designed a program with dual objectives: (1) to stabilize the economy in the short-term by reducing aggregate demand and the size of the government budget deficit; and (2) to enhance the efficiency of the economy in the production of goods and services by reforming the underlying structure of key economic and social sectors.

This thesis will concentrate on the structural adjustment program (SAP), although stabilization and adjustment complement one another and are therefore strongly correlated.

The SAP has been supported by a series of IMF stand-by arrangements (for the rescheduling of official and commercial debts) and sectoral adjustment loans. Structural reforms were initiated in the trade and industrial sector, and in the agricultural sector. Other sectoral adjustment operations have involved education and the health sector. In addition, restrictive fiscal and monetary policies were imposed to eliminate the imbalance between aggregate domestic demand and resource availability. These reforms have entailed cuts in public investment programs; reduction in consumer subsidies; and credit restraint. The social implications of these measures are reviewed in this chapter.

#### B. The Costs of Adjustment

Today, for most countries in Africa and Latin America, "adjustment policy is the dominating economic preoccupation for setting the frame and constraints within which all other economic and development issues have to be considered" (Cornia et. al.,1987: 5).

However, against a background of severe deterioration in social and economic conditions, questions have been raised about the impact of adjustment programs on the poor, and about the ability of governments and international agencies to protect the poor in the process of adjustment

The consequences of adjustment for the poorest of the poor have been of growing interest in recent years. The implications for

poverty are controversial; they will be examined throughout the chapter.

Before presenting an analysis of the relationship between structural adjustment and the distribution of income, it is useful to outline the main features affecting distributional patterns in LDCs. Briefly, these are: (1) technological and institutional dualism; (2) limited access of lower-income groups to complementary assets; and (3) differences in socio-economic behavior, especially with respect to savings and fertility rates (Chenery et al., 1974: 210).

In addition, an interdependence exists between growth in one socio-economic group and another. Linkages exist between the different income groups, and those ensure that the growth of income in one group is not simply a function of capital accumulation in that group but also a function of growth of production and income in other groups. Hence, the determinants of the distribution of income cannot be separated from the determinants of growth in the economy (Chenery et al., 1974: 218).

### 1. Transitional and Longer-Term Costs

In their attempts to assist the poor under structural adjustment, policy makers have not been able to rely on theoretical or applied economics. "Economic theory has neglected the tradeoff between macroeconomic balances and distributional balance." (Demery and Addison, 1987: 1). Most analyses have fallen short of emphasizing the tradeoff in that they have failed to point out the



unavoidability of transitional costs, as well as the strong likelihood of longer-term costs being incurred.

A distinction must be made between transitional and long-term costs or what Corden (1988) calls primary adjustment costs and secondary adjustment costs.

Transitional costs are of three types (Huang and Nicholas, 1987a: 4). First, the effort to restore macroeconomic balance between aggregate demand and aggregate supply usually depresses output, employment and consumption. These costs are typical of a recession. Second, the changes in the structure of incentives stimulate the reallocation of resources and hence benefits between sectors and activities. Consequently, the groups that previously benefited from subsidies and other forms of protection from market forces will suffer substantial declines in income and wealth, while those in stimulated activities benefit. Third, transitional costs are also incurred when lags and difficulties in moving productive resources into alternative uses, in response to change in relative prices arise.

As for long-term costs, these result from prolonged unemployment and output losses that may be caused by failure to devalue sufficiently, by real wage resistance, or by inappropriate use of import restrictions. These factors reflect inefficiency in adjustment and result in the economy operating below capacity. Hence the poorest segments of society may not benefit from the adjustment process. With adjustment proving to be a longer and more arduous effort than originally expected, the benefits of growth

are less certain. They take longer to materialize, and reach the poor only to the limited extent that trickle down occurs. The relationship between adjustment and poverty therefore extends beyond a notion of social cost that features only short-term effects. (Demery and Addison, 1987: 1)

## 2. Structural Adjustment and the Distribution of Income

Economists know very little about distributional consequences of these policies in developing countries. Dethier, given the importance of the topic, calls this a “scandalous omission” (1986: 19). The answer is not easy to arrive at because social costs are often indistinguishable from the external factors that necessitated the adjustment as well as internal factors such as social deprivation that arise from the extensive poverty of the country in question.

In assessing the social costs of adjustment programs, the focus is on the welfare of the poor. That segment of society is defined as the poorest 30 to 40 percent of the population in per capita income or consumption and its characteristics have been presented in Chapter I, section C. The focus is therefore on poor farmers; the landless; unskilled labor; and women and children in low-income households.

Based on the stabilization cum-structural adjustment package, the various channels through which the poor are affected are presented below, with a focus on the distributional effects of the following measures:

- (1) trade and exchange rate system

- (2) tax structure
- (3) agricultural pricing policies
- (4) social sector programs
- (5) monetary and fiscal policies
- (6) wages and administered prices

This "list" follows Huang and Nicholas (1987a).

### 2.1 Distributional effects of trade policy reforms

Following the balance of payment crisis of 1983, the Moroccan Government began to reorient its industry and trade strategy from inward looking development based on import substitution, with extensive state intervention and major public sector projects, to one designed to promote exports and efficient import substitution with greater reliance on the private sector (CEM, 1987:14). So far, substantial efforts have been made to reduce the average import tariff rate and disparities in protection with the aim to (1) reduce present distortions in resource allocation and import licensing, (2) remove quantitative restrictions (QRs) and import licensing, and (3) to eliminate export duties and simplify trade procedures. In addition, a more flexible exchange rate policy was adopted which allowed for the devaluation of the Dirham. Devaluation was undertaken in order to correct an overvalued exchange rate, the legacy of the short-lived price boom in phosphate. More generally, devaluation is included in the package of reforms in order to improve tradability and the current account through an "expenditure-switching" process.

Accompanying these policies is a less interventionist approach on the part of the government. Indeed, in 1985, twelve years after the Moroccanization of the economy, the newly appointed government announced “a determined policy of denationalization and of returning to the private sector everything that naturally belongs to it.”

In 1987, Morocco became an official contracting party to the GATT, thereby reaffirming the economy's orientation towards increased liberalization.

The short-run implications of trade liberalization and currency devaluation measures are recognized to be adverse, entailing a loss of output, a decline in spending, and an increase in unemployment. In Morocco, where almost half of the poor population is located in urban areas, devaluation imposed immediate costs (in terms of lower levels of income and consumption) on the urban poor who are locked in the production of nontradables, or engaged in nontradable activities such as construction, utilities, services and informal sector activities. The decrease in the relative price of nontradables also hurt farmers growing non-exported crops. Improved price incentives did not prove to be more successful for the rest of the farmers. Given that poor farmers are barely served by infrastructure services such as irrigation and transportation, they face capacity constraints which prevent them from increasing output in response to higher prices. These farmers suffer even further because adjustment involves fiscal restraint which translates into lower spending for infrastructure development.

Moreover, devaluation was ineffective in improving the plight of the rural poor because land ownership is still highly concentrated (in the 1970s, almost 75% of farming families still owned no land as barely two percent of the land was distributed to the farmers). Hence, increased producer prices on export crops have no effect on the landless who cannot cultivate them, instead the implications for the poor may be severe if they are consumers of these crops.

Consumers in both the rural and urban sectors were hurt by increases in the prices of goods (triggered by escalating intermediate input costs) and the poor were the most vulnerable to the increase in those of food. In addition as real wages of workers in the nontradable sector and in formerly heavily protected industries declined relative to those in the tradable sector, it was once more the poorest segments that were the worst off.

Finally, given that the nontradable goods sector is labor-intensive, workers laid-off in that sector were not able to find employment in the tradable sector which is more capital-intensive. However, those workers that were absorbed by the tradable sector benefited from higher wages and greater job security.

The World Bank and the International Monetary Fund claim that these costs, although unavoidable, are only transitional in nature. However, Huang and Nicholas (1987a: 35) identify several factors that combine to prolong the period of transition. Most important are the following:

- Price and wage rigidities which render the reallocation process lengthier and the unemployment problem more severe.

- Even under conditions where relative prices do change, the expenditure-switching process may be slow. This may be because exports are at full productive capacity, or because the supply by farmers is unresponsive to price increases.
- Finally, when the export sector is monopolistic, a price increase may not have a full effect on production.

Orthodox economists insist that in the long-run, the liberalization of trade leads to increased efficiency gains, which in turn increase income for the population as a whole. Moreover, they believe that devaluation is a necessary measure of austerity which, in the long-run is justified by the positive effects it has on the economy through the “restructuring of incentives.” In fact, they regard exchange rate action as the single most important policy instrument of structural adjustment. It is a principal element of “getting the prices right”.

The structuralist riposte is that the only reason such policies may work is because of the changes that occur in the distribution of income as a result of forced savings and of relative price changes. Taylor (1988) argues that efficiency gains (or the “little triangle” welfare gains) from trade liberalization are “trivial” as Harberger discovered in 1959. They amount to a small fraction of GDP and hence fail to compensate for the costs that such a procedure incurs. With respect to devaluation, the structuralist consensus is that, although it does, in the short-run, reduce the trade deficit through economic contraction, it carries severe implications for the poor in the longer term. Devaluation affects the poor through three main channels. First are the price effects which are the result of increasing intermediate import costs. Second is a stagflationary effect, which

occurs especially when the export response is weak, and can develop into an excessive contraction or “overkill” when the devaluation is accompanied by monetary restraint (as is the case in Morocco). Finally are the wage and employment effects. The behavior of employment has been significantly affected by the evolution of real wages which have been negatively impacted by the devaluation. The result is a shift in the income distribution towards groups with a higher propensity to save.

The World Bank however argues that the social costs of lower real wages and reduced purchasing power have been in part compensated by the positive employment effects, which followed the decline in real wages, especially as production shifted to more labor-intensive, exporting activities.

Given that in Morocco employment is a politically more sensitive issue than wage levels, it is understandable that this positive employment effect has been highlighted, as it ensures that the continuation of the adjustment program is more “palatable” politically. In reality, however, the adjustment and stabilization period has been characterized by open unemployment, mostly in urban areas, for women and young adults. In 1986 unemployment was at 9.3% accompanied by estimates of the total labor force in the informal sector ranging from 30% to 76%.

Moreover, the jobs that have been created between 1982 and 1986 have been mostly characterized by low wages and productivity; and whatever increase in employment has been attributed to the adjustment program is more a reflection of

seasonality. Indeed, during the 1980s, the share of temporary jobs (likely to be causally related to poverty) in total employment increased, mainly in the services sector, transport, urban construction sites, and government work camps. Ennaji writes: “part-time work is no novelty, nor is it a Moroccan speciality, but it has become more and more typical of the labor situation in Morocco in the last fifteen years or so” (1986: 45). These conditions have been further exacerbated by the falling trend in real wages.

Finally, “the ratio of economic benefits to political opposition engendered by trade and exchange rate policies can be very small..., rendering the reforms unsustainable” (Rodrik, 1988: 29). Indeed these reforms are threatened by the growing opposition of certain domestic interest groups to further trade liberalization, as well as increasing world protectionism illustrated in part by the increasingly difficult conditions of access to European Community markets which in the past have absorbed 60 percent of Morocco’s exports, and the pressing need to narrow the budget deficit in the face of structural revenue constraints. However, sustained support of trade policy reform by the government has been the determinant factor ensuring the successful implementation of the liberalization program. A World Bank report writes: “In the context of the overall implementation of trade policy reform, Morocco has arguably become one of the more liberal trade regimes within the developing world.” (SAL, 1988: 4)



## 2.2 Distributional Effects of Tax Adjustments

Tax reforms in Morocco aim at achieving three objectives: (1) to increase the level of revenues to the Treasury; (2) to harmonize the tax system with the other objectives of improving the efficiency of resource allocation and in particular with trade liberalization; and (3) to ensure that the “tax burden” is shared in an equitable way across the population groups.” (Mateus, 1988: 73)

The effect of tax reforms on poverty and equity is a major consideration because of their highly visible impact on the incomes of vulnerable groups. Most studies express difficulties in analyzing who actually pays the tax. A tax levied on a producer may be passed forward on to the consumer through higher prices or backward to factors of production.

Studies on the redistributive effects of tax systems have shown the overall impact to be modest. In the short-run, the immediate effect of a tax is the change in the purchasing power of existing income either through changed income levels (direct tax) or through changed price levels of commodities purchased with the income (indirect taxes). Hence, direct taxes tend to influence the decision to save, and therefore also the long-run growth of the economy. As for indirect taxes, they may alter the size of (pre-tax) income, as factors are reallocated away from heavily taxed activities, thereby affecting production and hence factor returns. In general, however, tax policies are not a particularly suitable instrument for alleviating poverty. In Morocco, most of the rural poor remain untouched by the

tax system because their incomes are too small to be taxed and their consumption basket comprises largely untaxed goods.

Corporate tax rates on profits and personal income taxes paid by the higher income groups were lowered twice between 1987 and 1988. These measures are not expected to significantly affect the poverty situation of the poor; however they will adversely impact the distribution of income. On the other hand, also in the context of the adjustment program, several direct tax measures were undertaken that were supportive of a more equal distribution of income. First, there was a broadening of the tax base; second the zero-bracket threshold applied to the personal income tax was raised from DH 6,000 to DH 8,400 (in response to the fiscally regressive impact of inflation on low-income groups) (SAL, 1988: 11) and a movement toward the elimination from the tax base of a larger number of low-income tax payers (whose contribution is already minimal) is underway. Additional measures that provided possibilities for a more equitable taxation system included the taxation of the real estate (immovable property especially land) and agriculture (especially large farms), sectors that in the past had been exempt of taxation. The Budgetary law for 1988 further repealed certain exemptions that had been allowed for some financial institutions.

Indirect taxes in the form of a Value Added Tax (VAT) were introduced on goods and services in 1986. Although they have proved to be a sizable generator of revenues, they have affected distribution in an adverse manner. More recently, exemptions from

VAT have been eliminated on a number of products in order to widen the tax base, and in the effort to reduce dispersion, rates have been increased on such items as coffee, rice, cattle feed, and transportation services with the expected negative implications for both the rural and urban poor.

These indirect taxes have a more immediate effect on lower income groups because they change the prices of goods in the consumption basket. Moreover, taxes on consumption tend to be regressive because a larger proportion of the incomes of the poor is spent on consumption.

The orthodox view argues that such efforts are usually partly counteracted by the prevailing use of tax exemptions for basic necessities consumed by the poor; that whatsmore consumption taxes are usually restricted to processed goods, so their regressive effect is more diluted the poorer and more rural-based the economy. In Morocco, however, almost 50% of the poor are urban based and consume a large share of manufactured and processed products, hence they do feel the tax burden more than their counterparts in sub-Saharan Africa who consume mostly home-produced or untaxed products for cottage industries. (Huang, 1976)

If more explicit emphasis is placed on distributional issues, indirect tax measures would include a general broad-based tax on goods and services, higher differential rates of tax on goods and services consumed by higher-income households, such as cars, petrol, alcohol and tobacco, household "white goods," electricity, telecommunications, hotels, restaurants and air travel. These taxes,

because on selective goods and services that are generally highly income elastic, have a favorable impact on income distribution, though by themselves they do not improve the poverty situation.

Of the tax measures affecting trade, the rationalization of the tariff structure as well as the reduction of exemptions have proved to be important in increasing revenue. The net impact of import duties on household incomes depends on consumption patterns for the commodities being taxed. In general, households in higher income groups tend to consume more imports and more “luxury” goods that carry higher tax rates, than do lower income households. Hence higher income classes tend to pay more taxes and higher rates. Moreover, with the replacement of QRs by tariffs, importers who usually belong to higher income groups will enjoy lower economic rent, with the government receiving increased revenues. These measures affecting trade, besides raising revenue, may contribute to an improved distribution of income. It must be remembered, however, as noted previously, that reduced exemptions may adversely affect poverty groups to the extent that import items (such as flour and edible oils) are part of their consumption basket. As for reductions in tariffs on luxury items, the inevitable result is a worsening of the distribution of income.

Finally, the strengthening of existing institutions and rationalizing of tax administration efforts that are being undertaken in parallel to the structural reform in the fiscal system (to be covered later in the chapter), may result in the improvement of equity in the long-run, especially as it concentrates on tax evasion

which is substantial for the higher-income groups. However, such a policy requires commitment on the part of staff and officials and can take years to implement. A study by the Fiscal Affairs department of the IMF concludes that: “while improved tax administration is desirable, it cannot be relied on as a short-run solution to a problem of insufficient revenues, and for this reason it is unlikely to have a significant redistributive impact in fund programs” (IMF, 1986: 15).

### 2.3 Distributional Effects of Agricultural Pricing Policies

The ingredients of the agricultural prices and incentives reform as described by Mateus (1988: 74) include the following: (1) external trade liberalization across the sector, lifting prohibitions and other quantitative restrictions on exports and imports, and instituting a small effective protection rate across all subsectors; (2) liberalization of domestic markets in grains; (3) gradual elimination of consumer subsidies and expansion of direct food aid programs to compensate the urban poor; (4) freeing crop systems in irrigated areas in order to better respond to market price signals (this would entail a drop in sugar production, a crop heavily subsidized by the government); and (5) progressive elimination of input subsidies, especially on fertilizers and water.

The World Bank argues that the above reform is essential to counteract the anti-agricultural bias that characterizes past policies established by the government which include output taxes, low procurement prices, and macroeconomic and exchange rate policies

that reduce producer incentives. As for food and inputs subsidies, the Bank states that both result in lower income as well as lower incentives for the poor, rather than helping the poor and promoting equity.

The argument is that lower producer prices impede agricultural growth by reducing returns to labor and capital in agriculture thus inhibiting the discovery and adoption of new technologies that would result in lower cost production functions and agricultural growth. Moreover, subsidies on flour, made in large part from imported grain, have depressed agricultural prices of local cereal grain, much of which is not marketed through government channels, but which competes with subsidized flour. This is thought to have been responsible for much of the terms of trade disadvantage of the agricultural sector (CEM, 1987: 21). In addition, the poor are hurt by low producer prices in two ways, first indirectly through the reduction in growth (this is assuming that growth will eventually have trickle down effects) and more directly through the fall in the real incomes of households, mostly rural for whom food is not only a commodity item but also a source of revenue.

Even though increased producer prices do stimulate agricultural production, their distributional implications cannot be ignored. The IMF writes: "Few policies undertaken under fund-supported programs receive as much critical attention as reductions in budgetary subsidies through increases in the prices of basic goods" (IMF, 1986: 27). The basic good relevant to this section is

food. In section 2.6 of this chapter, subsidies on other basic goods such as petroleum and electricity will be reviewed.

In Morocco, as in other countries, low prices for food symbolize in part the government's commitment to protect the lower-income classes. In the early 1980s, the government spent 10% of its recurrent expenditure on basic foodstuffs (cereals, sugar, edible oils, milk, butter and petroleum products) in order to cover the price increase that was triggered by the devaluation and the commodity price boom. This figure corresponds to 31% of total government social spending, making food subsidies the second largest component of government provisions behind education and ahead of health. The rates of subsidy in flour and edible oils (that are in large part imported) were about 50% of import cost (Mateus, 1988: 14). By establishing a wedge between producer prices, import prices, and consumer prices, the government also aims at stabilizing prices (thus reducing income fluctuations), at keeping wages down and therefore avoiding inflation. Dethier (1986: 40) adds: "In poor countries, food constitutes a high share of total production and consumption, and interventions in food markets attempt to maintain ... the status quo between interest groups involved."

In general, cuts in food subsidies will favorably affect the income of farms that produce food, and negatively affect the income of urban workers and the rural landless. In Morocco, the poor population is mostly constituted of urban laborers and the rural landless, hence the cuts in food subsidies introduced in January 1984 had immediate adverse repercussions on the well-being of the poor.

In fact, five months after the measures had been adopted, movements of social unrest and widespread riots broke out. Student-based protests began in Marrakesh and spread to five northern cities, with substantial participation of adults from the poorer neighborhoods. "The same economic and political grievances were everywhere apparent, and some protesters carried banners denouncing (King) Hassan personally" (Tessler, 1985: 46). In addition to the increase in food prices, these movements broke out in response to the decrease in real income and recessionary effects of these price increases.

The question is therefore: why does economic adjustment require increases in the prices of goods that are so directly associated with consumer well-being?

Besides the fact that such a policy entails positive effects on the government deficit (through decreased expenditures) and the balance of payments (through decreased demand for food imports), the general argument based on several studies undertaken by the World Bank and the IMF is that most food subsidies are directed toward the urban sector, whereas the majority of the poor population lives in rural area. This is not the case of Morocco where the spacial distribution of the poor is almost equal between the urban and rural areas. Nevertheless, it is estimated that only 16% of the subsidies actually benefit the bottom 30% of the population. In addition, it may be true that while rural hunger may be more severe, urban hunger is more visible and therefore more politically dangerous. Most countries have found that upper income groups



tend to appropriate an excessive share of food subsidies, and that the urban and politically more articulate groups benefit disproportionately (Dethier, 1987: 40). What's more, it is specifically these groups that are more likely to speak out and threaten retaliation, rather than rural agricultural workers who are too unorganized, are often not qualified for the benefits, or may even, as in the case of the ultra-poor, be unaffected by the program modification because they do not have the purchasing power to buy certain food products, even at subsidized prices.

However, this distributional pattern of the benefits of food subsidies does not imply that the removal of these subsidies will have no effect on low-income households. Because these households' consumption basket is mainly comprised of food, with a larger share of income spent on cereals than any other food, a cut in subsidies may entail very adverse effects on the standard of living of the poor.

The long-run effect of cuts in food subsidies depend on how the measure will affect the general level of activity, that is how those changes in nominal income affect demand for non-agricultural goods, prices and real incomes. Taylor (1983: 195) writes: following cuts in food subsidies "demand for food products will fall, leading to a decline in either imports or the internal producer's price (or both). There may be a spillover into demand for non-agricultural goods, leading to overall output contraction. Once again, a foreign balance improvement is obtained at the cost of reduced economic activity and a price-induced shift in the income distribution against the poor, who devote a large share of their spending to food."

Moreover, programs that provide subsidized food to urban unskilled labor can in part explain the constant migration of unskilled workers from the country-side and the resulting decrease in urban wages.

The consensus is that most of these problems can be avoided through targeting selectively to vulnerable households, based on income, location, health and nutrition status. Improved targeting can be achieved by concentrating subsidies on food items consumed primarily by the poor.

Alternative food compensatory programs will be explored in Chapter III. The design of an effective system has become urgent as the government plans to entirely eliminate subsidies by 1990.

With respect to input subsidies, fertilizer is the most widespread in Morocco. Because fertilizer provides higher incremental yield on irrigated land, farmers that benefit most from irrigation are the ones that benefit from fertilizer subsidies. Moreover, in the case of rationing of subsidized fertilizer, the allocation will be biased in favor of the larger farmers. Furthermore, with increased emphasis on fertilizer-intensive crops, labor is gradually substituted by fertilizer, and the landless are the worst hit. Meanwhile as the availability of non-fertilizer — intensive crops (mostly cereals) decreases, so does the consumption or calorie-intake of the rural poor.

Producer subsidies have been used in irrigation and sugar production not only as agricultural inputs but also to stimulate the livestock subsector, and for exports. Producer incentives aim at

promoting agriculture, a “priority” sector as well as promoting certain types of production. In addition, investment subsidies in irrigated agriculture aim at promoting investment in that sector and speeding its recovery.

While these subsidies may be motivated by the belief that poor farmers need protection and income transfers, the distributional pattern of subsidized credit or water, like other subsidized inputs, again favors the relatively few well-off and politically influential groups.

A drop in sugar production (a crop heavily subsidized by the government), and the reduction in input subsidies (particularly fertilizer) — two components of the policy reforms in agriculture — will lead to an increase in costs of production thus adversely affecting farmers. However, to the extent that these cuts would also lead to a reduction in the production of fertilizer-intensive crops, and a freeing of government resources to be used for improving existing systems, further expanding irrigation facilities and increasing supplies of complementary inputs, poor farmers may end up benefiting to a greater degree from government resources. Moreover, to the extent that a reduction in these input subsidies is likely to decrease mostly the income of the upper income class it will narrow the income differential between the poor and the relatively well-off.

#### 2.4 Distributional Effect of the Provision of Social Services

In the effort to reduce public expenditures, the Moroccan government has significantly curtailed public expenditures on the social sector.

In 1985, total government expenditures on social services in Morocco accounted for about 10% of GDP, and the share of social expenditure in total government outlays of that same year was 29%. These figures are comparable with those of Brazil and are slightly higher than those of Mexico and Korea.

The high priority generally given to public outlays on social services is justified on grounds of welfare and equity. In Morocco, total social outlays, as well as per capita expenditure decreased severely in 1983, 1984, and 1985 as a result of the stabilization-cum-adjustment policy adopted in 1983, after having continuously risen between 1978 and 1982. This translated into a reduction of real per capita expenditures on social services by 12% p.a. during 1983-1985, compared to a real per capita GDP growth of 0.4% p.a. during the same period (WB, 1988: 6).

The orthodox view is that underinvestment in social services may also be the result of restrictions on private sector participation and the pervasive use of public subsidies which, it is believed, distorts incentives. Another plausible reason advanced is the belief that resources are not necessarily allocated to activities with the highest social rates of return. This mistargeting is present in Morocco within sectors and within programs. Mistargeting within sectors is characterized by spending on programs that are unlikely to

benefit the poor, especially in public education and health. In the education sector, minimal funds have been devoted to primary education and literary programs important for the poor, while 63% of total education expenditures were allocated to higher and secondary education in 1985. Moreover, disparities in educational participation are noticeable between genders and among geographic areas, with women and the poor constituting the groups most suffering from “educational poverty.”

The poor have also suffered from mistargeting in the health sector where most of the spending has been devoted to high cost curative care, at the expense of preventive care, which is more likely to benefit the poor. The allocation of resources is also highly biased towards urban regions, thus draining resources away from the less developed, rural areas. In sum, the health sector suffers from, first an internal inefficiency problem, reflected by the inappropriate distribution of health care professionals, medical supplies and drugs, particularly in rural areas; and second an equity problem, as the poor have benefited little from public spending.

This pattern of spending not only does not benefit the poor as much as intended, but it also creates second order negative effects. The concentration of government spending in urban areas makes it difficult to develop facilities in the country-side (WB, 1988).

Mistargeting also occurs within programs, the foremost example being that of food subsidies which accrue to the high income groups, as has already been noted earlier in this chapter.

The implications of the trends and levels of per capita social expenditure on the standard of living of poor households can be related to a number of issues (WB, 1988). These are: (1) how the intersectoral allocations relate to the hierarchical structure of the overall needs of the poor households, (2) whether the magnitude of the social expenditure matches the basic needs of these households, and (3) how cost efficient the production and distribution of social services is. These issues are examined further below.

With respect to the structure of government social spending, the intersectoral allocation of social expenditures in Morocco appears to favor education over nutrition and health. The largest share in total government social expenditures, higher than 45%, has been spent on education between 1978 and 1986. During that same period, the second largest component of public social spending was on food subsidies, which in 1985 accounted for 31% of the total. Health was the third largest component, amounting to 7% of the total in 1985. During the period between 1978 and 1985, the shares of education and health declined considerably, partly as a result of the significant increase of the share of food subsidies after 1973, but also because of resource constraints. The smallest components of public social spending were housing and employment creation programs which accounted for only 2% of the total or less.

In the future, there will be a growing need for more efficient and equitable health, nutrition and compensatory employment programs. This will be elaborated on in Chapter III.

With respect to the magnitude of public spending on social programs, it is clear that it does not match the basic needs of poor households. Performance evaluations of the overall education delivery system in Morocco, by Bank staff show that the current levels of educational services are insufficient to serve the whole population, because of the lack of facilities and/or appropriate equipment, and personnel. Despite progress made since the start of the Education Reform Program, overall participation in primary and secondary education in Morocco is lower than in countries with similar income, with 56% of children between the ages of 7 and 12 living in rural areas having limited access to primary schools. Moreover, the overwhelming prevalence of adult illiteracy in poor households attests to the inadequacies of the educational delivery system. However, it is not clear whether these inadequacies are due to insufficient levels of public expenditures — as Morocco's share of education in total government outlays compares favorably with the average of other low middle-income countries — or whether they are due to cost inefficient spending of such funds.

With respect to health, indicators as well as other empirical findings suggest that current levels of health services fail to meet the basic needs of the population, especially those of the poor. In Morocco, 60% of the rural population has no access to basic care, because of such factors as lack of facilities, distance, inadequate transportation means, and financial, social and educational barriers. The nutritional status is more strongly correlated with adjustment and consequently has suffered more from the decline in per capita

social expenditure since 1983, than did other health indicators. (In fact, IMR and life expectancy improved despite the recession and the adjustment program.)

The level of government expenditures on health still compares poorly with countries with the same and even lower per capita income. It can therefore be argued, despite the question of cost efficiency in the provision of health services, that the level of public spending on health in Morocco is insufficient.

Regarding the cost inefficiency of the production and distribution of social services (the third issue raised by the social sector strategy), it is attributable first to the inadequate management of infrastructure, such as technology, and second to the over-centralization of the provision of social services. Foremost, cost inefficiency has been identified as resulting from the great degree of dispersion of the population into small and scattered settlements in rural areas. This dispersion implies unequal access to public services, especially education and health. In general the Central and Western regions (which contain the largest urban concentrations in the country) are the better served. There are fewer than 10,000 inhabitants per doctor in these two regions, as opposed to more than 20,000 in other regions such as the South and Tensift. Hence, even if social services were subsidized, the rural inhabitants have to incur the costs of transportation and the opportunity cost of time securing these services. Because of these costs the poor may value and use health and education services less than higher income groups do,



especially if they do not consider them essential for their survival (H&N, 1987a: 43).

The above issues, namely underinvestment, mistargeting and high cost inefficiency in the provision of social services suggest that the income redistributive effects of government expenditures will be negligible or even negative.

As for the distributional effects of cuts in the provision of social services, particularly of health, nutrition and education, they can be severe for the poorer beneficiaries who lack the savings to pay for alternative services. Such cuts would therefore negatively affect the human capital of poverty groups.

Even if the adjustment effort requires fiscal austerity, the access to social services for the poor should be maintained possibly financed by freed resources accumulated from improved targeting. Efforts to this effect will be discussed in the following chapter.

## 2.5. Distributional Effects of Monetary and Fiscal Policies

“(Monetarist policy is) simply a campaign against the standard of life of the working classes (operating through) the deliberate intensification of unemployment ... by using the weapon of economic necessity against individuals and against particular industries” (J.M. Keynes as quoted in Dethier 1986: 12).

The Moroccan adjustment program includes one, a variety of contractionary monetary and fiscal measures designed to curtail excess demand in the economy; and two actions for the liberalization of the financial sector.

Both contractionary monetary and fiscal measures control the fiscal deficit as an instrument to curb public sector borrowing and thereby restrain demand. The Moroccan government exerts monetary restraint through high reserve requirements and by imposing ceilings on bank credit, the latter as part of the stabilization measures agreed with the IMF. At the same time, the government is relaxing other constraints on the financial sector such as the tight regulation of interest rates, these have now been raised to positive levels; and the restrictions on the functions of specialized public sector institutions, which are now allowed to compete with commercial banks in mobilizing deposits and in lending. However other restrictions remain. These are related to legislation and the market structure. The medium-term goal is to identify these obstacles and remove them in order to increase competitiveness and diversify financial instruments and thereby improve the financial sector's effectiveness.

The orthodox view argues that failing to curb monetary growth in the presence of a fiscal deficit can accelerate inflation, the costs of which are mostly borne by the poor who typically pay most of the inflation tax. The poor are the least able to protect their real incomes (through the indexation of their wages) and their assets (by moving into real or foreign assets to avoid taxation).

Structuralist theory on the other hand argues that it is the policy curbing monetary growth itself which exerts inflationary pressures by pushing up interest rates. However, "interest rate cost-push is left out of standard models, which inevitably show monetary

contraction to be anti-inflationary (Taylor, 1983: 7). Moreover, given that such a policy mainly operates through restraining aggregate demand, it often results in a loss in growth and employment which inevitably hurts the poor.

If unemployment affects unskilled labor more than skilled labor as it usually does, the net effect of monetary contraction is likely to be an increase in poverty.

Restrictive monetary policy can also affect the distribution of income over time, through changes in the distribution of assets. Due to interest rates control and scarce funds as a result of monetary restrictions, loans in the formal banking sector tend to be allocated to the larger, more established firms, and to consumers and producers in the urban sector. Relatively smaller firms and rural entities may have to use informal “curb” markets for their credit needs. This pattern of allocation places the smaller firms at a disadvantage and leads to potential bankruptcy and asset concentration. However, poorest cultivations are exposed to a lesser extent to the effects of a monetary contraction as the loans they receive are mostly in kind such as seed and fertilizer.

The IMF (Heller et al., 1988: 15) advocates the liberalization of the financial market (which involves raising interest rates, decreasing market fragmentation, and increasing competition) in order to correct the bias in favor of larger firms and urban sectors. By facilitating access to credit markets for all, this process allows the poor, engaged in either small-scale enterprises in the informal sector or in small farms in the rural sector, to expand their productive

capacity and increase their participation in the process of economic development and structural adjustment. However, given that the poor cannot offer collateral, they will remain risky customers regardless of the level of interest rates. Moreover, historical experience has shown that extreme liberalization (accompanied by speculation) can lead to capital flight which in turn can result in financial collapse.

An equally if not more significant distributional concern is the distributional effects of cuts in public expenditure. Fiscal adjustment efforts often lead to reduced capital expenditure which results in decreased employment opportunities and a slowing down of future economic growth. Consequently, output, consumption and investment are also affected because the marginal productivity of labor and private capital is directly affected.

During the past two decades, the development strategy has remained the same, mainly consisting of heavy investment in irrigation in agriculture, the development of “forward-linkages” in the phosphate sector, and the build-up of material infrastructure. However, by 1987, the rate of public investment had dropped to 21.1% as compared to a peak of 34.2% in 1977 during the phosphate price boom. In fact, besides suffering from the adverse economic conditions which characterized the early 1980s, public investment has taken much of the brunt of the fiscal adjustment in the past, with government investment being curtailed to the point that real expenditures declined by over 50% between 1981 and 1986. Moreover, while the adjustment and liberalization efforts

undertaken by the Government since the 1983 crisis sought and obtained a higher share of private investment in total gross fixed capital formation (GFCF), rising from 12.9% in 1982 to 16.6% in 1986, the level of public investment has fallen below the minimum necessary to meet the development needs of the private sector and the social needs of the population, particularly the economically disadvantaged (SAL, 1988: 13). Hence the narrowing of the fiscal deficit from 12.2% of GDP in 1983 to 6.0% of GDP in 1987 has been achieved, in large part at the expense of public investment. As a result, many suspensions and even cancellations of investments in key economic and social sectors continue to threaten future growth and the development of human capital.

The potentially deleterious long-term effects of cutbacks in the health and education sectors on the human capital of the most vulnerable groups has already been covered in a previous section. Cutbacks in other areas, such as infrastructural operations and maintenance have equally severe ramifications for the poor. Low-levels of investment in infrastructural projects that are characteristically labor intensive (such as construction) affect the poor through decreased demand for low-skilled labor (which translates itself into lower wages and even unemployment), and by contributing to the deterioration of the infrastructure which is detrimental to the value of the assets owned by the poor.

The government maintains however that it is committed to mitigating the hardship to the poor caused by the present economic difficulties by redesigning its programs so as to reduce their high

costs to the budget, and by directing them more effectively to the really poor. A significant part of the current economic problems are attributable to the planning, allocation, and management of public sector resources, as illustrated in the design and execution of the 1981–85 plan which suffered from the lack of adequate project appraisal and hence failed to match growth objectives with available resources. As previously stated, an increase in the level and efficiency of public investment expenditures is a major component of the adjustment program. It is reflected in the Target Investment Program (TIP) formulated by the Moroccan government in consultation with the World Bank, on the basis of growth objectives, sectoral priorities, and identified projects in the 1988–1992 plan.

## 2.6 Distributional Effects of Adjustment in Wages and Administered Prices

Reforms in administered prices (through the reduction in subsidies and the elimination of price controls) and in the structure of wages are integral components of the Moroccan adjustment program.

Liberalizing price controls is expected to improve the financial position of the public sector as well as promote efficiency in the allocation of resources, but it also clearly has distributional consequences.

As has been already covered, the rationalization of agricultural prices proved to be one of the politically more sensitive areas of the government's structural adjustment program. Other dismantling of price control efforts have involved the energy sector.

The rationale for reducing and eventually eliminating petroleum and electricity subsidies is the elimination of inefficient energy use (which, in the case of petroleum would relieve the foreign reserve shortages that are significant in Morocco). Moreover, eliminating such subsidies would discourage resource allocation bias in favor of energy-intensive and labor-saving technology which leads to the unemployment of unskilled, low-income laborers.

In addition to avoiding the above employment effects, it is argued that allowing energy prices to reflect the opportunity cost to the country, may improve the distribution of income because it taxes the rich for whom the consumption of energy is substantial, that of poverty groups being insignificant. However, increases in petroleum prices are inevitably translated into higher transportation costs of goods, which in turn are reflected in higher prices of goods, thus affecting all income groups, but mostly the poor.

With respect to reforms in the structure of wages, Morocco has directed wage control measures specifically at the public sector, in the effort to reduce the government budget deficit. This is because personnel expenditures constitutes the main cost in the recurrent budget, having risen from 8.5% of GDP in 1970 to 16% in the early eighties, and are now around 11% of GDP. Moreover, the number of civil servants increased from 278,000 in 1970, to 584,000 in 1984 and by 1986 reached 604,000 (CEM, 1987: 16).

Structuralists believe that, "freezing of wage demands is (included in orthodox packages) to cut inflationary pressure and perhaps shift the income distribution (through forced savings)

towards high-saving profit recipients and the upper class” (Taylor 1983: 191).

As a result of a wage restraint policy limiting salary increases to the lower end of the scale, government workers have experienced a substantial decline in their purchasing power, the real income having decreased over the last three years. Today, as a result of its intervention in the labor market, the government is faced with a decline in productivity, and pressures on the budget placed by pent up salary demands which can prevent the allocation of budget resources for supplies and services needed to allow the personnel to operate effectively.

In addition when government workers are much underpaid, as they are in Morocco compared with their counterparts in the private sector, it becomes difficult to attract skilled and competent employees, (instead widespread corruption prevails), and hence a lower quality of services is provided to the low-income groups. In response to pressure, the government announced a 10% increase in civil servants' salaries which was made effective beginning of January 1989.

Releasing redundant workers is politically difficult, instead, the Moroccan government has adopted a law in 1983 eliminating jobs in the education sector that are vacated by retirement, and this law has been extended to other sectors. These ceilings on overall government employment have imposed hardship on some public service segments, but they may in the long-run improve the efficiency of public resource allocation, and increase those resources to the



benefit of the poor. Though how the latter is to be achieved is not specified.

There is no easy solution for problems generated by wage policies because of the severe financial constraints facing the government. The World Bank (CEM, 1987: 17) suggests that the salary structure be reassessed annually to determine the trade-off between expanding employment and salary increases. Moreover, it advises that in response to declining productivity, a working group in the Ministry of Administrative Affairs should be set up to determine how to increase productivity and introduce performance evaluations that would replace the present system of automatic promotion.

Having reviewed the implications for poverty of the different policy measures, several conclusions emerge. First, the impact of the different adjustment policies has been largely determined by Morocco's economic and social structure, the most important determinants of changes in distribution having been (1) institutional factors such as the existence of trade unions, lobbies and other politically powerful interest groups which on the whole, given their limited influence, have cooperated with the government's reforms; (2) the weakness of mechanisms such as wage indexation which was responsible for the declining trend in real wage; (3) the labor-intensity of production in both the tradable and non-tradable sectors which meant that reforms in the production system as well as devaluation hurt the poorest groups; (4) patterns of consumption, with imports strongly figuring in even the poor's consumption

basket, thus making them share in the costs of adjustment; and (5) other features of the economy such as the large size of the subsistence sector vis-à-vis the “modern sector.”

Second, the transitional costs of adjustment may be greater in Morocco than in low-income sub-Saharan Africa. This is because, Morocco suffers from a greater debt burden, its land-ownership is more concentrated and almost half the poor are low-wage urban workers thus more vulnerable to the removal of subsidies such as those on food and energy.

Third, most policy reforms affect the poorest groups more than marginally. In fact, transitional costs may have longer-run repercussions on the poor, especially if, as structuralists maintain, the effects of orthodox policies are stagflationary. As Addison and Demery (1987) write: adjustment policies shape development and influence the distribution of income for years into the future. Hence the poverty costs of adjustment are not simply a short-term problem.

Finally, the adjustment program in Morocco (as in other countries) has involved a trade-off between short- and long- term economic objectives and between various social objectives. First, the adjustment program has entailed a decline in short-term growth, however the World Bank promises benefits in the long-run that will cover the costs. Second, various policies have achieved external balance at the expense of internal balance, entailing a different trade-off between inflation and unemployment. Both inflation and unemployment have proven to be among the politically most

sensitive issues given the policy of gradually removing subsidies, and the high rate of employment and underemployment. Finally, the way a policy is implemented can also involve a trade-off between efficiency and equity. While a gradual adjustment process helps mitigate the costs to the labor-intensive sectors and the poorest income groups, it is argued on economic grounds, that a quicker, more uniform adjustment is more efficient. Given economic, social and political considerations particular to Morocco, a compromise must be reached with respect to the pace of the reforms. Without a good balance between the different considerations, the sustainability of the program becomes questionable.

The World Bank concludes otherwise with respect to the distributional changes that resulted from the Structural Adjustment Program. On balance, it finds that "the extensive reforms implemented in 1983 have initiated a significant transformation of Morocco's underlying economic structure without unmanageable stress to the social fabric (SAL, 1988: 6). As for the IMF (1986: 37), it finds that on the whole, the only measures that hurt the poor are the ones that have increased the wealth of the upper-income groups. Nonetheless, concern for the social impact of adjustment has evolved since the introduction of the SAP. Moreover, it is now increasingly believed that policies to mitigate the social costs of adjustment are feasible without threatening the achievements of adjustment programs. The following chapter will determine to what extent the concern with poverty alleviation and the protection of the poor's living standards from the negative impact of austerity measures is

reflected in the design of the Bank-supported adjustment program. In addition, less “orthodox” measures to safeguard the interests of the poor during the program, and to minimize the tradeoff between economic and social objectives will be reviewed.

### **Chapter III: Policy Reformulation and Recommendations to Protect the Poor**

#### **A. Overview**

The World Bank's original purposes, as stated in its Articles of Agreement, include "raising productivity, the standard of living and conditions of labor." However, it was not until the early 1970s, when it was recognized that the benefits of rapid growth of the 1950s and 1960s (in which the Bank was involved through lending to power, transport and industry projects in relatively advanced developing countries) had not "trickled down" to the poor, that the Bank began to concentrate its efforts on activities that would benefit the poor directly (Beckman, 1986: 26). Arguing that economic growth was a prerequisite for the reduction of poverty, the Bank shifted lending to projects designed to expand economic output while simultaneously reducing poverty. Such projects included agriculture and rural development which were directed to the rural poor, while other projects such as slum-upgrading and low-income housing focused on urban poverty.

However, with the economic turbulences of the 1970s and early 1980s, the World Bank turned its attention to helping countries cope with the debt crisis. These pressures led to a decline in the share of bank activity specifically directed toward the reduction of poverty. As a result, "critics have charged that, (in the process), the Bank (has) retreated from its poverty mandate" (Beckman, 1986: 26).

As for the IMF, it has generally maintained that distributional issues are primarily an internal political concern. "This stance has led

some observers to suggest that Fund-supported adjustment programs ... favor vested interests and are inimical to the needs of the poor” (Sisson, 1986: 33).

In order to determine the Bank’s current level of commitment to alleviating poverty and the extent to which the Bretton Woods agencies’ programs are “inimical to the needs of the poor, I will first establish whether the SAP program has supported a more desirable income distribution in Morocco. Second, I will review “orthodox” recommendations for protecting the poor, and determine whether concern about poverty alleviation was reflected in the design of Morocco’s Bank-supported adjustment program. In conclusion, I will present the heterodox approach to adjustment which includes recommendations for protecting the most vulnerable groups.

#### B. A More Desirable Distribution of Income?

As has been noted in the previous two chapters, it appears that inequalities in income distribution have been reduced only slightly over the period 1970 to 1985. By 1985, although the incidence of absolute poverty in the population had declined, in both urban and rural areas, the absolute number of poor had increased, and expenditure per person was uneven, with greater inequality in the urban areas. These findings indicate that the rapid development of the 1970s and early 1980s, as well as the Moroccan government’s commitment to social welfare have failed to reach the poorest groups of the SAP, short-run indicators provide evidence that, on the whole, they have been negative, with the largest share of the costs being

borne by the poor who are the least able to protect themselves. Given that the SAP was only launched in 1984 and that limited data are available for the period after 1985, one can only speculate as to long-run distribution of income.

Kuznets writes: "It seems plausible that in the process of growth, the earlier periods are characterized by a balance of counteracting forces that may widen the inequality in the size distribution of income for a while" (1966: 67). Kuznets's "inverted-U" hypothesis more explicitly promises greater equality in the long-run (for Morocco as for any other country characterized by a mostly agrarian economy which is beginning to industrialize). The "inverted-U" represents the nature of the dependence between the level of economic development (as measured by GNP per capita) and the degree of economic inequality in a country (as reflected by the Gini coefficient). Graphically, it illustrates the hypothesis that the relative income inequality rises at the initial stages of development then declines in the middle and later stages.

Whether Morocco's income inequality will follow this pattern, and decline in the long-run is debatable. Much research effort has attempted to refute the inverted-U pattern as well as the supposed trade-off between growth and income equality (at least in the short-run). Whereas most studies<sup>(1)</sup> agree that the initial phase of development is necessarily marked by substantial increases in the

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(1) See Pawkert 1973, Chenery and Syquin 1975, Ahluwalia 1976, Lydall 1977, Fields 1980, Adelman and Robinson 1987.

inequality of the distribution of income, there is now growing consensus that whether inequality does or does not decrease in the later stages of development depends on the policies which countries follow, and on the extent to which the policies adopted narrow the mean income gap between sectors; the extent to which they decrease the dispersion of income with the modern sector; and the relative speed of absorption of labor into the modern sector (Adelman and Robinson, 1987). Furthermore, it has been found that the determinants of income inequality and changing inequality are less reflected by economic development (or GNP per capita) than they are reflected by factors that accompany economic development such as improved education, decline in the importance of agriculture, urbanization, and reduced income inequality.

Having established that it is policy choice which will determine whether the initial deterioration of income will persist in the later stages of the development process, and that income distribution is less determined by the level of development than it is by the type of economic development pursued, the obvious question becomes: does the structural adjustment program offer the appropriate set of policies and “type of economic development for Morocco’s economic and social structure, or is the burden of economic adjustment for the poor greater than that of maintaining the status quo? The orthodox view is that “countries have little choice about whether to adjust to the new realities of the international economy” (H&N, 1987a: iii). The only choice is believed to be between an orderly adjustment and a haphazard one. Based on country experience, the orthodox argument



states that an early and orderly adjustment will produce fewer social costs, while a disorderly or delayed adjustment is believed possible only through rapid inflation of the continuation of unsustainable economic imbalance suppressed through direct government controls, which often result in black markets in goods and currencies (Heller et al., 1988: 32). Both situations would severely hurt the poor as these bear the inflation tax burdens associated with unsustainable policies (whereas the better-off are able to shift their assets abroad or to switch them to real assets). The least skilled also suffer from unemployment (they are often the first to be laid off) which not only translates into reduced income but may also in the longer-term negatively affect their human capital. Poverty groups may also be locked in the production of nontradables when unsustainable policies provide the wrong economic signals and hence misdirect the productive resources of the economy. Failing to “get the prices right” may in addition hurt the poor by forcing them to pay the high prices prevailing in the black market, as they have no access to goods at official prices. (However, as has already been noted, devaluation often results in large increases in officially measured prices and raises costs through intermediate imports, therefore also adversely affecting the poor). Finally, political interventions that become necessary in the absence of orderly adjustment tend to divert resources into rent-seeking activities and raise rents based on political privilege rather than on economic performance. These points have been raised in an IMF Occasional Paper (Heller et al., 1988: 32). It can be argued, as structuralists do, that the proper

comparison is not with a disorderly adjustment, but with a more balanced adjustment process which places less emphasis on demand management. The structuralist approach will be developed later in the chapter.

The World Bank does not ignore the counterarguments to the above points. It recognizes that during the process of adjustment some social groups gain while others lose, particularly when, as in the case of Morocco, the adjustment is aimed at a shift in sectoral resources allocation. The concern over implementing adjustment programs without inflicting undue hardships on the poor has recently been the subject of much debate within the World Bank and IMF community as well as in the structuralist school.

### C Orthodox Recommendations for Protecting the Poor

In the mainstream, there have been two broad suggestions for protecting the poor. The first is based on the belief that any attempt to deal with poverty would undermine adjustment and that consequently measures to help the poor are limited to short-run compensation schemes, while longer-run implications for poverty must be left to the trickle-down effects of growth. The second is based on the more optimistic view that there is potential for designing structural adjustment policies to assist in poverty alleviation. It recommends protecting the poor during the difficult transitional period as well as safeguarding their interest over the long-run (Addison and Demery, 1987: 41).

As was concluded in Chapter II, the impact of the different adjustment policies has been largely determined by Morocco's economic and social structure. Accordingly, the actions needed to protect the poor during adjustment will depend on the conditions within Morocco. However, the consensus is that "the key to achieving adjustment that improves prospects for the poor lies in the participation of the poor directly in the adjustment effort" (Addison and Demery, 1987: 41). There is controversy however within the development community as to which poor should be drawn into the adjustment process, as evidenced at the Symposium on Poverty and Adjustment held at the World Bank in April 1988. Three broad poverty groups are candidates (Zuckerman, 1989: 3). First, are the "new poor" who are the direct victims of adjustment such as civil servants and private sector employees who were better off prior to the austerity measures. Second are the "borderline poor" or vulnerable, low-income groups who are affected most severely by higher prices on consumption items, especially food, and by cutbacks in social programs. In Morocco, the group constitutes 29.5% of the population and includes the elderly, infants, women, and landless and poor farmers, all of whom are the least able to protect themselves from adjustment and recessions. Third are the extreme or structural poor. Within this group, the urban poor tend to be more affected by changes in the availability and prices of consumption items than the rural poor who were already too marginalized before the adjustment program was implemented. The extreme poor suffer from malnutrition, illiteracy, disease, short life expectancy and high

infant mortality rate. In Morocco they constitute 18% of the urban population and 14% of the rural population.

Following much debate, the Symposium on Poverty and Adjustment agreed that measures to help the poor under adjustment should cover all the poor, not just the “new” or “borderline” poor. As to which measures to use, several recommendations dominate the development field. In general, recommendations center around the design of poverty-oriented adjustment programs that maximize primary income-generating activities for the poor, in so far as these are economically active or are potentially productive. Primary incomes or incomes derived from productive activities may be raised by the adjustment process in four ways (Addison and Demery, 1987: 41). First in the spirit of “redistribution with growth”, access to productive assets, such as land irrigation and production inputs can be improved. Second, as advocated by the neoclassical school, rates of return on the assets of the poor can be raised by dismantling distortions. Third, given that in most developing countries, the poor people’s chief endowment is their labor, increasing their access to employment through improvements in the operations of the labor market may be effective in raising their incomes. Fourth, the human capital of the poor can be protected by ensuring their access to health and education services through a restructuring of public resource allocation.

## 1. Improving Access to Productive Assets

Improving the access of the poor to productive assets is not central to the adjustment program but would be consistent with its objectives in that output and productivity can be raised in the process. The choice of assets to distribute in Morocco includes irrigation, fertilizers, electricity, and credit. The allocation of these inputs has been biased in favor of the big and middle-sized farms, while landless farmers have barely had access to them. A sustained effort must be made to direct more investment towards depressed areas, and to ensure a more equitable distribution of agricultural inputs. In addition to facilitating access to agricultural inputs, the most promising solution for the fight against the impoverishment of the landless farmers lies in increasing their access to land ownership. In Morocco, landlessness is a major contributor to the poverty problem, with barely two percent of the land having been distributed to the farmers following the independence of the country. Land reform is therefore an indispensable means of alleviating rural poverty; and by limiting rural exodus, can also contribute to improving the standard of living of the urban poor. However, such a measure presents a significant challenge to the government who is already faced with the difficult political choices that the structural adjustment programs entail. There has been no attempt by the government to introduce a general land reform since independence, although modifications of land ownership and inheritance patterns have been made in areas subject to development programs and irrigation schemes. Ennaji (1986: 44)

believes that under the present socio-political trends, there is little hope of facilitating access to land ownership to the landless. Instead, he suggests intensified farming, greater crop variety, better markets, higher pay for labor, and technical training according to need as means to improve income in rural areas and hence halt the rural-urban migration.

## 2. Raising the Returns on Assets

The Moroccan Bank supported adjustment program has sought to remove distortions in product markets, raising output prices and reducing input costs in order to promote greater efficiency in resource allocation as well as a reduction in poverty. This liberalization process has inevitably affected incomes and poverty but not necessarily for the better. As has already been covered in Chapter II price reforms have tended to increase inequalities among the rural poor and to overburden the urban poor. "Increasing the return on assets held by the poor therefore may require more than improved price incentives" (Addison and Demery, 1987: 14). Improvements in rural infrastructure and agricultural services are necessary.

The World Bank's involvement in raising the return on assets has been concentrated in its Agriculture Sector Loans. Bank supported investments in the agricultural sector have so far focused on area development, small and medium irrigation systems, and agricultural credit. In the future, emphasis will also be placed on natural resource management and the development of research and

extension packages, which would benefit smaller farmers in both rainfed and irrigated areas.

As always, the World Bank relies on stimulating growth (in this case, in the agricultural sector), in order to improve distributional patterns. Moreover, given that it is the small farmers who are at the center of the Bank's strategy for the agricultural sector, it is doubtful whether the landless poor will benefit directly.

In urban areas, measures to enhance the poor's access to income-generating activities and some form of consumption transfer may be required. Such measures imply a need for more resources, including development aid, than is available to a country in crisis such as Morocco.

### 3. Improving Employment Opportunities

Morocco's poor possess few productive assets other than their labor, hence improving their access to productive employment may be effective in raising their standard of living. Morocco however is still at the stage of minimizing unemployment problems inherited from past policies, as well as those caused by the adjustment program. Morocco's unemployment rates have remained high during adjustment because while some sectors — mainly nontradables — contracted rapidly, others expanded at a slower pace, thereby creating a transitional unemployment problem. The high level of unemployment is also the result of the contraction in aggregate demand and the reduction of the public sector.

Given these constraints, the task for policy is “to increase the occupational and geographical mobility of the target groups” (Addison and Demery, 1987: 181).

In Morocco, unemployment is concentrated in the urban sector which, in addition to increased unemployment between 1982 and 1986, has also suffered declining real wages. The above measure ensures that the poor benefit from the expansion of employment, particularly in the tradable sector.

The social sector strategy for Morocco suggests that more jobs have been created during the adjustment process, but that these have been mostly temporary jobs offering low-pay and low productivity. Ennaji (1986: 44) adds: “the creation of non-agricultural jobs is limited and continues to give priority to the urban and not the rural areas.” To compensate the poor more directly, the government has created work camps. However, less than 5% of the poorest families have benefited from this operation (200 days of work per person a year), while the “new poor” such as retrenched civil servants have been the major beneficiaries.

Based on the above, the policy options for the future should include: (1) better targeted compensatory programs to protect the poor from expected cuts in social expenditures. This should only be a short-term measure. For a longer-term, more sustainable effort, policy should focus on: (2) increasing productivity and low wages by providing appropriate vocational and training programs, and upgrading the structure of the demand for labor; (3) facilitating informal sector activities through providing access to credit, capital



and productive inputs for the poor through Grameen-Bank type of institutions; and (4) legitimizing initiatives such as the “Commission Nationale de la Promotion de l’Emploi des Jeunes” (WB, 1988:9).

To achieve the above, it is not sufficient to provide financial or administrative measures. “The problem is to make a global change in the economy, increase purchasing power in urban areas, and bring about a positive change in the demand for labor (part-time work having characterized the labor situation in Morocco in the last 15 years) (Ennaji, 1986: 45). Ennaji points out the need for improvements in labor legislation, to be backed by a strong social movement. In addition, he highlights the importance of serious investment programs for the realization of the various policy options.

#### 4. Ensuring Access to Education and Health Services

Expenditures on human capital are essential to protect the poor during adjustment and to help them break out of their poverty. In Morocco, total social outlays as well as per capita income continued to rise between 1978 and 1982, however since the implementation of the SAP, public spending on social programs has been severely cut, so much so that the social sector strategy (1988) suggests that what may become imperative in the coming years is the preservation and protection of human capital rather than its development.

Policy options include improving demand for education and literacy, and more direct paths to the workplace. On the supply side,

educational poverty may be reduced by redirecting educational resources to the poorest sectors of society (WB, 1988: 16). Currently, the World Bank is designing an Education Sector Loan with the aim to provide greater equity of access to educational services. The focus is on basic education, particularly in rural areas, where measures to increase female participation rates have received special emphasis.

For the health sector, Akin and Birdsall (1987: 41) suggest four policies as an agenda for reform: (1) charging (mainly the relatively wealthy) users of government health facilities; (2) introducing health insurance programs by making them compulsory for the better-off urban workers while subsidizing the cost of insurance premiums for the poor; (3) encouraging provision by the nongovernment sector of health services for which households are willing to pay - this sector may include missionaries and other nonprofit groups, independent physicians and pharmacists, and traditional healers and midwives; and (4) decentralizing certain government health services to improve organization efficiency in the provision of services. Finally, resources for this sector must be increased.

With respect to measures taken by the Bank within the Public Health sector, expenditure patterns are being restructured away from the traditional urban-based, curative health care system to emphasize preventive health care, particularly in rural areas. Moreover, the increase in the level and efficiency of overall public investment expenditures is a major component of the adjustment program. To this effect, a target investment program (TIP) is being

developed to complement private investment as well as provide for the most urgent social needs.

Regarding public spending in general, the social sector strategy (World Bank, 1988) finds that the current sectoral and project-based policies are disconnected from the population distribution of the country, suggesting a population redistribution or growth pole development policy-framework may be more appropriate. Moreover, the same report argues that the access to the above mentioned social services should be maintained for the poor, even in conditions of fiscal austerity. Suggested financing arrangements include: (1) external borrowing, (2) transfer of funds from non-social to social sectors, and (3) transfer of funds from other social sectors of lower priority.

The degree of emphasis on each of the four approaches depends on which groups constitute the poor. In Morocco, the ultra-poor or extreme poor constitute 16% of the population. This group is not economically active; it is not engaged in any productive activities and hence cannot be drawn into the restructuring process. For the ultra-poor therefore, additional measures to the ones stated above need to be considered. These may include well designed and targeted income and/or consumption transfers.

##### 5. Supplementing the Resources of the Poor with Transfers

Many poor people are often locked in the production of nontradables or are not economically active (for example women or the elderly), they may also be locked in poverty by poor health and

limited education. Hence their problem cannot be alleviated through changes in primary income claims (as these are derived from productive activities), rather income and/or consumption transfers may be the only effective means of providing support to them (Addison and Demery, 1987: 35). This measure is more problematic than the above four because of the inconsistency between increasing transfers to the poor and cutting the government's budgets. The trade-off can be minimized by targeting such transfers to those that need them most, while restructuring them to maximize their benefits.

Income transfers, include employment programs which range from direct employment to labor subsidies, to direct compensation. Direct employment programs primarily generate employment for the poor. However, in Morocco these "work camps" have benefitted less the ultra-poor than they have the "new poor" such as retrenched public employees. The government and donors also operate food-for-work programs as another attempt to provide direct employment. These schemes are also effective in managing emergencies and in developing infrastructure.

The second alternative, namely labor subsidies, deserves to be developed as it can increase the demand for labor and hence correct the trend of increasing temporary work which has prevailed for the last fifteen years. However, it is difficult to ensure that such programs reach the poor.

Finally with respect to direct compensation to the unemployed, such a scheme should be maintained even if not cost-effective in

times of fiscal restraint. However, it should be complemented by programs to provide credit and training to redundant public employees as well as to rural manpower.

Another important way of protecting the welfare of the poor is through food transfers. In Morocco, the nutritional status of the poor has been negatively affected by devaluation, high unemployment, falling real wages, and more directly by the cuts in food subsidies that were introduced in 1986. These social costs, the result of adjustment measures, establish the need for compensatory food programs which are all the more urgent since the government plans to entirely eliminate subsidies by 1990.

In Morocco, the rural landless and the urban poor have been the most vulnerable to the social consequences of adjustment. Possibilities to protect their nutritional status include the financing by government of the difference between subsidized consumer price for the needy and a higher market price for producers (H & N, 1987: 60). However, the fiscal burden of such dual-pricing schemes is not in line with the fiscal restraint objectives of adjustment programs.

The World Bank's efforts to cushion the adverse consequences of the cuts in consumption subsidies have been concentrated on targeted compensatory programs for low-income urban and landless rural poor. Such an effort can be improved on through the combined use of two approaches (CEM, 1987: 21). One would use the special agencies, which have functioned well and are precise in their targeting to deliver nutritional assistance for specific groups such as school children, nursing mothers, etc. The other would use "inferior

good” varieties with lower consumer appeal that could be subsidized at the production/processing stage and commercialized without attracting strong demand from the not-so-poor.

In fact, socially inferior but nutritionally superior flour will be targeted to poorer areas. This is expected to result in substantial budgetary savings. Finally, the government and donors also operate income transfer programs for the poor through food-for-work, school meals, and material and infant feeding programs.

To sum up, the Bank’s involvement in protecting the poor has been concentrated in targeting food subsidies, education, and health services. These actions by the Bank should be taken as particular rather than typical. Moreover, not all the efforts met their stated goal of protecting the poor and alleviating poverty. Finally, even if the Bank has aimed at benefitting the poorest 40% of the population, its efforts to reach the bottom 15 to 20% have been minimal.

#### D. The Heterodox Approach

Ideally, adjustment should induce long-term growth and an improved standard of living for the poor. Structuralists attack adjustment for achieving the opposite, namely stagflation and deteriorating social conditions.

The two policies mostly criticized by the structuralist school are those of trade liberalization and demand restraint. First, structuralists argue that liberalization policies are not necessarily an “engine of growth”, and second that demand restraint can even be biased against economic growth and the needs of the poor.

With respect to liberalization policies, several empirical studies<sup>(2)</sup> have stated that trade policies and trade distortions are not correlated with performance and countries' response to external shocks (and these have been numerous in the past two decades). As even Ann Kruger, a strong proponent of liberalization, writes: "while there are numerous microeconomic changes that accompany devaluation, liberalization, and altered (trade policy) bias, it (is) not possible to detect significant effects of these changes on growth performance" (1978: 277). Hence there is an agreement that policies that stress export-led growth or that advocate "getting prices right" can rarely be the major determinant of growth. "Internal factors are more important in explaining the wealth of nations" (Lal, 1985a: 48).

Today, these arguments are all the more relevant in the wake of the debt crisis (to which openness to international capital flows contributed) and the apparent failures of many liberalization attempts (foremost that of Mexico in the 1980s). "It is therefore appropriate to rethink the issues" (Taylor, 1986: 1).

In his 1980 Nobel lecture, Lewis talked of "trade pessimism", and throughout the 1980s, a wave of protectionism has gained momentum. However, protectionist policies have proved to be disappointing, as in some cases they intensified the foreign exchange constraint rather than alleviated it. Nonetheless, given the current world crisis and slow growth in the industrialized world, the foreign

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(2) See McCarthy, Taylor, and Talati (1986); Balassa (1985a).

exchange constraint on countries' development is, according to Taylor (1986), making inward orientation and non repayment of debt increasingly attractive options. The structure of the Moroccan economy however is outward looking, and this orientation cannot be easily reversed. Moreover, Maghreb markets cannot significantly replace European ones. Taylor nevertheless maintains that: "in the 1980s, the trade liberalization strategy is intellectually moribund, kept alive by life support from the World Bank and the International Monetary Fund" (1986: 32). Morocco should therefore be cautious that liberalization and debt-repayment do not undermine its regional development. The government should concentrate on furthering economic unity and cooperation among North African countries, rather than pursuing increasing openness, especially in the face of rising world protectionism.

In addition to arguing that the impact of liberalization on growth is uncertain and even detrimental to the regional development of LDCs, the structuralist school criticizes adjustment programs for seeking excessive reduction in aggregate demand, which results in an unnecessary contraction of output, employment and standards of living of poverty groups.

Having stated these points, progressive economists' recommendations are several. Although he describes the policies included in orthodox packages as "ploys", Taylor by his own admission writes: "a structuralist package would no doubt include many of the (orthodox) policies. Not many others are known" (1983: 202). However, improvements on the package are suggested. First,



given that the various policies have been shown to cause output loss or trigger inflation, it is recommended that they not be imposed simultaneously. The case for gradualism is even stronger given that in Morocco, as in most countries, those negatively affected are the poor. In addition, political considerations tend to dominate the arguments in favor of gradualism.

Second, a more balanced adjustment process which places less emphasis on demand restraint is believed to be more desirable, entailing less social and economic costs that usually threaten the financial and political systems.

Third, the distributional and employment implications of the program should be incorporated. Based on social accounting matrices, the relevant economic groups can be identified, as well as their role in the macro system, and their political and economic interconnections.

Fourth, it is recommended that the program be redesigned to reflect more adequately institutional settings and the circumstances of the country in question. Attention needs to be paid to institutions, grass roots organization and culture. "The relatively high rate of failure for projects in Africa has stemmed from mistaken assumptions about the likely behavior of the people involved" (Beckman, 1986: 29). Hence, "listening to the people" is strongly advocated as a means of ensuring the viability of the program and the welfare of the poor.

These recommendations all require substantial resources, more than is available to an economy in crisis; hence additional external financing is essential.

Other suggestions within the development community have been advanced. They mainly underscore the need to protect the poor during the initial period of adjustment, as well as in the longer-run. In particular, arguing that reviving growth (and thereby increasing the absolute income of the poor) is not a sufficient measure to protect the poor, Adelman (Adelman and Robinson, 1987) advocates a policy of “redistribution before growth,” which in the context of Morocco would encourage tenurial reform in agriculture before the implementation of policies designed to improve the productivity of agriculture; and massive investments in education before rapid industrialization.

Finally, the UNICEF study<sup>(3)</sup> presents a strong argument for the adjustment program to assume an activist role. It stresses that adjustment policies should be used as an instrument for mitigating the adverse distributional implications of external shocks and even for improving the welfare of poverty groups. This hence advocates for adjustment to be seen in the broader context of strategies for poverty alleviation. However, it must be noted that even the strategies designed specifically for poverty alleviation (whether by governments, the World Bank or other agencies) have rarely attempted to reach the bottom 15 to 20% of the population. Yet these

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(3) See Cornia, Jolly, and Stewart (1987)

are precisely the people who need support. In Morocco, they constitute 18% of the population.

## Chapter IV. Conclusions

Recently, there has been controversy surrounding the social costs of stabilization and adjustment in developing countries. One side claims that the programs have substantially deteriorated the standard of living of the poor, while the other argues that the costs borne by the poor are only transitional and that the failure to adjust would worsen social conditions further.

This study has shown that the Moroccan Bank-supported adjustment program has so far had severe implications for income distribution. The changes in income distribution are not considered the undesirable side-effects of the program by its designers, rather they are its intended outcome. These changes are the principal incentives for resource reallocation; they facilitate the "expenditure switching" process and are therefore believed essential for the realization of the objectives of adjustment.

This is not to argue that adjustment is unnecessary, or that its economic and social costs are greater than those of maintaining the status quo. On the contrary, adjustment is increasingly recognized as being necessary for correcting the severe economic imbalances that characterize developing countries today. However, this does not imply that all adjustment policies are equally adequate for ensuring an adjustment program that is compatible with growth.

Adjustment which promotes increases in exports, savings, and investment is more supportive of growth and improved living standards for the poor than a program which relies on cuts in

investment and public spending. However, when the latter contractionary policies are necessary to deal with the substantial balance of payments and budget deficits, economic efficiency and public awareness must be increased to better target scarce resources towards the needy. Moreover, austerity measures need to be accompanied by compensatory programs to protect the most vulnerable groups.

The concern is therefore with how to integrate human considerations into the process of economic policymaking. This concern is best captured by the "adjustment with a human face" approach (Cornia et. al., 1987) which advocates for a poverty alleviation dimension to be added to adjustment, in the same way as "redistribution with growth" and "basic needs" added such a dimension to growth. The need to protect the poor is even greater given that the international economic environment is such that growth may not be assumed. Indeed, in many developing countries, output per capita is declining, hence entailing falling incomes for the poor, even with constant income distribution; and as has been demonstrated, the burden of adjustment policies often fall disproportionately on the poor.

This thesis has shown that there is much potential for improving program design and implementation towards the addition of a poverty dimension to adjustment; and that this can be achieved without undermining the objectives of adjustment.

The success of the Moroccan program will therefore depend on fresh approaches to reducing poverty, which are consistent with

adjustment and improve on past efforts. Poverty alleviation must become an explicit objective before policies to restore economic stability and revive growth can benefit the poor.

The main conclusion is that social development can and should be promoted simultaneously with economic adjustment. Apart from its social justification, achieving tangible progress in raising living standards and providing employment opportunities in what still is a very poor country is also important for the stability of the political system. If the economy remains in crisis, or the adjustment measures continue to be perceived as detrimental to the poor, either the army or Islamic Fundamentalists (though neither currently poses a threat) could become the outlet of unsatisfied demand for social justice.

Hence, the economic challenge facing the government is to ensure that, by the early 1990s, the espousal of the neoclassical economics embodied by the IMF's and the World Bank's adjustment program will be perceived as the appropriate orientation for the economy.

Finally, regardless of how successful a strategy is, it is less likely to generate unrest if the population believes that the burden is being distributed fairly and that it can influence the political process. In order to mobilize public support for reform, the king must pursue a policy of decentralization of power, an initiative he introduced in 1975 only to abandon in the late 1970s. He must permit not only a major restructuring of his economy, but also that of the nation's patrimonial political system.

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